

# Privatisation and liberalisation of public services in Europe

An analysis of economic  
and labour market impacts

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public services  
Europe  
labour market

edited by Maarten Keune, Janine Leschke and Andrew Watt

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## **Introduction: liberalisation, privatisation and the labour market**

### **Introduction**

The liberalisation and privatisation of public sector activities in Europe and other advanced economies have been the subject of heated debate since the 1970s. At issue are various normative and cognitive conceptions concerning the most effective, legitimate and socially acceptable ways of providing key services and thus where lines may appropriately be drawn between the public and private sectors and the proper role of competition and markets. Much of the discussion has centred around questions such as the responsibilities of the public sector, how accessibility and quality of certain services can be guaranteed for all, to what extent public sector services are efficient and productive, how the public sector can contribute to employment creation and what the effects of liberalisation and privatisation are on quality of employment and industrial relations. The chapters in this volume contribute to this debate by analysing in detail the effects of liberalisation and privatisation on productivity and service provision, employment, wages and working conditions. The focus is on the service sector, which accounts for around 70% of GDP and employment in Europe and has been the main (often the only) source of employment growth in recent years. Indeed, the rapid growth in service employment during the last few decades has been one of the most prominent socio-economic trends in many countries. The effects of privatisation on service employment are at present hotly debated, but serious systematic analysis is lacking. Through a series of case studies of privatisation processes and outcomes, as well as four quantitative and comparative analyses of the differences between public and private service sector employment, the present volume helps to fill this gap. In this introductory chapter we first discuss the political and economic context in which privatisation and liberalisation of services takes place, with a focus on

Europe. We then summarise the main findings of the studies in the book, presenting them thematically.

## **1. Liberalisation and privatisation**

### **1.1 The global trend towards liberalisation and privatisation**

Today, the debate on the liberalisation – that is, the expansion of market coordination at the expense of non-market types of coordination – and privatisation (that is, the sale of public assets to private owners) of public sector activities tends to be dominated by those who underline their benefits and desirability. What is more, it has been argued that liberalisation – as a broader phenomenon – was the main characteristic of political-economic change in the last two decades of the twentieth century (Streeck and Thelen 2005; Boyer and Drache 1996). Until the 1970s, however, it had been relatively uncontroversial that the state had a central and active role in the economy, managing aggregate demand through public expenditure and investment in pursuit of growth and employment objectives, as well as being a major employer, not only in public administration and related activities but also in many industrial and service sectors.

It would be useful to begin by recalling why in most European countries key services were provided by the state. The main arguments for public ownership – the relative importance of which varied from country to country, depending on the characteristics of the sector in question – included the following:

- to ensure equal access to essential services, often conceived as human rights, and thus to promote social justice and territorial cohesion;
- to control (natural) monopolies/oligopolies in the presence of economies of scale and high fixed costs;
- to achieve rationalisation and economies of scale and thus reduce costs and prices;
- to gain access to low-priced capital for large-scale investments in a context of national private capital markets that were small and underdeveloped;
- to control the ‘commanding heights’ needed for economic planning;
- to address national security concerns (in the context of the Cold War).

Since the late 1970s there has been a move away from welfare capitalism and Keynesianism and towards neo-liberalism, which has had a huge impact on the perceived role of the state in the provision and regulation of services. The rise of neo-liberalism started in the wake of the first oil crisis of the 1970s,

which was followed by rising unemployment and inflation and economic stagnation in the West, calling into question the viability of Keynesian demand management, planning and public ownership. The post-war consensus was contested with great success by the advocates of neo-liberalism, including many prominent economists, a number of Western governments, spearheaded by Margaret Thatcher and Ronald Reagan, and international organisations such as the IMF, the World Bank and the OECD. A dramatic loss of faith in the capacity of collectives to express their will through institutions other than private firms developed (Crouch et al. 1999: 8), and state intervention in the economy was increasingly deemed to be inefficient and inflationary, ‘crowding out’ private investment and reducing an economy’s attractiveness to international capital (Standing 1999: 74).

The core of neo-liberal discourse is its reliance on neo-classical economics and its belief in the superiority of the market over other types of governance. Indeed, the ideal-type neo-classical market economy is its major theoretical inspiration: basically, neo-liberalism represents a set of ideas concerning what actors and institutions can best approximate the ideal-type market economy. These include a ‘minimalist welfare state, taxation, and business regulation programmes; flexible labour markets and decentralised capital-labour relations unencumbered by strong unions and collective bargaining; and the absence of barriers to international capital mobility’ (Campbell and Pedersen 2001: 5). Following this line, neo-liberals insist on the need for general ‘deregulation’ and for the state to abstain from intervention in the economy. Liberalisation and privatisation of public activities are major elements of this argumentation.

This was paired at the macroeconomic level with a focus on sound money and the primacy of fighting inflation, following the growing prominence of monetarist ideas. The reduction of budget deficits became a central objective. Contrary to the key role of public expenditure in regulating the economy in the Keynesian era, the new neo-liberal/monetarist consensus argued for modest and balanced budgets and against public debt. At this level, too, privatisation and liberalisation of public sector activities are major elements, presented as ways of reducing government expenditure by cutting subsidies and raising revenue through the sale of assets.

The shifting ideological basis for government policy was accompanied and, to some extent, supported by important shifts in background conditions compared with the post-war ‘*trentes glorieuses*’. Fiscal pressures increased substantially, leading governments to seek to reduce spending and tap additional sources of revenue. The globalisation of trade and investment



increasingly undermined the idea of national markets. Indeed, with the ongoing expansion of markets around the globe, nations were seen increasingly to have lost control over their economic destiny to global economic forces. Specifically, trade liberalisation decisions taken at the WTO, especially in terms of the General Agreement on Trade in Services, have created pressure for privatisation of public services.

At the same time, changes in the financial markets and their international integration have given private companies access to a much bigger pool of capital. The pace of technological change (especially in telecoms) has accelerated dramatically. In many areas this has reduced transaction costs and enabled individual steps in production chains to be geographically separated, promoting tradability and hence the globalisation of both goods and services production. Also, the end of the Cold War rendered national security considerations less pressing and, arguably, reduced the incentive for elites to take social justice issues seriously. As incomes rose, consumer demand developed and became focussed more on choice and product differentiation, similar to goods markets.

## **1.2 Liberalisation and privatisation in Europe**

In line with the global trend, in Europe too liberalisation and privatisation have been high on the agenda in the last few decades. This has been the case most dramatically in Central and Eastern Europe where the former state-socialist countries turned to capitalism at the end of the 1980s, resulting in the rapid liberalisation and mass privatisation of largely state-owned economies. In Western Europe, the UK under Margaret Thatcher introduced the most far-reaching project of economic liberalisation and privatisation between the end of the 1970s and the early 1990s. Other Western European countries followed to varying degrees, constituting a common trend but with strong inter-country differences (as shown in the country chapters in this volume). As a result, most of formerly publicly owned manufacturing has now been privatised across Europe, while there is more variation in the extent of public ownership of services, in accordance with different national traditions, values, perceptions of the role of the state and the resources available to governments. As a result, today's privatisation debate largely concerns what role the state should play in providing 'public' services as an owner of the means of production and/or as a regulator of the activities of private suppliers.

Alongside the national level, in Europe the European Union plays a decisive role in processes of liberalisation and privatisation, in a number of ways (Brandt et al. 2008; Jacobi and Kowalsky 2002). The creation of the Internal

Market is one of the basic pillars of European integration (Scharpf 1996, 2002) and EU market making is increasingly acquiring a self-reinforcing character (Fligstein and Stone Sweet 2002). Within this framework, EU economic integration has promoted the privatisation of public services, among other methods by subjecting public services to competition regulations and placing restrictions on state aid for economic activities. The implementation of the Maastricht fiscal convergence criteria, which require member countries to cut their deficit and debt ratios, has affected public services insofar as it has forced governments to reduce subsidisation and has also encouraged the sale of public enterprises as a way of reducing government debt (Hall 2001).

EU sectoral directives aimed at creating a single market, and so permitting competition between producers from different EU countries on often highly monopolised domestic markets, cover the areas of telecommunications and broadcasting, transport, electricity and gas, as well as postal services. Regulations vary significantly in terms of method and extent from one sector to another. While telecommunications and energy have been subjected to full open market competition, postal services still remain relatively regulated (Raza et al. 2004). The speed of implementation of liberalisation directives also varies markedly between the member states. The Directive on electricity, for example, came into force in February 1999, but five years later DG Energy and Transport (2004) found full competition only in the UK, Sweden, Finland, Norway and Denmark. Overall, the activities of the European Commission and, not least, the European Court of Justice have done much to accelerate the liberalising tendencies already present at national level.

At the same time, and in spite of the clear move towards monetarism/neoliberalism at the national and European levels, it is important to emphasise that states have not withdrawn from economic management, nor have markets become all-encompassing. Indeed, non-market modes of coordination continue to be of crucial importance in European economies. Partly this is because privatisation has created an additional need for government regulation to set the rules for competition, to ensure that public service obligations are met or to constrain price setting. More generally, the state remains an important player as an owner, employer and regulator of economic activities, if less so than in the past. In most European countries also other modes of coordination, such as collective agreements, restrict market coordination. And although state and other non-market types of coordination have been under pressure for quite some time, concerns are growing as regards the extent to which liberalisation and privatisation of public services are desirable, not to mention their effects on productivity,

employment creation, working conditions and industrial relations. These issues will be further discussed below. First, however, we present a brief overview of the characteristics of and developments in the service sector in Europe, which are important background conditions for subsequent evaluation of the outcomes of privatisation and liberalisation.

### **1.3 The service sector in Europe**

Over recent decades there has been a pronounced sectoral shift away from manufacturing and extractive industries in the EU – and in some countries also from agriculture – towards a service-dominated economy. By 2004 services accounted for over 70% of GDP in the EU-25. Employment trends are quite closely related to output trends: services increased their employment share by over 5 percentage points between 1995 and 2005, to 70%. Simulations in Kemekliene et al. (2007) suggest that, on current trends, by 2020 up to 80% of all employment in the EU will be in the service sector.

The expansion of employment in services is driven by a number of factors. Standard explanations revolve around both demand and supply side factors, including income elasticities of demand for services that exceed 1 (meaning that consumption of the service rises more than proportionately with income), limited scope for labour productivity improvements in the supply of consumer services and the rise in demand for coordination and intermediation services associated with structural change. Furthermore, advances in information and communication technologies, amongst other factors, are increasingly permitting cross-border trade in services, accelerating the growth of service activities by expanding potential supply and reducing costs. Coupled with increasing foreign direct investment in services, this is at the same time opening up to competition sectors that until recently were considered non-tradable and thus ‘sheltered’.

Although there is not a clear distinction between public and private sector employment in EU-wide data (see the chapters in this volume for more detailed country data), of total services employment in the EU-25 in 2005 health and social work account for about 14%, public administration and education about 10% each and transport and communication 9%. These sectors, which can, in a very broad sense, be identified as ‘public’, thus represent around one third of total service employment.

While service sectors are heterogeneous, a number of general characteristics of service-sector employment compared with that in industry stand out (see Kemekliene et al. 2007; the figures are for the EU-25):

- Gender: women are more highly represented in service sectors than in the economy as a whole. They represent 56% of total service sector employment. This falls to just under half if public administration is excluded, but even this is much higher than their share in industry (just under one quarter).
- Pay: there is a strong divergence among services. In particular, in hotels and restaurants, but also in wholesale, retail and repairs, earnings are low in comparison to industry. In contrast, in financial intermediation earnings are high, at 71.1% above earnings in industry. Low pay is a serious problem in many service sectors. To some extent this reflects low skill levels, but also difficulties organising effective worker representation in small-scale enterprises with high turnover and irregular working patterns and among more marginal sections of the labour force.
- Non-standard contracts: both part-time and fixed-term employment contracts are more prevalent in services than in industry. However, these averages conceal a substantial diversity within the service sector. In particular, there has been a substantial rise in the use of fixed-term contracts in many service sectors.
- Skills: the percentage of high-skilled employees in the service sector is higher than that for the economy as a whole and for industry, and the percentage of low-skilled employees is lower. But major differences exist between the different service sectors. Over time, in services, as in the economy as a whole – but to a slightly lower degree – there is a trend towards an increasing skill profile for employees, resulting from improved educational levels and changing consumer demand.
- Unionisation: the service sector needs to be divided up into its public and private sector components in order to understand developments. Except in those countries in which unionisation is universally high, union density tends to be substantially higher in the public sector than in industry, and this is much higher again than in the private service sector. In most EU countries fewer than one in five workers in private sector services is a union member: only in the three Nordic countries is the figure above 50%.

## **2. Service sector employment and the effects of liberalisation and privatisation**

Against the background of the academic and political debate and the characteristics of the service sector in the European economy described above, we can develop a number of preliminary hypotheses regarding the

impacts of liberalisation and privatisation on economic outcomes, such as efficiency and productivity, as well as on the consumers of services and the workers employed in the service sector.

At the most basic level the expected impacts of privatisation or liberalisation of a given sector in a given country will clearly depend on the characteristics of the national ‘social economy’ (legal framework, labour market institutions, and so on), the sector itself and the specific way in which privatisation or liberalisation is implemented in each sector.

- National ‘social economy’: the outcomes of a given privatisation/liberalisation strategy will depend on structural features of national economies, industrial relations and welfare state systems. Strong trade unions and protective labour market regulation will tend to protect workers otherwise exposed to market competition. The existence and political influence of consumer lobbies may have an effect on service quality. The taxation system will influence distributional outcomes.
- Sector: characteristics likely to affect the outcomes of privatisation/liberalisation include natural monopoly characteristics, capital and other costs of market entry, exposure to cross-border competition, the pace of technological change and the overall trend of product demand. The capital requirements for power generation, for instance, are so great that only a limited number of firms can effectively compete; by contrast, hospital cleaning services can be performed by large numbers of firms offering cleaning services. On the other hand (facilitated by regulatory liberalisation) electricity is increasingly traded across borders, exposing that sector to limited but growing foreign competition. Overall, such characteristics determine the extent to which a privately run sector will be prone to market failure. Also, the extent to which specific sectors are covered by collective agreements and the strength of trade unions in particular sectors are likely to ameliorate the effects of liberalisation and privatisation on wages and working conditions.
- Nature of privatisation/liberalisation: most crucially, the way in which the government – against the background of the specific sector’s characteristics, as well as requirements stemming from the European level – opts to structure the privatisation/liberalisation process will decisively affect outcomes. A simple sale of public assets in an inherently highly monopolistic sector will almost certainly harm efficiency and leave consumers worse off, as private oligopolies divide

up markets, reduce supply and drive up prices. The existence of specific regulations to control prices and public service obligations to ensure wide access to services and the introduction of effective regulatory agencies to oversee liberalised sectors can be expected to be crucial determinants of outcomes and distributive effects. Overall, the institutional design of the privatisation/liberalisation process determines the extent to which sectors are actually ‘marketised’, the extent to which regulatory action can correct for market failure and, conversely, the extent to which the privatised/liberalised sector suffers from ‘government failure’.

These considerations, at rather a high level of abstraction, already suggest that it is extremely likely that privatisation and liberalisation will have highly differentiated effects depending on the precise mix of national, sectoral and privatisation-policy characteristics: given such complexity it is highly unlikely that simple good–bad classifications of outcomes will be possible, especially in a European comparative perspective. It is precisely the task of the ten substantive chapters of this book to tease out the effects for workers, consumers and economies/societies at large of specific cases of privatisation and liberalisation. But can anything be said in terms of general hypotheses regarding likely effects?

#### *Impact on workers*

The introduction of a heightened market orientation is likely, other things being equal, to lead to a lowering of the level of wages and working conditions as new corporate governance principles and pressure from competition prioritise cost control. Within such a general trend, increased market orientation is likely to benefit those with scarce skills and increase competitive pressure on those whose skills are in surplus on the wider labour market. This can be expected to lead to increased differentiation in pay and working conditions between groups of workers that is likely to benefit the highly skilled over the low skilled. The severity of this effect will depend on the overall state of the labour market (unemployment) and the existence of non-market and protective institutions. It will also depend on practices in the public sector. Since the 1980s, following the New Public Management school, there has been a trend to progressively introduce private sector principles in the public sector. Where this has been most far-reaching, the differences between the public and private sectors are likely to be smaller, as will be the effect on workers of any subsequent privatisation and liberalisation.

### *Impact on the level of employment*

This is uncertain *a priori*. Focusing on activities that are profitable is likely to lead to downsizing at the company level. However, increased competition and possibly price declines induced by greater competition may expand overall demand and thus (unless offset by higher productivity) raise labour demand at the sectoral level. It will be hard to disentangle the specific employment effects resulting from privatisation/liberalisation.

### *Impact on productivity*

Similarly, productivity effects are likely to be hard to measure effectively. Indeed, the typical indicators may give perverse results: private monopolies will be able to raise prices and thus, although possibly technically inefficient, may appear highly productive. Conversely, effective regulation (which, for instance, lowers output prices) may depress measured productivity. Ultimately, the key factor is expected to be whether 'real' competition can be introduced and this is promoted by the regulatory regime in operation. Otherwise, incentives to raise productivity through innovative reorganisation of production and also through capital investment will be missing.

### *Impact on consumers*

The impact on consumers is also hard to predict *ex ante*. Focussing on profitable services is likely to reduce supply unless a substantial inflow of new suppliers is induced. The shift from administrative to market rationing can generally be expected to transform a previously relatively equal access to supply to one that is more highly varied by region and by ability/willingness to pay, unless the regulatory regime takes effective counteraction (public service obligations). If effective competition is introduced falling prices may boost demand and generate a virtuous circle of falling unit costs that widens access to services (air travel is an oft-quoted example). On the other hand, competition brings new cost burdens from duplication and product differentiation, advertising, and so on, which will tend to raise prices.

## **3. Effects of privatisation and liberalisation – findings**

The studies presented in this volume are aimed at shedding more light on the effects of privatisation and liberalisation of public services on productivity and employment, as well as on consumers. Furthermore, they discuss in detail the impact of privatisation and liberalisation on the quality of employment in terms of wages and working conditions. They do so from two different perspectives. The first part of this volume relies on sectoral case studies in selected countries. The case studies directly analyse the influence

of privatisation and/or liberalisation on levels of employment, output and productivity, quality of services, and wages and working conditions. Five of the chapters focus on specific countries and sectors: Brandt and Schulten look at the German postal and hospital sectors; Thörnqvist focuses on Swedish postal services and electricity; Hall discusses the UK water and health care sectors; van der Meer looks at the electricity sector, public transport and home care in the Netherlands; and Darškuvienė focuses on the telecommunications and transportation sectors in Lithuania. Hermann's and Atzmüller's chapter is comparative and discusses railways, public transport, post, electricity, natural gas and water utilities in Austria, Germany, the United Kingdom and Sweden.

The second set of contributions focuses on wages, working conditions and work–life balance in the public and private service sectors, based on quantitative and comparative studies. The four chapters utilise individual and firm-level survey data and compare the situation in the two sectors as an indirect indicator of the (potential) impact of privatisation. Leschke and Keune analyse working conditions and wages in the UK and Germany; Ghinetti and Lucifora focus on skill levels and wages in France, Italy and the United Kingdom. The focus of the chapter by Meurs and Ponthieux is on the gender pay gap in eight Western European countries; and Chung examines work–life balance options at firm level in 21 European countries.

### **3.1 Efficiency, productivity and employment**

Efficiency and productivity gains are usually put forward as the main reason for privatising and liberalising public services. Three of the chapters of this volume address this issue in detail for individual countries. Liberalisation of the electricity market in the Netherlands has resulted in a substantial increase in the efficiency of production. A cost–benefit analysis prepared by the Netherlands Competition Authorities shows a gain of more than 1 billion euros for the period 2001–2006 – the most important contribution to the efficiency gain resulting from the decline of real prices and more efficient distribution (see van der Meer in this volume). In contrast, according to Hall (in this volume) water privatisation in the UK has been disappointing in terms of generating additional investment and raising productivity: labour productivity rose initially but this was due to a one-off labour shedding process. Over a longer period there is no evidence that privatisation has helped boost efficiency (as measured by total factor productivity). For the UK health sector Hall concludes that compulsory tendering has served to reduce costs, but this has largely been at the expense of the employees, whose pay and conditions have worsened – even where, as often happened, the



incumbents won the contract – rather than from any efficiency gains. The use of public–private partnerships has helped to promote total investment in an environment of constraints on public spending. However, there are doubts concerning whether this makes sense in the longer term, as current payments to private sector companies (whose borrowing costs are higher than those of the government) remain high over the lifetime of the investment. Thörnqvist cites the results of a recent public investigation into the outcomes of liberalisation in Sweden that shows increased productivity for all industries under scrutiny (postal services, railways, domestic aviation and telecoms). In contrast, trends in production volumes and profitability are less clear – depending on the industry they have either increased, decreased or remained unchanged. These mixed findings reflect not least the difficulty of clearly defining what ‘productivity’ implies in the context of public services and also the more general problem of a counterfactual; we cannot know how productivity would have developed without privatisation. This is particularly the case in those countries undergoing transformation from a planned to a market economy, as the case of Lithuania (Darškuvienė) in this volume indicates: developments there have been so rapid and comprehensive that the specific impact of privatisation/liberalisation is hard to distinguish.

The findings from the country studies can perhaps be tentatively interpreted to suggest that there has been an increase in measured productivity. However, we are unable to come to clear overall conclusions as to what the source of this increase is since it remains too complicated to distinguish the (unambiguously positive) effect of greater investment and better work organisation (that is, higher efficiency) from the (highly ambiguous) effect of a worsening of working conditions and/or job losses; the latter effects, while beneficial to taxpayers and/or the new capital owners, are clearly at the expense of the formerly public sector workers concerned.

Several of the chapters look into the employment outcomes of privatisation and liberalisation. Hermann and Atzmüller review a number of studies suggesting that in many sectors (telecommunications being an exception) liberalisation and privatisation have resulted in net losses of public sector jobs. In the EU-15 the loss of employment in the electricity sector, for example, amounted to 31% between 1995 and 2004, and there was a 12% reduction of employment in the gas industry for six countries within four years. The postal sector in several countries has also seen a substantial decrease in employment following the stepwise introduction of competition, but also because of technological changes (especially automatic sorting). In railways, the reduction in five member states amounts to 16% on average. Also in other sectors job losses at the former monopoly suppliers go beyond those

experienced at the sectoral level. For Austria, a detailed analysis of sectoral and company data shows that employment created by new service providers cannot as a rule compensate for the losses at the former monopoly suppliers.

Van der Meer's findings for the electricity sector in the Netherlands are less clear cut because the direct and indirect employment effects are hard to disentangle, given the emerging patterns of in- and outsourcing and restructuring of companies. Clear job trends in the various companies include the loss of jobs for production workers, whereas there has been an expansion of administrative staff due to the increasing information exchange and contracting with consumers. Another noteworthy development is the growth of higher skilled jobs, for instance in the forecasting of market developments and energy prices. The Dutch electricity sector first experienced a decrease in employment, but employment levels rose again when market liberalisation was introduced, mostly due to the administrative preparations and in front offices for marketing activities and consumer services.

According to Hall the effect of UK water privatisation on employment levels, but also on unionisation and collective bargaining, was dramatically negative. The core water companies cut around one in five jobs during the 1990s. Job losses in cleaning and other ancillary health-sector services were even more dramatic, although to some extent offset by growing employment in private sector firms.

From their case study on the German postal service (Deutsche Post AG) Brandt and Schulten conclude that employment was cut within Germany due to competition on domestic markets, while Deutsche Post AG strongly expanded employment abroad so that now less than half of their workforce works in Germany. For the German hospital sector, on the other hand, the decline in employment as an outcome of privatisation was relatively modest – employment in this area has dropped by about 4.3% since the early 1990s, the number being rather higher if we look at full-time equivalents (9.6%).

Thörnqvist comes to a similar conclusion for the Swedish electricity sector. The private company Vattenfall downsized domestic employment while substantially expanding employment abroad. The number of employees in the Swedish postal service has been falling continuously since the mid-1990s, starting before the onset of formal liberalisation.

As in other East European countries the liberalisation experience in Lithuania was rather different from that of Western European countries. Darškuvienė describes in her chapter that the takeover of the national telecom monopoly by Nordic telephone companies was accompanied by major job losses in the company itself, whereas employment in the sector increased markedly. This

tended to be to the disadvantage of older workers, while benefiting those with new skills. The sector – about one third of whose employees remain in publicly owned firms – has experienced rapid expansion but as in telecoms this overall expansion has gone hand in hand with job losses in existing companies.

Overall, job losses in the formerly publicly owned companies seem to be the order of the day. In some cases, though, this has been offset by employment gains in competitors and in some cases also via expansion of former national monopolies abroad. In a number of sectors, especially telecommunications, technological and demand-side effects (the rise of mobile telephony) have swamped the concurrent privatisation impacts.

The extent to which job losses due to privatisation are cushioned by social measures depends strongly on the bargaining power of workers and on the legal regulations (especially where unions are weak, as in Lithuania). In this regard, there are various mechanisms to alleviate the impact of retrenchment. Many privatised businesses have made use of early retirement, severance payments and bonuses for employees who take voluntary redundancy. Furthermore, there are often accompanying measures to facilitate the reintegration of laid-off workers into other forms of employment (help with job search, mobility assistance, retraining or vocational training, job creation schemes). Such measures are also part of the policy of making privatisation socially acceptable.

### **3.2 Effects on consumers**

Some of the chapters make it possible to draw conclusions concerning the kind of effects privatisation and liberalisation of services have had on *consumers*. A popular argument put forward by privatisation proponents is that by increasing competition privatisation will lead to more choice for consumers and better prices.

In the Dutch electricity market consumers have been offered more choice. Over recent years prices have gone up, however, although this was due mostly to the almost continuous increase in oil prices. In the German postal sector the impact on service quality has been mixed: delivery times have improved and business clients are offered discounted prices, but a large number of local post offices have been closed. Similar trends can be seen in Sweden where the new company (Posten AB) retains an overwhelming share of the letters market but the competitive threat has nevertheless led to the widespread closure of traditional post offices. For the Swedish electricity sector studies of the impact on prices are conflicting since it is difficult to

separate the effects of privatisation from other factors. Concerning private hospitals in Germany the staff to patient ratio is considerably lower than in public ones and there is some evidence that commercial pressures are reducing the length of hospital stays. In the UK the privatisation of cleaning (and the associated cuts in pay and conditions) has been implicated in sharp falls in standards, leading to an injection of substantial government funding. Water consumers initially faced drastic increases in their water bills, although this was subsequently corrected under public pressure after a change of government. In Lithuania, finally, significant improvements in the provision and quality of public services were accompanied by cost and price increases, not least due to the dominance of oligopolistic structures after privatisation.

### **3.3 Wages and working conditions**

The effect of liberalisation and privatisation on wages and working conditions is addressed in two ways in this volume: directly, in the various case studies of the impact of privatisation and liberalisation processes, and indirectly, through the comparison of wages and working conditions in the public and private sectors in a number of countries, based on individual and firm-level micro data.

A first important conclusion is that liberalisation and privatisation tend to lead to a deterioration of wages and working conditions. The case studies show that both processes induce companies to look for ways of reducing labour costs; apart from the earlier discussed downward adjustment of the number of jobs, this is also reflected in pressure on wages and working conditions. This pressure may stem from increased competition following liberalisation or from changes in corporate governance in the case of privatisation. For example, liberalisation of the postal sector in Austria, the Netherlands, Sweden and Germany has led to the entry of new competitors alongside the former monopoly providers (see the chapters by Hermann and Atzmüller, Thörnqvist, and Brandt and Schulten). These new competitors pay considerably lower wages than the former monopolist and employ their workforce on more flexible contracts. In Germany, hourly wage rates paid by the new competitors are between 25% and 50% below those of the former monopoly provider Deutsche Post AG, while those newly employed by Deutsche Post AG itself are hired at lower wages than their colleagues. In Austria the majority of the workers employed by the new mail operators are self-employed, lacking any form of employment protection, but also earning significantly less than regular postmen employed by the former monopoly provider Austrian Post AG. In this way, pressure is exerted on wages and working conditions in the entire sector.

Similar processes can be observed in other countries and sectors. Van der Meer shows how wage levels in one of the major companies in the liberalised (but still largely publicly owned) electricity sector in the Netherlands have been adapted to the market average for newly entering employees, who earn about 24% less than existing workers, and that a substantial part of the workforce has been put on flexible contracts. Increased competition and budgetary pressure in the Dutch home care sector have spurred domiciliary health care organisations to substitute part of their qualified nursing labour force by unqualified housekeeping employees to reduce labour costs and also partly to replace qualified staff by self-employed persons who work on their own account and are not covered by the collective agreement and related pension and social benefits entitlements in case of illness or unemployment.

Following liberalisation in the German health sector, private hospitals pay lower wages than those common in public hospitals, while staff are expected to treat more patients. In a more direct fashion, in the UK the privatisation of bus companies resulted in immediate cuts in basic wages and an extension of working time, while health workers had to make concessions on pay (and conditions) in order to secure service contracts. Such direct wage cuts or working time extensions affecting the workforce already employed in the public companies remain exceptional, however. More often these employees are faced by reductions of supplements and benefits and by increased flexibility demands.

The results of the case studies are supported in a more general and indirect manner by the quantitative comparison of wages and working conditions in the public and private service sectors. The chapters by Leschke and Keune, Ghinetti and Lucifora, and Meurs and Ponthieux show that wages in the public sector are higher than in the private sector in the eight countries they discuss. Although this can to a large extent be explained by differences in sectoral composition (characteristics of organisations and employees) there is also an independent public sector pay premium. This premium exists along the wage distribution but is in most countries highest for the lowest wage levels, for the unskilled and for women. In this sense the public sector exhibits greater equality than the private sector. This suggests that in these countries privatisation would lead to a lowering of wages, in particular for the low skilled and for women. The stronger the public sector pay premium, the stronger this privatisation effect would be. At the same time, as Ghinetti and Lucifora argue, the more compressed wage distribution in the public sector not only includes a higher 'floor' but also a 'ceiling' that often remains below private sector wages for the highest skilled.

As far as non-wage issues are concerned, the picture is more mixed. Leschke and Keune show that in the German public sector, all other things being equal, workers are less likely to be affected by excessively short or long working hours; in the UK, however, this is not the case. According to Hermann and Atzmüller the direct extension of working hours after privatisation is exceptional (examples include local transport in the UK and railways in Germany), but a range of indirect measures are applied to lengthen the working day. These include the reduction of the number and shortening of the length of breaks and time-off periods in addition to those required by law (for example, additional holidays). Often, the impact of privatisation and liberalisation on working conditions varies between categories of workers. In the Swedish electricity sector, for instance, blue-collar workers' representatives were highly critical of changes in working conditions and practices, training opportunities, and so on, whereas union officials representing white-collar workers were more positive (Thörnqvist). Many of the case studies and some of the empirical studies give examples of deterioration in terms of contracts (for example, increasing use of fixed-term contracts, marginal part-time employment and (own account) self-employment) and reports of increased workload, stress, greater insecurity and less job satisfaction.

As regards training provision outcomes are not clear-cut. Whereas Leschke and Keune conclude for the UK and Germany that the public sector provides more training than the private sector, van der Meer points out that in the liberalised Dutch electricity sector for most staff internal career possibilities have improved, whereas in the public transport sector HRM and training policies are being reduced.

Chung shows that in 14 of the 21 countries she analyses public sector employees are offered more work–life balance options, while in the other seven the private sector makes more such options available. She concludes that in the former privatisation may lead to fewer possibilities for employees to balance work and life, but in the latter it might actually improve such possibilities.

### **3.4 The role of institutions and changes over time**

The above-discussed differences between the public and private sectors show important variations across countries and sectors. For example, although in all countries discussed in this volume the public sector has a more compressed wage structure than the private sector, the distance between the two is larger in some countries than in others. This suggests that national and sectoral institutional factors – that is, norms, rules and regulations – influence

the differences between the two sectors and, by extension, also mediate the effects of liberalisation and privatisation processes on wages and working conditions.

Indeed, as van der Meer suggests, the relationship between liberalisation, privatisation and employment conditions appears to be a complex one, involving interaction between various levels: European regulations, national regulations, sectoral characteristics (that is, type of competition, type of 'market', sectoral collective agreements), enterprise policies (possibly at the level of the multinational headquarters) and establishment policies and interactions between companies and (organised) employees. The chapters in this volume present some evidence on these various levels, in particular the national and sectoral dimensions.

Where differences between countries are concerned, Ghinetti and Lucifora show that in Italy, France and the UK the pay gap between the public and private service sectors is 29%, 25% and 16%, respectively, while intra-country differences between the various NACE sectors also show substantial differences. They argue that the fact that public–private wage differences are so much higher in France and Italy than in the UK stems from a number of institutional factors. These include the fact that in France and Italy wages and working conditions are set in a much more centralised manner – especially in the public sector – than in the UK where it is strongly decentralised; the fact that wage setting in the public sector in the UK takes the private sector as a reference to an important extent, while in France and Italy the development of the cost of living and the conditions of the public budget are much more important; and the fact that in France and Italy an important part of public sector employees are employed on lifetime contracts in which seniority plays a key role. Where work–life balance options are concerned, Chung shows that the differences in their provision by public and private companies are affected by the extent to which national regulations establish such options for workers in all sectors of the economy.

Turning to the sectoral level, van der Meer shows that the way in which competition is institutionalised here affects company HRM policies and the definition of wages and working conditions. Similarly, sectoral agreements are shown to establish a floor in the sectoral labour market, while their absence allows for a more aggressive downscaling of wages and working conditions. The latter is often the case in sectors in which there was previously a monopoly provider (and thus a company, rather than a sector-wide, multi-employer agreement). When such sectors are liberalised the former monopoly provider often has a relatively worker-friendly collective

agreement, but new competitors are not bound by this. An example of the latter is the German postal sector. New entrants in this market started to aggressively underbid Deutsche Post AG. One effect of this was that at Deutsche Post AG, too, wages and working conditions were affected negatively. But another was the demand from trade unions and, in part, political parties for a state-set sectoral minimum wage to prevent this downward spiral from getting out of control (Brandt and Schulten).

Finally, there is the issue of institutional change. Two major issues emerge here. One is the relationship between changes in national models of labour market regulation and the effect on the public and private sectors. Leschke and Keune show that the UK and Germany followed quite opposite processes of macro-level institutional change between the mid-1990s and the mid-2000s, with the UK going through a (limited) re-regulation of the labour market under New Labour, while Germany progressively deregulated its labour market through the Hartz reforms. As a result, in the UK several aspects of wages and working conditions improved, while in Germany they deteriorated. Interestingly, in both countries both the public and private sectors followed the general trend and differences between the two remained largely stable or increased slightly. This points to the fact that the national regulatory framework of the labour market plays a key role in setting the boundaries for both sectors.

The other issue is that today's public sector does not resemble the public sector of three decades ago. Whereas, as argued by Hermann and Atzmüller, the public sector previously played a key role in ensuring full employment (notably by hoarding labour during economic downturns) and as a pacesetter for the improvement of private sector employment and working conditions, today this is much less the case. With the turn to neo-liberalism and the growing importance of New Public Management-type philosophies, private sector principles have progressively been introduced in the public sector since the 1980s (see, for example, OECD 1995) and this trend towards a recommodification of public sector employment does not seem to be slowing down. The danger with this switch to private sector standard setting as far as labour conditions are concerned is that the overall trend may become one of downward adjustment and polarisation in both sectors.

## **Conclusions**

The chapters of this book contribute to the debate on the actual and potential effects of privatisation and liberalisation of services through a series of case studies and quantitative and comparative analyses. As far as the 'economic' effects of privatisation and liberalisation are concerned, the case studies



demonstrate that these are anything but clear-cut. In terms of production volumes and investment the cases show that there are no general positive or negative trends. The same goes for the effect on consumers, as choice often improves whereas the impact on prices and quality can go either way, depending on the sector and the specific policies adopted. Where productivity is concerned, the case studies suggest increased productivity for all industries under scrutiny, but the extent to which this is due to greater investment and better work organisation or to a worsening of working conditions and/or job losses remains unclear. What is clear is that the positive expectations concerning the economic effects of privatisation and liberalisation of services that dominate today's political debate and mainstream economics are far too simplistic and one-sided.

The studies are more straightforward in their conclusions on the effects on employment and wages. As far as employment is concerned, liberalisation and privatisation clearly lead to job losses in the companies concerned. In some cases this is accompanied by employment gains in competitors or by the expansion of former national monopolies abroad, while increased demand may also have positive employment impacts. But the overall effect is one of employment decline.

Wages, too, are clearly negatively affected by liberalisation and privatisation in the case studies considered, in particular where newly-hired workers are concerned. Moreover, the comparative studies all show a public sector pay premium across Europe, even allowing for other differences in sectoral characteristics. Overall, workers appear to 'pay the price' for privatisation and liberalisation through increased pressure on wages, and this affects most of all the lower qualified and women. Where working conditions are concerned, the effects are somewhat less clear, although on balance privatisation and liberalisation seem to be associated with a worsening of conditions, again for the weakest groups on the wider labour market.

A further point demonstrated by several of the chapters is that the labour market effects of privatisation and liberalisation are mediated in an important way by national and sectoral institutional factors, which may magnify or dampen the severity of their effects on employment, wages and working conditions.

These conclusions point to three important political lessons. One is that the prevailing simplistic and optimistic expectations of privatisation and liberalisation should be abandoned. A far more realistic and evidence-driven approach is needed. Second, the negative effects of such processes on workers, today not a core element of the debate, require much more attention

and should be part and parcel of decision-making processes when reforms are considered. Finally, when privatisation and liberalisation take place, politics can play a key role in cushioning their social effects.

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I. Effects of privatisation and liberalisation on efficiency, productivity and employment



## **Privatisation and liberalisation of public services in Germany: the postal and hospital sectors**

### **Introduction**

The postal sector has already undergone transformation from a state monopoly to a fully liberalised and privatised market, with far-reaching consequences for consumers and employees. More recently the postal sector became a prominent issue in the German public debate, since it was obvious that, without social regulation, the new element of competition in the liberalised postal market would have been introduced almost exclusively at the expense of the employees. The outcome so far has been the introduction of binding minimum wages for employees in letter services.

In contrast, hospital sector privatisation is part of an ongoing privatisation and liberalisation process which is highly disputed, with many conflicts emerging at local level. While public and non-profit clinics still account for the majority of hospitals, private hospital corporations are increasingly gaining importance.

The postal and hospital sectors are of particular interest because Germany is a European forerunner with regard to privatisation and liberalisation in these areas. Before we analyse their development, we will give a short overview of privatisation as a whole in Germany.<sup>1</sup>

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<sup>1</sup> This chapter is partly based on findings of the EU research project 'Privatisation of Public Services and the Impact on Quality, Employment and Productivity' (PIQUE), which is a three-year project funded by the European Commission's 6th Framework Programme (Project Number: CIT5-2006-028478) It involved research centres from six European countries (Austria, Belgium, Germany, Poland, Sweden and the UK (see: <http://www.pique.at/>).

## 1. Overview of privatisation in Germany

In contrast to many other European countries Germany has never experienced a broad wave of nationalisations; the number of national state-owned industry companies has always been limited. The public sector has been concentrated mainly in general public services, such as telecommunications, postal services, large parts of the transport sector and

**Table 1:** *Reorganisation phases of the public sector, Federal Republic of Germany*

Phase	Government	Policy guidelines for the public sector	Mode of privatisation
1949–1984	Led by CDU (1949–66) Great coalition of CDU and SPD (1966–69) Led by SPD (1969–82)	‘Expansion of the public sector’	A few privatisations of industrial firms in the mid-1960s
1984–2000	Led by CDU (1982–98) Led by SPD (1998–2005)	‘More private – less state’ (consolidation of public budgets, promotion of ‘national champions’, strengthening of international competitiveness)	Since 1984, privatisations of industrial companies and first outsourcing measures of local public services Since 1990, change from public to private legal forms of public-owned companies Between 1990 and 1993, privatisations of state-owned enterprises in East Germany after unification Since 1996, large-scale privatisations of (nationwide) public infrastructure
Since the new millennium	Great coalition of CDU and SPD (since 2005)	Between ‘priority for the private sector’ and ‘public–private partnerships’	Privatisation of social, municipal infrastructure Privatisation of social security

Source: Modification of Deckwirth (2007: 72).

public utilities (Deckwirth 2008). At national level the most important state-owned enterprises have been the Federal Post and the Federal Railway companies. In addition, large parts of the German public sector can be found at the level of the Federal States and at municipal level. Compared to other European countries the municipalities have strong political autonomy and are important economic actors at local level. Broadly speaking, three privatisation waves and overlapping reorganisation phases of the public sector can be distinguished in Germany (Table 1).

### **1.1 Privatisation up to the mid-1980s**

After the Second World War until the mid-1980s ‘expansion of the public sector’ was the policy guideline. The governments led by the Christian Democratic Party (CDU) (1940–69) considered the public sector crucial for economic reconstruction and growth. At least since the late 1950s the Social Democratic Party (SPD), as well as the German trade unions, have abandoned their more far-reaching nationalisation plans. In the first half of the 1960s there was a first wave of (partial) privatisations which, however, affected only a few industrial enterprises. In the 1970s SPD-led governments did not carry out any major privatisation but instead promoted expansion of the public sector.

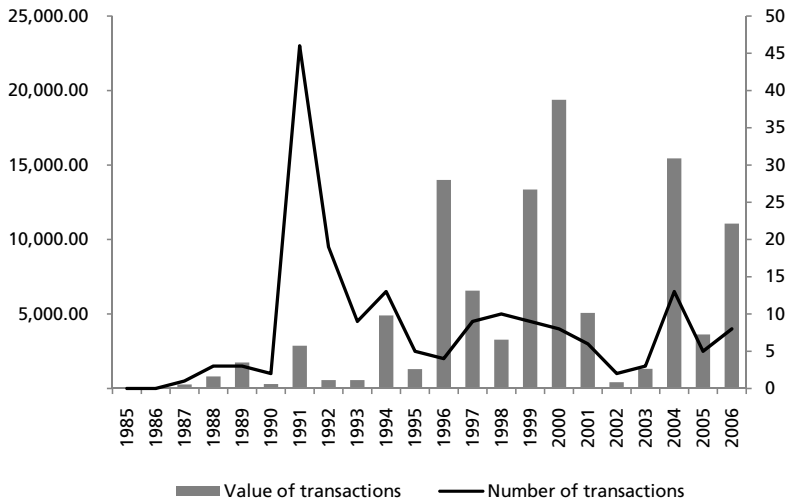
### **1.2 Privatisation milestones between the mid-1980s and 2000**

In the 1980s Germany saw a general shift towards more neo-liberal policies, including more fundamental restructuring of the public sector, and ended up with a new phase of privatisation. The new policy guideline was now: ‘More private – less state’. Besides ideological considerations major drivers of privatisation were the growing deficits of public budgets, the promotion of ‘national champions’ (for example, in telecommunications and postal services) and the general strengthening of international competitiveness. A first wave of privatisations took place in the second half of the 1980s, focussing on industrial companies, such as VIAG, VEBA, Volkswagen and Lufthansa (Tofaute 1992, 1994). The number of share companies held by the Federal State decreased from 808 to 132 (Deckwirth 2008). In addition, the first outsourcing of local public services – for example, in local public transport – took place.

After German Reunification in 1990 the East German economy was transformed from a centrally-planned state economy into a market economy. This process was accompanied by a major wave of privatisations. Although the value of the transactions involved was relatively low in comparison to the



**Figure 1:** *Privatisations in Germany; value (USD million) and number of transactions*



Source: Privatisation Barometer (<http://www.privatizationbarometer.net/>)

value of the privatisation of national infrastructure companies in the late 1990s (Figure 1), they had a significant political and ideological influence in promoting the idea of privatisation, also in West Germany. Apart from that, it was also the policy of the European Union, which enforced privatisation policies in Germany through its liberalisation policy in core sectors of public infrastructure and indirectly through the adoption of the Growth and Stability Pact, which increased the pressure to reduce fiscal deficits.

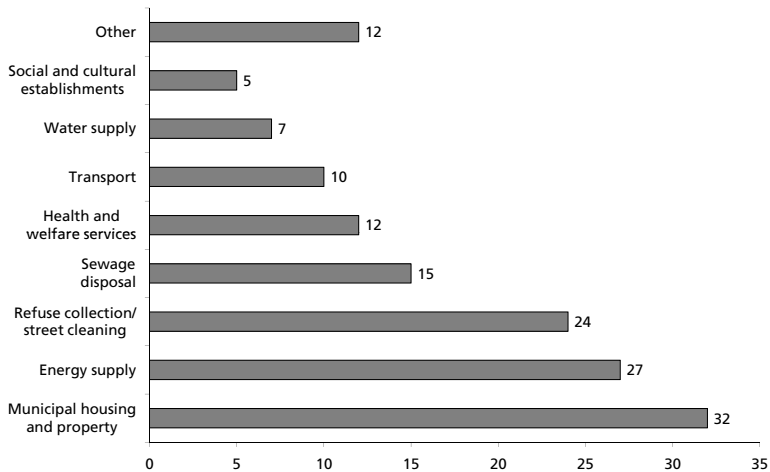
Before the full privatisation of public companies there was usually a process of restructuring, which included the change from a public to a private legal form. From the mid-1990s the German government started to issue public tenders for (nationwide) public infrastructure enterprises. In 1996 revenues increased mainly through the public tender of 26% of the capital of Deutsche Telekom. Privatisation of the telecommunication sector in particular was linked with price-cutting for consumers and technological innovation. These arguments were used for further privatisations in other sectors (Deckwirth 2008). The change to a new government led by the SPD in 1998 did not lead to a change in privatisation policy; on the contrary, according to Privatization Barometer the value of privatisation transactions reached its peak in 2000. Among the most significant transactions of this period were the partial sales of Deutsche Telekom and the initial public offer of Deutsche Post.

### **1.3 Increasing privatisation of local social infrastructure since 2000**

From 2000 Germany entered a new phase with an increasing number of privatisations of municipal infrastructure (housing, hospitals, education) and social security schemes (health- and pension insurance). This process increased with the massive privatisation of state-owned residential properties in 2001 (114,000 housing units owned by Deutsche Bahn AG). Furthermore, partial privatisations of municipal utilities and infrastructure were concluded in 2001 and 2002. Generally, since 2001 the policy guideline for the public sector has been somewhere between positive proclamations of 'Priority for the private sector' and 'Public-private partnerships'. The proclamation of public-private partnerships can be interpreted as a reaction to the increasing number of privatisation critics. Nevertheless, privatisation of public network infrastructure has continued: in 2004 and 2005 further shares of Deutsche Post and Deutsche Telekom were sold. In 2005 a new coalition government led by the CDU was formed, but this brought about no policy change: 2006 and 2007 were characterised by major sales of both central and local States' assets, involving shares in Deutsche Telekom AG and WestLB banking group and, at local level, sales of housing organisations. On the other hand, the initial public offering of German Railways, originally planned for 2006, has been postponed to 2009.

The emergence of new areas of privatisation affecting social and municipal infrastructure is significant because in Germany municipalities currently account for around two-thirds of all public investments (Deckwirth 2008). According to a representative survey carried out by Ernst & Young a growing number of municipalities have carried out privatisations in areas such as municipal housing, energy and water supply, refuse collection, sewage disposal, health care and social services (Janetschek 2007; Figure 2). Cities which have been active in privatisation represent more than 50% of the German population (Richter et al. 2006: 114, 121). This has been legitimated with reference to financial problems due to tax reforms and decreasing tax revenues (Janetschek 2007: 5).

**Figure 2:** *Privatisations by German municipalities (%)*



Note: \* in % of all municipalities which have experiences with privatisations.

Source: Janetschek (2007).

## 2. The German postal sector

The privatisation and liberalisation of postal services in Germany shows some interesting features in contrast to other European countries. Germany is one of the very few countries in Germany where private shareholders hold a majority of shares in the postal incumbent. Before the complete opening up of the letter market there was a significant increase in competition. Complete liberalisation in 2008 was directly linked with the introduction of a special statutory minimum wage for letter services, which has caused massive political conflicts and affected the current public debate on the introduction of a general minimum wage in Germany.

### 2.1 The process of privatisation and liberalisation

Prior to privatisation the Federal Postal Service (Deutsche Bundespost), as part of the Federal Administration, was responsible for postal- and telecommunication services. It was controlled by the former Ministry of Post and Telecommunication and had a monopoly on items weighing less than 20 kg. In the 1980s discussions started about the privatisation and liberalisation of the postal sector (Cox 1999; Wehner 2005). In 1985 the conservative-liberal government appointed a government commission with the aim of reorganising the postal and telecommunications sector. Later, in 1989 the so-

called First Postal Reform (Postreform I) was enacted against the resistance of the opposition Social Democrats and the German Postal Workers' Union (Deutsche Postgewerkschaft, DPG). The Federal Postal Service was divided into three state-owned companies: postal services, financial services and telecommunications services. The monopoly of the Federal Postal Service was maintained (Brandt 2007). In the course of the Second Postal Reform (Postreform II) of 1995, all three postal corporations were transformed into public limited companies. The successor of postal services was renamed Deutsche Post AG (DPAG). In advance of this (1994), the German constitution was amended to allow privatisation of these enterprises. After 1998 significant liberalisation steps were followed by the Third Postal Reform (Postreform III) as a result of the new Postal Act of 1997, which transposed the first European Postal Directive of 15 December 1997 into national law. Hereby the German postal market was gradually opened up in keeping with the EU timeframe by lowering the weight limit for the reserved letter post market to 50 grams by 2006. The end of the exclusive license was originally set at 2002, but was later extended until the end of 2007. The German postal reforms of 1995 and 1998 were largely influenced by the EU. According to former German Minister of Post and Telecommunication Wolfgang Bötsch, it was 'clear to all political parties and unions that the EU decision to liberalise the postal market would reduce jobs' (WDR5 2007: 23).

Since 1998 DPAG has acquired several other companies abroad. In November 2000 the privatisation of DPAG began with its initial public offer (IPO) and the DPAG was renamed Deutsche Post World Net (DPWN). Since 2005 private investors have held a majority of shares in DPWN, currently the world's leading logistics company due to a worldwide buying up of logistic and express companies.

## **2.2 Impact on market structure and employment trends**

As already mentioned, by 2006 the weight limit for the reserved letter post market was reduced to 50 grams. In addition, some exemptions were introduced, for example, for the so-called D-license for 'premium services' (for example, same-day delivery), which are a German construction and not based on EU directives. These exemptions in particular have led to the opening up of new business areas for competitors. Since 2006, 50% of the letter market has been open to competition (Bundesnetzagentur 2007a: 114).

There has been a strong increase in the number of new postal companies, too, mostly small companies offering their services on local markets. Since around 2004 a market adjustment has taken place in favour of companies with a turnover of more than €1 million (Table 2).

**Table 2:** *Number of new letter companies and turnover, 1998–2007*

Year	> €10,000	€10,001– 100,000	€100,001– 500,000	€0.5 mil.– 1 mil.	€1 mil.– > 10 mil.	> €10 mil.
1998	30	51	26	3	7	3
2000	91	178	129	23	15	4
2002	96	186	149	32	41	7
2004	181	263	175	53	77	10
2006	116	190	108	39	103	21
2007	110	197	110	43	119	23

Source: Bundesnetzagentur (2007b: 26); data for 2007 are preliminary; DPAG excluded.

In this way two large companies have been established in the letter market by mergers and acquisitions as the two main competitors of DPAG, namely TNT Post, which is a subsidiary of the Dutch TNT, and PIN Group AG, whose shareholders are mostly newspaper publishers. Both companies have managed to build up their own nationwide delivery infrastructure, mainly through the acquisition of local postal companies. In contrast to the large number of other new competitors, they do not focus exclusively on lucrative business post in urban agglomerations. Because the number of distributed letters has remained almost constant in recent years, competition has been cutthroat (Input Consulting 2006b).

Although DPAG's market share has fallen in recent years, it was still almost 90% in 2007. But in the liberalised letter market segment the new competitors had achieved a market share of 25.5% by 2007, up from 21.5% in 2006. This is an enormous increase and represents a turnover of €1,274 million (in 2007). TNT and PIN Group AG together had a turnover of €400 million in 2006 (Bundesnetzagentur 2007b). In contrast, DPAG's letter services had a turnover of €13,286 million in 2006, that is, 22% of the total turnover of the consolidated company DPWN with its different business areas (letter, logistic, financial services). DPAG's profits in 2006 were €2,054 million (EBIT margin) in its letter business unit, that is, 53% of the total profits of DPWN, €3,872 million (Deutsche Post World Net 2007).

Before privatisation at the end of the 1980s almost 400,000 persons were employed by the Federal Postal Service (Lotz 2007). During the 1990s the company reduced employment on a massive scale to the historical low of 260,520 in 1998 (Table 3); prior to privatisation the share of civil servants was above 50% but it had fallen to 12% by 2006. However, due to the

**Table 3: Changes in employment at Deutsche Post World Net (DPWN)\***

	Employees	Full-time equivalents	Germany** (full-time equivalents)	Civil servants	Letter business unit (full-time equivalents)
1995	308 502	268 512			
1996	287 695	250 131			
1997	270 817	233 350			
1998	260 520	223 863			
1999	301 229	264 424			142 332
2000	324 203	284 890	227 092		140 613
2001	321 369	283 330	223 555	77 688	137 130
2002	371 912	334 952	219 067	73 157	133 692
2003	383 173	348 781	207 398	70 130	133 651
2004	379 828	340 667		67 618	126 913
2005	502 545	455 115		64 491	125 282
2006	520 112	463 350		62 560	129 922

Notes: \* In each case by 31 December. \*\* Since 2004 separate data for Germany are no longer published.

Source: Deutsche Post World Net, company reports 1997–2006.

company's expansion abroad total employment at DPWN increased to 520,112 in 2006; the share of employees working in Germany is now below 50%.

Especially in DPWN's letter business unit there has been a considerable reduction in employment due to workflow rationalisations. This was linked to the introduction of letter sorting machines from the beginning of the 1990s and organisational measures, such as the contracting out of transport services or the extension of the letter delivery districts of employees, which caused an increase in workload (Wehner 2005).

Regarding liberalisation, currently around a quarter of all employees in the German letter market are employed by the new competitors (Table 4).

After liberalisation of the letter market DPAG shed around 29,100 jobs between 1999 and 2006, whereas new competitors have created around 30,500 new jobs (Bundesnetzagentur 2007b). But the latter new jobs are predominantly (58% in 2006) based on marginal part-time employment (so-called 'mini-jobs'), which offer maximum wages of €400 per month and

**Table 4:** *Employees in the letter market, Germany (annual average 2006)*

	DPAG		Competitors		Total	
Full-time	92 413	62.4 %	8 618	17.9%	101 031	51.5 %
Part-time	50 116	33.8%	11 625	24.1%	61 741	31.5 %
Marginal part-time	5 566	3.8 %	27 928	58.0%	33 494	17.0 %
In total	148 095	100%	48 171	100%	196 266	100%

Source: Bundesnetzagentur (2007b: 40, 41); own calculations.

mean that workers have to rely on supplementary income from state benefits, tantamount to a job subsidy to the employer. In contrast, in 2005 DPAG had more than 1,600 subcontractors, which often provide only precarious employment (Bundesnetzagentur 2007a). Due to the strong increase in part-time jobs the employment balance (in working hours) has decreased in the letter market (Input Consult 2006).

### 2.3 Impact on labour relations and working conditions

Initially, the trade unions campaigned against the privatisation of the Federal Postal Service. After the privatisation was finally decided they changed their strategy and focused on the social consequences of the privatisation process. Based on a trade union density of almost 80% the unions tried to use their political weight in order to prevent operational redundancies and to maintain the rights of the post office civil servants. Indeed, the massive reduction in employment took place without any operational redundancies. This was made possible by ‘natural wastage’, early retirements, partial retirements and redundancy payments (Wehner 2005: 44). The latter was possible only because of the unions’ readiness to take industrial action, as, for example, when the union held the longest strike in the history of the German Post in 1995 (Völlings 2004).

In 2003 an ‘employment pact’ was concluded between DPAG and the United Services Union (Ver.di)<sup>2</sup> in which the company promised that there would be no operational redundancies until the end of March 2008. In return, trade unions accepted longer working hours, more part-time employment and

<sup>2</sup> In 2001, the German Postal Workers’ Union (DPG) was one of five unions which merged to form the United Services Union (Verdi).

relocation of employees. They also accepted dismissals with the option of altered conditions of employment.

A central point in the bargaining process was the development of a new framework collective agreement incorporating lower wages. In 2001 a new framework collective agreement was introduced with a new pay scale system for bluecollar workers (for example, delivery workers) and in 2003 for whitecollar workers. As a result a new two-tier wage system was introduced whereby the differences in wages for established and newly hired employees doing the same job have been up to 30% (Brandt et al. 2007). Employees taken on before 2001 are paid on the basis of a collective agreement (DPAG Besitzstand) with a higher wage level (currently about 75% of all employees). In contrast, employees taken on since 2001 are paid on the basis of the lower agreement (DPAG Tarifvertrag). Some newly hired employees have only a temporary employment contract (with a duration of three or six months) and have a higher workload, for example, when they are assigned in different delivery districts.

But working conditions at the new competitors are even worse; none of the latter have signed valid collective agreements. Trade union density was estimated to be well below 10% and less than 4% of the employees have a works council (Input Consult 2006: 58). Due to the large proportion of precarious employment and the strong resistance on the management side it has been hard for trade unions to organise the employees. As a result, large-scale wage dumping has occurred in the German letter market. Wages at the

**Table 5:** *Pay and working conditions of a German delivery worker 2006\**

	PIN AG **	DP AG (DPAG Tarifvertrag)
Basic pay per month***	€1 020.00	€1 765.88
Basic pay per hour ***	€5.86	€10.54
Weekly working time	40 hours	38.5 hours
Holidays	21 days	29 days
Holiday pay	€0.00	€332.34
Annual bonus	€0.00	€1 765.88
Overtime bonus	0%	25%

*Notes:* \* 35 years old with 5 years of employment. \*\* In the Berlin region. \*\*\* Without premium payments.

*Source:* Ver.di 2007.



two most important competitors (PIN AG Group and TNT Post) are 30–60% below the level of DPAG (Input Consult 2006: 90). In 2006, the majority of new competitors paid their delivery workers a hourly wage of between €6.5 and €8.0 in West Germany and between €5.0 and €7.0 in East Germany (ibid.: 48). The new competitors usually do not pay annual bonuses or holiday pay either. In contrast, hourly wages for delivery workers (including fixed holiday pay and annual bonuses) at DPAG in 2007 started at €11.43 (DPAG Tarifvertrag) and €16.78 (DPAG Besitzstand) (Teuscher 2007).

Wages for full-time employees at the new competitors are often not high enough to guarantee a certain subsistence level; the employees are therefore entitled to additional social benefits.

#### **2.4 Political conflict concerning a sectoral minimum wage for letter services**

In 2007 liberalisation of the letter market and its effects on working conditions was one of the central topics of German political debate: the public was generally aware of the emergence of cutthroat competition based on wage dumping. Against this background both DPAG and the United Services Union Ver.di demanded that the opening up of the market should be postponed, arguing that the government should not give postal companies from abroad market access when other European countries were still unwilling to open up their markets. Ver.di followed a double strategy. On the one hand, it increasingly tried to influence the regulatory agency's licensing. On the basis of the German Postal Act of 1998 they stated that postal licences should be approved for competitors only if their wages are similar to those paid by DPAG (Brandt and Schulten 2007). This resulted in conflicts based on judicial opinions and surveys of working conditions. On the other hand, Ver.di tried to reach collective agreements with the main new competitors in the letter market. A precondition for this seems to be that the union strengthen its organisational basis in these companies. However, trade union initiatives to organise the employees at, for example, PIN AG have sometimes encountered strong resistance on the part of the local management.

One successful action was organised by Ver.di in Berlin (Frank 2007). The main business clients of PIN AG in Berlin – such as the public administration – and the press were provided with information about working conditions at PIN AG. The pressure to accept works councils and start negotiating a national collective agreement was increased. Finally, the Berlin Senate declared in 2007 that in public tenders it would consider only firms that have concluded collective agreements. Thereupon PIN AG Group engaged in

collective bargaining for the first time. But according to Ver.di, in the course of the bargaining process – August 2007 – PIN AG suddenly halted the bargaining process (Teuscher 2007, 2008).

On 24 August 2007 the government coalition of the Christian Democrats and Social Democrats reached an agreement according to which full liberalisation of the letter market from 2008 should be accompanied by the introduction of a branch-level minimum wage for letter services in order to avoid further downward competition on wages. The minimum wage should be based on a collective agreement which afterwards would be extended to the whole sector via the German Posted Workers Act (*Entsendegesetz*). A few days previously, on 21 August 2007, DPAG, together with some smaller postal companies – but without the participation of its main competitors, PIN Group and TNT – established a new employers' association for postal services (Arbeitgeberverband Postdienste e.V.). In September 2007 this employers' association, together with Ver.di, signed a new collective agreement on the introduction of minimum wages in letter services, which varies between €8.00 and €9.80 per hour, depending on the job and region (West or East Germany). This minimum wage is significantly above the average wages of most new competitors, but far below the lowest wage grades at DPAG (from €11.43 to €16.78).

While DPAG and Ver.di have asked the government to extend this minimum wage agreement to the whole sector, the new competitors have organised a campaign against it, arguing that such a minimum wage would only safeguard the market position of DPAG. The campaign has been strongly supported by some leading German media corporations, such as Axel Springer AG, the majority shareholder of the Pin Group (Röhm and Voigt 2007). Furthermore, under the leadership of Pin Group and TNT, the new competitors have not only founded their own employers' association, but have also given strong support to the foundation of a new 'trade union' for letter services. Later, these new organisations concluded a separate collective agreement on 'high-order letter services', with a much lower minimum wage rate of €7.50 per hour for West Germany and €6.50 for East Germany. But the German Parliament finally adopted the extension of a minimum wages concluded by DPAG and Ver.di for 'all companies and company units which *predominantly* deliver correspondence for third persons', which became valid from 1 January 2008 (Teuscher 2008).

It remains to be seen whether the new minimum wage will be able to lift wages at the competitors. The latter have sought to circumvent the minimum wage in a number of ways, for example, by using newspaper deliverers as

letter deliverers. Self-employed persons contracted at subcontractors of DPAG will not benefit either. In any case, the market effects are hard to estimate.

