THE SEARCH FOR EUROPE
Contrasting Approaches

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KEES VAN KERSBERGEN
Kees van Kersbergen holds a PhD in Social and Political Sciences (European University Institute, Florence, Italy, cum laude). He is professor of Comparative Politics at Aarhus University. He has published widely in the area of welfare state studies in refereed journals and with major university presses. His latest book is *Comparative Welfare State Politics: Development, Opportunities, and Reform* (2014, with Barbara Vis).

This chapter discusses the strengths and weaknesses of European welfare states, which protect citizens in hard economic times. In many countries, governments tend to respond with austerity policies that not only undermine the protective function of the welfare state, but also weaken its economic, social and political support base. Increasing inequality is one of the observable consequences, which is associated with bad social and political outcomes in terms of health, social mobility, social and political trust, political representation and participation.

THE WELFARE STATE IN EUROPE

Introduction

Allow me to start this chapter by saying that there is no such thing as the European welfare state. Nevertheless, the welfare state is seen as something thoroughly European in origin, in character and even in terms of identity.

The welfare state is European *in origin* because its birth is commonly dated to late 19th century Germany. Around 1850, most industrializing capitalist countries already had some version of a modern poor law and had started to introduce labour protection measures (Polanyi [1944] 1957). The Prussian state, moreover, had already started to experiment with social insurance or health funds (see Hennock 2007) in the 1840s. But it was in imperial Germany that Bismarck first introduced mandatory social insurances on a grand scale (Kuhnle and Sander 2010), including sickness insurance in 1883, an industrial accident scheme in 1884 and old age and invalidity insurance in 1889. Other European countries followed, some early on (Austria) while others comparatively late (the Netherlands).

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The welfare state is European *in character*, because the wide-ranging, interconnected social policies that make up the welfare state reflect the historical European experience of social misery, turmoil, protest, political conflict and war, on the one hand, and reconciliation, cooperation, stability, order, harmony and peace, on the other. The welfare state came to embody a unique answer to the question of how to build and maintain a relatively cohesive economic, social, political and cultural order.

Bismarckian social insurances, after all, were not merely pioneered to deal with the social risks of industrial society and to improve workers' living conditions, but they were principally launched to serve the political goals of state- and nation-building and social order. The very term "welfare state" was popularized, if not invented, by the Archbishop of York, William Temple, who used it in 1941 to contrast this ideal state with the Nazi "warfare state".

In terms of identity, the welfare state has established itself as an idea and an ideal that Europeans share, a political and social accomplishment highly valued by European publics and an institution to which people attach their (national) identity. This is perhaps more true for the Scandinavian realm than for other areas, and it also holds more weight for some of the welfare state's programmes than for others. Yet, even in the United Kingdom, where the public entrenchment of the welfare state is arguably much weaker than in Scandinavia, the National Health Service (NHS) is considered to be one of the best in the world and, more importantly, an institution that makes people proud to be British. Tellingly, the NHS beat the Armed Forces, the Royal Family and the BBC in a popularity contest (Ipsos MORI 2014; Quigley 2014).

In the broader European Union context, the catchphrase "European Social Model" has come to refer to something that is uniquely European to the extent that this model is capable of promoting positive-sum solutions to what elsewhere (e.g., in the allegedly not-so-social American model) are considered to be unavoidable trade-offs between sustainable economic growth, on the one hand, and social justice and social cohesion, on the other. Because of its effectiveness, the European Commission champions the developed welfare state as an example to mimic for other countries and at the supranational European level. In the words of former President of the European Commission Barroso:

> Yes, we need to reform our economies and modernise our social protection systems. But an effective social protection system that helps those in need is not an obstacle to prosperity. It is indeed an indispensable element of it. Indeed, it is precisely those European countries with the most effective social protection systems and with the most developed social partnerships, that are among the most successful and competitive economies in the world (Barroso 2012).

The welfare state in Europe represents a huge accomplishment; thriving economies, livable and trustful societies and efficient polities are almost unthinkable without it. Yet, at the same time, the welfare state is under siege as it faces a number of demographic, economic, financial and political challenges.

