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BOOK REVIEWS

T. Boeri – A. Börsch-Supan – A. Brugviani – R. A. Kapteyn – F. Peracchi (eds):
Pensions: More Information, Less Ideology
Boston/Dordrecht/London: Kluwer Academic Press, 2001, 196 pp.

As its subtitle suggests, the book addresses a very important task for 21st century economics: assessing the long-term sustainability of European pension systems – data requirements, analysis and evaluations. The list of editors is promising, although most of the participants are opponents rather than proponents of the present continental system (an unfunded public system).

As is well known, birth rates are dropping below equilibrium values in the First and Second Worlds, while life expectancy is still spectacularly growing in the First World. Small wonder, therefore, that many forecasters speak and write about an old age crisis (World Bank 1994). The bulk of the experts hold unfunded public pension systems responsible for the emerging scenario and put their hope into a pre-funding and privatising of the system.

The editors start the book with a short introduction. We learn from this that "in February 2000, a group of about 100 experts on pensions in Europe … issued an Appeal to the President of the European Commission, Romano Prodi, requesting that European citizens be better informed about the long-term sustainability of their pension systems and, more broadly, as to the implications of the ageing of the European population". The Appeal, which is reproduced in an Appendix, "was subscribed to by scholars having different views as to the ideal pension system that should accompany the demographic transition … It called for more information and less ideology." The two main issues are: (1) Are the recommendations still valid? and (2) What kind of data would then be needed?

The first paper by Anderson, Tuljapurkar and Li analyses the following question: *How accurate are the demographic projections used in forecasting pension expenditures?* The basic idea is a replacing of the usual three-case scenario (low, medium and high) with a stochastic forecast where 1000 cases are compared and the corresponding confidence intervals are conveniently determined. There are different types of uncertainties here, which affect forecasts. For example, a demographic lack of certainty in turn comprises a lack of certainty in mortality, fertility, immigration and as regards population dynamics modelling. To refer to

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a concrete issue, the US total fertility rate wildly fluctuated between 1940–2000 (starting from cc. 2.4 in 1940, peaking at cc. 3.8 around 1955 and dropping to cc. 1.75 in 1975, and slightly rising to 2 since then.) The corresponding forecast oscillated similarly, following on from oft-rejected and so-called naive expectations i.e. what exists today can be forecast for tomorrow. Yet how can we be sure that we will not commit similar errors in the future? Turning to pension systems and policy analysis, the authors consider the general structuring of pension forecasts, then look at their most important characteristics, after this the economic uncertainty aspect and, finally, they give an example from the OASDI.

The second chapter is by Boeri, Brugiviani and Maignan and discusses *Early retirement: reasons and consequences*. The starting point to this is obvious: rising life expectancy and the normal retirement age are accompanied by declining *effective* retirement age. To give just one related statistic: in the 1960s, older male labour force participation rates were between 60–80%, while by the late 1990s they had dropped to 20–60%. And there are various theoretical explanations for this phenomenon, each starting from the same principle: people optimise their lifetime utility, given social security and private pension rules. Changes in the rules lead to significant drops in retirement age – yet there is no agreement concerning causes and remedies. Most economists argue that introducing actuarial fair benefit rules will automatically solve the problem. However, several economists (including the present reviewer) have showed that the very notion of actuarial fairness will be ambiguous if the individuals involved are heterogeneous in lifespan and labour disutility and when the government does not know these individual characteristics (i.e. there being asymmetrical information). In such a case, the recommended rule here overpenalises people with short lifespans and over-rewards those with long lifespans, thus implying an aggregated *loss*. There is also a disagreement over whether early retirement mitigates unemployment or not – and given the affirmative, how long the interval for improvement would be.