## **2.5 Impact on postal service users**

Concerning the impact on postal service users the Postal Act of 1997 regulates the prices of DPAG and the universal service obligation (USO). These regulations are administered by the Federal Network Agency (BNetzA), set up at the beginning of 1998. Through the second amendment of the Postal Act of 1997 in 2001 DPWN was directly obliged to provide universal services during the term of its exclusive license. The content and extent of universal services and the related price level are defined in detail by the so-called Order on Universal Postal Services (Post-Universaldienstverordnung, PUDLV) of 1999 (amended 2001). By means of this order DPWN was obliged in 2001 to keep at least 12,000 so-called ‘postal services facilities’ (that is, post offices) until the end of 2007. The amendment in 2001 was necessary after DPAG had reduced its postal service facilities from 15,331 in 1997 to 12,818 in 2001. Prior to privatisation in 1992 the number of ‘post offices’ was 22,000 (Wehner 2005: 25) – in other words, in the space of 10 years the German Post has closed over 9,000 post offices. Moreover, the number of letterboxes was reduced from almost 140,000 to about 100,000 in 2003. At the end of 2007, there were 12,628 post offices, but less than 50% of the personnel was employed by DPAG; since the mid-1990s DPAG has installed over 7,000 postal service agencies via cooperation-contracts in retail outlets (Bundesnetzagentur 2007b: 57; WDR5 2007). This worsening in postal service availability due to the dramatic closure of post offices (–42.6% between 1992 and 2007) and the cutback of letterboxes has been strongly criticised by the public, especially with regard to the difficulties experienced by the elderly and people living in the countryside.

At the same time, prior to privatisation letters were delivered, on average, in three to four days, but by 2004, DPAG was delivering 87.9% of letters in one day and 99.5% in two days. This was made possible by new large letter sorting centres outside the cities; new letter sorting machines accelerated the distribution of letters. Transport of letters between the new sorting centres and local distribution points in the cities was linked with a shift from railway transportation (previously, sorting centres were located very close to railway stations) to road transportation.

Only the tariffs of DPAG are affected by the price regulation. In contrast to the majority of other European countries, in which prices have increased, private consumer tariffs have remained stable. The prices of the new

competitors are largely below the level of DPAG. Generally, there have been significant price reductions across the board for business clients. According to the regulatory agency, price reductions for regular end consumers are not expected, however. So far, there have been no significant developments concerning new letter products, but an increase in new letter products is expected, for example, discounts for business clients who accept longer delivery times (Bundesnetzagentur 2007b: 34–39).

Since the end of the exclusive licence DPAG no longer has to adhere fully to the universal service obligation. But according to the Postal Act of 1998, in case of non-fulfilment of some universal services the regulatory agency can oblige one or more corporations to provide them. Nevertheless in 2007 DPAG announced that it would voluntarily provide universal services. In contrast to its competitors DPAG is exempt from VAT, arguing that this is necessary in order to finance universal services; its competitors consider this an unfair competitive advantage for DPAG, however.

## **2.6 Conclusions**

Liberalisation of German postal services has led to a deterioration of both service quality (especially postal service availability for the bulk of private costumers) and employment conditions. Business clients, however, have benefited from discounts. Liberalisation has established a mode of competition based mainly on labour costs, leading to a reduction in employment, extremely low wages and an increase in precarious employment, with significant additional costs for the social security system and society as a whole. The liberalisation of German postal services can therefore be seen as a paradigm case for the contention that liberalised markets need strong regulation with regard to social and consumer affairs. All in all, the German experience strongly calls into question the whole purpose of privatisation and liberalisation and sends a warning signal to other European countries currently planning to open up their postal markets.

## **3. The example of the hospital sector**

The hospital sector is another example of Germany becoming a forerunner in the liberalisation and privatisation of public services in Europe. With the exception of France, in no other European country have private for-profit clinics come to account for more than a quarter of the whole. There has been a wave of hospital privatisations in Germany that more recently has included even larger clinics, as well as for the first time a university hospital. These privatisations have been part of a comprehensive restructuring of the German

hospital sector and are the result of a liberalisation policy which promotes the economisation and commercialisation of hospital services through the introduction of market-oriented mechanisms and the encouragement of competition (Wettke 2007). All these developments have had far-reaching consequences for both patients and employees.

### 3.1 Restructuring

There were 2,104 hospitals with more than 510,000 beds in 2006 (see Table 6). Since the beginning of the 1990s hospital capacity in Germany has shown a continuous decline; the total number of hospitals fell by about 13%, while the number of beds decreased by about 23%. In 2006 there were only 620 beds per 100,000 inhabitants compared with 832 beds in 1991. Although the number of hospitalisations has shown a continuous increase, the average occupancy rate fell from 84.1% in 1991 to 76.3% in 2004. The main reason for this was a strong decline in the average length of stay, from 14 days in 1991 to 8.5 days in 2006.

In terms of employment, there are a little over 1 million people working in the German hospital sector. In comparison with the fall in the number of hospitals, the decline of employment has been relatively moderate; since the early 1990s the total number of employees has dropped by about 4.3%. Calculated on the basis of full-time equivalents, however, the decline has been more than twice as high, at 9.6%. This indicates increasing use of part-time and marginal part-time employment in German hospitals.

**Table 6:** *Trends in hospital services, Germany*

	1991	2006	<i>Change 1991/2006</i>
Hospitals	2 411	2 104	-12.7%
Hospital beds	665 565	510 767	-23.3%
Beds per 100,000 inhabitants	832	620	-25.5%
Employees (total)	1 119 791	1 071 995	-4.3%
Employees (full-time equivalent)	875 816	791 914	-9.6%
Cases	14 576 613	16 832 883	+15.5%
Average length of stay	14.0 days	8.5 days	-39.5%
Average occupancy rate	84.1%	76.3%	-9.2%

Source: Statistisches Bundesamt (2007a), calculations by WSI.

Since the early 1990s the restructuring of the German hospital sector has been promoted by fundamental reform of the health care system (Busse and Riesberg 2004). The crucial element has been a fundamental transformation of hospital financing, from a system of full cost coverage to a system of capped hospital budgets (Schulten 2006). Before 1993 all operational expenditures had to be financed from the social health insurance funds, so that it was not possible for hospitals to run a deficit. Financing was carried out mainly on the basis of per diem payments in terms of which each day's treatment per patient was compensated at a flat rate, irrespective of the individual treatment input required. Since 1993 the annual growth in financing for individual hospitals has been restricted to the annual rise in the health insurance funds' revenue, irrespective of the services actually provided. In 1996 the reimbursement system based on per diem fees was replaced by a mixed payment system of per diem fees and case fees.

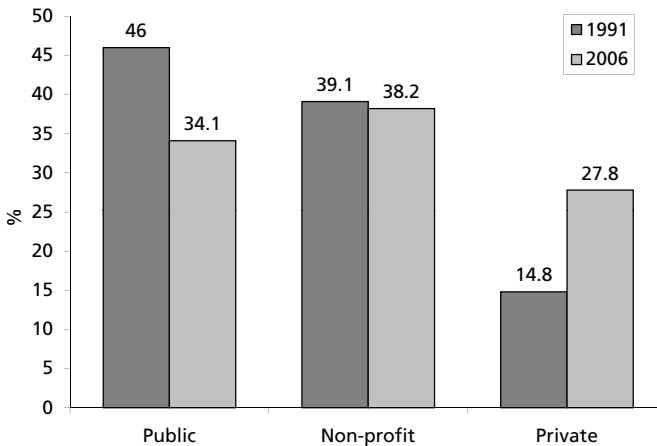
Finally, in 2000 the German Federal Government decided on an even more fundamental change of the hospital financing system, the introduction of the German Diagnosis Related Group (G-DRG) system. The introduction of the DRG system started in 2003 and, after a transitional period, is planned to be fully operational from 2009. The basic notion underlying the DRG system is that every case should be reimbursed by a uniform flat-rate determined by a DRG, irrespective of the actual treatment and the corresponding costs of an individual hospital. It is widely expected that full introduction of the DRG system will further promote the ongoing restructuring of the German hospital sector. According to a study by the Allianz Group Economic Research Department the new DRG system 'brings greater transparency and keeps up the rationalization pressure, particularly for those hospitals whose costs per case are above average. ... But even institutions operating at below-average costs have a strong incentive to continue cutting expenses, since the difference between in-house costs per case and the case-based lump-sum remuneration remains as their operating profit' (Hess 2005: 6). One major consequence of the DRG system will be a further reduction of the average length of stay, since 'the logic behind case fees calls for ideally short hospitalization periods' (ibid.). This will have further organisational consequences for the hospitals which more and more will divide their activities between core inpatient care and supplementary outpatient care. Moreover, the growing rationalisation pressure from the DRG system will lead to a further concentration in the hospital sector. The Allianz study estimates that by 2020 the number of hospitals and hospital beds will have fallen by 20% (ibid.: 11).

### 3.2 Privatisation of the public hospital sector

The German hospital sector has always been composed of a variety of companies and organisations with different ownerships. Besides the public hospitals, which are owned by municipalities, regional districts or the German federal states, there is a long tradition of non-profit hospitals run by Christian churches and various welfare organisations. For a long time there have also been private hospitals, mainly rather small and specialised clinics.

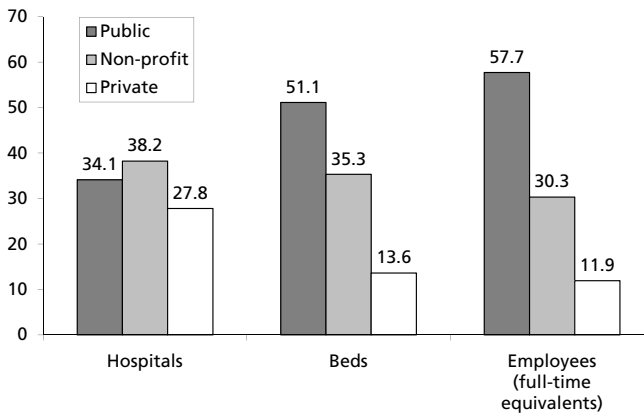
Although the first privatisation of a public hospital took place as early as the mid-1980s, there was not much change in the composition of hospital ownership until the early 1990s. After German Reunification in 1990 a first wave of hospital privatisations took place – mainly in Eastern Germany – as part of the transformation process from a former state-socialist to a capitalist market economy. Since the beginning of the new millennium a second wave of hospital privatisations has got under way, covering all regions of Germany (Bähr et al. 2006). Between 1991 and 2006 the proportion of private hospitals increased from 14.8% to 27.8% (Figure 3), while the share of public hospitals fell from 46% to 34.1%; the proportion of non-profit hospitals remained relatively stable. The decrease in the number of public hospitals has resulted from both the closure of public clinics and sales to private providers.

**Figure 3:** *Ownership of hospitals, Germany, 1991 and 2006 (%)*



Source: Statistisches Bundesamt (2007a), calculations by the WSI.

**Figure 4:** *Proportion of hospitals, beds and employees by ownership, Germany, 2006*



Source: Statistisches Bundesamt (2007a), calculations by the WSI.

Although public ownership is no longer in a majority regarding the total number of hospitals, it still has a dominant position in terms of the number of hospital beds. In 2006 the majority – 51% – of all beds were still provided by public hospitals in comparison to only 13.6% by private hospitals (Figure 4). The dominance of public hospitals in this regard becomes even more pronounced in relation to the number of employees: nearly 58% of all hospital workers were employed in public hospitals, while private hospitals accounted for only 12% of all employees.

Traditionally, hospital privatisation has affected smaller clinics; in recent years, however, Germany has seen a number of cases in which larger hospitals have been privatised:

- In July 2001, the private hospital chain *Helios* bought 51% of the shares of the hospital of the City of Erfurt (*Klinikum Erfurt*), with 1,121 beds. In November 2002 it bought the remaining 49% of the shares, so that *Klinikum Erfurt* is wholly owned by *Helios*.
- In January 2003 *Helios* took over 94.9% of the shares of the hospital of the City of Wuppertal (*Klinikum Wuppertal*), with more than 1,000 beds.
- In 2004 the private hospital company *Asklepios* bought the main hospital group of the Federal State of Hamburg (*Landesbetrieb Krankenhäuser, LBK*), involving seven hospitals with 5,688 beds.



- In January 2006 Germany saw the first privatisation of a university hospital when the private hospital corporation *Rhön Klinikum AG* acquired the university hospitals of Marburg and Gießen from the Federal State of Hesse; together these university hospitals had more than 2,400 beds.

Almost all studies on the German hospital sector assume that privatisation will continue and will increasingly include larger hospitals. Some estimates indicate that the proportion of private hospitals will increase to 40% over the next 10 to 15 years (Hess 2005; Bähr et al. 2006).

The increasing importance of the private hospital sector has led to the emergence of some major private hospital corporations (Table 7). They include four large corporations: Asklepios, Rhön-Klinikum, Helios Kliniken (part of Fresenius) and Sana Kliniken, which account for nearly one third of all private hospitals. All four companies are following a strategy of continuous expansion and are expected to acquire a much larger market share in future.

The wave of hospital privatisations in Germany is first of all the result of increasing public budget deficits rooted in a particular fiscal and tax policy. Since the 1990s the German federal states, which are responsible for the financing of hospital investment, have been more and more reluctant to provide hospitals with sufficient financial resources. Estimates of the current backlog of investment in hospitals vary between €30 and €50 billion (Hess 2005). Moreover, with the introduction of capped budgets many hospitals

**Table 7:** *Important private hospital corporations, Germany, 2006*

	Hospitals (Emillion)	Employees	Turnover
Rhön-Klinikum	45	30 400	1 934
Helios Kliniken	56	26 800	1 673
Asklepios	72	25 700	1 600
Sana	33	12 400	792
MediCin	30	6 900	370
Damp Holding	11	5 600	300
Marseille Kliniken	66	5 200	215
Paracelsus	30	5 000	237

Source: Stumpfögger (2007).

have got into financial difficulties and are no longer able to cover their operational costs. In 2006 the annual balance sheets of about 28% of all general hospitals showed a deficit (Deutsches Krankenhausinstitut 2007: 77).

The financial losses of the public hospitals have to be borne by their public owners, which are often themselves in serious financial difficulties. Against that background hospital privatisation can be attractive to public authorities, for several reasons (Hess 2005). First, the sales revenues might help to reduce the public debt; second, the public authorities are no longer responsible for balancing the financial deficits of the hospital; moreover, they can shift at least part of the costs for needed investments to private providers.

### **3.3 Impact of liberalisation and privatisation on employees and patients**

It is claimed that private hospital companies have a number of competitive advantages in comparison to public hospitals (Hess 2005). First, they have much easier access to private capital markets to obtain the financial resources for investment. Second, private hospital companies are able to operate more efficiently; for example, they are able to realise better economies of scale and synergies through close cooperation between different hospitals within the private hospital chain. Third, private hospital companies maintain that they have much lower labour costs because they are not covered by the more 'expensive' collective agreements of the public sector. According to a survey by the German Hospital Association, only 14% of all employees in private hospitals are covered by the public sector agreements, in contrast to a majority of 62% covered by company or other sectoral agreements and 24% with no collective agreements at all (Table 8).

**Table 8:** *Collective bargaining coverage in German hospitals, 2007 (%)\**

	Public	Non-profit	Private
Public sector agreements	85.7	8.1	14.1
Company agreements	3.1	–	20.3
Other agreements	10.7	17.3	41.6
Special agreements for			
church-related organisations	–	73.6	–
No agreements	0.5	1.0	24.0

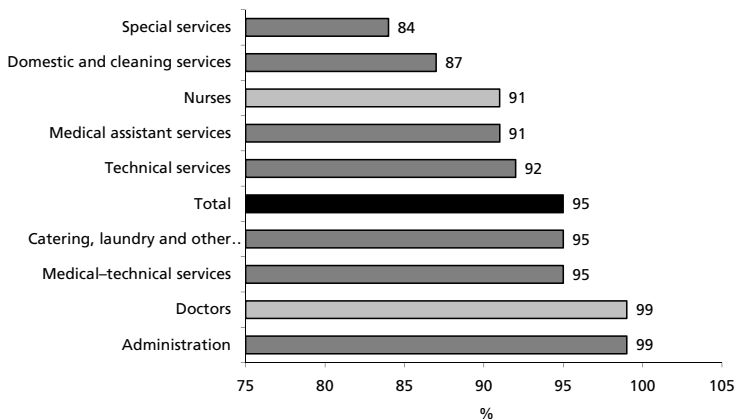
*Note:* \* Coverage of all employees except for doctors.

*Source:* Deutsches Krankenhausinstitut (2007: 62).

Although the trade unions still use – often successfully – public sector agreements as a benchmark for collective bargaining in non-public hospitals (Stumpfögger 2007; Gröschl-Bahr and Stumpfögger 2008), private hospitals have achieved lower labour costs than their public competitors. In 2006 the average costs per employee were 5% lower in private than in public hospitals (Figure 5). In general, private hospitals seem to have a higher wage dispersion. There is almost no difference between public and private hospitals regarding the average costs for doctors or administration staff, but the costs for nurses in private hospitals are 9% lower and for domestic and cleaning services 13%. The latter can also be seen as an indicator that the general trend towards the outsourcing of, in particular, non-medical services – which can be found in all hospitals (Jaehrling 2007) – is even more pronounced in private hospitals. Since labour costs amount to nearly two thirds of overall costs in German hospitals, the differences in pay and other labour costs create a major competitive advantage for private hospital corporations.

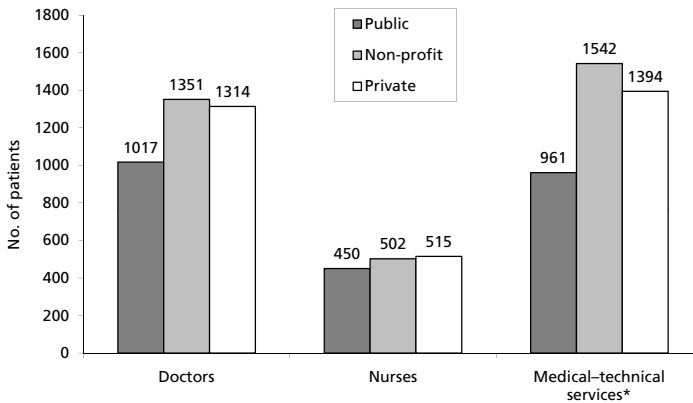
The overall economisation of hospital services through the new DRG-based system of hospital financing has far-reaching consequences for working conditions, irrespective of hospital ownership. Various studies have shown that reorganisation and rationalisation in hospitals has led to strong intensification of work (for example, Marrs 2007). Again, there is some

**Figure 5:** *Average costs per employee in private hospitals as a percentage of costs in public hospitals, Germany*



Source: Statistisches Bundesamt (2007b), calculations by the WSI.

**Figure 6:** *Number of patients per full-time hospital employee, Germany, 2006*



Note: \* Physiotherapists, psychologists, speech therapists, pharmacists, social workers, and so on.

Source: Statistisches Bundesamt (2007b), calculations by the WSI.

evidence that this tendency is even more pronounced in private hospitals and clinics. On average, the latter have far fewer staff per patient than their public competitors: in 2006 a doctor working for a private hospital had on average 1,314 patients in his care, while his colleague at a public hospital had only 1,017 patients (Figure 6); a nurse in a private hospital was responsible for 515 patients in comparison to 450 patients in a public hospital. Regarding medical-technical services, which include physiotherapists, psychologists, pharmacists, social workers, and so on, an employee in a public hospital has to care for 961 patients in comparison to 1,394 patients in private hospitals. Interestingly, the ratio of staff and patients in non-profit hospitals is often worse than in private hospitals and clinics.

As far as the effects of hospital privatisation on the quality of health care services are concerned no detailed studies are yet available. But some studies have analysed the consequences of the growing economisation and commercialisation of hospital services, which have mainly been pushed through the new system of hospital financing (Kühn 2003; Kühn and Klinke 2006). There is a broad concern that the increasing economic pressure will influence hospital services in such a way that the treatment of patients will increasingly be governed not only by medical but also by economic criteria (Simon 2001) and that private hospitals and clinics are leading the way in this

respect (Bundesärztekammer 2007). According to a recent study, more complicated and expensive cases are still very much concentrated in larger hospitals, usually public. Instead, private hospitals and clinics tend to follow a cherry-picking strategy, concentrating treatment on more profitable cases (Braun and Müller 2006).

Since the new hospital financing system promotes a shorter length of stay, there is a strong financial incentive for hospitals to check out patients as early as possible, with the danger of ‘bloody check outs’ (Kühn 2003: 7). According to a recent survey study the average proportion of patients who had the impression that they had been discharged from hospital ‘too early’ was by far the highest in private hospitals (Braun, Müller 2006: 35f.). Moreover, the study came to the conclusion that in comparison to previous patients’ surveys service quality in private hospitals was much worse (ibid.: 40).

### **3.4 Challenges to further hospital privatisations**

There has been a growing scepticism among citizens, employees and patients against the privatisation of hospitals in Germany; in recent years almost all major privatisations have faced strong resistance from various stakeholder groups. For example, the sale of the *Landesbetrieb Krankenhäuser* (LBK) in Hamburg, so far the largest hospital privatisation case in Germany, was confronted by a broad anti-privatisation alliance, including regional trade union organisations, political parties and ‘alterglobalist’ groups, such as Attac (Boehlke 2007). With the slogan ‘Health is not a commodity’ the alliance launched a broad political campaign against privatisation and collected more than 100,000 signatures, forcing the Hamburg government to hold a referendum; 65% of those entitled to vote participated in the referendum, nearly 77% of whom voted against privatisation. Although a broad majority of the people of Hamburg have shown their disapproval of privatisation in the end the Hamburg government sold the *LBK* to the private hospital corporation *Asklepios*.

In the meantime, local referendums have become a widely used political instrument against hospital privatisation. The relevant local organisation of ver.di, by far the largest union in the German health care sector, usually has a leading role in organising political alliances in favour of such referendums. Referendum results have usually shown a broad majority against privatisation, but only in a few cases have they actually prevented a hospital privatisation (Schulten 2006). So far, many referendums have failed, either for formal judicial reasons or because participation was too low (Mittendorf 2008).

Although most business and consulting experts take the view that the current trend towards more hospital privatisations will continue, the future of the German hospital sector is not set in stone. On the contrary, the recent restructuring of hospitals in Germany is the result of political decisions underlain by a dominant economic belief that the liberalisation and privatisation of public services will result in more efficiency. In relation to the health care sector in particular, however, this has been called into question. As a result, hospital privatisations will continue to be confronted with anti-privatisation alliances composed of various stakeholders, so that the future development of hospitals in Germany will depend on the outcome of these political struggles.

### **Outlook: increasing conflict concerning privatisation**

Since liberalisation and privatisation have put the affected sectors under enormous competitive pressure, this has had a significant impact on labour relations, in particular in labour-intensive industries. In order to save labour costs, privatised companies have tried to withdraw from the 'more expensive' public sector labour relation regimes and to set up new forms of regulation. This has led to a deterioration in collective bargaining, wage levels and employment conditions (Brandt and Schulten 2007: 1). The switch from former monopoly suppliers of public network infrastructures to new global players has led to a massive reduction in employment. Trade unions have been unable to prevent privatisation, but also consumer protests against the worsening of public services have been rather modest. The public debate in the 1990s was clearly dominated by the advocates of privatisation.

In recent years the political climate seems to have changed, however. Opinion polls and surveys have shown that large parts of the German population seem to be sceptical of further privatisations (Güllner 2008). More and more people have the practical experience that the promised results of privatisation, such as better services and more jobs, have proven ill-founded. As a result, there is also growing political resistance to further privatisation. One prominent example is the battle over the initial public offer of German Railways (Deutsche Bahn), which was planned for 2006, but has become uncertain after strong protests from trade unions, environmental and consumer groups, political parties, and so on.

Moreover, local opposition to privatisation is increasing, with political alliances of local trade union organisations and other civil society groups resorting – sometimes successfully – to local referendums to avoid planned

privatisations of municipal housing, hospitals or other municipal facilities (Mittendorf 2008). Finally, an increasing number of municipalities have the experience that the privatisations of some public services have led to higher prices and poorer services. Some of these municipalities have already started a 're-communalisation' whereby the provision of certain services has been given back to public companies; according to a recent study, about 10% of all municipalities have plans to withdraw some privatisations (Janetschek 2007: 18).

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## **Marketisation in Swedish electricity and postal services**

### **Introduction**

The so-called ‘Swedish model’ of industrial relations is well known far beyond Swedish borders. Less known is the fact that for almost a century there was also a Swedish model of economic infrastructure. The opening up of the markets for railways, electricity, telecoms, aviation and so on, was part of the same process and occurred within the same ideological framework. Postal services and electricity were deregulated and exposed to competition at the same time, but the outcomes in some respects differ widely: postal services are still recognisable in comparison with their previous form, with an incumbent, Posten AB, that still holds more than 90 per cent of the market (though challenged in some important branches by its only serious competitor, CityMail). The electricity industry, on the other hand, has been diffused among several actors representing a great variety of ownership forms. It is difficult to obtain a complete overview of the industry, at least not on the retail side. Hence, the two industries can be seen as two polar extremes on a continuum of marketised public businesses. To try to discover what impact marketisation has had on the labour market, employment, industrial relations and service quality we start with some background information to shed light on how these infrastructural systems came into existence. The postal system, though an important part of Swedish infrastructure, has a somewhat different origin from electricity and other state-owned industries.<sup>1</sup>

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<sup>1</sup> It should further be noted that both electricity and postal services were industries in which all public ownership was controlled by the Swedish state. In several other industries that were privatised over the 1990s, such as local transport, nursing and health care, the former owners were local or regional municipalities.

## 1. Historical and theoretical background

The notion of a special Swedish infrastructure system on the analogy of the famous Swedish model of industrial relations was first developed by Arne Kaijser (1994). Its unique feature was, according to Kaijser, the shared responsibility between government bodies and municipal and private parties. Government bodies were responsible for the national level, while local bodies took charge of the regional level. Contacts were often informal and there were no public supervisory bodies. The development of this infrastructural model began in the late nineteenth century, half a century before the better-known Swedish model of industrial relations.

An illuminating example of how the model worked in practice is the hydro-electric power system, the world's first state-owned energy producer (Högselius and Kaijser 2007: 35). Factors contributing to the development of this system include the fact that waterfalls in Sweden were public property. In addition, existing state-run systems, such as the railways and the telegraph system, worked well and so furnished a model. Furthermore, the still expanding railway system, as well as expanding privately-owned industries, desperately needed a continuous supply of the 'new' power, electricity (Kaijser 1994: 166–80; Jakobsson 1996: 74–76). Other infrastructural sectors developed in a similar way. Most infrastructural systems were formed as a result of cooperation between the Swedish state and other interested parties. The most important exception is the postal system that was funded, organised and administered as a strictly government body from the mid-seventeenth century until its liberalisation in the 1990s.

The cooperation between the Swedish state and private companies also manifested itself in generous government support of 'national champions'. Much of the technical competence needed to create the infrastructural system existed in relatively small firms based on single technical inventions or innovations. Therefore the Swedish state filled the order-books of a number of leading innovative companies to give them an opportunity to develop products at their own pace, sheltered from market competition. The most important example of this symbiotic relationship is the cooperation between the state and ASEA, the predecessor of ABB. The founding of ASEA in 1890, too, was promoted by the Swedish state as a means of harnessing hydro-power (Fridlund 1994).<sup>2</sup> Infrastructural systems have always consisted of

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<sup>2</sup> 'National champions' were not restricted to Sweden, of course; similar phenomena occurred everywhere when the need for national technological infrastructure emerged (cf. Rosenberg 1982).

both material and immaterial elements that are not separable (Jäger 2004): according to Thomas P. Hughes (1983, 1987), such systems are primary social, not technical; the systems are socially created and also driving forces in societal change (Hughes 1987: 51–54). A prominent feature of such systems is what Hughes calls ‘reverse salients’. The term is of military origin, referring to a section of an advancing battle line that comes to lag behind; Hughes uses it as a metaphor for part of an expanding system – whether technical, economic or political – that does not keep pace with the other parts and so hinders progress. One example is the transmission of electricity, which was not profitable until the invention of the three-phase transmission system (Hughes 1983: 79–80).

Hughes’s theory has been applied by Eva Jakobsson (1996) in a study of the development of hydro-power in western Sweden in the early 1900s; this has a theoretical bearing on how the same electricity system was dismantled almost a century later. In the early 1900s, neither lack of technical knowledge nor financial resources was a problem for the extensive expansion of hydro-power. But there was a ‘reverse salient’, namely an old riparian principle that prohibited any alteration in a water-flow that endangered agriculture; hence local farmers tended to oppose any hydro-power development. To overcome this, in 1918 the Swedish government, strongly encouraged by privately-owned power companies, passed new legislation and established a special ‘water court’. The riparian principle could be circumvented if the interference with the water-flow brought a substantial benefit to business or the community.

To summarise concerning the Swedish electricity sector in the early 1900s, we find:

- a need for electricity for important industries and households;
- an ideological consensus between enterprises and the government;
- actors willing to invest in a technological system ready to expand;
- *but also* a reverse salient in the form of riparian rights that would be seriously violated if the technological system expanded.

The reverse salient was easily removed because of the consensus between the state and industrial capitalists. At the time, the average possessor of riparian rights did not even have the right to vote due to the income/property threshold. The result was a highly profitable technological system; but the trade-off between state and private capital also led to the development of technical innovations and patents that were successful in the market. Removing reverse salients could also have an impact on employment relations; in the case of hydro-power development in western Sweden, the removal of riparian rights

led to a rapid decline in the number of smallholders, but an increase in the number of industrial workers with comparatively secure jobs (Jakobsson 1996).

The main question for this chapter, however, concerns whether this theoretical concept has any bearing on developments over the last two decades. From this point of departure, Section 2 briefly outlines marketisation in Sweden as a whole, while Sections 3 and 4 deal with the development of postal services and electricity.

## 2. The opening up of sheltered markets

The idea of opening up markets sheltered from competition was first raised in the 1980s, under a social democratic government. But the idea was not really put into practice until a new, centre-right government came to office in 1991. The ideological foundation was the so-called ‘bourgeois’ (*borgerliga*)<sup>3</sup> parties’ joint electoral programme. The programme was strongly influenced by neoliberal ideas and the whole campaign was conducted under the banner of a new, liberal society based on individual choice, private enterprise and low taxes. All remnants of the classic Swedish welfare state were declared outdated and so obstacles to renewal and vitalisation. When the ‘bourgeois’ coalition won the election, therefore, the path had already been laid for privatisation.

The growing cost of public services had been noted since the oil crises of the 1970s, but the problem was discussed more actively in the 1980s when the Swedish economy was obviously suffering from falling productivity. In 1989, the social democratic government launched a so-called ‘public investigation’ of low productivity, which was finished two years later. The investigation, led by the right-wing economist Assar Lindbeck, analysed both the private sector and public services (SOU 1991: no 82). Theoretically, it was deeply rooted in neo-classical microeconomics and denied any fundamental difference between manufacturing and services: measures for increasing productivity in privately-owned industry were applicable to public sector services too (Thörnqvist 2007: 19–21). To get productivity back on track, it recommended cost cutting and the exposure of sheltered businesses to competition (SOU 1991 no. 82: 335–42). As already mentioned, the

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<sup>3</sup> Generally speaking, the centre-right parties, which all refer to themselves as ‘bourgeois’ (*borgerliga*), form an electoral coalition; the parties in question are the Conservatives (*Moderaterna*), the Liberals (*Folkpartiet*), the Centre Party (*Centern*) and the Christian Democrats (*Kristdemokraterna*). While the term ‘bourgeois’ is politically charged in some countries, in Sweden the term ‘*borgerlig*’ is entirely neutral and merely descriptive.

investigation was launched by a social democratic government, but reform took off only under the ‘bourgeois’ government of the early 1990s. When the Social Democratic Party returned to office after three years, it did nothing to reverse the process (Lindvall 2004).

Although there was a consensus between the social democrats and the ‘bourgeois’ parties about the need to open up sheltered markets, there was little popular support for such measures. According to the annual opinion polls undertaken by the Department of Political Science at the University of Gothenburg, opinions for and against the privatisation of public companies had been about equal, or slightly negative, since 1993. A huge public debate on the issue had taken off in the mid-1980s as plans emerged for selling off the public telephone company, Telia, so most people had already made up their minds about privatisation by the 1990s. Furthermore, the polls show clearly that attitudes to privatisation were never a matter of satisfaction or dissatisfaction with the existing public service, but rather ideological in nature (Nilsson 2001).

Despite the ideological character of the issue, another ‘public investigation’ in 2005, (*Regelutredningen*), on the effects of marketisation, argued that the process was very much characterised by many small changes that step by step were transforming infrastructural markets. For example, no government bills or parliamentary decisions pinpoint the start of liberalisation (SOU 2005 no. 4: 150–52). Moreover, the reforms took off during the biggest economic crisis in Swedish post-war history, which *Regelutredningen* emphasised as a major driving force behind the reforms, of more significance than ideology. The reasons for reform were more pragmatic than ideological (SOU 2005 no. 4: 152–54).

Be that as it may, even the ‘pragmatism’ noted by *Regelutredningen* had ideological roots. The detected problems together formed a ‘reverse salient’ that prevented Swedish infrastructure from functioning properly, but how the problem might be solved was still an ideological question. ‘Public investigations’ are seldom as ‘neutral’ as they might seem. *Regelutredningen*’s mission was to investigate the effects of the liberalisation process on consumer prices, but the implication was that the result should be positive. *Regelutredningen* did not find such a positive result, however, only excuses for the lack of them. The investigation covered six, very important industries (see Table 1).



**Table 1:** *Developments in six major industries after liberalisation, Sweden*

	Postal services	Taxis	Railways	Domestic aviation	Electricity	Telecoms
Prices compared with the general price trend	Increased	Increased	Increased	Increased	Increased	Decreased
Production volume	Decreased	–	Increased	Decreased	Unchanged	Increased
Profitability	Unchanged	Increased	Unchanged	Decreased	–	Unchanged
Employment	Decreased	Increased	Decreased	Decreased	Decreased	Decreased
Revenues in relation to trade and industry in general	Decreased	Decreased	Decreased	Decreased	Increased	Increased
Productivity	Increased	–	Increased	Increased	–	Increased
Market concentration	Decreased	Decreased	Decreased	Decreased	Decreased	Decreased
Accessibility	–	Increased	Increased	–	–	Increased

Source: *Regelutredningen*, SOU 2005 no. 4: 48.

*Regelutredningen* presented a number of arguments to explain why liberalisation had not produced the expected results. It is notable that they all depended on the idea that marketisation had not been carried out properly, not that there might be fundamental flaws in the concept. Several critical economists have questioned the theoretical coherence of the neo-classical theory that ‘perfect market competition’ is better for consumers than a monopoly (cf. Keen 2004: 97–107). In practice, this applies particularly to infrastructural markets: ‘demand’ is a vague concept in such markets and prices are set by the relation between marginal costs and marginal revenues, which is a much more complex issue (Keen 2004: 103). All important actors at the time agreed that something had to be done to improve infrastructural systems, but it was not discussed whether the commonly suggested solution, that is, marketisation, might lead to other, perhaps equally serious problems or ‘reverse salients’. The ideological influence of the ‘productivity investigation’ of 1991 is obvious. *Regelutredningen*’s negative conclusions have also been called into question, as we shall see, but there has never been a thorough discussion of other parameters than efficiency and consumer prices. Such parameters shall be addressed in the section on the effects on employment and employees, but we shall first present developments in postal services and electricity in more detail.

### **3. Changes in the postal system**

The postal system is one of the oldest government bodies in Sweden. Its origins date back to the Thirty Years’ War and the need for reliable military intelligence; the first statute on the Swedish Post Office bears the date 20 February 1636. Hence, it was a history of public administration lasting over 350 years that was brought to an end in March 1994, when the Post Office was unbundled and transformed into the company Posten AB.

The ‘postal market’ in Sweden comprises the distribution of items of mail. The producer is the company that distributes letters and the customers pay for the service. This definition excludes distribution of newspapers, advertising brochures and hand deliveries, but such demarcation is not written in stone. Only the distribution of items of mail weighing less than two kilos was liberalised in 1994. Heavier items, as well as newspapers, and so on, have always been open for distribution by private entrepreneurs. An important dividing line between post covered by the monopoly and post open to private entrepreneurs concerned whether the sent item was ‘written’ or ‘printed’; that is, items copied in one way or another and delivered en masse were open for private distribution, while items directed to a single recipient were solely a matter for the Post Office (Löfström 2003; SOU 2005 no. 4: 397–98).

The unbundling was carried out by the centre-right government in office in 1991–94, but the previous social democratic government had paved the way. A government bill (1990/91 no. 87) was the first move towards liberalisation, but there was still a strong belief among leading social democrats that the break up of the ‘natural’ postal monopoly would lead only to rising costs, for society as a whole as well as for individual consumers. After the change in government in autumn 1991, the centre-right coalition soon presented a new government bill (1992/93 no. 132), arguing that both the judicial and the cost-related problems attendant on replacing the monopoly were mere technicalities and that opening up the service to competition should soon benefit the customers. The bill was passed in January 1993, but did not come into force until March 1994, which meant that the first steps towards liberalisation were taken in a legal limbo. The guidelines for regulation of the postal market(s) were provided by EC legislation. The Directive (67/97/EC) that came into force in 1998 was immediately transposed into Swedish law.

According to *Regelutredningen*, it is hard to differentiate the effects of liberalisation from those of technological development because the competition arising from other forms of communication, in particular electronic distribution, was increasing so much at the same time. Nevertheless, *Regelutredningen* argues that competition has had a positive effect overall on the letter market in Sweden. The empirical evidence for this conclusion is somewhat thin, however. Posten AB has only one significant competitor on the letter market, namely CityMail. In 2003, ten years after liberalisation, Posten AB still had 92.9 per cent of the market; CityMail had 6.6 per cent and other competitors accounted for the remaining 0.5 per cent. In the words of *Regelutredningen*, Posten AB’s extreme dominance is the result of four main factors:

1. the company is efficient and therefore has managed well even after being exposed to competition;
2. the letter market has all the hallmarks of a ‘natural’ monopoly;
3. there are high ‘entry barriers’ to the market;
4. Posten AB has used its dominant position to exclude competitors using ‘competitively disgusting [in Swedish: *motbjudande*] means’ (SOU 2005 no. 4: 418–22).

Be that as it may, *thinking* within Posten AB has changed dramatically during the period of liberalisation. Carina Löfström (2003) has shown that a great deal has been going on beneath the surface, activities that have both resulted from and given rise to new ways of thinking. A major difficulty was to

integrate new ideas with old habits; ideas did not ‘travel’ well within the organisation. For the average customer, therefore, it appears that not much has happened; the only change that has directly affected people’s everyday lives is post office closures – today there are only small ‘postal stores’ for economic transactions, while the sale of stamps, and the sending and receiving of items too big for a letterbox are now handled by supermarkets and convenience stores. In the eyes of ordinary postal employees, however, the changes have been dramatic, as we shall see.

When Posten AB was formed in 1994, the new company had to take over most of the Swedish Post Office’s obligations; unlike its ‘free’ competitors, Posten AB *has* to provide daily services to the whole Swedish population. This means that Posten AB must be prepared to distribute 20 million items of mail per day to and from 4.5 million households and 900,000 companies, five days a week. Posten AB’s, but also the Swedish government’s obligations are regulated in five different laws and decrees. All guiding EC directives have been transposed in these laws/decrees and the preparatory work originates from both social democratic and centre-right governments (Andersson and Thörnqvist 2007).

Stakeholders outside the political establishment were barely relevant in the liberalisation process. The Swedish Employers’ Confederation was – as always – in favour of opening up sheltered markets, but there was no strong lobbying for the transformation. It was not necessary, thanks to the political consensus. Moreover, very few protests were heard from trade unions or other social movements.

Few important private companies were eager to take over parts of the letter market in Sweden. In fact, the only important competitor, CityMail, is owned by the Norwegian Post. Thanks to its monopoly in Norway, the Norwegian Post can use its surplus to expand in the competitive Swedish mail market. It is true that CityMail has only a 5–7 per cent market share, but it was never the company’s intention to compete in all areas, only in the most profitable branches of the postal service. As a result, CityMail has focused on such lucrative areas as mass distribution from firms with many customers, involving large quantities of items of mail that are easy to handle. Since Posten AB has particular obligations, competition in the exposed segments is highly favourable to CityMail (Hamark and Thörnqvist 2007).

The CEO of Produktion Meddelande, a branch of Posten AB affiliate Posten Meddelande AB (Posten Messages AB), reported that Posten AB had lost 10 per cent of its former volume in the areas in which CityMail is expanding, ‘so

of course we must improve our efficiency and productivity'.<sup>4</sup> The new challenge has not been met by any particular campaigns, however, but by 'normal management measures', planned and launched centrally, but aiming to reorganise local branches in line with the new approach. The competitive means, he said, are close customer contacts and quality, not price.

#### 4. Changes in the electricity industry

According to Högselius and Kaijser (2007: 80–81) it is possible to pinpoint the exact date when reform of the electricity market became a political aim, namely 26 October 1990. The social democratic government launched a reform drive to cope with the currency crisis and to make the administration of public assets more efficient; one measure was the transformation of Vattenfall into a government-owned stock company. More prominent aspects of the reform drive meant that the changes in the electricity sector were little noticed at first; they emerged in the political debate little by little and in a roundabout way.

Until that October day in 1990, the electricity sector had been the clearest example of the Swedish infrastructural model described above. The government's role was largely indirect. Control was carried out through the dominant role of the government body Vattenfallsverket, while the electricity market was regulated by 'self-governance' in a similar way to the labour market, in the form of so-called 'clubs' (*klubbar*), voluntary associations of enterprises engaged in the production and/or distribution of electricity. The premise was that cooperation would promote 'collective utilities' and Vattenfallsverket held the chair in each club. Small entrepreneurs had a say in development, however, and could also benefit from the sheltered market; they therefore willingly accepted the clubs' self-imposed responsibilities for regulation and development. Price setting was legally regulated, however (Hjalmarsson and Viederpass 1992; Damsgaard and Green 2005: 36–38; SOU 2005 no. 4: 157–59).

After some preparations, mergers and other organisational changes, the new, unbundled company Vattenfall was founded on 1 January 1992. Several later investigations, under both 'bourgeois' and social democratic governments, prepared the ground for further marketisation, and on 1 January 1996 a new law was passed that opened up both generation and supply to free competition. Transmission of electricity was, due to its large-scale character, exempt from marketisation. The existing three levels of transmission, that is,

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<sup>4</sup> Interview in September 2007.

national, regional and local, together formed a ‘natural’ monopoly, with little to gain from privatisation or market competition. Accordingly, the electricity market now consisted of three segments: generation/production, transmission and retail directed towards individual customers, including households (Damsgaard and Green 2005: 39–40; Högselius and Kaijser 2007: 138–39; Andersson and Thörnqvist 2007).<sup>5</sup> After deregulation, the electricity sector became subject to stricter legal regulation. The government regulatory authority, Energimyndigheten, receives its instructions in the form of annual ‘regulatory letters’ or *Regleringsbrev*. These are very detailed and regulate not just issues of competition and security, but also research and the introduction/diffusion of alternative power sources, especially wind power stations. All EU laws and decrees have been transposed into Swedish legislation and are thus covered in the regulatory letters (Andersson and Thörnqvist 2007).

Berg (1999) argues that there were three main driving forces behind the liberalisation of the Swedish electricity market: the wish to adapt to the free-market policies of EFTA and the EU; the opening up of other Nordic countries’ markets – in particular the Norwegian liberalisation in 1991 and the creation of the common Nordic electricity market, Nord Pool; and a ‘strong political desire’ to liberalise and privatise public-owned assets. The last factor was, as we have suggested, probably the most important. Högselius and Kaijser (2007: 100) claim that a few civil servants in important government departments were even more influential in the process than politicians themselves. Högselius and Kaijser (2007: 72) further point out that an important ‘reverse salient’ was removed in the mid-1980s: because the electricity industry was so complex, far-reaching liberalisation had not been possible due to the problem of handling the huge amount of data involved, but thanks to the rapid development of ICT during the 1980s this became possible at a reasonable cost.

Table 2 briefly summarises and compares the situations before 1996 and in 2004, with respect to the ‘monopoly’ and the main new market actors.

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<sup>5</sup> The parliamentary decision was taken by the centre-right government; accordingly, it was merely the implementation of the decision of 1996. But the social democrats did nothing to reverse the decision when they returned to office in 1994 (Högselius and Kaijser 2007: 125–39).

**Table 2:** *The Swedish electricity market before 1 January 1996 and in 2004*

	Before 1 January 1996	2004
Generation	Vattenfallsverket (a government authority) + privately- or municipality-owned so-called 'clubs' under government influence	Vattenfall AB, state-owned: 70.0 TWh (49.3%); Sydkraft (E.On), privately-owned: 33.9 TWh (23.8%); Fortum, privately-owned: 24.0 TWh (16.9 %); Skellefteå Kraft, municipality-owned: 3.1 TWh (2.2%); Others: 11.1 TWh (7.8%)
Transmission	Stammätklubben (a government-run club with private members)	Svenska Kraftnät (a government company with privately- and municipality-owned affiliates, of which the most important are Vattenfall, Fortum and Sydkraft)
Supply/sales	Vattenfallsverket + the clubs	Vattenfall AB, state-owned (22.7%); E.On (Sydkraft), private-owned (17.3%); Fortum, private-owned (17.3%); Others (42.7%)

*Source:* Energimyndigheten, homepage: [www.stem.se](http://www.stem.se) (generation); Energimarknadsinspektionen, homepage: [www.energimarknadsinspektionen.se](http://www.energimarknadsinspektionen.se) (supply/sales).

As we can see, the incumbent Vattenfall is still the strongest actor, but not as dominant as Posten AB in postal services. The opening up of the market has attracted new actors, but the former quasi-monopoly has been replaced by an oligopoly with three dominant players rather than by a neo-classical ideal market. It should be noted, however, that the *number* of small companies in the industry, all of them in supply, grew considerably after deregulation, from 238 in 1987 – that is, during the ‘club era’ – to 338 companies in 2002, an increase of 42 per cent (SOU 2005 no. 4: 50, 168–70). Although together they still control more than 40 per cent of the supply market, there has been a concentration of capital due to the dominance of the three strongest actors (Damsgaard and Green 2005: 40–47).

Electricity consumption stagnated from 1987, a fact that sets Sweden apart from most other industrialised countries. On the one hand, this made the electricity market less interesting for small-business entrepreneurs, since it is harder to get established on a market that is not expanding (Högselius and Kaijser 2007: 48–51, 57); on the other hand, even small competitors now saw a chance to compete in markets outside their own municipalities, that is, markets that, although not expanding, were now opened up to new actors (Högselius and Kaijser 2007: 142).

The biggest company is the incumbent, Vattenfall, which is now a publicly-owned joint-stock enterprise. The Swedish state still owns all the shares, but the company shall be run and regulated in the same manner as a privately-owned enterprise, not as a government entity. Since 2001 E.On/Sydkraft has been a subsidiary of the German E.On group, that is, registered on the stock exchange in Frankfurt and New York and with its headquarters in Düsseldorf. It is therefore difficult to discern the precise ownership of E.On Sweden. The Swedish government does not own any stocks in the company, nor do any important Swedish investment groups. The third major owner, Fortum, is today the biggest electricity company overall in the Nordic countries; its headquarters are in Espoo, Finland, and it is listed on the Helsinki Stock Exchange. But it is not possible to ascertain the exact ownership figures for its interests in Sweden. The Swedish subsidiaries, however, include one state-owned company (Svensk Naturgas) and one joint corporation with the City of Stockholm (AB Fortum Värme). None of these companies can be said to have a significant influence on Fortum’s activities in Sweden, however.

It is worth noting that the transmission network owners who transform and transport electricity from the producers to the consumers are all affiliated to the government company Svenska Kraftnät (Swedish Power Mains) and must be licensed by the government body Energimyndigheten (the Energy



Authority). As a consequence, this segment of the market is still highly monopolised. The monopolies are regional, however, covering different parts of Sweden. Paradoxically, this means that Vattenfall, Fortum and Sydkraft – that is, the same competitors as in the production and supply of electricity – each have their own regional monopoly and so do not compete with one another. Besides these three actors, there are a few municipalities and industries that own considerable parts of the regional transmission network (Svenska Kraftnät, homepage, [www.svk.se](http://www.svk.se), Jan. 2008).

As we have seen, *Regelutredningen* found that consumer prices had increased after deregulation compared to the general price trend. In a more subtle analysis Damsgaard and Green (2005: 63–69) argue that consumer prices did not change much in any direction before 2002. At the end of that year, prices rose rapidly due to the extraordinarily low rainfall and reinforced by high Nord Pool prices. Damsgaard and Green further claim that, even if marketisation has not led to visible benefits for electricity customers or society at large, the situation would have been far worse without deregulation. This conclusion draws solely on a counterfactual analysis of what *might* have happened if market regulation had remained as it was before 1996, however. Furthermore, the research was carried out under the influence of a ‘reference group’ consisting of representatives from more or less all the companies and government bodies (2005: 10) that might benefit in one way or another from a ‘positive’ result that showed that marketisation was and is the only way forward. No critical voices were involved in the reference group and all tested models drew on mainstream neo-classicism, which left no room for other solutions than neo-liberally influenced market economics.

## **5. Marketisation on the shopfloor: the effects on the workers**

So far this chapter has largely dealt with changes in ownership and competition. But one important question remains: how have the changes affected industrial relations and work organisation? This section draws on information, both oral and written, from trade unionists working at the two incumbents, Posten AB and Vattenfall, in particular from six interviewees, three from each company. This offers an employee and trade union perspective on the changes, although there is also some complementary information from interviews with Posten AB management. The trade union interviewees at Posten AB are all active in the main union for government bluecollar workers, SEKO, either as full-time employed ombudsmen, that is, trade unionists employed to support members in legal matters, individual wage negotiations etc., or as local trade union activists in the Gothenburg

area. Regarding Vattenfall, two of the interviewees are from SEKO, both full-time ombudsmen. Formal interviews were supplemented with information provided by telephone and e-mail, and references to SEKO's official 'energy policy programme', published in 2003 and dealing in particular with the effects of deregulation. Since a large part of Vattenfall's employees are white-collar workers, the third interview partner is from the largest union for salaried employees, Unionen. As we shall see, views differ considerably on several points between the blue- and white-collar unions.<sup>6</sup> All six interviewees are men and worked for their company before liberalisation, so providing them with a long-term perspective on the changes.

### **Posten AB**

To start with Posten AB, marketisation has had a considerable impact on working conditions and labour relations, despite the fact that the incumbent has seemingly maintained so much of its monopoly position. One interviewee strongly emphasised that market deregulation commenced before the democratic political decision was made. The politicians did not understand what impact liberalisation would have, he argued; it was a strictly ideological decision to expose postal deliveries to free-market competition without any consideration of the consequences. Furthermore, although the competition from CityMail was only in one segment, it affected postal distribution in general. CityMail, as one interviewee put it, had no interest in the 'yellow letterboxes' in which ordinary customers post their postcards or letters. The yellow mailboxes are necessary to maintain the same standard of postal services as before liberalisation, but they are not particularly profitable. Another added that because of Posten AB's 'national' obligations, the problem of unfair competition is most notable in less populated areas in northern Sweden, where Posten AB must handle and distribute mail that does not cover its own costs, the kind of service that CityMail has no obligation to provide in any part of the country. CityMail further took over the so-called 'postcode lottery' (*postkodlotteriet*) 'by more or less unfair means'. *Postkodlotteriet* is a nationwide lottery based on people's postcodes and very popular – and so very lucrative.

Another result of the growing competition is that the number of employees has been falling continuously since the mid-1990s. According to figures from SEKO, there had been a reduction before unbundling, when about 14 per cent of the workforce was made redundant. Taking into consideration all

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<sup>6</sup> It is a Swedish or, more correctly, Scandinavian characteristic to have separate, nationwide trade union confederations for blue- and white-collar workers (Thörnqvist 2006).

employees engaged in postal work – that is, persons in mail and parcel services, but not drivers and management – the Posten AB workforce was reduced from 35,250 workers in 1990 to 30,500 by the beginning of 1994, a fall of about 14 per cent in the years before formal liberalisation. By 1995 the figure was 31,200 and did not change very much until the beginning of 2001 (32,700 employees).<sup>7</sup> From early 2001 to the beginning of 2007, however, there was a strong decline of almost 30 per cent, to 25,450 employees. In late 2007, there were, according to the CEO of Produktion Meddelande, about 15,000 full-time postmen in Sweden employed by Posten AB; that is, temps who work only at seasonal peaks are not included.

Work tasks are basically the same as before unbundling. A general reduction in working hours from 40 to 38 hours per week took place at the end of the 1990s. About 80 per cent of postal delivery workers work on full-time contracts and the gender distribution is approximately equal. A normal working day is 7 hours and 35 minutes, starting normally at 6.30 a.m., with some local variation. Work schedules are determined on a monthly basis, however, to meet varying volumes. Mondays and Thursdays in particular are work intensive, since most commercial advertising is distributed on those days. This kind of working time flexibility has become more and more common in recent years as a means of making distribution more efficient. The interviewees argued that the agreement that gave the workers the 38-hour week has been ‘paid for’ by very low wage increases over several years.

The Swedish bargaining system is very solid and has not been particularly affected by the liberalisation process. But largely because of the new employment forms in Posten AB, local trade union work has become trickier. Before unbundling, a local trade union representative could ‘just look at a few old notes and files and work out how to handle things or solve problems’, but after unbundling, the general regulations within the company were replaced by ‘customised’ and ‘profitability-related’ solutions. Consequently, it is now more difficult to recruit new local trade union activists.

The interviewees stated that postal workers’ real wages had fallen since unbundling, at least in comparison with other occupations. This is supported by statistics from SEKO. Moreover, total remuneration has in practice suffered since unbundling because overtime possibilities have been lost or have at least diminished considerably.

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<sup>7</sup> Due to changes in definition by the beginning of 1995, the number of employees in mail and parcel services, but also drivers and management, is not comparable with the previous period.

Initially, CityMail took a rather hostile attitude towards the trade unions, but the company has since become more positive. A more important reason for the lower trade union density in CityMail is the differing employment policies of the two companies. It has always been a common understanding between Posten AB and the trade union that being a postman is a real profession; it is a job that has to be learned and improved upon by practice, and one which people might continue in until they retire on a pension. For CityMail, on the other hand, postal delivery is a job people take for a short while, usually when they are young and waiting for other job opportunities. Annual employment turnover at CityMail is today about 30 per cent, according to SEKO. Young employees at CityMail therefore do not really understand the need for trade union work to secure collective agreements, insurance, and so on.

On the other hand, our trade union interviewees claim, CityMail is sometimes more union friendly than Posten AB, particularly concerning recruitment. The company initially offers a short-term contract and when the contract expires the employee can choose whether to quit or to take up a permanent position, provided he or she has performed reasonably well. Posten AB, on the other hand, has 'an ability to mess things up!' The company offers too many different forms of short-term contracts and few permanent positions. CityMail 'knows' that even people with permanent positions will probably leave within a few years and so are less keen to offer such contracts. The internal employment rules were easier and much more transparent before the unbundling of Posten, one of our trade union interviewees stated. The number of part-time jobs has decreased, not only among postal delivery workers but also office staff; on the other hand, job security for those on full-time contracts has deteriorated. One informant remarked that postal jobs are not advertised in newspapers or employment offices any longer. The aim is now to cut down, not to attract new, eager employees.

### **Vattenfall AB**

According to SEKO, Vattenfall claims weak overall profitability in the electricity industry in order to weaken both collective agreements and individual employment contracts. It is not unusual for management to claim that it is impossible to compete in a free market as a result of collective agreements that are too costly. The SEKO view, on the other hand, is that the main problem is too high overheads, not labour costs. Be that as it may, increasing costs and greater pressure for profitability have led to rationalisation programmes, with heavy employment reductions as a consequence. In particular, personnel with technical jobs in support,

maintenance and investment have been affected. Sales and marketing, on the other hand, has expanded; according to SEKO, this shows the company's preference for sales at the costs of 'traditional' production and maintenance. SEKO figures show that about one third of all electrical fitters have lost their jobs due to deregulation. The ratio between administrative personnel and 'field workers' (*fältpersonal*) has changed from roughly 30/70 to 70/30.

Another result of deregulation is a lack of preparedness for interruptions in electricity supply. Small interruptions have always been common, but the last five years or so have seen storms big enough to take out the whole electricity system, leaving consumers without lighting, cookers, refrigerators, TVs, and so on. Neither our interviewees nor the official documents from SEKO explicitly blame the new forms of organisation, but it is clear that the problem is at least partly the lack of competent personnel due to the 'slimming down' of the organisation.

Despite SEKO's arguments, it is difficult to tell whether unbundling has led to an overall staff reduction or not. As the interviewee from Unionen pointed out, Vattenfall was a public utility with 9,000–10,000 employees in Sweden in the late 1980s, but is today a northern European group with 32,300 employees in total, of whom 8,400 work in Sweden. 'Most likely it's a net increase, but the comparison is very difficult.' He was also less hostile towards the rationalisation programmes. Vattenfall had to do something to meet the new competition. He also underlined that some aspects of rationalisation had their roots as far back as the mid-1980s, when demand for electricity stopped increasing.

Another problem, connected to the organisational change and highlighted by SEKO, is the lack of resources for training. There are no courses or programmes within the ordinary school system and the big electricity enterprises have wound up the courses they ran before deregulation. The only training course today is safety education, which is mandatory under the law for all employees in service and maintenance firms. For a long time the energy companies also made funding available for skills development within the framework of collective agreements, but as the pursuit of cost reductions has gathered pace, and alongside continuous reorganisation and the growing job turnover between companies, such funding has dried up. No one has been able to access it, and some has even been discontinued. Moreover, the average age of employees is high and recruitment is 'almost non-existent', which, together with the lack of skills development, worsens the labour force's preparedness to meet the future. Due to layoffs, enforced early retirement and the lack of recruitment, most linemen are today more than 50

years old. The official retirement age for most occupations is 65 years in Sweden, but because of the heavy physical strain, not many electricity linemen manage to remain in the job for that long.

The SEKO interviewees strongly emphasised that unbundling had led to deskilling. The number of SEKO members on permanent contracts had gradually fallen because the main companies – that is, not just Vattenfall – preferred to buy services from smaller, specialised companies, which was more in line with the ideology of slimming the organisation. The new HRM policy after unbundling – that is, the outsourcing of some maintenance and other services – had led to a division of personnel into an ‘A- and a B-team’. This seems to have been most accentuated in transmission, that is, the segment of the electricity industry controlled by Svenska Kraftnät, and less so in producer and supplier firms. In my view, there is considerable fear of a move towards Atkinson and Meager’s (1986: 4) famous model of the ‘flexible firm’, with a core group of workers, a peripheral group and agency temps, with the two latter groups having both worse working conditions and less pay due to growing competition. The work environment has already worsened considerably due to the lay-offs, which have increased individual workers’ workload and stress. Consequently, a crucial issue, according to SEKO, will be to protect the contents of collective agreements, ensuring that also peripheral workers and temps have decent standards and wages.

None of the problems the SEKO representatives brought up seemed to constitute a threat to the Unionen members. Trade union work was no more complicated than before unbundling and relations with Vattenfall’s management, though not without friction, were in general very good. Moreover, the number of salaried employees, and so the number of Unionen members, had increased since marketisation had begun; working hours and work tasks had not changed in any unforeseen or undesirable way either. In response to a direct question, the informant said that he could not see any negative consequences at all from unbundling. On the contrary, the owner – that is, the state – no longer meddled in details as it did before. But the respondent did show some disappointment with the declining attention paid to the long term: Vattenfall had become more dependant on the need to show successful quarterly results.

## **Conclusions**

The opening up of postal services and the electricity market had different points of departure, so not surprisingly the outcomes differed. Still, it is the similarities rather than the differences that are worth highlighting. In the

letter market, the state monopoly was too strong to be seriously challenged by private interests, but the new company, Posten AB, has adopted organisational thinking from rationalisation processes in private industry. It is also being challenged in some of its most profitable segments by its nearest competitor CityMail.

In electricity, there were several actors besides the state even before liberalisation, organised in ‘clubs’. Although the state was by far the strongest and in every respect the most important one, the other actors had already entered the market and possessed the necessary skills and knowledge to be successful at the time of liberalisation. The electricity industry also immediately attracted interest from foreign companies.

Regarding liberalisation, Högselius and Kaijser (2007: 104) ask whether in Sweden such a major reform has ever been introduced in a sector that was considered largely to be ‘working well’ (cf. SEKO 2003: 16). The quality of postal services also had a very good reputation, so one might ask why there were any changes at all in these two industries in the mid-1990s. In both cases, a political and ideological consensus on the urgent need for productivity increases was the main driving force behind marketisation. Opinions within the Social Democratic Party were divided (cf. Högselius and Kaijser 2007), but neither in Parliament nor the public debate did the Party ever seriously oppose the overall need for reforms; it merely disagreed on particular points about how they should be carried through and at what cost. It was also the Social Democrats, not the centre-right parties, that introduced the idea of opening up the electricity market.

In Section 2 we encountered some ideas introduced by Thomas P. Hughes, which we have referred to throughout. Borrowing Hughes’s term, government ownership was unquestionably a ‘reverse salient’. When the infrastructural and technological systems were developed a hundred years earlier, state subsidies and involvement were absolutely necessary. But in a ‘globalising world’ such involvement was seen solely as a hindrance to necessary change, productivity development and organisational flexibility, and so had to be replaced by competition according to market economic principles. Other, less important ‘reverse salients’ were trade union/worker resistance and perhaps lukewarm public support for the reforms. This was mostly regarded as a communicational problem, however – a matter of information (cf. Löfström 2003). The legal system might also be regarded as a reverse salient in the postal services in the early and mid-1990s, but only for a short while.

It should be emphasised that the infrastructural changes in the 1990s differed in one important aspect from the changes a century earlier. When ‘reverse

salients' were encountered in the early 1900s, nobody expected a problem solution to be universally applicable. But the privatisation drive in the 1990s appeared to offer just such a solution: all problems in public sector management could be traced back to the lack of competition, and so on, no matter whether it was heavy industry – such as electricity – mail deliveries or health care. Public ownership was in all cases the reverse salient that was allegedly blocking progress.

But public ownership was defended by many people. Was it really totally obsolete? Economic studies (such as those discussed above) tend to analyse ordinary people only in terms of their role as consumers in the market, never as producers/workers. At least one thing stands out clearly from our study: bluecollar trade unionists are not happy with the changes. All changes have aimed at reducing costs and improving quality for consumers; apparently there was never any concern for the same people as employees in the affected industries. Perhaps liberalisation has reinforced the differences between blue- and whitecollar employees, but the seemingly positive attitude among the latter is based only on a single informant and a few documents from Vattenfall. This distinction does not apply in postal services, since all postmen are by definition bluecollar workers in Sweden. Anyway, there is strong evidence that marketisation in both the industries studied in this chapter has led to lay-offs, deskilling, more stress, less job satisfaction and, at least in postal deliveries, lower wages. Both industries functioned well even before unbundling, and the main goal thus seems to have been to maintain existing quality at lower costs and with less personnel and material resources. The lesson to be learned from this study, in particular from the employees, is that the efficiency-promoting organisational changes and rationalisations were triggered not by new competition, but above all by ideas about how to meet new competition in a free market – even though such a market barely existed. Since unbundling, competition in all segments or branches has affected working conditions in the industry as a whole.



