Comment on Gilles Saint-Paul: ‘Political economy of reforms’

European Commission workshop on ‘Sequencing and incentives for reforms’
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Political economy of reform (1)

- *Constituency effect* captures persistence of the status quo as a hurdle to reform.
- *Exposure effect* captures (and simplifies) heterogeneity of those affected by reforms.
- *Identifiability effect* captures (one form of) uncertainty about reform processes.
Political economy of reform (2)

- But what about so-called *aggregate uncertainty* about the good or bad outcome of a (partial) reform?
  - Blurs distinction between winners and losers, constitutive for the exposure effect and the identifiability effect;
  - Makes recessions less easy to interpret as a cleansing mechanism, basic for the identifiability and the constituency effects.
Sequencing (1)

What is the relevant reference for the sequencing of labour market reforms?

- Here: reference is the phase of the business cycle.
- How about alternatives such as:
  - timing with respect to previous or next election;
  - other reforms in product market regulation, old age security, budgetary institutions.
Sequencing (2)

Business cycle reference does not provide a clear guide to sequencing of reforms.

The proper timing for effect is:

- **Exposure**
- **Identifiability**
- **Constituency - support**
- **Constituency - opposition**

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Conclusion

✓ The three political economy effects go some way but do not exhaust the circumstances to consider.

✓ In particular, they do not capture the uncertainty about how beneficial particular reforms of labour markets are (cf CEC report on ‘jobless growth’).

✓ The business cycle does not provide clear indication of how labour market reforms should be timed.