The third chapter, *The OECD experience with projecting age-related expenditure*, comes from Oxlay. The author makes a review of various projections concerning population and social spending forecasts. Even population forecasts show quite significant amounts of dispersion – for example, the old age dependency ratio for 2040 in terms of 1995 varies between 202.4 and 246.4 in the case of Germany; and it is not known which forecast is the better one. When we compare past forecasts, the situation is different though; we learn from *Table 3a* that the corresponding forecast from 1980 to 1995 was 101.9, while the actual figure is 95.8. Rather than displaying a multitude of figures, however, I can make one important remark here: “In the end, the reforms in some countries may not be sustainable over the longer term. In practice, many changes to pension systems have aimed at a progressive reduction in average benefits. In the absence of additional measures…, levels of income replacement among the elderly will fall and poverty could increase" (p. 71).

The fourth chapter, addressing the issue of *Population ageing and the sustainability of public finances in the EMU*, is by Buti and Costello. As is well-known, the Maastrich-treaty set strict upper limits to the annual budget deficit (3%) and the government debt (60%), both as related to the GDP. Yet if the authors are correct that the ageing factor will affect different countries in different ways, then these figures tell us too little about the long-term sustainability of public finances.

How should we measure pension liabilities in EU countries? Disney answers this question in the fifth chapter of the book. Perhaps the simplest definition of pension liability is the following: the discounted present value of pension obligations a government or firm should pay out if the existing pension system were to be closed down. There are different versions of this concept and, given its central role in pension reform debates, it is important that they are assessed in a logical and standardised way. Opponents of an unfunded public pension systems rely on such a concept, arguing that the astronomical figures involved signal a crisis of these systems in the future. (It appears almost tragic that, in Italy, it would take 2.6 years of GDP to repay all pension debt.) The underlying assumption is that workers are much more ready to pay high contributions into their own pension funds than into a government account. (Are they, however?) The supporters of an unfunded system speak out against a full or partial prefunding simply by making threats about the danger of making an implicit debt *explicit*. The author of the chapter belongs in the first group, saying that "… these accrued liabilities are exactly consistent with, and represent a similar burden for, other forms of government debt, given the 'pension promise' inherent in social insurance". The author of the review cannot help but remind the reader that the Maastrich criteria rejected this equivalence – governments can, in practice, renege on implicit debt much more easily than they can on explicit debt. (For example, concerning pensions, the Hungarian government in 1998 replaced wage indexation with a combined wage-price indexation, significantly reducing the implicit debt and without, however, causing any reactions.)

The writer of the sixth chapter, Börsch-Supan, asks the following question: *What do we know and what do we not know about the willingness to provide self-financed old-age insurance?* While the author here shares "the view that we have no choice but to base a significant part of future retirement income on self-provision …, planning out such a transition will not be an easy task" (p. 113). Börsch-

Supan goes on to discuss the implication of a partial privatisation of public pensions within either a voluntary or a mandatory framework and he correctly stresses that "we know shamefully little about these important questions" (p. 114).

The author uses Germany as an illustration. Without mentioning it, though following the logic of the latest pension reform, he assumes that the contribution rate will become frozen at the level prevailing in 2008 so that, in consequence, the rate of replacement will diminish. He assumes "… that this pension gap will be completed with prefunding, so that the sum of future-reduced PAYG pension benefits and the new funded pension will remain equal to the current PAYG pension benefits" (p. 115). Working with group rather than individual policies, "the resulting net rate of return to the customer is 4.5% in real terms" (p. 117). This policy implies maximal additional savings of 3.2% for a birth cohort from 1965, and it stabilises the total contribution rate at a location much below that implied by maintaining the old, pure PAYG system. If capital markets fare less beneficially – if, say, the real rate of return is only 3% – then additional contributions will jump by 4.7% at a maximum. The author admits, however, that these calculations are uncertain, not having good theoretical or practical grounds for making such a forecast. A major lack of certainty connects with the following: how will persons' ordinary savings react to increased pension contributions? Econometric evidence as well as international comparisons are scanty here, and Overlapping Cohorts models signal a partial crowding out.