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## **Privatisation in water and health services in the UK**

### **Introduction**

The UK was a pioneer of privatisation under Margaret Thatcher in the 1980s. These initiatives involved the sale of many state-owned industries, and also the outsourcing of many jobs in local and central government and health services. The subsequent Conservative government of John Major, and then the New Labour governments of Blair and Brown from 1997, developed the use of public–private partnerships, largely through the so-called ‘private finance initiative’ (PFI), and increased the proportion of health care services outsourced to private companies. This paper analyses the objectives and consequences of these privatisations in two sectors: water and health care.

These sectors share the common feature of being considered essential public services; the organisations in them are statutorily required to provide universal access to water and sewerage services and universal health care, respectively. They differ in respect of two economic characteristics: first, the water sector is highly capital-intensive, whereas the health service is labour-intensive; second, the water sector derives nearly all its income from charges to users, whereas the health service is largely financed from tax revenues, with user charges only for items such as drugs.

They also differ in the forms of privatisation introduced by successive UK governments. The water sector was privatised by sale, through an initial public offering on the London stock exchange in 1989. Employment and investment policies since then have been decided by the private companies. No significant part of the NHS has been sold, but three policies have increased the role of the private sector in the health service:

1. competitive tendering of the jobs of specified categories of support workers;
2. the promotion of PFI schemes to build new hospitals;
3. a series of measures designed to increase the proportion of clinical services, through greater outsourcing of clinical services.

As a consequence of these different forms of privatisation, the forms of governance are also different. The water sector consists of private companies with regional monopolies regulated by an independent economic regulator, OFWAT, with the powers of a government department without minister; in health care, NHS hospitals remain state-owned, and the operation of private companies is regulated by means of contracts negotiated between the companies and the government and health authorities.

The motives and objectives of privatisation were similar in both sectors. Fiscal policy was a strong motive for water privatisation, which removed the borrowing required for investment in water from the balance sheet of the public sector, and for PFI, which has the same effect in relation to the programme of hospital building. An ideological commitment to increasing the role of the private sector featured in both cases, with a less explicit motive of weakening public sector unions and reducing the pay and conditions of public service workers: 'to reduce the power of the trade unions [was] ... a more or less hidden objective' (Florio 2004: 32). The stated economic objectives were also the same in both sectors: to provide higher levels of investment than would otherwise have been the case, and to increase efficiency, which was expected to more than offset the higher costs of capital for the private sector. Thus in the water sector: 'The proposals for privatisation of the water industry were in response to the need for more investment in the industry than the government was prepared to fund from public finance. There was also a prevailing policy which favoured privatisation as a means of securing efficiency' (OFWAT/DEFRA 2006: 30); and the PFI programme has an 'important role in the delivery of the Government's investment plans for public services ... sustained increases in investment and matching reforms are needed to deliver efficient and responsive services' (HM Treasury 2003).

The following sections examine the evidence concerning what happened in the water (section 2) and the health sectors (section 3) in terms of the stated economic objectives (investment and efficiency), and also the distributional effects on users/consumers, workers and private capital.

**Table 1:** *Features of the water and health sectors in the UK*

	Water	Health
Factors of production	Capital-intensive	Labour-intensive
Financing	Trading (charges)	Non-trading (free)
Mode of privatisation	Privatisation by sale/IPO	Outsourcing/PPPs/ internal market
Governance	Independent regulator	Public ownership
Fiscal motivation	Yes	Yes (PFI)
Ideological motivation	Yes	Yes (outsourcing, PFI)
Investment objective	Yes	Yes (PFI)
Efficiency objective	Yes	Yes (outsourcing, PFI)

## 1. Water

Until 1974, water services in England and Wales were run by local authorities, as they still are in nearly all other countries. In 1974 the regional water authorities (RWAs) were created, each covering a river basin area, under the effective control of central government. In 1989 the Thatcher government privatised these regional companies by selling shares on the stock exchange. In Scotland and Northern Ireland water remains controlled and operated by the public authorities.

### 1.1 Investment

One of the key reasons for privatisation was to improve the level of investment. It was expected that this would be financed by private investors, who would be induced to invest their money by the opportunity for good returns provided by the regulatory mechanisms. This would be more efficient for the national economy, it was claimed, than using public finance for investment.

The level of capital investment in the water industry has in fact been much higher since 1989 than it was in the previous decade. This is now claimed as an indicator of the success of privatisation: a factsheet published by OFWAT gives the figures for investment before and after 1989 and claims: ‘Under

OFWAT, investment in water and sewerage services is at its highest ever level.' According to OFWAT, a total of £55 billion has been invested in the 15 years since privatisation, an average of £3.7 billion per year, compared with an average figure of £2 billion per year during the 1980s; this is a difference of £1.7 billion per year, or 46% of all expenditure (all figures are at 2004–2005 prices; OFWAT 2005, 2006).

This picture exaggerates the difference between investment levels before and after 1989, however. The RWAs did not sustain the same level of investment throughout the 1980s, but they did show a clearly rising trend towards the end of the decade, recovering from the long decline in investment imposed by successive governments between 1975 and 1985. Between 1985 and 1989 investment rose steadily, from about £1.6 billion to over £2.2 billion per year, so that their investment had been increasing at a rate of 8% per year in the second half of the 1980s. The OFWAT comparison assumes that there would have been no further increase by the RWAs, but this is very implausible: because of the legal requirements for investment (see section 2.2) the RWAs would certainly have had to continue increasing their level of investment. Even if this increase had averaged just 4% per annum – *half* the rate they were delivering in the second half of the 1980s – they would have generated a total investment of over £50 billion over the next 15 years: about the same as the private companies have achieved.

**Table 2:** *Investment levels and growth rates before and after privatisation (£billion, 2003–2004 prices)*

	1985 (£billion)	1989 (£billion)	2004 (£billion)	Growth (period)	Average annual % growth rate
RWAs (pre-privatisation)	1.6	2.2	–	1985–89	8%
Privatised companies and OFWAT	–	2.2	3.6	1989–2004	3%

*Source:* OFWAT 2006, author's own calculations.

An examination of the factors behind the need for investment and the financing mechanisms used also suggests that the credit for the improvement should not lie with the act of privatisation nor the activities of OFWAT.

The principal driver of this increase in expenditure was the EU directives on higher standards for the quality of drinking water, the cleanliness of beaches and, in particular, the treatment of wastewater. There are various estimates of the scale of this. In 1993 the government claimed that the water companies were investing £3 billion per year to achieve the standards required in the directives<sup>1</sup> – this was clearly an exaggeration, as that would represent over 100% of actual capital expenditure in that year. In 2004 OFWAT estimated that about 50% of all capital expenditure – equivalent to £1.9 billion per year, more than the whole increase in spending – was required in order to meet new quality standards, which largely stemmed from the EU directives. This is consistent with OFWAT's estimate in 1992 that the implementation of EU directives would cost £10 billion (adjusted to current prices).<sup>2</sup> An EC report in 2000 estimated that the EU wastewater directive alone had required investment in the UK averaging £0.6 billion per year since 1990 (EC 2000). It seems reasonable to conclude that at least half of all the increase in capital investment since privatisation is entirely attributable to the requirements of the EU directives. The UK was legally obliged to carry out this investment whether privatisation happened or not.

The privatisation process in itself simply changed the source of resistance to these improvements. Whereas in the 1980s the government had sought to avoid paying for the improvements required by the EU, from privatisation onwards both the companies and OFWAT tried to avoid making such investments. During the passage of the privatisation law, the government tried to insert a clause to exempt the privatised water companies from prosecution by the European Commission (EC) for failure to comply with the directives:

The latter point is of crucial importance to City analysts, with growing doubts about the value of buying into a privatised water industry for which ministers are promising a tough regulatory regime on prices and higher environmental standards requiring heavy investment. Ministers have been seeking to allow privatised water companies to delay implementation of tough EEC directives on drinking water standards.<sup>3</sup>

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<sup>1</sup> UK Parliament Written Answers to Questions, Tuesday 19 October 1993, ENVIRONMENT Col 197. <http://www.publications.parliament.uk/pa/cm/199293/cmhansrd/1993-10-19/Writtens-1.html>

<sup>2</sup> *The Guardian* (London), 14 August 1992, Water bills 'to double by turn of century': Watchdog challenges profit margins and EC standards.

<sup>3</sup> *The Times* (London), 20 February 1989, Ministers in water and power battles: privatisation.



This attempt failed: the EC warned the government that it had no power to waive EU laws in this way.<sup>4</sup> The opposition to the directives' requirements nevertheless continued after privatisation, with OFWAT itself challenging the need for the investment in 1992, 1993 and later.<sup>5</sup>

Following privatisation a higher level of investment was financed. This was partly due to the government injecting a large amount of money by writing off all the water companies' debts before privatisation, plus a further 'green dowry' to meet the environmental standards required by the EU. In addition to this cash injection, the government allowed the private companies to make large real increases in the price of water (see below), which the RWAs had been prevented from doing, and the private companies were not subject to the limits on public sector borrowing.

The final value of the debt write-off was over £5 billion, and the green dowry was worth £1.5 billion – roughly equivalent to the total received for the sale of the companies (the water and sewerage companies even gained an extra £120 million merely by having these gifts in the bank in 1990/1991). These public subsidies alone financed roughly one-third of all investments in the first 10 years of privatisation. There was a further subsidy in the form of tax relief on the companies' profits, worth £7.7 billion. The total amount of public finance injected into the privatised water companies was thus over £14 billion (though much of the tax relief was subsequently clawed back by the 'windfall tax' introduced by the New Labour government in 1997) (OFWAT 1995; Schönback et al. 2004; OFWAT/DEFRA 2006).

All of these things could have been done without privatisation, as a *Financial Times* editorial pointed out in 1989 under the heading 'Private water, public costs':

One of the Thatcher Government's odder justifications for privatising the water services is that the state would never have found enough money to clean up the industry to meet the state's own standards. However, Mr Michael Howard, the minister in charge of the sale, yesterday announced steep price rises stretching to the end of the 1990s and a large injection of government money. This will help pay for improvements in the purity of drinking water and the removal of untreated sewage from rivers as required by the Water Act 1989. These expenditures are necessary, but it is not obvious why privatisation was necessary to achieve them. The Government has now been obliged to put £5.4

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<sup>4</sup> *Financial Times* (London), 5 May 1989, Water row starts to cool ahead of sell-off.

<sup>5</sup> *Financial Times* (London), 5 November 1993, Byatt's water escalator.

billion up front to grease the slipway to flotation, writing off the industry's debts to the Treasury and adding a cash bonus imaginatively decked out as a 'green dowry'.<sup>6</sup>

When the companies were privatised, they were expected to finance investment like other private companies – by shareholders investing in the company ('equity'), supplemented by the company increasing its debts by issuing bonds or bank loans. The water companies had almost no debt when they were privatised in 1989, due to the abovementioned government write-off. The broad expectation was that, as the water companies made profits, investors would continue to inject money, and the price limits had been set in order to create this incentive: 'OFWAT's aim at each price review has been to ensure that returns assumed should provide shareholders with sufficient incentives to provide additional funds, either in the form of retained earnings or new equity, to enable companies to make new investment where this is appropriate.' But in practice, there has been a sharp and steady increase in debts and a reduction in shareholder equity. The water companies' gearing<sup>7</sup> has risen from an average of 0% to an average of 60%, with a number of companies having gearings over 75%. Instead of shareholders putting money into the industry, there has been a significant *withdrawal* of shareholder equity from the water companies – the exact opposite of the effect desired from OFWAT's regulation. A significant part of the borrowing has been from the European Investment Bank (EIB), a public sector bank owned by the European Union that is able to lend at very good rates (OFWAT/OFGEM 2006; OFWAT/DEFRA 2006).

This equity withdrawal has happened in two phases. First, during the decade following privatisation, the companies paid out a lot of dividends to their shareholders, with a return on capital reaching 12%. Interest rates were far lower than this, however, and so the companies preferred to borrow to finance investment, and used the profits from higher prices to pay dividends to their shareholders. The second phase followed the price review of 1999. Following the 1997 general election, the New Labour government introduced first a windfall tax on utility company profits, and then OFWAT set price caps that required 12% cuts in prices. The combined result was to squeeze industry profitability. The rate of return on capital was halved, from 12% to 6%. The response of many companies to this was to withdraw equity capital as far as possible and instead to use debt to finance the great majority of operations.

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<sup>6</sup> *Financial Times* (London), 3 August 1989, Editorial: Private water, public costs.

<sup>7</sup> Net debt as a proportion of regulatory capital value.

Different methods of withdrawing equity were adopted. The most extreme was used in Wales, where corporate multinational owners decided to transfer all the water company's assets, liabilities and statutory functions to a not-for-profit company, run by an appointed and self-perpetuating group of individuals and financed entirely by debt. (This entity is neither elected by citizens nor owned by shareholders or customers, but is often wrongly described as a cooperative or a mutual.) Other companies have simply reduced their equity stakes and replaced them with debts. Many have now been bought by private equity funds.<sup>8</sup>

The effect of this change has been to highlight how expensive it is to finance investment using shareholders' equity. As OFWAT has acknowledged: 'debt financing has, other things being equal, been a significantly cheaper source of finance than equity since privatisation' (OFWAT/DEFRA 2006).

Indeed, OFWAT pointed this out very soon after privatisation in a 1991 paper that estimated that the cost of equity for the water companies was about 5–7%, the cost of company bonds about 3–5% and the cost of government bonds about 2–4%. A detailed study of long-term rates of return over the whole of the twentieth century, commissioned by OFWAT in 2003, concluded with similar figures: the long-term average cost of equity is around 5.5–7.5%, whereas the 'risk-free' rate (typically of government bonds) is about 2.5%. OFWAT also noted that the actual cost of long-term government bonds since the First World War has been less than 1%, which is also the effective cost of long-term index-linked bonds observed at the start of 2006. The figures used for government debt in these papers are broadly in line with other estimates.<sup>9</sup> In simple terms, they mean that if a private company replaces equity with debt, the cost of capital falls by roughly a third. If a company has an equal mixture of debt and equity – 50% gearing – then its average cost of capital is 5%, and moving from here to 100% debt would reduce the cost of capital by a fifth (Wright et al. 2003; Helm 2006; OFWAT 1991).

Moving to 'risk-free' government debt would reduce it still further (and if the actual rate of long-term government bonds is achieved, the cost of using capital is one-sixth of the cost of using equity). As the IMF recently observed:

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<sup>8</sup> See presentation by Keith Tozzi, Chief Executive, Swan Group plc, at IEA Water 2002 Conference, London, June 2002: Corporate restructuring: journey or destination? <http://server1.thewwwcompany.net/swangroup/phpnew/mediastory.php?contentid=10>

<sup>9</sup> Sawyer and O'Donnell (1999, p. 12) estimate the average real cost of government borrowing at 3%.

‘private sector borrowing generally costs more than government borrowing’.<sup>10</sup> Because the water industry is very capital intensive, the potential savings are significant.

OFWAT and other regulators, however, have been concerned that this drift to cheaper debt undermines the basic concept underlying privatisation, which is that private shareholders can drive efficiency improvements. A 2004 report on whether the structure of the industry was still ‘fit for purpose’ concluded reassuringly that it was. In 2006 a paper by economist Dieter Helm was followed by a joint paper from OFWAT and OFGEM (the regulator for gas and electricity) on ‘Financing network services’. Helm discusses four different models of finance (including ‘private equity in partnership with direct pension fund investment’), but – like all the other papers – ignores the possibility of public ownership. But elsewhere in the same paper Helm points out that ‘the alternative – and the overwhelmingly dominant one in recent history – is state ownership and guarantees. Roads, and now much of rail, remain in that category in Britain, and across Europe, nuclear electricity in France and municipal water are in this category too’ (Smith and Hannan 2003; Helm 2006; OFWAT/OFGEM 2006).

## **1.2 Efficiency**

The second major expectation of privatisation was that it would improve the efficiency of the water industry. Private ownership was expected to bring stricter cost management, driven by the incentive to increase profit margins; as a result the companies’ productivity would improve, enabling consumers to benefit from lower prices, while the companies would benefit from higher profits. OFWAT’s regulatory system is also designed to create incentives for the companies to increase their profits by making efficiency savings. The expectation would therefore be that the industry’s operating costs would be reduced.

The data on operating expenditure, however, do not show any significant reduction in the 15 years since privatisation. After adjusting for inflation, the operating expenditure reported by OFWAT increased in the early 1990s, before falling back to the same level as the year after privatisation.

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<sup>10</sup> International Monetary Fund, Public–private partnerships, 12 March 2004, para 38, <http://www.imf.org/external/np/fad/2004/pifp/eng/031204.htm>

**Table 3:** *Operating expenditure of water companies, 1990–91 to 2004–2005*

	1990–91	1994–95	1998–99	2004–2005
£m 2004–2005 prices	2 946	3 219	2 955	2 937
Index 1990–91=100	100	109	100	100

*Source:* OFWAT 2005, PSIRU calculations.

But changes in operating expenditure reflect not only productivity changes but also outputs, and so a level performance in terms of operating expenditure still reflects productivity growth if output rises. For example, the EU directives on quality require not only increased capital expenditure but also higher maintenance costs: an EC study estimated that the wastewater directive alone requires an extra £290 million per year in operating expenditure by 2010 (EC 2000). The overall productivity of the water companies has certainly increased since privatisation, but the question of the impact of privatisation and regulation on productivity remains.

The empirical evidence indicates that there has not been a significant improvement in productivity performance since privatisation. One study analysed the growth in productivity in the five years before privatisation and the 10 years after privatisation, and concluded that: ‘despite reductions in labour usage, total factor productivity growth has not improved since privatisation’. A further study using a different method showed that total factor productivity may have improved after 1995 but ‘neither paper finds any evidence of an increase in TFP growth that can be directly attributed to privatisation’. Since 1999 performance appears to have got worse; a paper commissioned by OFWAT in 2004 found a decline in productivity growth rates after 2001. This study focussed on operating expenditure, but it also found that for the water-only companies ‘capital efficiency appears to be declining ... particularly after the 1999 price review’. A further study, published in 2007, with a further change in methodology, confirmed the broad picture, and concluded that ‘while technical change improved after privatization, productivity growth did not improve ... average efficiency levels were actually moderately lower in 2000 than they had been at privatization’ (Saal and Parker 2001; Saal 2003; Stone and Webster 2004; Saal et al. 2007).

So the private companies cut jobs more rapidly than had been the case in the five years before privatisation, but although labour productivity has risen

slightly faster, when other factors are taken into account, including capital, the total factor productivity of the companies has grown less rapidly since privatisation than in the five years before privatisation.<sup>11</sup>

Table 4 summarises this evidence.

**Table 4:** *Productivity growth before and after privatisation*

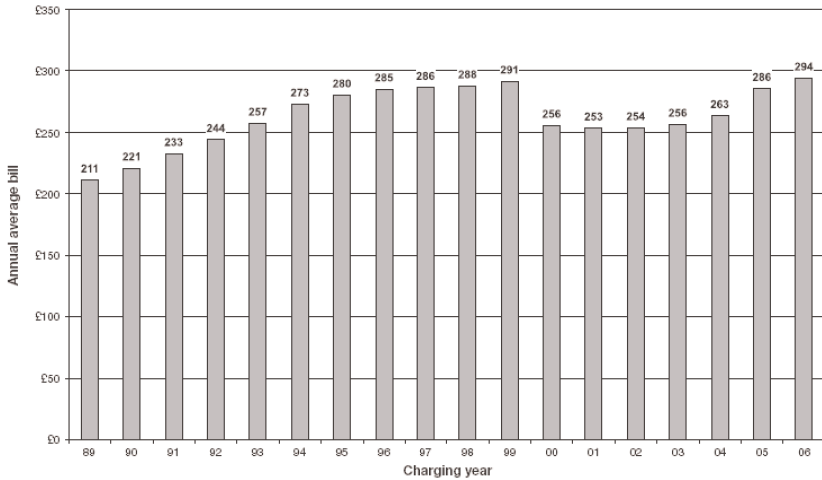
	Before privatisation 1985–90 Average annual % change	After privatisation 1990–99 Average annual % change	2000–2003 Average annual % change
Growth in output	2.7	2.6	
Change in employment	-1.9	-2.8	
Labour productivity	4.5	5.4	
Total factor productivity	2.3	1.6	
Opex productivity (water & sewer cos)		1.9*	1.8
Opex productivity (water only cos)		1.3*	1.2

*Note:* \* Operating expenditure (opex) productivity average for period 1993–99.

*Source:* Saal and Parker (2001), Stone and Webster (2004) and author’s own calculations.

The studies also found that the companies had been increasing their prices more quickly than their costs, which suggests that the OFWAT regulatory regime has failed to fix prices to reflect efficiency gains: ‘Moreover, total price performance indices reveal that increases in output prices have outstripped increases in input costs, a trend which is largely responsible for the increase in economic profits which has occurred since privatisation’ (Saal and Parker 2001). The universal experience of water privatisation in the UK has been a sharp increase in the cost of water; in cash terms, the average

<sup>11</sup> A comparison with a longer period before privatisation may be even less favourable because the RWAs reduced employment from 80,000 to 50,000 in the 15 years between 1974 and 1989, an annual reduction of over 6%; see Bernard Barraque, *Les politiques de l’eau en Europe* (1995, p. 233).

**Figure 1:** *Average annual cost of water, 1989–2004*

*Note:* £ real terms, 2006 prices, excluding general inflation.

*Source:* OFWAT 2006b.

annual bill for water and sewerage rose from £120 per year in 1989 to £294 in 2006, an increase of 245% in 17 years. In real terms, this represents a rise of 39% above the general rate of inflation.

The pattern of rises shows clearly that there was an initial rapid rise during the early 1990s, slower but still significant rises during the later 1990s, and then a one-off drop of about 12% in 2000 following the price review. The price reductions in the 1999 review were largely due to ‘clawing back’ the overgenerous settlements of previous years. Prices then levelled out, but since 2004 have risen sharply once again, following a new price review. The increase from 2004–2006 is the highest rise over two years since 1993–1994. A breakdown of the component elements in water bills shows that operating costs have remained roughly constant in real terms (as noted above). The entire increase in customers’ bills is due to the various elements associated with capital – capital charges, interest and profits – which have approximately doubled, in real terms, over this period (OFWAT 1999).

### 1.3 Employment, pay and conditions

Privatisation reduced the role of the trade unions. Overall union membership was nearly halved following privatisation; national bargaining was abandoned in favour of company negotiations, with some companies deciding to de-recognise specific unions, and the development of individual payment schemes undermined the importance of collective agreements. Workers in general felt less secure, while senior managers gained considerably from increased pay, bonuses and share options (Florio 2004).

There was an overall reduction in employment in the companies' water and sewerage operations. Jobs fell by 21.5% – 8,599 – between the first year after privatisation (1990) and 1999 in water supply and sewerage in the UK, excluding the effects of the companies' diversification into other areas. Employment fell in six of the companies: at least two of the others, Northumbrian and Anglian, would show a similar pattern were it not for extra employees taken on as a result of acquiring smaller water companies in recent years (Hall and Lobina 1999).<sup>12</sup>

One factor was the impact of mergers and takeovers, resulting in substantial job cuts at North West Water, Welsh Water, Northumbrian Water and Southern Water.<sup>13</sup> This commercial logic was reinforced by the administrative demands of the regulator, who insisted on significant reductions in operating costs as a condition for approving the mergers. Another reason for job reductions in the core water company was growth in the subcontracting of work previously carried out by specialist water workers. This also led to the creation of different employment conditions, even where these subcontractors were subsidiaries of the same group: Thames, Southern and Yorkshire all did this. As well as reducing jobs, some companies deliberately eroded employee rights; Northumbrian, for example, systematically put more and more of their employees on short-term contracts of 23 months in order to be able to dismiss them at will without the employees concerned being able to make use of the protection against unfair dismissal legislation (Hall and Lobina 1999).<sup>14</sup>

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<sup>12</sup> Northumbrian Water: following the takeover by Lyonnaise des Eau in 1996, Northumbrian was merged with North East Water, and so the employment levels were no longer comparable. Anglian Water took over Hartlepool Water in 1998.

<sup>13</sup> For example, according to Scottish Power's 1997 annual report, restructuring and disposals following the takeover of Southern later cut 624 jobs in the water operation, a reduction of 14%.

<sup>14</sup> *Northern Echo*, 23 August 1994, 'Northumbrian Water is asking new recruits to sign contracts which include a clause waiving their rights under employment protection legislation. The fixed term contracts generally run for two years, but the clause prevents workers from claiming unfair dismissal or redundancy pay if they lose their job at the end of the period'.



This decline in employment in the core water companies is obscured by the employment trends in the groups as a whole, employment in four out of five of which, including their diversifications overseas and into other sectors, rose markedly.<sup>15</sup>

**Table 5:** *Overall fall in employment in core water and sewerage companies, 1990–99*

	1990	1996	1999	Change in numbers, 1990–99	Percentage change, 1990–99
Employees in water supply and sewerage, 10 regional companies	39 962	34 578	31 363	–8 599	–21.5%

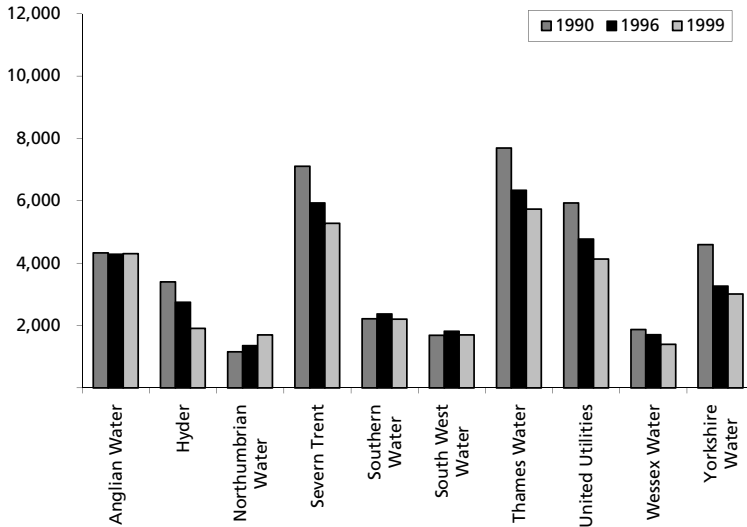
*Source:* Hall and Lobina (1999).

**Table 6:** *Employment growth in groups owning water companies, 1990–99*

	1990	1996	1999	% growth 1990–99
Anglian Water	4 328	5 261	5 297	22
Severn Trent	7 298	10 037	11 095	52
South West Water	1 684	3 005	3 508	108
Thames Water	7 790	10 360	12 492	60
Yorkshire Water	4 591	4 318	4 209	–8

*Source:* Hall and Lobina (1999).

<sup>15</sup> Source data: PSIRU database, companies' annual reports; for the sake of comparability the data include only those companies not involved in major mergers since 1990.

**Figure 2:** *Employees in water and sewerage companies, 1990, 1996 and 1999*

Source: Hall and Lobina (1999).

## 2. Health care

The UK's National Health Service (NHS) has been the subject of a series of reforms, many of which include the extension of the role of private sector. This section focuses on two of these initiatives:

1. the policy of competitive tendering of non-clinical services, introduced in the 1980s;
2. the Private Finance Initiative (PFI) introduced in the 1990s.

### 2.1 Competitive tendering of non-clinical services

The policy of tendering hospital cleaning, catering and laundry work was introduced by the Thatcher government following pressure from cleaning contractors. From 1983 all health authorities were expected to put this work out to tender, with the in-house team submitting a parallel bid. The expectation was that this would lead to substantial cuts in costs, and thus an increase in efficiency. As shown in Table 7, there was a substantial reduction in the number of jobs (PSPRU 1992).

**Table 7:** *Reduction in jobs of NHS ancillary workers, England and Wales, 1983–91*

	No. of jobs (full-time equivalent)	No. of jobs		
		Total	Men	Women
1983	205 000	280 000	66 000	214 000
1991	121 000	169 000	45 000	124 000
<i>Change</i>				
Jobs	-84 000	-111 000	-21 000	-90 000
%	-41	-40	-32	-42

Source: PSPRU (1992).

The average reduction in costs observed following these exercises was 26% on cleaning contracts, with larger cuts recorded where private contractors won the tender; savings in catering services were 10% (NAO 1987; Shaeff 1988). An econometric analysis of the impact, based on a study of hospitals in Scotland, also observed average cost reductions of about 25% in cleaning costs following tendering, but, after adjusting for time-trends and hospital characteristics, concluded that the actual level of savings attributable to tendering was 5.9%. The savings to the health authorities were higher if a private contractor won (8.9%) than if an in-house bid won (5.0%), despite having to sustain the contractors' profit margins (Milne and Wright 2004).

In such labour-intensive services, virtually all these savings came from reduced labour costs: four-fifths of the cost savings came from reductions in the hours worked, either through reductions in staff numbers or through reductions in the hours of the (largely part-time) workforce. The rest is attributable to reductions in pay and conditions by contractors, especially where union organisation was weak, and both contractors and in-house teams have reduced bonus or other supplementary elements of earnings. Although in-house bids won about three-quarters of the cleaning contracts, they also frequently cut jobs and hours in order to be competitive against private contractors (Schaeff 1988; PSPRU 1992).

The impact on pay and conditions was intended by the government. It was made possible by repeal of the Fair Wages Resolution that had required contractors working for public authorities in the UK to give their workers at least the same pay and conditions as specified in the current collective agreement for local government workers (Clegg 1970). When the policy of

competitive tendering in the NHS was introduced in 1983, contractors were thus free to set any level of pay and conditions that they chose. The effect was spelled out by a government publication:

Most of the savings from contracting out arise because contractors offer poorer conditions of employment ... they eliminate costly bonus schemes and overtime working, provide little or no sick pay, and avoid national insurance payments by means of more part time working. The difference in total labour costs may typically be of the order of 25 per cent. Pensions are the main single element in it. (HM Treasury 1986)

In practice, the contractors largely observed NHS pay rates and holidays (although they did not do so later when local government services were tendered), but they did not provide a pension scheme. This also clearly explains how contractors could offer higher savings than in-house teams, while still generating a profit margin: they were essentially a transfer from employee benefits.

This had wider consequences than the direct impact on working conditions. The process reduced the coverage of collective bargaining, so that a significant proportion of workers in the NHS – those now employed by contractors – were no longer protected by collective agreements. It reduced the level of unionisation because the contractors resisted attempts at organisation. It fragmented the workforce amongst a number of different employers. It created job insecurity for workers, which was repeated as the five-year contracts came up for renewal and further tendering.

In assessing the impact on efficiency, two aspects need to be considered. First, cost reductions were being achieved in ancillary services in the NHS before competitive tendering. In England and Wales, employment of ancillary workers in the NHS fell by 3% per annum between 1981 and 1984, compared with an average reduction of 5% per annum in the following seven years under competitive tendering. Milne and Wright estimate a background trend of 3.9% annual savings in Scotland, with competitive tendering delivering an extra 5.9%. The rate of reduction in employment was thus accelerated by tendering. It was the tendering process that delivered the great majority of these extra savings, not the change of ownership itself: as already mentioned, the in-house bids won three-quarters of all cleaning contracts (Shaeff 1988; PSPRU 1992; Cumming 1992; Milne and Wright 2004).

Table 8 summarises the overall picture using the Milne/Wright figures. These are consistent with the earlier estimates that about 80% of total savings came from reductions in jobs and hours, and that the overall reduction in jobs averaged 5% per annum.

**Table 8:** *Savings from NHS trend productivity, competitive tendering and contractors*

Mechanism	Source of saving	Saving as % of total labour costs
NHS trend productivity	Jobs/hours reductions	-4%
Tendering	Jobs/hours reductions	-1%
Contractors	Pay/conditions reductions	-1%

Second, in the absence of measured output, cost reductions may reflect service reductions. Five per cent of all contracts won by contractors were terminated, and many others reported problems with standards of performance. The effect on staff of the tendering process was predictably demoralising, and in some cases led to prolonged strikes lasting a year or more, for example at Barking and Addenbrookes hospitals in 1984 and 1985: ‘the longer staff had worked at the hospital, the more demoralised they seemed ... long service staff perceived change as negative and unwelcome’ (PSPRU 1992; Cumming 1992). Since the 1990s there has been a significant rise in infections acquired in hospitals, such as MRSA and *C. difficile*, whose control is related to standards of cleanliness. The subsequent concerns about the quality of cleaning led to investment by government rather than by private companies. In 2000 the government introduced a Clean Hospitals programme, which included the injection of an extra £31 million to improve standards of cleaning, together with new standards, including cleaning frequencies, in a new manual, the employment of extra ward housekeepers and annual inspections by ‘patient environment teams’, suggesting a lack of confidence in the effectiveness of cleaning contracts (Davies 2005). Problems of monitoring and incomplete contracts, coupled with pressures of tendering indicate that contractors may seek to erode the level of service delivered. As a result, the cost savings associated with tendering could, in part or even in whole, simply reflect a poorer service. Milne and Wright conclude that:

It is not inconceivable that the small cost savings that we observe could have been generated by equally small reductions in the quality of the cleaning services delivered. If this were the case, then the cost savings that we estimate may have had nothing to do with the tendering process per se, and simply reflect the outcome that competitive tendering delivers a lower quality service at a lower cost. (Milne and Wright 2004: 21–22)

There is no direct consumer benefit, as there are no patient charges in the NHS, so the benefits from savings are fiscal gains to taxpayers. The gross cost savings overstate the fiscal benefit: the indirect effects of reductions in jobs and incomes include increased unemployment and other benefits, reduced income tax and national insurance contributions, and reduced VAT as a result of lower spending. The net fiscal benefits are thus substantially smaller than the gross reduction in public expenditure (CPS 1995).

The impact on investment was negligible. Private investment was not an objective of the policy of tendering these services. In such a labour-intensive service as cleaning there was no expectation that contracting out services would involve capital investment by contractors, although both catering and laundry services involved capital equipment that would be financed by contractors following outsourcing.

## **2.2 PFI**

In 1981 the Thatcher government set up new rules allowing it to consider using private finance for public infrastructure investments. The objective was to avoid expenditure controls by disguising assets as private, and also (as an ideological component) to find ways of introducing private capital into the public sector. These ‘Ryrie Rules’ stated that a project should be privately financed only if this was more cost effective than public financing, and that it should still be counted against the public body’s capital budget. No private investment project ever met these criteria (the government used private finance for the Dartford Bridge in 1986, but had to break the rules to do so). They were therefore abolished in 1989.

In 1992 the Private Finance Initiative (PFI) was created to encourage such schemes, but still no private schemes were viable until in 1994 it was made compulsory for all government departments to consider private financing for every capital project. In 1997 legislation was passed that guaranteed government payment of any debts incurred by health authorities under PFI schemes, even if the health authority went bankrupt. The New Labour government also resisted proposed rules from an accounting standards body that would have made it very difficult to treat PFI projects as private rather than public investments. A later ruling from Eurostat allowed PPPs (public–private partnerships) to be treated as private investments as long as the contractor carries availability risk – that is, maintaining the building or facility in useable working condition – an easy criterion to fulfil. The great majority of PFI schemes are thus off the public sector balance sheet, thus achieving the scheme’s fiscal objectives (Spackman 2002; Hall 2004).

In addition to these rules favouring PFI schemes in general, the process of selecting, agreeing and overseeing PFI schemes also creates opportunities for contractors to obtain better returns. The PFI itself uses 'notional', not actual, public sector comparators, which are invariably increased by adjustments for risk and assumptions of cost overruns, so as to make PFI more attractive. Successful bidders engage in further negotiations that can either reduce the outputs expected or increase the costs:

significant cost escalation occurs between strategic and outline business case stages (SOC and OBC) and between outline and full business case stages (OBC and FBC) ... in five schemes reported to the Health Select Committee in 2003 PFI costs increased from SOC to OBC stages by between 64.7 and 171.7 per cent ... in first wave hospital PFI schemes PFI costs increased from OBC to FBC stages by between 33 and 229 per cent. (Pollock et al. 2005)

The negotiations also led to sharp reductions in the schemes' outputs: in the first wave of PFIs, there was on average a cut of 30% in the number of beds, and clinical staff were cut by up to 25%, compared with original specifications. Once schemes have started, and their future earnings are secure, companies can sell the scheme to new owners, taking a capital gain, and/or take advantage of improved credit ratings to refinance schemes on better terms. By March 2006 40% of operational projects had changed ownership, and in 50% of the cases of changed ownership the debt had been refinanced as well (Pollock 2004; Pollock et al. 2005).

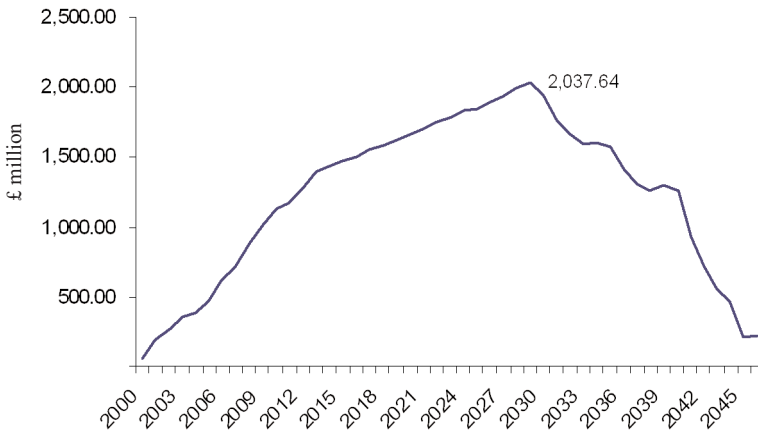
These rules and processes make it easier to justify PFI projects, and make them more attractive to the private sector, but the theoretical advantages of risk transfer and reduction of cost overruns are not evident in practice (Pollock 2004). The actual cost of capital in PFI schemes remains higher than if the same project was conventionally procured by the public sector because of the lower rate of interest obtainable by the government compared with the private sector. The fiscal advantage of PFI is not therefore apparent in reduced costs to the taxpayer, but in enabling increased capital expenditure on projects that would otherwise be constrained by UK or EU limits on government borrowing.

The PFI system has certainly delivered investments. According to a 2006 report, 'the NHS capital programme leaves Britain building more hospitals than the rest of the G7 nations put together' (Bosanquet et al. 2006: 4). By February 2008, a total of 93 deals had been signed for projects delivering total investment of just over £10 billion.

There is considerable evidence that this finance is delivered at the expense of the budget available for health services, however. Under a PFI scheme the NHS leases the hospitals from the PFI contractor for a period of 30 years or more. The annual payments include interest, the principal of the debt and capital maintenance costs; they are contractually required and come out of the trusts' own general budget. Figure 3 shows that the annual payments by NHS trusts to PFI contractors will continue for the next 38 years, peaking at £2 billion per year in 2029, over three times the level of payments in 2006. The payments will total £57 billion in respect of investment worth £10 billion (all figures in current terms).

The sheer scale of PFI projects has also been a factor in the emergence of deficits at a number of NHS hospital trusts. Instead of central government managing the capital costs of loans and bond finance before distributing funding for services to health authorities, the trusts themselves now have to manage capital costs as part of their delegated budgets. On average, NHS trusts with PFI schemes are having to pay 8.3% of their total income in charges and other payments linked to PFI – more than the 5.8% of income allocated to each trust for capital costs. This funding gap of 2.5% has to be covered by drawing on income intended to pay for services (Hellowell and Pollock 2007).

**Figure 3:** *Expenditure on PFI schemes in the NHS*



Source: Calculated from Treasury PFI projects list [http://www.hm-treasury.gov.uk/documents/public\\_private\\_partnerships/ppp\\_pfi\\_stats.cfm](http://www.hm-treasury.gov.uk/documents/public_private_partnerships/ppp_pfi_stats.cfm)



The schemes will entail large fixed expenditure for many years ahead, which cannot be adjusted in response to changing circumstances and so transfer unforeseen risks onto the part of expenditure for providing services: ‘many of the building projects impose costs that are not justified in terms of income under payment by results ... Trusts which have much less contracted expenditure – current as well as capital – are going to be much better placed in the near future to cope with the rigours of the reform agenda as it will be easier to adjust to variation in revenue’ (Bosanquet et al. 2006: 10–11).

The problems have been demonstrated at the Queen Elizabeth Hospital trust in Greenwich, which has a major PFI scheme the costs of which have risen to 11.3% of the total budget, nearly double the government allocation for capital costs. A report by the Strategic Health Authority warned that QEH and other local trusts in a similar situation would ‘incur recurrent [income/expenditure] and cash flow deficits even if they operate as efficiently as the average hospital trust in England. A high proportion of their underlying [income/expenditure] and cash flow deficits are attributable to this effect’.<sup>16</sup> In 2007 the QEH announced cuts of around 10% in clinical services.

The general impact of PFI on efficiency is unclear. There is a general problem with measuring the output of public services such as health care in the absence of priced output, and UK national accounts now calculate output by using a bundle of treatment activities, such as hospital in-patients and day cases, ambulance journeys, consultations with and prescribing by family doctors and district nurse visits. Input measures are also sensitive to the use of different assumptions in valuing capital consumption, for example. Subject to these limitations, the National Statistical Office has estimated that from 1995 to 2003 NHS output (not allowing for quality change) grew by 28%, and NHS inputs by between 32% and 39%, and thus NHS productivity declined by up to 1% per annum between 1995 and 2003 – covering the period in which PFI schemes were introduced (NSO 2004). This provides no evidence to support the view that PFI has improved efficiency overall, and leaves open the possibility that PFI has contributed to a negative or static performance. Under government rules for PFI in the NHS, no medical, nursing or paramedical employees are outsourced to contractors. The same set of support staff as were subject to competitive tendering were usually transferred under the early PFI schemes – cleaning, catering and laundry workers, as well as porters – along with building management teams, but

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<sup>16</sup> South London and Maudsley Strategic Health Authority (2007), ‘Acute sector deficits in SE London’.

since 2004 the Treasury no longer requires such staff to be transferred. Originally, these employees became employees of the private contractor, as under competitive tendering, but from 2001 the government agreed that they would be treated as ‘seconded’ NHS employees. The effect on conditions of employment was more complex than under outsourcing alone because the ‘trusts’ that now run NHS hospitals have been given freedom to vary national pay and conditions. In one hospital with a PFI scheme, non-clinical staff were subject to four different sets of conditions – national, local trust, conditions created by a private contractor following competitive tendering, and the new conditions of the private PFI contractor. This created problems and animosity, with some staff receiving shift premia for weekend work and others receiving none. Changes in working practices also had a destabilising effect. For example, the turnover of catering staff rose from 10–15% per annum to over 100% following PFI, largely due to a change from cooking in kitchens to distribution of pre-cooked meals (Earnshaw and Ellis 2004).

## **Conclusions**

Five broad sets of conclusions can be drawn from this review, concerning:

1. political objectives (fiscal and ideological);
2. economic objectives (investment and efficiency);
3. distributional impact;
4. effectiveness of governance regimes;
5. prospects and constraints for future policies.

The political objectives have been largely met. In fiscal terms, the large investment programme of the water sector, and the investments through the various PFI schemes, are off the government’s balance sheet. In ideological terms, the private sector remains dominant in the water sector and has substantially increased its role in health services. The objectives of compulsory tendering under the Thatcher governments – namely reduced pay and conditions and weakened unionisation – were also achieved; subsequent agreements have halted these trends but not reversed them.

It is less clear that the stated economic objectives have been achieved. In terms of efficiency, the evidence suggests that the water sector has performed poorly in terms of productivity growth compared with previous trends under the public sector; and in the health service, there is no compelling evidence that efficiency gains have varied from trend as a result of either compulsory tendering or PFI, while there is some evidence of service effectiveness deteriorating as a result of both outsourcing and, especially, PFI. In terms of investment, the water companies have delivered higher investment than

under the public sector in the 1980s, but this has been driven largely by external political requirements, which the public sector was beginning to respond to, and at a higher cost of capital than would have been the case in the public sector. The PFIs in the health sector have also delivered a substantial investment programme, again driven by political requirements, also at a higher cost of capital than under conventional procurement and with greater negative impacts on levels of service. In the absence of offsetting productivity gains, these private capital programmes have been, and continue to be, a source of increased burdens on both water users and patients.

The policies have had a negative redistributive effect. Outsourcing of ancillary work in the NHS has generated new returns to capital at the expense of employment levels and conditions. Consumer expenditure in a privatised monopoly (water) and public expenditure on health service PFI schemes are now sustaining higher rates of return than would be the case under direct government borrowing, at the expense of employees or consumers (in the water sector) and employees or taxpayers (in the health sector), or a mixture of both. In health services, the structural effect of both outsourcing and PFI on ancillary workers has been to create fragmented organisation and bargaining, greater insecurity and an overall worsening of conditions through the two-tier workforce.

The similarities in terms of governance issues in both services are striking, despite the fact that their formal ownership and regulatory structures are completely different. The water companies have negotiated price cap settlements that successfully deliver higher returns on capital than envisaged by the independent water regulator, OFWAT; the consortia involved in PFI deals have negotiated contracts that successfully deliver higher returns, even at the expense of lower levels of service compared with government and NHS objectives. The closeness of relations between the water companies and OFWAT over regulatory issues is mirrored by the closeness of private sector companies to policy-makers in the health service; in both sectors, this influence is stronger than that of either consumers or unions.

Current policies are likely to continue in both sectors for the foreseeable future. Surprisingly, the fiscal motive for the continued privatisation of water is perhaps weakest. The UK's 'golden rule' could certainly justify the substantial savings that could accrue from renationalisation, and the EU Stability Pact rules create no obstacle to the renationalisation of the water sector, as trading entities are treated the same whether publicly or privately owned. But the fiscal motives remain as strong as ever for the use of PFI and other forms of PPPs, in health and other public services, as these successfully

reduce apparent borrowing under both UK fiscal rules and EU Stability Pact rules. The EU policy choice between strict enforcement of fiscal rules and encouragement for PPPs now firmly favours the latter.

The ideological motive for promoting a private presence in public services remains a constant. Although this is less enthusiastically articulated than under the Thatcher government, the superiority of private sector economic performance remains a central assumption of current government policies despite the lack of empirical evidence, and the evolution of EU internal market and procurement rules favours the growth of outsourcing of public services. This ideological assumption is at odds with a stubborn public resistance to the use of privatisation in both these sectors, as shown by the successful opposition to water privatisation in both Scotland and Northern Ireland. In general, the devolved parliaments and executives in Scotland, Wales and (now) Northern Ireland are showing signs of responding to this, but are constrained under the fiscal controls exercised by the UK government, which shows little sign of changing policy.

The private water companies and PFI consortia now enjoy sufficient contractual and statutory security to make it expensive or difficult for governments to reverse the privatisations. The economic inefficiency and regressive distributional effects of privatisation are thus likely to persist in both sectors, until government policies change. The key measure required to obtain best value from services is the refinancing through the public sector of all the private water companies and PFI schemes.

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## **Implications of privatisation and marketisation in Lithuania – telecommunications and transport**

### **Introduction**

Rapid growth of the service sector due to the development of new services has been a significant factor in growth and structural change in the Lithuanian economy, as well as elsewhere in the EU. Services have become more diverse and complex, increasing overall employment as well as enterprise. However, Lithuania, a small country that was part of the Soviet Union until 1990, stands somewhat apart and can be viewed as a special case, since these changes coincided with the transition from a planned to a market economy, through privatisation, the establishment of market institutions, and the liberalisation of product, financial and labour markets. During this period the country was transformed from a small closed economy into an open economy, with increasing exposure to international market pressures. These developments have significantly affected both corporate governance and labour relations. Reforms have brought about a significant shift in labour management, particularly in terms of reducing the extensive social benefits offered by the Socialist state. The implications of privatisation and marketisation for employment, as well as output and productivity, particularly in public services, remain unexplored.

This chapter focuses on two branches of the service sector. Telecommunications has undergone full liberalisation and marketisation. The privatisation and restructuring of the state monopoly, along with strong entrepreneurship trends, induced the establishment of a strong competitive environment, influencing the extent, range and quality of public services provision. Transport, on the other hand, shows the complexity of restructuring and the evolution of ownership. Privatisation in this case



included the transformation of state-owned monopolies, as well as municipal enterprises. Sectoral restructuring is ongoing, and its diverse consequences are affecting both employment and consumers.

## 1. Overview of privatisation in Lithuania

Lithuania's transition to a market economy was fostered by political changes driven by independence in 1990. Economic policy was put at the top of the reform agenda, with leading politicians and economists of different hues supporting liberalisation and privatisation. The future of the economy was debated by supporters of the so-called Swedish model and of the Anglo-Saxon-type financial markets-based model. But these models, especially the manner in which the necessary transformation was to be accomplished, were only vaguely understood. Therefore, significant changes in direction and methods were encountered throughout the process of privatisation and liberalisation. Lithuania's new governmental authorities played a major role, re-establishing the legal system, for example, introducing laws and regulations on privatisation that were based on ideological consensus. The labour movement, on the other hand, has played a minor role. The old Soviet trade unions, which served as executors and supporters of the Communist state, among other things distributing various social benefits and services, ceased to exist. Some employees became actively involved in the nationwide 'Sajudis' movement, which brought the country to independence and introduced privatisation and transformation policies within companies, while others resisted change or merely remained on the sidelines.

### 1.1 Privatisation phases, methods and results

The extent and effects of privatisation have differed significantly by sector. The economy's strong industrial orientation, well developed agriculture and the underdeveloped service sector inherited from the planned economy formed the backdrop for economic transformation. A diverse structure of state ownership was characteristic of public sector enterprises: large strategic companies, centrally managed by the Soviet authorities, dominated industry, while those serving regional and local needs were under local administration, including the municipalities. Therefore, reform was initially oriented towards privatisation of the largest industrial companies, with the transformation of services and infrastructure postponed.

The short period of *early privatisation* (1990–1991) was driven by a political will to make change irrevocable by accelerating the break up of the largest industrial companies. Since the legal foundations were still under

development, many companies were privatised on the initiative of the management. Though privatisation during this period involved only a small number of entities (approximately 60), experience was accumulated and some of the key principles of the first Law on Privatisation laid down.

During the *first stage* of privatisation (1991–1995) the intention was to provide all Lithuanian citizens with an equal opportunity to participate in privatisation and so ensure social justice. Thus, the main direction of privatisation was the creation of ‘shareholder capitalism’, with strong employee participation. It was oriented, first of all, at the rapid privatisation of state-owned manufacturing companies, the largest employers in key sectors of the economy (Darškuviene, Hanisch and Mygind 2006).

The success of this stage is mainly indicated by the sheer volume of companies concerned (Table 1): in total, 5,714 entities or 30% of the total book value of the assets of state-owned companies listed for privatisation were privatised; 71% of all state-owned entities went through the process of voucher privatisation, involving several methods of acquiring company shares (public share offerings, auctions, tenders for best business plans); 50% of the companies concerned were privatised by public subscription; a dozen companies through tenders for the best business plan; and the rest were small entities privatised by auction. A high level of privatisation – by number of companies – was achieved in construction (98%) and in household services (97%). As a result of rapid privatisation, by 1996 the private sector, including companies with at least partial private equity, accounted for 68% of GDP.

**Table 1:** *Privatisation results in Lithuania, 1991–95*

	1991	1992	1993	1994	1995
Number of privatised entities	846	2224	1257	1071	566
Privatised equity, million USD	30.3	261.8	309.5	205.3	112.8

Source: [www.vtf.lt](http://www.vtf.lt)

However, if we evaluate the results of privatisation by equity ownership, the results are not straightforward. By the end of the first stage, the state equity ownership share was still significant, accounting for 48% of the capital of all privatised entities. Only 201 entities of all the companies undergoing privatisation had 100% private equity; in other privatised entities state ownership varied from 10% to 50%.

A lack of transparency in privatisation, imperfect and incomplete legal regulation, especially concerning joint stock investment companies, the large number of inexperienced minority shareholders, and the strong influence of insiders, especially concerning lending and other operations of privatised companies did not allow for quick and efficient company reorganisation. Joint stock investment companies played a negative role in privatisation. Having accumulated huge volumes of vouchers from citizens, they managed to acquire more than 39% of the equity of privatised entities. However, a lack of general management and, especially, of marketing skills on the part of the managers of joint stock investment companies prevented them from handling company operations well; the companies found themselves lacking financing due to voucher privatisation, the limitations imposed on foreign investors, weak commercial banks, but also cash drainage caused by weak and incompetent new owners. Such developments stopped the flow of investments. The underdeveloped banking system became an additional factor that adversely affected privatised companies. Many fell into financial crisis, halting wage payments to employees and even discontinuing operations. There are no reliable statistics on employment in privatised companies by the end of 1995, but some conclusions can be drawn from general statistics related to private sector employment. Unemployment increased as layoffs and the closure of a number of large privatised companies got under way.

This economic and social context marked the transition to commercial methods of privatisation, laid down in the new Law on Privatisation, marking the start of the *second stage* (1995–2000). Voucher privatisation was replaced by cash privatisation, and the emphasis was put on finding strategic investors for the remaining large state-owned companies. As the transition was coupled with economic crisis, privatisation of the largest infrastructure companies was postponed until the next stage. With too many governmental institutions (ministries, agencies) involved, an overreliance on the views of the individual state agency or ministry that was considered the ‘founder’ of the state enterprise in question and a lack of technical competence in the management of privatisation the process was inefficient.

The second stage of privatisation encountered significant difficulties; many entities were privatised for cash only after several rounds; and a number of privatised companies accumulated debts and huge losses. Privatisation acquired a negative reputation among the general public because of the financial distress, collective redundancies and even bankruptcies of a large number of privatised companies, the blame being attributed to the new owners and managers.

The *third stage* of privatisation (2000–present) involves the remaining minor state shareholdings, real estate and property, and state-owned companies that were previously excluded from privatisation under the law, including mainly shares in infrastructure companies and companies with a dominant market position. One designated privatisation method could be used or a combination of several. In some cases the state retained a ‘golden share’.

Though the second and third stages of privatisation show impressive results, they proceeded much more slowly than the first, especially as regards the sale of indebted and unprofitable enterprises. Data on second and third stage privatisation show an increase in the number of privatised entities until 2000, but a fall thereafter (Table 2). Possibilities for employees to acquire shares in their enterprises were limited to trading on the Stock Exchange; during this period shares in only two companies were sold to employees. The majority of privatisation methods favoured foreign investors, strong domestic investment groups and insiders.

**Table 2:** *Privatisation results in Lithuania in 1996–2003*

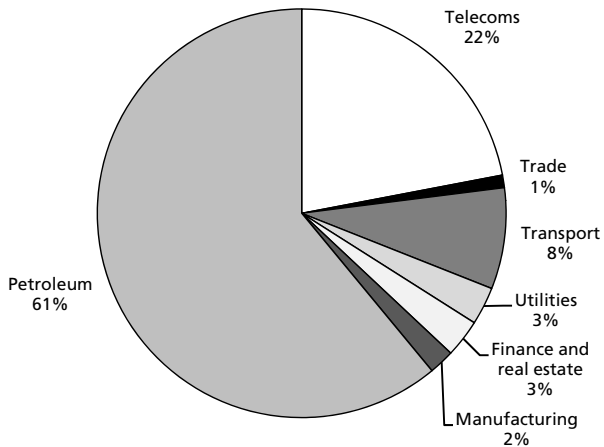
	1996	1997	1998	1999	2000	2001	2002	2003
Number of privatised entities	47	272	344	703	694	606	510	787
Privatised equity, million USD	0.8	20.3	582.5	117.9	229	108.8	66.5	227.6

Source: [www.vtf.lt](http://www.vtf.lt).

Analysis of the distribution of privatisation revenues by sector in 2006 shows the leading role of oil companies (61%), followed by telecommunications (22%) and transport (8%) (Figure 1).

By 2007 privatisation was nearly complete: key sectors of the economy, including manufacturing, construction and services (banking, telecommunications, a major part of transport) had been privatised. Major assets still in government control included companies in the energy sector, the monopolistic state Railway Company, postal services, education and health care. Liberalisation and marketisation policy, coupled with the need for investment and productivity improvements, have given rise to different approaches to the remaining public companies. The energy sector, being vitally important for Lithuania from a political point of view, is undergoing complex restructuring, partial privatisation and an opening of the market to

**Figure 1:** *Distribution of privatisation revenues by sector, Lithuania*



Source: <http://www.privatizationbarometer.net>.

private new entrants. The postal sector is being liberalised, including the former state monopoly along with 76 other postal service providers. The State Postal Company is viewed as an attractive acquisition target; however, the government has deferred its privatisation, taking into account the recommendations of EU directives. Education and health care, providing key public services under conditions of low incomes and a distorted cost structure for the majority of the population, are still not subject to privatisation.

Table 3 provides a synoptic overview of the differences between the three stages.

**Table 3:** *Overview of privatisation stages in Lithuania*

Privatisation stage	Policy guidelines	Mode of privatisation	Outcomes
<i>1st stage</i> 1990–95	Mass privatisation Promotion of social justice Limited privatisation to foreign investors	Initial privatisation Voucher privatisation	Partial privatisation of companies in majority of cases Initial capital accumulation Establishment of employee ownership Break up of Soviet trade unions Employee representation through political movement
<i>2nd stage</i> 1996–2000	Priority shift towards private sector Objectives include increasing investment and efficiency of privatised enterprises Strengthening competitiveness of privatised enterprises	Introduction of multiple privatisation methods Cash sale of enterprises	Staged privatisation Largest FDI privatisation transactions Privatisation of state monopolies to strategic investors Changes in initial ownership from inside to outside Concentration of ownership Reorganisation and bankruptcies of privatised enterprises, mainly industrial Non-trade union representation of employees
<i>3rd stage</i> 2001–present	Market liberalisation Productivity improvements Restructuring and privatisation of infrastructure companies Compliance with EU directives on market liberalisation since 2004	Use of multiple privatisation methods Priority: open tenders Cash sale of enterprises	Further concentration of ownership Redistribution of ownership Company mergers, acquisitions and takeovers Privatisation mainly to local investors Rising influence of trade union movement

## **1.2 Implications of privatisation for employee ownership**

The economic policy promoted by the political forces that brought the country to independence, as well as by subsequent governments, has played an important role in privatisation from the very outset, including possibilities for employees to have real power over enterprise decision-making, including the removal of managers and putting into effect the principle of social equality.

At the start of the transition employees possessed considerable power, which was in particular connected to the general political movement and the Workers' Councils within enterprises, and were quite active in making demands about the distribution of enterprise property and employee ownership. The result was a strong emphasis on the voucher system and on preferences for employees. Privatisation policy put much more emphasis on workers' interests and extended preferences for employee share acquisition: the percentage of shares available for employees was increased from 10% in 1991, to 30% in 1992 and to 50% in early 1993. Moreover, because of the only partial indexation of the price of the assets and the value of the vouchers the advantage of employees increased over time.

This system enabled employees to obtain a considerable ownership share, even in large enterprises with high capital intensity. The 20% of extra shares reserved for employees after 1993 initially did not have voting rights, but later on the general meeting of company shareholders could decide to convert them into normal voting shares. Employee ownership thus became an important element in privatisation, especially in large enterprises (Darškuvienė, Hanisch and Mygind 2006). During the first stage, vouchers and cash quotas were given only to residents and had limited transferability (to family members; later on, in exchange for outstanding housing loans). Later the possibility to invest or exchange them in return for shares in private investment funds was introduced. Though there are no official statistics on employee investment in these funds, their high number shows that the practice was widespread, which eventually reduced direct employee ownership.

At the end of the first stage of privatisation, due to changes in its direction and methods, employee preferences were abolished. Employees could acquire shares in the enterprises that employed them only by way of auction or public subscription. In a number of cases of privatisation by auction the company was taken over by insiders, most often the management. As a trend, ownership was further concentrated, and by the end of the transition period employee ownership became almost negligible. Non-employee investors have increased their stakes considerably through new share issues.

The end of the mass privatisation period was also marked by changes in the labour movement. The need for employee interest representation in the face of financial crisis and company restructuring encouraged the establishment of new trade unions, especially in large industrial companies, with the subsequent development of trade union associations.

## **2. Privatisation of the telecommunications sector**

Privatisation in the Lithuanian telecommunications sector is, on the one hand, part of a broader trend affecting European countries at the end of the twentieth century, reflecting real or supposed inefficiencies and the dangers of a pervasive government role in the economy (protectionism, government subsidies) (Stiglitz 1998). However, the Lithuanian case, together with other post-Soviet and former communist countries in Central and Eastern Europe, stands apart and presents a more difficult task for interpretation, as it took place alongside a much more fundamental process of market creation and economic restructuring from the very start of the transition period.

### **2.1 Background conditions for telecom privatisation**

Back in the 1990s the telecommunications sector in Lithuania, as in the majority of post-communist countries, was characterised by the dominant role of the state monopoly *Lietuvos telekomas*. Public services, technical support and commercial services were concentrated in this major provider of fixed-line services. The technological lag of telecom companies in Lithuania was considerable, and obstructed significant improvements in performance. As the telecommunications industry became the fastest growing industry in almost every country, further technological advances and industry growth required substantial financing. However, the state, given the general political and economic instability of the transition period, was no longer able to finance the necessary mass investment in developing services infrastructure. Thus, one of the major criteria for the sale of the state-owned monopoly became the investors' ability to finance investment in the restructuring of telecommunications networks.

Telecommunications privatisation in Lithuania was strongly interrelated with political decisions. As early as 1992 the strategic importance of modernising the sector was acknowledged by politicians. Influenced by the experiences of other countries, telecommunications were seen as an essential public service, which must be regulated in order to ensure that they are supplied in a manner consistent with the general public interest. For Lithuania liberalisation of the sector has meant introducing market competition and the reorientation of the sector's companies towards neglected consumer demand. The experiences of



other countries had shown policymakers that privatisation entails risks. The most dangerous included the failure of privatised enterprises in competitive markets, or the abuse of market power, for example, excessive pricing or anti-competitive behaviour by dominant companies. Therefore they sought a special approach for the privatisation of telecommunications in Lithuania.

The first stage of privatisation imposed a number of important constraints: the voucher approach entailed specific limits on ownership and deprived enterprises of a significant source of financing, equity inflows. Therefore, privatisation of the largest strategic companies, including telecommunications, was delayed until the second stage of privatisation, after a new Law on Privatisation introduced alternative privatisation methods, including cash sales and qualification criteria for strategic investors. Privatisation of the state monopolist – in fact, nearly the whole telecommunications sector – had to ensure strong inflows into the Privatisation Fund. Private owners were expected to improve efficiency, to bring know-how into the management of businesses, improve productivity and benefit consumers.

