

SOCIAL INEQUALITIES IN EUROPE

THE CHALLENGE OF CONVERGENCE AND COHESION

Frank Vandenbroucke | *Professor at the University of Amsterdam and the University of Antwerp, Social affairs adviser at the Jacques Delors Institute*

David Rinaldi | *Research fellow at the Jacques Delors Institute*



In all the countries of the European Union, the welfare state has come under intense scrutiny as a result of budgetary pressures and wider societal developments. The Vision Europe initiative has chosen to focus this year on the future of the welfare state, and aims to develop innovative policy recommendations on how to ensure the long-term sustainability of national welfare systems in Europe. This paper is one of the four studies edited in the framework of the Vision Europe project for the year 2015 which have presented on the occasion of the first Vision Europe Summit, which took place in Berlin on 17-18 November 2015.

Vision Europe is a consortium of think-tanks and foundations that came together in 2015 to address some of Europe's most pressing public policy challenges. Through research, publications and an annual summit, it aims to provide a forum for debate and a source of recommendations for improving evidence-based policy-making at both national and EU levels.

Vision Europe participating organizations: Bertelsmann Stiftung (Germany), Bruegel (Belgium), Calouste Gulbenkian Foundation (Portugal), Chatham House (United Kingdom), Compagnia di San Paolo (Italy), Jacques Delors Institute (France), The Finnish Innovation Fund Sitra (Finland).

SUMMARY

Europe is becoming more unequal, both between and within countries, but there is no one-size-fits-all explanation for this. The EU has stopped being a 'convergence machine'. Overall, new member states recorded impressive economic growth after their accession to the EU, but the Eurozone crisis triggered a process of divergence between the Eurozone members. Within the member states, the overall position of pensioners has improved, but, among the non-elderly population, two mutually reinforcing processes of polarisation are leading to more inequality at the bottom end of the income distribution. First, more people are living in work-poor households, i.e. households with a weak attachment to the labour market; second, these households are experiencing higher poverty risks. The latter trend already started before the crisis.

There is no silver bullet to tackle increasing inequalities; we need a set of complementary strategies and instruments that can improve both the social protection and the employment perspectives of households with a weak attachment to the labour market. The role and quality of traditional instruments of social policy, such as unemployment insurance, activation and minimum wages, have to be reconsidered, both within the member states and at the level of the EU. Simultaneously, innovative approaches with regard to social services and benefits are necessary to overcome policy stalemates in certain areas, such as the social situation of lone parents.

The founding fathers of the European project who prepared the Treaty of Rome optimistically assumed that growing cohesion both between and within countries could be reached by supranational economic cooperation; domestic social policies were to redistribute the fruits of economic progress, while remaining a national prerogative. This traditional division of labour is not fit for the current challenges. As a matter of fact, the EU has already had a considerable impact on the member states' social policies. Hence, we must now define what we expect from the EU in the domain of social policy.

“ TO CREATE A VIRTUOUS CIRCLE WHEREBY BOTH PAN-EUROPEAN COHESION AND NATIONAL COHESION ARE ENHANCED”

European social policy responses need national and regional contextualisation. Simultaneously, the European Union needs a sense of common purpose and a common policy framework in support of national and regional social policies. Its aim should be **to create a virtuous circle whereby both pan-European cohesion and national cohesion are enhanced**. Cohesion is about income and employment, but also about other dimensions of well-being. The European Union deserves a **Social Triple A**, if it actively supports both convergence towards higher aggregate levels of well-being across the member states and convergence towards more equality of individual well-being within the member states.

The EU should stimulate and support the member states to develop policy packages that pursue both aims simultaneously. Such ‘dual-use’ policy packages do exist: education offers a telling example. Upward convergence in the quality of our human capital is a key condition for long-term upward convergence in prosperity and well-being across the EU. Currently, the European Union is deeply affected by a human capital divide, both between and within the member states. The European Commission has developed a comprehensive agenda on education, training and skills. However, this educational agenda does not carry sufficient weight in the setting of budget priorities. Real public expenditure on education was lower in 2013 than before the crisis in 10 member states, including those that badly need to improve their education system.

Reducing background inequalities between families with children and investing in child care and education contribute both to national cohesion and to long-term EU-wide convergence. Obviously, creating greater access to success in education for all children is not just a question of money; it also requires reforms in the education system in many member states. In other words, a child-centred social investment strategy that addresses inequalities in opportunities serves a dual purpose. Governments pursuing such a strategy deserve encouragement and opportunities to learn from other EU governments, but also tangible support from the EU, notably when they are in budgetary dire straits. We need more ‘solidarity in reform’.

