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RECONCILING WORK AND POVERTY REDUCTION

HOW SUCCESSFUL ARE EUROPEAN WELFARE STATES?

EDITED BY BEA CANTILLON
AND FRANK VANDENBROUCKE

OXFORD

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How Successful are European Welfare States?

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INTRODUCTION

Bea Cantillon and Frank Vandenbroucke

This book originated in a soul-searching experience driven by a common concern for social cohesion in Europe. At the time, the co-editors were both actively committed, albeit in different capacities, to the renewed ambition to add a social dimension to the policies of the European Union (EU). But were the concepts, the statistical systems, and the monitoring arrangements that underpinned this ambition creating added value? Were the policies that had been advocated delivering tangible results?

The new social ambition took shape in a context of significant change, both at EU level and within individual European welfare states. The decades around the turn of the millennium had seen the implementation of the Economic and Monetary Union project and the accession of post-Communist countries following the fall of the Berlin Wall in 1989. Increasingly, the EU had been presenting itself as an important player, first in the fields of budgetary discipline and employment, and subsequently in the promotion of social inclusion as an over-arching policy objective. In 2000, the first social agenda in the history of the EU was launched. The Lisbon Council had concluded that "the number of people living below the poverty line and in social exclusion in the Union [was] unacceptable," and boldly asserted that "steps [had to] be taken to make a decisive impact on the eradication of poverty."[1] In what may be regarded as the first move toward "Social Europe," the Lisbon Strategy proposed a loose and flexible policy approach. Known as the Open Method of Coordination, its purpose was to allow the Member States to learn from one another's experiences in outlining national policies toward a common goal. Crucially, a set of social indicators was agreed upon that would enable policymakers "to define in a more precise way the substance of the European Social Model" (Vandenbroucke, 2002a; Atkinson et al., 2002). Subsequently, a stronger emphasis on social rights and solidarity was incorporated into the Lisbon Treaty. Concurrently, combating poverty came to the fore quite prominently and consistently as a specific area for EU policy coordination and cooperation.

This evolution unfolded at the very moment that European welfare states were committing to a process of major reorientation in finding ways to successfully combine budgetary restraint, employment growth, and equality. With hindsight, that reorientation has been interpreted as a turn toward a new policy focus: uneven, disparate, not always consistent, but sufficiently clear across a large group of welfare states to label it a "social investment turn." In Chapter 8 of this book, Hemerijck explains that a key idea in the new concept was to "prepare" individuals and families to adapt to changing career patterns and working conditions, to new social risks and population aging, instead of simply "repairing" damage caused by unemployment, social exclusion, and poverty. The social investment perspective underlines the importance, for the long-term development of human capital, of early childhood development, training, education, lifelong learning, and family reconciliation policies. Looking back, one may say that the Lisbon Strategy was instrumental in promoting "social investment" as a policy recipe for success in the fields of both employment and social inclusion. For sure, at the time, social investment was less of a reference concept in scholarly literature than it is today. Moreover, it has always been a somewhat ambiguous concept, open to many interpretations. One can even debate the actual importance of the Lisbon Council in promoting policy change. To the extent that a "social investment turn" is discernible in European social policy, in many countries this process began well before 2000. Nevertheless, we may look back on the first decade of this century as a period when social investment was put firmly on the agenda of the EU, in a drive to modernize social policy. As the Lisbon Council put it: "Investing in people and developing an active and dynamic welfare state [is] crucial both to Europe's place in the knowledge economy and for ensuring that the emergence of this new economy does not compound the existing social problems of unemployment, social exclusion, and poverty." Aspirations were high, given that the Council conclusions spoke of "the eradication of poverty" as a strategic social policy goal within the Union. Obviously, such a bold statement reflects political rhetoric, but the hope was nonetheless that higher employment would reduce social spending levels and reorient expenditure toward more "productive," activating and inclusive policies, and toward combating poverty, either directly through work or, indirectly, through more adequate, inclusive social provisions.