## **2.2 Privatisation of the state-owned telecom company and its results**

Privatisation policy and its effects on the telecommunications sector are best indicated by the case of Lietuvos Telekomas. Delayed until 1998, after the end of voucher privatisation, it was one of the last in the region (Estonian Telecom was privatised in 1993 and Latvian Telecom in 1994). However, the process started earlier. In 1992 regional networks and local companies were merged into a state-owned monopoly. In 1997 the state-owned company was reorganised into a stock company. A number of reorganisations were carried out aimed at a reorientation towards core activities and increased efficiency. A number of services were separated off by the establishment of a group of companies. Lietuvos Telekomas obtained equity participation in the majority of them, at the same time remaining the state monopolist in fixed-line phone services, which were considered to be key assets subject to privatisation.

Due to the size of the company, the specifics of the business and its extreme political importance, staged privatisation using different modes was carried out. During the first stage of partial privatisation, 60% of the shares were acquired by Amber Teleholding A/S, at the time a consortium of the Swedish Telia and Finnish Sonera companies. The strategic Scandinavian investor, which later merged to form TeliaSonera, thereby becoming the largest telecommunications company in Scandinavia and Northern Europe, paid 2.04 billion litas (510 million USD, with a commitment to invest another 210

**Table 4:** *Lietuvos Telekomas – financial indicators, 1997–2006*

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Revenue										
growth, %	–	35.4	8.0	6.0	1.8	–8.5	–16.5	10.8	1.7	0.02
EBITDA										
growth, %	–	55.0	23.6	26.6	7.6	–10.6	–23.4	–12.7	5.1	–0.6
EBITDA										
margin, %	32.3	36.9	42.2	50.4	53.3	52.0	47.8	46.7	48.5	47.9
Net profit										
margin, %	14.5	7.3	10.6	23.2	17.2	6.9	–4.5	4.5	11.5	17.8
Change in										
net profit, %	–	–7.2	3.4	12.5	–5.9	–10.2	–11.4	8.9	7.1	6.2
ROE, %	10.2	6.6	10.1	21.6	15.1	5.5	–3.1	2.9	7.5	11.8

Source: Author's calculations, based on Lietuvos Telekomas financial statements.

million USD) in a negotiated auction. At the time, the deal constituted the largest FDI in Lithuania. The privatisation agreement offered the strategic investor a number of favourable conditions. Along with market liberalisation policies, the newly adopted Law on Telecommunications (1998) granted a preferential position to foreign investors, namely a monopoly of fixed-line services until the end of 2002. After that date the market had to be fully liberalised. Zero profit tax and the possibility of expatriating dividends were also granted to the new owners. During the second stage of privatisation, in 2000, resulting from state budget deficits, another 20% of state-owned shares were offered in a public share offering through local and foreign stock exchanges, the first in the history of Lithuania's financial markets. The final stage of the privatisation of Lietuvos Telekomas was related to the government's decision to use the remaining state-owned shares as part of its restitution policy concerning land and other property: any person claiming his or her rights to land or other property owned before nationalisation by the Soviet government after the Second World War could choose between two options: (i) ownership of the previously owned property, (ii) an equivalent number of common shares in certain companies while relinquishing ownership rights. By 2006 the state-owned share in equity had diminished to 2.0%.

Strong shareholder control over management resulted in company restructuring, which sharply improved financial results, aiming at maximising shareholder value. In line with trends in privatised telecoms in

other countries (Megginson and Netter 2001), during the first three years after privatisation net profit margins rose from 7.3% to 23.2%. The EBITDA margin increased from 32.3% before privatisation to 53.3% by 2001, one of the largest in Central and Eastern European telecommunication companies. The company enjoyed strong cash flows, which allowed for dividend payments. As Table 5 indicates, the debt burden increased during the first three years following privatisation. The debt ratio (total liabilities to assets) reached 47.6% in 2000, mostly due to steeply rising long-term borrowing, while short-term liabilities were reduced. Subsequently, the debt has been reduced significantly (the debt ratio falling to 11.2% in 2006), following telecom trends in other countries.

However, since 2002 further revenue growth in the liberalised market has been limited, due to mobile services' cannibalisation of fixed-line services. Therefore the company had to look for new products and services for business development. Long-term business prospects were dependent upon investment by the telecommunications operator in networks and their maintenance, and a substantial up-front investment in switching equipment, transmission facilities and terminals, which will significantly reduce the average cost of services. As the fixed services market was not flooded with competitors, the company had time to reorganise and change the structure of services based on its up-front investments. As Achterberg (2000) recognises, even in an unregulated market the competitive advantage in terms of costs for an incumbent telecommunications service provider is a sustainable and effective barrier to entry.

Investment in Lietuvos Telekomas was rising steeply, affecting EBITDA growth. In 1997, before privatisation, total investment exceeded EBITDA by 33%, but the EBITDA rise was much steeper; starting from 2000 the amounts invested became lower compared to earned EBITDA. Total investments slowed in 2003. High depreciation caused a drop in company net profits from 2001, and even brought losses. However, the company's policy of network modernisation allowed it to maintain its competitive position in fixed-line services, and to lease lines to new private entrants to the market. Investment excesses on the assumption of steep demand growth led to overcapacity. Despite an increasing number of new market entrants, high entry barriers in terms of investment offered a competitive advantage for the company in the local market.

The need to finance these investments also changed the financing structure of the company. State financing was switched for debt, as the company borrowed from banks and issued bonds in the face of market uncertainties.

**Table 5:** *Lietuvos Telekomas – debt and investment indicators, 1997–2006*

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Investment, million Lt*	361	393	551	517	368	207	51	75	74	98
Investment growth, %	–	40.2	40.0	–6.1	–28.8	–43.0	–75.4	47.0	–1.3	32.4
Debt ratio, %	30.28	38.85	47.56	44.32	40.52	34.92	26.11	12.06	12.14	11.16
Change in debt ratio, %	–	8.57	8.71	–3.24	–3.79	–5.60	–8.82	–14.05	0.08	–0.99

Note: \* Current euro exchange rate: 1 euro=3.4528 litas.

Source: Author's calculations, based on Lietuvos Telekomas financial statements.

Large-scale restructurings were carried out in order to increase the efficiency of service provision and to introduce new services. But liberalisation of the local market, followed by new private entrants in the most competitive niches in 2002, did not leave much room for an increase in revenues from fixed-line services and, under significant pressure from new shareholders, productivity growth was approximately 44–45% during the first two years after privatisation (see Table 6).

**Table 6:** *Lietuvos Telekomas – productivity and employment indicators, 1997–2006*

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Productivity, thous.Lt/ employee*	65.6	95.3	137.6	163.4	184.1	213.7	226.5	231.1	242.8	237.2
Change in productivity, %	–	45.2	44.5	18.7	12.7	16.1	6.0	2.0	5.1	–2.3
No. employees/ year end	10152	9521	7122	6357	5749	4531	3586	3120	3005	3098
Change in number of employees, %	–	–6.2	–25.2	–10.7	–9.6	–21.2	–20.9	–12.9	–3.7	3.1

Note: \* Current euro exchange rate: 1 euro=3.4528 litas.

Source: Author's calculations, based on Lietuvos Telekomas financial statements.

The significant increase in productivity of 149% during the period 1997–2006 was related to employee layoffs, and partly to spin offs, that is, establishing companies providing non-core services that could be outsourced. During the ten years following privatisation employment at JSC Lietuvos Telekomas was reduced by two thirds, including both spin-offs and layoffs. At the same time, the company established a training centre, one of the largest in the country, engaging in training and upgrading of skills.

Privatisation led to the company's transformation into a dynamic, efficient business. The introduction of new products (digital TV, internet services) allowed it to strengthen its market position, and brought a small increase in employment. This trend, if it continues, bearing in mind expectations of strong telecommunications market growth and the company maintaining its strong position, would be in line with Birdsall's and Nellis's (2002) view on job layoffs as a temporary trend after privatisation, although in this case the job losses were substantial.

### **2.3 Private sector development and marketisation in telecommunications**

Service liberalisation in the telecommunications sector brought in new segments, first of all mobile and related services. As early as 1995 Motorola (US) came into the market, establishing a closed stock company Omnitel, with a shareholding of 38%. Another 62% of equity was brought by a Lithuanian business family. In the same year Teledanmark, the leading company in the telecommunications sector in Denmark, established a greenfield investment closed stock company Bite GSM with the participation of Lithuanian private enterprise. The aggressive strategies of the two companies and strong investments brought double-digit revenue growth. As early as 2001 the total number of mobile subscribers exceeded fixed-line subscribers. Despite several more licences issued for mobile operators, the two companies became the leaders of the mobile service sector, fostering changes within the whole telecommunications sector. Table 7 indicates the growth dynamics of mobile services. The double-digit growth during the ten-year period came at the expense of the fixed-line service provider and has changed the service structure. The fall in the growth rates of new mobile subscribers to a mere 8–9% in 2006 indicates that market saturation has been reached.

**Table 7: Dynamics of public fixed-line and mobile telephone networks, 1997–2006**

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Growth in the number of active cellular mobile telephone subscribers, %	195.7	77.5	28.4	48.1	100.0	60.3	28.8	45.1	42.7	8.4
Growth in the number of active cellular mobile telephone subscribers per 100 population, %	200.0	81.0	28.9	49.0	100.7	60.8	29.5	46.1	43.5	9.0
Growth in the number of main telephone lines connected to digital exchanges, %	–	–	–	–	36.1	5.2	–8.6	0.4	–1.6	–1.3
Growth in the number of fixed telephone lines per 100 population, %	6.1	6.8	3.8	3.7	–2.7	–18.5	–10.8	0.0	–1.7	–0.4
Growth in the number of main public pay-phones, %	–	–	–	–	–5.3	–12.5	–9.5	0.0	–21.1	–20.0
Growth in the number of xDSL subscriptions, %	–	–	–	–	–	320.0	139.0	102.0	106.7	70.1

Source: Lithuanian Department of Statistics.

The development of private businesses brought diverse market structures to different telecommunication subsectors. Though the number of fixed-line service providers reached 52, Lietuvos Telekomas, renamed TEO LT, remains the leader, accounting for over 45% of total revenues (see Table 8). Thus the monopolistic structure remains in fixed-line communications, radio and TV transmission, even after market liberalisation in 2002. At the other extreme is the cable TV market where the market share of the two largest companies is only 10%. The Lithuanian mobile service market is highly oligopolistic: by 2006 the number of mobile service providers was just 7 – Bite and Omnitel alone accounted for 40% of total sector revenues as of 2006.

**Table 8:** *Telecommunications market structure, 2006*

Subsector	Total market revenues in 2006 (million euros)	Market change during 2006 (%)	Number of market participants	TEO LT share of total market in 2006 (%)
Fixed telephone services	425	-4.3	52	96.0
Devoted line services	25	-2.9	15	51.7
Internet access services	265	24.2	115	45.2
Data transmission services	47	16.9	14	50.4
Network connection services	607	14.3	+4	19.1
Mobile telephone services	1238	5.2	7	–

*Source:* Lithuanian Department of Statistics, author's calculations.

As competition increased in the Lithuanian market, saturation made it less attractive for later entrants, flattening market growth and consolidating the position of incumbent operators. The operators compete mainly on market share and the provision of a range of differentiated services, with less competition on price.

## 2.4 Ownership and governance

Diverse ownership and governance systems have emerged in the sector. After staged privatisation the former state-owned fixed-line monopoly Lietuvos

Telekomas became a listed corporation. The governance structure became characterised by the strong control of the major shareholder, a foreign strategic investor, and a number of minority shareholders, with clearly expressed and diverse economic interests (majority foreign shareholder vs minority shareholders, and so on). After a series of divestitures and spin-offs Lietuvos Telekomas has equity participation in a group of related companies. Other governance structures emerged in private companies in the sector, with ownership highly concentrated in the hands of major owners, that is, entrepreneurs, as well as local and foreign private equity funds. Managers have to overcome the inherent conflict between the interests of their parent companies and those of their own companies.

Strong competition between service providers, growth of the sector and international mergers stimulated the concentration of ownership. A few examples illustrate the active transfer of ownership within the major sectoral enterprises towards a higher level of share crossholdings. The expansion policy of Scandinavian investors was indicated in the takeover of 55% of the equity of mobile service provider Omnitel by the major shareholder in Lietuvos Telekomas in 1998, later increased to 100%. The merger of Telia and Sonera means that the two Lithuanian market leaders are now within the same international group. Another case of share crossholding was the investment by a Lietuvos Telekomas subsidiary in the shares of mobile market leader Bite, and their subsequent sale in 2000. The trend towards equity concentration was also clearly illustrated when TDC (former Tele Danmark, A/S) increased its shareholding in Bite to 100% in 2000 (subsequently sold to a private equity fund).

Concentration of ownership in the sector has led to increased regulatory attention in order to reinforce competition (see <http://www.rtt.lt>). The common EU regulatory framework has been applied in the Lithuanian telecommunications market since EU accession in 2004. Four main areas in which operators can be regarded as having significant market power were defined: fixed-line telecommunications, GSM, leased lines and interconnections. From the legal point of view, there are cases in which telecommunications operators can be treated as having a 'natural monopoly' and some limitations are imposed upon them. An entity can be treated as having significant market power if its share in the relevant telecommunications market is 25% or more. Another form of intervention is price regulation: the law imposes an obligation to justify a reasonable rate of return on investment and a cost-oriented price cap for the provision of certain services.



One of the key success factors has been the ability to attract significant foreign direct investment into the sector. Table 9 compares FDI growth rates in the Lithuanian economy as a whole and in the telecommunications sector in particular. The data indicate that privatisation deals have considerably influenced total FDI inflows and their growth. By 2002 cumulative FDI in telecommunications accounted for the largest share in total cumulative FDI: nearly 28% compared to 25.6% in manufacturing, 20.4% in wholesale and retail and 26.1% in other sectors.

**Table 9:** *FDI development in the telecommunications sector, 1998–2006*

	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total FDI growth rate (%)	–	59.6	30.7	15.0	16.4	27.0	4.3	14.8	50.8
Share of telecom sector in total FDI (%)	7.6	18.6	19.6	17.9	15.3	12.4	12.3	12.6	13.4
Growth rate of FDI in telecoms (%)	–	292.2	37.4	4.9	–0.2	2.5	3.9	17.5	59.8

*Source:* Lithuanian Department of Statistics, author's calculations.

The Lithuanian government has played an active role in the sector's development. A long-term development strategy was adopted for the telecommunications sector aimed at promoting universal access to basic telecommunications services, fostering competition, creating a favourable environment for investment and protecting consumer rights. According to the strategy the sector's share in GDP is expected to increase substantially (to 17.5% by 2015).

## 2.5 Impact of privatisation on employment and labour relations

Characteristic of transition processes in Lithuanian telecommunications, as well as in other sectors, is the low level of trade union influence. From the start the trade unions were widely viewed as representatives of the Communist system and lacked worker support. The major role in ameliorating the negative social consequences of privatisation and supporting employment, wages, working hours and conditions has been played not by

the labour movement, but by the government and the State Privatisation Agency. On the sale of a company to foreign strategic investors (for example, Lietuvos Telecomas), the acquiring company had to provide a business plan incorporating the resources (including HR) necessary to support its effective implementation. The privatisation agreement included clauses on investment and employment levels for a 2–3 year period subsequent to privatisation, imposing requirements or limitations on employment reductions. However, after the expiry of the agreement the investor was free to change employment policy.

Privatisation has had mixed effects on employment and labour relations in the telecommunications sector. The reduction of employment at the largest company, Lietuvos Telekomas, involved layoffs due to the closure of regional branches. This was coupled with changes in the age structure of employees, as company investments in new technology and the introduction of new services imposed particular requirements in terms of employee skills. Further employment reductions can be attributed to the spin-off of non-core operations. However, post-privatisation reorganisation of telecommunications companies and layoffs did not lead to a reduction in the total number of employees in the sector. In fact, the layoffs coincided with general growth of the economy and of the sector in particular, absorbing many of those made redundant. Privatised and newly established companies, offering a wider range of new services for customers, became attractive employers for young, skilled persons, offering wages comparatively higher than in other sectors.

The end of privatisation in the sector in 2000 marked an increase in trade union activities. As of 2008 as many as 56 trade unions are operating in the 270 companies in the sector: as a rule, separate trade unions are established at individual companies. The membership of the sector's major trade union is 4,330, making it one of the largest in the country.

As the sector is dominated by foreign investors, Western European practices have been introduced for dealing with workers' representatives. Companies controlled by foreign investors have a more positive attitude to the trade unions than those in local hands, viewing them as a channel for bargaining with employees. Huge private investment in the sector includes investment in labour, the increase and upgrading of skills and the introduction of new efficient and innovative labour management practices. The private companies in the sector use innovative employee motivation systems, including the first share option plan for employees. Labour relations in the telecommunications sector have not led to strong resistance or tensions.

## **2.6 Conclusions**

The privatisation and liberalisation of the telecommunications sector in Lithuania, alongside broader technological developments, have led to growth and qualitative improvement in the services provided to customers. Investors created a market for new types of services, offering modern products, at the same time investing in technological development. However, since 2000 investment in network infrastructure has fallen by two thirds (without negative effects on revenues), signalling the end of fundamental restructuring in the sector. Liberalisation of services established competition within the sector, although it is limited due to the high natural entry barriers. The operators have adopted a policy of service differentiation, with less competition on the price dimension. The low number of competitors means that customers have not benefited from discount policies on services. As the sector boomed, total employment within it increased, and attractive job opportunities, mainly for young employees, were offered, including higher wages compared to other sectors. Despite this, there is a need for stronger regulation, primarily in relation to consumer needs.

## **3. Privatisation of the transport sector**

The structure of the Lithuanian transport sector is determined by the country's geographical location, and includes road transport (freight and passenger), railway transport (dominated by the state railway monopoly), water transport (freight and passenger) and air transport (several airline companies, including the former state monopoly). From the start of the transition the diversified and developed transport system suffered greatly due to the collapse of former transportation networks, a lack of resources to maintain transport infrastructure adequately and energy price rises after liberalisation. Initially, total traffic fell to below 50% of pre-independence levels.

### **3.1 Background conditions of transport privatisation**

Policy for the privatisation and liberalisation of the transport sector was based on a number of circumstances. First, the natural monopoly features of transport subsectors were well acknowledged, driving the decision to retain control of key companies. In the transport sector, network effects and economies of scale are particularly important; it needs a developed infrastructure, which imposes high entry barriers. Therefore, the model of the vertically integrated enterprise was viewed as the best form of organisation by privatisation policy makers.

Another set of considerations was related to the specific advantages and disadvantages of each transport subsector. The well developed internal road network had and still has limited external connections. The major seaport, on the other hand, had several advantages in terms of cargo shipment over other ports in the region, as it is ice-free all year round and possesses good and fast motorway and rail connections; however, it required improvements in its infrastructure to remain competitive. Air transport was characterised by an oversupply of airports (three large airports, and a number of smaller ones), and the airlines were dominated by the state monopolist. Public transport services were not sufficient to satisfy public demand, underdeveloped and undergoing continuing deterioration.

The lack of public financial resources led to a deterioration of assets; the high level of investment needed could not be financed by the state. The task of privatisation was, among other things, to bring sufficient investment inflows and to ensure viability. The transport industry was initially viewed as potentially attractive for the private sector. However, due to the perceived strategic importance of the largest monopolistic transport enterprises, their privatisation was postponed, and then often carried out sporadically.

### **3.2 Privatisation modes and extent**

Privatisation of the transport sector was particularly politicised due to the need to reorganise monopolistic enterprises, on the one hand to liberalise the market and introduce competition, and on the other to ensure the provision of public services.

The transport sector has experienced a diverse range of privatisation modes, commencing with voucher privatisation. In many cases staged privatisation was applied, starting with partial privatisation to employees and management. However, state participation has been retained in many cases. Initial privatisation favoured management, maintaining its significant role in many cases.

A number of enterprises were subject to restructuring prior to privatisation. However, the breaking up of large firms before bringing them to market for sale has not been a simple process. Considerable technical expertise was required to identify economies of scale and scope in enterprise organisation, distinguish organisational components, split up monopoly structures, determine efficient integration within enterprises and design plans for effective break up. A large number of enterprises listed for privatisation were not sold at the first attempt, and in the course of several rounds of unsuccessful privatisation the financial position of such companies often

deteriorated, and uncertainty about the future created tension and employee discontent. A lack of transparency created the conditions for corruption and speculation, ultimately causing the hurried sale of enterprises at knockdown prices.

During the second stage of privatisation various other methods were used to bring transport companies to the market, including privatisation to foreign investors, auctions and cash sales. However, the privatisation of most of the largest enterprises in the sector was delayed to the later stages of privatisation, as late as 2000–2005. Each company was dealt with separately, identifying policy issues, carrying out restructuring, seeking to solve employee and management entrenchment problems, valuing the enterprise and choosing the appropriate privatisation technique. The actors involved in the process included ministries, the State Property Fund, the Privatisation Commission, the Tender Evaluation Commission and advisors.

Privatisation in the transport sector ended with only one large strategic foreign investment (DFDS's – from Denmark – purchase of a cargo/ferry line). Most other companies (Lithuanian Shipping Company, Lithuanian Transport Company, Klaipeda Transport Fleet, Lithuanian Airlines, and so on) were sold to domestic companies, which actively formed diversified business conglomerates. These complex processes led to diverse ownership and governance structures.

The case of the Lithuanian Shipping Company, which was the fourth largest in terms of fleet size in the Baltic region and one of the largest employers in the sector back in 1995, serves as a good example of the complexity of the process. Initial privatisation of the company ended with 75% of equity still state-owned, the sale of which was postponed until the introduction of cash privatisation. However, the international tenders launched in 1998 and 2000 coincided with the Russian economic crisis and the world shipping crisis and so were terminated. During this period the company's profitability fell below one tenth of previous levels, enabling foreign bidders to reduce the price from 51.2 to 47.6 million USD and the level of post-privatisation investment from 92 million USD to 76 million USD in the second tender round. In this case, as well as in a number of other cases of privatisation, mainly to strategic investors, domestic businesses were eliminated from participation.

Government efforts to maintain company operations and employment were recognised in the privatisation agreement signed by the State Property Fund. It permitted the new owners to sell, mortgage or lease the fleet only if the investment conditions were met. The government retained the right to approve the sale or transfer of potentially unprofitable shipping lines. Closure

of unprofitable lines was made subject to the conclusions of independent experts, and double vessel registration (including home country registration) rules were to be applied. At the same time, some provisions of the privatisation agreement entailed the risk of significant layoffs. Moreover, the government deleted the clause on the 'golden share', which would have enabled it to prevent the new shareholders from taking risky and unfavourable decisions. This caused minority shareholders (mainly employees) to contest the agreement and terminate privatisation. Since their votes (20.03% of total company shares) alone were not sufficient, minority shareholders formed the LISCO shareholder association and appealed to the courts to stop the transfer of vessels to the offshore companies. It was one of the first cases in Lithuania in which the privatisation agreement was terminated due to the inability of investors to pay for the acquired company in due time. Only in the third round of privatisation was it possible to find a foreign investor and finalise the deal.

This and other cases of privatisation to foreign investors gave rise to criticism of the government's privatisation concept. Opponents argued that it hampers the formation of domestic capital and that profits tend to be repatriated. As a result, the later privatisation of large companies allowed for the participation of domestic investors.

Transport privatisation has been significant mainly in logistics, road transport and port operations. Road construction companies have been privatised and road maintenance was contracted out to the private sector on a competitive bid basis. Air infrastructure has been maintained under public supervision. National carrier Lithuanian Airlines was privatised only in 2005 by sale to a domestic consortium, although its subsidiary airline was privatised earlier. Due to their perceived strategic importance, the government decided to retain key companies such as Lithuanian Railways and the Klaipeda Seaport as semi-public enterprises. Mass restructuring and the modernisation of infrastructure, along with planned technical improvement projects, made it possible to transform these enterprises into profitable ones.

As a result of public transport liberalisation, restrictions on market entry have been removed. Urban transport has attracted a number of private companies, licensed by municipalities to provide public transport services. However, the main urban transport companies (46 bus companies and two trolley-bus lines) are still owned by municipalities. Their privatisation was constrained by several factors. First, the need to replace obsolete vehicles demanded a high level of investment. Second, as service pricing decisions are controlled by the municipalities, privatisation was not considered attractive. On the other hand,

the situation is complex because the Law on Privatisation granted municipalities the right to decide what property to include in their privatisation list. Some municipalities are opposed to the privatisation of assets under their control, especially if these are used for commercial purposes. Finally, because of the unclear division between state and municipal functions and budgets, both the responsibility and the financial burden related to these public entities fall on the state and the taxpayer ([www.llri.lt](http://www.llri.lt)). Major privatisations have taken place in intercity passenger transport, however. Marketisation of transport services in this segment has helped to maintain low prices, while providing consumers with the opportunity to choose higher quality services.

An important factor in the growth of the private transport sector overall is the early (1995–96) privatisation of road freight transport and the emergence of new private companies engaged in international and domestic freight. Due to the rapid expansion of this subsector, the number of road transport companies was 1,942 by the end of 2006, accounting for 67% of all companies in the sector, compared to just 21 company in water transport and 10 in air transport. The conclusion is that road transport has the most potential for liberalisation and marketisation. Private shareholders, driving efficiency improvements, have influenced total sector turnover and value added growth rates, making it one of the most dynamic in the economy.

### **3.3 Financial implications of privatisation and restructuring in the transport sector**

Besides liberalisation, the opening up of the Lithuanian economy, particularly since EU accession, has made the transport sector extremely competitive. The new environment, along with EU regulation, supported by the Lithuanian Transport and Transit Development Strategy, is expected to continue to influence future developments in terms of output, productivity and employment. The strategy entails the development of a multimodal transport system, transport networks and infrastructure, promoting the competitiveness of Lithuanian transport companies.

Privatisation and subsequent reorganisations, along with increased competition, have brought a steady increase in turnover, value added and employment. At the same time, the importance of the sector within the economy has increased, accounting for almost 10% of total value added and expanding rapidly for a number of years in succession. The years following EU membership were extremely successful for the sector. It became the absolute leader in the economy in terms of growth of value added (12.5% at constant prices in 2005). The number of enterprises, personnel costs and the

number of employees have shown relatively similar trends, while turnover has been on the rise, reaching 9.9% of the economy by 2005 (see Table 10). Labour productivity is one of the highest in the economy: in 2005 it increased by another 13.8%, 51.3% above the average for the economy.

**Table 10:** *Share of the transport sector in the economy as a whole, 1997–2005*

	1997	1998	1999	2000	2001	2002	2003	2004	2005
Number of enterprises, as % of total	5.8	6.7	9.0	10.1	10.1	10.4	10.1	9.9	9.5
Number of persons employed, as % of total	11.9	12.3	12.0	12.0	11.9	11.5	11.0	10.8	10.9
Number of employees, as % of total	12.2	12.5	12.2	12.1	12.0	11.6	11.0	10.8	10.9
Turnover, as % of total	8.2	8.6	9.2	9.4	9.1	9.7	9.7	9.5	9.9
Personnel costs, as % of total	13.9	15.3	15.9	14.6	14.5	14.4	13.5	13.0	13.1

Source: Lithuanian Department of Statistics, author's calculations.

Revenue in the transport sector also demonstrated impressive growth – 27.6% in 2005 – and pre-tax profits more than doubled. However, the financial indicators of transport companies differed by subsector. The increasing debt financing trend among privatised companies resulted in higher debt to equity and debt to capital employed ratios by 2006, averaging

**Table 11:** *Financial ratios of transport subsectors, 2006*

Financial ratios	Transport and storage, total	Land transport	Water transport	Air transport
Debt/equity ratio, %	30.4	39.6	19.7	–439.7
Return on equity, %	1.9	2.0	3.3	254.7
Return on assets, %	1.1	1.0	2.4	–10.1

Source: Lithuanian Department of Statistics, author's calculations.



30.4% and 24%, respectively. Air transport and road transport companies have reached even higher borrowing levels. Despite company restructuring, the profitability ratios – in terms of return on equity, as well as return on assets – have remained low, at 1% to 3%.

In contrast to the telecommunications sector, FDI did not have a significant influence at the sectoral level. Higher growth rates in FDI were achieved when a few enterprises from the transport sector were privatised (for example, the acquisition of the Lithuanian Shipping Company by DFDS). By the end of 2005 FDI accounted for just 3% of total foreign investment in the economy.

### **3.4 Impact of privatisation on governance, employment and labour relations**

The share of private sector employment has increased steadily. Only about one third of employees – around 76,000 – were still employed by public sector companies by 2006. Average monthly earnings of sectoral employees were 107% of the national average, experiencing significant annual growth (7% to 10%) for the last few years.

The transport sector is a good example of the development of diverse corporate governance structures subsequent to privatisation, as well as a range of experience in labour relations, which can be traced through specific company cases. The establishment of employee ownership through initial privatisation created the conditions for employee participation and brought with it shareholder activism. This is illustrated by the Lithuanian Shipping Company, one of the largest employers in the sector (over 1,400 employees in 1995). Initial privatisation of the company formed a significant employee equity stake, and 75% of equity was still state-owned. During subsequent privatisation stages, the company was reorganised into two entities, causing the dilution of shares, which hit minority shareholders, including employees. They formed an association and brought the case to court, but the various disputed issues were resolved in a way unsatisfactory to minority shareholders.

Given the employment losses due to early privatisations and the weak bargaining power of the trade unions the state had to act to limit employment reduction as a consequence of privatisation. The privatisation agreements signed by the State Property Fund obliged the buyers of the largest companies – mainly strategic investors – to maintain jobs subsequent to privatisation. Thus, in 2001 the privatisation agreement of Baltic Lisco Services included the requirement to maintain 380 jobs for a year; the total number of jobs to

be maintained and monitored by the Fund reached 3,594 in 43 privatised companies in the course of the year. The privatisation agreement concerning the Lithuanian Transport Fleet included 348 jobs, out of a total of 15,070 under Fund control in 38 privatised companies in 2003 ([www.vtf.lt](http://www.vtf.lt)).

As new, concentrated ownership structures were formed, labour came under threat whenever shareholder value or simply profit maximisation was the reason for restructuring. Focused on cost reduction, they resulted in employee layoffs, as well as changes in the employment structure; for example, more experienced employees on higher wages were substituted by younger, inexperienced ones on lower wages (the case of an airline company).

Solutions to governance problems at the large companies in the sector emerged through institutionalised employee representation. The trade union organisation of labour by transport subsector allowed for more efficient sectoral bargaining. The railway transport trade union (with 3,200 members from 26 trade union branches), the road transport trade union (1,600 members from 29 trade union branches) and the water transport trade union (representing 423 members at one large company) have joined the largest trade union confederation in Lithuania, with more than 77,000 members. The organised labour movement now also has representation in air transport companies. However, total trade union membership remains rather low.

After Lithuania's accession to the EU a number of laws were amended and a new framework for collective agreements was introduced, providing additional bargaining possibilities. According to the law, while concluding collective agreements employees can be represented by a non-union representative, if there is no trade union within the company. Transport sector trade unions are actively participating in collective bargaining, not only at company, but also at sectoral level. Though currently bargaining concerns mainly pay and working conditions (for example, double time for overtime and holidays, payment for enforced breaks, limiting overtime and labour outsourcing at railway and road transport companies), the need for information and consultation has begun to be acknowledged.

Management attitudes towards the labour movement are generally more positive at foreign-owned companies, which have experience of dealing constructively with trade unions in their home countries and advocate the positive aspects of negotiating with employees. The managements of companies privatised by domestic investors tend to be more reserved or even negative. Steps hindering trade union growth may be taken, such as forcing employees to leave the company, company reorganisation and spin-offs.

### **3.5 Conclusions**

The privatisation and liberalisation of transport subsectors have, in general, been accompanied by better company performance, restructuring and comparatively higher wages. The sector has seen employee layoffs subsequent to privatisation, but they have been partly absorbed by newly established small private transport companies. Strong domestic and international competition, coupled with oligopolistic structures, have resulted in wage restraint and limited improvements in working conditions. However, the labour movement, though not strong, is actively shaping collective bargaining.

### **Outcomes and spillovers**

The privatisation and liberalisation of services in Lithuania, along with the creation of the basis for a market economy, has led to strong growth in service provision both for the general public and for business. Despite strong entry barriers within the sector, the opening up of the economy and the rising number of private enterprises increased competition. Significant improvements in the provision and quality of public services were accompanied by cost and price increases. The break up of former state monopolies, privatisation and subsequent company restructuring brought to dominance oligopolistic structures in service subsectors. As a result, customers have seen little improvement in terms of prices.

Privatisation, initially widely supported by both the public and politicians, has brought diverse effects. Having formed the conditions for a market economy, it has also brought significant pressures on labour relations. The employee ownership established within large industrial companies has promoted stakeholder activism, although that has not prevented mass layoffs and worsening labour relations in privatised enterprises. However, employee ownership ultimately proved unsustainable, and by the end of the transition had been largely substituted by concentrated outside ownership. As privatisation itself did not lead to the expected increases in efficiency and higher employment, and did not prevent bankruptcies in a large number of companies, the generally positive political attitude has changed to one of caution or even scepticism. At the same time, the unemployment effects of company layoffs and bankruptcies have been softened by high growth rates and, especially, the rapid development of the service sector.

After the Soviet-era trade unions collapsed, it was a decade before a strong organised labour movement re-emerged in Lithuania. Trade unions, organised mainly on a sectoral basis, have combined into several associations

(for example, the Lithuanian Trade Union Confederation, *Solidarumas* and the Lithuanian Labour Federation). At present representation is mixed: labour can be represented either by trade unions or by non-union representatives, if no union is present. Strong incentives for the development of employee representation emerged as a new framework for collective agreements was introduced after Lithuania's accession to the EU. This also provided possibilities for more efficient collective bargaining. However, the existence of several competing trade union organisations within sectors, coupled with low union membership, mean that union representation is still not an effective channel for social dialogue within domestic companies.

Privatisation and liberalisation have so far influenced only a part of the service sector in Lithuania. Health care and education, the largest subsectors in terms of employment not only within services, but also in the economy as a whole, remain publicly-owned. A series of reforms within health care and education did not bring the expected improvements in service provision and increased efficiency. Low wages combined with low productivity, as well as continuing social problems and conflicts within the economy have led to significant labour frictions. The privatisation of these subsectors is not even being discussed. Postal services, provided by a state-owned post monopoly and a number of private businesses, will be subject to further privatisation and liberalisation. Recent political discussions on the possible privatisation of the state postal company were closely followed by a deterioration in its financial indicators. This gave rise to a negative public reaction that forced the government to defer privatisation. In general, since EU accession market liberalisation policies and directives have had a major impact on the service sector. The direction of privatisation policy remains unchanged, but public scepticism concerning the privatisation of remaining public companies has become more pronounced.

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## **Liberalisation, privatisation and employment conditions – the evidence of public utilities, public transport and home care in the Netherlands**

### **Introduction<sup>1</sup>**

After the introduction of the Internal Market in 1993 and the development of European regulations for the tendering of public services, a number of semi-public services in the Netherlands have been subjected to market principles through liberalisation and/or privatisation. Liberalisation refers to the economic coordination of products and services that was previously determined by the state and is now governed by market prices under the scarcity conditions of demand and supply. In the literature liberalisation is considered one of the most important developments in advanced political economies (Boyer and Drache 1997; Hall and Thelen 2005). Privatisation refers to the transfer of state shares of previously public companies into private ownership, which is often one step in the wider process of market creation. For markets to function properly, free access to the market is necessary for various players, information needs to be transparent and prices must reflect changes in demand and supply (Megginson and Netter 2001).

In the Netherlands, liberalisation and privatisation are the outcome of long political debates in which many minor decisions were taken about small, gradual reforms rather than radical breakthroughs. As Neil Fligstein (1996, 2001) argues in his studies on market creation in the United States, in such a

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process developments at the macro, meso and micro levels of decision-making are strongly connected. In European member states, international and national political decision-making define the rules of the game, including the normative dimension of social order and mutual relations between societal actors, and the establishment of a new judicial apparatus and market authorities for monitoring and market evaluation. At the meso level of particular sectors of industry, the various corporate organisations, sectoral institutions and stakeholders, such as the interest organisations of trade, consumers, employees and the environment, together compose an 'organisational field' in which various patterns of competition and cooperation occur. At the micro level of individual companies, strategies, internal organisation and mutual relations between several departments of the company determine the definition of strategic goals and the use of scarce resources. We shall see that the processes of reform and market creation discussed in this chapter have a decision-making structure in which governments, political parties, public interest organisations and trade unions call for the privileging of national interests and seek to improve efficiency in service provision. At the same time, action is determined within the organisational field at sectoral level, and influenced by the product and labour market strategies of individual companies at micro level.

This chapter discusses the liberalisation and privatisation of public companies in three sectors of economic activity: the electricity market in public utilities, bus transport in public transport and home care in public health care. The extent of market building is not identical in these three sectors (Van der Meer, Schaapman and Aerts 2007). In public utilities, company ownership is still in public hands, though liberalisation in 1998 has led to increasingly internationally integrated markets. Public transport has been fully privatised since 2001, but markets are still highly influenced by government. Home care has experienced various waves of reorganisation in terms of the definition of competition and allocation of public budgets. The sector was involved in the first serious forms of market coordination after the introduction of tendering principles for municipal care provisions in 2007.

The analysis combines a public choice argument about market building and government regulation in case of market failures with a sociological-legal account of the changes in employment conditions in each of the three sectors. The sectoral analysis is illustrated by means of case studies concerning the changes in the internal labour markets of three leading companies that are both subject and object of liberalisation. The general question that we shall attempt to answer is: What are the consequences of liberalisation and privatisation for the determination and level of employment conditions in public utilities, public transport and home care?

The chapter is organised as follows. In Sections 1 and 2, the theoretical debate about market creation is placed in the context of liberalisation in the Netherlands. In Sections 3, 4 and 5 we discuss sectoral development and present the case studies.

## **1. The development of political ideas about liberalisation in the Netherlands**

Dutch politics has always been favourably disposed towards market principles, since the performance of the country's open economy has been highly contingent on developments in Germany and other European countries. Over the last two decades the international rules of market capitalism have gained ground since liberalisation started in 1982. First, two path-breaking reports by the Netherlands Scientific Council for Government Policy challenged the usefulness of Keynesian demand management, which was then still prevalent in the country (WRR 1980, 1981). Subsequently, the newly appointed first Christian-Liberal coalition government under Mr Lubbers (1982–1986) opted for a 'no-nonsense' approach to policy reforms, highlighting the need to retrench public expenditure and to give more space to the market. The Lubbers cabinet launched six 'larger operations', which were directed towards rebalancing the role of the state in the market economy and improving the effectiveness of government intervention. Privatisation was one of the six operations, and was introduced in May 1983 to achieve three major aims (Haffner and Berden 1998):

1. to reduce public expenditure by improving efficiency in the match between demand and supply of services;
2. to improve efficiency in public management by restructuring public enterprises and reducing their size;
3. to strengthen the private sector by introducing competition and providing companies with more opportunities to develop.

After 1986, the main goals of government policy gradually shifted towards attempts to achieve efficiency and to strengthen the private sector, although the scale of the privatisation process remained modest. During the first and second Lubbers governments (1982–89) various public activities were privatised in three phases. These processes were also continued after the inclusion of the Labour Party in the third Lubbers government, in 1989, and later during the first and second Purple coalition governments of the Labour and Liberal parties under Wim Kok (1994–2002). In many cases, companies were sold by public offering or by offering their shares for sale in private markets, but the predominant pattern was that public enterprises attained



corporate form, whereas ownership was initially kept in the hands of the state (Haffner and Berden 1998).

Around 2000, competition and market principles were introduced in a number of product and financial and insurance markets, under the explicit control of the Netherlands Competition Authority (*Nederlandse Mededingsautoriteit*, NMA) that was established in 1998 to monitor compliance with the revised Competition Act of the same year. Perhaps more than elsewhere in continental Europe, brokerage agencies, notary offices, pharmacists, a part of Dutch railways and several public utilities corporations were liberalised. Since then, particular Competition Authorities have been established for financial markets, post and telecommunications and health care. The codes of corporate governance have also been changed for listed companies, in pension funds and in the health sector, demanding both transparency and market-based performance.

Recently the Dutch Minister of Economic Affairs ordered an evaluation of market principles in twelve sectors that had previously been under public control.<sup>2</sup> The research shows a rather diverse picture (Poel et al. 2008). According to all respondents more attention is now paid to efficiency and cost control, as well as to customers as an important stakeholder in the organisation of services, within the framework of which new function areas are being developed, such as marketing and call centres for responding to customer queries. Employment conditions have altered in all twelve sectors; often there are more flexible contracts, but there is no general pattern of change. The most dramatic impact on employment conditions has been in the postal sector, in which new market entrants do not have a collective agreement and have undercut wage levels, so leading to direct competition on labour costs.<sup>3</sup> In the present chapter, we shall deal only with cases in which a sectoral collective agreement applies, covering all companies in the industry.

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<sup>2</sup> The decision to start this research was made by the Minister of Economic Affairs after a parliamentary debate in April 2007 about the study presented in this chapter. The twelve sectors are: energy, railways, nurseries, air traffic, notary offices, public transport, postal services, public employment services, taxis, telecommunications, health care and home care.

<sup>3</sup> In August 2007, TNT Post proposed to freeze wage levels for 30 months, to cut bonuses for working at inconvenient hours, to reduce pension contributions, to abolish travel compensation and to calculate working hours on an annual rather than a daily basis. For a more detailed analysis, see Kok and Felsö (2006).

## **2. Liberalisation, privatisation and their effect on employment conditions**

According to standard economic theory, full competition occurs only when actors have free access to the market, individual companies cannot set prices in the long run, information is freely available without costs and no transaction costs emerge when contracts are signed. Such conditions are hard to find in reality, leading to suboptimal allocation, efficiency and innovation. Imperfect outcomes, for example, are due to the lack of transparent information, natural monopolies, the concentration of economic actors, which form oligopolies and concentrate market power, and unpredictable and diffuse consumer demand. Under such conditions the government can intervene in the market in order to protect consumers and employees by seeking to overcome market failures (Teulings et al. 2003). At the same time, government intervention can result in suboptimal outcomes when competition is hampered and service providers have no incentive to work efficiently.

Next to market failure and government failure, the public administration literature distinguishes another mode of production, 'quasi markets', in which the government introduces elements of competition, but at the same time determines the rules of price-setting. Such 'quasi-markets' prevail in public transport and domiciliary health care (Bartlett and Legrand 1993). According to the Netherlands Scientific Council for Government Policy, state intervention in such markets is justified to satisfy the general interest (WRR 2000).

This chapter relates the provision of public services in markets to the development of employment conditions (pay levels, contract types and working conditions) in particular sectors. This is seldom studied in detail; nor is there a direct causal relationship between these issues. In what follows we will propose an analytical distinction between the effects of liberalisation and privatisation on employment conditions.

First, where privatisation is concerned, we may presume that a change in ownership will not immediately lead to a change in market conditions, in either product markets or labour markets. The changing ownership regime, however, may result in a new form of corporate governance, since the position of the various stakeholders (owners, management, employees and customers) will be redefined as ownership changes. *Ceteris paribus*, one may assume that the direct consequences of privatisation for the definition and level of wages and related employment conditions will take shape via the wage-setting intermediaries that previously belonged to the public sector and

will now reflect the wage leadership of companies in national and international markets. Since we know that income distribution is wider in the private than in the public sector, in which there is strong wage coordination, we assume that income distribution will become more unequal in the market sector.<sup>4</sup>

Second, the causal effect of liberalisation on employment conditions will work out differently. Here we have to consider what form of market will develop, and how management and labour subsequently set wages and labour conditions under the new market conditions. When a product market becomes subject to full competition, wages have to be adapted to the market clearing average. Collective bargaining or HRM principles that set wages above the market-clearing rate will in the short term lead to unemployment. In the long term such an economic rent is not tenable, however, and a further downward revision of wages will be necessary. When companies are operating in an oligopoly or under conditions of clear market concentration, wage rents negotiated above the market equilibrium are still possible. Here too it is necessary to consider – alongside the specific form of competitive relations in the product market – which forms of collective wage setting and HRM policies will prevail in terms of the development of employment conditions in the labour market.

We applied our research question to three sectors of economic activity, in respect of which we studied both the forms of government intervention and the development of internal labour markets in three companies. All industries subject to liberalisation exhibit a combination of market and government failure. The following sections will first discuss the form of market creation, which we studied on the basis of changes in legislation, sectoral documents, trend studies and statistics. Subsequently, we present a case study for each sector. The enterprises in question are well established, leading companies. They all have institutionalised forms of wage setting and cannot be considered pure price-competitors. In each of the companies we studied HRM principles and collective agreements; we also spoke to a number of key informants, including the CEO, as a representative of the board of directors, the HR director, the unions, one or more works council representatives and a delegation of employees.

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<sup>4</sup> See Heijma and Salverda (2006) for a detailed analysis of the differences in wage levels between the market sector and the public sector.

### **3. Public utilities: electricity**

Government intervention in the gas and electricity sector has its roots in the nineteenth century when municipalities granted concessions for the establishment of gas factories and themselves bought gas for street lighting. Soon the municipalities took over the sale of gas, which helped finance public services. There were other reasons for state intervention in this sector. The transmission of gas and electricity in regional networks is expensive and requires scale advantages that can best be achieved by a state monopoly. In addition, negative external effects on environment needed to be overcome. It took more than a century for market creation to become an issue, with the opening of national energy markets in the late twentieth century following the European Summit in Florence in 1996 (see Sabel and Zeitlin 2007). Since then, municipalities have gradually sold off part of their stakes in electricity companies.

In the Netherlands, the electricity market is something of an oligopoly. There are four major companies (Eneco, Essent, Nuon and, on a more limited scale, Delta), and a number of smaller competitors. Ownership of the larger companies is still in the hands of regional and local government; they are not listed on the Amsterdam Stock Exchange, though their market value is reflected in a fictitious internal exchange rate. The 1998 Electricity Act (which was followed in 2002 by the Gas Act) defines the following principles for the production and provision of utilities:

1. Production of gas and electricity is open to all producers.
2. Production requirements are restrictive, however, given environmental considerations.
3. Transmission of gas and electricity is the responsibility of TenneT, a state monopoly.
4. Distribution of gas and electricity used to be integrated with production in a single company, but in April 2007 the government proposed to split them. Companies previously responsible for both the distribution and provision of gas and electricity will now need to separate their distribution networks from the provision of utilities.
5. Providers of gas and electricity are free to access the market and their mutual competition is in principle unlimited.
6. Consumers are free to select their provider, which allows for competition between various providers of gas and electricity.
7. A government authority monitors market competition.

In what follows we will restrict our analysis of public utilities to the electricity market. According to government studies, liberalisation of this

market has resulted in a substantial increase in production efficiency. A cost–benefit analysis prepared by the Netherlands Competition Authorities shows a gain of more than €1 billion for the period 2001–2006 (Haffner and Meulmeester 2005). The most important contribution to the efficiency gain is the decline of real prices by 12%. Also, distribution has become more efficient, though some authors have also pointed to a number of suboptimal outcomes (Van Damme 2005). For electricity consumers, more choice has been offered between various packages of electricity and gas, which enables their clients to fix a stable electricity price for a shorter or longer period of time. Over the last few years, however, prices have gone up, mostly due to the almost continuous increase in oil prices.

Since the introduction of competition in the production market for utilities, employment patterns have changed. However, the direct and indirect employment effects are hard to disentangle given the emerging patterns of in- and outsourcing and restructuring of companies. Clear job trends in the various companies include the loss of jobs for production workers, where scale advantages have been achieved. Also significant is the increase in administrative staff due to the increasing information exchange and contracting with consumers. Another noteworthy development is the increase in higher skilled jobs, for example, in the forecasting of market developments and energy prices.

Available statistics show an overall decrease in employment in the energy sector of 3.3% or 4,000 full-time equivalents (FTE) from 31,000 to 27,000 FTEs in the period 1993–2001. This decline was caused by efficiency gains (45%), scale enlargement (25%) and outsourcing (30%).<sup>5</sup> After 2001, when market liberalisation was introduced, employment levels rose again with 6,000 FTEs, mostly due to the administrative preparations and in front offices for market competition. Currently, one quarter of all employees are working on a temporary contract.

### **Case study: NUON**

We tried to trace internal labour market developments at NUON, one of the four leading electricity companies. Facing liberalisation, the company appears to have prepared itself for competition relatively well. Since its establishment in 1999, the company has undergone a series of mergers and reorganisations, leading to a staff increase from 6,900 in 1999 to 9,600 in 2005. At the start of liberalisation, the company aimed at world-wide

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<sup>5</sup> Source: Boston Consultancy Groups, 2005.

expansion in energy and water management, but soon discovered that its core business was in energy production and supply in the Netherlands and in part of Germany and Belgium. Due to efficiency gains, scale enlargement and outsourcing resulted that led to a number of redundancies. For example in 2000, 963 employees lost their jobs, above all in the traditional segments of the company, namely the distribution and provision of electricity, gas, heat and water, but also in middle management. In the same year, 851 employees entered the company, 462 due to mergers and takeovers, but 389 new jobs were created in trade and marketing, e-business and asset management. The new focus on customers has resulted in an increase in temporary administrative jobs in payments and customer complaints.

Personnel reductions took place in three rounds of reorganisation, which were negotiated in social agreements between the HRM department and the unions. In the first (1999–2003) guarantees of work and income security were the core issues, whereas in the latter two (2004–2005) and (2006–2007) a new HRM policy was implemented. Instead of guarantees of work, wage supplements and early exit for older workers, now competency development, efficiency improvement and competitive behaviour are explicitly mentioned and have become internalised in the HR philosophy. Both in personnel planning and labour conditions, sick leave and commitment, related provisions for optimising skills and performance have been introduced.

In the area of employment conditions, the company has been more restrictive than in the past. Previously the collective agreement was of a ‘golden’ nature, with wages that were substantially higher than the benchmark for comparable jobs in the labour market. Now wage levels have been adapted to the market average for newly entering employees, who earn about 24% less than the previous cohort (source: interview with personnel management). In addition, income differentials in the companies have grown, an issue that led to an open letter from the trade unions questioning the – in their view – excessive compensation of senior executives in 2004.<sup>6</sup> For most staff, internal career

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<sup>6</sup> Above all the CEO’s 42% pay increase, including share options, to some €815,000 for 2004 raised eyebrows, also in Parliament and the Cabinet. The indignation was boosted by the publication of a website of senior executive compensation by the National Association of Shareholders (Vereniging van Effectenbezitters), which argued in its annual report for 2004 that the bonuses of top managers generally are not in accordance with their performance, also in light of the new Code of Corporate Governance (2003) which aimed to reduce the power of management and to increase transparency in business (see, for example, Elsevier, ‘Verontwaardiging over salarissen topmanagers’, 31 March 2005 and Press Bulletin trade union Abvakabo, 25 April 2005).

possibilities have improved and about 15% are now on performance-related contracts. Overall, HR policy concerning employees appears to be productive, since company research shows an increase in employee satisfaction and decreasing illness.

The flipside of the individual treatment and evaluation of employees includes the partial erosion of the social dimension. In the past, less qualified staff could be hired and below average performance was more easily accepted than today. The reorganisations have made the least productive staff redundant. Interview respondents also lamented the pressure on individual performance, which hampers team performance and cooperation. Accordingly, income differences have widened, and social cohesion, work atmosphere and the focus on joint performance are all paid less attention. Management has been called upon to improve these things.

We conclude that this case illustrates a substantial revision of employment patterns in electricity companies with simultaneous processes of job destruction and job creation. Such processes will very likely continue given the further opening of the product market and the coming separation of network and service provision. Employment conditions are affected by these processes, but not to the same degree for all employees. The wage level for newly entering employees has been decreased to the market average and a substantial part of the work force are now on flexible contracts. At the same time, an upgrading of personnel management is noticeable with positive effects for contractual agreements in the case of collective redundancies, as well as for the individual career paths of incumbent workers.

#### **4. Public transport: buses at regional level**

In public transport, government intervention is motivated by equal income distribution. Accessible public transport at a reasonable price is considered necessary for younger people, people without a driving licence, the handicapped and the elderly. In addition, within particular geographical areas public authorities grant companies a local monopoly of service provision.

Until 1998, public transport was organised in regional organisations that were part of the wholly state-owned *Verenigd Streekvervoer Nederland* (VSN – United Netherlands Regional Transport organisation). As a general rule, the government underwrote these organisations financially, giving them no incentive to operate efficiently.

Competition was introduced in the Act on Public Transport (*Wet personenvervoer*, 2000), which came into force in 2001. Competition is not competition ‘in’ the market enabling travellers to choose between various

companies, but competition ‘for’ the market, in the sense of companies being able to win the right to offer public transport in a particular area. From 2001, 19 regional governments organised public tenders to distribute concessions to provide transport in their area. This ended the former state monopoly. The system is not based on full competition, as occurred in the United Kingdom under Mrs Thatcher. In the Netherlands, three larger (Arriva, Connexion and BBA-Veolia) and some regional companies compete for the right to organise transport; this makes them responsible for efficient provision for a fixed number of years. Competition is therefore not full and journey ticket prices are still set by the government. Under the concession all details concerning number of services, timetables, punctuality, financial accountability and quality of service provision are negotiated between the government and the provider. The general idea is that the government controls service provision, and companies try to achieve the best trade-off between price and quality.

In the public transport sector, all the leading companies have become part of an international holding in recent years, which provides them with scale advantages in terms of electronic scheduling of rosters and cost advantages when buying buses and so on. Tender competition remains strong. At the same time, the three main companies cooperate in collective bargaining and the transfer of personnel when, under the Act on Public Transport, a public transport concession is lost in a tender.

### **Case study: BBA-Veolia**

We conducted a case study of a regional transport company in the province of Noord-Brabant (BBA), with 865 employees. Since 2001 the company has been part of a French multinational holding, Veolia. The company has substantially changed its internal organisation over the course of the past seven years. Personnel policy has been decentralised. HR policy is no longer defined at headquarters but by plant managers at the company garages. These managers have become responsible for the entire HR cycle of recruitment and selection, scheduling working hours, development and pay for 60 to 120 employees. The employee representatives have supported this line of decentralisation, and the more direct personnel management has resulted in decreasing sickness leave and improved satisfaction, according to several spokespersons. Although the general motto of the company is ‘it’s all about people’ (*‘het gaat om mensen’*), the ‘too socially engaged’ employer of the past has become leaner and more efficient. Some 250 persons have been made redundant in the reorganisation process, all of whom either took early retirement or found work elsewhere. According to management sources, the company now can stand the heat of competition (also with the help of the



international holding), and failure in tendering (which almost occurred in 2006) would not amount to a 'coup de grâce' for the company.

Not all is going well, however. After the introduction of the new Act on Public Transport in 2001 and until 2006 the provincial authorities in Noord-Brabant made hole and corner arrangements, in the wake of which official tendering was considered necessary in order to achieve retrenchments. BBA-Veolia had already successfully competed for several contracts at the regional level, though according to the management the tender procedures generally appear to be too strict in their time schedule and extremely demanding in terms of their administrative load. When we were conducting our case study, coincidentally, the tendering procedure in 2006 resulted in a court case, which revealed a number of unexpected dimensions of liberalisation. The bidding criteria were based on 100% price competition, in contrast with the previous year when only 85% price criteria were required next to 15% quality criteria. The winner of the bid was the bus company Connexxion that had offered its services for about €800 million, roughly €90 million below BBA-Veolia. Connexxion had underestimated the costs of additional work ('a spelling mistake' according to company sources), however, and had thus calculated far too low a price offer. When it admitted the need to withdraw from the contract, public transport was under immediate threat given the limited time horizons that were applied by the provincial authorities, especially since BBA-Veolia had already arranged to lay off its driving and office staff in accordance with the Act. The judicial dispute that followed, resulting in various employee demonstrations and rumours in the national press, was only solved when BBA-Veolia replaced Connexxion, after the mediation of the trade unions.

The effects of liberalisation on employment conditions are not easily visible from the case study. Primary and secondary employment conditions for core office employees, drivers and maintenance people have remained unchanged, in a transport sector that is growing in volume. The sectoral collective wage agreement was retained to establish wages and working hours. At the same time, the cost of personnel policies is important, and HRM and training policies are being reduced, whereas working schedules are becoming more demanding for drivers. Furthermore, individual employees have made sacrifices with regard to their tertiary employment conditions; all kinds of surpluses and bonuses for irregular work have been limited for newly entering staff. This sacrifice is considered important in a sector in which irregular time shifts are general practice. The change in concessions, moreover, produces uncertainty and stress among permanent staff, which is further heightened by a freeze on days-off, which was required after the halt

in recruitment at the end of the concession contract. Trade unions have also expressed their worries about the early deducting of the value of buses in the annual accounts and the subsequent limited level of vehicle maintenance. They also complain about the minimisation of security for bus drivers; in the past the latter were supported by a mobile brigade of inspectors who could step in, for example, when accidents occurred. Now security is monitored with the help of television cameras. In addition, there is major concern among the trade unions that drivers in local services might be substituted by less qualified staff work for lower wages. The unions also fear regime shopping between various collective agreements, since the company may substitute bus drivers by taxi drivers or smaller buses, which have lower labour costs per hour.<sup>7</sup>

This case thus provides another example of change in personnel management under new market conditions. The combination of internalisation and decentralisation of decision-making at company level has resulted in more direct handling of individual employees, which is considered a positive change by all respondents. The consequences of liberalisation are most visible during tendering procedures, when companies have to make bold calculations, which results in uncertainty among staff. Moreover, personnel costs increasingly matter under competition, which results in work stress and the limitation of individual arrangements.

## **5. Home care services**

Government intervention in the health care sector is legitimised on the basis of redistribution arguments. The health care sector in the Netherlands is broadly dependent upon the state budget, apart from a small (but growing) number of private clinics, particularly in some larger cities. The continuously rising costs of health care – currently 12% of GDP – have made the government aware of the need to control public budgets, and efficient budget

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<sup>7</sup> After this research was concluded, in June 2008 an open labour conflict emerged in public transport that lasted exceptionally long for more than two weeks with negative effect for both companies, employees and travellers. During the conflict, the former president of the Social and Economic Council and current Member of Senate, Klaas de Vries, was invited to write an ‘independent’ analysis of public transport blaming the ‘unpredictable’ National State in stead of employers’ associations and trade unions as prime responsible actor for the lack of transparency and predictability in the sector, where market creation is incomplete (a quasi-market in the terminology of this chapter), and thus costs and benefits are only indirectly visible and investment is hampered. According to the author, both national and regional government need to coordinate their activities and play the role of ‘market superintendent’ (De Vries, 2008).

allocation is currently at the centre of decision-making in all Dutch hospital and health care institutions.<sup>8</sup> This has resulted in a wide public debate about the quality, accessibility, solidarity and cost control of health care services.

After enduring political immobility and the postponement of political decision-making, a new public social insurance system was introduced in 2006. Private health insurance organisations offer standard and additional insurance packages of medical and dental treatment, but are not allowed to refuse anyone. To obtain more control over (unfair) market concentration and to stimulate market allocation a supervisory National Care Authority was introduced in 2006. This Authority monitors the quality and spread of health care supply and is acquiring an increasingly authoritative position in evaluating the effects of liberalisation in the health care sector.

The overall idea in the health care sector is thus to introduce a single market for health insurance associations in which there is competition for customers, and health care institutions have to contend with each other on the basis of price and quality. Within such a 'quasi-market' (Le Grand and Bartlett, 1993), cost consciousness in the organisation of care services should be encouraged. Given the increase in health care demand and the need to cut budgets, hospitals and health care institutions are trying to minimise the duration of patients' stays. This implies that home care will gradually become more important.<sup>9</sup>

In home care, the major effect of competition was felt in 2007 when the Exceptional Medical Expenses Act was changed and a new Act for Societal Support (*Wet Maatschappelijke Ondersteuning*) was introduced, which had a direct effect on the composition of employment in home care services. Home care is a particular part of the health care industry that originates from private initiatives in the late nineteenth century that aimed at improving living conditions and controlling infectious diseases. From the 1970s, the government supported scale-enlargement for the sake of efficiency gains and over time the number of home care organisations declined from 500 in 1980, to 200 in 1987 and 100 in 1990. Each held a monopoly in its own geographical area.

From the early 1990s, private companies entered this market to provide health services to clients that have left hospital, but are still dependent upon daily health care. Since 1994, all home care activities have been paid for

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<sup>8</sup> See my chapter in *Low wage work in the Netherlands* (Salverda et al. 2008).

<sup>9</sup> The effects of other market incentives in health care, such as the new health insurance regime or the introduction of the diagnosis treatment combination, are not dealt with here.

under the Exceptional Medical Expenses Act. In 1995, a personal budget was introduced that allows customers to select between various health care organisations competing for clients.

Since 2007, home care services have been financed under the Exceptional Medical Expenses Act (AWBZ) and partly under the Societal Support Act (*Wet Maatschappelijke Ondersteuning*, WMO), introduced in the same year. The Societal Support Act aims at full participation of citizens in society. According to the Law, municipalities rather than the health insurance associations have become the ‘principals’ in the allocation of household work for ill people living at home. Municipalities are now responsible for delivering services for persons who are ill or handicapped to allow them to participate fully in society (the so-called ‘compensation obligation’). The municipality needs to draft a policy of service provision. The policy for household services is subject to tendering procedures according to European law, implying that companies can bid for a part of the market for household services for ill or handicapped persons.

Three quarters of all municipalities distinguish simple cleaning (HH1, household service 1) from cleaning that also involves organisation of the household (HH2, household service 2). The difference between the two services is determined by the extent to which the client is physically able to coordinate his or her own housekeeping. In the remaining quarter of municipalities a household service 3 is distinguished, referring to disordered households in a neglected and dirty state. The three task profiles vary in content and thus in job evaluation and wage levels.

Cost reductions can be achieved in various ways. One issue is the definition of the clients’ need for home care. According to various reports no substantial erosion has occurred here, thus clients’ needs are evaluated as before. A related issue involves the applied protocols for the definition of clients’ needs. Some municipalities now allow telephone interviews instead of home visits, which are of course cheaper but also raise the political question of whether the basic needs of clients can be determined over the telephone.<sup>10</sup>

A second dimension of service provision involves the quality home care organisations provide when delivering their services. In 2006, 30% of services involved HH1 versus 70% for HH2. In 2007, the figures were reversed: 85% was now provided under HH1 and only 15% under HH2. The conclusion is that in the past services were provided at a higher level than was strictly necessary given the customers’ needs. As a result of this

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<sup>10</sup> Letter to Parliament, DMO/WMO-2793797, 26 September 2007, p. 10.

change, domiciliary health care organisations have substituted part of their qualified nursing staff with unqualified housekeeping employees. Due to the tendering procedures, more variation resulted between the lowest and highest rates: €14.00–€18.50 for HH1, and €20.00–€24.50 for HH2. Average unit labour costs declined in 2007 in comparison to 2006, when they stood at €15.20 for HH1 and €24.30 for HH2 (Research for Beleid 2007: 51–52).