There is a growing awareness that we need to promote solidarity within the European Union; witness the recent Five Presidents’ Report on the future of the Eurozone and the refugee crisis. The promotion of solidarity requires mutual trust. Mutual trust is needed with regard to the quality of the social fabric in the member states. Mutual trust is also at stake in the social dumping debate. A crucial condition for European public opinion to accept labour mobility and migration is that they should fit into a regulated social order; they must not undermine that social order. Reconciling mobility and the four freedoms, on the one hand, with the internal cohesion of national welfare states and industrial relations, on the other hand, is a complex challenge, but it is not an insurmountable one. This ‘balancing act’ should figure high on the European agenda.

In short, the EU’s role in social policy can be summarised as follows. The EU should provide a framework that reconciles openness and mobility with domestic social cohesion; it should support national welfare states on a systemic level in some of their key functions; it should guide the substantive development of national welfare states by indicating general social standards and objectives, leaving ways and means to the member states.

Acknowledgements

The authors are grateful to Katharina Barie, Iain Begg, Timo J. Hämmäläinen, Timo Lindholm, Robert Niblett, Daniel Schraad-Tischler, Joscha Schwarzwälder and Karen Wilson for comments and discussions in the framework of the Social Aspects Working Group of the Vision Europe project. The authors remain responsible for the analysis and opinions expressed in this Policy paper.

TABLE OF CONTENTS

INTRODUCTION	4
1. A European approach to social inequalities: two perspectives on solidarity	5
2. Convergence, well-being and equality: how to define a ‘Social Triple A’ Europe?	7
3. Median incomes and relative income poverty	9
4. Income poverty, pensions and non-pension transfers	12
5. Work-poor and work-rich households in the EU and the changing nature of employment	16
6. The human capital divide	20
7. Health, health care and the environment	28
8. ‘Dual-use’ policy packages for convergence and cohesion and the role of the EU	30
9. Solidarity and mutual trust	32
10. Envoi	33
REFERENCES	34
ON THE SAME THEMES...	36

INTRODUCTION

This paper focuses on inequality within and between EU member states. It does not recapitulate all the functions of the welfare state. Welfare states not only organise redistribution from the better-off to the worse-off. They are also ‘piggy banks’, enabling citizens to insure themselves against social hardship and to spread their income more securely over their lifetime. And they have a social investment function, with the state investing in the nation’s human and social capital.¹ However, as we argue in this paper, tackling inequalities requires an adequate combination of the redistributive, the piggy bank and the social investment function.

“TACKLING INEQUALITIES REQUIRES AN ADEQUATE COMBINATION OF THE REDISTRIBUTIVE, THE PIGGY BANK AND THE SOCIAL INVESTMENT FUNCTION”

We will not repeat existing analyses on the extent and the causes of inequality, for which we refer the reader to an impressive set of publications by the OECD, the European Commission and academics. The yearly *Social Justice in the EU - Index Report*,² which quantifies a multidimensional approach to social justice and underscores the diversity of national contexts, should also be seen as an important complement to this paper. We focus, selectively, on observations and arguments which we consider particularly relevant for a true European perspective on social inequalities. For instance, the analytical part of the paper emphasises the need to integrate two perspectives: a perspective on inequalities within member states, and a perspective on inequalities between member states. There is no one-size-fits-all explanation for increasing inequalities across the EU. This has two implications. First, there is no silver bullet to tackle increasing inequalities; we need a set of complementary strategies and instruments. Second, member states share challenges and risks, but European policy responses need national and regional contextualisation. Simultaneously, the EU needs a sense of common purpose and a common policy framework in support of national and regional social policies.³ The policy question that informs this paper can be summarised as follows: *how can we create a virtuous circle whereby both pan-European cohesion and national cohesion are enhanced?*

The structure of the paper is as follows. In the first section, we argue that we need two perspectives on solidarity: a pan-European and a domestic perspective. In the second section, we sketch a framework that allows a definition of the Social Triple A notion launched by the President of the European Commission, and we briefly add some normative considerations. In the third section, we illustrate this framework with summary data on median incomes and income poverty. In sections four and five, we dig a little deeper into the data on income poverty and relate them to the pension challenge⁴ and to employment. In the sixth section, we add education and skills to our framework. In section seven, we signal data on other dimensions of well-being (health and the environment), without elaborating upon them. In section eight, we argue that policy packages should and can contribute both to positive convergence and stability across the EU and to increasing cohesion within the member states. In section nine, we elaborate upon solidarity, trust and the need to reconcile openness and domestic cohesion. In section ten, we provide a conclusion.

1. This is explained in the ‘chapeau paper’ for the Vision Europe Summit: Begg, Mushövel and Niblett (2015).

2. See Schraad-Tischler (2015).

3. The need for a common framework and a sense of common purpose is developed in Vandenbroucke and Vanhercke (2014) and Friends of Europe (2015).