Prior to the financial crisis, the Lisbon Strategy could be regarded as a qualified success in the field of employment, at least if one assumes there to have been causal relationships between the Lisbon Agenda and growing employment rates across Europe. On the other hand, though, the Lisbon Strategy largely failed to deliver on its ambitious promise concerning poverty, certainly if one uses national at-risk-of-poverty rates (the number of individuals living in a household with less than 60% of the national median household income) as the benchmark. In this book, we focus on poverty rates among the non-elderly population only. By 2007, the overall picture was not one of success in both employment and social inclusion, but rather seemed to combine three features: stability in at-risk-of-poverty rates for the non-elderly population in the majority of countries, increasing poverty rates in some countries, and decreasing poverty rates in yet another subset of countries.[2] In a technical sense, between 2004 and 2007 there was "convergence" of national at-risk-of poverty rates: Poverty rates increased in some Member States, where they had been traditionally low, while they decreased in other Member States, where they had been traditionally high. So conceived, the verdict on the antipoverty ambition of the Lisbon Strategy was unequivocal: Poverty had not decreased in most of the Member States of the Union (Social Protection Committee, 2009). In Chapters 1 and 2 of this book, we assess that verdict on the basis of facts and figures. But Chapter 2 also qualifies it with a pan-European perspective on cohesion among Member States, by proposing a truly pan-European definition of poverty. The reader of this book will soon become aware that the expression "social cohesion in Europe," used without further specification in the opening sentence of this introduction, conveys two meanings: social cohesion in each of the Member States of the European Union, and cohesion among the Member States of the Union.

CENTRAL QUESTIONS, TIME FRAME, AND SCOPE OF THE BOOK

If the poverty record of most European welfare states prior to 2008 is disappointing, from 2008 onwards the overall picture became truly negative. By 2010 the at-risk-of-poverty rate had decreased in only two Member States (Poland and the United Kingdom [UK], but with a concomitant decline in median incomes in the UK), compared to the situation in 2004. In a large group of Member States poverty had increased, sometimes quite substantially. Therefore, against the background of ongoing population aging and the lasting impact of the financial crisis—as a result of which the future is looking much bleaker than the past—it is important to gain insight into what happened before the present downturn. Why did most of the rich welfare states fail to cut poverty levels prior to the financial crisis, and which factors contributed to the success of many of the new Member States? Our purpose is not to assess the effectiveness of European governance as such. Nor do we intend to analyze the details of social policy in individual Member States. Our aim is rather to "map" changes in poverty, employment, and social spending on the basis of data that have become available for those same years via the European Statistical System. Such a "mapping exercise" is a necessary first step in gaining an understanding of the reasons behind what has ultimately been a failure to achieve stated objectives. We thereby confine the analysis to the non-elderly population, given the importance of the employment-poverty nexus in our analysis of welfare state change.

Chapter 1 introduces this "mapping" by focusing on two key parameters, social spending and "household employment," and by exploring their explanatory power with regard to poverty outcomes across European welfare states. We describe different patterns of "household employment" across the EU by distinguishing individuals living in "work-rich households" from individuals living in "work-poor" households. This distinction is based on the "work-intensity" of households: The work-intensity of a household measures the degree of labor market participation by the working-age adults in that household. Work-poor households are characterized by relatively low levels of work-intensity; they typically face much higher poverty risks than work-rich households. Chapter 1 starts from the following observation: at-risk-of-poverty rates correlate negatively both with social spending (though the correlation is far from perfect) and with the share of individuals living in work-rich households (though, again, the correlation is not very strong). This observation is explained by two basic facts: First, in all European welfare states, individuals in work-rich households are confronted with relatively lower levels of poverty than individuals in work-poor households; second, across European welfare states, high levels of social spending are associated with less poverty within both work-poor and work-rich households. This account of cross-country differences in poverty rates sets the scene for the central themes developed in the book, which may be summarized in four sets of *analytical* questions. They all start from observations with regard to at-risk-of-poverty rates among the non-elderly population and should shed light on the fundamental *policy* challenge underlying this book. That policy challenge refers to the notion of *employment-centered welfare reform* and can be summarized as follows: is it possible to structurally replace spending on cash benefits for working-age adults and their families with employment creation, and to simultaneously reduce poverty among working-age adults and their children? We thereby focus on an analysis of the social performance of European welfare states during the good economic years that is substantive rather than related to weaknesses in the Lisbon governance architecture: the transition from the old distributive welfare state to a new social investment state may be more difficult than expected.