Another part of this story is that qualified staff are partly being replaced by self-employed persons working on their own account (so-called *alfahulpen*). These persons are not covered by the collective agreement and related pension and social benefits rights in case of illness or unemployment (Groot et al., 20003). The number of self-employed has substantially increased and now stands at 50,000 persons, equivalent to 8,000 full-time employees (NRC Handelsblad, 16 February 2008).

As a result, municipalities' costs have fallen by €200 million. The left's political response to these results was that the budget 'of course' had to be spent on health care, though liberal parties and the national organisations for municipalities claimed that more efficiency gains were still possible. In a similar vein, the National Care Authority has argued that the benefits of liberalisation have not been sufficiently felt in consumers' pockets (NZA, 2007). An associated political question concerns whether wage levels in the past were too high, or are now too low. A related organisational debate asks whether the tasks and obligations of home care employees are too diversified (do they only need to do the housekeeping, or can they also spend some time talking to the client and taking care of their particular needs?). Alternatively, can home care staff perform a broad range of tasks and responsibilities allowing them to function flexibly and to respond to various needs and conditions, so enabling them to attain higher positions on the health care occupational ladder?

These are not just rhetorical questions, but affect how the 'high road' of quality production and value added service provision can be attained. The recently appointed Secretary of State, Jet Bussemaker (Labour Party), has created a €20 million budget for a one-time investment in further and job-mobility training for redundant staff. She has also argued that the 'socially conscious' tendering procedures need improvement; for example, wage levels below productivity are not sustainable and in tendering procedures minimal quality provisions need to be included.<sup>11</sup>

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<sup>11</sup> Letter to Parliament, DMO/WMO-279397, 26 September 2007, p. 14.

### **Case study: Amsterdam Thuiszorg (Amsterdam Home Care)**

The company we studied in Amsterdam has undergone various processes of internal reorganisation to reduce overheads and focus more on efficiency in a growing market. In 2006, the organisation had 4,000 employees and had a market share of about 80% in the larger Amsterdam metropolitan area.

From 2000 to 2003 the company changed from a supply-driven into a demand-driven organisation leading to a decentralisation of decision-making. In line with the law, in 2005 functional cost-accounting (*functionele bekostiging*) of customers was introduced, making an exact price calculation for each task undertaken, which resulted in an increasing administrative load for monitoring productivity within various time schedules. In 2004–2006 a number of business units were established in anticipation of the coming liberalisation. According to our respondents, the increasing responsibility of individual employees due to decentralisation resulted in increasing uncertainty and stress at work. In 2006 a recentralisation of personnel management took place. According to management respondents, the new HR motto ‘Performance and accountability’ (*resultaatgerichtheid en aanspreekbaarheid*) implies greater attention to binding employees to the goals of the organisation than in the past. Moreover, internal flexibilisation of labour in home care is shaped via part-time work contracts, variable working hours and differentiated opening hours, which are also in the interest of employees, many of whom have stated that they prefer part-time jobs.

Nevertheless, personnel policy at Amsterdam Thuiszorg is less well developed in comparison with the two other cases in this chapter, whereas employees in home care perhaps need more organisational support given their relatively low qualifications, the rise of flexible contracting and the large share of the work force with part-time jobs. The nature of work at clients’ houses also contributes to the loose nature of the employment relationship. In addition, the continuous reorganisations result in fear and uncertainty among the staff. The recent recentralisation of HR policy in Amsterdam implies that employees have less say about working hours and that earlier employee achievements, such as the prohibition of ‘broken schedules’ (that is, working for two separate periods during one day), are being discussed again. In contrast to the other companies examined in this chapter, no annual cycles of evaluation and remuneration occur, which is important if employees are to be treated fairly in terms of their career development. Recently, however, Amsterdam Thuiszorg improved its approach to recruitment and selection, among other things via the provision of language courses for ethnic employees. Such investments are considered necessary given the increased staff turnover. Committing people to the aims

of the organisation is also deemed necessary given the expected growth of home care services and the expected scarcity of qualified staff. Training possibilities have become more limited, however, and since the abolition of the sectoral training fund in 2004, further training for the purpose of enabling workers to improve their qualifications is no longer permitted.<sup>12</sup> Finally, the need to reduce absenteeism due to sickness is central in strategic policy-making, since the budget model of ‘functional cost-accounting’ (*functionele bekostiging*) compensates only directly productive working hours in the client’s home. Subsequently, indirect working hours and organisational costs due to absence have to be paid by the company.

The combination of various waves of reorganisation in the home care market, increased competition and constant internal restructuring has not been without consequences. In autumn 2007, the company incurred substantial financial losses and became ‘technically’ bankrupt, to the indignation of the staff. Now, the top management has been replaced and the organisation will need to merge with a strategic partner in order to survive. The National Care Authority is monitoring this process and has warned potential allies concerning unacceptable market concentration. Accordingly, in the press alternative scenarios have been presented in which Amsterdam Thuiszorg will be split up in order to join a strategic partner.<sup>13</sup> Ironically, despite competition and liberalisation, a leading home care company cannot go bankrupt and easily disappear from the market since health care services are in urgent need.

## **Conclusions: permanent reorganisation and employment conditions**

Liberalisation and privatisation of public enterprises in the Netherlands is a political process that was put on the national agenda in the early 1980s under the promise of efficiency gains and labour market improvement. These developments were criticised by the trade union movement and the left-wing opposition in parliament, although they were unable to block many decisions (Soeterbeek and Walraven 1985). After the Labour Party came to power in 1989, the public debate about privatisation and liberalisation evolved into a rather pragmatic and technocratic process in which the rules of the game,

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<sup>12</sup> The Ministry of Health Care contributed an annual €160 million to this education fund. Unfortunately the unions were unable to mobilise their members to successfully block this example of public retrenchment.

<sup>13</sup> See: ‘Fusies van zorgconcern op nieuwe markt zijn vuurproef voor politiek Den Haag’, NRC Handelsblad, 21 February 2008.

property rights and market control were redefined stepwise, often with the help of reports by consultancy organisations portraying the potential public benefits and employment effects of market creation.

The relationship between liberalisation, privatisation and employment conditions has hardly been studied and appears to be an indirect one. This relationship is the result of the interaction of developments at various levels: (changes in) European regulations; (changes in) national regulations; characteristics of the sector (type of competition, type of 'market', sectoral collective agreements); enterprise policies (possibly at the level of multinational headquarters); and establishment policies and interactions between companies and (organised) employees.

Employment conditions in (former) public companies that were subjected to liberalisation and/or privatisation have changed in the wake of these processes. There are a number of general trends but also many particularities at the micro level. In Scheme 1 below we enumerate the various dimensions of change in the product market in the three sectors, including the structure of production, the nature of consumer demand, the form of price-setting, the duration of contracts, the ownership of companies and the justification for state intervention. In the bottom four rows, we summarise the most important developments in the labour market by distinguishing the changes in the occupational profile, HRM, industrial relations and employment conditions.

In response to our hypotheses, we can indeed conclude, first, that privatisation leads to new ownership patterns and corporate governance regimes. The ownership dimension is important for understanding what values matter in the management of such corporations. The debate in the electricity company about the pay of top managers illustrates that in oligopolistic markets upward pay increases for senior executives and thus rising income differences between the top and the lower levels of the company are likely to occur.

Second, liberalisation in product markets does not automatically lead to full competition in the labour market, though labour costs do matter strongly in public tendering procedures. Next to competition, collective bargaining and (upgrading of) HRM policies matter for the position and development of the staff involved. All the companies under study have negotiated social plans to arrange the outflow of redundant parts of the workforce. These developments need not be the consequence of liberalisation and market creation. Collective agreements and job grading systems support the objective definition of work and pay. Collective bargaining thus functions as a buffer between product market dynamics and competition for jobs in the labour market.



**Scheme 1:** *The impact of liberalisation and privatisation on product markets and labour markets*

	Electricity sector	Public transport	Home care
<i>Product market</i>			
Market structure	Concentration in four companies; also some price-fighters	Concentration in three companies	Increasing concentration in larger home care organisations; alongside deconcentration in the market
Consumer demand	Well articulated	Drafted by provincial government	Drafted by either the intermediate health care associations (for nursing and caring in health care); or by municipalities (for household services)
Price-setting	Free in production and delivery; regulated in transport	By government	By intermediate associations
Duration of concessions	Based upon consumer choice	For example, six to eight years, depending on tendering procedures	For household services, depending upon duration of contract defined by municipal authorities
Ownership	Ownership with regional government, trend is towards privatisation	All three companies have become part of multinational companies	Ownership with health care foundations
Reasons for government intervention	Partly negative external effects (environment and security); partly natural monopoly	Redistribution	Redistribution

<i>(cont.)</i>	Electricity sector	Public transport	Home care
<i>Labour market</i>			
Occupational structure	Job creation and destruction	Stability and growth in number of jobs	Substitution in provision of household services
Internal organisation and HRM	Reorganisations and upgrading of HRM	Decentralisation of decision-making to garages; more direct form of HRM management	Demand-driven work organisation; recentralisation of decision-making; introduction of business units structure; attempt to professionalise HRM
Industrial relations	Cooperatively negotiating collective agreements for redundancies; pragmatic attitude in collective bargaining	Cooperatively negotiating collective agreements for redundancies; unions fear regime shopping; wage conflicts in collective bargaining	Scepticism about further reorganisations; pragmatic attitude in collective bargaining
Employment conditions	Flexibilisation of contract types, introduction of performance-related compensation	Limitation of tertiary employment conditions; work stress among drivers	Further flexibilisation of working hours; uncertainty among employees

The analytical distinction between a macro, meso and micro level of analysis in this chapter has proved useful for obtaining a better understanding of market development and competition. At *macro* level, the Internal Market has so far been the driver of market creation at the national level (see also Adnett and Hardy, 2005), though liberalisation is incomplete and many failures have emerged, whereas in some sectors quasi-markets have occurred so that the full consequences of market creation cannot be established. Still, tax payers have benefited from the introduction of market means, although the extent varies from sector to sector and the quantitative estimates of the Competition Authorities need further elaboration. It will be necessary in future research to consider whether and how the economic rent that management and labour in the public sector have hitherto divided among themselves has been returned to tax payers.

Furthermore, national governments are shaping the degree of marketisation, as becomes clear from the sectoral studies at the *meso* level. Here, particular forms of market concentration have emerged in each of the cases under analysis. In both utilities (with four major players) and public transport (three major players) a clear oligopoly has emerged. These companies also show clear elements of international takeovers and partnership. In health care a debate is now starting about the likelihood of unwanted market concentration due to mergers and takeovers between larger organisations. The tendering procedures for buses and home care appear to be administratively complex and costly. In public transport court cases resulted, whereas in home care there have been deliberations about the need to stop the downward spiral in the quality of service provision.

At the *micro* level, the employment conditions are mediated by a series of other factors. As our case studies make clear the previously public companies are today engaged in almost constant reorganisation. All the companies under study show a pattern of restructuring, the introduction of new business units and changing internal labour markets in which new jobs have been created and old jobs have been lost. All three companies have redefined their HRM principles. In the public utilities company a professionalisation of HRM occurred, whereas in the transport company a decentralisation of decision-making resulted. Amsterdam Thuiszorg aimed to recentralise HRM management but the attempt came too late and the organisation was declared technically bankrupt. In all cases in this chapter, the variety of employment contracts has widened, more flexible employment contracting has developed and the definition of daily working hours has been enlarged. In the case of home care, significant job substitution has taken place and services to patients have been watered down, from household level HH2 to level HH1.

There can be no surprise that continuous company reorganisations have led to a public debate about the need to stabilise employment relations and to improve the quality of service provision. After substantial market failures, adverted to in this and other recent evaluation studies, Minister of Economic Affairs Van der Hoeven recently argued that ‘such critical incidents provide a clear signal that reorganisations of the market go together with associated pitfalls’ (NRC Handelsblad, 19 February 2008). In my opinion, there is no need to cease application of the general principle of liberalisation in the sectors under analysis, though the definition of minimal quality in service provision is urgent, and above all in transport and health care more careful experiments and evaluations are necessary for further market creation.

The debate on liberalisation will also benefit from an argument that Wolfgang Streeck (1997) introduced when referring to the importance of the ‘beneficial constraints’ of market regulation, which is here applied to public services. Streeck argued that legal and regulatory conditions could encourage businesses to voluntarily strive for superior social and economic performance, as in the case of German ‘diversified quality production’ and the Japanese high volume quality electronics industry. The application of this idea here is that when the contours of pro-active company behaviour are laid down in general regulations or public laws, the conditions for competition are set *ex ante*, and companies have an incentive to develop pro-active behaviour regarding employment policies. This gives them an opportunity to develop a high quality production and HRM policy, and to compete on value added instead of on costs. In a similar vein, it can be argued that in case of liberalisation, within the framework of European tender procedures, components of a pro-active personnel policy can be laid down. Legal issues such as personnel transfer during periods of change in concessions in public transport, the importance of safety measures in public transport and the need for qualified staff in home care can influence the development of personnel policy. Such considerations are now part of the debate on home care services, in which the Secretary of State has defined the need for permanent employment contracts and the mutual investment of employers and employees in labour contracts. An alternative approach is that the government sets thresholds and ceilings to price levels in order to compel companies to compete on quality. In domiciliary health care, for example, a price rating model has been introduced in terms of fixed prices per hour, which compels the organisations involved to upwardly adjust the quality of their services.

Finally, the debate on liberalisation leads to a new role for trade unions. The unions have not necessarily lost ground due to the liberalisation process, a fear expressed by the trade union FNV (2007). In my view, the debates trade unions are engaged in are changing. The unions still play an important role in all the companies studied and negotiate concerning the collective agreement and social funds during periods of company restructuring. On this basis they can contribute to the development of a pro-active HRM management policy and promote the mutual investment of employers and employees in the employment relationship. As also underlined by Lucio Baccaro (2003), trade unions need to explain the new economic realities to their rank and file. This is by no means an easy task, but one that has become inevitable.

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## **Liberalisation and privatisation of public services and the impact on employment, working conditions and labour relations**

### **Introduction**

This chapter describes changes of employment, working conditions and labour relations in public services.<sup>1</sup> We argue that liberalisation and privatisation have profoundly altered the public sector employment regime.<sup>2</sup> The result is not only a substantial deterioration of public sector work and employment conditions but also a recommodification of labour that in the long run may have negative repercussions for private sector employees. We begin with a description of what constitutes the traditional public sector employment regime of the post-war period. In Section 2 we briefly summarise the liberalisation and privatisation of public services in Europe before discussing in more detail the impact of these processes on employment and working conditions, focussing on the impact on the level of employment, wages, working hours and working and employment conditions. The chapter continues with a reflection on the impact on trade union organisation and a brief summary, including a discussion on the wider impact of the dismantling of the public employment regime.

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<sup>1</sup> By public services we mean services such as energy, post and telecommunications, public transport and utilities. Of course, after 1945 in many countries the public sector also included nationalised industries with a different privatisation history that cannot be covered in this chapter.

<sup>2</sup> Liberalisation refers to the replacement of former monopolies by markets with multiple competing suppliers. Privatisation, in contrast, means the transfer of assets from the state to private holders.



## **1. The public sector employment regime**

There are important differences between the various sectors and activities that are commonly subsumed under public services. In addition, national traditions of public administration and industrial relations systems have a strong impact on the regulation of public sector work in different countries (Bach 1999; Clifton et al. 2003). But there are a number of characteristics that tended to emerge in public service sectors in all (Western) European societies in the post-war period and that subsequently formed the essence of what we understand as the public employment regime (Atzmüller and Hermann 2004a). In a situation of full employment some of these characteristics could be gradually extended to private sector work, although the public–private divide was never fully overcome (Corby and White 1999: 15). Such characteristics include the long-term nature of the public sector employment relationship and the subsequent extraordinary degree of employment stability. Many public sector workers traditionally had civil servant status or the equivalent in the sense that they could be dismissed only in exceptional circumstances (*ibid.*; Bordogna 2007: 15). In some cases job protection went as far as requiring management to gain consent from the respective employee and/or work council representative to reassign workers to new posts within the same service organisation or company. The high degree of job protection, together with a strongly seniority based wage scale (low starting salaries but high final wages and pensions) led to low labour turnover rates and consequently to an extraordinarily high level of identification of public sector workers with their employing organisations. As management relied primarily on internal labour markets when filling new posts in the organisation the result was the development of life-long public sector employment careers.<sup>3</sup> But the high level of job security resulted not only in comparatively low rates of personnel turnover, but also persuaded workers to take up public sector jobs, even if public sector wages could hardly keep up with those in the private sector at the height of the post-war expansion.

Another key feature of the public sector employment regime was the virtual absence of individual wage agreements. Wages were negotiated exclusively on a collective level and laid down in detailed wage schemes. Assignment to particular wage groups was based on ‘objective’ criteria such as formal education and seniority rather than individual performance and experience or, for that matter, the ability to make an impression on future employers in job

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<sup>3</sup> Railway workers or postmen remained railway workers or postmen for their entire professional lives and sometimes even as pensioners.

interviews (Keller 1993: 102–104). In this system there was hardly any room to hire specialists with specific skills who demanded particularly high wages. Instead, such skills had to be developed within the organisation. With few exceptions, this was also true for management, which consequently earned significantly less than their private sector counterparts. Performance criteria or performance-based supplements played no or only a marginal role in public sector wage relations. Instead, wages were attached to workplaces and supplements derived from the performance of specific tasks and seniority, sometimes resulting in rather complex sets of rules and regulations, difficult to understand for managers and legal experts outside the public sector.<sup>4</sup> Due to the absence of individual wage agreements and performance-based supplements, wage inequality – that is, the difference between the highest and the lowest salary groups – was much less pronounced than in private companies (see Ghinetti and Lucifera in this volume).

The higher degree of income equality was also the result of the relative stability of working hours. In the post-war period the 40-hour week became an almost universal working time standard. But private businesses frequently required their employees to put in overtime hours to cope with growing demand during the post-war expansion. Although there were a number of professions and jobs in the public sector that had particularly long working hours and were exempted from regular working time regulations (for example, emergency services), public employers preferred to take on additional staff rather than rely on overtime. In several countries they continued to do so during recessions in order to compensate for cyclical job losses in the private sector. In countries with a strong tradition of apprenticeship training, such as Austria and Germany, the public sector not only hired additional workers, but also trained more apprentices than needed to meet a particular organisation or company's own requirements (sometimes also because public sector organisations could not afford to pay the wages private sector companies offered skilled workers). As a result, the public sector, including public services, fulfilled a number of important macroeconomic functions that helped to achieve and maintain full employment during the post-war decades. The growing proportion of public employment in total employment, furthermore, helped to increase the pressure on private employers to improve employment and working conditions.

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<sup>4</sup> In German sometimes called *Nebengebührenordnung*.

In times of labour scarcity some countries even departed from the 40-hour standard and created part-time jobs in public services in order to give women the possibility to combine domestic work and care obligations with paid employment. This was a deliberate strategy in, for example, Sweden where labour markets became increasingly tight in the 1960s.<sup>5</sup> But as these part-time hours were relatively stable, in the sense that they did not fluctuate from week to week, and the jobs paid comparatively decent wages they can hardly be compared with the marginal part-time positions that we increasingly see today. The high degree of wage equality and the standardisation of working hours were later attacked as public sector rigidity, preventing the efficient deployment of labour resources. But the lack of wage inequality and the limited flexibility of working hours were responsible for the relative uniformity attained by public sector employment relations and therefore essential components of the public sector employment regime (Atzmüller and Hermann 2004a).

The absence of performance criteria also had an important effect on working conditions. Working conditions were seen as an essential part of a complex set of formal and informal rules that governed the provision of public services. These rules, which typically led to an extensive codification of public sector work and employment relations, were meant to make sure that economic pressure did not compromise the quality and security of services. At the same time, they gave the public sector employment regime an explicitly political character (Atzmüller and Hermann 2004b). Public sector workers were subsequently less motivated by expected wage increases than by the public sector ethos, including a high degree of identification with the employing organisation, loyalty, accountability, a sense of community and a sense of justice (Whitfield 2001: 111).<sup>6</sup> But public sector workers were able to gain additional benefits and, in certain countries and areas, they even managed to negotiate shorter working hours and earlier retirement ages, making the public sector highly attractive as a source of decent jobs for low and medium qualified workers, including women and, in some countries, migrants.

The public employment regime was decisively shaped by the public sector industrial relations system (Brandt and Schulten 2007). In fact, the attractiveness of public sector jobs was first and foremost the result of the

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<sup>5</sup> The Nordic countries, as a result, still have a high proportion of female employees in public services: according to Bordogna (2007: 11) at least seven out of ten public employees are women.

<sup>6</sup> But there were of course also plenty of public sector workers who clearly lacked motivation.

strength of the public sector trade unions, translating into a high degree of centralisation of labour relations, comprehensive collective bargaining structures, strong works councils and a high rate of union membership. Although many public sector unions lacked formal bargaining rights (Bordogna 2007: 24ff), their organisational strength and the threat of public sector strikes made sure that public employers sat down at the negotiating table. Public sector unions were, not accidentally, among the most powerful unions in Europe, and although they have lost power as a result of liberalisation and privatisation they are often still stronger than their private sector counterparts. The high level of trade union organisation, in turn, gave public sector employees a strong influence over decision-making concerning the standards and norms that govern public sector employment, even if standards were set by statutory regulations rather than collective agreements. In some countries and sectors they also enjoyed additional codetermination rights that went beyond those granted in private sector enterprises.

While the strength of the unions was certainly essential in shaping the public sector employment regime, the absence of markets and competition was similarly important. It meant that the organisation of public services and, with it, the structure of work and employment relations were not subordinated to the overall objective of profit maximisation, with the important effect that the reduction of labour costs was not a priority. Instead, other objectives, such as equal access to and quality of services but also macroeconomic goals such as the maintenance of full employment, were more important. In turn, the specific quality of public sector employment relations and the nature of the public sector employment regime contributed decisively to the relative decommodification of paid labour in what is retrospectively called the Fordist period of capitalist development (Atzmüller and Hermann 2004a: 34). On the other hand, the absence of competition and cost-effective regulation meant that there were few incentives to limit production costs. In addition, the expansion of hierarchical-bureaucratic structures put further pressure on costs and frustrated workers as well as consumers.

The lack of flexibility, democratic accountability and mounting costs paved the way for liberalisation and privatisation. Liberalisation and privatisation were widely advocated as measures to increase efficiency and service quality. In reality, however, the main focus of restructuring has been on cutting costs and, in labour-intensive services, on cutting labour costs (Brandt and Schulten 2007). The reduction of labour costs demanded a radical reorganisation of public sector work and employment relations, including a reduction in the number of public sector employees, as well as a far-reaching

flexibilisation and individualisation of employment and working conditions. As a result, privatisation and liberalisation have profoundly altered the traditional public employment regime. Not surprisingly, trade unions and works council representatives in many countries and sectors have fought liberalisation and privatisation vigorously.

In Section 2 we will briefly summarise the European politics of liberalisation and privatisation before describing the changes in the employment system.

## **2. The politics of liberalisation and privatisation**

In contrast to the United States, most European countries created large public sectors in the post-war years. The public sector included nationalised industries, banks and public services. Public ownership gave governments the possibility to intervene actively in the economy. Even in Britain, some 20% of GDP was produced by the public sector in 1975 (Leys 2001: 39; Florio 2004). In the period of Keynesian macroeconomic governance, state intervention was seen as a benign instrument to correct market failure. Market failure was expected in those areas in which large investments presented a considerable barrier for new market entrants. A classic example is network industries, which were considered natural monopolies and therefore nationalised after the Second World War. But even in those countries where the networks were operated by private providers, they were subject to a comprehensive set of regulations, starting with the control of investments and ending with the establishment of mandatory price structures (Hermann and Verhoest 2007). Some essential services, moreover, were considered to be too important for the functioning of the economy or national security to be left to the freeplay of market forces. More generally, public services were seen as an important instrument to improve social and geographical cohesion. The state-owned monopoly providers were obliged to offer equal access and service quality throughout the national territory.

Attitudes towards public ownership shifted in the emerging crises of the post-war settlement in the 1970s. In Europe Margaret Thatcher's Britain paved the way in the early 1980s; the Tory government privatised not only state-owned industries, but also public services, such as British Telecom and various transport and energy providers (Florio 2004). Other European countries followed the British example and started to disinvest in nationalised industries and banks in order to raise money to pay back debt that had increased considerably as a result of the 1970s economic crisis (Parker 1999). Outside Britain, however, public services mostly remained unaffected until the early 1990s when liberalisation and privatisation were gradually extended

to public services across Europe. Here the motive was not so much the reduction of the budget deficit – although this certainly played a role – as the belief that markets and competition would improve efficiency and the quality of services, even if the British experience had plainly shown negative or at best mixed results.

The European Union has played a major role in promoting the liberalisation of public services in its member states (Hall 2002; Hermann 2007). In a series of directives, the Council required member states to introduce legal measures that established a gradual opening up of public service markets. As a first step, the respective enterprises were transformed from public enterprises into private companies. In some cases, they were split up into a number of companies, but more often they were forced to create formally independent subsidiaries for their vertically distinct fields of activity. The reason was to make sure that competing firms could access intermediate services such as the transmission and distribution of energy without being discriminated against by the former monopoly providers. Regulation, consequently, was limited to certain aspects of the supply chain while more and more aspects of service provision were left to the free play of market forces. Only in a few sectors, including telecommunications and postal services, did governments require at least one provider to fulfil a universal service obligation (Hermann and Verhoest 2007).

The first sector that was liberalised in this manner was telecommunications. The telecommunications directive was adopted in 1990, followed by further directives on railways (1991), electricity (1996), postal services (1997) and gas (1998). Since then, most directives have been amended in order to guarantee full market access for private competitors. While the telecommunications, electricity and gas markets are almost fully liberalised, the remaining reserved area in postal services is expected to be opened up in 2009 or 2012. In other sectors, such as local public transport, health care and social services, there is no clear-cut European liberalisation policy, but the European Commission and the European Court of Justice have exerted considerable pressure on member states by banning state subsidies, imposing public procurement rules and promoting cross-border service provision. Consequently, in these sectors privatisation and liberalisation often take the form of economisation, including competitive tendering, outsourcing, public–private partnerships and, in the case of the UK, private finance initiatives.

The European directives did not require member states to privatise the former monopoly providers. But in many cases liberalisation was linked to

privatisation as governments took the opportunity to sell entire companies, or portions of the shares, to private investors. In fact, liberalisation in the European Union was more successful in changing ownership structures than in enhancing competition (Hermann and Verhoest 2007). While many companies were successfully privatised, competition has often been distorted by mergers and acquisitions with the result that the number of providers has actually decreased as former local or regional monopolies have been replaced by national oligopolies (*ibid.*). On the other hand, some of them have become active outside their national boundaries and thereby transformed themselves from national monopoly providers to European, if not global, players. But a dominant economic position did not prevent these companies from restructuring work and employment relations in the same way as those exposed to strong competition. What is more, many of the changes described in Section 3 were introduced before liberalisation and privatisation in order to turn them into profitable organisations and/or prepare them for sale to private investors.

### **3. Effects on employment, working conditions and labour relations**

In this section we will present the main results of our research on *the impact of liberalisation and privatisation on employment, working conditions and labour relations* (Hermann and Atzmüller 2005). We will focus on five main areas of change:

1. level of employment;
2. wages;
3. working hours;
4. working conditions;
5. labour relations.

The following sectors were included in the research: railways, public transport, post, electricity, natural gas and water utilities. The study contains empirical analyses (data collection, interviews, analyses of company reports and other documents) on the development of public services in Austria, as well as an evaluation and systemisation of existing studies, reports and additional information (from national experts, trade union representatives, and so on ) from Germany, the UK and Sweden. Occasionally the results of some newer studies have been added. Because of the limited scope of the survey, a lack of systematic research and limited availability of data, however, the results are not necessarily representative or give a full picture of the process of change. We are, however, convinced that the main trends that

we have identified can also be found in other sectors and countries that are not included in the survey.

### **3.1 Level of employment**

While the expansion of employment in the public sector was an important element in achieving and maintaining full employment during the post-war decades, liberalisation and privatisation in many sectors and countries have led to a reduction of the level of employment (see Table 1 for an overview of a number of recent studies on this employment effect). The shrinking proportion of public employment in total employment not only limited the access of low and medium qualified workers to decent jobs, but also weakened the pressure exerted by the public employment regime on private sector employment and working conditions. The reduction of employment took place against the prediction of the European Commission, which assumed the creation of nearly one million new jobs in the liberalised network industries (EC 2003: 4). While there may be a positive employment effect in telecommunications – although it remains to be seen if this effect is sustainable – in many other sectors liberalisation and privatisation have resulted in net losses of public sector jobs. In the electricity industry alone nearly a quarter million jobs have been eliminated in the past ten years (ECOTEC 2007: 26–27). In the EU-15 the loss of employment in the electricity sector amounts to 31% between 1995 and 2004; in some countries, including Italy and the Netherlands, the reduction amounts to 40 and 39% respectively (*ibid.*). If we extend the period to the early 1990s almost half of the jobs in the British electricity industry disappeared after privatisation (*ibid.* 66–72).

The electricity sector is not an exception. The same study also shows a 12% reduction of employment in the gas industry for six countries in only four years (*ibid.* 57). The postal sector in several countries has also seen a decrease in employment following the stepwise introduction of competition. According to national labour force survey data the number of employees in Austria and Sweden decreased by 25% between 1995 and 2005, while in Germany job losses amounted to 15% over the same period. A study commissioned by the European Foundation for the Improvement of Living and Working Conditions reveals a similar fall in employment in railways. On average, the reduction in five member states amounts to 16% (European Foundation 2006a: 15). The reduction of employment in the unified railway sector in Germany amounted to a staggering 52% between 1991 and 2001, after which it started to grow again because of Deutsche Bahn's takeover of logistics companies (*ibid.*; Hermann and Atzmüller 2005: 108). If we look at



the company level, a number of former state-owned railway companies have reduced employment by more than 50% since 1990; for example, the Spanish and Portuguese national railway companies have cut employment by 70% and 80% respectively (Hillal 2007: 4). Also in other sectors job losses at the former monopoly suppliers go beyond those experienced at the sectoral level (Hermann and Atzmüller 2005). For Austria, a detailed analysis of sectoral and company data shows that employment created by new service providers cannot as a rule compensate for the losses at the former monopoly suppliers (Atzmüller, Hermann and Raza 2005).

**Table 1:** *Studies on the impact of privatisation and liberalisation on the level of employment*

Sector	Study	Countries	Period covered	Employment changes
Electricity	ECOTEC	EU-15	1995–2004	–31%
		Germany	1995–2004	–34%
		Italy	1995–2004	–40%
		Netherlands	1995–2004	–39%
		Spain	1995–2004	–34%
		Sweden	1995–2004	–33%
Gas	ECOTEC	12 Member States (CZ, DK, DE, SP, IT, LV, LT, HU, AT, PT, SL, FI)	2000–2004	–12%
Postal Services	PIQUE	Austria	1995–2005	–25%
		Sweden	1995–2005	–25%
		Germany	1995–2005	–15%
Railways	European Foundation	5 Countries (GE, IT, NL, SW, UK)	1996–2003	–16%

*Sources:* ECOTEC Research & Consulting: *The Employment Impact of the Opening of Electricity and Gas Markets* (2007). European Foundation for the Improvement of Living and Working Conditions: *Employment, Industrial Relations and Working Conditions in the European Rail Transport Sector* (2006). *Privatisation and Impact on Quality, Employment and Productivity (PIQUE): Analysis of National Labour Force Survey Data* (2007).

Despite massive job losses in European public service sectors, staff reductions in the areas and companies included in our survey were typically carried out in ‘socially acceptable’ ways – and formally without forced lay offs. The exception is the UK where some public service workers were laid off without their consent. In Austria and Germany employees were instead typically offered various schemes, such as early retirement or redundancy

payments above the legal requirement (golden handshakes) to voluntarily leave the company. In Sweden the former monopoly provider Posten AB has initiated a special restructuring programme in which the company continued to pay 'redundant' employees their wages for 18 months while the workers were free to look for a new job. As part of the programme the company also paid for education and skills training for a maximum of ten months for each employee (European Foundation 2006b).

But in spite of these socially acceptable measures, layoffs were not really voluntary. As the earlier-cited studies show, company restructurings (for example, the German railways and postal services) frequently forced employees to quit because to move or commute to new company sites was not an option for them – especially for women with family obligations and lack of transport. Many employees and in particular older ones, moreover, left the company because they could no longer stand the growing pressure of work and the increasing frustration and insecurity in the workplace. On the other hand, it was often the younger and better educated employees that took the money and looked for other employment opportunities or started their own businesses.

The mode of reduction to a large degree depends on the strength of trade unions, the system of industrial relations, labour law and norms, as well as public opinion. Although dismissals were the exception, the threat of forced redundancies was repeatedly used by company managements to force trade unions and workers into agreements and cooperation on restructuring measures. In countries with a strong social partnership tradition (Austria, Germany) 'redundant' workers were sometimes 'parked' in the enterprises' own employment agency and training organisations. These served on the one hand to reorganise the internal labour market and on the other to improve internal company 'resource allocation'. In connection with retraining measures, however, workers are also trained and prepared for the external labour market and, for example on the German railways, even hired out to other companies as agency workers (Atzmüller and Hermann 2005: 111–14).

For the workers affected by such measures the transfer to an internal employment agency was usually seen as a dead end as regards their career and as an assault on their self-respect because as agency employees they are subject to a distinct employment regime that has strong similarities with the public unemployment system. Employees with German railways' own employment agency *DB services*, for example, had to accept job offers even if they entailed significant losses in income; after refusing a job offer once, the next time they could be sacked (*ibid.*). In contrast to German railway

employees, Austrian postal workers cannot be hired out. However, management instead forced ‘redundant workers’ assigned to the company’s internal job pool Jobline to show up every morning and serve their time without being given any tasks to perform. According to the company’s works council this can be an extremely frustrating experience (ibid. 35).

Alongside the personnel reductions mentioned above, liberalisation and privatisation have also led to cuts in apprenticeships as service providers no longer see it as their responsibility to train young workers beyond their immediate requirements (for example, the German and Austrian railways, the German postal service and the Austrian electricity company). In addition, the conventional proclamations of improvements in training and further education that can be found in virtually all annual reports of liberalised and privatised public enterprises are often far from the truth. In the case of a liberalised bus company in Austria, for example, the lack of investment in the training of drivers and the resulting operational problems have led to repeated assaults by angry passengers on drivers (ibid. 73).

### **3.2 Wages**

Job cuts in public services companies were partly compensated by investments in new labour-saving technologies (for example, the application of new information technology). However, as many public services are labour intensive – that is, labour costs make up the major part of total production costs – technological rationalisation has its limits. Many public sector firms therefore look for additional means of reducing labour and wages costs. One possibility is immediate cuts in basic wages. Such wage cuts exist – employees in the privatised British bus companies were confronted with the introduction of a new wage system with lower basic wages<sup>7</sup> – but they are an exception. More widespread measures to reduce labour costs are dismissals with the option of altered conditions of employment and the employment of new workers under worse conditions. Former monopoly suppliers in several countries and sectors have negotiated new and typically unfavourable wage schemes for new entrants. For example, in the case of the city of Vienna’s own municipal utilities, employees who were hired after 1 July 2001 had to accept a wage cut of 13% compared to those hired before (ibid. 66).

In addition to growing wage disparities within former monopoly providers, differences also emerged between the former monopoly providers and the

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<sup>7</sup> Employees were paid “compensation” (or bribes) to accept the new system (Atzmüller/Hermann 2005: 135).

new competitors. The latter often do not fall under any collective agreement or are part of a different collective agreement with worse conditions (for example, postal services in Germany). Moreover, the international companies that quickly appear on the newly deregulated public service markets often disregard existing regulations and pay according to their own company-specific wage schemes (for example, the water utilities in Germany). In some sectors new providers deliberately employ wage-dumping practices in order to gain market share from the former monopoly suppliers, thereby threatening to turn entire industries into low-wage sectors.

The post sector is an example here: 60% of the workforce created by the new mail operators in Germany is hired as marginally employed workers in so-called 'mini jobs' paying no more than 400 euros a month. Another 22% are part-time workers, while only 18% of the newly created jobs are full-time positions (Brandt, Drews and Schulten 2007: 269; see also Brandt and Schulten in this volume). If we compare hourly wage rates, the new competitors pay between 25% and 50% less than the former monopoly provider Deutsche Post AG (Brandt and Schulten in this volume). Many of the workers employed by the new providers are eligible for state allowances because their income is below the national minimum standard (*ibid.*). In Austria the majority of the workers employed by the new mail operators are self-employed. As self-employed mail deliverers they not only lack any form of employment protection, but they also earn significantly less than regular postmen employed by the former monopoly provider Austrian Post AG (Hermann 2008). Former monopoly providers in the postal sector have frequently established low-cost subsidiaries in other countries where they apply the same wage-dumping practices they accuse the new competitors of introducing in their home markets. For example, Deutsche Post World Net through its subsidiary Selekt Mail pays significantly less than the former monopoly provider in the Netherlands, while TNT does the same thing through its subsidiary TNT Post in Germany.

Apart from these changes, the above-mentioned studies point to a number of indirect measures for reducing labour costs, including changes in seniority-based wage increases and the reduction of existing or the creation of new wage categories. The termination of company agreements in order to eliminate company-specific supplements and bonuses, as well as social provisions (sickness pay, family allowances) and company pensions, are also popular methods of cutting labour costs. Alongside these measures the decoupling of working hours and wages is a dominant strategy in the transformation of traditional wage structures and pay systems. Hence overtime pay and supplements for weekend work and unsocial hours are

avoided by means of more extended calculation periods, while the introduction of working hours accounts and the flat-rate payment for overtime hours regardless of the number of hours actually worked (all-inclusive agreements) also help to avoid the payment of overtime bonuses.

Another form of indirect wage cut is the outsourcing of jobs to other firms specialised in certain services and covered by different and typically unfavourable collective agreements or free of any mandatory wage regulations. A popular example is cleaning services, which have been widely outsourced to private cleaning firms. In the case of the Austrian railways cleaning personnel employed by a private cleaning firm earn about a quarter less than the railways' own cleaning staff (*ibid.* 48).<sup>8</sup> Moreover, workers performing outsourced tasks not only earn lower wages than in-house staff, but also suffer from worse working and employment conditions, including constant time pressure, highly flexible working hours and, in some cases, less or no employment protection.

In some sectors (postal services, local transport) payment practices has reappeared that were widely considered as obsolete (piece rates for letter delivery, wages dependent on customer frequency for counter workers). In the Swedish bus sector large numbers of drivers are today employed as day labourers by the companies to balance out the labour shortage that occurred as a consequence of the worsening of working conditions created by liberalisation and privatisation (*ibid.* 160–61). According to the Swedish bus union, these workers are almost on an equal footing regarding social security, but they receive no sickness pay. Because of the labour shortage in the bus sector at least they can more or less choose their own shift patterns and route plans. This, however, has negative consequences for the working conditions of the permanently employed bus drivers, who are subject to company directives (*ibid.*). More generally, while the application of performance-based wages is limited to certain sectors and jobs, the introduction of performance-related wage components and the individualisation of forms of payment are general features of the restructuring of wage conditions in liberalised and privatised public services.

### **3.3 Working hours and working conditions**

Apart from the level of employment and wages, liberalisation and privatisation have also had a major impact on working hours. As already mentioned, the public sector employment regime was characterised by a high

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<sup>8</sup> According to the collective agreements for railway workers and for cleaning personnel for monuments, façades and buildings.

degree of working time stability and predictability. Liberalisation and privatisation have led to a far-reaching flexibilisation of working hours. Flexibilisation includes the greater use of part-time work, the extension of calculation periods and the introduction of working-hours accounts. According to national labour force survey data, part-time work in the Austrian and German postal sector increased by almost 28% between 1995 and 2005. For the UK, data from the Annual Business Inquiry show a 44% increase in part-time jobs in the postal sector between 1998 and 2005. A similar increase (plus 41%) took place at the former monopoly provider Austrian Post between 1996 and 2002 (Atzmüller and Hermann 2005: 33). In addition to the surge in part-time jobs, some sectors or specific groups of workers have experienced a growth in long hours and overtime working to compensate for personnel reductions and partly also for losses of income. According to the railway workers union, the 4,300 train drivers employed by the state-owned Austrian railway company accumulated almost one million overtime hours up to 2003 (*ibid.* 47)

Although a direct lengthening of daily or weekly working hours is the exception it does take place. Examples include local transport in the UK (Atzmüller and Hermann 2005: 139) and railways in Germany, where the working week was extended by one hour in 2005 (Hillal 2007: 8). However, instead of directly extending working hours frequently, a range of indirect measures are applied to lengthen the working day. These include the reduction and shortening of breaks and rest periods in order to increase the 'productive' part of the working day. This strategy is predominantly to be found in labour-intensive sectors, such as local transport. In Sweden, for example, angry drivers responded to reductions in breaks with a so-called 'pee break strike' (Atzmüller and Hermann 2005: 161).

Furthermore, company managements have also demanded cutbacks to plant-specific additional work-free periods (plant-specific vacations, additional holidays). This has, for example, been pushed through on the railways in Sweden, where those employed by the company for a certain number of years could claim 36 days of vacation and retirement at 60, whereas newcomers receive holiday and pension entitlements according to the general Swedish employment and social security regulations (*ibid.* 157). Apart from this, in many sectors company-specific and sector-specific pension regulations are being dismantled, resulting in a lengthening of the working life.

As far as working conditions are concerned, although data on the changes in working conditions in the public sector are difficult to obtain, our interviews and additional information indicate a trend towards an increased intensity of

work and growing work-related constraints, as more work has to be performed by fewer employees. This is primarily forced upon workers by job enlargement, the downward shifting of responsibilities with a simultaneous increase in the control instruments employed by headquarters (performance monitoring and cost control), as well as the stimulation of internal and external competition through the use of cost and profit centres and international benchmarks.

### **3.4 Trade union organisation**

For the advocates of liberalisation and privatisation, trade unions are a major cause of the supposed inflexibilities in public services, which applies to both labour processes and wage costs. In some countries (in particular the UK) liberalisation and privatisation were therefore pursued with the explicit objective of weakening the trade unions. In the countries and sectors we studied all trade unions accepted liberalisation and privatisation, although sometimes after putting up a lengthy fight and engaging in public campaigns. In the end, however, the unions gave in and, where possible, cooperated with company managements in order to have a say in the transformation process and as far as possible protect the rights and employment conditions of the existing workforces – often at the expense of new workers or the workers of the new service providers. In addition, unions used concession bargaining to make sure that those employees that had to leave the company would receive appropriate compensation (including early retirement or redundancy payments, further training for the external labour market). Although there are country-specific differences, liberalisation and privatisation in general have led to a significant decentralisation and fragmentation of collective agreements and bargaining structures. This development seems to be particularly marked in the UK, but also in Austria.

Moreover, although trade union leaderships emphasise their success in averting forced redundancies and maintaining collective agreements, liberalisation and privatisation of public services have nevertheless fuelled growing conflicts within and also between trade unions (for example, in the railway sector in Germany). Conflicts result from the fragmentation of employment conditions following the application of different collective agreements for the same category of workers in different enterprises, but also in the same company. It should be evident that such differences can exacerbate existing differences within the workforce and so undermine the basis for solidarity and trade union organisation in the public sector. This process is further amplified by company managements that offer better employment conditions to certain groups of workers in order to intensify

existing aversions and prejudices between workers that can be economically exploited.

The trade unions are also confronted with the fact that the changes in wages and working hours discussed earlier have not only lowered labour costs, but have at the same time called into question the collective and relatively uniform working and employment conditions typical of public sector jobs. Variation in wages between companies and within companies, the introduction of performance-based wage components as well as the flexibilisation of working hours have led to the increasing individualisation of working and employment conditions, while the growing use of atypical forms of employment, including (marginal) part-time work, short-term contracts, agency work and new self-employed workers, has fuelled fragmentation and segmentation in the public sector workforce. The result is the emergence of an employment hierarchy with those still enjoying full civil-servant status on the top and those employed under precarious conditions at the bottom of the scale.

Another challenge facing the trade unions due to liberalisation and privatisation is the need to transform themselves from company to sectoral unions. Some of them, moreover, have to learn how to organise new members at the new enterprises, since in some countries union membership was almost mandatory at the former monopoly suppliers. As a result of this strategic reorientation, however, it can also be expected that public trade unions will in future focus their resources on the protection of their members' interests rather than on general political issues, such as the fight for high standards in the provision of public services.

## **Conclusions**

The liberalisation and privatisation of public services has led to the far-reaching dismantling of the public employment regime of the post-war decades. Growing variation in wages in companies and between companies, the introduction of performance-based wage components, the flexibilisation of working time and the use of atypical forms of employment, such as marginal part-time, self-employment and agency work, have not only led to an increasing individualisation and fragmentation of employment and labour relations, but in many companies and workplaces the subjugation of service provision to profit maximisation has also caused a significant deterioration of employment and working conditions. The reduction of employment has furthermore deprived the public sector of its macroeconomic function as sustainer of full employment and pacesetter for the improvement of private



sector employment and working conditions. Many of the changes described above are well known from the restructuring of private sector work and employment relations. Hence, while during the postwar decades better public sector employment conditions were gradually extended to private sector jobs, liberalisation and privatisation of public services has reversed this process with worse private sector conditions increasingly being adopted in the public sector. The result is again a gradual adjustment of public and private sector labour standards with the important difference that this time it is a downward adjustment. However, the dismantling of a public sector alternative is contributing to a recommodification of employment in the current neoliberal phase of capitalism and will therefore in the long-run likely also have repercussions for private-sector employees.

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## II. Effects of privatisation and liberalisation on wages, working conditions and work–life balance



## **Precarious employment in the public and private service sectors: comparing the UK and Germany**

### **Introduction**

The present chapter compares the incidence and characteristics of precarious employment in the public and private service sectors in Germany and the UK. In both these countries, in line with the rest of the industrialised world, the service sector accounts for by far the largest share of employment and for most new jobs created in recent decades. This service sector growth raises concerns about the quality of employment, however. While the service sector offers important opportunities and high quality employment, it is also the sector of ‘McJobs’, of low quality, precarious employment (Kemenkliene et al. 2007). As an earlier study on service employment in Germany and the UK concluded, the growth of this sector offers both ‘high-end’ and ‘low-end’ jobs and implies increasing polarisation and growing inequality (Fagan et al. 2005). But as we shall discuss below, the UK and Germany represent two quite different types of capitalism in which the incidence and distribution of precarious employment can be expected to differ.

One factor that seems to be important for the quality of employment is whether it is exercised in the public or the private sector. Indeed, it has been well established that wages and working conditions, on average, are of higher quality and less polarised in the public sector than in the private sector. These differences vary across countries, social groups, sectors and time, however (on this see, for example, Ponthieux and Meurs 2005; Lucifora and Meurs 2006; Chung in this volume). Also, the extent to which they can be attributed to an independent public–private sector effect or rather to structural differences between the two sectors, including gender, educational levels, NACE sectors, age and other things, remains a question of debate (ibid.).

The present chapter aims to contribute to clarifying these issues by addressing two core questions: (i) the extent to which the incidence and characteristics of precarious employment differ between the public and private service sectors, and how this has changed in the last decade; and (ii) the extent to which the differences found can be attributed to the ownership factor as such or to differences in terms of educational levels, share of female employment, age structure, NACE sectors or enterprise size. This analysis is then set in the context of the major differences between the capitalist systems of the two countries, as well as their quite different paths of reform between the mid-1990s and the mid-2000s. The analysis is based on data from the German Socio-Economic Panel Study (SOEP) and the British Household Panel Survey (BHPS).

The chapter is organised as follows. In Section 1 the background of the two country cases is discussed, pointing out the differences in their models of capitalism, as well as different reform paths in recent years. Also, in this section the main hypothesis for the subsequent empirical analysis will be formulated. In Section 2, the data will be discussed. In Section 3 the differences between the public and private sectors in terms of a number of quality-of-employment indicators will be presented in a descriptive manner for each country, as well as their development over time. We shall also present a number of indicators for precariousness and compare precarious employment in the two sectors for each country. Section 4 proceeds with a multivariate analysis to determine which independent variables affect the level of precariousness in the two sectors. The main question to be answered here is whether the expected differences in the incidence of precarious employment between the public and private sectors are caused by the ownership factor or derive from the different distribution of other factors in the two sectors. The final section presents conclusions.

## **1. The UK and Germany: different types of capitalism, different reform paths**

Although in both the UK and Germany the service sector is the largest and fastest growing sector, the two countries show a number of basic differences. One difference is that the UK has one of the highest percentages of service employment in Europe (76.6% in 2006), clearly above the EU-15 average (70.1%), while in Germany industry remains a key sector in terms of employment and the service sector is relatively small (68.0%). The UK is also among the best performers in Europe as far as employment and unemployment rates are concerned (71.5% and 5.3% respectively in 2006), while in Germany unemployment is among the highest in the EU (9.8% in

2006) and the employment rate – although above the EU-15 average – lags some 4 percentage points behind that of the UK, at 67.5% in 2006.

Another difference between the two, key for the present chapter, concerns their models of capitalism. Britain is generally presented as the main European example of a liberal market economy, in which economic activity is based mainly on market relationships (Hall and Soskice 2001). It is pictured as a deregulated, individualised labour market in which only about 30% of employees are covered by decentralised collective agreements, mainly in the public sector (Kersley et al. 2006). Germany, on the other hand, is often considered to be the archetype of the coordinated market economy, in which competition is complemented by cooperation between economic actors, the labour market is much more regulated by law and the coverage of – mainly sectoral – collective agreements is high (Hall and Soskice 2001).

These different models of capitalism are likely to result in differences in terms of precarious work. In the liberal market economy individual employees are less protected in the employment relationship, which is characterised by a fundamental asymmetry of power in favour of the employer. As a result, solidarity and redistribution tend to be weak and wages and working conditions are more polarised than in coordinated market economies.

Models of capitalism are not static over time, however. Indeed, in both the UK and Germany important reforms of labour market institutions have been made in the last decade. In Britain, until 1997, the long rule of the Thatcherite Conservatives had resulted in a profound deregulation of the labour market. Many key elements of employment relations remained outside the scope of statutory regulations, including the determination of pay and other terms and conditions. These were regulated mainly through voluntary agreements between employers and workers. Unionisation and the coverage of collective agreements declined significantly in the private sector in this period but remained quite high in the public sector. Specifically concerning the public sector, in the 1980s the Conservatives argued that this sector was wasteful, over-bureaucratic and underperforming (Ferlie et al. 1996). To cure these ‘diseases’ New Public Management (NMP)-type strategies were instituted, introducing private sector management approaches and emphasising such things as marketisation, privatisation, managerialism, performance measurement and accountability (see, for example, Larbie 1999; Ferlie et al. 1996). This included a call for efficiency-oriented employment relations based on market coordination.



Since 1997, however, consecutive Labour governments have ‘introduced a programme of legislation establishing, for the first time, a comprehensive framework of minimum employment standards’ (DTI 2005). These standards include many elements of working conditions, work–life balance and collective labour relations.<sup>1</sup> Paramount among them is the minimum wage, introduced in 2000 and today the third-highest statutory minimum wage in Europe. As a result of these re-regulation efforts legislation attained a much more comprehensive role in setting minimum standards; and these standards affect all employees, independent of whether they are unionised or covered by a collective agreement (Dickens and Hall 2006).

At the same time, unionisation and the coverage of collective agreements remain important determinants of wages and working conditions, and there are marked differences between the public and private sectors in this respect. Unionisation is much higher in the public than in the private sector: in 2004, union density was 64% in the public sector and 22% in the private sector (Kersley et al. 2006: 110, Table 5.1). Also, in 2004, 82% of employees in the public sector were covered by collective agreements, compared to 14% in the private sector (*ibid.*: 180, Table 7.1), while collective bargaining was part of the pay determination methods in 77% of workplaces in the public sector, compared to only 11% in the private sector (*ibid.*: 184, Table 7.4). This is important for the present study since collective bargaining is positively associated with compressing pay at workplace level, as well as with reducing the incidence of low pay and with fringe benefits (Kersley et al. 2006: 196–201).

In Germany, labour market reforms in recent years have gone in the opposite direction from those in the UK. Germany in the mid-1990s was a comparatively highly regulated and coordinated economy, especially compared to Thatcher’s Britain, in terms of both labour legislation and the much higher coverage of collective agreements, mainly at the sectoral level. In the last decade a number of changes have taken place, however. Where

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<sup>1</sup> According to the DTI report, ‘Legislation introduced to date includes a national minimum wage (NMW); the Working Time Regulations (WTR); parental leave; time off for employees with dependants; enhanced maternity leave and pay; protection against unfair treatment for part-time workers and fixed-term employees; a right to statutory trade union recognition; European Works Councils; legislation outlawing discrimination in employment on grounds of sexual orientation and religion or belief; a duty on employers to consider requests for flexible working from parents with young and/or disabled children; the introduction of statutory dispute resolution procedures in the workplace; amendments to employment tribunal regulations and regulations on information and consultation’ (DTI 2005: 5).

labour market regulations are concerned, in the early 2000s the Hartz reform introduced a number of reforms aimed principally at deregulation and the increased use of flexible and marginal employment forms (Leschke forthcoming). In terms of collective bargaining, a process of decentralisation and differentiation can be observed in which the importance of sectoral agreements is declining while that of company agreements is increasing; in addition, there is less coordination of collective bargaining between and within sectors (Bispinck 2006; Seifert and Massa-Wirth 2005). As a result, there has been an increase in precarious jobs, including more low paid jobs as well as more marginal jobs in terms of contracts and working time. Also in Germany, trade union membership is higher in the public than in the private service sector and the coverage of collective agreements is higher in the former (Goerke and Pannenberg 2007; Addison et al. 2006).

NPM-type reforms have also been introduced in the German public sector; however, this happened quite a bit later than in the UK and less comprehensively. Only since the 1990s, under the heading of the ‘New Steering Model’, has administrative modernisation inspired by NPM ideas been implemented, first at the level of local government and later also at the *Land* and federal levels (Wollmann 2000; Barzelay and Füchtner 2003). Hence, whereas in the UK much of the effect of NPM strategies had taken place before the starting point of our analysis, in Germany much of these reforms happened during this period.

In this context, what is to be expected concerning the differences in wages and working conditions between the public and private sectors in the two countries and how did this change in 1997–2005? As already argued, we start from the hypothesis that wages and working conditions are of a higher quality and less polarised in public sector than in private sector services. We also assume, however, that these differences are not stable or static over time. For the UK we expect Labour’s re-regulation efforts to lead to some improvement of the quality of employment across the board, but also, for example, to lead to a stronger decline of temporary contracts in the private sector, where their incidence in the 1990s was higher than in the public sector.

For Germany, the general trend is expected to be the reverse, namely towards a worsening of employment quality, following the deregulation and flexibilisation of the labour market. This process is expected to affect both public and private employment, but to be stronger in the private service sector, considering the lower trade union density and coverage of collective agreements.

As far as the incidence of precarious employment is concerned, since the public sector is expected to offer better quality employment on average, less precarious employment is expected to be found here than in the private sector. But the question here remains whether this is due to the ownership difference, or to other differences between the two sectors that do not concern ownership but rather other variables that influence precariousness, that is, different characteristics in terms of age, education, gender, sector and size of organisation. In Section 4, these variables, together with the ownership variable, will be used in a multivariate analysis to determine their explanatory power for the incidence of precarious employment in the two sectors.

## 2. Data

The following analysis is based on the German Socio-Economic Panel Study (SOEP) and the British Household Panel Survey (BHPS).<sup>2</sup> Both provide up-to-date longitudinal representative micro data on individuals and households. The SOEP started in 1984; in 1990 it was extended to the former GDR. The first survey year of the BHPS is 1990. Since the BHPS was in part modelled on the SOEP, both data sets cover similar topics, such as labour market, income and wealth, housing, health and socio-economic values, and use international standard classifications for the most part; they are appropriate for comparative data analysis of working conditions. As we will see, there are some limits to comparability, however: the questionnaires are not identical, and the phrasing of questions but also different cultural backgrounds are expected to lead to differences in response behaviour that we cannot account for. Importantly, country comparisons of education levels are very restricted because the BHPS uses a country-specific variable and not the international standard classification of education (ISCED).<sup>3</sup>

The aim of our study is to detect changes over time in public and private services; the following analysis will therefore be restricted to cross-sections.

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<sup>2</sup> For information on the SOEP, such as questionnaires, codebook and overview of publications, refer to <http://www.diw.de/english/soep/26636.html>. For information on the BHPS refer to <http://www.iser.essex.ac.uk/ulsc/bhps/>.

<sup>3</sup> We create three education levels based on the country-specific education variable (xqfedhi) provided in the BHPS. High educational level contains the categories of xqfedhi 1–4, medium educational level contains the categories 5–8 and low educational level the categories 9–12.

Information about standard classifications such as ISCED and NACE can be found under Eurostat's metadata server RAMON: <http://ec.europa.eu/eurostat/ramon/index.cfm>

We will compare working conditions in the public and the private sector in 1997 and 2005, currently the latest available data.<sup>4</sup> Comparisons over time are facilitated by the fact that questions remain very stable over time. Since the focus of the chapter is on working conditions in the service sector, only the information for people of working age (16–64) who are employed in the service sector (NACE codes 50 to 98) is used. Self-employed are excluded from the analysis. We decided to keep students and persons in the dual apprenticeship system in Germany in the sample in order to get a full picture of precarious employment in the service sector. Precarious jobs that are held by students or apprentices, of course, have to be judged differently because they will in many instances act as an organised stepping stone to regular work.

All descriptive results are weighted with the cross-sectional weights provided in the SOEP and the BHPS data in order to adjust for different sampling probabilities and non-response, and thus render the survey representative for the corresponding population.<sup>5</sup> For 2005, data for more than 15,000 (20,000) individuals were available in the BHPS (SOEP); both data sets thus provide sufficiently high case numbers to allow analysis of sub-groups, such as precarious workers in the service sector.

### **3. Descriptive analysis**

#### **3.1 The UK**

The share of the public and private sectors in total service employment did not change in the period 1997–2005: the public sector accounted for 35.3% of total service employment in 1997 and for 35.7% in 2005. The respective figures for the private sector are 64.7% and 64.5%. There were, however, certain changes in the main characteristics of the two sectors. Table 1 presents their general structure for 1997 and 2005. Five major variables are presented: educational levels, age, gender, sector and organisation size. Where educational levels are concerned, this is clearly higher in the public than in the private sector. In 1997, 53.2% of employees in the public sector had higher education, compared to 34.1% in the private sector, while the share of

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<sup>4</sup> For the BHPS the classification of economic activities in the European Community (NACE) is not available for the survey years 1995 and 1996, so we decided to use 1997. This is also the first year of the New Labour era in the UK and therefore suitable as a starting point for our analysis.

<sup>5</sup> For information on the construction of weights in the SOEP and the BHPS compare Haisken-DeNew (2005: 37–41) and Taylor (2007: A5-1–A5-13), respectively.

**Table 1:** *General structure of the public and private service sectors in 1997 and 2005, UK*

	1997			2005				
	Total	Public	Private	Public/Private	Total	Public	Private	Public/Private
		Qualification level			Qualification level			
Low (ISCED 0–2)	17.6	12.2	20.6	0.6	10.3	6.0	12.7	0.5
Medium (ISCED 3–4)	41.5	34.6	45.3	0.8	34.0	24.4	39.4	0.6
High (ISCED 5–6)	40.8	53.2	34.1	1.6	55.7	69.2	47.9	1.4
		Age categories			Age categories			
16–24 years	18.0	5.9	24.6	0.2	18.0	6.7	24.2	0.3
25–54 years	73.0	84.2	66.8	1.3	67.7	76.1	63.1	1.2
55–64 years	9.1	9.9	8.6	1.2	14.3	17.3	12.7	1.4
		Gender			Gender			
Men	41.7	32.9	46.5	0.7	42.3	30.3	49.0	0.6
Women	58.3	67.1	53.5	1.3	57.7	69.7	51.1	1.4
		NACE Industry Sector			NACE Industry Sector			
Wholesale and retail trade; repair of motor vehicles, and personal and household goods	21.5	0.1	33.1	–	21.0	0.2	32.4	–
Hotels and restaurants	7.4	1.0	11.0	–	7.4	1.8	10.5	–

	NACE Industry Sector			NACE Industry Sector		
Transport, storage and communications	8.9	4.2	11.4	–	–	–
Financial intermediation	7.2	0.2	11.1	–	–	–
Real estate, renting and business activities	12.9	1.5	19.1	–	–	–
Public administration, defence, compulsory social security	10.6	29.7	0.2	–	–	–
Education	12.2	30.2	2.4	–	–	–
Health and social work	14.2	29.2	6.0	–	–	–
Other community, social and personal service activities	5.0	4.1	5.5	–	–	–
Private households	0.2	0	0.4	–	–	–
				Organisation size (%)		
0–24 employees	38.4	23.7	46.4	0.5	35.9	43.4
25–99 employees	26.0	28.6	24.5	1.2	24.8	23.3
100–199 employees	9.8	10.8	9.2	1.2	9.7	8.3
200–999 employees	15.9	18.3	14.6	1.3	17.9	18.4
1000+ employees	9.9	18.5	5.3	3.5	11.7	6.7
				Organisation size (%)		
				22.3	20.9	6.7
				43.4	23.3	1.2
				27.6	12.2	8.3
				17.0	18.4	0.9
				3.8	5.1	0.2
				0.0	0.0	–

*Source:* Own calculation based on weighted BHPS data, several years.

lower and medium-level education in the public sector was substantially lower. Eight years later, in both sectors the educational level was much higher: the share of highly educated employees increased by about 16 percentage points in the public sector and by 13.8 percentage points in the private sector. The share of lower and medium educated fell in both sectors. As a result, the public sector continues to have a much higher educational level than the private sector.

Related to this, the public sector also has a higher age profile: the share of young people was 5.9% in 1997 and 6.7% in 2005, compared to 24.6% and 24.2%, respectively, in the private sector. For the middle and higher age groups the shares are higher in the public sector in both years. Over the eight year period the share of young people was stable in both sectors, while that of the middle group declined and that of the higher age group increased, particularly in the public sector.

In terms of gender, the public sector is clearly female dominated, with about two-thirds of employees being women and the trend slightly increasing between 1997 and 2005. The private service sector is much more balanced; in 2005 the share of men and women was almost 50–50.

Where NACE sectors are concerned, a clear division exists between public and private, and little change has taken place over time. Wholesale, trade and repair, hotels and restaurants, transport and communication, financial intermediation, private households and real estate, renting and business services are all clearly private sectors, and only in transport and communication is the share of the public sector substantial. In contrast, public administration, defence and social security, education and health and social work are all clearly publicly dominated sectors, with only health and social work having a substantial share of private employment. Only the small other community, social and personal service activities sector is clearly a dual sector in which public and private ownership have similar weight.