I will proceed in this chapter by first shortly portraying three views that often pop up in debates on the welfare state and that are meant to challenge its very *raison d"être*. They contain important truths, but only tell part of the story. Next, I discuss what the welfare state does and argue that it is primarily about providing protection against social risks and much less about redistributing income. I then describe how welfare states in Europe differ enormously in how well they protect their populations and in how they address income inequality. Welfare states are not static, and in the last two decades or so, many have reoriented their social protection systems towards labour market activation and social investments so as to deal with the challenges of new social risks and ageing. This has been a pan-European and—in an economic and social sense—a relatively advantageous development, but one which the financial crisis and the economic recession that followed it are now seriously jeopardizing. The formidable task welfare states are facing is to find yet again new ways to continue to provide social protection while promoting sustainable economic growth (see Begg et al. 2015).

Three half-truths about the welfare state

Three beliefs often pop up when people talk about the welfare state. One view frequently heard is that it is a very expensive, inefficient human invention that we, at best, can just about afford, but that most likely is depleting our resources and is, in any case, unmaintainable in the long run. The welfare state is making us all worse off because of the prohibitively high level of contributions and taxes it requires. In other words, although the welfare state might perhaps be valued as in some way useful from some social point of view, overall it is primarily an economic burden. Indeed, the welfare state obviously requires large financial resources to function and has built-in economic disincentives, but this is only one side of it. The other part is that the welfare state—on the demand-side via consumption smoothing—greatly contributes to macroeconomic stability and—on the supply-side through investments in human capital (e.g., education and training) and social services—stimulates economic development. Recent research even finds that welfare state generosity does not create work disincentives; on the contrary, it increases employment commitment (Van der Wel and Halvorsen 2015).

The second belief recurrently voiced is that the welfare state is in crisis or is itself causing a crisis in the economy or in politics. The intriguing observation to make here is that the welfare state has almost always been considered to be in crisis or to be causing one. In 1975, the trilateral commission (Crozier et al. 1975) published a report on the worldwide overload and ungovernability crisis of democracy. This was allegedly caused, among other things, by the continuously rising expectations and demands of citizens on the welfare state. The oil crises of the 1970s were argued to have led to a fiscal and legitimacy crisis of the welfare state. Some predicted that the welfare state caused economic collapse because its redistributive policies undermined the profitability of capital and hence impeded investment. Others highlighted that the expansionary spending of the welfare state was crowding out private investment.

SOME PEOPLE CONSIDER
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More recently, predictions of crisis and collapse are coming from analyses that highlight the negative impact on the welfare state of increasing interdependence, internationalization and globalization. Social systems are believed to be in need of dismantling for reasons of international competitiveness. Governments are caught in a “race to the bottom”. On top of this, intensified European integration is argued to favour “social tourism” and “social dumping”, phenomena that are undermining national welfare states, and European solutions still lag behind. In spite of these alarming stories, however, the welfare state not only clearly survived several crises (Starke et al. 2013), but has continued to function. In fact, it has performed its functions of social protection surprisingly well given the extreme challenges it has been facing (see Van Kersbergen and Vis 2014: chapters 5 and 10).

The final idea that frequently crops up is that the welfare state is fundamentally a kind of “Robin Hood” institution that steals from the rich and gives to the poor. This perspective obviously arouses strong sentiments as some worship Robin Hood and his Merry Men as heroes of the poor, while others see him and his helpers as villains who should be detained and rendered harmless. The Robin Hood metaphor, in a sense, is invoked to underpin the two other views: the welfare state as a millstone around the neck of the economy and the welfare state in crisis and as the cause of crises. Although such ideas obviously capture parts of the reality of welfare states in Europe, they merely tell part of the story and, hence, show an incomplete truth.

Robin Hood versus the Piggy Bank

So, what is the whole story about the welfare state? What is the welfare state and what does it do? Let me focus on the Robin Hood issue. Is the welfare state really a kind of Robin Hood institution that steals from the rich and gives to the poor? The first thing to note here is that although income redistribution is an aspect of many social policy programmes that make up the welfare state, especially those tailored to fight poverty, it is not the reason why the welfare state exists. The welfare state is a collection of institutionalized policies and entitlements as social rights, which in various ways offer protection for all who might experience economic and social hardship. The welfare state is, therefore, foremost about the pooling and redistribution of social risks, particularly the risk of income loss, and not (necessarily) about income redistribution. The metaphor best depicting this essential function of the welfare state, as Barr (2001) has so imaginatively suggested, is the piggy bank: a device to help people insure against social risks and to assist people in redistributing resources over the life cycle. Importantly, welfare states differ enormously in how well their piggy banks protect citizens against social (labour market and life cycle) risks and how much their Robin Hoods redistribute income.

