Welfare States and Welfare State Theory

Jørgen Goul Andersen

Centre for Comparative Welfare Studies (CCWS)
Department of Political Science
Aalborg University
www.ccws.dk

Centre for Comparative Welfare Studies
Working Paper
Editor: Per H. Jensen
E-mail: perh@epa.aau.dk

www.ccws.dk

Working papers may be ordered from:
Inge Merete Ejsing-Duun
Fibigerstræde 1
9220 Aalborg Ø

E-mail: ime@epa.aau.dk

Tlf: (+45) 99 40 82 18
Fax: (+45) 98 15 53 46

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Content

1. The welfare state in a modern society

The welfare state is an essential institution in any modern society. In Western Europe, the first basic pillars of social protection emerged around 1900, but the modern *welfare state* – a term coined in the early 1940s – developed from the 1950s to the 1970s. Social protection was extended to a broader range of social risks and services, coverage was widened to most of the population, and compensation levels came to reach well above subsistence level. As a consequence, tax extraction reached between one third and one half of the economy (GDP), occasionally more. Since the 1980s welfare states have continued to expand, but typically without raising the rate of taxation.

Welfare states have also developed in recently industrialized countries and in former communist countries, following the transition to market economy. Among significant "newcomers" China started developing a modern welfare state in the 1990s. Taking a broad view, the welfare state seems intrinsically linked to market economy and industrialism, as claimed by functionalist writers more than 50 years ago (Wilensky & Lebaux, 1958). However, different welfare models or "welfare regimes" can be traced back to the formative period. Since the 1980s or 1990s, most welfare states have undergone significant restructuring, recalibration or even transformation, but this has not eliminated "regime" differences.

Defining the welfare state

What is, exactly, a welfare state? Actually, the concept is not very often defined, but a long definition provided by historian Asa Briggs would seem to grasp the essence quite adequately, even if it might contain a British/Scandinavian bias and appear a bit ambitious:

> "A welfare state is a state in which organized power is deliberately used (through politics and administration) in an effort to modify the play of the market forces in at least three directions
> - first, by guaranteeing individuals and families a *minimum income irrespective of the market value* of their work or their property;
> - second, by *narrowing the extent of insecurity* by enabling individuals and families to meet certain "social contingencies" (for example, sickness, old age and unemployment) which lead otherwise to individual and family crisis; and
> - third, by ensuring that all citizens without distinction of status or class are offered the *best standards available* in relation to a certain agreed range of *social services*." (Briggs, 1961)

In short, the welfare state modifies the impact of the market, by providing some sort of minimum guarantee (mitigating poverty); covering a range of social risks (security), and providing certain services (health care, child and elder care, etc.) – at the best standards available. Welfare states differ as regards the level of ambition and the mix between these aspects: Coverage may include a broad or a narrow range of risks and services, and minima may alleviate poverty or aim at providing equality (see welfare regimes below). Briggs' definition is related to the tradition of thinking social policy in terms of citizenship (as the founding fathers – especially TH Marshall and Richard Titmuss at the LSE, and later scholars like Walter Korpi and Gøsta Esping-Andersen).

The welfare state as a response to modernization & conflict

There are several types of explanations of welfare state development. As hinted at above, "structural" explanations link the welfare state to market economy, industrialization and modernization (Wilensky, 1974). The welfare state alleviates the inequality and insecurity of modern capitalist, industrial society. Fulfilling these needs, the welfare state also serves to maintain social cohesion. In addition to such functionalist thinking (explaining why the welfare state is "necessary" for society), a conflict approach would emphasize (class) interests. The welfare state is linked to the emergence of an industrial working class, its organization in trade unions and Social Democratic parties, and to class and party alliances with old or new middle class groups. In this *power resource* perspective, the welfare state (and different welfare *regimes*) is a product of interest conflicts, more specifically, of class struggle and class alliances (Korpi, 1974, 1980, 1983; Esping-Andersen, 1990).

In addition to such structural explanations, other scholars (following the pioneering work of Heclo, 1974; see also Beland & Cox, 2011) have underlined the role of ideas (often transferred from one country to another), and of institutions. As regards institutions, it is argued that welfare states crystallize in different regimes – "frozen landscapes" that resist change (Pierson, 1994), or at least develop in regime-specific ways when exposed to exogenous pressure (Swank, 2001; Kautto & Kvist, 2002).

Among the structural explanations of welfare *reform* we find changing family structures, ageing populations, globalisation, migration, etc. But again, ideational and institutional theories are highly important in explaining change.

The key issue of modern politics

As one quarter to one third of GDP is allocated to collective welfare schemes (narrowly defined), it is the core policy issue in modern societies. In broad terms, welfare policy would even include education, making its significance even larger. Moreover, some of the most basic issues in the economic field (economic policy, tax policy etc.) concerns trade-offs between private and collective consumption, and between equality and efficiency.

By the same token, the welfare state is of key importance to the living conditions of any individual. Services are provided from the cradle to the grave – from child care to elderly care; as a giant insurance system, the welfare state protects against social risks throughout the life course; and it provides redistribution of income and life chances. This is particularly outspoken in the welfare states of Scandinavia and Western Europe.

2. Welfare regimes - different principles of solidarity

A crucial point of modern welfare state theory is that welfare states not only differ regarding public expenditure levels, but even more in institutional terms: What are the underlying principles of solidarity behind the rules of eligibility (who should receive support) and entitlements (how much)? Gøsta Esping-Andersen (1990) coined the names of three ideal-typical welfare (state) regimes: The Liberal, Social Democratic and Conservative regimes (Figure 1).

Esping-Andersen's ideal types builds on Richard Titmuss' (1974: 30-32) distinctions between three different principles of welfare: the residual model, the institutional model and the industrial achievement-performance model. However, Esping-Andersen named them according to the political forces behind them. As we do not find the association between regimes and political parties that straightforward we prefer the labels: *Residual*, *universal* and *corporatist* welfare model. At least these terms refer to the dependent variable and not to the (presumed) independent variable. It should be mentioned, however, that there are many names, in particular for the corporatist/ conservative/ industrial performance-achievement model.

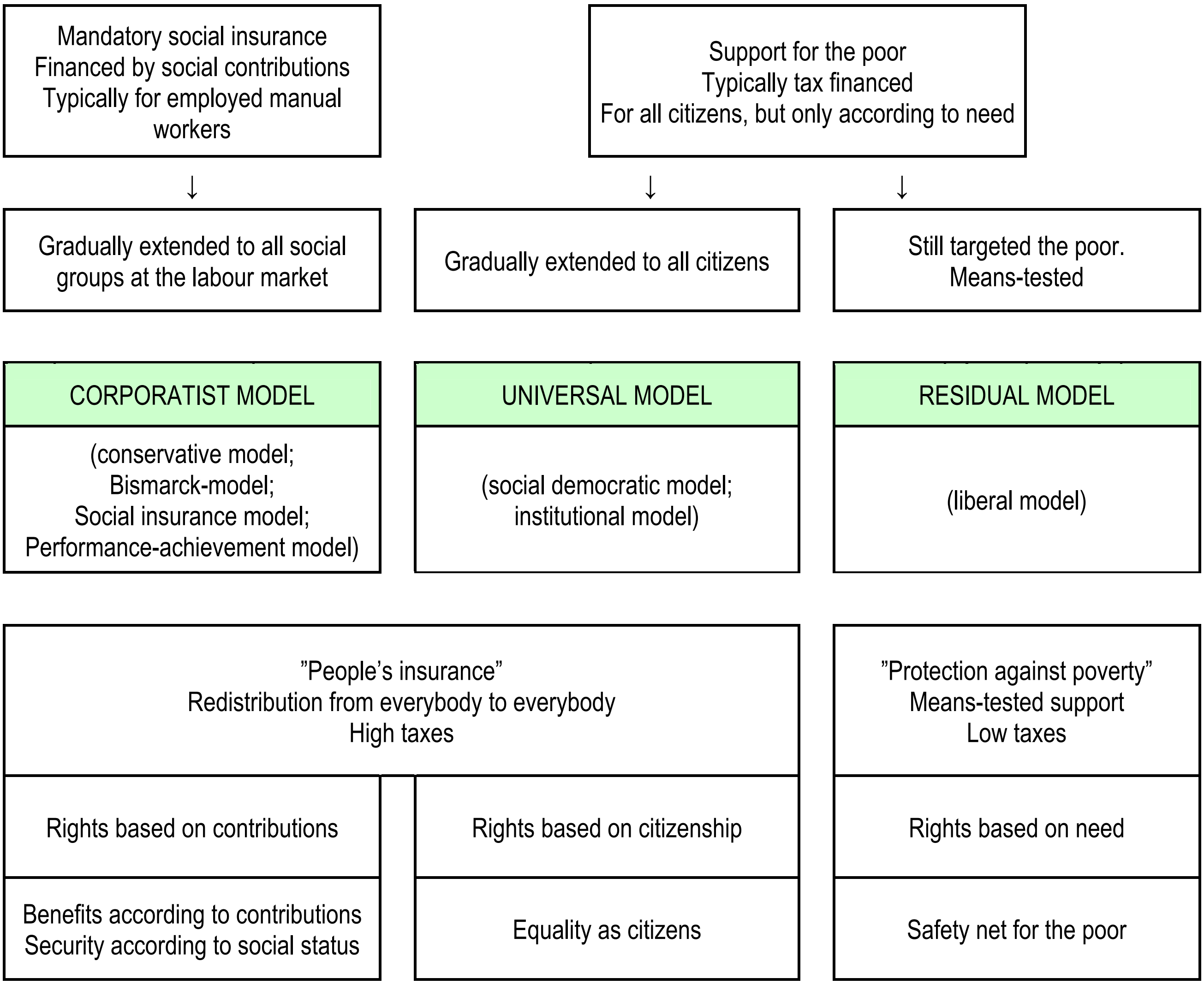
The corporatist model is also referred to as the social insurance model, as the Christian Democratic welfare model (van Kersbergen, 1995), or the Bismarckian welfare state (Palier, 2010). The German chancellor Otto von Bismarck was the first to introduce mandatory social insurance in the 1880s. These insurances were mainly financed by social contributions paid jointly by workers and their employers. The label "corporatist" denotes that insurances are typically administered jointly by representatives of the employers, the workers and the state. "Performance-achievement" refers to the principle that rights depend on contributions – most significantly in the field of pensions. In other words, there is reciprocity between contributions and entitlements. The label "Conservative" is consistent with the fact that these systems were not aimed at equality, but at security (in accordance with people's position in the social hierarchy). Risk sharing across classes was intended to be small. Initially, corporatist schemes typically covered only particular categories of workers, but after World War II, coverage was gradually extended to (nearly) the entire working population.