Finally, a much lower percentage of public sector organisations have fewer than 25 employees (23.7% compared to 46.4% in 1997), while a much larger percentage have more than 1,000 employees (18.5% against 5.3%). Indeed, 36.8% of employees in the public sector are employed in large (200–999 employees) or very large (1000+ employees) organisations, while in the private sector no less than 70.9% are employed in organisations with fewer than 100 employees. Between 1997 and 2005 the major change in this picture is the increased importance of larger organisations in the private sector.

Table 2 presents a comparison of working conditions in the two sectors. A number of important differences emerge. First, monthly pay of full-time employees is about 10% lower in the private service sector, in both 1997 and 2005. Also, in the private sector the percentage on low wages (that is, below 60% of the overall median) is much higher for both years, and while this percentage declined over the 8-year period, probably linked to the introduction of the minimum wage, it declined more quickly in public services than in private ones. Moreover, pay is much less equally distributed in private services, which have an 80/20 labour income quintile ratio of 4.4 for 1997 and 4.0 for 2005, compared to 3.2 and 2.8, respectively, in the public sector. Hence, on all pay indicators, the two sectors differ substantially.

This is much less the case as far as types of contract are concerned. The percentage of employees on permanent full-time ('standard') contracts and on part-time contracts is virtually the same for both years. The percentage on non-permanent contracts is slightly higher in the private sector but after a generalised decline over the 8-year period the difference is no longer significant. What is different is the much higher share of seasonal and casual contracts in the group of non-permanent contracts in the private sector (only available for 2005), most likely linked to the important role of hotels and restaurants.

Over time, average full-time working time declined overall, as did the percentage of workers working very long (>48) and very short (<15) hours. But differences between public and private services remain fairly stable: for both years, the full-time working week is about two hours shorter in the public sector, the percentage working very long hours in the public sector is less than half the percentage in the private sector, and the percentage working fewer than 15 hours is substantially lower in the public sector and declining faster over time than in the private sector. The public sector also performs much better in terms of providing workers with training: over 40% of workers in the public sector receive training, while in the private sector this percentage remains below 30%. And while in both sectors this percentage increases slightly, the difference between the two remains almost the same.

Trade union membership is much higher in the public than in the private sector and the difference between the two sectors has only become bigger: in 1997 it was 3.7 times higher in the public sector and in 2005 4.2 times. The overall decline in membership of 3.7 percentage points over these years was proportionally stronger in the private than in the public sector. Also, a higher percentage of public sector workers are active in a trade union, even though



**Table 2: Working conditions in the public and private service sectors in 1997 and 2005, UK\***

	1997			2005				
	Total	Public	Private	Public/ Private	Total	Public	Private	Public/ Private
		Gross pay			Gross pay			
Average pay (full-time workers)	£1449.5	£1538.6	£1397.0	1.1	£1958.1	£2106.2	£1876.1	1.1
Average pay (full-time workers)	€2093.7	€2221.6	€2017.9	1.1	€2863.6	€3080.1	€2730.5	1.1
Share that earns less than 60% of (overall monthly) median	28.3	19.2	33.2	0.6	25.0	15.9	31.0	0.5
80/20 (overall) labour income quintile share ratio	4.1	3.2	4.4	0.7	3.6	2.8	4.0	0.7
		Contract type			Contract type			
Permanent full-time	77.2 (n.s.) *	79.0 (n.s.)	76.2 (n.s.)	1.0	75.7	75.9	75.6	1.0
Part-time (less than 30 hours) (perm + fix)	27.0 (n.s.)	25.0 (n.s.)	28.1 (n.s.)	0.9	26.5	25.7	26.9	1.0
Non-permanent	10.7	9.8	11.1	0.9	6.2 (n.s.)	5.9 (n.s.)	6.4 (n.s.)	0.9
Seasonal/temp. job	6.9	3.9	8.5	0.5	—	—	—	—
Fixed-term contract	3.8	5.9	2.6	2.3	—	—	—	—
Share seasonal in non-permanent	—	—	—	—	7.8	1.3	11.1	0.1
Share fixed-term in non-permanent	—	—	—	—	29.4	54.3	16.7	3.3
Share TWA in non-permanent	—	—	—	—	15.3	14.0	16.0	0.9
Share casual in non-permanent	—	—	—	—	28.5	13.4	36.1	0.4
Share other in non-permanent	—	—	—	—	19.1	17.0	20.1	0.8

	Working time		Working time	
Average full-time (excluding overtime and meal breaks)	38.4	37.1	39.1	0.9
Average part-time (excluding overtime and meal breaks)	15.2	16.4	14.6	1.1
% >48h (excluding overtime and meal breaks)	5.3	2.7	6.7	0.4
% less than 15h (excluding overtime and meal breaks)	13.0	10.7	14.1	0.8
Training: yes	32.3	41.9	27.6	1.5
	Participation in training (1998)		Participation in training	
	34.5	43.4	29.7	1.5
	Interest representation		Interest representation	
Trade union membership	27.0	51.2	13.8	3.7
Active in trade union	6.1	12.1	2.8	4.3
Union or staff association at workplace	51.2	92.1	28.2	3.3
	Employer pension scheme		Employer pension scheme	
Employer runs a pension scheme	67.0	94.3	51.8	1.8
Entitled to company pension (company with pension scheme)	75.7	84.7	66.5	1.3
	74.4	96.1	61.9	1.6
	70.5	86.8	55.9	1.6

Note: \*n.s. stands for 'not significant'. It is displayed in the relevant cell when the results of the Pearson chi-square test are not significant at the 0.5 level. Pearson chi-square controls for the hypothesis that the rows and columns in a two-way table are independent. For the variables income and average working time confidence intervals were taken into consideration.

Source: Own calculation based on weighted BHPS data, several years.

in both sectors this group is diminishing strongly over time. Moreover, in more than 90% of workplaces in the public sector a union or staff association is active, compared to less than 30% in private services.

Finally, in 2005, 96.1% of workers in the public sector worked for an employer that ran a pension scheme, up slightly from 94.3% in 1997. In the private sector the respective percentages were much lower, though increasing rapidly: 61.9% and 51.8%. In the public sector the percentage of workers at an employer running a pension scheme who were actually entitled to the company pension is much higher and increasing over time, from 84.7% to 86.8%; in the private sector it is much lower and declining over time, from 66.5% to 55.9%.

From Tables 1 and 2 we can conclude that there are clear differences between the two sectors in terms of their structural characteristics and working conditions. Workers in the public sector are older, better educated, more often female and work in different NACE sectors and in larger organisations than the private sector workers. Also, public sector workers are better paid, work fewer hours in full-time jobs, have fewer very long or very short working hours, receive more training, are better represented and are much more often entitled to a company pension scheme. Indeed, working conditions are clearly better in the public sector than in the private one. In Section 4 we will express these differences in terms of precarious employment and discuss whether they are due to the sectors' different structural characteristics or there is also an independent public sector effect. Now we turn to the descriptive analysis of the German case.

### **3.2 Germany**

In contrast to the UK, in Germany we see the weight of the private sector in total service employment increase in the 8 years under analysis: in 1997, the private sector share was 54.5%, but by 2005 it had risen to 60.4%. Hence, it is coming closer to the stable UK level (it is now only around 4 percentage points behind). Similar to the UK, there are structural differences between the two sectors (Table 3). In Germany too, the educational level of the public sector is higher than that of the private sector, even though these differences do not really concern the percentage of low educated (where we saw a huge difference in the UK). Rather, in the private sector the share of medium-level educated is much higher (23 percentage points difference in 1997, 20 percentage points in 2005), while in the public sector the share of highly educated is much higher (22 percentage points in 1997, 21 percentage points in 2005). This difference has become somewhat smaller over time, though not by much.

As in the UK, in Germany the private service sector is younger and differences between the two sectors are increasing over time. In 1997 the percentage of young people amounted to 15.8% in the private sector, compared to 9.4% in the public sector; in 2005 the respective figures were 14.4% and 6.4%, hence showing a strong decline, especially in the public sector. There are hardly any differences for the 25–54 age group in both years and this was also true for the 55–64 age group in 1997. By 2005, however, the share of the higher age group had increased by 5.3 percentage points to 17.1% in the public sector, while it had declined by 1 percentage point in the private sector.

Where gender differences are concerned, in contrast to the UK, in both years it is in private services where the share of women is highest, even though in both sectors women are in the majority. Over time it has increased more quickly in the public sector, so in a few years they will probably converge.

As far as NACE sectors are concerned, wholesale, retail and repair, hotels and restaurants, real estate, renting and business activities, and other services are overwhelmingly private sector activities, while public administration and education are overwhelmingly public. Transport was a dual sector in 1997 but had become more private by 2005, just like other community services. Also, the private sector is more important in financial intermediation in both years, but an important public component remains. The reverse is true for health and social work. Here the share of the public sector is much larger but the share of the private sector is important and increasing.

Finally, concerning size of organisation, 64% of employees in the public sector worked in organisations with 200 or more employees in 1997, which declined to 59.2% in 2005. In the private sector the respective percentages are much lower, at 33.2% and 32.0%. The situation is the exact reverse in the case of organisations with fewer than 20 employees, which in both years employ around 10% of employees in the public sector and around 30% in the private sector. Hence, as in the UK, the public sector in Germany is much more characterised by large organisations and the private sector by small enterprises.

Table 4 compares working conditions in the two sectors, showing a number of important differences. First, as in the UK, the monthly pay of full-time employees is about 10% lower in the private service sector, in both 1997 and 2005. Also, in the private sector the percentage on low wages is much higher for both years and pay is much less equally distributed. In contrast to the UK, however, both the percentage of workers earning a low wage and the 80/20 labour income quintile ratio increased over time for both sectors. Hence,

**Table 3: General structure of the public and private service sectors in 1997 and 2005, Germany\***

	1997			2005				
	Total	Public	Private	Public/ Private	Total	Public	Private	Public/ Private
	Qualification level							
Low (ISCED 0-2)	17.8	18.2	17.5	1.0	14.4	13.8	14.8	0.9
Medium (ISCED 3-4)	50.9	38.4	61.4	0.6	51.4	39.3	59.5	0.7
High (ISCED 5-6)	31.3	43.4	21.2	2.0	34.2	46.9	25.7	1.8
	Age categories							
16-24 years	12.9	9.4	15.8	0.6	11.2	6.4	14.4	0.4
25-54 years	76.1	78.8	73.9	1.1	76.4	76.6	76.2	1.0
55-64 years	11.0	11.8	10.4	1.1	12.4	17.1	9.4	1.8
	Gender							
Men	43.5 (n.s.)*	47.0 (n.s.)	40.6 (n.s.)	1.2	39.8 (n.s.)	42.1 (n.s.)	38.3 (n.s.)	1.1
Women	56.5 (n.s.)	53.0 (n.s.)	59.4 (n.s.)	0.9	60.2 (n.s.)	57.9 (n.s.)	61.7 (n.s.)	0.9
	NACE Industry Sector							
Wholesale and retail trade; repair of motor vehicles, and personal/household goods	22.3	0.2	40.8	-	19.6	1.3	31.6	-
Hotels and restaurants	3.3	0	6.0	-	3.8	0.3	6.0	-
Transport, storage and communications	9.4	8.9	9.7	-	7.7	5.5	9.1	-

Financial intermediation	6.9	4.0	9.2	–	6.1	3.4	8.0	–
Real estate, renting and business activities	9.5	1.5	16.3	–	12.4	2.1	19.1	–
Public administration, defence, compulsory social security	14.4	31.4	0.3	–	12.2	30.4	0.3	–
Education	10.3	20.7	1.6	–	11.5	25.1	2.6	–
Health and social work	16.4	26.5	7.9	–	18.7	26.3	13.8	–
Other community, social and personal service activities	6.3	5.9	6.8	–	6.1	4.6	7.1	–
Private households	0.6	0.8	0.5	–	0.8	1.0	0.7	–
Services other	0.7	0.2	1.1	–	1.1	0.2	1.7	–
	Organisation size (%)				Organisation size (%)			
0–4 employees	8.4	1.3	14.4	–	9.3	2.4	14.0	–
5–19 employees	17.5	8.6	25.0	–	19.2	8.0	26.3	–
20–199 employees	26.8	26.1	27.3	–	28.9	30.8	27.8	–
200–1999 employees	21.4	26.5	17.1	–	20.1	28.5	14.7	–
2000+ employees	25.9	37.5	16.1	–	22.5	30.7	17.3	–

Note: \*n.s. stands for 'not significant'. It is displayed in the relevant cell when the results of Pearson chi-square are not significant at the 0.5 level. Pearson chi-square controls for the hypothesis that the rows and columns in a two-way table are independent. For the variables income and average working time confidence intervals were taken into consideration.

Source: Own calculation based on weighted SOEP data, several years.

**Table 4: Working conditions in the public and the private service sector in 1997 and 2005, Germany\***

	1997			2005					
	Total	Public	Private	Public/ Private	Total	Public	Private	Public/ Private	
	Gross pay			Gross pay					
Average pay (full-time worker)	€2298.6	€2421.5	€2178.2	1.1	€2877.8	€3080.2	€2713.3	1.1	
Share that earns less than 60% of (overall monthly) median	19.5	11.94	26.1	0.5	26.4	13.7	35.7	0.4	
80/20 labour income quintile share ratio	2.4	2.0	2.7	0.7	3.1	2.3	4.0	0.6	
	Contract type			Contract type					
Permanent full-time	74.1	79.6	69.5	1.1	68.3	71.8	65.9	1.1	
Regular part-time (perm + fix)	22.4	19.8	24.6	0.8	25.7	24.8	26.3	0.9	
Marginal part-time (perm + fix)*	4.4	1.8	6.5	0.3	9.1	3.3	13.0	0.3	
Temporary contract	14.5	15.7	13.5	1.2	13.1	12.9	13.1	1.0	
TWA (Leiharbeit/Zeitarbeit) (can be either permanent or temporary)	Not asked	Not asked	Not asked	–	3.5	3.2	3.8	0.8	
	Working time			Working time					
Average hours (full-time) (excluding overtime)	40.7	39.8	41.7	1.0	41.0	40.5	41.5	1.0	
Average hours (reg. part-time) (excluding overtime)	22.4	24.1	21.3	1.1	23.9	25.5	22.9	1.1	

%>48h (excluding overtime)	7.5	4.8	9.8	0.5	7.4	6.5	8.0	0.8
% less than 15h (excluding overtime)	7.5	4.1	10.3	0.4	10.3	4.5	14.3	0.3
	Participation in training (1993)				Participation in training (2004)			
Training: yes	36.4	44.1	27.5	1.6	34.6	43.0	29.0	1.5
	Interest representation (1998)				Interest representation (2003)			
Trade union member	19.4	28.2	12.4	2.3	16.9	24.5	11.4	2.1
Professional association member	8.7	13.9	4.6	3.0	9.7	14.5	6.3	2.3
Works/staff council member	Not asked	Not asked	Not asked	–	4.0	6.2	2.5	2.5
	Employer pension scheme (1995)				Employer pension scheme			
Employer runs a pension scheme	27.7	34.9	21.1	1.7	Not asked	Not asked	Not asked	–
Entitled to company pension (company with pension scheme)	74.0	76.3	70.3	1.1	Not asked	Not asked	Not asked	–

Notes: \* Marginal part-time employment is currently defined as work with income of less than 400 euros. Until 2003 the income threshold was lower and there was an additional hours rule – only part-time work of fewer than 15 hours falls under the marginal employment category. Marginal workers – unlike their employers who pay a global contribution and a global tax - do not pay social security contributions and have only limited rights to social security. \*\* n.s. stands for 'not significant'. It is displayed in the relevant cell when the results of Pearson chi-square are not significant at the 0.5 level. Pearson chi-square controls for the hypothesis that the rows and columns in a two-way table are independent. For the variables income and average working time confidence intervals were taken into consideration.

Source: Own calculation based on weighted SOEP data, several years.



while the UK is reducing low pay and becoming more equal, Germany is increasing low pay and becoming less equal. What is more, the share of service sector workers earning a low wage is higher in Germany than in the UK for 2005, while inequality in the same year almost reached UK levels. The latter is most likely linked to the low wage employment introduced by the Hartz reforms, as well as the pressure on wage bargaining following from demands for concessions from employers.

In the public sector the share of permanent full-time employment is higher in both years but also declining more quickly: in 1997 this type of employment affected 79.6% of public sector workers, falling to 71.8% in 2005; the respective percentages for the private sector are 69.5% and 65.9%. Regular part-time contracts increased slightly for both sectors and are somewhat more common in the private sector. At the same time, marginal part-time contracts doubled for both sectors over the 8-year period, but occur almost four times more frequently in the private sector. Temporary contracts seemingly somewhat reduced in importance over time and affected about 13% of workers in both sectors in 2005. But only in 2005 was a separate question asked about temporary work agency employment, which in both sectors amounted to some 3.5%, more than cancelling out this apparent decline.

Full-time employees in the private sector work more hours than those in the public sector; but the difference between the two declined from 1.9 hours in 1997 to 1 hour in 2005. The percentage working more than 48 hours increased over time in the public sector and decreased in the private sector, the 2005 percentages being quite close: 6.5% for the public sector and 8% for the private sector. Reflecting its higher percentage of marginal part-time employment, the private sector also has a higher and increasing share of workers working fewer than 15 hours (10.3% in 1997 and 14.3% in 2005). In the public sector the share remained relatively small (4.1% in 1997 and 4.5% in 2005).<sup>6</sup>

As in the UK, in the public sector many more workers receive training than in the private sector – about 1.5 times as often. But this percentage is slightly declining in the public sector and slightly increasing in the private sector. As a result, for both sectors in 2005 the percentages receiving training are more or less equal to those in the UK. Overall trade union membership in Germany is declining and is substantially lower than in the UK, the difference being particularly large for the public sector where it was about half the UK figure

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<sup>6</sup> It is difficult to compare working hours in Germany with those in the UK because whereas in the UK they clearly exclude breaks, in Germany this remains unclear.

in 2005. German public sector workers were union members about twice as often as private sector workers in 2005, but membership is declining somewhat more quickly in the public sector. Finally, in 1997 the employers of about one-third of employees in the public sector ran a pension scheme, covering 76% of their workers. In the private sector the respective percentages were substantially lower, at 21.1% and 70.0%. No data are available on this for 2005.

In conclusion we can say that, overall, whereas working conditions are improving on most accounts in the UK, they are worsening on most accounts in Germany, reflecting the different reform paths. The two countries are now much more similar in terms of working conditions than they were in 1997. As in the UK, working conditions are better in the public sector than in the private sector in Germany, although the differences are often smaller than in the UK and decreasing. In Section 4 we will discuss for 2005 whether these differences are due to the sectors' different structural characteristics or whether there is also an independent public sector effect. First, however, we will discuss, again for 2005 only, the extent to which we can observe an accumulation of precarious working conditions.

### **3.3 Accumulation of precarious working conditions**

Within the context of the above description of (differences in) working conditions in the public and private sectors, here we briefly review the extent to which different factors that may make jobs precarious are accumulating and the extent to which they are doing so differently in the two sectors. Due to data restrictions (not all the variables for the given year derive from the same wave) and the aim of comparability, here we restrict ourselves to three dimensions that capture important dimensions of precariousness: 'low pay', 'very short or long working hours' and 'temporary contracts'.

Low pay is defined as 60% of the median hourly wage.<sup>7</sup> In line with the common definition of marginal employment, working times of fewer than 15 hours a week are defined as low hours. In our definition excessive working hours are weekly working hours exceeding 48 hours. Temporary contracts are all those concluded for a limited duration: for example, fixed-term contracts, temporary work agency contracts,<sup>8</sup> seasonal contracts and casual contracts.

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<sup>7</sup> This differs from the tables above in which we used monthly wages. Since we do not have reliable information on hourly wages in the data we divide the monthly wages by the usual working time.

<sup>8</sup> In Germany, temporary workers often have a permanent contract with the temporary work agency.

As far as the UK is concerned, 21.4% of jobs in the service sector are precarious on only one of these three dimensions (Table 5). This percentage is substantially higher in the private sector (24.6%) than in the public sector (16%), suggesting that precarious employment is more common in the private sector. This is further confirmed by the other two categories: in the public sector 3.2% of jobs are precarious on two of these dimensions and 0.1% on three dimensions. The respective figures for the private sector are much higher: 7.9% and 2.3%.

If we look at how the different precariousness dimensions combine the following picture emerges for the United Kingdom: while 86% of workers with a permanent job also work normal hours this is the case for only about 57% of those with a temporary contract (Table 6). About 41% of temporary workers, compared to 9% of permanent workers, have marginal working hours, while extensive working hours are not very common and concentrated among those with a permanent contract.

**Table 5:** *Difference between public and private sectors in precariousness indicators in the UK, 2005 (%)*

	Precarious in one dimension (% employed)*	Precarious in two dimensions (% employed)*	Precarious in three dimensions (% employed)*
Public	16.0	3.2	0.1
Private	24.6	7.9	2.3
Total	21.4	6.1	1.4

Note: \*The three categories are exclusive categories.

Source: Own calculation based on weighted BHPS data for 2005.

**Table 6:** *Working time among workers with permanent and with temporary contracts in the UK, 2005( %)*

	15–48 hours	>48 hours	<15 hours
Permanent job	86.26	5.22	8.52
Temporary job	57.25	1.67	41.08
Total	84.64	5.02	10.34

Source: Own calculation based on weighted BHPS data for 2005.

Also, while 11% of permanent workers have hourly wages below 60% of the median, this is true for about 35% of temporary workers including full-time students (about 15% of temporary workers excluding full-time students; Table 7). As to the combination of hourly wages and working time, approximately 9% of those with normal working hours (15–48) have hourly wages below 60% of the median, while the share stands at 36% among those with low hours and at 14.2% among those with excessive working hours.

In Germany just over one third of all jobs in the private service sector are precarious on one dimension, while in the public service sector this is true for 21% of contracts (Table 8). Differences between the public and private sectors are similarly pronounced if we look at combinations of two dimensions of precariousness; this is the case for about one fifth of workers

**Table 7:** *Low wages, contract type and working time in the UK, 2005 (%)*

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*Hourly wages below 60% of the median among:*

All workers	12.4
Permanent workers	11.0
Temporary workers	35.4
Temporary workers excluding students	15.4

*Hourly wages below 60% of the median among:*

Those with 15-48 hours	9.4
Those with fewer than 15 hours	36.2
Those with more than 48 hours	14.2

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*Source:* Own calculation based on weighted BHPS data for 2005.

**Table 8:** *Difference between the public and private sectors in terms of precariousness indicators in Germany, 2005 (%)*

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	Precarious on one dimension (% employed)*	Precarious on two dimensions (% employed)*	Precarious on three dimensions (% employed)*
Public	20.7	8.4	1.2
Private	36.1	21.3	1.7
Total	29.8	15.8	1.4

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*Note:* \*The three categories are exclusive categories.

*Source:* Own calculation based on weighted SOEP data for 2005.

in the private sector and about every 12th worker in the public sector. Similar to the UK very few people have jobs that incorporate all three dimensions of precariousness; the shares amount to 1.2% in the public sector and 1.7% in the private sector.

Taking into consideration combinations of the different dimensions of precariousness the following picture emerges for Germany: unlike in the United Kingdom there are hardly any differences in working hours between permanent and temporary workers. About three quarters of all services workers with temporary or permanent jobs have weekly working hours between 15 and 48 hours, whereas about 8% of both groups work very low hours and 7% work very high hours (Table 9).

**Table 9:** *Working time among workers with permanent and workers with temporary contracts in Germany, 2005 (%)*

	15–48 hours	48+ hours	1-15 hours
Permanent job	84.4	7.3	8.3
Temporary job	84.7	7.2	8.1
Total	84.4	7.3	8.3

Source: Own calculation based on weighted SOEP data for 2005.

On the other hand, clear differences emerge if we look at contract type and low wages. On average, about 22.7% of all workers have hourly wages below 60% of the median (Table 10). This is true for only 15% of permanent workers but for about 59% of temporary workers including apprentices, and

**Table 10:** *Low wages, contract type and working time in Germany, 2005 (%)*

*Hourly wages below 60% of the median among:*

All workers	22.7
Permanent workers	15.3
Temporary workers	59.1
Temporary workers excluding apprentices	38.4

*Hourly wages below 60% of the median among:*

Those with 15–48 hours	18.9
Those with fewer than 15 hours	49.9
Those with more than 48 hours	27.9

Source: Own calculation based on weighted SOEP data for 2005.

for 38% of temporary workers excluding apprentices. There also seems to be a strong link between weekly working hours and average hourly wages: while about 19% of those with normal weekly working hours have hourly wages below 60% of the median this is true for about 28% of workers with excessive working hours and about 50% of those with low working hours – many of these will be so-called mini-jobbers who according to German law are not liable to social security contributions if they earn less than 400 euros.

From the above it emerges that the figures are substantially higher than in the UK concerning the percentage of employed with one or two dimensions of precariousness, suggesting that precariousness as we measure it here is higher in Germany. Of course, this finding is due to the way we have defined our indicator. Temporary contracts are, for instance, more frequently used in Germany but this can at least partially be explained by, for example, the fact that dismissal protection is stronger in Germany than in the UK. But in both countries the incidence of precariousness is structurally higher in the private sector. This again begs the question of whether this is due to the sectors' structural characteristics or whether there is an independent public–private effect. This will be discussed in Section 4.

#### **4. Multivariate analysis**

Section 3 showed that private sector workers are on average more likely than their public sector counterparts to be in an employment relationship that is precarious in at least one dimension (hourly wages below 60% of the median, low or excessive working hours or temporary contract). They are also more likely to accumulate different dimensions of precariousness. Does this result prove true in a multivariate setting that controls for different profiles of both sectors, namely gender, age and educational composition, as well as economic activity (NACE) and organisation size?

Our main interest lies in the public/private sector effect on accumulation of precariousness. Nevertheless, to get a clearer picture of the three dimensions of precariousness, we first test in three separate regression models whether there are sectoral effects on low wages, low/excessive working hours and temporary contracts if we control for worker and organisation characteristics. In a second step, a regression model is calculated on a dependent variable that contrasts employment relationships that are not precarious at all with those that accumulate at least two dimensions of precariousness. If the coefficient on the sector variable turns out to be significant there is a genuine effect on precariousness deriving from ownership characteristics; if not, the differences in working conditions between the two sectors detected in the

descriptive section are due to varying characteristics of workers (gender, age, education) and organisations (sector of activity and size of organisation).

Since our dependent variables are all dichotomous we calculate a logistic regression model. Instead of beta coefficients, odds ratios are displayed and used for interpretation.<sup>9</sup> The overall fit of the models is measured by McFadden's Pseudo R<sup>2</sup> ( $p^2_{MF}$ ).<sup>10</sup> The multivariate analysis focuses exclusively on the situation in 2005.

#### 4.1 UK models

In the UK, for the three dimensions making up precariousness a genuine public/private sector effect can be detected only for low wages. The results of this model show that, controlling for worker and organisation characteristics, employees in the private sector are three times more likely to have low hourly wages (<60% of the median) than employees in the public sector (Table 11). The coefficients for the other independent variables in the model look as expected; there is, for example, a strong effect of being a woman on having low wages (not shown).

No significant sectoral effect is found in the models that look at low/excessive working time and temporary contracts, respectively. Controlling for the composition of the two sectors thus cancels out the sectoral differences on these indicators that we observed in Section 3. Looking at the other independent variables in the model, there is no significant gender effect on low/excessive working hours, which is probably due to the fact that women are more likely to work low hours and men are more likely to work excessive hours. The effects of being young and working in a small organisation (0–24 workers) on working low/excessive hours, on the other hand, are positive and significant, and there is a significant negative effect of being highly educated (not shown). In fact, the share of highly qualified is much larger in the public sector, while the shares of young people and of employees in small firms are much larger in the private sector. A similar cancelling mechanism operates in the temporary contracts model. Here, young people and those with medium qualifications – both groups predominately working in the private sector – are significantly more likely to

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<sup>9</sup> They are the exponential of the coefficient and can be interpreted in the following way: 'For a unit change in  $x$  the odds are expected to change by a factor of  $\exp(b)$ , holding all other variables constant.' For  $\exp(b) > 1$  the odds are  $\exp(b)$  times larger. For  $\exp(b) < 1$  the odds are  $\exp(b)$  smaller.

<sup>10</sup> McFadden's Pseudo  $r^2$  ( $p^2_{MF}$ ) cannot be interpreted analogous to  $r^2$  from linear regression. In practice,  $p^2_{MF}$  values are lower than  $r^2$  values; all one can say is that the higher  $p^2_{MF}$  the better the model fits (Kohler et al. 2001: 272–273).

**Table 11:** *The effect of working in the private sector on low wages, low/excessive hours and holding a temporary contract, UK, 2005 (odds ratio)*

	Low wages	Low/excessive hours	Temporary contract
Private sector	2.99**	1.25	0.72
P values	(0.000)	(0.136)	(0.119)
p <sup>2</sup> MF	0.2286	0.0786	0.1309
Prob>chi2	0.0000	0.0000	0.0000

*Notes:*

+ significant at 10%; \* significant at 5%; \*\* significant at 1%.

Besides the public/private sector effect, the models control for gender (reference: male), age (reference: 25–54 years), educational level (reference: low qualified), sector of activity (reference: public administration) and firm/organisation size (reference: 1000+ employees).

*Source:* Own calculation based on BHPS data for 2005.

hold a temporary contract than the reference groups. The gender effect on temporary contracts is – barely – not significant at the 5%-level and in favour of women; that is, women are less likely to hold a temporary contract than men (not shown).

We shall now accumulate the three dimensions of precariousness and contrast the extreme cases – those that are not precarious at all (according to our dimensions) and those that are precarious in at least two dimensions. Controlling for worker and organisation characteristics the effect of the private sector on accumulation of precariousness is not significant at the 5%-level (Table 12). But if we take full-time students out of the sample the private sector effect becomes positive and significant – regular workers (non-students) in the private sector are more likely than those in the public sector to accumulate precariousness. As expected, young people are significantly more likely to have precarious working conditions than prime age workers (odds ratio of 8.41), whereas the effect on older workers is not significant at the 5%-level. The effect on young people remains significant but decreases to odds of 2.6 when we take full-time students out of the sample. A highly significant effect also emerges for highly educated employees; they are less than half as likely as people with a low educational level to have a job that accumulates dimensions of precariousness. Concerning economic activities we use public administration and defence as the reference category since it most clearly represents the public sector. In all other sectors except financial intermediation the accumulation of precarious working conditions is more



**Table 12:** *Logistic regression model on precarious working conditions, UK, 2005*

Dependent variable: precarious in two or three dimensions (contrast not precarious)	Odds ratio
Private sector	1.50+
Female	1.15
REFERENCE: 25–54 years	
16–24 years	8.41**
55–64 years	1.50+
REFERENCE: low education level	
Medium education level	1.21
High education level	0.43**
REFERENCE: Public administration, defence	
Wholesale and retail; motor and household goods	7.42**
Hotels and restaurants	17.27**
Transport, storage and communications	3.92*
Financial intermediation	0.27
Real estate, renting, business act.	4.62*
Education	14.21**
Health and social work	5.90**
Other community, soc. and pers. service	8.49**
Private households	13.44**
REFERENCE: organisation size 1000+ workers	
0–24 workers	2.53**
25–99 workers	1.65
100–199 workers	1.11
200–999 workers	1.30
Observations	4220
p <sup>2</sup> MF	0.2925
Prob>chi2	0.0000

Note: + significant at 10%; \* significant at 5%; \*\* significant at 1%

Source: own calculation based on BHPS data for 2005.

likely, though not significantly so. Especially bad working conditions in terms of precariousness are observed in the hotels and restaurants sector (odds of 17.27), but also in education (odds of 14.21) and private households (odds of 13.44). The at first sight surprising effect for the education sector can be explained by the fact that, unlike in most other countries, in the United Kingdom there is a positive relationship between holding a temporary contract and level of education (compare European Commission 2005). The

organisation size effect is significant and positive only for organisations with fewer than 24 workers, contrasted to very large ones with more than 1,000 workers – the odds of accumulating more than two dimensions of precariousness are more than twice as high in very small than in very large organisations. The gender variable is not significant, which is due to a cancelling process that was demonstrated in the earlier regression analyses on the single indicators making up precariousness.

## 4.2 Interpretation of the German models

In Germany, we detect a genuine effect of the sector variable on both low wages and low/excessive working time if we control for worker and organisation characteristics, although the explanatory power of the latter model is very weak (Table 13). As in the UK, the effect of the sector variable on holding a temporary contract is not significant. The additional control variables in the wages model all look plausible (not shown). There are strong and significant age, gender, education and organisation size effects – women and young workers are much more likely to have low wages, whereas the likelihood of having low wages decreases with education and organisation size. Particularly badly off are the hotels and restaurants sector and the other community, social and personal services sector.

In the model on low/excessive working time, individual characteristics are for the most part not significant, which may be explained by the accumulation of very low and excessive working hours in one category for

**Table 13:** *The effect of working in the private sector on low wages, low/excessive hours and holding a temporary contract, Germany, 2005 (odds ratio)*

	Low wages	Low/excessive hours	Temporary contract
Private sector	2.23**	1.61**	0.81
P values	(0.000)	(0.000)	(0.126)
p <sup>2</sup> MF	0.2571	0.0568	0.2088
Prob>chi2	0.0000	0.0000	0.0000

*Notes:* + significant at 10%; \* significant at 5%; \*\* significant at 1%

Besides the public/private sector effect, the models control for gender (reference: male), age (reference: 25–54 years), education level (reference: low qualified), sector of activity (reference: public administration) and organisation size (reference: 2000+ employees).

*Source:* Own calculation based on SOEP data for 2005.

this variable (not shown). The sectoral effects, on the other hand, are almost all significant, all sectors being worse off with regard to low/excessive working hours than public administration. Again, hotels and restaurants fare worst, followed closely by education and other community, social and personal services.

The private sector effect on having a temporary contract is not significant; in fact, the descriptive results in Table 4 have shown that in 2005, unlike in 1997, there are no longer any significant differences in the extent of temporary contracts between the public and private sectors.

We now accumulate the precariousness factors again and calculate a logistic regression on the dichotomous variable that contrasts working situations that are not precarious in any of the three dimensions with those that are precarious in at least two.

After controlling for individual worker and organisation characteristics, the odds of accumulating precariousness are almost twice as great in the private than in the public sector and the results are highly significant (Table 14). As in the British case, young workers are considerably more likely to hold a precarious contract than prime age workers (odds of 16.33); this effect remains positive and significant with an odds ratio of 6.23 if we take apprentices out of the sample. The effect for older workers is not significant. Unlike in the United Kingdom, women in Germany are somewhat more likely than men to accumulate factors of precariousness. Furthermore, as expected, and in line with the UK results, the odds of accumulating dimensions of precariousness decrease considerably with rising education levels. In fact, employees with medium qualification levels are only half as likely, and those with high qualification levels only one quarter as likely as the low qualified to accumulate precariousness factors. Looking at economic sectors, with public administration and defence as the reference category, hotels and restaurants fare worst with odds of 4.24, followed by the education sector (odds of 2.20) and other community, social and personal services, with odds of 2.18. The effects for the other sectors are not significant in the German model. The ranking of economic sectors was similar in the UK regression model but effects with reference to public administration and defence were considerably stronger than in Germany. As in the UK, the odds of accumulating precariousness are larger in smaller organisations/firms. In fact, the odds are about three times greater in very small organisations/firms (fewer than 20 workers) and in medium sized ones (20 to 100 workers) compared with very large organisations/firms (2000+).

**Table 14:** *Logistic regression model on precarious working conditions, Germany, 2005*

Dependent variable: precarious in two or three dimensions (contrast not precarious)	Odds ratio
Private sector	1.78**
Female	1.33**
REFERENCE: 25–54 years	
16–24 years	16.33**
55–64 years	0.73
REFERENCE: low education level (ISCED 1–2)	
Medium education level (ISCED 3–4)	0.47**
High education level (ISCED 5–6)	0.24**
REFERENCE: Public administration, defence	
Wholesale and retail; motor and household goods	1.30
Hotels and restaurants	4.24**
Transport, storage and communications	1.17
Financial intermediation	0.67
Real estate, renting, business act.	1.35
Education	2.20**
Health and social work	1.27
Other community, soc. and pers. service	2.18*
Private Households	0.97
Services (no economic classification)	1.12
REFERENCE: organisation size 2000+ workers	
0–20 workers	3.33**
20–100 workers	2.70**
100–200 workers	1.34
200–2000 workers	1.33
Observations	4122
p <sup>2</sup> MF	0.3072
Prob>chi2	0.0000

*Note:* + significant at 10%; \* significant at 5%; \*\* significant at 1%.

*Source:* Own calculation based on SOEP data for 2005.

## **Conclusions**

The United Kingdom and Germany traditionally represent the ‘archetypical’ examples of the liberal market economy and the coordinated market economy, respectively, the two main varieties of capitalism distinguished in the literature. The differences between the two economies traditionally included very distinct ways in which the labour market was regulated, with the UK labour market being deregulated and individualised and the German labour market being more regulated by law as well as by collective agreements. But the characteristics of the labour market institutions of the two cases have changed in opposite directions in the past decade: the UK has demonstrated a process of (limited) re-regulation and Germany one of progressive deregulation. As a result, the two cases have become more similar over time, even though important differences remain, in particular where the coverage of collective agreements is concerned. This approximation concerns labour market institutions, but also the weight of the service sector in the labour market and the share of services that belong to the public and private sectors.

As far as the service sector is concerned, in both cases important differences exist between the public and the private sector, although they have again changed somewhat over time. In terms of structure, in both cases the educational level of the public service sector is higher, the percentage of young people is lower and the organisations are on average larger. A major difference is that in the UK the share of women is higher in the public sector, while in Germany this is the case in the private sector.

In terms of working conditions, in both cases the public sector generally performs better. In both countries, in the private sector average pay is substantially lower, the share of workers on low pay is higher and pay is less equally distributed. But whereas in the UK low pay is diminishing and equality is increasing, in Germany the opposite is true. Similarly, in both cases the working time of full-time employees is higher in the private than in the public sector, but in the UK average working time is declining while it is increasing in Germany. Also, in both cases in the private sector there is a higher percentage working more than 48 hours or fewer than 15 hours than in the public sector. Again in both cases, the public sector provides more training to employees, is more likely to offer a company pension scheme and scores higher on trade union membership. One difference between the two cases here is that in the UK the share in total employment of permanent full-time contracts and of part-time contracts is fairly stable over time and fairly similar between the public and private sectors, while in Germany the share of

permanent full-time contracts is declining (and now substantially below the UK level) and that of part-time is increasing (and now almost at the UK level). What is more, the share of marginal part-time contracts has rapidly increased in Germany, due to the Hartz reforms.

Important differences between the private and public sector also exist in both cases when we move from singular indicators to composite indicators of precarious employment, an exercise limited to 2005. Using three dimensions of precariousness (low pay, very short or long working hours and temporary contracts), in both countries in the private service sector the percentage of workers affected by one, two or all three of these dimensions of precariousness is higher than in the public sector. There is, however, a major difference between the two cases: in Germany the percentages of employees affected by one and especially by two dimensions of precariousness are much higher than in the UK; and the differences between the public and the private sector are much bigger.

Separate regression analysis for each dimension of precariousness shows that in the UK there is a strong and significant independent public/private sector effect on the likelihood of employees having low wages, with workers in the private sector having a significantly higher likelihood. This effect does not exist for the other two dimensions. In Germany such a significant independent public/private sector effect exists for both the wage dimension and the low/excessive working time dimension. When contrasting the cases that are not affected by any dimension of precariousness with those that are precarious on at least two dimensions, in both countries there is a significant public/private sector effect, although in the UK only when we take full-time students out of the sample.

Hence, despite the different models of capitalism, in both countries working in the private service sector significantly influences the likelihood of having precarious employment. This suggests that the public/private sector effect exists independent of what model of capitalism we are discussing. Taking into consideration the two countries' labour reform paths over the last decade, it may even be the case that as far as the labour market is concerned the two cases can less and less be considered two radically different models of capitalism.

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## **Public sector pay gaps and skill levels: a cross-country comparison**

### **Introduction**

The analysis of wage differences between the public and the private sectors has important implications for a better understanding of the welfare consequences of public service privatisation. Wages represent the main source of an individual's well-being; because of institutional and structural differences, we may expect that they will differ between public and private employment, even for workers with similar characteristics. Working conditions and pay structures in the private sector may represent what former public workers may expect should privatisation transfer the service they helped provide to the private sector. This is particularly important when – as has recently been the case in several European countries – reforms involving the contracting out and privatisation of public services are accompanied by labour market reforms, for example towards more wage bargaining decentralisation in the public sector.

In many OECD countries public sector employment accounts for a significant share of both total employment and public sector expenditures, and is an important factor in economic performance. In general, public sector jobs are characterised by different working conditions and produce goods and services that do not necessarily have private substitutes. Moreover, as an employer the public sector often has a monopsonistic position in the labour market and it offers lots of high-ranking jobs. Moreover, both the institutional setting of human resource management and pay determination are very different between the public and private sectors.

All these features may affect labour market functioning and performance, from both a macro and a micro perspective. In the aggregate, while – as

Keynesian tradition predicts – public sector job creation can be used as a countercyclical tool to reduce unemployment and stimulate the economy during recessions or economic stagnation, recent evidence suggests that, because of higher wages in the public sector, public sector job creation is not necessarily ‘additive’, as it may crowd out private sector jobs. Among other things, this may have important implications for labour market functioning, since a positive public wage premium may attract onto the labour market a number of individuals who would not otherwise have participated. It may also induce some workers to lengthen their unemployment spell while ‘waiting’ for a public job. As a result, public employment typically increases both participation and equilibrium unemployment rates. This is particularly true when public enterprises provide not only ‘pure’ public goods, but also goods (and services) for which there are also private producers (Algan et al. 2002).

At the micro level, differences in both wages and working conditions between sectors – a more compressed and flat pay structure in the public sector, as well as better working conditions and lower probability of job loss – may affect the public sector’s ability to select, motivate and retain high-productivity workers, so preventing it from offering efficient and high quality services to the community.

In this chapter, we focus on the micro level and investigate public–private pay determination, using French, UK and Italian microdata. By focussing on different countries we exploit institutional differences to gain insights into the process of pay formation.

Of course, several features that are missing from a simple pay comparison might also be relevant in the explanation of differences between public and private jobs; for example, other working conditions and features of the employment relationship that matter for workers’ well-being, such as job security and health and safety at work, may play a role (Hamermesh and Wolfe 1990; Sandy and Elliott 1996). Also, workers might be heterogeneous across sectors in a non-random way with respect to some unmeasured characteristics, such as a preference for public sector work, a desire to be a civil servant/state employee or to work in the non-profit sector. While we acknowledge the caveats that these features imply, we analyse public–private differences as measured by net hourly wages and focus on pay differentials between the public and private sectors that emerge across the full spectrum of wage distribution. The advantage of using this wage measure is that, in contrast to monthly and/or gross wages, it measures the available income for consumption for a unit of labour, as it is not influenced by differences across countries as regards tax schedules and hours worked.

Nonetheless, comparison of public–private wages is complicated by a number of factors. First, some occupations (for example, teachers) are to some extent *sui generis* as they are present in one sector, without a close counterpart in the other. Second, the mean, but also the shape of the wage distribution is different across sectors. Finally, earnings vary according to several characteristics – for example, skill and sectoral composition – which are differently distributed across sectors and we want to compute wage statistics free of these compositional effects.

The aim of this chapter is thus to analyse public–private sector gaps not only in average wages, but also looking at their overall distribution across sectors. We compute these statistics separately for the three countries under scrutiny, as well as by skill levels (bluecollar, whitecollar, managerial) and sector of employment, for both the whole economy (excluding agriculture) and the sub-sector of services. We will also analyse in more detail specific services, such as education and health care, which are available in both sectors.

Even after controlling for observed characteristics, we find an overall positive wage differential for public sector workers. But this differential is sensitive to the choice of quantile and the premium varies with skill levels. We argue that the decomposition of predicted wage gaps at different quantiles provides a more accurate set of measures for the size of the part of the wage gap that is attributed to different returns to skills between the public and private sectors. In general, the public (private) sector pays more (less) in the lower part of the wage distribution than the private (public) sector, whilst the opposite is true for the upper part. Finally, when the wage differential is decomposed by quantile, a significant portion is explained by observed characteristics (over 60 per cent on average) and is generally increasing over the wage distribution. Symmetrically, the unexplained part due to the wage differential between public and private sector decreases and becomes close to zero at the highest quantiles, suggesting that differences in unobserved characteristics are more important at lower quantiles.

## **1. Institutions, wage determination and the structure of collective bargaining**

During the late 1990s, significant reforms were introduced in several European countries in both the private and public sectors to allow both employment and wages to be more flexible and reactive to productivity and business conditions. In the private sector, reforms concerned recruitment procedures and temporary contracts, as well as an increased role for decentralised (firm-level) bargaining. In the public sector, reform mainly

concerned the so-called ‘privatisation’ of employment relations, which was designed to make job conditions and wage setting more like those in the private sector and more sensitive to productivity gains (Elliot et al. 1999). The purpose was to encourage innovation in organisational structures, methods of service delivery and pay structures to improve efficiency and reduce costs. This decentralisation had two main aspects. The first was related to the progressive outsourcing of public industries and services, with a significant reduction of public-owned companies and the public monopoly in some formerly protected industries (such as energy and telecommunications). The second concerned reform of the terms and conditions of employment in the public sector, such as recruitment and careers – based both on open competition to fill job vacancies and massive resort to temporary contracts, even in the public administration – mobility, job classification systems and compensation schemes.

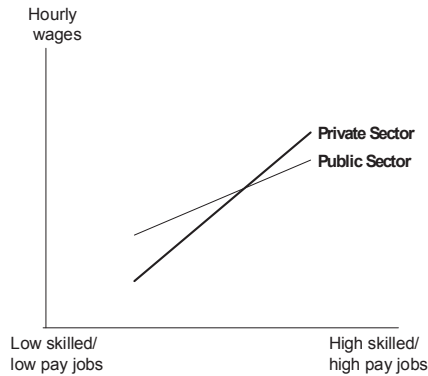
But in many countries this process is still far from complete, and despite the substantial changes introduced in recent decades to increase both competition and efficiency in the public sector, in many countries significant differences still exist with the private sector, especially concerning the rules governing terms and conditions of employment and pay. The latter range from the criteria adopted in each sector for selecting, recruiting and promoting workers, and adjusting wage levels, to wage profiles, career advancement and the role played by collective bargaining and the trade unions.

The sectoral and skill dimensions are among the most important sources of variation in the pay gap; for example, concerning the skill component, several studies suggest that in many countries the pay structure is more compressed in the public sector, as shown in Figure 1 (Bender and Elliott 1999; Bazen et al. 1998; Katz and Kreuger 1991; Lucifora 1999).

This is the result of several features that impact differently on the private and the public sectors. A wider union presence and more effective use of union power – which protect low-paid workers – as well as ‘fair’ rates of pay offered by the state (as a ‘good employer’) to the least skilled, all tend to reduce wage dispersion in the lower part of the distribution in the public sector as compared to the private (Bender and Elliott 1999).

Conversely, the rates paid to the most senior public servants are often reported to be substantially lower than those paid to individuals with comparable skills and responsibilities in the private sector: public opposition to high rates of pay for public servants seems to account for this feature (Katz and Kreuger 1991; Lucifora 1999). Whilst the combined effects of these features are conducive to a much flatter public wage structure in comparison

**Figure 1:** *Stylised wage profiles in the private and public sectors, by skill*



to that of the private sector (as shown in Figure 1), there is an additional effect due to the larger proportion of low-paid individuals in the private sector, in which monopsonistic effects – that is, firms’ ability to set wages below or just at the level of labour productivity, without sharing the rents with workers – have been documented as larger (Bazen et al. 1998).

The economic consequences of this imbalance, taking the private sector as the reference sector, are that the public sector pays more than the opportunity wage for unskilled and low-paid labour. In contrast, on the hypothesis that labour market failures are less relevant for skilled individuals in the private sector, the rates paid to high skilled workers in the public sector appear to be less than what would be needed to attract, retain and motivate such workers (see Nickell and Quintini 2002). Clearly, the underlying distortions in relative pay, on both sides of the distribution, make human resource management particularly difficult.

For the private sector, there exists substantial research on the effects of different centralisation/coordination arrangements across countries on both wages and employment (Calmfors and Driffil 1988). In general, both centralised and decentralised systems have a better labour market and economic performance than intermediate ones. Much less evidence exists on the effects on public–private pay gaps of differences in bargaining procedures and wage-setting policies in the public sector. A notable exception is the study by Dell’Arlinga and Lanfranchi (1996), who provide a combined analysis of the institutional framework in both the public and private sectors; they suggest that in this context three possible main outcomes can be identified:

1. A centralised pay system, that is, one in which wages are set centrally in both the private and the public sectors. One example is France, where the main difference is that private sector bargaining establishes industry minima for wages and employment conditions, whilst in the public sector the trade unions also take part in national wage negotiations but the outcome is not legally binding for the government.<sup>1</sup> In practice, civil servants are not allowed to engage in collective bargaining and their pay is set by statute, with the same pay scales applying to all public sector workers (Guillotin and Meurs 1999).
2. A two-regime system, in which pay policy is decentralised in one sector (typically the private sector) and centralised in the other. This is the situation in Italy, where private wages are set at industry level by collective bargaining, and public wages at the central level, with only minor reforms in the recent past towards greater decentralisation in the public sector (Dell'Aringa and Della Rocca 1996).<sup>2</sup>
3. A decentralised pay system, in both the public and private sectors. This is the case in the UK, where individual public agencies can decide about recruitment and pay scales, and private pay is used as reference for the public sector. In more detail, civil servants/public employees in the UK are covered by a variety of different arrangements, including Review Bodies, index linking, and decentralised as well as centralised collective bargaining. In recent years, policies such as contracting out and competitive tendering have also contributed to a progressive 'privatisation' of pay setting procedures (Bender and Elliott 1999).

In the UK, private sector pay is used as a reference for public sector wage determination (at least in part); in France and Italy, however, the reference is, generally speaking, the cost of living and public budget conditions. In this context, differences between countries in the rules governing public and private sector employment are likely to affect the structure and size of the public sector pay gap. In Italy and France public employees are still generally recruited on the basis of open, competitive examinations – for which a given

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<sup>1</sup> Collective bargaining was extended as a result of the so-called 'Auroux law' in 1982.

<sup>2</sup> Public sector pay negotiations cover each of the eight functional sub-sectors defined as a result of the 1993 civil service reform, in which an independent agency (*Agenzia per la RAppresentanza sindacale nel pubblico impiego* – ARAN) was charged with negotiating for public sector employees. The police and armed forces, university professors and other academic staff, judges and prosecutors, as well as senior civil servants are excluded from these negotiations.

level of education is required – and, once hired, enjoy lifetime contracts in which seniority plays a major role.<sup>3</sup>

In general, public employees in France and Italy cannot be made redundant, except for misconduct, and the statutory terms apply regardless of whether the individual is employed at national, regional or local authority level. In the UK, in contrast, the process of decentralisation has led, on the one hand, to significant variations in both the recruitment criteria and pay levels of civil servants across different departments within the public sector, and on the other hand, to a number of services being progressively contracted out.

In the private sector, regulation is generally much lower in all countries. Italy and France, however, are still characterised by fairly strict employment protection measures, extensive collective agreement coverage and a centralised wage determination system; in the UK, in contrast, wage determination is highly decentralised, unions are weaker and employment protection is fairly low (OECD 2000). As might be expected, pay inequality is greater and low-paid employment is more widespread in the UK as compared to both France and Italy (OECD 1996; Lucifora 2000).

The different institutional settings that govern public sector wage determination in all three countries provide an interesting source of variation for the analysis of how collective bargaining practices, private sector pay and other factors influence public–private wage differentials.

## **2. Stylised facts and descriptive evidence**

In this chapter we use the 2001 wave of the European Countries Household Panel (ECHP) for the UK, France and Italy.<sup>4</sup> This archive is unique for our purposes as it allows detailed international comparisons. Indeed, a close questionnaire was used in all countries participating in the survey.<sup>5</sup> Besides wages, we have information on standard human capital variables (that is,

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<sup>3</sup> In Italy, however, recruitment policies in the public sector have changed slightly in recent years. Indeed, because of the need to reduce persistently high levels of public deficit and debt through strict budget discipline, public sector employment has been subject to the so-called ‘*blocco del turnover*’, that is, a prohibition on hiring new workers on permanent contracts unless they replace workers who retire. This has increased temporary contracts in the public sector relative to the private one (see Dell’Arling et al. 2007).

<sup>4</sup> This is the most recent available wave of the ECHP Survey. The follow-up data set, EU-SILC, cannot be used for the purposes of our study as it does not include a public–private sector identifier in the user data base.

<sup>5</sup> In particular, after the first three ECHP waves, the UK decided to output-harmonise its existing panel study (BHPS) to ECHP.



education, gender, age), occupation, region of residence, gross earnings, hours worked and contract type, as well as a detailed classification of employment sector and workers' public–private status.

In contrast to other surveys, the information about public–private affiliation comes from a different question than the one on employment sector; that is, the information on public employment does not exactly overlap with the sector identifier. As a result, the definition of public employment is enlarged as it includes not only Central and Local Administrations, Health and Education (the group traditionally termed 'civil servants'), but also employment in firms financed by the state, but operating in the market. Thus, public employees can also be found in sectors such as manufacturing (if they work in public companies) or other services, such as communications. A detailed description of the sectoral composition of public and private employees is given below.

We restrict our samples to non-agricultural paid employees aged from 15 to 65 who normally work at least 15 hours a week. Given our selection criteria, we end up with approximately 3800–4000 observations for each country. In Table 1, we report the main features of the data on personal characteristics and job attributes, and compare public and private sector workers. Descriptive statistics show that, on average, public employees are older, better educated and work shorter hours in all countries. The public sector employs more females and a larger proportion of clerks. Moreover, some of the differences between countries in terms of structure of economic activities and labour market characteristics emerge from the data. Not surprisingly, the proportion of public employees is greater in Italy (35%) and France (32%) than in the UK (25%). Concerning job attributes, Italy possesses the most traditional economic system, with the largest share of bluecollar workers (36%) and clerks (25%), and a smaller proportion of teachers and managers.<sup>6</sup>

Looking at sectoral differences, some public sector features differ quite substantially across countries, and especially between the UK on the one hand, and France and Italy on the other; Table 1 shows, for example, that public employment in the former is concentrated almost exclusively in the service sector. In contrast, a high incidence of public employees is found in firms operating in manufacturing industry in the two Continental countries. In more detail, in all countries the bulk of services traditionally offered by the state (public administration and social security, education and health care)

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<sup>6</sup> Occupational categories are defined as follows: bluecollar and service workers, clerks, professionals and teachers, managers.

**Table 1:** Sample means: personal characteristics, job attributes and sectoral composition

Variables	France		Italy		UK	
	all	private	public	all	private	public
Public sector	0.32			0.35		0.25
<b>Personal characteristics</b>						
Age	39.38	38.08	42.14	39.19	36.77	43.68
Low secondary education or less	0.55	0.60	0.46	0.36	0.44	0.21
High secondary educ.	0.11	0.11	0.12	0.50	0.47	0.54
Tertiary education	0.33	0.29	0.42	0.14	0.08	0.24
Female	0.47	0.42	0.57	0.42	0.37	0.51
<b>Job attributes</b>						
Bluecollar & service workers	0.43	0.50	0.28	0.48	0.62	0.24
Clerks	0.19	0.18	0.21	0.25	0.22	0.29
Professionals & teachers	0.33	0.25	0.49	0.25	0.15	0.44
Managers	0.05	0.07	0.03	0.02	0.02	0.02
Permanent contract	0.90	0.90	0.90	0.88	0.86	0.92
<b>Sectors</b>						
Industrial sector	0.28	0.39	0.05	0.32	0.47	0.04
Mining, electricity, gas & water	0.07	0.03	0.75	0.06	0.05	0.32
Service sector	0.72	0.61	0.95	0.68	0.53	0.96
Other services	0.42	0.69	0.06	0.31	0.58	0.70
Transport & comm.	0.09	0.07	0.10	0.10	0.13	0.07
Pub. admin. & social sec.	0.14	0.02	0.30	0.16	0.01	0.32
Education	0.15	0.03	0.31	0.19	0.03	0.35
Health care	0.15	0.12	0.20	0.14	0.08	0.20
Personal & social services	0.06	0.08	0.03	0.10	0.16	0.04
n. obs	3 779	2 566	1 213	3 831	2 486	1 345
				4 101	3 058	1 043

Note: All the variables are in percentage points except age, which is measured in years.

accounts for more than 80 per cent of total public employment in France, and more than 85 per cent in Italy and the UK. The private sector, on the other hand, is concentrated in the 'other services' group (which includes wholesale and retail trade, hotels, real estate and business activities, and financial intermediation), as well as in personal and social services.

A finer disaggregation of public–private differences in the composition of employment by sector is presented in Table 2, which reports the employee share of the two groups for each macro-sector (industry and services), and for a number of sub-sectors.

**Table 2:** *Percentage distribution of public–private employees, by employment sub-sector*

	France		Italy		UK	
	private	public	private	public	private	public
Service sector	57.51	42.49	50.48	49.52	66.46	33.54
<i>of which:</i>						
Other services	93.77	6.23	95.19	4.81	97.87	2.13
Transport & communications	48.05	51.95	65.37	34.63	83.83	16.17
Public administration & social security	7.57	92.43	4.43	95.57	2.11	97.89
Education	10.92	89.08	8.59	91.41	17.65	82.35
Health care	45.52	54.48	28.22	71.78	34.47	65.53
Personal & social services	77.27	22.73	81.82	18.18	78.79	21.21
Industrial sector	94.29	5.71	95.89	4.11	98.55	1.45
<i>of which:</i>						
mining, electricity, gas & water	36.99	63.01	78.38	21.62	95.92	4.08

*Note:* In each country, the rows sum to 100.

Thus, while public employees account for half of the employment in services in Italy, their share is lower in France (42.5 per cent), where they are more present in the industrial sector, particularly in energy (63 per cent). In the UK, the lower incidence of public employees is reflected in their small share in manufacturing, while in the service sector they represent only one third of total employment. In services, public employees always account for about 90–95 per cent of public administration and social security. As regards other

sub-sectors in which there might be competition between public and private producers, the incidence of public employment in Italy is higher than in the other two countries, especially in the education and health care sectors, in which more than 90 and 70 per cent, respectively, of workers are employed by the state. Also in France and the UK the share of public workers in such industries is greatest, but their incidence is lower, especially in the health care sector (54 per cent in France; 65 per cent in the UK). Concerning transport and communications, not surprisingly the share of public employees is higher in France, where, traditionally, several state-controlled firms operate. In contrast, in Italy, where recent reforms privatised the major company in this industry, the share of public employees in this sub-sector is relatively small (34 per cent); the same is true for the UK (16 per cent).

As regards sectoral wage structures, Table 3 shows that the average net wage in the UK is almost €800 higher than in Italy (€1062), and €300 higher than in France (about €1500). But these numbers are not directly comparable as they are not expressed in purchasing power parity units. Concerning sectoral differences, public employees earn higher wages, whether measured on a monthly or an hourly basis.<sup>7</sup> Wages across sectors also differ in terms of dispersion; in particular, the standard deviation of hourly wages appears to be wider in the UK and France, and much lower in Italy, especially in the private sector.

Since wage dispersion is not the same in the public and private sectors, a simple comparison of (conditional or unconditional) mean earnings cannot provide a complete description of public–private wage differences, as they are not expected to be constant along with the wage distribution. Moreover, if the degree of wage dispersion varies across countries, restricting the analysis to mean wages may be even more problematic. As a consequence, it is preferable to apply techniques that account for public–private differences in wage distribution as a whole. We start by inspecting wage distribution across sectors with a non-parametric kernel density estimator to fit the density of (log) hourly wages. The plots are given in Figure 2, separately for each country. Next, in the econometric analysis, we investigate the extent to which the (conditional) public pay gap varies at different quantiles of the wage distribution.

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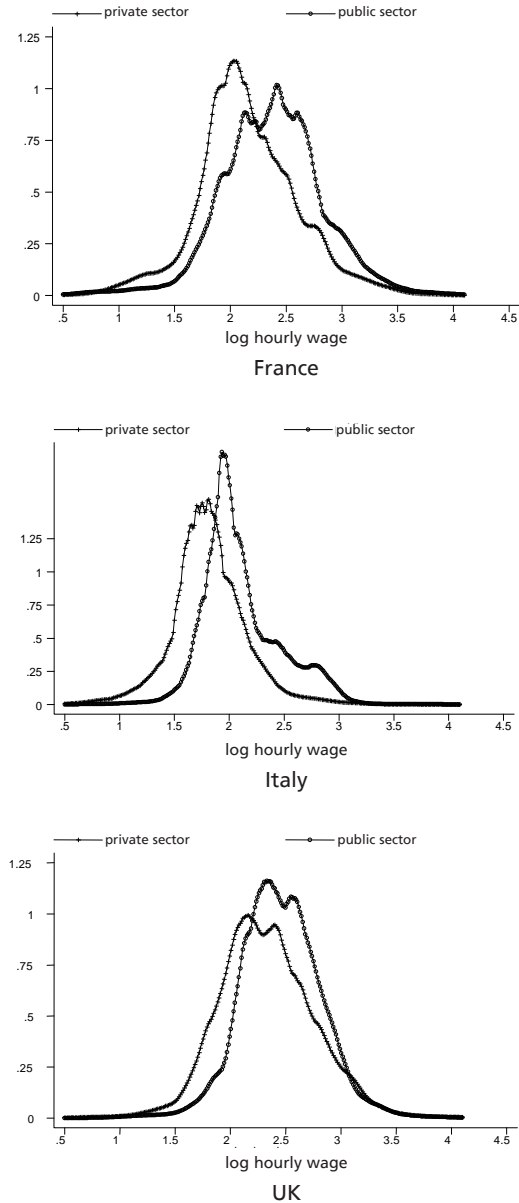
<sup>7</sup> In 2001, parities for the euro were fixed within the framework of Economic and Monetary Union (EMU), and this is what we used for France and Italy; as far as the UK is concerned, we used the average exchange rate for 2001 (provided by ECHP).