The second thing to stress in this context is that there is no such thing as the welfare state. Welfare states differ quite dramatically in the size of the budgets devoted to social protection and redistribution, with net social spending (2011, after taxes, tax breaks and social benefits are taken into account) ranging from a low 14.2% of Gross Domestic Product (GDP) in Estonia to a high 31.3% of GDP in France (OECD 2013). Moreover, welfare states not only contrast sharply in cash, they also diverge distinctly in kind: they are qualitatively very different in how they organize and finance their systems of social protection and how they design and how they spend their social budgets. These differences, most importantly, have huge consequences for the functioning of the labour market, for the organization of people's working and family life and for the level of social protection and income equality societies foster and people enjoy.

In many welfare states, Robin Hood plays a less prominent role than the piggy bank for the straightforward reason that the systems are simply not designed to redistribute income (even though they all do to some extent). In fact, in the conservative and southern welfare states (see below) income redistribution was a secondary goal and occurs as a side-effect if it enters social policy at all. Only in the social democratic universalist welfare states does Robin Hood redistribute large sums of money, not only to the poor, but also, most strikingly, to the middle class. What welfare states do is to offer protection against social risks (old age, unemployment, disability, etc.) and provide income maintenance. Most income redistribution is actually horizontal, that is, intrapersonal over the life course and within income groups, and much less from the rich to the poor. Only in the lean liberal welfare states is Robin Hood supposed to play the superhero of the poor because here many of the social provisions exclusively cater to the poor. However, recent research (Levell et al. 2015) shows that even in the liberal welfare states (e.g., the United Kingdom), more than half of income redistribution is of the intrapersonal kind and over the life-course: people put money in the piggy bank during their active working life and smash it when they are in need later in life.

Different kinds of welfare states in Europe

The kind and quality of social rights that the welfare state guarantees entail one dimension that has to be taken into account to understand the extent to which individuals and families can uphold a decent life in case of sickness, unemployment or old age, independent of their performance on the labour market. How strict are the eligibility rules for a benefit? How long should one have contributed to a scheme before one is entitled to a transfer or service? Does a social benefit depend on one's former income and does qualification depend on a means test? This quality of benefits and services is high if it is relatively easy to qualify for them, for example, when the required contribution period is short and when there are no means tests. Similarly, a social right is of high quality when a benefit's replacement rate is high (how much of a wage or salary is replaced by a benefit) and its duration is long.

The other dimension that one needs to look at to evaluate the quality of social protection is to what extent the welfare state alters, reproduces or even reinforces social and economic stratification. As Esping-Andersen (1990, 55) has famously argued, welfare states "are key institutions in the structuring of class and the social order", and depending on their institutional set-up, they have widely divergent effects on social structure. Welfare states "may be equally large or comprehensive, but with entirely different effects on social structure", and they come in different shapes: "One may cultivate hierarchy and status, another dualisms, and a third universalism. Each case will produce its own unique fabric of social solidarity" (58). Esping-Andersen distinguished three types of welfare states: liberal, social democratic and conservative.

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The liberal welfare state is market-oriented, and public provisions for income maintenance and relief mainly cater to the poor. Most people in countries such as Australia, the United States and the United Kingdom (with the notable exception of health care) are able to find social protection in the private market. Low and flat rate tax-financed benefits characterize the system, and access to benefits is restrictive because benefits are means-tested. Private social insurance is encouraged via tax exemptions and allowances, which favour the middle class and the rich. The liberal welfare state is also service-lean, and transfers are modest to mean. The inequalities generated in the private market are not countered in this system, and those who can afford it are well-protected, whereas others come to depend on means tested assistance. This model came under political pressure early on (Reagan, Thatcher), and austerity politics became the dominant response to many of the challenges the welfare state faces.

The social democratic welfare state grounds social rights in citizenship or residence and, hence, to a substantial extent, does away with status differentials. This model, as found in the Nordic countries, is generally also tax-financed, but access to social provisions is much more open, and benefits and services are more generous than in the liberal model. The model provides social services for all without strict qualifying conditions. The role of the market in service and benefit provision is played down. Several of the Nordic countries went through performance crises in the 1990s, but managed to recover from this by essentially maintaining their path of development, stressing maximum labour force participation, flexible but protected labour markets and social investment.