Universal welfare states started as residual ones. Usually, the source of financing was taxes rather than contributions. The Danish old age support of 1891 was deliberately designed to be different from the first old age and disability insurance introduced by Bismarck two years earlier. The Danish scheme was targeted at old people[1] who could not provide for themselves. The criteria and size of benefits were left to the discretion of local authorities until 1922 when "old age support" was renamed "old age allowance", and eligibility and entitlements were fixed in the law. From the very origin, however, the Danish welfare state included all citizens, regardless of employment record and gender. Most German insurances only covered manual workers – but the pension scheme covered nearly all employees. When New Zealand followed as the third country in 1898, it emulated the Danish old age support scheme, but entitlements were more clearly specified in the law. Like Denmark, New Zealand was less industrialised and strongly reliant on agriculture.

Like in corporatist welfare states – and even more – coverage in what became universal welfare states was gradually extended to the entire population. Targeting the poor was economically necessary from the outset, but the division between a universal and residual model took place decades later and was a matter of political choice.

[1] The age limit in Denmark was 60 years; in Germany it was initially 70, but the scheme included disability pension.

Figure 1. Three welfare models: Corporatist, Universal and Residual.



Both corporatist and universal welfare states are encompassing social insurance systems that take care of social risk and services for most of the population throughout the life course. Residual welfare states are based on the conviction that people should handle most of their welfare needs themselves; the role of the state should mainly be confined to providing a safety net for the poor.

This completes the division into three welfare regimes. These are *ideal types*, that is, “pure” types or theoretical constructs. They illustrate the basic ideas and the mechanisms (the *modus operandi*) of different welfare principles. Next, they serve as measuring points for description of actual welfare systems where principles are mixed. The Nordic countries, however, largely follow the universal model; Continental European welfare states adhere to the corporatist model; and Anglo Saxon welfare states to the residual one. A “Southern European” model is sometimes presented as a regime of its own (Ferrera, 1996), sometimes as a sub-species of corporatism.

As regards the administration of the corporatist model, there is a huge variation. Administration can be divided by purpose (unemployment, pension, sickness, old age care etc), by social category, or both. The lion's part of social expenditure is financed by contributions from employers and employees (typically fifty-fifty). As contributions are mandatory by law, these contributions are counted by OECD and others as taxes – *de facto* contributions are ear-marked, proportional income taxes, sometimes with a maximum corresponding with the maximum benefit obtainable.

Universal welfare states impose income taxes rather than social contributions, but sometimes supplemented by payroll taxes on employers. Taken together, taxes on labour power (income taxes, payroll taxes and social contributions), calculated as proportion of gross wage expenditures, tend to be lower in universal welfare states than in the corporatist ones (OECD, 2012a); hence, universal welfare states are often pictured as more "employment friendly" (e.g. Scharpf, 2000). In return, indirect taxes (e.g. VAT, fees, etc.) are higher in universal welfare states (OECD, 2011a), even though border trade set limits. Income taxes are typically low in liberal welfare states; in return, they collect the highest property taxes (OECD, 2011a).

Eligibility, entitlements and redistribution

As indicated, criteria of social rights are highly different. In corporatist welfare states, the basic criterion of eligibility is contributions paid during employment. Entitlements depend on contributions – this is the achievement-performance principle. This is sometimes referred to as the "Matthew principle" ("For unto every one that hath shall be given, and he shall have abundance: but from him that hath not shall be taken away even that which he hath"). This is fair, however, from the principle of *reciprocity*: Contributions are paid in order to get insurance, and the insurance obtained depends on the contributions that are paid.

The basic principle of the residual welfare state could look like the "Robin Hood principle": Take from the rich and give to the poor. The basic (ideological) principle is that people should manage on their own. If and only if this is impossible, they are entitled to public support. *Need* constitutes the basic criterion of eligibility and entitlements: Support is *targeted* at the poor.[2]

In universal systems the basic criterion is citizenship (which in practice normally means residence). All citizens for whom the support is relevant are entitled to receive support. Needless to say, labour market participation is a condition of unemployment benefits; disease (as assessed by a professional) is a condition of health care. Even *need* is inevitably a criterion of certain benefits like housing benefit (housing policy may also include various forms of general support for a particular sector or for particular types of dwellings, but this is not a matter of individual rights).

Universalism is equality-oriented, but not necessarily aimed at maximum equality; rather the goal is equal citizenship – enabling everybody to participate in social, political and cultural life as equal citizens (despite modest economic inequality). This was the ideal put forward by TH Marshall (1949) in his seminal essay "Citizenship and Social Class".

[2] There are important variations of targeting. There is a difference between excluding the rich and targeting the poor. Targeting the poor often involves stigmatization. This is not the case with excluding the rich. Previously, this was sometimes used to picture Australia and New Zealand as a type of their own (Castles & Mitchell, 1991).

Crowding in or crowding out private welfare

If social security is not provided by the public sector, people have to take up private insurances or buy private services wherever possible. In other words, there will be a *crowding in* of private markets in insurances and services.[3] If public arrangements are sufficiently generous, also for the upper middle classes, this will tend to *crowd out* private solutions.

Table 1. Net social expenditures. Public and Public + Private. 2005. Per cent of GDP.

	Gross Public Expenditure	Net Public Expenditure	Net social expenditure, public + private	Rank Net social expenditure
Sweden	34.6	27.3	29.3	5
France	33.8	30.4	33.6	1
Denmark	31.9	24.1	25.7	10
Austria	30.6	24.9	26.5	8
Germany	29.9	28.1	30.2	3
Belgium	29.9	26.2	30.3	2
Finland	29.8	23.5	24.4	11
Italy	28.8	24.8	26.6	7
UK	24.3	22.9	29.5	4
Norway	24.1	19.9	21.2	12
The Netherlands	23.6	19.3	25.8	9
USA	17.1	18.4	27.2	6
OECD-26	23.6	20.8	23.3	

Source: Adema & Ladaique (2009: 48). Per cent of GDP at factor costs. Calculations based on GDP at conventional market prices are slightly problematic methodologically, but provide similar results – with Germany, USA and Austria moving one rank up; Belgium, Sweden and Italy one rank down (pp.83-84).

OECD has calculated the net cost of welfare across countries, correcting for different tax rules and including private welfare insurances and services (table 1). Net *public* expenditures corrected for taxation reveals that social expenditures are at least as high in continental European welfare states as in Scandinavia. This is a stable finding: The universal welfare state is *not* particularly expensive.

Next, in accordance with functionalist theories emphasizing the association between modernisation and welfare, we find much less variation in *total* expenditures for welfare including private costs. Liberal welfare states crowd in private solutions, but the total sum of welfare expenditures in the US by 2005 was higher than in Denmark, Finland and Norway. If welfare is not publicly provided, it is provided by the market, but with a different social distribution.

Welfare regime and redistribution

In the general public, one may find the perception that targeting benefits as in the residual welfare model is the most redistributive. However, any empirical evidence proves the opposite. Maximum redistribution is obtained in the universal welfare model, followed by the corporatist whereas the residual model is the least redistributive. A Southern European model tends to redistribute as little as the liberal model, due to insider/outsider divisions and inadequate social assistance.

[3] This should not be conflated with *outsourcing* of welfare to private producers. This is an important trend, but if public *financing* is maintained, outsourcing does not count as an alteration of welfare regime.

As indicated by table 2, the conventional wisdom is still confirmed. Economic inequality remains much larger in the liberal welfare states and in the Southern European ones (in spite of substantial reduction of inequality in Spain 1985-2009). Inequality has grown in Scandinavia, but it remains lower than in the Continental European welfare states.

Table 2. Economic Inequality. Gini coefficients

	C.1975	C.1985	C. 1995	2000	C. 2005	C. 2009
Denmark		.221	.215	.226	.232	.248
Sweden	.212	.198	.211	.243	.234	.259
Finland	.235	.207	.228	.261	.269	.263
Norway		.234	.256	.261	.276	.250
Av. Nordic		.215	.228	.248	.253	.255
Netherlands	.251	.259	.282	.278	.271	.294
Belgium		.274	.287	.289	.271	.269
Germany		.257	.272	.270	.298	.295
Austria		.236	.238	.252	.265	.265
France		.300	.270	.270	.270	.293
Av. Continental		.265	.270	.272	.275	.283
Italy		.309	.348	.343	.352	.337
Spain		.371	.343	.342	.319	.309
Av. Ita+Spain		.340	.346	.343	.336	.323
U K	.282	.325	.354	.370	.335	.341
USA	.316	.338	.361	.357	.381	.378

Source: OECD (2008; database figure.2). 2009-data from OECD (2011b). Gini coefficients vary between 0,00 (everybody receives the same) and 1,00 (one person receives all income in society).

There are several explanations for the failure of redistribution in residual welfare states. In the first place, redistribution depends on volume. The corporatist and universal model simply redistributes a higher share of the social product. Next, there is the question of stigmatisation. If recipients of support are mainly to be found among the poor, people are more inclined to believe they are "undeserving", as compared to a situation where taxpayers and recipients are basically the same people in different roles (Albrekt Larsen, 2006). Finally, the poor are less able to speak up in public. Having people with high resources included among recipients does not only contribute to a feeling of community ("being in the same boat"); it also makes it easier to articulate resistance against deterioration. Ironically, the poorer recipients are, the larger are the risk of cuts in benefits.