**Table 3:** Average wages in the public and private sectors, by country

Variables	France			Italy			UK		
	all	private	public	all	private	public	all	private	public
Weekly hours	37.25	37.96	35.76	37.43	39.19	34.19	39.79	40.63	37.33
(st. dev)	7.72	7.60	7.75	7.78	7.43	7.35	11.55	11.54	11.22
Monthly wage	1 536	1 480	1 654	1 062	1 014	1 152	1 857	1 853	1 869
(st. dev)	922.66	973.75	791.42	450.33	443.24	449.81	1 071.4	1 117.07	925.03
Hourly wage	10.35	9.60	11.94	7.33	6.54	8.79	11.62	11.30	12.55
(st. dev.)	5.60	5.22	6.02	3.31	2.78	3.69	5.70	5.72	5.53
log hourly wage	2.22	2.14	2.37	1.91	1.81	2.11	2.36	2.32	2.46
n. obs	3 779	2 566	1 213	3 831	2 486	1 345	4 101	3 058	1 043

Note: All monetary values are expressed in euros (2001).

Figure 2: Distribution of log hourly wages in the public and private sectors



Estimated densities confirm that, especially in Italy and the UK, (log hourly) wages in the public sector have both a higher mean and a lower dispersion as compared to the private sector. Moreover, both the shape of the distributions and the differences between sectors are specific to each country. We also compute the average public–private wage differential, measured by the difference between the means of the natural logarithms of public and private wages.<sup>8</sup> The results are given in Table 4 and indicate that the pay gap between the public and private sectors differs across countries; in France, Italy and the UK, it is equal to 23, 29 and 13 per cent, respectively. All these coefficients are statistically significant at the 5 per cent level.

Comparing (gross) pay levels across the public and private sectors is not without problems. The greater the extent to which the public sector undertakes activities that are not found in the private sector, and the lower the substitutability of the goods and services provided by each sector, the more difficult is comparability and the greater the scope for pay differences across sectors. Moreover, since the vast majority of doctors, nurses, teachers, policemen and judges are employed in the public sector, while insurance salesmen, assembly workers, and stock and bond dealers work exclusively in the private sector, average qualifications and job contents are likely to differ and hence comparison of (unconditional) pay levels across sectors can prove misleading.

With these caveats in mind, we also present estimates of the wage gap by sub-groups of workers, as defined by occupation level or employment sector. From Table 4 we see that the public sector premium is, in general, higher for bluecollar workers (14–19 per cent) than for clerks, with the exception of France, where the two categories of workers show approximately the same wage difference. Clerks in Italy and the UK also earn more in the public sector, but the premium is only about 5 per cent. As regards teachers and professionals, the premium from public employment is substantial in both France (16 per cent) and Italy (26 per cent), while in the UK they earn the same in the two sectors. Finally, the return to public employment for managers is about 12–16 per cent, without significant differences between countries. Although in principle one might expect that a manager would earn more in the private than in the public sector, our result may be due, on the one

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<sup>8</sup> Note that this way of expressing the public–private wage gaps – in common use in the empirical literature – is only an approximation. Indeed, the true wage differential, which is the  $[(\text{mean wage public} - \text{mean wage private}) / \text{mean wage private}]$  is the first term in the Taylor expansion of  $[\text{mean } \ln(\text{wage public}) - \text{mean } \ln(\text{wage private})]$ .

hand, to compositional effects – for example, higher seniority levels for public sector managers – and on the other to the fact that top managers in the private sector with very high salaries may be unlikely to participate to the survey or to report their true salary.

Table 4 also disaggregates the premium by sector, with a finer decomposition within services. We observe that in France and the UK public workers earn relatively more in industry, while in Italy the opposite is true.

**Table 4:** *Raw public–private wage differences, by sector and occupation (percentage points)*

	France coeff	Italy coeff	UK coeff
All	0.23	0.29	0.13
By occupation			
Bluecollar & service workers	0.14	0.19	0.14
Clerks	0.14	0.05	0.06
Teachers and professionals	0.16	0.26	0.01
Managers	0.12	0.16	0.14
By sector			
Industry	0.31	0.12	0.26
Services	0.25	0.29	0.16
<i>Other services</i>	<i>0.30</i>	<i>0.21</i>	<i>0.14</i>
<i>Transport &amp; comm.</i>	<i>0.25</i>	<i>0.06</i>	<i>-0.05</i>
<i>Public admin. &amp; social security</i>	<i>0.02</i>	<i>0.10</i>	<i>0.20</i>
<i>Education</i>	<i>0.35</i>	<i>0.22</i>	<i>-0.02</i>
<i>Health care</i>	<i>0.25</i>	<i>0.18</i>	<i>0.23</i>
<i>Personal &amp; social services</i>	<i>0.34</i>	<i>0.18</i>	<i>0.22</i>

When sub-sectors within services are considered, the scope for interpreting the premium for persons employed in the public administration is very limited – they are almost all public workers – and it is more interesting to look at results for sub-sectors such as education and health care. Table 4 indicates that in all countries there is a positive premium for public workers employed in the health care sector, ranging from 18 to 25 per cent. In education, the premium is positive and substantial (22 and 35 per cent, respectively) in Italy and France (where both the absolute number and the share of public workers is higher, as is, presumably, their bargaining power), and negligible and, if anything, negative in the UK. In contrast to France and Italy, in the UK there is no evidence of any robust premium attached to public



employment in the service sub-sectors considered, except for health care, personal services and ‘other’ services.

### 3. Public–private pay differences and skill levels

The descriptive evidence suffers from several limitations, however. In particular, in the calculus of wage premia we did not account for the differences between public and private employees in a number of individual and job characteristics – such as age and education – which also matter for wages. Thus, a more precise measure of the public wage gap can be obtained once we correct the premium for differences in the nature of public and private jobs, and in terms of the characteristics of workers in the two sectors. In this connection, Table 5 reports estimates that account for heterogeneity in the two sectors by conditioning the computation of the premium on a set of personal and job characteristics. In general, as shown in Table 5, controlling for a larger set of variables, overall pay differentials are now between 9 and 15 per cent, depending on country. In most cases, the coefficients are statistically significant.<sup>9</sup>

Thus, controlling for observable characteristics reduces both the estimated gap and differences across countries. In other words, as we might expect, the variability of the raw premia between countries was partly due to their heterogeneity in the composition of employment and in the structure of jobs. In particular, while the descriptive evidence suggested that Italy was clearly associated with the highest premium, regression results indicate that this was simply a compositional effect: Italian public employees have on average ‘better’ observable characteristics that *di per se* guarantee higher wage returns.

Moreover, in contrast to the abovementioned descriptive results, we find that the premium is higher among low level occupations (bluecollar and service workers) and lower among managers.<sup>10</sup> Indeed, in the latter group the premium is statistically different from zero only in the case of the UK. In contrast, teachers and professionals, *ceteris paribus*, receive a positive

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<sup>9</sup> A value of statistical significance lower than 5 per cent indicates that, when we observe a positive gap in our sample, the probability of no systematic wage differences across sectors in the total population of employees is less than 5 per cent, that is, very unlikely. The lower the probability, the higher the informative value of the statistics computed from sample data.

<sup>10</sup> There is no straightforward explanation of the rather counterintuitive result for managers. Perhaps it is due to the higher concentration of public than private managers in sectors in which the average wage is higher and/or to their better unobserved attributes (self-selection problems).

**Table 5:** *Estimates of the public sector wage gap (percentage points)*

	Overall	Occupation				Sector	
		Bluecollar & service work	Clerks	Teachers & professionals	Managers	Industry	Services
France	0.15***	0.20***	0.09***	0.11***	0.04	0.20***	0.14***
Italy	0.10***	0.13***	-0.03	0.15***	0.06	0.08**	0.09***
UK	0.09***	0.21***	0.03	0.01	0.11**	0.13	0.09***

*Notes:* Results from OLS regressions including a public sector dummy and a set of controls (education dummies, age, age squared, female dummy, permanent contract dummy, and occupational and sector dummies whenever needed). Statistical significance: \*\*\* = 1 per cent; \*\* = 5 per cent; \* = 10 per cent.

premium only in France and Italy, and clerks only in France. Concerning the heterogeneity of the wage differential between sectors, in general the premium is higher in industry than in services, except in Italy, where the difference is negligible.

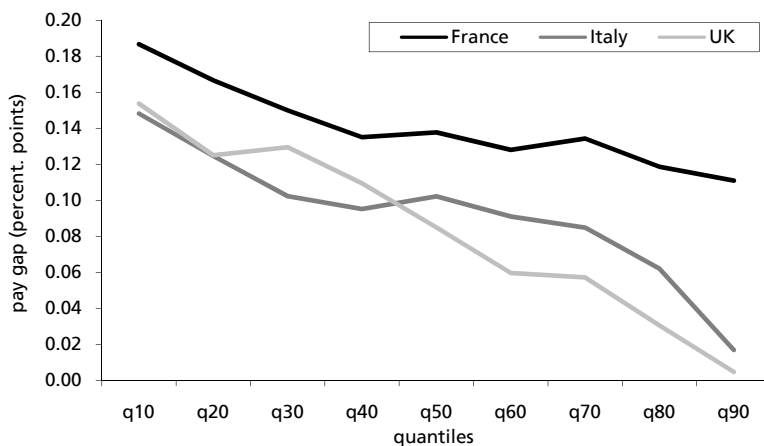
Given the differences in the distribution and dispersion of pay between the sectors documented in Figure 2, the standard approach based on analysis of the conditional mean of the distribution may lead to overly restrictive results and has been criticised in a number of studies. For the US, Poterba and Rueben (1994) suggest that the wage distribution for the public sector is much less dispersed and propose alternative methods for analysing pay differentials based on quantile regression. In the UK, Blackaby, Murphy and O'Leary (1999) and Disney and Gosling (1998) show that the public sector pay gap varies with the distribution, being higher for the lowest deciles than the top deciles. Melly (2002), in Germany, also finds that the differential decreases monotonically as one moves up the wage distribution. The analytical framework we adopt for the estimation is based on the quantile regression methodology developed by Koenker and Basset (1978) and applied, in the context of wage equations, by Chamberlain (1994), Poterba and Rueben (1994), Machado and Mata (1999) and Lucifora and Meurs (2006).<sup>11</sup>

The empirical analysis that follows examines the effects of different characteristics on the public sector pay gap measured at different points of the distribution. This is done by computing the wage gap at different deciles, and controlling for the same individual characteristics and job attributes used in Table 5. Figure 3 plots the results for the various quantiles. These values have been obtained from the pooled data set and by imposing the restriction that the returns to observed characteristics besides public employment are the same for the two sectors, and that public–private differences depend only on a shift factor, which is the value in Figure 3.

Apart from average differences, one feature shared by the three countries is that wages for the least skilled workers are higher in the public than in the private sector. Indeed, the main set of results from quantile regressions shows

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<sup>11</sup> The standard regression technique is based on estimation of the conditional mean of a given outcome  $y$  (say, the log wage) as a linear function of individual characteristics (for example, a vector  $X$  and a public sector dummy  $PUB$ ):  $E(y | X) = X'\beta + PUB*\delta$ . Instead, the quantile regression methodology assumes that not the mean, but the quantile  $q^{th}$  of the conditional distribution of wages is a linear function of workers' characteristics:  $Q^q(y | X) = X\beta^q + PUB*\delta^q$

**Figure 3:** Estimates of the wage gap, by deciles of the wage distribution

that the public sector pay gap declines along the wage distribution in all countries. Possibly, this higher compression of the wage structure in the public sector is caused by institutions interested in the enforcement of egalitarian pay policies. We also note that the premium is never negative, even at the top deciles. In terms of the stylised facts on public–private wage differences, as summarised in Figure 1, it means that the public sector wage schedule is not only flatter than that of the private sector, but also constantly above it. Results for other variables included (though not reported in the table) are pretty standard in the literature: returns to education and age increase over the deciles in all countries.<sup>12</sup> These findings confirm our previous claim that focussing on the average public sector gap may hide important aspects of the differences between public and private wages.

Concerning country differences, the conditional wage premium for public workers is higher in France, and it is relatively flat – in the interval 14–18 per cent – from the bottom to the top of the distribution. Again using the institutional framework as a guide to account for observed patterns in the structure of public pay gaps, centralised wage setting regimes in both sectors – but with higher union power in the public sector – may be able to promote

<sup>12</sup> The only exception is Italy, where returns to age decrease monotonically over the distribution.

coordinated policies which result in a flat and constant ‘marking up’ of public in relation to private wages along the whole wage distribution. In Italy, the two-stage wage setting regime in the private sector – in which the second stage is used to redistribute productivity gains at company level – is probably responsible for the widening of private wages in the right tail of the distribution, which, in turn, contributes to reducing the wage premium for public employees for whom the ‘wage drift’ at industry level does not exist. However, low and medium wage earners – that is, those workers in the right and central parts of the distribution – are still protected by centralised and egalitarian bargaining, as the premium for them is always substantial and above 10 per cent. In Britain, more decentralised wage setting regimes in both sectors are associated with small average wage gains for public employees at the top of the distribution. In a framework in which the wage should reflect productivity levels more, it might be that, among high wage earners, private employees are on average more efficient.

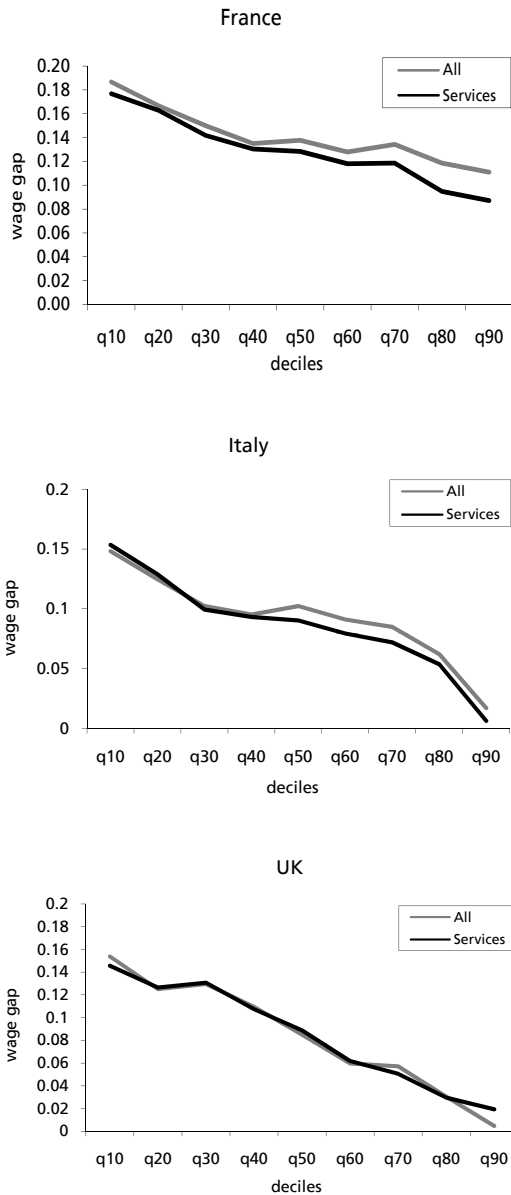
We have already observed that sector matters; in particular, the largest share of public workers is employed in the service sector. Thus, we also analyse the distribution of the public pay gap at different deciles within services. To this end, we estimate separate wage equations for public and private workers employed in the service sector at each quantile, using the standard set of conditioning variables; the results are presented in Figure 4.

For each country we report the wage gap estimated on the entire sample, and on the sub-sample of service workers. The difference between the two lines is given by the impact of public–private wage differences for workers in manufacturing. As a general comment, the gap measured within services mimics quite closely the differential estimated on the whole workforce. We also notice that in all the countries considered, along the whole wage distribution the wage gap in services is somewhat lower than the ‘overall’ gap. Also in France, where the premium computed on the whole sample was flat, there is a constant decrease as we move up the wage distribution of the service sector. The flipside is that, especially at medium and top deciles, the gap in the industry sector is in general higher than in the service sector.

Overall, French public employees in manufacturing earn more than their colleagues working in the service sector. This may suggest that working for state companies enables them to extract relatively higher rents than comparable private employees.

As already mentioned, pooled regressions fail to capture differences in productivity-related characteristics by sectors, which can be accounted for by fitting separate earnings equations for the public and the private sector. In

**Figure 4:** Estimates of the wage gap, by deciles of the wage distribution (all sectors and services)



general, results from separate public and private sector equations confirm the findings that the ‘rewards’ from observable characteristics are not stable along the wage distribution. But while returns to characteristics tend to decline over the wage distribution in Italy and France, in the UK the opposite pattern is observed.

This is hardly surprising given the institutional differences discussed in previous sections, with collective bargaining and trade union presence imposing lower returns to enforce a more egalitarian wage structure in Italy and France, and the prevalence of employer discretion in wage setting to attract and motivate workers in the UK. But since we are primarily interested in the public sector pay gap, we do not report the detailed results and use them in the next section to decompose the public sector wage gap into that part explained by differences in observed characteristics and that part due to differences in rewards.

#### **4. Decomposing the gap and explaining the differences**

We shall now decompose the wage differential into a component that is due to differences in observed characteristics between sectors, and a component that is due to differences in the corresponding rewards. The standard methodology for analysing public–private sector wage differentials at the mean of the wage distribution is to decompose the observed average gap into two components: (i) a difference in average worker characteristics and job attributes between sectors, and (ii) a difference in the returns to worker characteristics and job attributes between sectors, plus an interaction effect treated as a residual component (Blinder 1973; Oaxaca 1973; Oaxaca and Ransom 1994).<sup>13</sup> The evidence presented in previous sections, however, suggests that the public–private wage gap may be higher in the lower part of the wage distribution. To explore this hypothesis further we use a decomposition methodology due to Machado and Mata (2000) which extends the Oaxaca–Ransom approach to quantile regression settings. The main difference between the OLS and quantile regression methods (QRM) is that whilst OLS estimators ensure that the ‘predicted wage’ evaluated at the sample average vector of characteristics is equal to the sample average wage, QRM estimators are not linear and therefore do not share the same property.

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<sup>13</sup> In the literature, the wage differential due to different returns is often referred to as the ‘unexplained’ part and given a residual interpretation (that is, with respect to what is explained by different characteristics), but it is not clear whether the decomposition will over- or underestimate the residual; this should depend on whether omitted variables are positively or negatively correlated with productivity and on the distribution of the omitted variables across both sectors.

The procedure is to generate counterfactual densities at each quantile of the distribution.<sup>14</sup> In Figure 5 we report the results of decomposition.

First, when we allow returns from observable characteristics to vary across sectors the total public–private differential is in general higher than under the more restrictive specification used in the previous section. This means that in all countries the public sector is willing to pay more on the basis of personal and job attributes, and this is mirrored in steeper education and age profiles. Second, in Italy the wage differential obtained by fitting separate wage equations for public and private sectors exhibits an inverse U-shaped pattern, as it increases in the right tail of the earnings distribution. The observed differences in the estimated public wage gap between the restricted model of the previous section – in which returns to public sector were simple ‘intercept shifters’ – and the model in which also returns to observable characteristics can change depends on the fact that, in the second specification, the ‘base’ premium at top deciles is decreasing, but this effect is more than compensated by the rising rewards for seniority, age and education, and the final result is the observed U-shaped pattern.

Thus, the Italian public sector not only protects the low skilled more, but, as compared to the private sector, it also guarantees higher returns for observable characteristics (especially seniority) in highly skilled employees. This situation may be problematic as it may prevent the state from providing the right incentives to motivate workers and to stimulate effort and productivity.

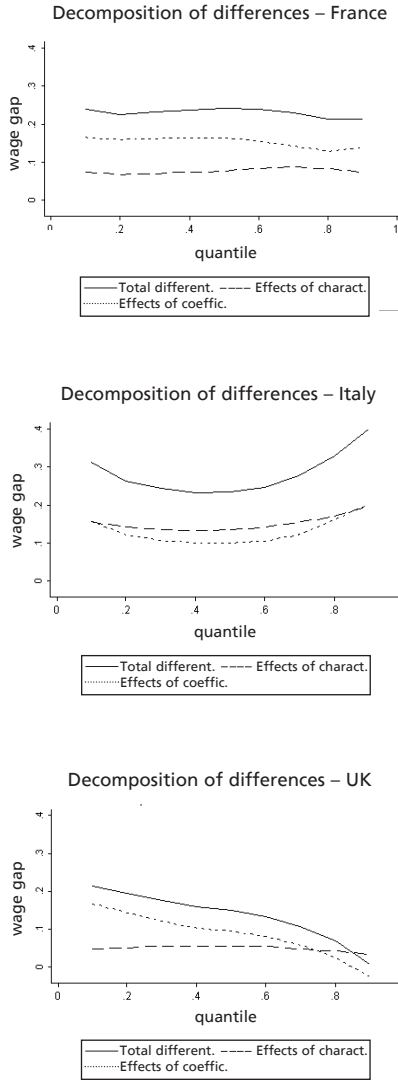
When decomposition results are accounted for, the portion of the public sector wage gap accounted for by differences in coefficients for observed characteristics (the so-called remuneration effect) declines monotonically from lower to upper deciles, except for Italy. In France and the UK the contribution of observed characteristics is roughly constant in its absolute value. Thus, if what mattered for wage formation was only the distribution of characteristics, the public premium would be constant and at a value well below 10 per cent in both countries.

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<sup>14</sup> In practice, we compare public and private workers’ characteristics (personal and job attributes) evaluated at the wage that an individual at random would get in the whole economy; and the density that would be observed if private and public sector workers, respectively, maintained their own individual and job characteristics but were paid like an individual chosen at random in the economy. In so doing, however, the difference between two quantiles of the marginal wage densities between the public and the private sector weighted by workers’ characteristics contains an additional component, which we consider of second-order magnitude and treat as a residual.



**Figure 5:** *Decomposition of public–private wage differentials*



Moreover, in the UK, where public–private wage differences are decreasing, the portion of the total public sector wage gap (which is decreasing) explained by individual attributes (which is constant) increases monotonically from lower to upper deciles. In France, where the total differential is in the 22–24 per cent range, at each decile approximately half of the gap is explained by differences in characteristics, especially in the upper part. But the portion of the public sector wage gap accounted for by differences in returns to (observed) characteristics (also called effects of coefficients) declines monotonically from lower to upper deciles. Overall, differences in returns can explain a significant portion of the differential in the lower part of the wage distribution, while this vanishes in the upper part. In the UK the estimated wage gap due to differences in returns becomes negative at top deciles, implying that there are significant differences in individual (observed) characteristics and occupations across sectors.

In Italy, which displays a pattern quite different from the other two countries, the public sector raw differential is the highest at each quantile, but differences in the estimated wage gap due to returns are smaller compared to the other countries, especially at low deciles. In contrast, the largest part of the premium is explained by ‘better’ average characteristics of Italian public employees. Indeed, in Italy the difference between public and private workers, especially as regards the educational and age structure, is the largest and favours the former group; both attributes exert a positive impact on wages.

## **Conclusions**

In this study, we have investigated public–private pay determination using French, UK and Italian microdata. At a descriptive level, we have documented that the samples of public and private employees are substantially different in terms of both workers and job characteristics, as well as sectoral composition: state workers are older, more educated and more likely to be whitecollar workers employed in the service sector, and – with the exception of public administration – in the sub-sectors of education, health care and communications. In contrast, private sector workers are over-represented in personal and ‘other’ services. Concerning pay structures, in each country public employees receive on average a higher wage than private workers, and this difference is higher in Italy and France, where the share of public employees and, in general, the ‘weight’ of the public sector in the economy is higher. This suggests that institutional factors and the way in which the economic system is divided into its public and private components may influence the process of wage formation, as well as wage differentials across sectors.

We have also documented that wage distribution is very different between public and private workers. As a result, the public pay premium varies as one moves up or down the wage distribution. In France, Italy and the UK the public sector wage premium is higher for low skilled public sector workers, whilst the opposite is the case for high skilled workers. These effects are more pronounced in the service sector.

Also, the variability of the public sector premium along the wage distribution may be partly explained by the differences in the institutional framework – especially bargaining procedures and wage setting rules and conditions – between public and private sectors, both within and between countries. In particular, whilst on the one hand public employees benefit from a higher degree of centralisation in terms of a positive mark-up on private wages (especially for the low skilled), on the other hand, they face a more compressed wage structure which, in turn, creates a ‘glass ceiling effect’ in public sector pay for workers at top deciles. This is what happens in, for example, Italy and France. In contrast, a decentralised wage setting system for both public and private employees, as in the UK, may result in similar wages in the two sectors for the high skilled (top deciles of the wage distribution). But at the bottom level, since public employees earn on average higher wages, decentralisation seems still to be associated with a ‘low floor effects’ for low skilled private sector workers.

Finally, although what we observe are static relationships observed only for 2001, our results seem to suggest that if a worker with certain characteristics was exogenously moved from the public to the private sector, he or she suffered a welfare (wage) loss, which is higher for the low skilled, who are most protected in the public sector. Thus, the privatisation of a given public service may in general impose some costs on the public employees involved. Moreover, such costs decrease with the level of wages. Of course, the underlying assumption is that after the reform a given worker remains in the same decile of the wage distribution, and that public sector reforms are ‘small scale’ and without residual effects on the differences between market relative wages across sectors. Obviously, the magnitude of these costs depends on the country in question, and so on the given institutional setting.

There are a number of economic implications; on the one hand, the empirical evidence confirms that the public sector acts as a ‘fair employer’, both reducing pay differences by gender and compressing pay dispersion with respect to the private sector; on the other hand, the existence of a positive public–private pay differential, along the whole wage distribution, also means that the public sector pays more than the opportunity wage, especially

for low skilled labour. Finally, the interactions of public and private labour market institutional arrangements play a crucial role in shaping the structure of relative wages across sectors; for example, when monopsonistic power in wage bargaining is relevant in both sectors – as, for example, in the UK – the private sector pays, in absolute terms, proportionally less, and also the public wage premium is smaller.

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## **Public and private employment and the gender wage gap in eight European countries**

### **Introduction**

In a labour market perspective, privatisation results in the first instance in more workers being employed by private employers and fewer by public employers. In this chapter, we investigate whether such a change affects women and men differently. From the workers' point of view, privatisation may have significant effects on employment stability, job quality and wages: compared to the private sector, although the differences are probably less striking than they would have been in the 1980s, jobs in the public sector tend to be more stable, unionisation rates tend to be higher – which can limit the deterioration of working conditions – the wage regime remains centralised and wages are largely based on pay scales that result in a wage distribution narrower than in the private sector.

Empirical studies have regularly found that workers with given characteristics are better paid in the public sector than in the private sector (for a review, see Gregory and Borland 1999); interesting work by Postel-Vinay and Turon (2005) even shows that the differential is positive when entire working lives are taken into account. Studies that analyse the public pay premium, not only at the mean wage but over the whole wage distribution, have also shown that pay differentials tend to be larger at the lower end of the wage distribution (Poterba and Rueben 1994; Mueller 1998; Lucifora and Meurs 2006; see also Ghinetti and Lucifora in this volume).

Studies of the sectoral pay gap in a gender perspective find that the public pay premium is larger for women than for men (Zweimüller and Winter-Ebmer 1994; Prescott and Wanderschneider 1999; Disney and Gosling 2003). Some conclude that it results in a smaller overall gender pay gap than that which

would prevail if all workers were paid at private sector rates (Grimshaw 2000; Ponthieux and Meurs 2005). But Datta-Gupta et al. (1998) find, in the case of Denmark, that the gender wage gap would have decreased between 1983 and 1994 (instead of remaining unchanged) if public sector employees had been paid at private sector rates. One debate in recent studies concerns the impact of workers' 'choice' of one or the other sector on the existence of a public pay premium; for example, Dustman and van Soest (1998) in a study of the public pay gap among male workers in Germany find that there is no public pay premium once selection is taken into account; Disney and Gosling (2003) obtain the same result for men in the case of the UK, but find that the public pay gap remains positive and significant for women.

All in all, it seems that women are at more of an advantage in public employment than men. It is also widely known that the public sector represents a higher share of women's employment than men's, and that women are more likely to be found in the low wage area than men – this is true in the public as well as the private sector. This constitutes a first set of reasons to believe that privatisation could affect women more than men.

Other reasons can be added: first, given gender differences in the employment structure by occupation and industry, it could be that privatisation does not take the same form for men and for women. Women are massively concentrated in tertiary activities, where privatisation is more likely to take the form of contracting out or subcontracting – in which case privatisation involves a shift from one public employer to several private companies – as opposed to 'straightforward' privatisation (in which case it involves a shift from one publicly owned company to one private firm). The form taken by privatisation may result in differences in terms of management of the workforce, wage regime and trade union power, which can obviously have different implications for the workers. In less skilled occupations, the form taken by privatisation may matter a lot: for example, Bernhardt and Dresser (2001), who document the impact of privatisation of public services in the USA (subcontracting and contracting out), with particular attention to women in low end occupations, show that the losses are potentially greater in such occupations because the most vulnerable workers are more protected in the public sector than in the wide variety of private enterprises. In contrast, Melly and Puhani (2007), who studied two companies that have been privatised (that is, sold to private firms), find that young employees with little seniority and high skilled workers gained from the privatisation, as did – they add, 'surprisingly' – very low skilled employees. They found, by investigating the firms' human resources departments, that this resulted from the need to render privatisation acceptable to the employees' representatives.

Second, it is generally acknowledged that the public sector is a more ‘family-friendly’ employer than the private sector; this would help to explain why it attracts more women than men. It is therefore not unlikely, at least as long as things remain as they are in terms of the gender division of family tasks, that a change towards less family-friendly employment conditions would affect women more than men; in terms of wages, the impact might be less obvious and would probably depend on the size of the gender wage gap along the wage distribution in both sectors; in other words, the combination of ‘sticky floor’ and ‘glass ceiling’ effects (see Arulampalam et al., 2004).

Finally, it is not unrealistic to expect that privatisation will be more detrimental to women’s labour market outcomes than to men’s. In what follows, we focus on one global indicator of women’s outcomes compared to men’s: the gender wage gap. We investigate the current impact of the public sector on its magnitude as an indication of the potential impact of privatisation. In order to be able to draw conclusions not limited to particular national situations, it is necessary to consider a large set of countries: we selected Denmark, Belgium, France, Germany, Italy, Portugal, Spain and the United Kingdom. They are different enough in terms of both gender inequalities and progress in privatisation trends to allow a general idea of the possible impact on gender pay inequality.

We begin by briefly reassessing gender inequalities in the labour market, focusing on those that are determinant for analysing the potential impact of privatisation (Section 1). We then analyse the public pay premium by gender, and the composition of the gender wage gap in the private and public sectors (Section 2). Then we shift to an analysis that takes into account the gender wage gap and the public pay premium, not only at the mean wage but over the entire wage distribution (Section 3); this analysis suggests that it is mostly women at the lower end of the wage distribution who suffer from privatisation, but to a greater or lesser extent in the different countries.

## **1. A brief overview of gender inequalities in European labour markets**

Our data are drawn from the eighth (and final) wave of the European Community Household Panel (ECHP), conducted in 2001. The advantage of this source is that the data have been harmonised at European level, allowing us to distinguish between workers in the private and public sectors.<sup>1</sup> It also

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<sup>1</sup> This is also, among the data sets provided within the European statistical system, the most recent with which such a comparison between workers in the private and public sectors is possible, since currently this information cannot be found either in EU-SILC or in the LFS.



provides the variables needed to analyse wage differentials (education, experience, occupation, industry, type of labour contract, working hours and, of course, wages) and the usual contextual information (region, cohabitational status, number of children, citizenship). Still, the ECHP has some limitations; first, although education and experience are fundamental in the analysis of wage differentials, the measurement of these two variables is rather poor: education is measured only by a three-level variable, and experience by the number of years since leaving education or first entering a job, without the possibility of taking into account intermediate periods of unemployment or inactivity. But we know that women, because of child-care responsibilities, are more likely to experience interruptions in their careers than men, probably leading to an overestimating of women's professional experience and an underestimating of the specific effect of career interruptions. Second, in some countries the information on weekly working time is given only for individuals who work at least 15 hours per week, which means it is not possible to compute an hourly wage for the rest; this tends to reduce the share and measurable effect of part-time work, again with a disproportionate impact in the case of women.

The sample of countries to be compared was selected solely on the basis of the sample sizes obtained once all the observations with missing values were removed for any of the relevant variables used in the analysis. The population is that of employees aged from 17 to 64, apprentices and trainees excluded, who work at least 15 hours per week. Countries for which the data were incomplete (Sweden and the Netherlands), or for which the samples were too small (Austria, Ireland, Luxembourg), have been left out. This leaves us with the eight countries listed above, and samples of employees ranging from 1700 to 4000 observations.

Although European countries share many common rules and objectives in terms of employment, gender equality and public sector downsizing, there is still much variation. It is not our purpose to review cross-country differences in all the dimensions involved, but to focus on those that are more likely to determine differences in the potential 'sensitivity' of the gender wage gap to privatisation; this depends primarily on the respective shares of women and public sector employees, then on structural gender and sectoral differences in occupations and sector of activity. This and the overall proportion of women among employees in turn determine the size of the gender and sectoral wage gaps.

In all the countries of our sample, but with significant cross-country differences, the proportion of employees is lower among women than among

men, and women represent a smaller proportion of employees than men, ranging from 39% in Spain to 48% in Denmark and the UK (Table 1). Among employees, we find the usual gender differences characteristic of all studies: women tend on average to have higher education levels than men and are more likely to be found in medium and low skilled non-manual occupations, while men are more likely to be found in manual or high skilled non-manual occupations (Table 2). There are of course some exceptions: in the UK men tend to have a higher education level than women, and in Denmark there is almost no gender difference in education levels. As regards occupations, the noticeable exception is that of the three Southern countries, where higher shares of high skilled occupations are found among women than among men.

The share of public sector employees varies notably between countries, ranging from 19% in Spain and Portugal through around 30% in Italy, France and Belgium, and up to 39% in Denmark (Table 3). In all countries, public employment represents a much higher share of women's employment than of

**Table 1:** *Percentage of women among employees – ECHP2001*

Country	DK	BE	FR	IT	SP	PO	GE	UK
Percentage	48.5	46.0	45.3	41.2	38.6	45.5	41.1	48.0

**Table 2:** *Gender ratios (F/M) of the distribution of workers by education level and occupation – employees, ECHP2001*

	DK	BE	FR	IT	SP	PO	GE	UK
Education								
(Isced 0–2)	0.9	0.5	0.8	0.7	0.6	0.8	0.9	1.2
(Isced 3)	1.0	1.0	1.3	1.3	1.2	1.1	1.1	0.9
(Isced 5–7)	1.0	1.2	1.2	1.1	1.5	1.9	0.8	0.9
Occupation								
Professionals and managers	0.5	0.9	0.6	1.8	1.4	1.3	0.8	0.8
Associate professionals	1.8	1.1	1.1	1.0	1.4	1.2	2.0	1.5
Clerks	4.2	2.0	3.6	1.7	2.6	2.2	2.6	2.7
Services and sales workers	3.1	3.1	2.6	1.3	2.4	2.0	3.6	2.5
Manual workers	0.3	0.3	0.4	0.5	0.4	0.6	0.3	0.2

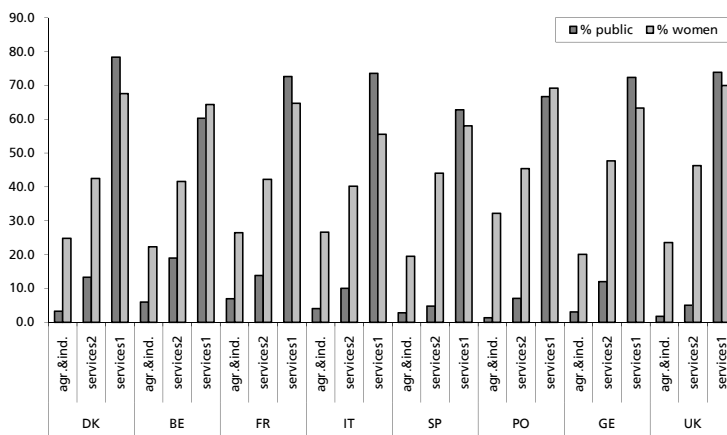
**Table 3:** Share of public employment, total and by gender – employees, ECHP2001 (%)

	DK	BE	FR	IT	SP	PO	GE	UK
Total	39.5	33.3	31.9	31.6	19.4	19.3	26.8	26.4
Among women	56.0	37.8	39.3	39.6	25.1	26.0	36.7	35.8
Among men	23.9	29.5	25.8	26.0	15.9	13.8	20.0	17.6

men’s, again with large differences between countries: the share of public employment among women is a minimum of 1.3 times higher than among men (in Belgium), rising to more than twice as high (in Denmark).

By sector of activity, the share of public employment is especially high in the service sector, and the share of women in this sector is particularly high. Public employment can nevertheless be found also in various other activities, in greater or smaller proportions in the different countries, depending on the progress of privatisation in these activities (see Figure 1). The notable cross-

**Figure 1:** Share of public employment and share of women by sector of activity – employees, ECHP2001 (%)



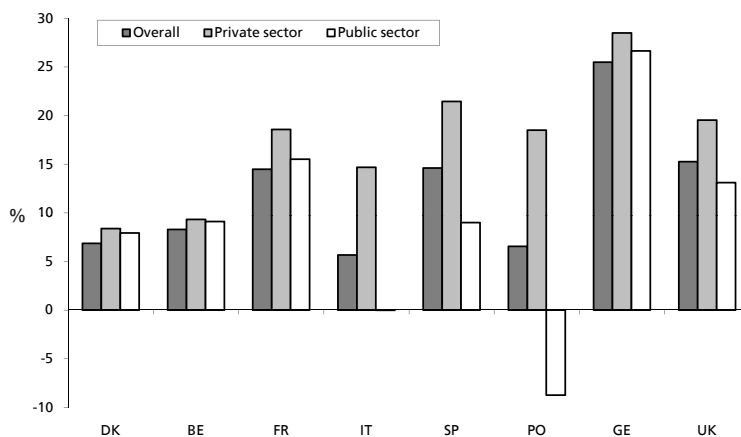
Note: ‘Services1’ groups education, health care, social services and public administration, and ‘Services2’ groups all the other service sectors (trade, hotels and restaurants, transport and communications, financial intermediation, etc.).

country differences observed in the shares of public employment by gender result mostly from the fact that women are massively concentrated in activities that are essentially provided by the public sector: education, health care, social services and public administration. As a result, in our sample a large majority (ranging from 55% in Italy to 70% in Portugal and the UK) of the workers in these activities are women ('services1' in Figure 1). Conversely, in the other service sectors (trade, hotels and restaurants, transport and communications, financial intermediation, real estate and other services – grouped in 'services2' in Figure 1), and even more in the rest of the economy, the share of women is much smaller.

Last but not least – but this does not come as a surprise – we found that women's hourly wages<sup>2</sup> are smaller than men's, in both the public and the private sector (Figure 2).

The size of the gender wage gap is everywhere smaller in the public sector, though only slightly in Denmark and Belgium. Three countries stand out, for different reasons: Germany, for the size of the gaps, in both the private and

**Figure 2:** *The gender gap in unadjusted hourly wages – employees, ECHP2001 (%)*



<sup>2</sup> We use hourly wages in order to neutralise the effects of gender or sectoral differences in working hours. Hourly wages are computed on the basis of information on monthly wages and weekly working hours.

the public sector; Italy and Portugal, because of the gender pay gap in the public sector: non-existent in Italy, negative in Portugal (which means that in this sector women are on average better paid than men); this is likely to result partly, as we shall see, from composition effects.

## **2. Public/private pay differentials by gender and the gender wage gap**

We shall now look at the pay differential between the two sectors, separately for women and men. First, comparison of average unadjusted hourly wages in both sectors shows, in all the countries reviewed and for both men and women, that there is a positive public wage gap – that is, the average wage is higher in the public sector than in the private sector (Figure 3). It ranges from rather small, especially in Denmark (about 4%), to larger in Germany, the UK and France, and very large in the Southern countries – up to 60% for women in Portugal. With the exception of Germany, it is everywhere larger for women than for men.

The higher average wage in the public sector is likely to result at least partly from various differences in employee or job characteristics (education, experience, occupation, and so on) in the two sectors. To investigate this, we apply the Oaxaca-Ransom technique<sup>3</sup> for decomposing wage gaps between two groups (here workers in the public or the private sector). The basic idea is to break down the sectoral wage differential into a part due to differences in the worker's individual and job characteristics<sup>4</sup> between the two sectors (this measures the wage gap 'explained' by structural differences), and a part due to the fact that the returns to given characteristics might not be the same in the two sectors (this measures the 'unexplained' gap). Decomposing the sectoral pay gap allows us to check for the existence of a public pay premium. It is worth mentioning that, given the high correlation between the pay gap and the sector of activity (services vs industry and agriculture), this public pay premium – when there is one – results almost entirely from public/private differentials *within* the service sector.<sup>5</sup>

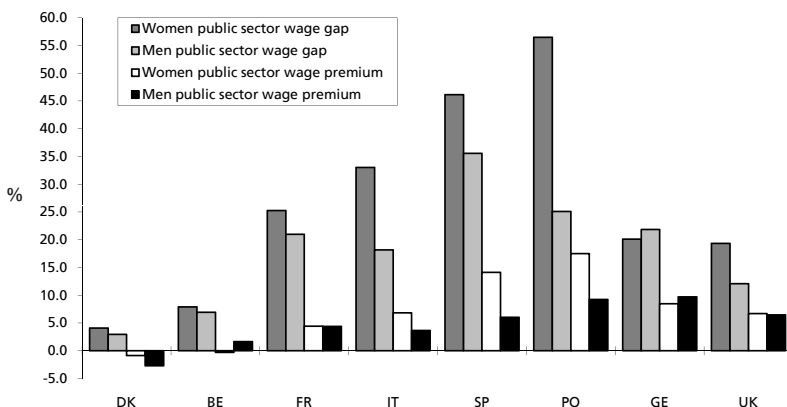
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<sup>3</sup> See Oaxaca and Ransom (1994).

<sup>4</sup> The variables introduced in the wage equation are: education, experience, tenure, type of employment contract, occupation, working time status (full time/part time), sector of activity (services vs. other sectors), and controls for region, family situation and citizenship. This specification is used in all the estimations presented in this chapter.

<sup>5</sup> A complementary analysis (not presented here), in which the decomposition was performed for the sample restricted to employees in the service sector (public or private), does not lead to significantly different results.

**Figure 3:** *The sectoral wage gap and sectoral pay premium by gender in the service sector (%)*



Since the type of service (education, health care, social and administration vs other services) and the type of sector (public vs private) are also highly correlated, it was not possible to consider separately the two types of service identified above (see Figure 1). The decomposition is therefore based on wage equations in which all services (as opposed to industry and agriculture) are taken together.

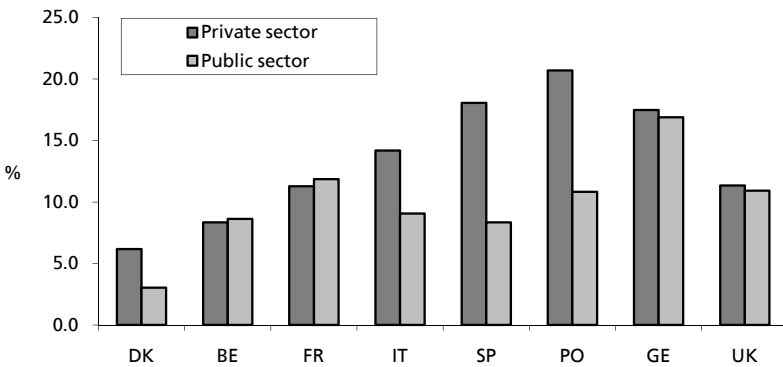
The results show that, in fact, not all the pay gap can be attributed to structural differences, with noticeable differences between the countries (Figure 3). First, in two countries (Denmark, Belgium), the decomposition shows that there is no public pay premium, but rather a public pay penalty. This is especially visible in the case of men in Denmark; for women, whether in Denmark or Belgium, it seems that all of the public pay gap can be attributed to structural differences, since once they are taken into account, no difference remains.

Second, the size of the wage premium (when there is one) is not systematically bigger for women than for men; in France and the UK it is the same for both genders, and in Germany and Belgium it is bigger for men. The case of Denmark is special in that it is less penalising for women to work in the public sector than it is for men. Only in the Southern countries is the relative advantage to women evident; for example, in Portugal (where the

public pay premium is the highest in our sample of countries) women with given characteristics<sup>6</sup> earn an hourly wage about 17% higher in the public sector, while the premium is only about 9% for men.

To complement this first analysis, it is also worth verifying whether gender discrimination (if any) follows the same pattern in the two sectors; so instead of decomposing the sectoral wage gap for each gender, we now decompose – using the same technique – the gender wage gap in each sector. It is usually assumed that the public sector is a fairer employer than the private sector. If this is true, we should observe that the ‘unexplained’ part of the gender wage gap (the part which does not result from differences in characteristics but from differences in the returns to these characteristics) is smaller in the public sector than in the private sector. The results of the decomposition of the gender wage gap show firstly that there is in fact a significant ‘unexplained’ gender wage gap, and for both sectors (Figure 4); in other words, men benefit from the fact that the returns to their characteristics are higher than average, whether in the private or the public sector. In Denmark, Italy, Spain and Portugal, however, this ‘unexplained’ gender wage gap is clearly higher in the private sector than in the public sector. In the other countries, the size of the unexplained gender wage gap is quite close in the

**Figure 4:** ‘Unexplained’ gender wage gap in the public and the private sector (%)



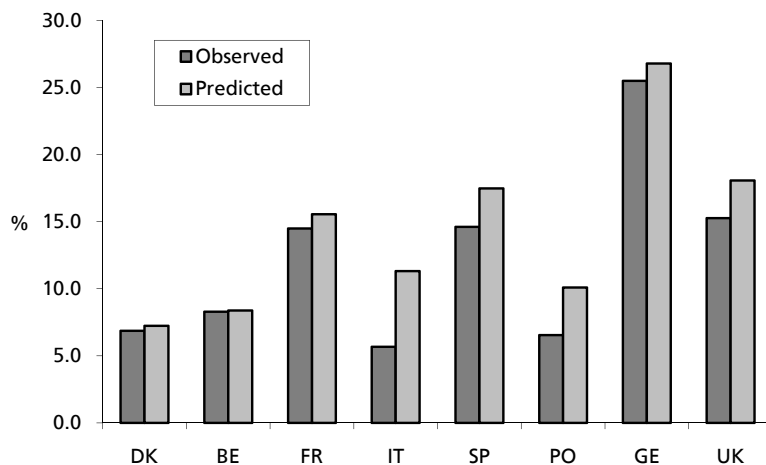
<sup>6</sup> Those introduced as regressors in the wage equations.

two sectors; slightly higher in the private sector in Germany and the UK, slightly higher in the public sector in Belgium and France.

The idea that the public sector is fairer (that is, it treats men and women more equally than the private sector does) is not generally verified; with our data, the results in the case of Belgium and France even suggest the contrary.<sup>7</sup> The next obvious question concerns what the gender wage gap would be if all workers, whether women or men, were paid following the rules that prevail in the private sector. Using the coefficients obtained in our previous wage equations, we can compute, for men and women, the hypothetical wage those working in the public sector would get if their characteristics were valorised as they are in the private sector; we can then compute a ‘predicted’ gender wage gap based on these hypothetical wages. The comparison between the observed and this predicted gender wage gap (Figure 5) suggests that the gender wage gap would everywhere be larger than it now is.

Countries differ in terms of the magnitude of impact, however: it ranges from very small in Denmark and Belgium, to small in France and Germany, and large in the other countries.

**Figure 5:** *Observed and predicted gender wage gaps under private sector conditions (%)*



<sup>7</sup> This could result from a selection effect in the public sector that our data do not allow us to control for.



The implication is nevertheless limited to a matter of descriptive interest because the estimation assumes that not only the workers' distribution by occupation and other job characteristics, but *all* other things would remain equal, hardly a plausible assumption. This result must therefore be taken mostly as indicating that the wage regime prevailing in the public sector – more centralised pay negotiations and wage setting – results in smaller inequality in general, hence less gender inequality in pay. This would be consistent with other international comparisons of the gender pay gap showing the impact of institutional differences in the explanation of cross-country differences in the evolution of the gender pay gap (Blau and Kahn 2003).

So far, we have measured the gaps only at the mean wages; when they are measured along the entire wage distribution, they differ significantly between various points: in general, the wage distribution is more compressed in the public sector than in the private sector; in the two sectors, women's wage distribution is mostly to the left of that of men, indicating lower wages (see Appendix 1). This indicates that the public pay advantage by gender and/or the gender wage gap in the public vs. the private sector could be different at various points of the wage distribution, and different for men and for women. Hence two questions arise:

1. To what extent does the 'public sector fairness' observed at the mean wage hold over the whole wage distribution?
2. How does the public pay premium vary along the wage distribution?

That is what we shall investigate in Section 3, on the basis of quantile regressions developed after Koenkler and Basset (1978).

### **3. Pay differentials over the wage distribution**

Previous studies have established that the wage structure is generally flatter in the public than in the private sector, and that the public wage premium, once controlled for observable characteristics, is decreasing along wage distributions. There are also gender differences in this general feature: the wage gap estimates suggest that women are better off working in the public sector, particularly at the lowest deciles, whilst the opposite is true for men at the highest deciles (Lucifora and Meurs 2006). Conversely, following the initial work by Albrecht et al. (2003), empirical studies on the glass ceiling effect tend to indicate a larger gender wage gap at the top of the distribution.

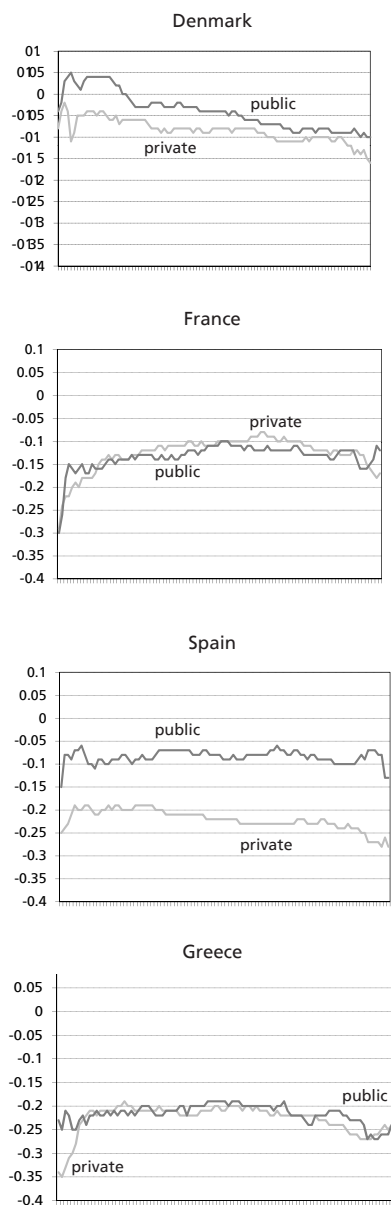
Taking these two stylised facts together, would women gain or lose from privatisation? This depends on the relative public wage premium of men and women, and their ranking in sectoral wage distributions.

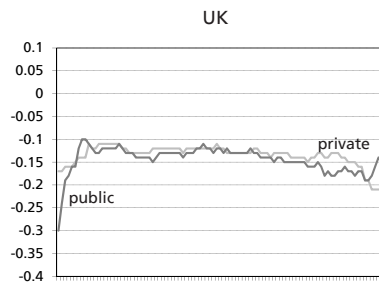
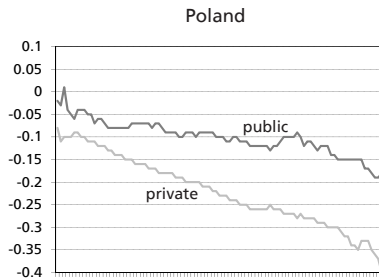
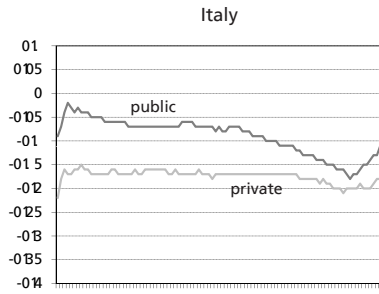
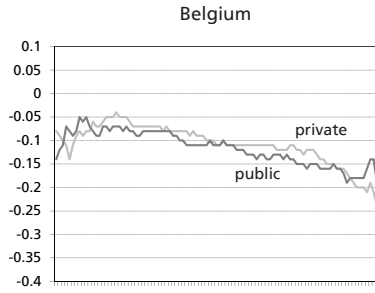
### **3.1 Gender pay differentials by sector**

In order to analyse the gender wage gap along the wage distribution in the two sectors, we compute, for each sector, the value of the coefficient of a dummy variable for gender (female) estimated for the pooled population of female and male employees along the wage distribution. The estimation controls for the same characteristics as those taken into account in the wage gap decompositions described above (Figure 6 overleaf).

The results show first that, at any point in the wage distribution, in both the public and the private sector, there is a pay penalty for women. There is one exception, however: in Denmark the penalty in the public sector falls on men in the lower part of the wage distribution. Second, the regression suggests that the public sector would be fairer than the private sector only in four countries: Denmark, Italy, Spain and Portugal. In Belgium, France, Germany and the UK, the size of the gender penalty is about the same in both sectors, almost the whole length of the wage distribution. Third, the shape of the gender wage gap tends to indicate the existence of a glass ceiling effect; that is, the gender wage gap increases towards the top of the distribution. This effect is clear in both sectors in Portugal, where the gender pay penalty increases almost monotonically from the bottom to the top of the distribution; it is visible also, though less pronounced, in Denmark, Belgium and, but only in the public sector, Italy. The shape is flatter over most of the wage distribution in the other countries, except in the case of France, where the gender wage gap tends to decrease between the bottom and about the middle of the wage distribution.

**Figure 6:** *Estimates of the gender wage gap by decile in the public and in the private sector*





### **3.2 Public pay differential by gender**

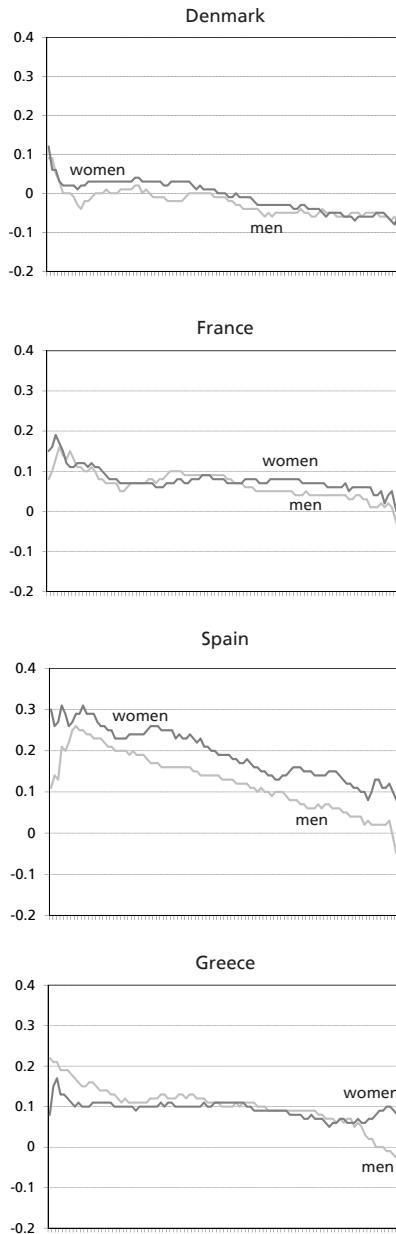
Using the same technique, we now estimate, for each gender, the coefficient of a public dummy variable over the entire wage distribution for the pooled population of public and private employees. This allows us to compare the public pay differential for men and women and its variation along the wage distribution (Figure 7).

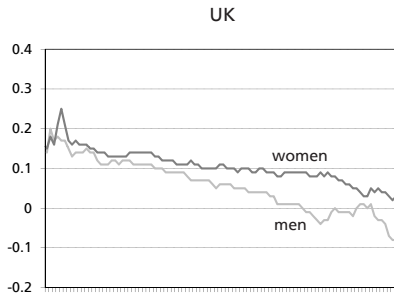
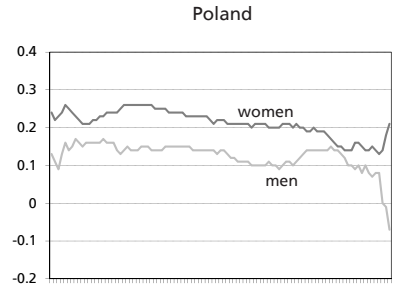
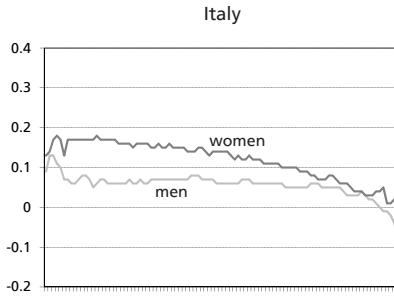
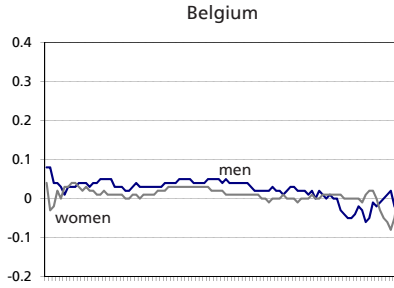
At first glance, the public pay premium appears to be positive over almost the whole wage distribution except in Belgium, where it mostly does not differ from zero, and Denmark, where it even becomes a penalty in the second half of the wage distribution. Except in Belgium and Germany, the pay premium also appears to be greater for women than for men, especially in Spain, Italy, Portugal and the UK – the same countries in which we found the largest potential impact of privatisation on the average gender wage gap.

In the majority of countries, this public premium tends to decrease when reaching the top of the distribution, for both women and men. For men, the decrease leads to a public pay penalty at the top deciles in all countries, so that in the upper part of the distribution women end up with a larger pay premium than men in most countries. Portugal and, to a lesser degree, Italy present a particular profile because the public premium rises for women in the very top deciles. These results suggest that in most countries high skilled men employed in the public sector would gain if they were paid ‘as if’ in the private sector, but this would not be the case for high skilled women.

At the lower end of the wage distribution, all public sector workers benefit from it, men as well as women. In all countries except Germany and Belgium, the public pay premium ranges from 10% to 20% for women in the first quartile of the distribution. For low skilled workers, the size of the public pay advantage probably results also from very low wages in the private sector, where wage bargaining is more decentralised than in the public sector.

Figure 7: Estimates of the public wage gap by decile for men and women





## **Conclusions**

The two last decades have been marked by a general privatisation trend in European countries, as well as ongoing attempts to limit the share of public employment in the labour market. These policies have taken several forms, from privatisation of public firms or contracting out of government services to flat numerical limitations in the number of public servants hired each year.

Since male and female workers are not equally distributed across the public and the private sectors, these changes in the size of the public sector are likely to affect them differently. Curiously, there have been few studies of the possibility that the wage and employment effects of these policies might be different for women and men. In this chapter we have tried to shed light on this issue. More precisely, we have tried to assess whether the differences in pay structures by sector and by gender may advantage – or disadvantage – women compared to men. We analysed eight European countries in 2001: Denmark, Belgium, France, Italy, Spain, Portugal, Germany and the UK.

The potential effect of privatisation on the gender wage gap combines three general features: (i) the public sector pays more on average than the private, controlling for individual characteristics; (ii) as the public sector is fairer than the private sector, the public wage premium is higher for women than for men; (iii) the public wage premium is higher for unskilled than for skilled workers. The result of combining these effects would be to worsen the gender wage gap as the private pay structure would cover a larger share of workers.

But the extent of these three general features differs across countries, and so does the potential impact of privatisation on the gender wage gap. Where both the public wage premium and the gender wage gap are limited, there would be almost no change in the gender wage gap if public employees were paid like those in the private sector. This is the case for Denmark and Belgium. More potential changes appear where there are strong differences in public and private pay structures, as observed for Italy, Portugal, Spain and the United Kingdom. In France and Germany, the average public wage premium is limited, but the gender wage gap is quite similar in both sectors. This means that gender wage inequality would not be affected by privatisation and would remain at quite a high level.

Apart from in Germany and Belgium, the public wage premium declines along the wage distribution and this trend is more pronounced for men than for women. This indicates that females are better off in the public sector than men, particularly at the lowest wage deciles; privatisation of unskilled and low paid jobs would probably worsen the position of female workers.