WELFARE STATE MODELS DIFFER SUBSTANTIALLY IN HOW MUCH THEY ARE COMMITTED TO SPEND

The conservative or corporatist welfare state model features Bismarckian social insurance programmes that are differentiated and segmented along occupational and status distinctions. In addition, in countries such as Germany and Austria, state employees (civil servants) receive privileged treatment in social insurance, particularly pensions. In this model, people, particularly men, qualify for a provision or benefit to the extent that they have contributed to a social scheme. Employment record is decisive for acquiring social rights. Employees pay contributions to social insurance funds and receive benefits that are earnings-related and depend on contribution period. This model is typically social service-lean and transfer-heavy.

These features of the conservative system imply that the existing stratification system and income inequality are largely left untouched and, in fact, tend to magnify rather than moderate existing differences in status and income. The employed, especially those working for the state, are well-protected insiders, whereas those without a strong attachment to the labour market are outsiders whose social protection depends on their family. The model came under strain in the 1980s and 1990s because many of its qualities (early exit schemes, passivity of benefits, dualism in protection, gender bias) precluded the necessary growth of labour market participation, especially of women.

Some argue that there is a specifically southern or Mediterranean fourth model found in Italy, Spain, Portugal and Greece. The model shares many features of the conservative one, but is characterized by much more fragmented and particularistic social insurances, a rather one-sided stress on pensions (although less so in Spain), a very pronounced insider-outsider and gendered structure of the labour market, an even more pronounced role of the (extended) family in the state-market-family mix of social protection, an under-developed social assistance system and clientelism in the allocation of benefits and jobs in the public sector. This model came under pressure because of problems of low (formal) labour force participation, wide social protection gaps, a weak state and, hence, suboptimal tax capacity (the quintessential example would be Greece, see Petmesidou and Guillén 2015).

These welfare state models, in short, differ substantially in how much they are committed to spend, but what matters most for social outcomes, such as social protection and inequality, is on what specific social purposes that money is spent, how the programmes are organized, taxed and financed and how transfer- or service-oriented they are.

The generosity of welfare states

One way of gauging the relative quality of what the welfare state does and how well it does this is by looking at the welfare state's generosity. Generosity depends on the replacement rates of key social benefits, the duration of such benefits, the kinds of demands people have to meet in order to qualify for a benefit, the number of waiting days included in the rules and how many people are covered by the social scheme. Generosity captures the extent to which social services and benefits have been institutionalized as social rights that allow people to "maintain a livelihood without reliance on the market" (Esping-Andersen 1990, 22).

In chart 1, countries are ranked (high to low) according to their generosity index in 1980. The higher the score on this index, the more generous the systems are. As can be seen from the table, in 1980, the Swedish social democratic welfare state was the most generous and the Australian liberal welfare state was the most tight-fisted. One can also quite easily recognize Esping-Andersen's classification of welfare states. In 1980, the most generous welfare states were the social democratic countries (except Finland), closely followed by the conservative countries. Most liberal welfare states (Canada, New Zealand, the United States and Australia) are found at the bottom of chart 1. In 1980, Italy's welfare state looked more like a liberal than a conservative European welfare model, whereas the liberal United Kingdom was closer to Austria and Germany than to any of the liberal welfare states.

Chart 1 also shows that in terms of generosity, the neat picture of the three worlds of welfare states has become somewhat blurred in 2010. The liberal welfare states have remained quite clearly distinctive in the relatively humble levels of bigheartedness of their welfare states. Interestingly, the United Kingdom seems to have become much more of a liberal welfare state than it used to be, dropping from place 9 in 1980 to 12 in 2010. Some of the social democratic states have become much less generous too. Sweden, the world's generosity champion in 1980, fell 5 places and ended at rank 6 in 2010, while Denmark descended from