It is important to note that the Gini coefficients do not fully reveal what is happening for the highest incomes, and we do not have standard measures of the top income group corresponding with the poverty rate (see below). OECD data indicates that inequality has grown more in the Nordic countries than in the Continental European ones. Still, according to the Danish Economic Council (Det Økonomiske Råd, 2011) the upper 10 per cent in the US had appropriated nearly 95 per cent of all improvement in incomes 1980-2010 (see also Hacker & Pierson, 2010). In Denmark, the figure was not much above 25 per cent, corresponding roughly with the share of income in 1980.

Finally, it is important to note that Gini coefficients are based on the distribution of disposable income. This does not take account of public services (typically provided for free, or at low costs). As public services are more comprehensive in the Nordic welfare states, and as services are relatively equally distributed, this means that the "true" distribution of consumption possibilities tend to be more equal in the Nordic countries than revealed by Gini coefficients. However, another factor pulls even more in the opposite direction: Gini coefficients do not take account of differences in commodity taxes which are highly regressive. If, for instance, income tax cuts are financed by higher VAT, or by taxes on what is considered "unhealthy" foodstuffs, the Gini coefficient will capture the impact of income tax cut. Lower income taxes almost inevitably provide higher Gini coefficients. However, Gini coefficients do not reflect the impact of higher living costs because commodity taxes are raised. This will inevitably add further to inequality, but this is not measured. As commodity taxes are very high in the Nordic countries, this omission exaggerate the "true" level of equality in the Nordic countries – in particular in Denmark and Norway.

De-commodification

In his seminal book *Three Worlds of Welfare Capitalism* (1990) Gøsta Esping-Andersen pointed out that the key difference between welfare regimes was the degree of de-commodification. In capitalist societies, labour power is a commodity, and the key characteristic of social policy is that it serves to relieve the social conditions of workers from this fundamental fact – in favour of equal status as citizens, to continue in TH Marshall's (1949) terminology. At best, the residual welfare state alleviates poverty but otherwise does not change very much. The corporatist welfare state provides social security whilst in principle maintaining status divisions; still, social equality is improved a lot as a side effect. Finally, the universal welfare state is oriented towards modifying the status system.

Esping-Andersen linked the formation of welfare regimes to the social classes/political forces behind the different models. However, the theory paid less attention to the behaviour of social classes *within* regimes. The working class or the Social Democrats in Western Europe would not have much opportunity to break fundamentally with the principles of welfare in the corporatist model. Instead, they could seek to *modify* these principles, in particular the strict association between contributions and social rights.

For instance, pensions could be related more to previous wages and less to contributions over the full life course. In the language of pension theory this would mean to move from *defined contribution* principles towards *defined benefit* pensions. Next, certain social rights could be extended beyond the employed, to groups outside the labour market, and to students. Minimum pensions could be introduced, in order to relieve people without a contribution record from dependence on social assistance in old age. Over the decades, a large number of such modifications were introduced in corporatist systems, not least in Germany. In the Netherlands, pensions even became a hybrid since they were financed by pension contributions (as a percentage of wages) whereas the corresponding benefit became a flat-rate pension like in an ideal-typical universal welfare state (Anderson, 2004).

As pointed out below, while the dominant trend of reform until around 1990 moved towards de-commodification, the trend in most significant reforms since then was reversed, even in universalist regimes, i.e. heading towards re-commodification.

De-familialisation

Another trend that has pulled in the same direction across welfare regimes is de-familialisation. Family structures have changed from single-earner families towards dual-earner families. The family dimension was fitted into a revised version of Esping-Andersen's theory (Esping-Andersen, 1999). Until then, corporatist welfare states had supported the traditional division of labour within the family, that is, single-earner families. One precondition was generous security in case of unemployment, sickness, disability etc. Another was tax rules giving advantages to families having their income concentrated on one person. By contrast, the Scandinavian countries had changed their tax systems towards treating the individual as the basic unit. This provided stronger work incentives for married women. The other main effort was provision of public child care and elderly care on a massive scale. This enabled more women to work and at the same time generated a huge number of new jobs in the public service sector.

This process was deliberately delayed in the Continental European welfare states. But pressure from well-educated women wanting a working life, and from demographic forecasts predicting a declining labour force, pushed towards modernisation. In addition, low fertility rates constitute a silent protest against unsatisfying child care facilities. Low fertility, in turn, aggravates the long-term challenge of ageing populations (Esping-Andersen et al., 2002).

When married women in the Nordic countries entered the labour force, there was an irresistible demand for public child care. When similar demands appeared in Continental Europe a couple of decades later, the “golden age” of expansion was over. Gradually, most countries have moved in the same direction, but more slowly and reluctantly. Political leaders in liberal/residual welfare states have welcomed women’s work but have not been very inclined to provide state financed child care facilities. This has left many families to solve the task themselves, e.g. by hiring domestic workers.

Even though reforms have moved in Scandinavian direction, this is an instance of parallel trends rather than convergence (Kautto & Kvist, 2001). De-familialisation remains a standard dimension for distinguishing between welfare regimes, with universalist welfare states promoting and supporting double-earning families. Residual welfare states have been less supportive, and corporative welfare states have moved from resisting change towards neutrality or active support. Still, the social care sector typically remains smaller than in the Nordic countries.

3. Regime approach – insurance approach – welfare mix approach

Welfare models can de described in different languages. The welfare regime approach remains the most widespread in social policy theory, but many economists prefer the language of insurance and risk management. As regards income transfers, these concepts make perfectly sense even though some concepts are stretched a little as compared to everyday usage. For instance, pensions are covering the *risk* of getting old. When it comes to services, conventional language must be extended even further to describe child care as risk coverage, but this is a matter of conventions.

Insurance approach

If the welfare state is analysed as an enormous insurance arrangement (figure 3.), welfare regimes may be distinguished on the basis of risk coverage and risk sharing/risk pooling. This is spelled out in Esping-Andersen (1999). Universal welfare states are described as providing widespread risk pooling (typically the entire population) for a broad range of risks. Coverage is a bit narrower in corporatist welfare states (family care less developed) [4]; risk sharing is divided by status, and those who are outside the labour market tend to suffer from insufficient social protection. The residual welfare state ideal-typically provides support for a limited scope of social risks.

Figure 3. Welfare Regimes as Models of Social Insurance.

		Risk Coverage/Scope	
		Broad	Narrow
Risk pooling	High	Universal/Social Dem.	X
	Low	Corporatist/Conservative	Residual/Liberal

The insurance perspective also facilitates discussions about public vs. private insurance. Competition usually forces private insurance companies to divide those insured into different risk categories with different premiums. As social risks are highest among the poor, they would be left with the highest payment. Moreover, some risks are almost impossible to insure (Barr, 2001). Unemployment insurance is particularly difficult. As risks are unequally distributed, competition would bring premiums that were impossible to pay for high-risk groups, and not worth paying anyway for those with low risks. This is one reason why unemployment insurance is mandatory in nearly all advanced welfare states. The state wants people to be insured because it is a welfare gain, but also because a safety net makes workers more mobile, flexible and willing to take risks (Andersen et al., 2007; Andersen, 2012). In short, there is a collective advantage of insurance.

Insurance terms also make it possible to define solidarity in terms of risk pooling. Solidarity is tantamount to pooling the “good” risks with the “bad” risks. When it comes to old-age pensions, for instance, “good” risk means a short life whereas “bad” risk means a long life. This has a significant gender aspect: If women are unable to pool their “bad” risks with the “good” risks of men, they are left with lower annual pensions even if they have the same earnings and contributions. As regards unemployment, the important question is whether low-educated individuals are punished for their higher risk of unemployment or are allowed to share risks with those having a better risk profile.

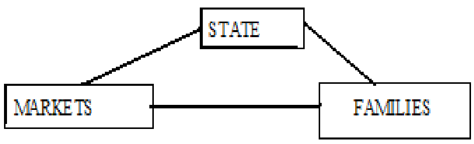
[4] Child care is expanding, as well as elderly care. It should be noticed that there have been kindergartens for decades in most Continental European welfare states, often run by the church, but with opening hours not being accommodated to normal working hours. Child care was traditionally a supplement for children who were taken care of at home.

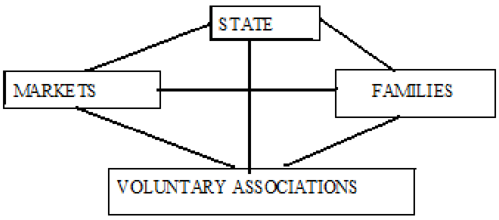
Welfare mix approach

Whereas the insurance approach is particularly relevant for transfers (cash benefits), the welfare mix approach is applied mostly for services. It should be underlined, though, that a welfare mix approach is inescapable for pensions where "multipillar pension systems" are composed of state, employment-related and purely individual private pensions.

Even though "the mixed economy of welfare" is a relatively new term (Powell, 2007), it is basically a classical perspective which was also embodied in Esping-Andersen's (1999) regime theory.[5] The approach is seeing welfare as being "produced" by some combination of the state, the market, and the family – the "welfare triangle". Sometimes voluntary associations are added as a fourth welfare producer – making the triangle into a "welfare diamond" (figure 4)

Figure 4. The welfare triangle and the welfare diamond.





As pointed out by Esping-Andersen (1999) and even more concisely by Kuhnle & Alestalo (2000), the universal welfare model puts extraordinary weight on the state; the residual welfare state emphasises the market; and the corporatist welfare state divide responsibilities between the state and the family. Kuhnle & Alestalo (2000) also identifies the Southern European Welfare State as a *sui generis*, distinguished from the corporatist model by its extraordinary emphasis on the family. Others (Ferrera, 1996) have added the universal health care system and an under-developed social assistance as important traits; missing the lowest safety net Southern Europeans become extraordinarily dependent on the family – and on undeclared ("black") labour.