A related question is whether workers would make savings voluntarily or should they be *compelled* to save. Economists prefer voluntary to mandatory action – yet what happens if incentives are not strong enough? "Economic theory is unclear regarding the effect of tax subsidies because the substitution effect (higher after-tax returns make savings more attractive than consumption) has an impact that is opposite that of the income effect (the subsidy increases one's total income, which increases consumption in all periods)" (p. 131).

For lack of space we can only make brief reference to the final chapters of the book, ones that deal with *Health and social welfare* (by Nazrog and Margot) and *The implication of the Europanel on ageing* (by Nicoletti and Peracchi).

In sum, this book is interesting and versatile. It displays within it the various aspects of people's ageing in the EU. It refrains from excessive idealisation of prefunding or of privatising the public system, though I, myself, do have my doubts with regard to underlying figures given with Börsch-Supan both in connection with cost efficiency pertaining to group policy and the relatively high, real yields coming with a rapidly contracting population (e.g. who would pay the high house rents that would go with a much larger population?)

I have already questioned some observations made here. I would like to add some new ones: What will happen to unemployment, still very high in the Continent, when the working population starts shrinking? In what ways will the number of years that students spend at a university alter when labour shortages reappear? Will there be changes in the liberal practice of granting an invalidity pension to relevant persons when the old-age demographic ratio is on the rise? Let us hope that a lot of things will move in the appropriate direction.

One final remark: Ten European countries are waiting to join the EU in 2004. Should an EU economist still neglect the effect that their accession will inevitably have?

András Simonovits

B. Å. Lundvall – G. Esping-Andersen – L. Soete – M. Castells – M. Telò – M. Tomlinson – R. Boyer – R. M. Lindley (ed.: M. J. Rodrigues):
The New Knowledge Economy in Europe. A Strategy for International Competitiveness and Cohesion
Cheltenham, UK, Northampton, MA, USA: Edward Elgar, 2002, 337 pp.

The Portuguese Presidency of the European Union in the year 2000 has left its mark on European strategic thinking when it comes to the issue of international competitiveness. At least since the late 1960s – the time of the electrifying success of *The American Challenge* by Jean-Jacques Servan-Schreiber – it has been a commonplace that Europe has got an increasing problem with regard to catching up with overseas competitors; while it is equally clear that the European social and political architecture is not going to readily offer itself up to an aggressive strategy of increasing competitiveness with the connected goal of enhancing labour market flexibility. In-depth reform of this architecture has proved politically impossible since this time. And Europe *still has* this catch-up problem now, i.e. in the early 21st century, as shown, for example, by e-economy data or the worsening balance of inward and outward FDI in the European Union.

A new strategy is really needed, and the Portuguese Presidency of the EU greatly contributed to the effort of laying its foundations. It seems no coincidence that a professor of Lisbon University, at the same time Chairperson of the Social Sciences Advisory Group of Social Sciences in the European Framework Programme, has edited a book on the theoretical and policy background to this strategic effort.

The underlying question is the following: what might be (if there are any) Europe's trump cards in connection with achieving a quantum leap with regard to its competitors in North America and the Far East, first of all in high-tech industries and services? If this *quantum leap* (to be measured, for example, in better R&D performance indicators of EU countries or an increase in European shares in world-wide exports of high-tech products) is ever to be accomplished, its *qualitative* implications will be important. Would this potentially mean that Europe could become a new international powerhouse in building not only the currently less popular New Economy but, rather, with its more sophisticated, more lucrative-appearing (and possibly better defined) cousin, the New Knowledge Economy?

The introductory study of the book by *Maria João Rodrigues (Introduction: For a European Strategy at the Turn of the Century)* explains why Europe has to think in new terms and act accordingly. The main questions asked are in line with the issues that were so popular in the „Future of Our Planet"-type debates on global economic strategy in the 1970s, though their focus here is distinctly European. The nature of leadership in the international economic order, the necessary pace and scope of European enlargement, the future of European governance and specialisation patterns – all of these strategic variables and choices largely depend on how the European economy can speed up structural and social change. How can a substantially higher level of competitiveness be achieved if greater social cohesion is also a must? The answer to such a question has as its basis references whose interpretation and „message" are a *Leitmotiv* in most of the book's chapters.