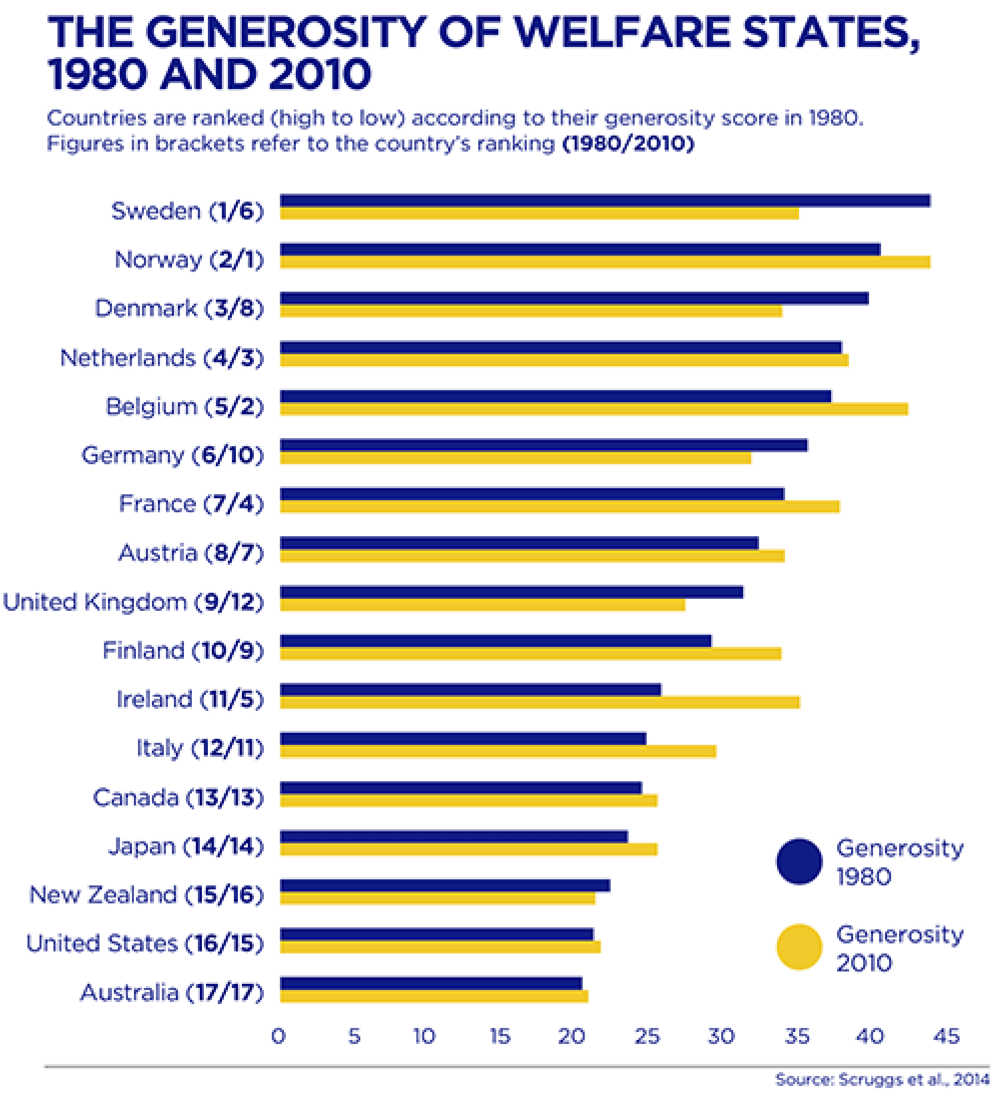

Chart 1

place 3 to 8. Three continental European countries (Belgium, the Netherlands and France) have surpassed the social democratic welfare states (except Norway) in generosity in 2010. The biggest change is found in Ireland, where the welfare state generosity index jumps from 25.8 to 35.3, locating this country at place 5, also above Sweden and Denmark. Even though the precise ranking of welfare states and the composition of the models have changed, it is obvious that there are still clear differences in the quality of welfare states as measured by the generosity index.

The welfare state and income redistribution

The generosity index cannot inform us precisely about the redistributive features of the welfare states, but it seems reasonable to suspect that the more generous systems are also more egalitarian. And, indeed, there is a reasonably strong negative correlation between how generous welfare states are and how much inequality they produce (Jensen and Van Kersbergen 2016). The OECD (2014) has published interesting data on how welfare states redistribute and which income groups profit relatively most from social benefits. It turns out that welfare states differ enormously in which income groups they most privilege. The southern European welfare states transfer a much higher proportion of social benefits to the highest income group than to the lowest one. Portugal leads this group of southern European countries, where the lowest income group receives clearly less than what the top receives: 11% of all cash benefits goes to the bottom 20% earners, whereas 40% goes to the top 20%. Portugal also has one of the highest levels of inequality.