Titmuss (1974) distinguished between social welfare, occupational welfare and fiscal welfare. Occupational welfare includes arrangements at the labour market, provided by the employers or through collective negotiations, e.g. pensions (in some countries also health insurance). Fiscal welfare includes tax subsidies for private welfare arrangements. In Denmark, health insurance provided by firms was tax-deductible for some years until 2012, that is, it represented a *de facto* expenditure for the state. It was debated whether it saved more money than the costs for the state.

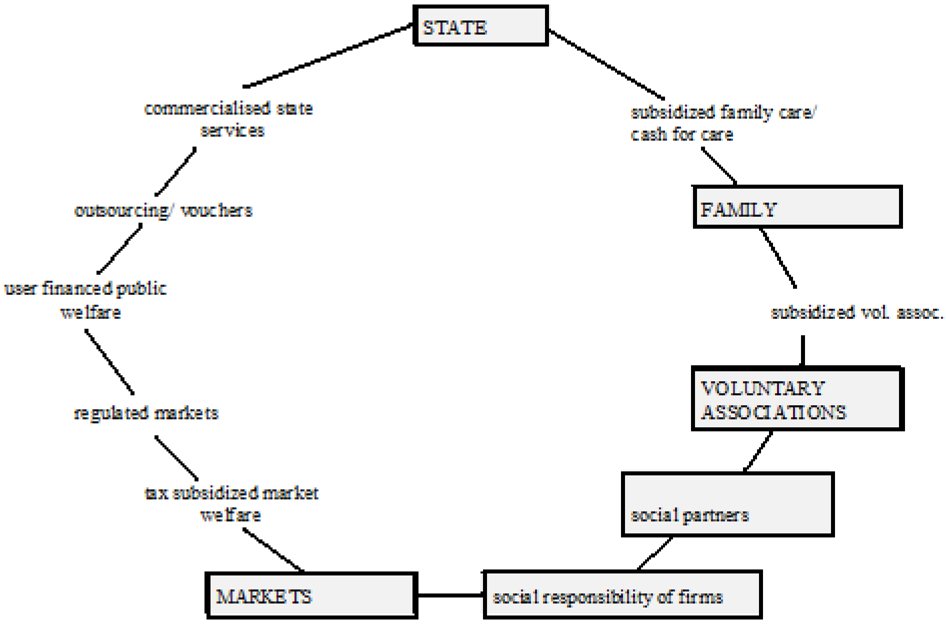
The welfare triangle and the welfare diamond are insufficient to describe the current welfare mix of e.g. Nordic welfare states. One would also have to take account of:

- The social partners (trade unions and employers' associations)
- Social responsibility of firms (overlapping with so-called "corporate social responsibility")
- Combinations including state subsidy to other welfare producers, e.g.:

[5] Johnson (1987) and others have referred to similar trends under the headline "welfare pluralism".

- Family (e.g. cash for care)
- Companies (e.g. subsidised employment)
- Voluntary associations (subsidies)
- The Market (tax subsidies or fiscal welfare)

Figure 5. An expanded welfare triangle/"governance model" of social welfare.



Moreover, the dichotomy between state and market should be replaced by eight possible combinations of *financing*, *deciding* and *delivering* welfare. *Outsourcing* combines private delivery with public responsibility for financing and decisions; *user charges* reduces public responsibility on the financing dimension; *commercial services* enables public providers to deliver supplementary services on market conditions; there is a name for each of the eight possible combinations.

Rather than seeing any intrusion of markets, firms, voluntary associations as re-commodification or welfare erosion, we need a broader perspective. From a social policy perspective, two aspects are crucial: First, the financing dimension because of its obvious implications for poverty and equality. And secondly, the state's responsibility for *outcomes*.[6] The key dimension regarding possible state vs. market combinations is financing, and several combinations of responsibilities may – in principle, at least – constitute *functional equivalents* to state welfare, provided that the state remains responsible for the *outcome* of the entire fabric (Seeleib-Kaiser, 2008).

[6] One version of Gilbert & Gilbert's (1997) concept of "enabling state" to assign such a coordinating role to the state.

4. Impact on welfare: Combating poverty, happiness, social cohesion

Redistribution and poverty

From welfare regime theory, we expect the universal welfare model to be most redistributive and adapted to mitigate poverty, followed by the corporatist model. Residual welfare states should redistribute the least. This was broadly confirmed by gini coefficients (c.f. table 2 above), and poverty rates basically reveal the same pattern (table 3). Poverty is conventionally defined as having less than 50 per cent of the median equivalised disposable income – disposable income denoting income after tax whereas "equivalised" means corrected for household composition and size[7]. The EU typically applies a poverty line of 60 per cent, reflecting higher equality ambitions.

Following the 50 per cent threshold, there are, according to OECD (Table 3), on average 7.3 per cent poor in the five Nordic countries, 8.2 per cent in six Continental European countries, 11.2 per cent in five Southern European countries (Corporatist model, southern version), and 13.2 per cent on average in five Anglo Saxon countries approaching the residual welfare model.

Table 3. Poverty before and after taxes and transfers, and poverty reduction. Late 2000s. Percentages.

Poverty threshold 50 %	Poverty before tax & transfers	Poverty after tax & transfers	Poverty Reduction: % pre-tax poor lifted
Denmark	22,1	6,1	72
Sweden	26,5	8,4	68
Finland	30,1	8,0	73
Norway	23,8	7,8	67
Iceland	19,0	6,4	66
Average 5 Nordic	24,3	7,3	70
Germany	32,5	8,9	73
Netherlands	24,1	7,2	70
Belgium	31,4	9,4	70
Luxembourg	26,9	8,5	68
Austria	28,8	7,9	72
France	32,6	7,2	78
Average 6 Continental	29,4	8,2	72
Italy	33,3	11,4	66
Spain	27,2	14,0	48
Portugal	28,4	12,0	58
Greece	31,1	10,8	65
Slovenia	25,3	8,0	68
Average 5 Southern	29,1	11,2	61
United Kingdom	31,2	11,0	65
United States	27,0	17,3	36
Australia	27,2	14,6	46
Canada	24,7	12,0	51
New Zealand	22,4	11,0	51
Average 5 Anglo Saxon	26,5	13,2	50

Source: www.oecd.org (read 2012-08-31; own calculations of poverty reduction).

[7] There is not one single method of calculation. The most simple method is to divide the household income by the square root of the number of people in the household.

Table 3 also shows how poverty is reduced by the welfare state since it includes the proportion of poor before taxes and income transfers. Pre-tax poverty is lowest in Scandinavia (24.3 per cent). As post-tax poverty is only 7.3 per cent, this means that 70 per cent are lifted out of poverty. Somewhat surprisingly, the proportion lifted out of poverty is at least as high in the Continental European welfare states. On average, Southern welfare states are less efficient in combating poverty (61 per cent lifted out of poverty). As expected, the Anglo Saxon welfare states are the least efficient. Pre-tax poverty is not extreme, but only one-half is lifted out of poverty. There is a great difference, though, between UK (65 per cent) and USA (36 per cent).

This ranking is relatively stable over time even though inequality and poverty has been increasing in all welfare regimes since the 1980s (OECD, 2008, 2011): Inequality and poverty remains lowest in Scandinavia, but Northern European corporatist welfare seem equally efficient in alleviating inequality and poverty. Southern European are less efficient, and Anglo Saxon welfare states contribute the least to inequality and poverty reduction. This would seem to confirm that the "Robin Hood" principle is not efficient.

Well-Being and Happiness

In the final analysis, the purpose of the welfare state is to improve the quality of life of its citizens. The Scandinavian countries have a long tradition of "living conditions suveys" including a wide array of aspects, mainly objective ones. Recently, OECD and others have put much effort into developing measures of the "Good Life",[8] combining objective and subjective measures. Regarding subjective measures, there are several possible indicators of well-being at the individual level; happiness or "overall life satisfaction" are the most widely used.

Needless to say, there are many determinants of happiness (Gilbert, 2007; Diener et al., 2010). At least until a level, higher GDP is among the most important ones, and at the individual level, it is social relations – alongside factors like employment/unemployment. But at least in Scandinavia, economic hardship is the most crucial aspect determining happiness among the unemployed (Goul Andersen, 2002; Ervasti, 2004; Gallie & Paugam, 2000).

Even though there is any reason to expect that welfare regime, inequality and poverty would impact on happiness and life satisfaction (Greve, 2010) – and even though bivariate associations between equality and welfare abound (Wilkinson & Pickett, 2009) – this remains a contested issue (Berg & Veenhoven, 2010) which cannot be discussed thoroughly here. Still, without drawing too hasty conclusions about causality we may observe that international survey findings conform to this assumption very nicely. Figure 6 pictures the findings of the 2010 European Social Survey where overall life satisfaction is measured on a scale from 0 to 10. At the highest rankings we find the four Scandinavian countries alongside the Netherlands and Belgium which are the corporatist welfare states coming most close to the Scandinavian ones.