A first set of analytical questions derives from a decomposition of changes in poverty rates over time, which is basically an accounting device. Changes in national at-risk-of-poverty rates can be decomposed on the basis of three contributory factors: (i) changes in the share of individuals living in work-poor households; (ii) changes in poverty risks in the population subgroup living in work-poor households; and (iii) changes in poverty risks in the work-rich segment of the population. Such a decomposition allows us to assess the following question: Are disappointing evolutions in poverty rates a consequence of relatively limited reductions in the share of individuals living in work-poor households (despite years of economic growth between 2004 and 2007)? Or, has the reduction in the share of individuals in work-poor households been "neutralized" by increasing poverty within the work-poor and/or the work-rich segments of the population? *In other words, was the distributive upside of creating jobs (fewer people confronted with high poverty risks in work-poor households) offset by a distributive downside (more poverty among the work-poor and/or the work-rich households) that may have been intrinsic to the way in which jobs were created?* Conversely, are we able to discern countries where "poverty success" was clearly the result of "employment success"? This first set of questions refers to a crude observation already made by the Social Protection Committee (2009) in its assessment of the Lisbon Strategy: In the EU15, the proportion of children and working-age adults living in jobless households had hardly decreased during the good economic years before the crisis. Household joblessness constitutes a crucial policy parameter in the Social Protection Committee's analysis, because the risk of poverty is much higher in jobless households than in households where at least one person is in work. This book builds upon that crude observation in two ways. Using relatively recent developments in Statistics on Income and Living Conditions (SILC) and the European Statistical System, we broaden the scope from jobless households to work-poor households, a concept that encompasses households that participate to a limited extent in the labor market[3] and allows a more fine-grained analysis of household employment rates. Simultaneously, we try to understand why household joblessness follows a different trajectory than individual joblessness, which is also the focus of the next set of questions.

The second set of questions refers to patterns of individual and household employment in European welfare states. If the share of individuals living in work-poor households diminished less than one might have expected, is this simply a consequence of the fact that the number of individual jobs increased less than one might have hoped during the boom years? Or, was there a limited "conversion" of increases in individual employment rates into increases in household employment rates? Such a limited conversion of individual employment success into household employment success may be explained by changing household structures and/or by sociological factors leading to a skewed distribution of individual jobs over households (Kalleberg, 2011). The latter phenomenon is coined "polarization" in Chapter 3, which explores this second set of questions.

The third set of questions relates to changes in social spending, notably spending on cash benefits for working-age adults and their households. (Throughout this book we will use "working-age cash benefits" as a short cut for this category of expenditures, and "working-age benefits" when we aggregate in-kind and cash benefits.) It starts from the observation that, in a number of EU Member States, poverty risks increased in the work-poor and/or the work-rich segment of the population. We therefore examine trends in poverty reduction through social transfers, as measured by the difference between pre-transfer and post-transfer poverty headcounts. Can we discern a structural trend toward less poverty reduction by transfers in work-poor households (for whom social transfers are very important) and/or in work-rich households? If so, is this attributable to the fact that the level of spending on working-age cash benefits was reduced, in a *structural* way, to make room for spending on pensions and health care, and/or to make room for spending on "social investment programs," such as child care, active labor market policies, education...? To assess these questions, we will document changes in the structure of social spending. But, apart from aging, increasing healthcare needs, and the shift to service provision related to social investment, there may also have been a paradigmatic shift. The emphasis on "making work pay," which has been part and parcel of the activation strategies pursued in the past, may have justified—and thus contributed to—the retrenchment of traditional unemployment benefit programs and, consequently, may have occasioned a structural decline in the capacity of governments to reduce poverty among working-age people.