There are two important causes for this phenomenon. First, most transfers in these countries are simply not meant to help the poor exclusively, but rather are to cover the social risks of all social strata. Second, benefits for the retired, disabled and unemployed are often linked to contribution period and are earnings-related, so that relatively more goes to the well-off than to the poor. This is especially true for pensions, and the southern—and some of the continental European—countries are typically pension states: Italy, Greece and Portugal, but also France, roughly spend between 13% and 16% of GDP to pensions, two to three times as much as the social democratic, liberal and some of the conservative welfare states (Switzerland and the Netherlands), which typically spend between 3.6% and 7.4% of GDP on pensions. This means that income redistribution in the pension-heavy welfare states is not from the rich to the poor, but primarily from one period in life to another. In other words, inequalities produced during working life are directly reproduced, rather than moderated, in retirement.

This redistributive pattern contrasts sharply with the liberal and social democratic welfare states, in which the bottom group receives relatively more than the top. Australia, for instance, clearly targets the poor as over 42% of total benefits goes to the bottom and only 3.8% goes to the top. However, given that Australia's level of inequality is close to that of Portugal, it is also clear that there is no one-on-one relationship between the allocation of public benefits to different income groups and inequality. The main reason is that the relatively high level of transfers to the bottom income group can be an effect of two different things: either a high level of overall spending, as in the Nordic countries, or targeting through means testing (i.e., offering usually minimum benefits exclusively to those who have no other means), as is the case in the Anglo-Saxon countries.

Another thing to take into account is that much of the effect of the welfare state on inequality depends on how social benefits and services are financed and allocated. The universalist and comprehensive tax-financed systems that are characteristic of the social democratic model turn out to be much more redistributive than the targeted systems, even if there is no progressivity in taxation (see Rothstein 1998). In a way, this is counterintuitive because these welfare states are very generous to the middle class and do not target the poor. In fact, higher income groups disproportionally profit from social services, especially health care and education. Hence, one would expect a fully means-tested system, in which a disproportional proportion of benefits goes to the poor, to be much more redistributive. However, means-tested systems tend to be tight-fisted, whereas social democratic universalist systems distribute much larger sums of money, and as a result, the latter come out as much more redistributive than the more targeted and means-tested ones, a phenomenon called the paradox of redistribution (Korpi and Palme 1998).

The redistributive effect of the welfare state can be directly measured by the percentage difference through transfers and taxes between inequality in market income and inequality of disposable income. Income redistribution is the outcome of public spending on cash benefits, how much the tax-benefit system targets the poor and the progressivity of the tax system. Adema et al. (2014) have shown that all welfare states redistribute and lower inequality, at least to some extent, but that the cross-national differences in the welfare states' redistributive effects are large, varying from a decline in inequality of 20% to 30% in the liberal welfare states to 45% to 47% in Ireland, Slovenia, Finland, Bel-

THE EFFECT OF THE WELFARE STATE ON INEQUALITY DEPENDS ON HOW SOCIAL BENEFITS AND SERVICES ARE FINANCED AND ALLOCATED

gium and Hungary. Interestingly enough, the countries with the lowest income inequality, namely the social democratic welfare states of Sweden, Norway, Finland and Denmark, are not among the countries with the top redistributive tax-benefit systems. This, first of all, reflects the fact that these countries have relatively equal market income distributions in the first place. In addition, the picture is somewhat distorted because the redistributive impact of the Nordic countries' extensive social services financed via taxation are not taken into account (Adema et al. 2014, 19).

Welfare state adaptation and social investment

Welfare states and welfare state models are not static institutions; on the contrary, they are continuously updated and adapted to constantly changing social, economic and political circumstances, including shocks, such as the financial crisis and the economic recession that followed in its wake. As documented in more detail elsewhere (Van Kersbergen and Hemerijck 2012; see extensively Hemerijck 2013), all welfare state models have undergone significant changes in the main areas relevant to social policies.

In macroeconomic policy, countries have converged around a policy framework centred on economic stability, hard currencies, low inflation, sound budgets and debt reduction. The introduction of Economic and Monetary Union turned monetary policy into a fixed parameter for policy reform in other fields. Most countries have also responded to internationalization with wage restraint, usually backed by broad social pacts between employers, unions and the government. Everywhere, there has been a reorientation of labour market policy towards activation with a view to maximize labour market participation. All welfare states have increased work incentives, although not all have managed to the same extent to accompany this stick with the carrot of human capital investment.