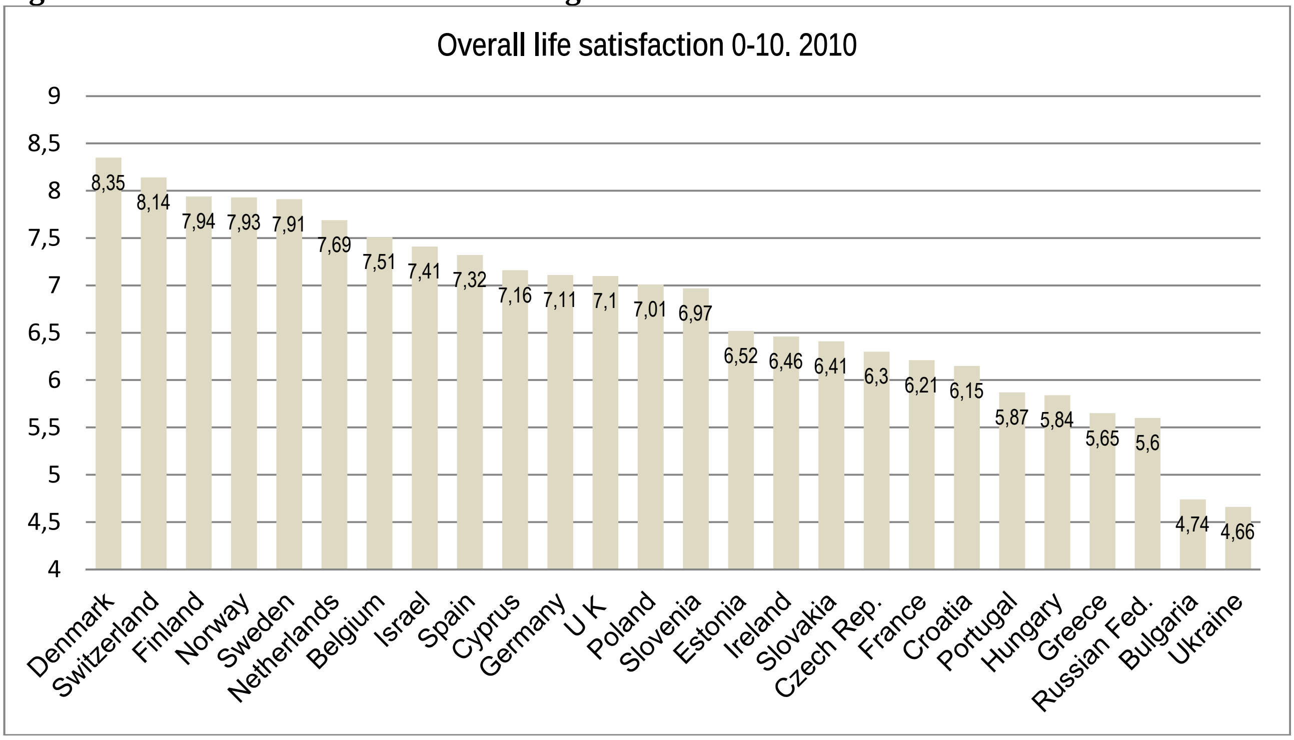
Social Capital

Another key argument regarding the welfare state is its presumed impact on social cohesion. Among several possible indicators we only include one: Social capital which is conventionally defined as norms of reciprocity and ability to cooperate. The normative side is usually considered the most important since it determines the behavioural side. The standard indicator of norms of

[8] For OECD's Better Life Initiative, see http://www.oecdbetterlifeindex.org/about/better-life-initiative/

reciprocity is social trust, that is, trust in people you do *not* know. Can most people be trusted, or do you have to be very careful when dealing with people – to paraphrase the standard question from the World Values Surveys.

Figure 6. Overall Life Satisfaction. Average on scale 0-10. 2010.

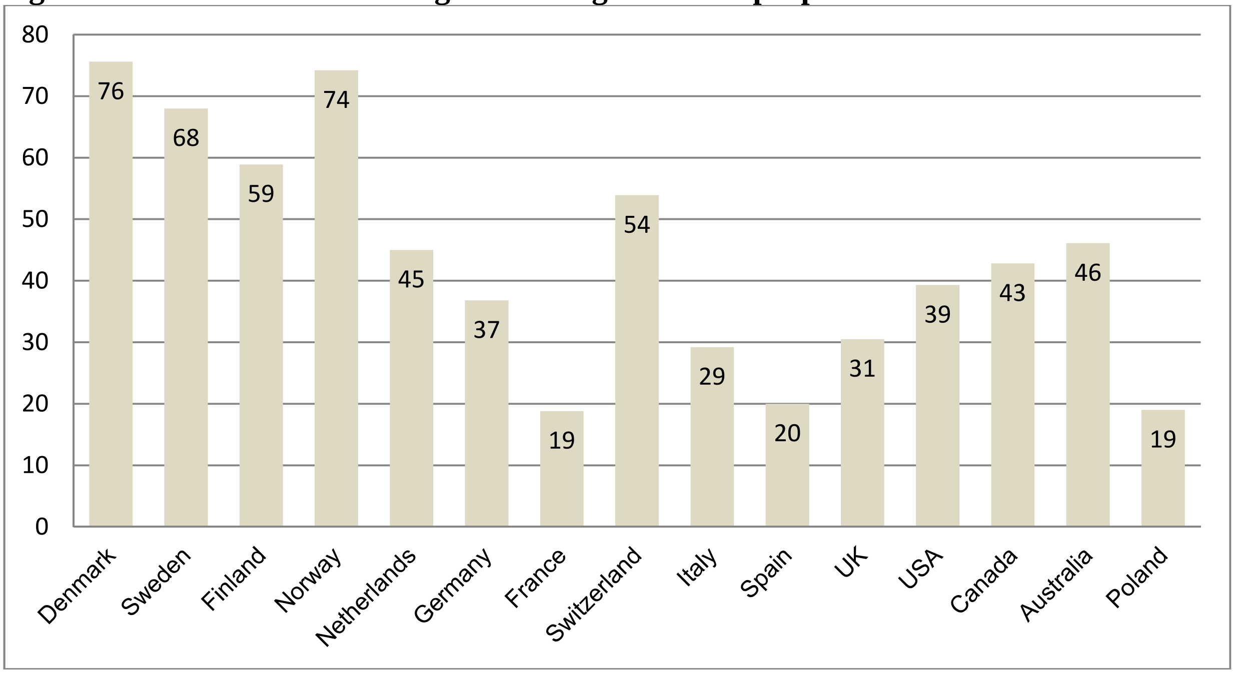


Question: "All things considered, how satisfied are you with your life as a whole nowadays? Please answer using this card, where 0 means extremely dissatisfied and 10 means extremely satisfied".
Source: ESS 2010 (own computations).

Declining social trust has been a source of concern in the Anglo Saxon countries, in particular the US (Putnam, 2000). In Continental Europe, however, no decline is indicated, and in Scandinavia social trust has rather increased. In social capital theory, social trust used to be linked to participation in voluntary associations. At the *macro level* there actually does seem to be a link; at the individual level, however, the association is weak. But it has also been demonstrated that universalist welfare institutions contribute to social trust (Rothstein & Uslaner, 2005), and others have argued that welfare generosity and mitigation of poverty is essential (Albrekt Larsen, 2007). Again, we are constrained to demonstrate that the Scandinavian welfare states are in an (increasingly) unique situation as regards social trust (see figure 7).[9]

[9] Sometimes former Communist countries are left out since low social trust in these countries has a "disturbing" impact. With the opposite sign, this also holds for Southern America as regards happiness.

Figure 7. Social Trust. Percentages believing that most people can be trusted. 2005-2008.



Question: Generally speaking, would you say that most people can be trusted or that you need to be very careful in dealing with people? 1 Most people can be trusted. 2 Need to be very careful.
Source: Calculated from 2005-08 wave of World Values Survey. (http://www.worldvaluessurvey.org) Danish data from 2010 survey of Immigration and Citizenship conducted by Epinion for the Ministry of Integration in cooperation with the author.

Like in the case of life satisfaction/happiness, there are variations over time, but the high prevalence of social trust in the Nordic countries is a stable finding, and the trend seems to be upwards rather than downwards, in spite of predictions about the impact of increasing ethnic heterogeneity etc.

Welfare and the Welfare State

The data above are insufficient to prove that welfare regime and welfare generosity determines the well-being of the population. Rigorous testing could bring us further, but we leave it here with the suggestion that welfare states seem to do their work: Alleviating poverty and insecurity, integrating people as citizens and enhancing citizens' welfare. It is not implied that all blessings are attributable to the welfare state. But most scholars would probably agree that the welfare state is co-responsible. Most decision makers – and public opinion – would also agree on the positive impact. The critical question – in the Nordic countries as elsewhere – is not whether the welfare state is desirable but whether it is sustainable. Targets of efficiency and sustainability have also overshadowed welfare within international associations like the OECD – until the significant growth in concern for the good life and for combating poverty and inequality within the last 5-10 years.

5. Demographic challenges and patterns of reform

Social challenges

Welfare states have always changed in response to changes in society at large (and *vice versa*), but phrasing this as "challenges" is relatively new. Taken literally, "challenges" could refer to new social risks, increasing inequality or new social needs, but in political and public discourse "challenges" typically denote economic challenges. It should be underlined, though, that social challenges are equally important.

Social problems are accumulating in many countries. As described above, the long-term trend towards equality and elimination of poverty was reversed from the 1980s. Increasing social inequality in health and longevity is another challenge (Brønnum-Hansen, 2006; Brønnum-Hansen & Baadsgaard, 2008) which moreover interacts with higher pension age brackets; for a considerable minority one can foresee long working age, bad health, and short retirement due to high mortality.

Most European welfare states also face increasing insider/outsider division on the labour market – referred to as *dualization* (Emmenegger et al., 2012) – with a corresponding growth in "precarious" jobs and of *working poor* – a concept previously referring to (and officially recognized in) the US (Fraser et al., 2011). Inspired by the US, European reforms aimed at alleviating the conditions of the working poor now include tax credits for the employed. Ironically, tax credits have also entered tax reforms in Denmark (2003 and 2012), even though the Scandinavian welfare states have so far experienced a *decline* in precarious employment (Dølvik et al., 2012).

One social issue is often referred to as a "challenge": Insufficient child care. The traditional family structure has eroded everywhere. Unstoppable by conservative policies aimed at maintaining the male breadwinner model, married women massively entered the labour market, much as they did in Scandinavia some decades ago. Child care facilities are typically inadequate (Esping-Andersen et al., 2002). Alternatives include domestic workers (often from abroad) and informal care by family members or older school children. Welfare states face two economic challenges: First, continuing pressure for improved public child care; secondly, low fertility rates that contribute to aggravate the challenge of demographic ageing. While the Nordic countries have solved these problems, most welfare states muddle through with some improvements in a context of long-term austerity.

Economic Challenges: Demographic ageing

Two good news are underlying the challenge of ageing populations. First, longevity has increased more than anybody could hope for. Second, declining fertility worldwide has alleviated the danger of overpopulation. In advanced industrial societies, however, the combination of these two trends constitutes an economic challenge. All countries face a significant increase in old age dependency ratios. This is normally measured as the number of elderly people (65 years or more), relative to the working age population (the 15-64 years old).