The magic word is: the *knowledge-based economy*. The political and philosophical background of this term is meticulously explored by *Rodrigues*, and this exploratory work is continued by the majority of the other contributors to the book. Nevertheless, a major question regarding the distinctive (or innovative?) character of this term seems to be left unanswered: is it due to just a *quantitative*, or rather a *qualitative*, difference that former economic and social systems are not known as "knowledge-based"? If the difference merely possesses a quantitative character, it can be said that this pattern of economic and social structures will be the one making the most efficient use of human knowledge possible. So the qualitative argument will now appear much more problematic. The latter would also mean that knowledge has played only a *secondary* role in the emergence of mankind as the first species really able to determine the course of global development – an argument that would be acceptable to most philosophers, past or present, only with great difficulty.

This philosophical bias is not present throughout the entire book. It seems that the authors were invited to participate on an interdisciplinary basis, so economics, management science, legal studies, social science and philosophy have all got a well deserved representation. It is therefore intellectually challenging to see how similar issues have been looked at with the use of tool-kits developed for and by such a diversity of academic disciplines.

Luc Soete explores *The Challenges and the Potential of the Knowledge-based Economy in a Globalised World*. An in-depth analysis of long-term growth patterns *à la Kuznets* shows that Europe's catching-up performance was, at best, Janus-faced *vis-à-vis* its major global competitors during the 1990s. The Asian crisis improved the EU's global economic position; the United States, however went on to increase its competitive edge over Europe via its success in making the transition to the knowledge-based economy.

We will not be dwelling again upon the meaning of this term. *Soete* is very clear in stating that differences between the roles played by the knowledge factor in consecutive economic and social systems have been principally quantitative. The qualitative reason for which the term is now being used as an identifier of a new pattern (i.e. as compared to former ones) is basically owing to the emergence of ICT as the new source of generating and disseminating knowledge – as well as its being a very important consumer of it. American investment in ICT is, in general, larger and more efficient than ICT-related investment in the EU. This is first of all due to the fact that the American private sector is much more keen on taking risks with regard to this new but rapidly ageing kind of technology than its European counterpart.

The resulting policy question is not only what the EU or European governments could do in order to close this investment gap. One should also bear in mind that the European performance picture is extremely diverse in this respect. Smaller, mainly Nordic EU economies seem to have excelled themselves in adapting to the requirements (ICT-related and other) of the knowledge-based economy. Thus, the "European policy problem" in this regard is largely an issue for the largest economies in the EU (including Germany, France and the UK). *Soete*'s last question is rather provocative: can Europe still afford to let *national* policy priorities dominate the European R&D agenda when the quality of European research could be greatly improved given a basis of economies of scale? Put more bluntly, the argument is that national R&D priorities should be swept aside if one or more of them conflict with European ones or if they simply inhibit their more rapid realisation and execution.

The starting point of *Gøsta Esping-Andersen*'s *A New European Social Model for the Twenty-first Century?* is not a question at all. He firmly believes the idea of a European-style welfare state cannot be swapped for the idol of a completely competition-based economy-cum-society model as associated with the Old Continent. Europe has to aim at a bridging of the traditional dualistic gap between "economic or social development". Furthermore, he doesn't give much credit to the simplistic model of the "Third Way", here understood as an education-based growth path leading to a fully acceptable (in a social sense) market economy order. His analysis is consequent upon one's accepting the diversity of national welfare regimes within the EU – and upon rejection of a narrowing down of the concept of society's entire welfare package to the idea of the *welfare state*. And there seems to be a striking similarity between social and R&D policy choices at this point: government policy and spending effort needs to lead the pack in both fields, although efficient usage of taxpayers' money can be expected only if private initiative also has a part in the game.