Another general trend has been labour market deregulation, particularly decreasing job protection, in order to make labour markets more flexible and to create opportunities for labour market outsiders. There are, however, large differences between countries in that only some (e.g., Denmark and the Netherlands) complemented the flexibilization of labour markets with measures that extend social protection to vulnerable groups, establishing systems of “flexicurity”. More generally, the trend in social insurance has been to focus more on labour market (re-)integration than on income maintenance. Retrenchment of unemployment protection has been part of the flexibility venture almost everywhere, although minimum income schemes have been introduced or improved in a number of countries where these were lacking.

WELFARE STATES ARE CONTINUOUSLY UPDATED AND ADAPTED TO CONSTANTLY CHANGING CIRCUMSTANCES, INCLUDING THE FINANCIAL CRISIS AND THE ECONOMIC RECESSION

Everywhere, reforms have been introduced to make pension systems sustainable under conditions of low or declining fertility and increasing life expectancy (see European Commission 2015). Measures include increasing the retirement age, limiting early exit, introducing occupational and private pillars on top of the public schemes and redefining the actuarial links between contributions and benefits. Many countries have also increased their efforts to assist people in their attempts to reconcile work and family, for example, by extending child care and preschool facilities and other services as well as parental leave provisions.

In Europe, policy reforms in welfare states of various kinds have often taken inspiration from the idea of social investment. The basic conviction is that social policies should not just passively compensate for social mishap, but should more proactively be used to prevent labour market inactivity, to adopt a life course perspective (e.g., lifelong learning) and to promote human capital so as to stimulate both equality and economic growth. Increasing the capacity of individuals over the life course to remain in employment not only provides a high level of social security, but also greatly enhances the long-term financial sustainability of the welfare state. It is in this sense that the term "investment" must be taken quite literally: an investment in human capital will yield great returns in terms of money saved on passive benefits and money earned from taxes and contributions. Investments in children are particularly promising, because they help smooth inequalities in (cognitive) abilities and health and prevent an accumulation of disadvantages over the life course, which would otherwise increase demands on passive welfare (Kvist 2015). The social investment strategy hence aims at developing policies that "help to simultaneously widen the tax-base, increase fertility, fight poverty and inequality, or improve the financial sustainability of certain key programmes such as pension schemes" (Morel et al. 2009, 10). The European Commission has promoted social investment as the key policy framework to guide member states in their social policy reforms (European Commission 2013) and to reach the goals of the Europe 2020 strategy for smart, sustainable and inclusive growth.

The impact of crisis and recession

Before the financial crisis hit, social investment was rapidly becoming the foundation of a new policy paradigm in most if not all welfare states as well as at the European Union level. One ingredient of the social investment strategy, namely employment and activation policies, was adopted everywhere and has helped to increase labour force participation, especially among women and older men. The economic recession, however, has greatly amplified the financial pressure on the welfare state, both by multiplying the number of people on benefits and by decreasing the financial contributions for social policy. Virtually everywhere this has led governments to increase their austerity policy efforts and to retrench on social entitlements so as to help rebalance the public budget. Even though in discourse the social investment agenda still seems intact, particularly at the European level, it has also become increasingly clear that social investment policies are particularly vulnerable to cuts in the short run, precisely because social investments yield returns only in the longer run, while cost containment is a necessity now.

Let me take as an example the social democratic welfare states, in which the social investment path has been followed far longer than anywhere else and where it has become an intrinsic component of the welfare state paradigm. If one, for example, compares public expenditures, one finds that the social democratic welfare states spend 3-4% of GDP more than the conservative, liberal and southern European welfare states on key social investment programmes (education, family benefits and active labour market programmes). The effects are evident in the use of public services, where the social democratic welfare states stand out in the large number of children they enrol in pre-education and children and adults in education (schools, training institutions, etc.). The public provision of childcare, education, work-life reconciliation initiatives and active employment policies not only provide people with the skills to work, but they also free up time to participate in the labour market and generate jobs. As a result, labour market participation rates of men and women are highest in the social democratic welfare states. Finally, as is well known, income inequality and poverty rates are lowest in the social democratic countries.