Even though child dependency ratios decline in tandem with increasing old age dependency, there will be, *ceteris paribus*, a substantial increase in expenditures for pensions, health care, elderly care etc. – and a smaller working age population to contribute. To maintain economic sustainability, governments have followed two paths. The first is to "prevent *ceteris paribus*" – making sure that other things are *not* equal. If the working age population shrinks, the task is to extract more work from those that remain – in short, to increase labour supply. The other path is pension reforms that seek to extend working life and to relieve the government from expenditures.

Activation of social protection/social investment welfare state

There are several over-arching labels for the attempt to extract more labour power. Barbier (2002) proposed the concept *Activation of social protection*, referring not only to activation, but to policies targeting all potentially employed, as well to tax policies aimed at improving labour supply. This may also involve social policies becoming subordinated to or integrated into labour market policy (Clasen & Clegg, 2011). Others have spoken of a transition to a *Social investment welfare state* (e.g. Morel, Palier & Palme, 2012). This concept is very much overlapping, but does not cover tax policy. Besides, it is somewhat more normative, but coupled to a Social Democratic vision and emphasizing investment in human resources, in particular for the young.[10]

At any rate, efforts to increase labour supply have included both carrots & sticks – and sometimes a helping hand. Activation, narrowly defined, has tended to move from a helping hand towards carrots and sticks – from a human resource approach towards a work first approach (Goul Andersen & Pedersen, 2007; Larsen, 2009; Eichhorst et al., 2008; Clegg, 2008; Clasen & Clegg, 2011; Betzelt & Bothfeld, 2011; Goul Andersen, 2012). Broadly conceived, instruments to activate include e.g.:

- Tax incentives to work longer hours, working overtime, having side jobs, etc.
- More conditionality (job search requirements etc.) for those unemployed
- Less generous security for those unemployed (shorter duration, lower benefits)
- Efforts to increase employment among immigrants
- Efforts to increase employment among the least employable: Long-term unemployed, people with health problems, disabled, and others (carrots and sticks, contacts with employers, upgrading qualifications, rehabilitation)
- Higher age brackets in retirement systems

The mix between these elements is subject to variation over time and between countries. “Social investment” denotes less emphasis on carrots and sticks, less on taxes, and more on human resources (education, upgrading qualifications). This is often combined with the other main strategy: Pension/retirement reforms.

Pension reforms

When Bismarck introduced old age insurance in 1889 for people aged more than 70, this affected a tiny minority.[11] A quarter of a century later the age bracket was changed to 65 years, and as fertility declined and longevity improved, costs slowly increased. Still, the rise in life expectancy for 60 years old did not really take off until the 1980s, and the very low fertility rates in many countries were reached in the 1970s. This puts pensions under pressure.

So-called *pay as you go* pension systems are vulnerable. They are based on the principle that the currently employed population pay pension contributions or taxes to support those currently retired. As pensions in corporatist welfare states are largely unfunded – contributions finance current

[10] Social investment in education and upgrading of qualifications has always been a core element in the Nordic welfare model. Still, in the new version social investment (not least for the middle class) is sometimes prioritized *at the expense* of social protection (mainly for the working class). It might be claimed that a class struggle is taking place *within* the welfare state, rather than *about* the welfare state.

[11] The pension scheme also included disability pension, however.

expenditures – these welfare states face a problem with the "generation contract": Having paid high contributions, people expect generous pensions in return; with a shrinking working age population this becomes difficult to finance. Pension contributions become excessively high. The state may relieve the burden by tax-financed subsidies (as in Germany), but after all, most of these taxes are also imposed on the working age population.

In the wake of the 1994 World Bank Report *Averting the Old Age Crisis*, most welfare states have taken efforts to reform the pension systems (e.g. Anderson et al., 2007; Bonoli & Palier, 2008; Kangas et al., 2010; Palier, 2010; Ebbinghaus, 2011). These reforms have several elements in common, all of which may be summarized under two headlines: "recommodification", and relief of the state from pension obligations:

- Doing away with formal or informal early retirement
- Higher pension age
- Longer contributions required for full pension entitlements (in defined benefit systems)
- Change of basic principles from *defined benefit* (politically determined entitlements, as a fixed sum, or as a proportion of wage during best years) to *defined contribution* (pensions strictly determined by contributions and returns on investments)[12].
- More *funded* pensions instead of *pay as you go*
- Movement towards *multipillar pension systems* combining a pillar of state pensions, a pillar of occupational pensions, and a pillar of purely individual pensions. This automatically involves increasing weight on the *defined contribution* principle and typically involves more emphasis on *funded* schemes

Gone are the days when welfare states were conceived as "frozen landscapes" (Goul Andersen, 2007a). All welfare states have changed in reaction to the challenge of ageing, sometimes by path-breaking reforms, sometimes by series of incremental changes that in the long run changed the path (Streeck & Thelen, 2005; Mahoney & Thelen, 2010). The Scandinavian countries were proactive in starting pension reforms already in the mid-1980s. Even though pension reforms have moved in the same direction, this is also an instance of *parallel trends* rather than convergence. Moreover, there are huge differences between welfare states as regards demographic challenges.

State and regime differences in demography

Welfare regimes and individual welfare states differ very significantly as regards demographic change. Due to large differences in fertility rates – and in net migration – countries face highly different futures of ageing (Table 4 and Figure 8). In Scandinavia, fertility has remained close to 2.0 (slightly less than required for reproduction). In most corporatist welfare states fertility is low, but France is an exception, and the Benelux countries have approached the high fertility group. This holds also for most Anglo Saxon countries. In the German-speaking countries and in Southern Europe, however, fertility has been low for decades. This is also the case for Eastern Asian welfare states which are often pictured as being most similar to the corporatist welfare model. Demography also looks troublesome for Eastern European welfare states; fertility is uniformly low. Southern Europe and Eastern Asia are among the regions with the highest life expectancy whereas Eastern Europe is lagging behind.

[12] Strictly speaking, defined contribution refers to funded systems. "Notional" defined contribution denotes systems that may be without any savings ("pay as you go"), but calculates pension entitlements according to contributions.

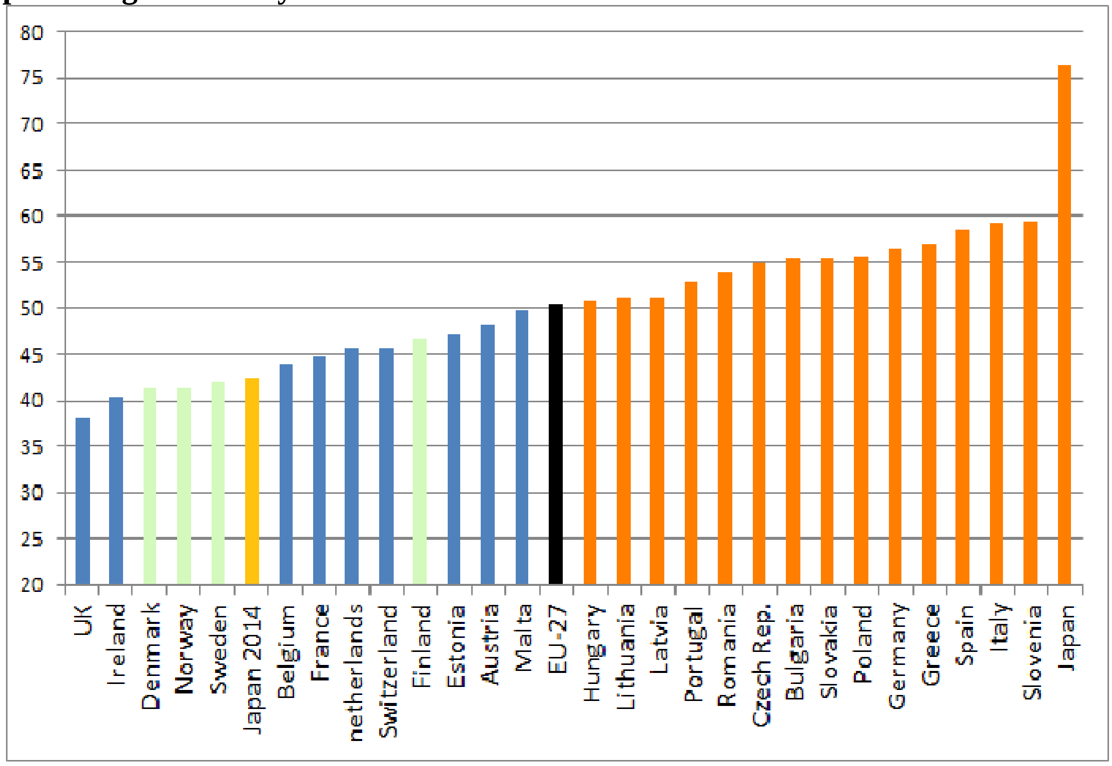
Table 4. Fertility and Life Expectancy, 2010.

		Life Expectancy at birth	
	Fertility	Men	Women
Iceland	2.20	79.5	83.5
Norway	1.95	79.0	83.3
Denmark	1.88	77.2	81.4
Sweden	1.98	79.5	83.5
Finland	1.87	76.9	83.5
France	1.99	78.0	84.7
UK	1.98	78.6	82.6
Netherlands	1.80	78.8	82.7
Belgium	1.87	77.6	83.0
Germany	1.39	78.0	83.0
Austria	1.44	77.9	83.5
Switzerland	1.54	80.3	84.9
Italy	1.41	79.3	84.7
Spain	1.38	79.1	85.3
Poland	1.38	72.1	80.6
Japan	1.39	79.6	86.4
USA	1.93	76.2	81.1
Russia (Rosstat)	1.54	62.8	74.7

Source: Eurostat; national statistics for non EU-countries.