This third set of questions prompts a *fourth set*. In the welfare states under review, the structure of social spending gradually shifted toward relatively more spending on services and relatively less spending on cash benefits. Hence, it may be the case that our assessment of poverty increasingly underestimates the redistributive impact of welfare states, since it does not take into account the value and distribution of growing public services when measuring the standard of living enjoyed by households. On the other hand, it can be argued that a shift from cash benefits to benefits in kind implies less redistribution, if the counterfactual benchmark we apply is more spending on cash benefits rather than on public services. In short, more spending on public services may imply more redistribution, if the counterfactual benchmark is less social spending *tout court*; but more spending on public services may be seen to imply less redistribution, if the counterfactual benchmark is substitution of cash benefits for public services, with unchanged levels of social spending. In Chapter 6, Verbist and Matsaganis examine this issue by broadening the income notion, with regard to both inequality and poverty. In Chapter 7, Van Lancker and Ghysels further explore the shift from cash to service spending, with specific focus on family policy (i.e., child benefits, childcare services, and parental leave benefits).

In short, starting from the idea that we can define "household employment rates," by counting the share of individuals in jobless (or, more generally, work-poor) households, our first set of questions decomposes changes in at-risk-of-poverty rates in changes explained by changes in household employment rates on the one hand and changes attributable to poverty evolutions within work-poor and work-rich households on the other. Our second set of questions examines the relationship between household employment rates and individual employment rates. The third examines the impact on poverty of spending on working-age cash benefits in work-poor and work-rich households. Our fourth set of questions, finally, broadens the notions of income poverty and income inequality in order to allow an assessment of the impact of spending on cash transfers and on public services respectively.

The ambition of this book is to formulate answers to these questions by means of survey data from the European Labour Force Survey (LFS), the European Community Household Panel (ECHP), the European Statistics on Income and Living Conditions (SILC), the German Socio-Economic Panel (SOEP), and spending data provided by Eurostat on the basis of the European System of integrated Social Protection Statistics (ESSPROS) system and by the Organisation for Economic Co-operation and Development (OECD) Social Expenditure Database (OECD SOCX). Hence, apart from OECD SOCX, we deliberately rely on the European Statistical System (ESS) and propose analytical tools that use this statistical apparatus creatively. The ESS was developed by the Commission and by Eurostat with a view to informing policymakers about changes in the distribution of work and well-being within and between Member States. In this sense, our book also constitutes a test of the European Statistical System's relevance in that policy perspective.

However, in addition to analyzing data made available in the European Statistical System, we also aspire to enrich the analytical questions listed above, in four ways. *First*, the at-risk-of-poverty headcount based on a threshold of 60% of the national median standardized household income, on which we focus, will be put in perspective. It is only one of the indicators agreed upon by the EU Member States in 2001. Various other indicators build on this notion, including indicators on the depth and duration of poverty. For the sake of simplicity, we mainly report results based on the at-risk-of-poverty headcount. We must of course be aware of the fact that this relative income measure has inherent conceptual and methodological shortcomings that may result in some failures and/or successes being overlooked. These issues are discussed at length in Chapter 2 of this book.

Second, the account of trends in at-risk-of poverty rates, trends in household and individual employment rates, and trends in social spending should highlight the different developments among the European welfare states. Over the past decade, remarkable differences in outcomes have been associated with the strong momentum of growth in the new Member States, instantiating the "convergence machine" that Europe has often been in good times (World Bank, 2012). But even within the EU15, the analysis has to disentangle a mixture of common societal trends and disparity in policies (Chapters 3 and 5).

Third, we consider it necessary to integrate the issue of in-work poverty in our analysis of the Lisbon-era results, and to link in-work poverty with the "household employment" approach that structures much of this book. The expressions "in-work poverty" and "working poor" refer to a situation where an individual is employed but lives in a poor household. Hence, belonging to the "working poor" is conceptually different from being a member of a "work-poor household": A member of a work-poor household may very well not be working at all, so that he or she is not among the working poor. Conversely, an individual in work may, in theory at least, be a member of a work-rich but financially poor household, and thus belong to the "working poor." Nonetheless, it appears that in-work poverty is explained to a large extent by the work-intensity of the household to which the working individual belongs (Chapter 4).

