economists of wide-ranging political persuasions. For example, the liberal American economist, Robert Haveman, poses the issue as a choice between wage stagnation ('the US model') and double-digit unemployment ('the European model'): 'a European-style policy package comprises generous and accessible social benefit programs, high minimum wage levels, and relatively stringent labor market regulations and constraints. It is accompanied by high unemployment and joblessness, slow employment growth . . .' (Haveman, 1997, p. 3). Similarly, Horst Siebert, a conservative German economist, attributes the unemployment problem in Europe to 'an array of institutional arrangements that form a complex web of incentives and disincentives on both sides of the (labor) market.' The solution can only be to 'undertake major reforms of the institutional setup of the labor market' (Siebert, 1997, p. 53).

Several dimensions of this claim can be addressed with the available evidence: (1) because of the rigidities imposed by European welfare states, the European unemployment experience should be clearly differentiated from that of the US over a substantial period of time; (2) if downward wage rigidities are at the heart of the unemployment problem, as the orthodox view contends, we should observe a clear tradeoff between earnings inequality and unemployment (and employment) rates across countries – relatively high wages for the less skilled will price them out of jobs; (3) since most labor market institutions are designed to protect the least skilled from the most damaging effects of labor market competition, the rise in European unemployment should have been driven by the less skilled, with declining unemployment rates for the more highly skilled (for whom demand has risen); and (4) statistical tests should show convincingly that unemployment is accounted for in large part by 'employment unfriendly' labor market institutions.

This chapter assesses the evidence for this widely accepted Labor Market Rigidity explanation for persistent high unemployment in many OECD member countries. The main conclusion of the chapter is that supportive evidence has remained remarkably thin, particularly given its widespread acceptance. The simple trends suggest numerous anomalies: trends across the OECD are far from uniform; the US did not show distinctively lower unemployment until the late 1980s, and European unemployment rates have lately shown strong convergence towards US levels; the evidence for a tradeoff between unemployment and inequality is ambiguous at best; where unemployment has risen, it has done so across skill groups, not just for the least skilled; and unemployment rates across countries are not impressively accounted for in regression tests by the usual welfare state suspects (e.g., union density, employment protection laws, and the generosity of unemployment benefits) – the results in the literature are widely

acknowledged to be extremely fragile, and our simple regressions show no explanatory power.

This absence of compelling empirical support for the Unified Theory challenges the current policy orthodoxy: that high European unemployment must be addressed with a strong dose of the American model of labor market deregulation, and that any attempt to address high wage inequality in the US with labor market institutions will only produce European levels of unemployment. This review of the evidence suggests that the continued status of the Unified Theory as conventional wisdom can be explained less by the compelling nature of the evidence than by the power of the simple demand/supply vision of the labor market. This vision, in turn, has discouraged research into alternative accounts. I suggest that high earnings inequality in the US and high unemployment in many parts of Europe reflect substantial pro-market ideological shifts on both sides of the Atlantic, which have eroded institutional protections for lower skill workers in the US and constrained the growth in job opportunities in Europe.

'EUROPEAN' UNEMPLOYMENT AND THE DISTINCTIVENESS OF THE US

How similar are national levels, trends, and sources of unemployment across Europe? If there is significant heterogeneity in the unemployment experience, a handful of countries with entirely country-specific explanations for rising unemployment may have played a major role in driving up the average unemployment rate for the entire region. Further, to the extent that there are similar levels of unemployment across European economies, this may reflect more the economic integration of the continent than the similarity of labor market institutions and their effects. As Stephen Nickell points out, 'while it is sometimes convenient to lump all the countries of western Europe together in order to provide a suitable contrast to North America, most of the time it is a rather silly thing to do' (Nickell, 1997, p. 55).

Figures 7.1a and 7.1b show a wide range of unemployment rates across Europe. Indeed, there is no obvious grouping of European nations in either of these bar charts. In the 1983–88 period, Sweden, Norway, Switzerland, and Austria had rates that were much closer to those of Japan (less than 3 per cent) than such close European neighbors as Denmark, France, the Netherlands, and Belgium (9–12 per cent unemployment). The same holds true for the more recent 1989–94 period, as Figure 7.1b shows: several European nations with highly developed welfare states – Austria, West Germany, Sweden, and Norway – had unemployment rates that averaged