The impact of such demographic parameters on population prospects is considerable (Figure 8). At one extreme we find Japan where the projected old age dependency ratio is expected to increase to 75 per cent. In Eastern and Southern Europe, the corresponding figure is close to 60 per cent whereas it is only around 40 per cent in the Nordic region and in a few other countries. This is about the same old age dependency rate as in Japan today (2013 or 2014).

Figure 8. Old-age dependency ratios (projections) in 2050. People aged 65 years or more as percentage of 15-64 years old.



Source: Eurostat and Japanese Statistical Yearbook.

The Japanese situation is critical since its population is estimated to decline by about two-thirds within the next 100 years. This is one of the biggest natural experiments in human history. At that time, the small Japanese population will be extremely old. Population decline means a massive downscaling, and it means that the country will probably enter a permanent negative growth situation since population decline exceeds productivity growth.

The same drama is to take place in much of Europe, albeit in slow motion. The EU is also on the verge of population decline, but until the 2020s, this can be offset by immigration. It seems that immigration is an option that Japan has not considered seriously. By contrast, in the United States the population continues to grow due to migration and high fertility rates (around the Nordic level).

Regime differences in pensions

As regards pensions, all Nordic countries are in a favourable situation. Pension systems are reformed, and demographic projections are good due to high fertility. The main threat is a decline in fertility. It is debated whether economic incentives in terms of child cash benefits may affect fertility. Some countries have designed their child benefit/tax systems to improve incentives by having larger support for the 3rd and successive children. Denmark went in the opposite direction in 2010 by limiting child benefits to two, sometimes three children. This may contribute to explain an unexpected decline in fertility from 1.874 in 2010 to 1.756 in 2011. Although the 2010 rules were repealed by the incoming government by the end of 2011, continued uncertainty contributes to low fertility throughout 2012. Over a few years, this could affect demographic prospects.

However, in the case of Denmark, an increasing share of pensioners will pay more in income taxes than they withdraw in pensions. The backbone of the pension system is changed towards fully funded labour market pensions, typically agreed upon by the social partners, with contribution rates from 12 per cent and upwards. In addition, there is a small supplementary state scheme (ATP) which is also fully funded. At the same time, the state system has become more of a residual system. Taken together, these pillars are expected to provide roughly the same outcomes as state financed contributory functions with guaranteed minima in Sweden and Norway. However, in Denmark public pension expenditures have since 1980 been *declining* relative to GDP (Goul Andersen, 2002; Det Økonomiske Råd, 2005), and in the future, large numbers of pensioners will pay more in income taxes than they receive in public pensions (Goul Andersen, 2012).[13]

[13] More specifically, this required in 2012 an income of 181.000 DKK (excluding public pensions) – about the equivalent of the labour market pension of a school teacher or a nurse. In addition to income tax, pensioners of course also pay VAT, all sorts of fees, property taxes etc.

6. Globalization as an economic challenge to welfare?

The discussion about globalisation as a challenge to the welfare state was initially linked to a new discourse about globalisation launched around 1990. This was also the time when the term "Globalization" was coined as an alternative to the previous term "Internationalisation". Moreover, internationalisation was traditionally assumed to be *positively* related to the welfare state.

Classic theories of small open economies

The most cited theories from the 1970s and 1980s – Katzenstein's (1985) book about "small states in world markets", and Cameron's (1978) analysis of the sources of public expenditure growth, had emphasised the need for large welfare states in small countries exposed to international competition. Small "open" economies (high exports and imports, relative to GDP) are highly exposed to business cycle fluctuations. This requires a high capacity of flexible adaptation and coordination of the economy in some sort of corporatist arrangements, it was argued, and a big welfare state serves to smooth this cooperation while at the same time stabilizing the economy. Hence, small states benefit from a large welfare state.

What's new about globalisation?

The new consensus that emerged in the 1990s was different. Mainstream economics had left Keynesianism and the belief in state corrections of market failures in favour of a strong belief in the market. Focus changed from market failures that required political solutions, to state failures that required market solutions. Concern with the supply side replaced concern with the demand side.

Arguably, there is a difference between internationalisation and globalisation. Internationalisation referred to any cross-national interaction. Globalisation, if taken literally, refers to interaction and dependence between continents. Critiques have argued that cross-continental trade remain modest. However, this argument ignores the issue of dependency. Previously, manufacturers could have a "home market" from which they might eventually expand to the world market. Currently, there is not much of a home market for products and services that can be traded. Except for sheltered branches, global competitiveness is imperative.

Economic globalisation usually includes three dimensions:

- Trade. Exports and Imports increase at a much higher speed than the GDP.[14]
- Foreign direct investments. The largest companies have become completely transnational and invest wherever it is most profitable.
- International capital movements. After deregulation in the 1980s, capital flows exploded

Rather than globalisation, one should perhaps speak of "globalisation regimes", distinguished by different rules of the games, set by different dominant actors. The period from the 1870s to 1913 was one such regime; the institutions set up in Bretton Woods in 1944 (lasting until 1971) was another; the extreme liberalisation 1980-2008 was a third. The crucial explanation of the globalisation regime and discourse from the 1980s onwards is political. The Reagan administration in the US, supported by Thatcher in the UK, successfully launched an international release of the

[14] It should be added that this is by no means a linear process. During the two World Wars, and during the 1930s, the trend was reversed. By 2010, some countries had not caught up the level of openness in the economy they had in 1913.

market forces, not least globalisation of financial markets. The accompanying market-oriented discourse became known as the "Washington consensus".

The global liberalization of financial markets nearly destroyed itself by the financial crisis of 2008. What follows after the great recession remains to be seen. Inevitably, the rules of the future will be co-determined by new players, in particular the "emerging economies" (a term that may become outdated as these economies mature and surpass the traditional economic giants).

In short, globalisation was never a linear process; it is *politically* determined; it is not necessarily linked to ever less regulated markets; and in the future, it seems to become less of an interaction between "poor" and "rich" countries, more of an interaction between countries at an increasingly similar economic level. Still, globalisation remains intrinsically linked to competitiveness.

Welfare states under pressure? Equality, taxation, autonomy in economic policy

Framing the question of globalisation in this language makes it possible to skip useless discussions about globalisation as a threat to the welfare state *as such*. That kind of debates followed the globalisation discourse of the 1990s, but currently there is agreement that it must be specified *what* may come under pressure. More recent discussions have focussed on three issues: Equality, taxation and autonomy in economic policy.

To begin with economic policy, there are constraints to the Keynesian steering optimism of the "golden era" of the welfare state from 1945 to 1970, aimed at full employment. Still, this does not mean complete loss of autonomy. Some instruments have disappeared, others have appeared. Maybe full employment has become more difficult to attain, but this does not necessarily constitute at threat to the welfare state.

There is a stronger logic behind the argument that globalisation entails a pressure against equality. The seminal OECD Jobs Study (1994) highlighted the trade-off between equality and employment: High minimum wages would make it impossible for employers to earn a profit on the labour power of the least skilled workers. Hence, minimum wages should be reduced. It was also argued that equality would sacrifice even more if people remained long-term unemployed, and new ideas of tax credits were disseminated as a means of alleviating the impact in equality.

However, European countries refrained from reducing minimum wages. OECD (1997) gave in and recommended activation/qualification as second-best solution. This idea was radicalised at the 2000 Lisbon summit where the EU committed itself to develop "the most competitive and dynamic knowledge-based economy in the world capable of sustainable economic growth with more and better jobs and greater social cohesion" before 2010. Leaving aside pompous language, it remains that improving qualifications among the least skilled, and avoiding poverty and social marginalisation, may contribute to mitigate the equality-employment trade off.

Empirical data have consistently shown that unemployment among the least skilled is lower in Scandinavian welfare states than elsewhere; employment rates are higher; and the ratio between unemployment at the lowest and the highest skill levels is smallest in Scandinavia where wage equality is most pronounced (Goul Andersen, 2007b). This would seem to contradict theories of liberalisation, but it is actually in accordance with the classical Rehn-Meidner economic doctrine of the Swedish labour movement (Erixon, 2011; see also Barth & Moene, 2009).

Globalization does constitute a challenge to equality as internationalisation always did. But there are other means than reducing minimum wages to match the qualification of the least skilled. Traditionally, the Scandinavian strategy has been the opposite: To improve qualifications of the least skilled to match the high minimum wages. It should be borne in mind that this remains a great challenge. But it does not leave the welfare state as a victim of the challenge of globalisation; it leaves it as a solution to this challenge.

The third argument about taxes has also been refined since it was projected in the 1990s that globalisation would force nation states into *a race to the bottom* in their competition to reduce taxes. Accordingly, there would be too little money for welfare. However, it is misleading to assume that taxes necessarily constitute a problem in relation to competitiveness. It must be specified *how* and *why* this is the case.

The crucial factor is mobility. Capital is highly mobile and is attracted by lower corporate taxes. However, taxes only constitute one incentive; being close to markets, qualified labour power, infrastructure etc. are only a few items on a long list. In fact, corporate tax rates have been significantly reduced, but mainly by widening the tax base, i.e. by removing favourable tax deductions etc. Corporate taxes as per cent of GDP have typically not declined, but most countries have abolished wealth taxes.

As regards taxes on commodities, the constraint is border trade. In the EU, this constraint has become tighter in tandem with abolition of customs control. However, there are also differences in commodity taxes between states in the US. As regards the Nordic countries, Sweden has been compelled to adjust some taxes to the Danish level, and Denmark to the German level. Still, commodity taxes have constituted a largely constant part of total revenues. Since commodity taxes are regressive taxes, however, it should be noticed that downward adjustments of commodity taxes pull towards a *more equal* distribution in the Nordic countries.

Since the 1990s, a main concern has been taxes on labour power. As labour power is conventionally seen as immobile, the traditional view was globalisation did not dictate any constraints in this field. However, for highly qualified workers with few language barriers, this might change. Hence, there has been more focus on taxes for this group.

It is important to note that it is marginal taxes that counts when the question is about incentives to increase labour supply. When it comes to globalisation, on the other hand, it is average taxes. This does not only include taxes on labour power but also indirect taxes. At least in Denmark, many political decision makers have not been conscious of this distinction, indicating that real motives are about distribution rather than concern for globalisation or labour supply.