Fourth, one should avoid too narrow a conceptualization, and thus an inevitably poor account, of welfare state change. Both survey data and administrative spending data allow one to test certain hypotheses with regard to the development of welfare states, but caution is urged in both instances. The limitations of survey data, for example with regard to statistical significance, are well-known and quite apparent in our research, too. Administrative data, for their part, may also offer less robust support for welfare state analysis than one may *prima facie* think. Therefore, we also rely on indicators of the generosity of social benefits. In Chapter 5 both average benefit levels measured in the ECHP and SILC surveys and calculated theoretical disposable incomes of standard family types are used to identify the impact of policies. We also make use of microsimulation models in order to assess the trade-offs between benefit generosity and employment traps.

A full understanding of the dynamics of change in welfare states requires a broader analysis that takes due account of changes in discourse, changes in macroeconomic policy, institutional changes, and—last but not least—demographic changes (Chapters 8 and 10, and the Appendix). So, together with the four sets of analytical questions listed above, these four preoccupations guided the organization of this book.

Ours is not the first book to have been prompted by disappointing poverty trends. The OECD publication "Divided We Stand" (OECD, 2011) examines in detail how globalization, regulatory reforms in labor and product markets, altered household structures, and changing tax and benefit regulations impacted rising inequalities. The present book adopts a somewhat different perspective, though, focusing on how pre-transfer poverty evolved, who benefited from expanding labor markets, and how the poverty reducing capacity of cash social spending evolved. Because the main goal is to gain a better understanding of the mechanisms at play during the "good" years (the future is, after all, pregnant with the past), the analysis focuses on the period covered by the SILC surveys 2005–2008; given the fact that the SILC data of year *T* generally refer to year *T-1*, the period considered is actually 2004 to 2007. While this is admittedly a rather limited time frame, the analyses are complemented where possible and useful with pre-2000 data drawn from ECHP and LFS and, in the case of Germany, with SOEP. Moreover, we add a perspective on the crisis years, by integrating results from SILC 2009–2010–2011 in Chapter 1, and from SILC 2009 in Chapter 2. Thus, the reader is able to assess the relevance of our analysis of the "good years" for the present predicament of the Union.

In all chapters, the analysis covers all EU27 Member States insofar as data availability permits. In some chapters, Norway and Iceland are added to the analysis, as their inclusion is deemed to make the analytical framework more robust and richer.

THE BOOK AT A GLANCE

Chapter 1 presents stylized facts concerning at-risk-of-poverty rates for the non-elderly population, household employment, and social spending for 27 EU Member States, Norway, and Iceland.[4] In order to set the scene for the following chapters, Vandenbroucke and Diris focus on the correlation between poverty risks on the one hand and household employment and social spending on the other, as explained earlier.

Chapter 2 considers the measurement of poverty in the European Union and presents a number of key methodological choices in relation to the metric of well-being, the determination of cut-off values, and the question of aggregation. Based on data from SILC 2005–2009, Decancq, Goedemé, Van den Bosch and Vanhille demonstrate that, far from being trivial, the choices for a specific metric of well-being and for a country-specific (as opposed to EU-wide) poverty line strongly impact on observed outcomes.

In Chapter 3, Corluy and Vandenbroucke explore the link between poverty risks and (increasing) employment rates. Because the former are conventionally measured through household income and the latter through individual employment rates, a first step in the analysis considers the distribution of employment at the household level. Focusing on household joblessness (as opposed to the more general notion of household work poverty), actual changes in household joblessness are decomposed in (i) changes due to changing individual employment rates and changing household structures; and (ii) changes in the distribution of jobs over households. This analysis is integrated into the decomposition of changes in the at-risk-of-poverty rates. This technique yields interesting insights into the trajectories that individual EU welfare states have followed over the past 10 years. It reveals the disparity of policy pathways in the EU during the Lisbon era. The results also show that evolutions in "polarization" of jobs over households reflect long-term trends that provide, for most countries, little explanatory power for short-term evolutions in poverty.

In Chapter 4, Marx and Nolan consider the nature of and evolutions in in-work poverty. Contrary to widely held beliefs, they do not observe a secular rise in in-work poverty linked to a general increase in wage inequality. Rather, they find in-work poverty to be strongly linked to work-intensity at the household level, which is associated in turn with institutional settings and the broader welfare state. In view of their findings, the authors consider relevant policy strategies, including the maximization of work-intensity, minimum wage setting, direct income supplements, and tax credits.