When referring to a knowledge-based economy, this might be understood as an employment model in which fast productivity growth comes first and full employment only afterwards. *Robert M. Lindley (Knowledge-based Economies: the European Employment Debate in a New Context)* uses the American example to show that productivity growth and massive job generation should not be understood as being mutually exclusive: one of the most daunting tasks for Europe is how its currently high unemployment rate could be brought down without sacrificing the productivity increase so sought after. *Lindley* lists a number of white-collar professions in which serious bottlenecks should be expected in the Swedish labour market by the year 2010. Similar analyses by and large offer the same picture for other industrialised EU economies.

The policy task emphasis seems to be shifting from government to market players here, too. A far-reaching change in the organisational fundamentals of an economy is needed if it to take the knowledge-based development path; the new organisational form is the "high-performance organisation" – i.e. as opposed to the "mass production system" – with the distinctive feature that learning, labour and innovation systems are linked much more closely within such organisations than in the case of traditional ones. *Lindley*'s vision of the social background of a knowledge-based economy also includes those persons suffering from „social exclusion". Here again, Europe is expected to be pioneer for a model of the "New Economy" in which competitiveness increases and social responsibility are able to proceed hand in hand.

Institutional Reforms for Growth, Employment and Social Cohesion: Elements of a European and National Agenda by *Robert Boyer* is, conceptually, a very rich essay on the multitude of institutional operations than Europe has to carry out if it really wants to become a well-performing part of the global knowledge-based economy. Monetary, fiscal and employment policies should, along with a major reforming of institutions and procedures, be realigned in order to become effective tools in the implementing of a new European policy agenda. This all should be, in turn, be built around what Boyer calls a "welfare-reform led virtuous circle", a new pattern of employment based upon higher activity rates and increased demand. And such a vision might become reality only if the idea of the

European knowledge-based economy as a generator of new jobs proves to be more than just wishful thinking.

Bengt-Åke Lundvall and *Mark Tomlinson* in their *International Benchmarking as a Policy-learning Tool* have produced an intellectually challenging opus that would seem to serve (at least at first glance) more as a textbook on strategic management than as a collection of studies on European policy reform. Still, their message has clear policy relevance. They insist that benchmarking is much more than a simple tool of performance comparison – and that it could have much use for public policy analysis as, for example, in assessing the performance of national innovation systems. The open question, then, is whether such a benchmark should be the American innovation system or, as the authors tend to suggest, the "new economy", whose initial pattern formations can already be seen in the more minor EU welfare economies. And we are now back at the recurrent message arising within many of the studies in this collection: Europe is, or at least can be made able to come up with its *own*-style model of the "New Economy" with a number of features distinguishing it from two things, namely, the U.S. model of the knowledge-based economy firstly and, secondly, an exclusively ICT-oriented one.

Manuel Castells' paper on *The Construction of European Identity* stands out from the book in the sense that it is a list of policy suggestions based on a much longer book by the same author. The issue is not simply how a European identity can be created: it is more than this, and the investigation points towards a European identity that is both realisable and needed with the Information Age at the door. Truly interconnected/interpenetrating educational systems, Internet-based network-building in European societies *and* European society as a whole, along with the domestic/foreign policy elements of such European identity are all on the *menu* of delicacies that the EU will be able to enjoy if Europe's future develops as it should according to this extremely positive scenario.

The closing study of the collection, by *Mario Telò (Governance and Government in the European Union: The Open Method of Co-ordination)*, brings us one step further from the starting point. This is a clear-cut, legal and policy analysis of how the "open method of co-ordination" (OMC) that the Lisbon strategy was built around can be expected to function. Earlier chapters had a more or less open essayist element with their reflections upon, and assessments of, future patterns inherent in the "knowledge-based economy" and its social, political or technological implications; while this chapter comes up with proposals that could be fully realised with the EU's current productivity, technological and employment levels.

It is probably not an over-exaggeration to say that policymakers in the candidate countries would be interested in this chapter most of all as it could tell them a number of things on what kind of a new European policy architecture can be expected to emerge. The keyword here is more social and political participation in relevant decision-making processes by *all* interested parties. And a question follows on from this: might newcomers to the EU realistically expect that they would also become such parties not just in future *years* but, instead, in the *months* that lie ahead?