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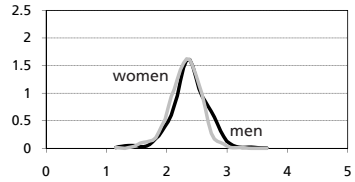
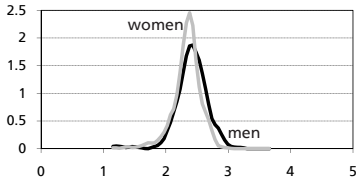
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## Appendix 1: Distribution of women's and men's log hourly wages

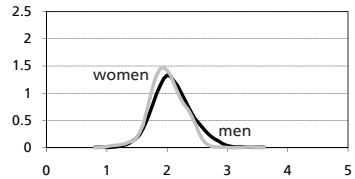
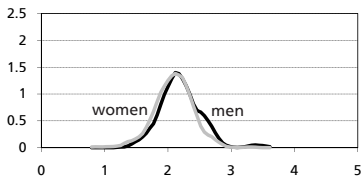
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### Private sector

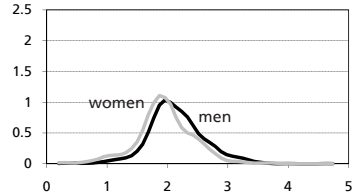
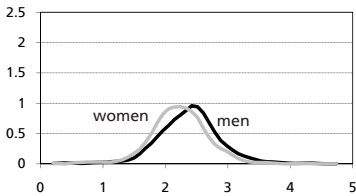
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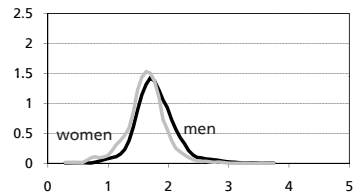
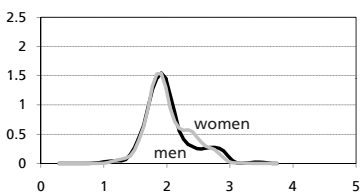
#### Belgium



#### France



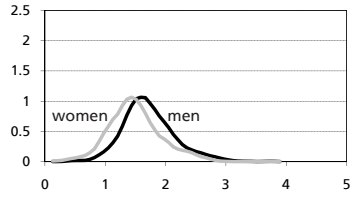
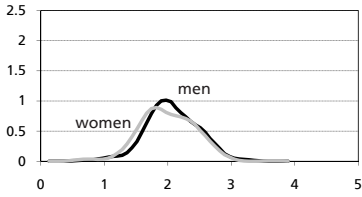
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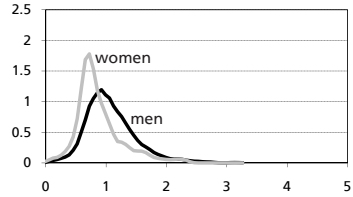
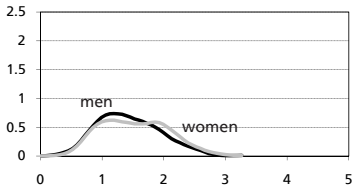
**Public sector**

**Private sector**

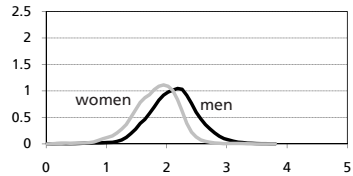
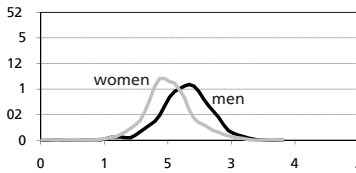
**Spain**



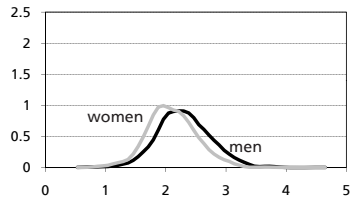
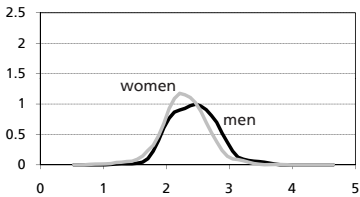
**Portugal**



**Greece**



**UK**





## **Provision of work–life balance arrangements in European companies: public vs private**

### **Introduction**

With the persistence of the trend towards the privatisation and marketisation of public services, there has been much interest in the performance and employment outcomes of privatisation (for summaries of a number of studies on these issues, see Megginson and Netter 2001; Kikeri and Nellis 2002). The focus has been on whether privatisation does indeed increase the performance or efficiency of companies and so in the longer term increases employment levels, as the advocates of privatisation so strongly argue. One aspect of this trend that has not been so actively addressed is changes in working conditions due to privatisation. Among working conditions, wage differences or differences in wage levels, distribution or structure and wage dynamics between the private and public sectors have been most frequently addressed (for example, Disney and Gosling 1998; Ponthieux and Meurs 2005; Postel-Vinay and Turon 2005; Lucifora and Meurs 2006). The difference between the public and private sectors with regard to other working conditions has not been addressed so often, however. Just as privatisation may affect workers' wage levels due to the greater need for profit generation and the lack of institutional restrictions, it has also been shown to have negative implications for various aspects of working conditions (EIRO 2005). But most studies have been limited to specific national or company case studies, while cross-national studies that examine a wider selection of sectors are limited. This chapter addresses this issue by examining the differences between the public and private sectors in the provision of work–life balance options. Here a work–life balance entails not only a balance between work and family life but also the various needs of individuals to diversify their working time throughout the life course to meet

different needs for education, leisure and other preferences. The options for work–life balance are distinguished in terms of three categories. First, there can be a work–life balance through variation of working hours day by day, week by week and even year by year. Second, various types of leave can be taken to meet different needs. Third, companies can provide facilities or services that enable a better balance of work and life, such as child care facilities.

In this chapter we shall attempt to answer a number of questions. Are there differences between the public and private sectors in the provision of work–life balance options with regard to working time, leave and work–life balance services? Does this effect persist after we control for other relevant company characteristics that affect the provision of work–life balance options? Are there substantial country differences in terms of the effects of being a public or private company? What interaction effects can we find between certain company characteristics that affect the provision of work–life balance options and being a public or private company? To answer these questions, we use the European Establishment Survey on Working Time and Work–life Balance (ESWT) provided by the European Foundation for the Improvement of Living and Working Conditions for the years 2004/2005.

The structure of the chapter is as follows. In Section 1, we examine some theoretical grounds concerning why privatisation may affect working conditions, as well as some empirical results from previous studies on the private–public divide in the provision of work–life balance options. In Section 2, we examine the ESWT survey in more detail. We also develop subcategories of the work–life balance options we examine, and explain the method used for analysis. In the analysis section (Section 3), we look first at descriptive bivariate analyses of each of the three subcategories of work–life balance options. This is followed by a multivariate analysis to examine the effect of being a public company rather than a private one on the provision of work–life balance options. Finally, we examine the interaction effect of being within the public sector and other company characteristics that affect companies' work–life balance option provision. Section 4 contains some conclusions.

## **1. Privatisation and company provision of work–life balance options**

### **1.1 Company-level work–life balance options**

Work–life balance policies or work–life reconciliation policies can be defined as policies that directly support the combination of professional,

family and private life (Plantenga and Remery 2005). Company-level policies are those introduced or implemented by firms to enhance the balance of work and life for their workers. This does not have to be the firm's independent policy – it could involve the implementation of national or sectoral collective agreements or legal regulations.

Companies can respond to workers' needs for a work–life balance in many ways. Evans (2001) divides the options into leave from work for family reasons, changes in work arrangements due to family reasons, practical help with child or elderly care, relevant information and training. Similarly, Den Dulk (2001) and Plantenga and Remery (2005) also distinguish four types of arrangements provided by firms for balancing work and life. They are flexible working time arrangements, leaves, child care arrangements and supportive arrangements. Based on these categorisations, we can divide work–life balance arrangements into three categories (Table 1).

First, there are those that entail changes in working time, that is, changes in work schedules or hours worked to fit workers' needs to balance family or life with work. Second, there are schemes in which workers take a longer period of time off work to take care of their responsibilities, such as parental leave. Third, there are services provided, either in the form of facilities, such as kindergarten or other childcare amenities, or other support services, such as training, information provision or laundry facilities. In this respect, work–life balance facilities and services can include many more options than those listed in Table 1. The extent to which these options facilitate the individual worker's need for a work–life balance can differ depending on the individual's preferences and needs, as well as differences in how the option is provided or used. Working time options and early retirement can be seen to facilitate both workers' and companies' needs for flexibility to a greater extent than other work–life balance options. For example, not all part-time work is for the purpose of satisfying workers' need to shorten their working hours for various reasons; companies' production needs, business cycles or other needs are also important factors. In other words, part-time work, flexible working time, working time accounts, phased and early retirement can be used for both employers' and employees' needs, or either, whereas other options are used directly in the workers' interest, although companies can and do benefit from their use indirectly. For this reason, we must divide these options into those that are genuinely used for the benefit of workers and those used to satisfy companies' needs. But this is not always easy and we must take into account the fact that working time options may have different implications for facilitating the work–life balance in comparison to leaves, as well as to services and facilities provided.



**Table 1:** *Work–life balance options provided by companies*

Type	Options
Working time/flexible working	Part-time Right to reduce working hours Phased retirement Flexible working schedules Working time accounts (saving hours) Job sharing Tele-work (working at home)
Leaves	Parental leave (maternity, paternity, adoption leaves and extensions) Leave for care of elderly or other family members or other family reasons (long and short) Early retirement Career break/sabbatical Leave for education and training
Facilities and services	Workplace or linked nursery, childcare facilities Other help – services and in kind, cash – for parental, other care and household management duties Information provision, training courses

*Source:* Based on Den Dulk (2001); Evans (2001); Platenga and Remery (2005).

## 1.2 Privatisation and the public–private difference in the provision of work–life balance options

The main argument for privatisation is that private actors under free market competition can be more effective in delivering goods and services due to their contracting abilities, different business goals in comparison to public companies, the high cost of government intervention and because public ownership allows less prosperous firms to continue to exist on the basis of government funding (Megginson and Netter 2001). But private companies' profit motive may have a negative impact on wage levels and working conditions. It has been noted that public ownership often entails greater attention to good industrial relations and provides more protection and guarantees for workers (EIRO 1999). This may be enhanced by the fact that the public sector is more likely to have a collective agreement and stronger unions (Bordogna 2007). A study carried out by the German Working Life Research Centre (FORBA) examined the impact of privatisation of public services on employment and industrial relations. They found a deterioration of working conditions in addition to effects such as substantial job cuts and

significant wage reductions (EIRO 2005). Here we shall not test the effect of privatisation on the provision of work–life balance options directly, however, but rather examine the differences between public–private companies in their provision of such options.

Numerous studies have pointed out that public companies, or public ownership, also do better in the provision of various work–life balance arrangements or in being family friendly (Whitehouse and Zetlin 1999; Evans 2001, 2002; Den Dulk 2001; OECD 2001; Plantenga and Remery 2005). The reasons put forward are as follows. First, the public sector is less subject to market pressures and may employ a larger proportion of women (OECD 2001; 147), which means they have more of a need and capacity to provide work–life balance arrangements. In addition, since most European governments emphasise the importance of gender equality and reconciliation policies, the public sector is seen as being under more pressure to take gender equality norms into account to set a precedent for other companies to follow (Plantenga and Remery 2005: 74). Evans (2001), based on several studies of employer surveys in Australia, Japan, the United Kingdom and the United States, concludes that public sector firms are more likely to be family-friendly than private sector ones, whether in their provision of leaves, flexible hours, childcare provisions or other types of services. This is also confirmed by employee-based surveys, not only for the four countries in question but also in the case of Europe, based on the outcome of the European Working Conditions Surveys. In these surveys it was shown that public sector employees generally have access to a wider range of family-friendly working arrangements (Evans 2001).

## **2. Data and methodology**

To examine the public–private differences in the provision of work–life balance options we use the Establishment Survey on Working Time and Work–life Balance (ESWT) of the European Foundation for the Improvement of Living and Working Conditions (EF). The ESWT provides us with information at the establishment level<sup>1</sup> on various arrangements used within the firm for flexibility and work–life balance issues. It covers 21 EU

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<sup>1</sup> The unit of enquiry for the survey was the establishment, that is, the local unit in the case of multi-site enterprises. The survey data in the ESWT are representative of establishments with 10 or more employees from all sectors of activity, except for agriculture (NACE A), fishing (NACE B), private households (NACE P) and extraterritorial organisations (NACE Q) (Reidmann et al. 2006, Annex1)

member states – the EU-15 plus six new accession countries, namely Cyprus, Czech Republic, Hungary, Latvia, Poland and Slovenia – and was conducted between 2004 and 2005 in over 21,000 establishments in which personnel managers and, if available, employee representatives (ER) were interviewed.

In this chapter we shall use the data from the manager survey, which covers a wider and more representative range of companies and contains more reliable answers.<sup>2</sup> But answers given by the employee representatives on the motives for taking up certain arrangements will be examined later to compare them with those given by the personnel managers. The ESWT survey covers a wide range of arrangements on which data were not available in other sources, especially data comparable across countries (Table 2). The arrangements that have been surveyed reflect the outcomes of previous studies examining types of arrangements used in practice to enhance the work–life balance for workers, along with flexibility strategies used by companies (see Anxo et al. 2005, 2006). The list might not be exhaustive but does include the major arrangements currently in use in companies throughout Europe.

In this chapter we examine the work–life balance options not separately but as bundles of arrangements. Among the numerous options to enhance workers' work–life balance, there are substitution as well as complimentary effects. For this reason, what is important is not only the use of a certain arrangement, but also the combination of various arrangements. Chung et al. (2007) show how companies can be categorised into six major types based on their take up of flexibility arrangements. In addition, various working time-related arrangements are not single entities but can be clustered on the basis of similarities between their latent characteristics (Chung 2007; Chung et al. 2007). For this reason examination of the use of a single arrangement or several arrangements separately will not show us the complete picture of how companies behave in the provision of work–life balance schemes. The question is, what type of categorisation of work–life balance we can expect. Based on previous studies of work–life balance options we can predict that work–life balance arrangements can be broken down into three categories, as in Table 1. This categorisation was confirmed empirically through the use of

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<sup>2</sup> There are three reasons why the manager survey was used. First, there were only about 5,000 companies where employee representatives were surveyed and the distribution was not proportional. Second, due to the nature of the questions, especially those seeking information, such as use of various flexible arrangements: it is likely that (human resource) managers know this information better than employee representatives. Finally, many employee representatives did not represent the workforce as a whole, but only part of it.

**Table 2:** *Work–life balance options covered in the ESWT survey*

Main category	Arrangements	Information	Proportion	Note
Working time	Part-time <sup>a</sup>	Use	O	
	Phased retirement <sup>a</sup>	Availability	X	Only surveyed in companies with workers over 50
	Possibility to change from full-time to part-time	Availability	X	
	Flexible working time/schedule <sup>a</sup>	Use	O	
	Working time accounts <sup>a</sup>	Availability	X	Possibility to accumulate hours for full days off
Leaves	Parental leave	Use	X	In past 3 years
	Paternal leave	Use	X	In past 3 years
	Leave for care or illness in family	Availability	X	Paid and unpaid
	Leave for education	Availability	X	Paid and unpaid
	Leave for other purposes	Availability	X	Paid and unpaid
	Early retirement <sup>a</sup>	Availability	X	
Work–life balance facilities/services	Kindergarten/crèche	Availability	X	
	Professional help for child care	Availability	X	
	Professional help for household management	Availability	X	
	Others	Availability	X	

Notes: O indicates the availability of data, X indicates no availability. <sup>a</sup> Only those perceived to be used for workers' needs.

factor analysis of the data (see Annex for more details). The factor analysis outcome shows us that a company will not just use one option on its own, but will probably use similar types of arrangements together: for example, a company that uses part-time work will probably use other types of working time-based work–life balance options, and the same holds true for the use of leave schemes and work–life balance facilities and services.

We shall examine the public–private differences in the provision of three bundles of arrangements: (i) working time arrangements for work–life balance needs; (ii) leave arrangements; and (iii) work–life balance facilities. We shall also examine the extent to which public and private companies differ in the aggregate provision of work–life balance options, that is, the totality of arrangements and facilities. On this basis, we shall arrive at four scores:

1. *Work–life balance through working time* (5 options) = use of part-time work in the employee’s interest + use of phased retirement in the employee’s interest + possibility to change from full-time to part-time on request + flexible working time in the employee’s interest + working time accounts in the employee’s interest (range 0 to 5).
2. *Work–life balance through leaves* (5 options) = parental leave + leave for care + leave for education + leave for other purposes + early retirement in the employee’s interest (range 0 to 5).
3. *Work–life balance through services* (4 options) = use of kindergarten or crèche + help for childcare + help for household management + other services (range 0 to 4).
4. *Total work–life balance option provision* (14 options) = working time score + leave score + services score (range 0 to 14).

For each arrangement, a score of 1 is given if the company uses it and 0 if it does not. Since the working time options and early retirement can be used for either or both workers’ and companies’ needs we consider only those used for the needs of workers. To do this, we use the answers given by managers concerning the motivation behind the exercise of these options. In other words, for these arrangements only those seen to be used to adapt to workers’ needs are included in the count. But it should also be noted that managers may not be entirely neutral or reliable in providing such information, especially when the actual motivation behind the use of these arrangements can differ between individuals. Due to the limited information available, however, managers’ perceptions had to be used.

In order to examine the public–private effect on the use of work–life balance facilities and services within companies, we shall carry out a binary logistic regression. Although four different types of work–life balance services were asked about in the survey, only a few (1,868) companies use one or more services to provide a work–life balance; in other words, the majority of companies do not use them at all. Therefore, we examine only differences between companies that use or do not use WLB services, and disregard the differences between companies that use different arrangements.

### **3. Analysis**

In this section we examine the differences in the provision of work–life balance options between the public and private sectors for the three categories of work–life balance provision. First, we look at the bivariate analysis for cross-country differences and the difference between the public and the private sector. Then we consider the multivariate analysis that controls for other factors that may influence the provision of work–life balance options in order to get an idea of the effect of being in the public sector on the provision of work–life balance options.

#### **3.1 Descriptive bivariate analysis (21-country manager survey)**

First, we shall examine the cross-country variation in the provision of work–life balance options in Table 3 and Figure 1 (scores are all average scores for each country). We can interpret the numbers presented in Table 3 as follows. The first two columns provide the average figures for working time and leave options provided by the average company of each country. The third column shows the percentage of companies within each country with WLB facilities or services. The last column shows the average number of work–life balance options provided, including all working time, leave and facilities. For example, at the average Danish company there are, overall, approximately five options that facilitate the work–life balance needs of workers, two of which are working time options and three are leave schemes. Also, approximately 1 in 20 Danish firms provides at least one work–life balance-related service or facility.

**Table 3:** *Cross-country comparison of work–life balance options in the service sector for 21 European countries (ESWT 2004/2005, manager survey)\* (establishment weighted)*

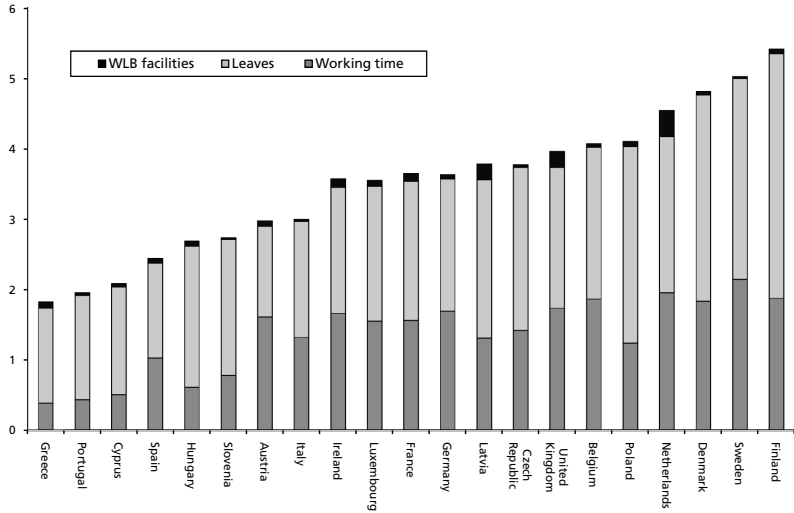
Country	Working time (average number of options)	Leaves (average number of options)	WLB facilities (% of companies with at least one option)	Work–life balance option total (average number of options)
Belgium	1.85	2.17	3.5	4.05
Denmark	1.82	2.94	4.7	4.90
Germany	1.68	1.89	5.2	3.68
Greece	0.39	1.33	7.7	1.75
Spain	1.02	1.36	6.1	2.47
France	1.55	1.99	9.0	3.65
Ireland	1.65	1.80	11.3	3.52
Italy	1.31	1.66	3.1	2.98
Luxembourg	1.54	1.93	7.3	3.63
Netherlands	1.94	2.23	34.4	4.64
Austria	1.60	1.30	7.0	2.96
Portugal	0.44	1.46	4.1	2.08
Finland	1.86	3.48	6.5	5.52
Sweden	2.15	2.84	3.1	5.03
UK	1.72	2.01	18.2	4.01
Czech Republic	1.41	2.32	2.8	3.78
Cyprus	0.51	1.53	3.8	2.11
Latvia	1.30	2.26	20.7	3.70
Hungary	0.61	2.01	5.1	2.70
Poland	1.23	2.80	6.6	4.15
Slovenia	0.78	1.94	1.5	2.80

*Note:*

\* For each score the number of companies included (N) is different. This is because there were different options that managers did not answer. For working time options there were 3,808 cases missing; for leave, 4,530 (4,611 including paternal leave) cases; and for facilities 212 cases. Overall this means that 6,645 (6,706) cases were missing altogether. For the services sector, of the 12,402 service companies, 3,942 (3,987) – approximately 32% – cases were missing due to a lack of information on at least one of the questions. This was due to 2,662 (2,720) missing cases for leave scores, 2,265 missing cases for working time scores and 139 missing cases for facilities scores.

Working time score (count method, ranging from 0 to 5), Leave score (count method, ranging from 0 to 5), WLB facilities (use or non-use of work–life balance services: 1 if used, 0 if not used), Total score (count method, ranging from 0 to 14); see Section 2 above for calculation methods.

**Figure 1:** *Cross-country variation in the provision of work–life balance options for 21 European countries (service sector; ESWT 2004/2005 manager survey) (establishment weighted)*



*Note:* Working time score (count method, ranging from 0 to 5), Leave score (count method, ranging from 0 to 5), WLB facilities (count method, ranging from 0 to 4), Total score (count method, ranging from 0 to 14); see Section 2 above for calculation methods.

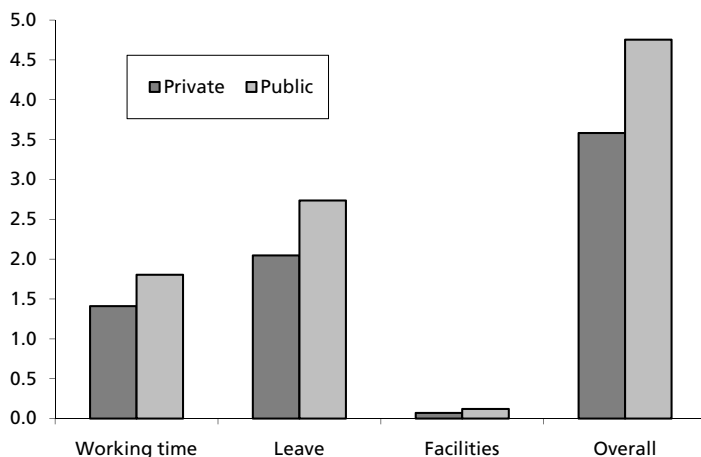
Figure 1 presents the average number and composition of work–life balance options provided in each country. Here the WLB facilities comprise the average number of options provided in each country, unlike the percentages of companies with at least one WLB facility presented in Table 3. As we can see from Figure 1, companies in Northern European countries – Finland, Denmark, Sweden, along with the Netherlands – provide the most work–life balance options. They score highly on both working time and leaves. The Netherlands scores the highest on the provision of work–life balance facilities with approximately 0.4 facilities per company. On the other hand, in the Southern European countries (Cyprus, Greece, Portugal, Spain and Italy), along with Austria, Slovenia and Hungary, companies have the lowest level of work–life balance provision, including both leaves and working time options. There is no clear distinction between the Anglo-Saxon countries and the continental European countries, which contrasts with what one might expect given welfare state regime typologies (Esping-Andersen 1990; 1999). This may be due to the fact that here we are examining the company level, which is different from national level institutions. Companies do not



necessarily mirror macro-institutions and many other aspects come into play in companies' policies in the provision of work–life balance options. Also, we can see that the new member states do not form a strong cluster on their own, but are scattered over the distribution. Poland, Czech Republic and Latvia are similar to the continental European and Anglo-Saxon country levels, while Slovenia, Hungary and Cyprus are close to the Southern European countries.

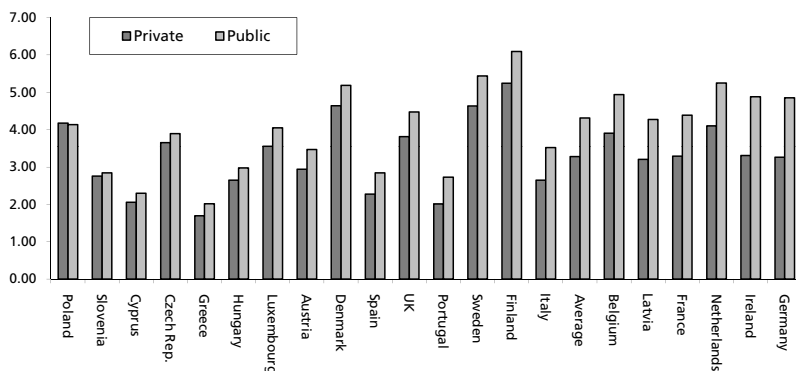
Now we turn to the public and private sector differences in the provision of work–life balance options in the 21 countries. As we can see in Figure 2, for the average European company within the 21 countries in the ESWT the public sector provides more work–life balance options in all three categories, as well as overall. On average, the public sector provides approximately one WLB option more, compared to the private sector. The differences in the provision of WLB options between public and private companies are statistically significant for all four accounts. But this is not always true. Figure 3 shows the public–private sector differences in the provision of work–life balance options overall, by country. In Germany, Ireland, the Netherlands, France, Latvia and Belgium the public–private differences are much larger than in the other countries. Companies in Poland, Slovenia,

**Figure 2:** *Differences in the provision of work–life balance options for companies in the service sector, average for 21 European countries*



Source: ESWT 2004/2005, manager survey – establishment weighted.

**Figure 3:** Cross-country variance in the difference between the public and private sectors in the provision of work–life balance options for 21 European countries



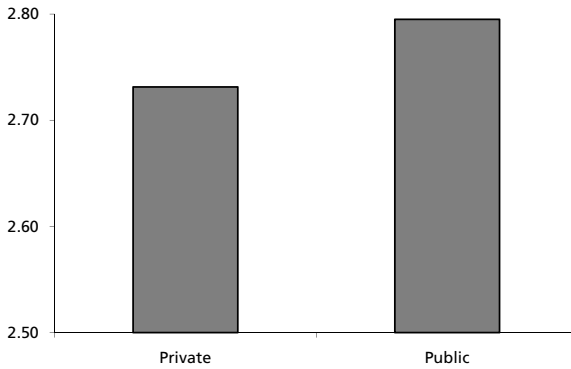
Source: ESWT 2004/2005, manager survey – establishment weighted.

Cyprus, Czech Republic, Greece and Luxembourg<sup>3</sup> exhibit no significant differences between the two sectors, and public and private companies seem to provide the same amount of WLB options. For all other countries, the public company effects are statistically significant.

As far as the perceptions of workers and managers are concerned, on average employee representatives in the public sector say that it is easier to combine work with other obligations compared to those in the private sector, and this difference is statistically significant in the 90% confidence interval (Figure 4). This is also the case if we examine managers' perceptions of company responsibility to facilitate workers' work–life balance. On average, more public sector managers answer that it is the company's responsibility to help workers to achieve a positive work–life balance than private sector managers, and this difference, although small, is statistically significant (Figure 5). But there are important country differences. In Greece, United Kingdom, Luxembourg and – to some extent – Spain, the Netherlands and France,

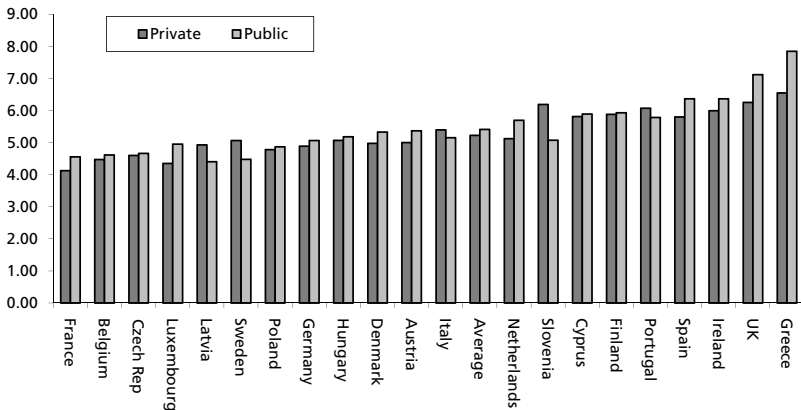
<sup>3</sup> In the case of Luxembourg, the difference between the two sectors is significant in the 90% confidence interval but not at the 95% level. Luxembourg also has low significance because of the low number of cases included, due to its size.

**Figure 4:** *Perceived ease of combining work–life responsibilities, average for 21 European countries*



Source: ESWT 2004/2005, manager survey – establishment weighted.

**Figure 5:** *Management's perceived company responsibility for facilitating worker's work–life balance, country averages for 21 European countries*



Source: ESWT 2004/2005, manager survey – establishment weighted.

public sector managers are more inclined to feel that it is the company's responsibility to take workers' work–life balance into account than private sector managers. On the other hand, in Slovenia, Sweden, Portugal and, to some extent, Latvia the opposite holds true. In all other countries there are no significant differences between managers' perceptions. In addition, it is strange that although in the Southern European countries, along with the United Kingdom and Ireland, managers declare that companies should consider the personal lives of their employees, in reality the provision of work–life balance options is the lowest in these countries. This may be because few work–life balance options are provided by the macro-institutional framework.

Although a descriptive analysis gives us a broad picture of the provision of work–life balance options across Europe and differences between the public and private sector, to see more precisely the effect of being within the public sector we must control for other factors. In Section 3.2 we will therefore examine the outcome of the multivariate analysis.

### **3.2 Multivariate analysis**

In this section we examine the outcome of the multivariate analysis that explains the provision of work–life balance options in European companies. The multivariate analysis takes into consideration how various firm characteristics can affect the provision of WLB arrangements within a company. It controls for these effects to show us the true effect of being in the public sector. We use the multi-level model or the random effects model in this chapter, which allows for the examination of cross-country differences in the effects of being in the public sector. Multi-level analysis enables us to see the contextual effect of being in a certain country by treating each country as a different group, similar to modelling each country separately. In addition, we examine the various interaction effects of the explanatory variables with the public sector. This allows us to see the added effect of certain characteristics of the public sector in comparison to the private sector. For example, we can see whether a high proportion of female workers within the company increases the number of WLB options and whether this effect is stronger for private or for public companies. In other words, in this chapter we examine (i) the effect of being in the public sector on the average European firm (fixed effects), (ii) differences between this effect between countries (random effects), and (iii) differences between the effect of the explanatory factors (company characteristics) between the public and private sectors (interaction terms). For each dependent variable, we arrive at the best fit model based on the goodness of fit and the theoretical explanation of the models.

The explanatory variables used in this chapter to control for other factors that may influence the provision of work–life balance options are the country the firm is located in and a number of company characteristics.<sup>4</sup> The latter include the sector of activity, being in the public or private sector, size, workforce composition (the proportion of females, skilled, young and older workers), whether or not the company has a collective agreement on working time, whether or not the company has an employee representative body (a union or a works council), daily, weekly or annual workload variation and whether this is foreseeable, and finally whether the company is doing well or badly economically.

The dependent variables are the number of working time-related WLB arrangements in the company, the number of leave-related WLB arrangements, whether the company has any WLB service or facilities within the company and finally the number of WLB arrangements, including the three previously mentioned arrangements.

#### *The average European firm*

Here we examine the regression analysis for the provision of work–life balance options of European companies (Table 4). First, we examine the regression analysis for each category of work–life balance options, that is, for working time, leaves and facilities. For the first two types of option we use linear regression models, while for the other (facilities) we use a logit model that calculates the probability of having one or more facilities in the company. We use both the multi-level model, which puts country as the second level, as well as interaction terms for significant effects.

There are sectoral differences in the provision of work–life balance options for all three categories. Financial intermediation, public administration and health and social work have more work–life balance in all three accounts than retail and repair, controlling for other factors. Other social services also have more options than retail and repair concerning both working time and leaves, but the odds of having work–life balance facilities do not differ significantly from those of retail and repair. Hotels and restaurants have about the same amount of working time options as retail, and the probability of this sector having work–life balance facilities is also about the same. But it has significantly fewer leave options. Transport and storage, on the other hand, is alike in terms of both leaves and facilities, but it has significantly fewer working time options. Real estate, renting and business activities have

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<sup>4</sup> For the theoretical reasoning behind the factors selected, see Chung (2007b).

significantly more working time options while having the same amount of leave options and about the same probability of having work–life balance schemes. Education is similar to retail and repair in terms of both working time and work–life balance facilities, while having more leave options.

The number of company employees has significant positive effects on all three categories of work–life balance options. In other words, larger companies usually have more arrangements for WLB, whether working time-related, leave-related or various services and facilities. Workforce composition is also important in predicting the number of work–life balance options provided. The proportions of female and skilled workers significantly influence the number of working time and leave options. Also, companies with a larger proportion of older workers have more working time options, although this effect does not hold true for leaves and work–life balance facilities. The effect of workforce composition on the provision of WLB options can be bi-directional. In firms with more women and/or older workers, there may be a greater need for various work–life balance options. At the same time, for firms to recruit and maintain female and older workers, they may have to provide more options than other companies. The same holds true for companies that employ skilled workers. Also, skilled workers may have more bargaining power to demand more WLB options.

Companies with collective agreements on working time have more working time options and leaves and have a higher probability of providing work–life balance facilities than those without. This may be because having a collective agreement increases the possibility of including various types of options. But one might also suspect a reverse causality in this relationship, where companies with more options have working time agreements. In other words, initially there may have been unsystematic use of various options, but as such use increased a need might have arisen to draw up a more formal agreement.

Workload variations also seem to affect the provision of work–life balance options, although this differs between different types of work–life balance. For work variations within a day, it decreases the number of working time options that are used for work–life balance in a company, while it increases the odds of having one or more work–life balance facilities within the firm. Longer variations, such as variations of work within a week or a year, increase the number of leaves offered in the company. Companies with work variation within a year also have more working time options than those without. Finally, companies with good or better economic situations have more work–life balance options. They may be in a better position to afford such provisions, but this effect can also be characterised by reverse causality,

where companies with more work–life balance options due to enhanced productivity, decreased absenteeism or other reasons may do better economically.

**Table 4:** *Multi-level regression analysis outcome for work–life balance options provision for 21 EU countries (ESWT 2004/2005) – fixed part*

	Working time		Leaves		Services	
	B	Stand. Error	B	Stand. Error	odds	Stand. Error
(Constant)	R 1.227***	0.106	R 1.753***	0.133	R [0.045]***	0.235
Hotel and restaurants	-0.019	0.047	-0.152***	0.056	1.124	0.163
Transport, storage	-0.128***	0.042	0.049	0.049	1.247	0.139
Financial intermediation	0.251***	0.054	0.155**	0.062	1.935***	0.150
Real estate, renting and business activities	0.241***	0.034	0.071	0.040	1.240	0.116
Public administration	0.295***	0.050	0.262***	0.056	2.010***	0.144
Education	-0.012	0.054	0.305***	0.061	1.323	0.165
Health and social work	0.122**	0.050	0.336***	0.058	1.974***	0.144
Other social services	0.215***	0.054	0.133**	0.062	1.218	0.174
Public sector	R -0.108	0.068	R 0.118	0.062	R 1.292	0.145
Number of employees <sup>1</sup>	0.118***	0.009	0.175***	0.009	1.174***	0.022
Female proportion <sup>1</sup>	0.106***	0.010	0.089***	0.010	1.054	0.028
Skilled proportion <sup>1</sup>	0.039***	0.007	0.037***	0.009	1.001	0.023
Younger proportion <sup>1</sup>	-0.020	0.011	0.009	0.014	0.955	0.037
Older proportion <sup>1</sup>	0.029**	0.013	-0.028	0.015	0.992	0.041
Working time agreement	0.124***	0.025	0.151***	0.030	1.297***	0.082

ER body exists	R 0.085	0.046	R 0.239***	0.054	1.023	0.084
Variation within a day	–0.062***	0.028	0.063	0.033	1.225***	0.083
Variation within a week	0.031	0.025	0.100***	0.029	0.995	0.077
Variation within a year	0.064**	0.027	0.122***	0.026	1.017	0.067
Economic situation <sup>1</sup>	0.053***	0.018	0.075***	0.020	1.204***	0.054
Public*female	–0.049***	0.018	–	–	–	–
Public*size	0.045***	0.014	–	–	–	–
Public*seasonal variation	0.117***	0.046	–	–	–	–
N	9107		8649		10 837	
–2*loglikelihood	26 052.850		26 971.180			

*Notes:* \*\*\* :  $p < 0.001$ , \*\* :  $p < 0.05$ , \* :  $p < 0.1$ . Reference category for sector: retail and repair. R: indicates random terms. 1: these scores were centred so that the average shows the median category of the variables. In other words, the average represents the company with 50 to 99 workers, with 40 to 60 per cent of female workers, skilled workers, younger workers and older workers, and whose economic situation is quite poor.

In the model, we also included interaction terms to examine the differences in the effects of various factors between the public and private sectors. This shows us the additional effect of that specific variable for public sector companies, in comparison with its effect for private sector companies. For the leave or facilities models, none of the interaction terms with the public sector were significant, and so we have not included them. But three interaction terms were significant in the model for working time work–life balance options. First, size of company affects the number of working time-related options in the public sector more than in the private sector. Also, the relationship between seasonal variation in workload and the provision of work–life balance working time options is stronger in the public sector. Lastly, we can see that the effect of the female proportion of the workforce was different for the public and private sectors; although a higher share of female workers also means more working time work–life balance options for the public sector, the effect is not as strong as in the private sector. In previous literature, it has been noted that the public sector may have more work–life balance options due to the fact that it employs more women and is under pressure to enhance gender equality policies (see Section 1). But examination of the European average firm shows that the size of the female proportion of the workforce does not affect the public sector as much as the private sector. This may be due to the fact that the public sector has more options in general.



The most important conclusion for the present chapter is that for the average European firm there is no significant relationship between being in the public sector and providing more WLB options in any of the three categories. This contrasts with what we find in the previous section with our bivariate analysis (see Figure 2). This tells us that after taking account of the effects of various company characteristics, such as sector, size, composition, existence of collective agreements and employee representatives, as well as economic situation and work variation, the differences between private and public companies become insignificant. But this holds true only for the European average and this effect varies across the 21 EU countries examined here.

**Table 5:** *Cross-country effects for factors that affect work–life balance options provision for 21 EU countries (ESWT 2004/2005) – multi-level analysis random effects*

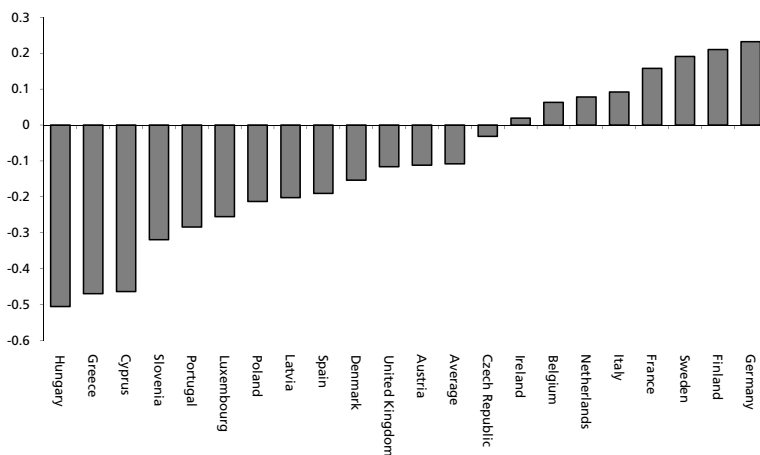
	Working time		Leaves		Services	
	Variance	Stand. Error	Variance	Stand. Error	Variance	Stand. Error
<i>Level 2 variance</i>						
Constant	0.195***	0.062	0.314***	0.100	0.724***	0.238
Public	0.060***	0.023	0.045**	0.020	0.204***	0.098
ER body exists	0.027**	0.012	0.039**	0.017		
<i>Covariance with constant</i>						
Public	0.074**	0.031	−0.063*	0.035	−0.032	0.110
ER body exists	0.044**	0.021	−0.076**	0.035		
<i>Level 1 variance</i>						
Constant	1.008***	0.015	1.304***	0.020		

Note: \*\*\* :  $p < 0.001$ , \*\* :  $p < 0.05$ , \* :  $p < 0.1$ .

As we can see from Table 5, with the multi-level model we find that there are variations between countries due to being in the public sector. In addition, the effect of having an employee representative differs concerning the provision of work–life balance options, and the average number of options provided in the average company for each country is also different. Here we will examine only the variance between countries due to being in the public sector and how that variance is related to the average number of arrangements provided.

First, for working time-related WLB options, for the average European company we find a statistically non-significant negative relationship between the number of arrangements provided in the company and whether the

**Figure 6:** Cross-country variance in the effect of being in the public sector in the provision of WLB working time options for 21 European countries



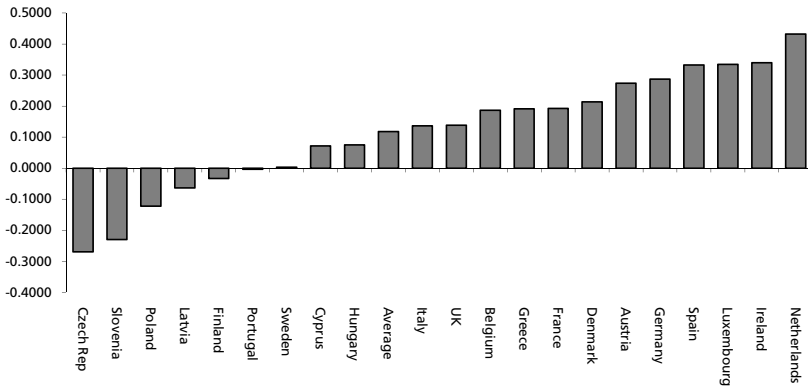
Source: ESWT 2004/2005 manager survey.

company was a public company. But as we can see in Figure 6, this effect differs across countries. The public sector in Germany, Finland, Sweden and France provides more working time options than the private sector, even when other characteristics are controlled for. German public companies, for example, provide 0.2 more options than private ones. On the other hand, in the Southern European countries and the new member states the negative effect of being in the public sector is bigger. Hungarian public companies, for example, provide on average approximately 0.5 less working time WLB arrangements in comparison to their private counterparts. The same applies to public companies in Greece and Cyprus.

On closer inspection (Annex 3), it seems that in the countries where the number of options provided in the average firm is higher, the effect of being in the public sector is often positive and bigger. For countries where there are few WLB working time options in general, it is more likely that private companies will use them, while public companies will not use them at all<sup>5</sup> or

<sup>5</sup> For example, in the average public company in Greece, Portugal, Hungary and Cyprus the average number of options used is close to 0.

**Figure 7:** *Cross-country variance in the effect of being in the public sector on the provision of WLB leave options for 21 European countries*



Source: ESWT 2004/2005 manager survey.

not as much. In countries where working time options are used widely and more frequently, however, there are few differences between private and public companies in terms of how many options they use, and it may be that public companies actually use more than private ones.

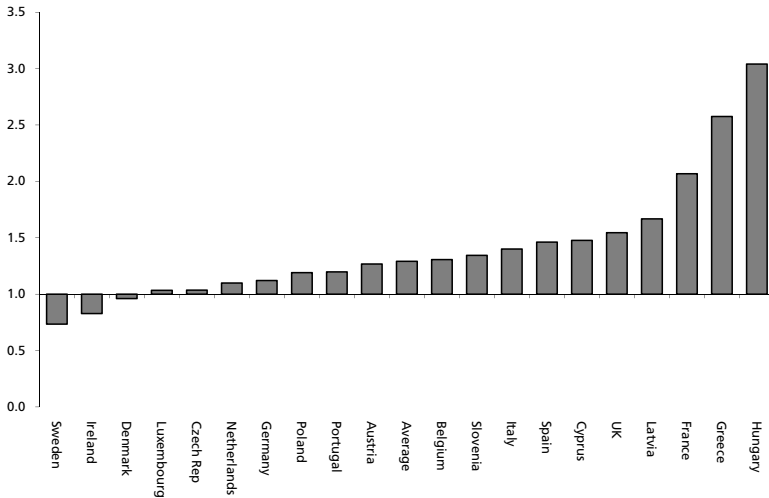
The effect of being in the public sector on the provision of work–life balance leave schemes for the average European firm is positive, although not significant. However, similar to the case for working time, there are large cross-national variations. As we can see from Figure 7, in most new member states (the Czech Republic, Slovenia, Poland and Latvia) being in the public sector decreases the number of leave schemes within the firm. For Finland, Portugal and Sweden, there seems to be no difference between the public and private sectors. On the other hand, there are countries where the effect of being in the public sector is significantly stronger than the European average, in particular the Netherlands, Spain, Germany and also Ireland and Luxembourg. In these countries the public sector provides more leave schemes than its private counterpart. In the Netherlands, where the gap between public and private companies is the largest, public companies have on average 0.4 more leave arrangements than private companies in the same sector with the same company characteristics.

In contrast to working time arrangements, there seems to be a slight negative relationship between the average number of leave options within a country

and the effect of being a public company in that country (see Annex 3). In other words, in the countries in which there are more leave schemes in general, the effect of being in the public sector is small or negative, whereas in those countries in which on average there are few leave schemes, the public sector has more options than the private one, even when we take account of other relevant factors. This means that, especially in countries in which companies do not provide many leave options, workers are much better off being employed in public companies because they will provide more leave arrangements. In countries in which the use and provision of leave schemes are common, however, it does not matter much whether the company is public or private; they will provide approximately the same number of leave arrangements. But this does not hold true in the new accession countries where public companies provide more leave options in most cases.

As far as WLB facilities are concerned, when we take other company characteristics into account the differences between public and private companies found in Figure 2 cease to be significant. But again, as we found for working time and leave arrangements, there are country variances in this relationship as well (Figure 8). For countries such as Hungary, Greece and

**Figure 8:** *Relative odds of public companies having one or more WLB facilities in comparison to private companies*



Source: ESWT 2004/2005 manager survey.

France, there seems to be a significant positive public sector effect, and public sector companies have higher odds of having one or more WLB facilities. For other countries, there seem to be no significant differences between private and public companies.

#### *Total work–life balance arrangements*

We shall now examine the effect of being in the public sector on the provision of work–life balance arrangements, combining all three categories (Table 6). First, examining the sectoral differences it seems that retail and repair, along with hotels and restaurants and transport and storage, are all similar in their provision of work–life balance options and they provide fewer options on average than any other service category. Public administration and health and social work provide the most, even if we control for other factors. Company size is another important factor: larger firms provide more work–life balance options than smaller firms. Also, the proportion of both females and skilled workers in the workforce positively affects the provision of work–life balance options. This supports the hypothesis that the needs of workers and companies' interest in recruiting and maintaining certain workers lead to work–life balance options being provided more in companies with a higher proportion of female workers and skilled workers. But unlike working time options, the proportion of older workers does not affect the provision of work–life balance options overall. Companies with working time collective agreements have more options, as do those with employee representatives. The effect of work variation on the provision of options differs between working time, leaves and facilities. Overall, it is the longer term variations – that is, the variation of workload within a week and within a year – that affect the provision of work–life balance options, whereas workload variations within a day, which affected the provision of WLB facilities, do not have significant effects. Also, in all three cases companies with better economic situations seem to have more work–life balance options. Lastly, as in the case of working time options, the effect of the proportion of females within the workforce is smaller in the public sector. In other words, although in both sectors the more female workers there are, the greater the chances that the company will provide more WLB options, female work composition has a stronger effect in the private sector than in the public sector. This goes against the notion that the public sector has more options due to the large number of female employees. But it may also be the case that due to the high proportion of female workers in the public sector in general, the exact proportion of female workers for a given company does not matter much.

**Table 6:** Multi-level regression analysis outcome for total work–life balance options provision for 21 EU countries (ESWT 2004/2005) – fixed part

	Total work–life balance options	
	B	Stand. Error
(Constant)	R 3.013 <sup>***</sup>	0.204
Hotel and restaurants	–0.116	0.091
Transport, storage	–0.073	0.079
Financial intermediation	0.476 <sup>***</sup>	0.101
Real estate, renting and business activities	0.342 <sup>***</sup>	0.066
Public administration	0.638 <sup>***</sup>	0.092
Education	0.317 <sup>***</sup>	0.100
Health and social work	0.545 <sup>***</sup>	0.093
Other social services	0.345 <sup>***</sup>	0.101
Public sector	R 0.097	0.103
Number of employees <sup>1</sup>	0.328 <sup>***</sup>	0.014
Female proportion <sup>1</sup>	0.206 <sup>***</sup>	0.020
Skilled proportion <sup>1</sup>	0.085 <sup>***</sup>	0.014
Younger proportion <sup>1</sup>	–0.032	0.022
Older proportion <sup>1</sup>	–0.006	0.025
Working time agreement	0.325 <sup>***</sup>	0.048
ER body exists	R 0.322 <sup>***</sup>	0.093
Variation within a day	0.019	0.053
Variation within a week	0.126 <sup>***</sup>	0.047
Variation within a year	0.226 <sup>***</sup>	0.041
Economic situation <sup>1</sup>	0.157 <sup>***</sup>	0.033
Public*female	–0.095 <sup>***</sup>	0.033
N	7634	
–2*loglikelihood	30 213.140	

Note: \*\*\* :  $p < 0.001$ , \*\* :  $p < 0.05$ .

Reference category for sector: retail and repair.

R: indicates random terms.

1: these scores were centred (see Table 5, footnote 15).

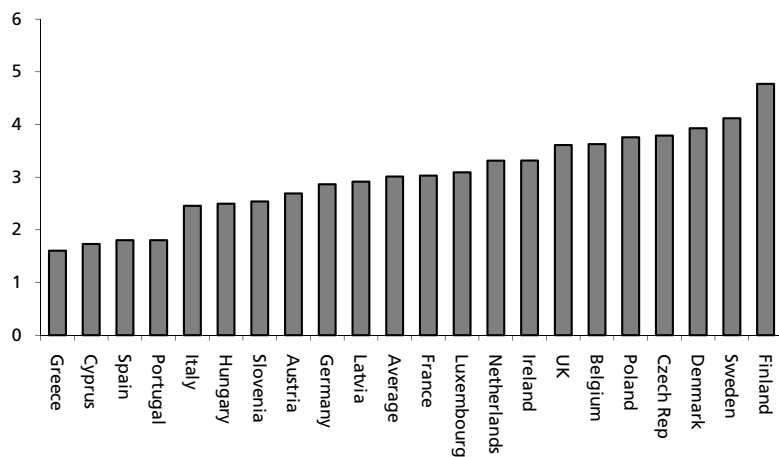
As was to be expected, there are differences in the average number of WLB options provided in the 21 European countries under examination (Figure 9). This is based on the significant variance in the constant term in the random part of the model (Table 7). However, the average number of arrangements and positioning of countries shown in Figure 9 differs from the one shown in Figure 1. The scores in Figure 9 tell us the country average when controlling for the company characteristics that affect WLB provision, such as size and workforce composition. In other words, these scores provide the pure country effect, when everything else is held constant.

Companies in the Nordic countries – that is, in Finland, Sweden and Denmark – have most arrangements to balance work and life on average, compared to other European countries. Also in the Czech Republic, Poland, Belgium and the United Kingdom significantly more WLB options are provided compared to the European average. On the other hand, Southern European countries, such as Greece, Cyprus, Spain, Portugal, Italy and Hungary, provide significantly fewer WLB options. Hence, the two extremes of the distribution are occupied at the high end by the social democratic Nordic country group, and at the low end by the conservative Southern European country group, similar to what we would expect following the welfare state regime typology literature (Esping-Andersen 1990, 1999). Contrary to the Esping-Andersen typology, however, there is not a big difference between the continental European countries and the Anglo-Saxon

**Table 7:** *Cross-country effects for factors that affect total work–life balance options provision for 21 EU countries (ESWT 2004/2005) – multi-level analysis random effects*

	Total work–life balance options	
	Variance	Stand. Error
<i>Level 2 variance</i>		
Constant	0.724***	0.231
Public	0.123**	0.054
ER body exists	0.120**	0.052
<i>Covariance with constant</i>		
Public	0.059	0.080
ER body exists	–0.010	0.078
<i>Level 1 variance</i>		
Constant	3.007***	0.049

Note: \*\*\* :  $p < 0.001$ , \*\*:  $p < 0.05$ .

**Figure 9:** Average number of WLB arrangements across 21 European countries

Source: ESWT 2004/2005 manager survey.

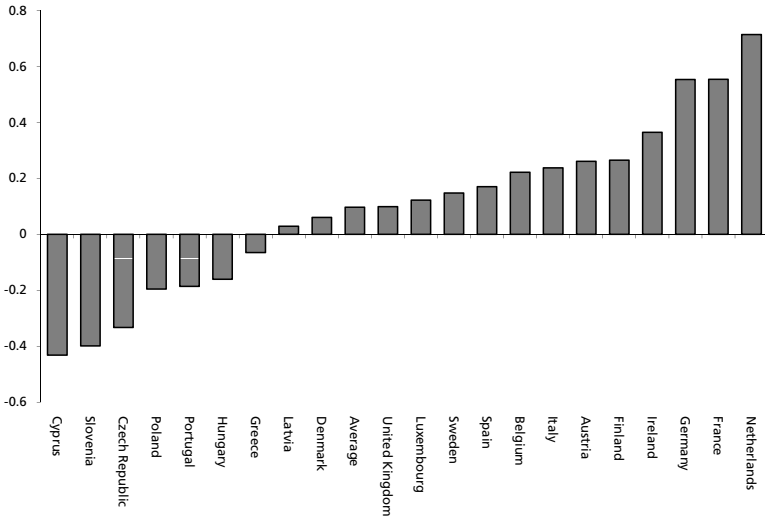
ones; also, the new member states do not form a distinct group of their own and are rather spread around.

Similar to the results of the three subcategories of WLB arrangements, the effect of being in the public sector was not significant in this model. This entails that the effect found in Figure 2 was cancelled out due to differences in terms of sector of activity, size, composition and other characteristics. However, again like the WLB subcategories, there seems to be a large country variance in this effect, where some countries have positive public sector effects and others have negative public sector effects (Figure 10). This could be expected just by looking at the country variance of the three subcategories of WLB arrangements, where for all three categories there was large public-effect variance across countries. What we can expect here is the combined effect of the three subcategories.

In countries such as the Netherlands, France, Germany and, to some extent, Ireland, the public sector is indeed better at providing WLB options. On the other hand, in Cyprus, Slovenia and the Czech Republic the public sector does worse than its private counterpart. For other countries the public and private sectors do not differ much in the provision of WLB options, when all



**Figure 10:** *Cross-country variance in the effect of being in the public sector on the provision of WLB options for 21 European countries (ESWT 2004/2005 manager survey)*



other relevant company characteristics are controlled for. Also, in the new member states the private sector does better than the public sector in the provision of WLB options, as was the case in working time options and leave schemes.

## Conclusions

This chapter examined private and public sector differences in working conditions, focusing on the provision of work–life balance options for workers in European companies. Here, WLB options are looked at in terms of overall usage, as well as divided into the categories of working time, leaves and work–life balance facilities. This is based on previous studies on work–life balance and factor analysis outcomes that show that WLB options can be distinguished into three categories. The results of the study show that at first glance public companies are indeed better on average in delivering WLB options in all three categories. In addition, employee representatives in public companies state that it is easier to combine work with other obligations than in private companies, while managers in public companies seem to feel that companies have more responsibility to take workers’ WLB into account.

Differences in the provision of WLB options between public and private companies cease to exist when we take various other relevant factors into account for the average European firm. On closer inspection, although we find this relationship in the average European firm, there are significant cross-country differences. That is, although the public sector effect of provision of WLB options overall is minimal for the average European firm, one can find negative effects in new accession countries and some Southern European countries, as well as positive effects for most of the EU-15. This effect differs for each type of WLB option. Concerning leave schemes, public companies seem to fare rather well in their provision, especially in EU-15 countries, while this is not the case for the new accession countries. Looking at working time schemes, private companies seem to use them more often, particularly in Southern European and new accession countries. Also worth noting is the fact that differences between public and private companies are affected by the overall prevalence of WLB options within countries. In countries in which there are few working time options, private companies seem to use more working time-related WLB arrangements than public companies; on the other hand, in countries in which there are few leave arrangements, public companies provide much more leave schemes than private companies.

These analysis outcomes imply that differences in the provision of WLB options between public and private companies vary depending on various types of WLB schemes and across different countries, or different country groupings. It also indicates that privatisation may have different implications for the working conditions of workers in different countries. For new accession countries, privatisation may actually increase the number of WLB options provided by firms, whereas for Southern European companies privatisation may lead to a shift from leave-based WLB schemes to working time-based WLB schemes. For the other European countries, privatisation may also reduce the number of options overall, especially leave schemes.

Although we have not directly addressed changes in working conditions at privatised companies, we do have some clue as to what kind of effect privatisation might have. To confirm the analysis, more in-depth studies on the effects of privatisation must be carried out on longitudinal time series data. From this analysis, however, it is clear that the results of privatisation are likely to be complex and diverse, and generalisations, especially across countries, may not be possible.

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## [Annex 1] Factor analysis of work–life balance options

Using principal component factor analysis (for more on this types of analysis, see <http://www.statsoft.com/textbook/stathome.html?stfacan.html&1>), we first arrive at five factors (Table A1). Among these five factors there is a distinct leave factor, where all leave arrangements have high factor loadings, with the exception of parental leave and early retirement. Furthermore, there is a distinct work–life balance facilities factor, with the arrangements for work–life balance facilities/services having high factor loading, with the exception of other services. Working time arrangements are divided into three factors: (i) flexible working arrangements and working time accounts, (ii) the two retirement schemes, and (iii) part-time, the possibility to change to part-time and parental leave. However, if we restrict ourselves to three

**A1:** *Principal component factor analysis, using varimax – five factor outcome*

Variable	Factor1	Factor2	Factor3	Factor4	Factor5	Uniqueness
Part-time	0.0219	0.1001	<b>0.7672</b>	0.0265	0.0416	0.3985
Flexible working time	0.0489	<b>0.8815</b>	0.0575	0.0200	0.0200	0.2164
Reduction of working hours	0.1673	0.1124	<b>0.6725</b>	0.0496	0.1381	0.4856
Working time account	0.0924	<b>0.8660</b>	0.0933	0.0122	0.0617	0.2289
Phased retirement	0.1091	0.0950	0.2980	0.0238	<b>0.6875</b>	0.4170
Parental leave	0.1455	0.0844	<b>0.6010</b>	−0.0054	−0.0604	0.6068
Leave for care	<b>0.8006</b>	0.0579	0.0969	0.0393	0.0553	0.3418
Leave for education	<b>0.8189</b>	0.0954	0.0863	0.0059	0.0572	0.3095
Leave for other reasons	<b>0.6674</b>	0.0589	0.0098	0.0210	0.0802	0.5441
Early retirement	0.0591	0.0309	−0.0633	−0.0023	<b>0.8423</b>	0.2820
Kindergarten	0.0233	0.0059	0.0334	<b>0.6546</b>	0.0426	0.5680
Help for child care	0.0182	0.0381	0.0841	<b>0.6750</b>	0.0232	0.5349
Help for house management	0.0456	0.0236	−0.0353	<b>0.6584</b>	−0.0422	0.5608
Other WLB facilities	0.1180	0.0349	−0.0932	0.0895	0.1460	0.9468

Note: Explained variance: 53.99%.

factors for simplicity’s sake (Table A2), we get more distinct working time-related arrangements, leave arrangements and work–life balance facilities factors. Early retirement now loads on the leave factor, and phased retirement on the working time factor. However, parental leave remains with the working time factors, and other work–life balance services do not show a high loading on any one factor.

**A2:** *Principal component factor analysis, using varimax – three factor outcome*

Variable	Factor1	Factor2	Factor3	Uniqueness
Part-time	0.1475	<b>0.5120</b>	0.0859	0.7088
Flexible working time	-0.0119	<b>0.7462</b>	0.0012	0.4430
Reduction of working hours	0.2953	<b>0.4741</b>	0.0985	0.6783
Working time account	0.0479	<b>0.7574</b>	-0.0041	0.4241
Phased retirement	0.3369	<b>0.3486</b>	0.0322	0.7640
Parental leave	0.2100	<b>0.3815</b>	0.0425	0.8086
Leave for care	<b>0.7803</b>	0.0498	0.0424	0.3868
Leave for education	<b>0.7936</b>	0.0740	0.0072	0.3646
Leave for other reasons	<b>0.6480</b>	0.0167	0.0169	0.5796
Early retirement	<b>0.2808</b>	0.1261	-0.0246	0.9047
Kindergarten	0.0340	0.0146	<b>0.6537</b>	0.5713
Help for child care	0.0291	0.0656	<b>0.6778</b>	0.5354
Help for house management	0.0185	-0.0250	<b>0.6530</b>	0.5726
Other WLB facilities	0.1339	-0.0098	0.0775	0.9760

*Note:* Explained variance: 37.73%.

## Annex 2: Variables used in the study

### Variables used

#### *Independent variables:*

A: *Country* (used as level 2 in the model)

B: Company characteristics:

1. Sector: 9 categories – Retail and repair/Hotels and restaurants/Transport, storage and communications/Financial intermediation/Real estate, renting and business activities/Public administration/ Education/Health and social work/Other community, social and personal services (reference: retail and repair<sup>8</sup>)
2. Public or private sector
3. Size – 6 categories<sup>9</sup>
4. Composition<sup>10</sup> – proportion of female workers (5 categories), skilled workers (5 categories) workers younger than 30 (5 categories), workers older than 50 (5 categories)
5. Collective agreement on working time – dummy
6. Existence of employee representative body – dummy
7. Workload variation – daily (dummy), weekly (dummy) seasonal (dummy) foreseeable daily (dummy), foreseeable weekly (dummy), foreseeable seasonal (dummy)
8. Economic situation of the company – 4 scale<sup>11</sup>

#### *Dependent variables:*

1. Provision of various working-time flexibility schemes for workers
2. Provision of various leave schemes
3. Provision of various work–life balance facilities/services (dummy)
4. Provision of overall work–life balance options

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<sup>8</sup> Here retail and repair was selected as the reference category since it was the largest service sector in this survey.

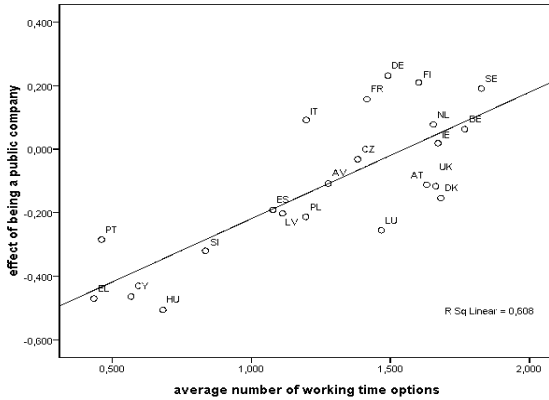
<sup>9</sup> For this variable six categories were distinguished: 10 to 19, 20 to 49, 50 to 99, 100 to 199, 200 to 499, and 500 or more.

<sup>10</sup> For this variable five categories were distinguished: less than 20%, 20% to less than 40%, 40% to less than 60%, 60% to less than 80%, and 80% or more.

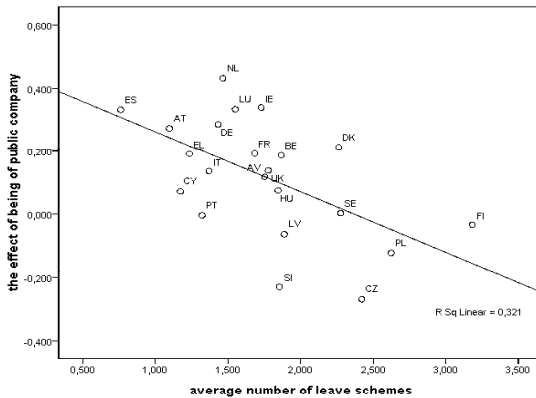
<sup>11</sup> For this variable four categories were distinguished: very bad, quite bad, quite good, very good

### Annex 3: Relationship between average numbers of WLB options and the effect of being in the public sector

**Figure A1:** Relationship between average numbers of WLB working time options provided in a country and the effect of being in the public sector (ESWT 2004/2005 manager survey)



**Figure A2:** Relationship between average number of leaves provided in a country and the effect of being in the public sector (ESWT 2004/2005 manager survey)







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