Whatever the “true” motives, it remains that both average and marginal taxes on labour are modest in the Nordic welfare states. In 2011, according to OECD’s annual *Taxing Wages* publication (OECD, 2012a), marginal tax for a single, average worker in Denmark was the same as in the US, and for all household types except one Danish average and marginal tax rates was below average for European OECD members (table 5). Corresponding Norwegian taxes are typically slightly

Table 5. Average and marginal taxes on labour for different houshold types (AW=Average Worker). 2011. Pct.

		Single, no children			Couple, two children
		67 % AW	100 % AW	167 % AW	100+67 % AW
Average tax	Denmark	36.8	38.4	44.8	33.9
	EU-21	37.8	41.5	46.1	35.6
Marginal tax	Denmark	40.9	42.3	56.1	42.3
	EU-21	48.1	51.0	52.2	49.6

Source: OECD (2012a, table I.1 og I.6.). EU21=EU countries members of the OECD.

lower than in Denmark, Sweden and Finland slightly higher, but in general, taxes on labour in the Nordic countries are around or below European average.

Now, considering incentives to emigration, one has to consider taxes *plus* necessary social expenditures. As pointed out above (table 1), what people save in taxes in low-tax countries like the US is typically spent on private welfare insurances and services.

One should furthermore consider that those most likely to be mobile are relatively young people for whom childcare costs play a significant role. At this point, the Nordic countries, especially Sweden, are in a favourable situation since childcare costs are much lower, relative to wages, than in most other countries (OECD, 2011c).

It is doubtful whether migration for high-skilled workers is determined by economic incentives. But except for people with very high incomes, there are no obvious tax/welfare motives to avoid the Nordic countries. If there is a brain drain problem, it is driven by career opportunities, job preferences, climate preferences and other factors which the welfare state can do little about.

Competitiveness of the Nordic countries

Finally, the economic performance of the Nordic welfare states and the corporatist welfare states in Northern Europe appear very convincing in the wake of the “great recession”. As revealed by table 9.6, these countries reveal very high surpluses on the balance of payments. In the opposite position we find the so-called PIGS-countries (Portugal, Italy, Greece and, Spain) as well as UK and USA.

When it comes to public budgets, it’s the same story, with the Nordic countries doing even better, comparatively speaking. Among EU Countries, only Denmark, Sweden, Finland and Luxemburg kept within the EU convergence criteria throughout the crisis. So did Norway and Switzerland which have remained outside the EU. Budget deficits have not exceeded 3 per cent of GDP at any time, and in Sweden, Finland and Norway there is no state debt at all. In addition, the Danish and Swedish state hold large but invisible assets in postponed taxes in pension savings.

Table 6. Balance of payment as per cent of GDP.

	2010	2011	Average 2006-11
Denmark	5.5	6.5	3.8
Norway	12.4	14.6	13.8
Sweden	6.9	7.2	7.9
Finland	1.7	-0.6	2.3
Iceland	-8.0	-7.1	-15.1
Netherlands	7.1	9.2	6.8
Belgium	1.3	-0.8	0.1
Germany	6.0	5.7	6.3
France	-1.8	-2.1	-1.5
UK	-3.3	-1.9	-2.3
USA	-3.2	-3.1	-4.1
Italy	-3.5	-3.1	-2.7
Spain	-4.6	-3.5	-6.9
Greece	-10.1	-9.8	-12.0
Portugal	-10.0	-6.4	-10.1
Japan	3.6	2.1	3.4

Source: OECD Economic Outlook June 2012 database.

Table 7. Public budget deficits and net public debt. Per cent of GDP.

	Budget deficit/ surplus			Net public debt/ assets		
	2007	2010	2011	2007	2010	2011
Denmark	4.8	-2.7	-1.9	-3.8	-1.7	3.5
Sweden	3.6	-0.1	0.1	-22.5	-24.0	-21.1
Finland	5.3	-2.9	-0.9	-72.6	-65.1	-52.6
Norway	17.3	11.2	13.6	-138.9	-164.9	-160.9
Iceland	5.4	-10.1	-4.4	-1.0	48.3	49.7
Germany	0.2	-4.3	-1.0	42.6	50.5	52.0
France	-2.7	-7.1	-5.2	35.7	57.4	63.0
Netherlands	0.2	-5.0	-4.6	27.8	34.4	39.0
Belgium	-0.1	-3.9	-3.9	73.1	80.1	81.6
Italy	-1.6	-4.5	-3.8	86.8	99.3	93.7
Greece	-6.8	-10.5	-9.2	82.6	114.6	134.6
Spain	1.9	-9.3	-8.5	17.8	40.2	48.6
Ireland	0.1	-31.2	-13.0	-0.0	57.4	74.2
UK	-2.8	-10.3	-8.4	28.4	53.8	68.3
USA	-2.9	-10.7	-9.7	48.0	72.9	74.2
Switzerlands	1.7	0.6	0.8	0.9	-2.4	-3.1
Japan[4]	-2.1	-8.4	-9.5	80.5	112.8	125.5
Euro area	-0.7	-6.2	-4.1	42.7	57.8	60.7

Source: OECD Economic Outlook June 2012 database.

Baumol's disease

If the "new challenges" do not by any means appear frightening in the Nordic case, one "classical" challenge should be mentioned. It is well-known that productivity increase is usually much higher in manufacture than in services. Improving productivity in welfare services is often believed to be particularly difficult – how can productivity be improved in child care, elderly care, teaching, hospital treatment etc?

As wage increases tend to be uniform across the labour market – largely following the sector(s) exposed to international competition (Dølvik et al., 2012) –relative price of services will increase. As is well-known by any customer at a hairdresser, the price of a haircut as compared to industrial consumer products has increased over the years. If one were to increase the number of haircuts at the same speed as the consumption of electronic equipment like mobile telephones, i-pods, laptops/tablets (once considered a luxury), haircuts would swallow an increasing portion of the budget. As people do not multiply their consumption of haircuts, this problem does not emerge. But when it comes to welfare services, the standard expectation is increase at the same speed (in fixed prices) as private consumption or GDP. However, as price per unit increases much faster when it comes to services, an equivalent growth rate (in fixed prices) make welfare services swallow an increasing part of the total budget.

Sometimes this problem is exaggerated by assuming that productivity growth in welfare services is zero. We know from health care that this is not the case. Still, welfare services (public or private) are, by their very nature, productivity laggards. This means that the growth rate (in fixed prices) has to be lower than overall economic growth unless one will accept an increasing proportion of GDP allocated to welfare services. This does not mean that welfare is doomed, or that taxes/private welfare expenditure is bound to approach 100 per cent of the budget. After all, if the economy grows by 100 per cent, one would not necessarily expect two teachers per classroom. But it contributes to explain why public budgets, in particular services, are always under pressure. Allocating most public expenditures to services, the Nordic welfare states are the most vulnerable at this point.

7. Conclusion & the political future of the welfare state

The welfare state is an inevitable concomitant of a capitalist market economy, but it has historically developed in different directions. These have crystallized in three institutional complementarities called welfare regimes. Politics matter for the establishment and maintenance of these regime models, but perhaps in slightly more complicated ways than suggested by the political labelling as Social Democratic, Conservative and Liberal. In particular, this perspective has tended to leave out the question how political forces work within the frame of different welfare regimes.

If functionalists were right in seeing the welfare state as necessary for the surrounding society and in predicting an increasing share of the GDP being spent for welfare – private or public – they are also right in emphasizing the importance of new challenges. The welfare state has always been forced to adapt to contextual factors, including demography and international competition.

It does not follow, however, that welfare states are forced to dramatic cutbacks because of demography and globalization. In the first case, the Nordic welfare states, usually considered the most generous ones, seem to perform better than their neighbours in this new context. Public budgets have remained stable even during the crisis, and big balance of payment surpluses indicate excellent competitiveness. As regards childcare, welfare is certainly part of the solution, not part of the problem.

Different welfare regimes face somewhat different challenges in the future, and they are likely to react in different, but regime-dependent ways. The Nordic experience shows that the challenges are by no means insurmountable, and the experience of the US and the UK perhaps that moving towards a residual welfare state does not solve many problems.

One major challenge is to adjust working age to the fact that people do not only live longer but also remain young longer. The youth period is stretched by several years as indicated by postponement of first childbirth from the age of 22 to the age of 29 in most of Europe, and on average, the biologically appropriate time for retirement is postponed by a similar number of years.

Another major challenge is to increase competitiveness by prioritising social investment, especially education for the young generation, but also upgrading of skills, and of course research that can ensure innovation.

These challenges may be large, but it seems difficult to argue that these challenges are larger than the challenges experienced by welfare states previously. It should be noticed, however, that there are also new social challenges. The considerable improvement of health for middle aged and elderly people is marked by a significant social gradient, and there are similar social challenges as regards the upgrading of qualification levels for the young generation. Finally, immigration may help avoid population decline in those countries most affected by declining fertility rates, but it also poses the challenge of avoiding new social divisions, and new social divisions coinciding with ethnic ones.

Still, the welfare state has always been exposed to challenges, and it is questionable whether the challenges of the future are larger, given the current level of production and wealth, than the challenges of the past.

This does not mean that welfare states are unlikely to change. On the contrary, there might seem to be quite significant changes under way, not least in the Nordic welfare state. But the causes are *political*. As it has been the case from the birth of the welfare state until now, political, ideational and institutional factors have been the important drivers of change. Certainly, there have been economic, social and other factors driving all market economies to develop some kind of welfare state. Moreover, we find a significant trend to convergence between developed nations as regards the proportion of the gross domestic product spent on welfare. But political factors determine whether this is state provided welfare or private welfare, political factor determine the financing, political factors determine the distributional outcome. This has been the case until now, and even though the welfare states always have to adjust to changes in the surroundings, political, ideational and institutional factors will definitely be the main determinants of destiny of welfare states also in the future.

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