Ádám Török

G. Gorzelak – É. Ehrlich – L. Faltan – M. Illner:
Central Europe in Transition: Toward EU Membership
Warsaw: Regional Studies Association, 2001, 371 pp.

An extensive and comprehensive analysis of Visegrád countries' accession processes has not yet been published – yet the book edited by Grzegorz Gorzelak, Éva Ehrlich, Lubomir Faltan, Michal Illner seems to be a good candidate for filling this gap in the literature. The experiences of transition countries and of their newly market-based economies are promising areas for deeper research.

The book is based on a research project that was conducted among Eastern and Central European countries. It attempts to take a step further by confronting reality with the initial assumptions, by providing details about accession conditions, and it also tries to make a projection of Central Europe's economic development for the year 2005, which time is near at hand. As a consequence of this, a realistic picture can be outlined; while, on the other hand significant changes cannot be expected. The book is a collection of twenty studies written by twenty-five authors – such a composition ensures a broad investigative scope. The authors attempt to focus on the similarities and differences of the four economies from four main perspectives: economic development; socio-political processes; education, science and technology; and regional dimensions. Specific characteristics of the countries are discussed in detail, and a critical approach has been taken with regard to examining how the Czech Republic, Hungary, Poland and Slovakia have been "floating" within the political and economic power structures of East and West.

One would expect that Visegrád countries have many matching characteristics arising from their historical backgrounds, their comparable levels of economic development, similar transformation processes and parallel accession negotiation processes. Moreover, these countries are linked by mutual economic relations as established under the CEFTA agreement.

In the first part of the book the authors investigate the transition and integration process accomplished by the Central and Eastern European countries up to now. This comprehensive analysis proves that easier access to the international capital markets will have a multifaceted leverage effect on the countries. EU membership will reduce uncertainties about the future development of the Visegrád countries' economies and, consequently, the *price* of the risk that enterprises from these economies have to pay on international capital markets due to such uncertainty will be reduced – and the lower costs will encourage additional investment projects. Decisions made at the beginning of the new century have great importance and might be helpful in paving the way toward EU membership. In all four countries balances of payments are showing definite improvements, and their structure has over time shown changes, too. Accelerated capital formation and external demand are recommended as being the major growth factors. As a conclusion to the economic analysis of these countries, the authors assert that the future development of FDI inflow will be – in addition to political and economic stability – dependent mainly on the qualitative development of the business environment.

Science and technology is another focal point of the book. Comparative studies of science and technology systems in the four countries have pointed to a shift from a linear to an interactive, non-linear innovation system. The authors use terms and expressions familiar from the literature of the 1980s – a science-pushed institutional framework instead of linear innovation system – which makes the language of this part somewhat diverge from the terminology used in the main science and technology analyses. The development of a strong research network leading not only to the production of new research findings, innovations and new technological procedures but also for the adoption of new technological procedures developed abroad is much needed. The diffusion of technology will lead to higher productivity levels, competitiveness and also to accelerated growth rates. A main conclusion emerging from the analysis here says that effective science and technology policies at a national level are essential for Central and East European countries for them to become globally competitive in the 21st century.

The concluding chapter of the book provides a detailed and complex assessment of regional patterns in the countries examined. The current regional government structures in all four countries seem to represent the outcome of an intermediate public administration reform with the stated purpose of increasing the effectiveness of public policy.

The book offers proposals for future research to seek to identify the strengths and weaknesses of Visegrád countries with regard to EU accession as well as opportunities and threats arising from their full exposure to the European economic, scientific and technological environment.

Readers can expect both a detailed description of the transition period within the four countries examined and a well-elaborated structure of analytical considerations in the studies of Gorzelak et al. This book should be recommended to all those who are interested in both the transition process of the Central and Eastern European countries and the requirements they need to fulfil to become members of the European Union.

Beatrix Lányi