Recent trends, however, seem to indicate a change of direction even in the social democratic social investment approach, namely a move away from universalism and inclusive social investment, with rising selectivity in social policy as an effect of tighter eligibility criteria, more targeting and privatization. Similarly, focusing on outcomes, there are signs of rising inequality and poverty as an effect of direct retrenchment and policy drift, that is, not updating social policies to new needs (see Van Kersbergen and Kraft 2016). The point to stress here is that if the social democratic welfare states are finding it already increasingly difficult to uphold their allegiance to the social investment oriented welfare state, then it is highly likely that other types of welfare states will find it close to impossible to remain committed to the social investment path they had started to follow before the financial crisis.

The financial meltdown of 2008 and the subsequent recession caused all welfare states to experience similar problems, including rising unemployment, reduced credibility of the banking sector, falling exports and rising budget deficits. Because of the problem similarity, governments initially responded in roughly similar ways. The immediate response was to massively support the financial sector and to protect demand by continuing existing social policies and introducing temporary measures to stimulate demand. But bailing out banks, recapitalizing them and a host of other measures to save the financial sector added up to a very high bill. And on top of that came rising social expenditures and decreasing taxes and contributions, which put public budgets under extreme financial pressure.

Interestingly enough, the financial crisis of 2008 and the Great Recession that followed in its wake, for obvious reasons, were not blamed on the welfare state, at least not initially. In fact, the welfare state was celebrated for how it cushioned the harmful effects of the crisis as its automatic stabilizers did exactly what they were meant to do: automatically stabilize demand and protect people from hardship. But then something happened, which Mark Blyth (2013) has labelled "the greatest bait and switch in modern history": although the fiscal crisis in European welfare states (except Greece) was a consequence of the

THE RECESSION CAUSED ALL WELFARE STATES TO EXPERIENCE RISING UNEMPLOYMENT, REDUCED CREDIBILITY OF THE BANKING SECTOR, FALLING EXPORTS AND RISING BUDGET DEFICITS

financial crisis, it became progressively portrayed as its cause. Because states took responsibility for the massive private debt that banks had caused by socializing it as public debt, the banking crisis was turned into a sovereign debt crisis, as if it had been the welfare states, rather than the banks, which had caused the predicament. Thus, the problem became reformulated as one of excessive (welfare) state spending and public debt, which had to be battled by a severe politics of austerity in order to solve the financial crisis and stimulate the economy.

As a result, the political conviction everywhere became that the costly initial response to the crisis and the recession was not sustainable in the long run because it was causing deficit spending to rise dramatically. This ushered in a period of austerity with a view to restore balanced budgets and contain public debt. Governments realized, or in some cases were reminded by the financial markets, that deficit spending had reached its limits. Consequently, the politics of reform increasingly came to revolve around the question of who was to pay for what, when and how. In other words, the outcome of these political struggles determines who will carry the heavy burden of financial and economic recovery. The crucial political choice virtually everywhere seems to be founded on the conviction that a swift return to a balanced budget is the only sensible route to economic recovery and that drastic retrenchment is the only means to achieve that goal. Governments have already agreed on significant public spending cuts, which add up to drastic reforms that particularly hurt social investment policies and induce new distributional conflicts, although more so in some countries than in others.

Conclusion

Let me highlight two issues by way of a conclusion. On the one hand, there has not been a major onslaught against the welfare state in the immediate wake of the financial crisis. On the other hand, there have been increasingly drastic spending cuts that seem to undermine the social investment path that welfare states had chosen to follow. During the last twenty 20 years or so, welfare states have been continually adjusting to new economic and social demands, and governments have pursued, albeit with considerable variation, apparently well-adapted and innovative social policies, such as social investment. But under increasing stress, especially in the wake of large budget deficits and pressures from financial markets, it is not evident that core social programs can be protected through reform; they may become victims of the pending distributional battles or of further policy drift.

Welfare states have been remarkably flexible and capable in their adjustment to their permanently changing environments. Their core social arrangements remain highly popular so that any attempt at a radical overhaul continues to meet public resistance. Yet, severe budgetary problems, the unpredictable but threatening responses of financial markets and the real economic consequences of the financial crisis not only pressure for further reform, but possibly undermine the political capacity to implement those reforms needed to guarantee the continued protection of people against social risks that the welfare state has so far offered.

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