4. The pension challenge is also discussed in the Vision Europe paper by Hüttl, Wilson and Wolff (2015).

1. A European approach to social inequalities: two perspectives on solidarity

Over the last few years, inequality has become a hot topic in public debates. Impressive analyses have been published by international organisations such as the OECD, by the European Commission and by academics.⁵ Our aim is not to repeat the existing analyses. Rather than simply recapitulating what has already been said elsewhere, we want to develop a truly *European* approach to the problem of social inequality.

“ THE SIMULTANEOUS PURSUIT OF ECONOMIC PROGRESS, SOCIAL PROGRESS AND COHESION, BOTH WITHIN COUNTRIES AND BETWEEN COUNTRIES ”

A European approach implies that we go beyond a purely national perspective on inequality, in which only inequalities among people living in the same country are deemed relevant. Given the increasing role of migration and mobility, entertaining a purely ‘domestic’ view on social justice is increasingly anachronistic in today’s Europe. A purely national perspective also ignores the fundamental goals that have been part and parcel of the European project since the Treaty of Rome of 1957: the simultaneous pursuit of *economic progress*, on the one hand, and of *social progress and cohesion*, on the other hand, both *within* countries (through the gradual development of welfare states) and *between* countries (through upward convergence across the Union). We believe that it is necessary not only to reconnect with this old ambition, but also to reconsider the role national welfare states and the EU have to play in realising this ambition.

The founding fathers of the European project who prepared the Treaty of Rome optimistically assumed that growing cohesion both between and within countries could be reached by supranational economic cooperation, together with some specific instruments for raising the standard of living across the member states (which were later brought together in the EU’s ‘economic, social and territorial’ cohesion policy). Economic integration was to be organised at the EU level, and would boost economic growth and create upward convergence; domestic social policies were to redistribute the fruits of economic progress, while remaining a national prerogative. The specific social dimension of the EU would, in essence, be confined to the coordination of social security rights for mobile citizens and to the gradual development of an (impressive) body of anti-discrimination legislation. Admittedly, after 60 years of piecemeal developments, the European *social acquis* encompasses other important policy areas that were shifted from the national to the EU level, such as health and safety standards at work. But redistributive policies, education policies and the development of social security remained – at least in theory – firmly anchored at the national level.

With hindsight (and in a slightly benign interpretation), one may say that the founding fathers of the European project created two perspectives on *solidarity*: a pan-European perspective and a national perspective. How would we understand this dual perspective?

The founding fathers wanted upward economic convergence and cohesion on a European scale. They also wanted to give individual Europeans the right to improve their own lives by working in a member state other than the one of which they are nationals, with no discrimination on the basis of nationality. Gradually, patients acquired the right to benefit, under certain conditions, from medical care in other member states than their state of residence. Is the word ‘solidarity’ an adequate description of the founders’ purpose? Their approach was not ‘redistributive’, nor was it about the mutual insurance of risks; historically, it was mainly about *fair access to opportunities*: trade and investment opportunities for countries joining the EU and personal opportunities for all their citizens wanting or needing to be mobile. One might also say that, in pursuing cohesion, it was motivated by *inclusion* on a pan-European scale. However, recent developments – those associated with monetary unification (the need for stabilisation), on the one hand, and international migration, on the other

5. See for instance OECD (2008), OECD (2011), OECD (2015), European Commission (2015) and the Commission’s reports on Employment and Social Development ESDE (2012), ESDE (2014), ESDE (2015), Council of Europe (2013), Salverda et al. (2014), Oxfam (2015) and Atkinson (2015).

hand (the refugee crisis) – are forcing upon the Union a classic notion of solidarity in coping with *shared risks*. A polity that initially emerged as an ‘opportunity structure’, motivated by the aspiration of growing cohesion, is in need of mutual insurance and true solidarity.

Solidarity within national welfare states is well-known territory. It refers to social insurance, income redistribution and the balance of social rights and obligations. As already indicated, the founding fathers did not believe that integration would diminish the potential for national solidarity, so conceived. On the contrary, they were confident that welfare state actors and institutions would redistribute the produce of economic integration, i.e. more economic growth, fairly within the member states, in tune with social preferences in each state.

We propose considering this dual perspective on solidarity, national and pan-European, which is the logical consequence of developments that started more than 60 years ago, as a defining normative feature of ‘the European social model’. The European social model is not simply a summary description of a set of co-existing national social models; it also describes the way these national welfare states interact with each other - or are supposed to interact with each other - in Europe.

This dual perspective on solidarity is inherently complex and multifaceted. Consecutive enlargements as well as monetary unification made this notion of solidarity even more complex and demanding. Indeed, what is seen by some as ‘the dynamics of upward convergence’ associated with the enlargement of the EU is seen as social dumping by others. At the same time, monetary unification necessitates forms of solidarity which have been, so far, a no-go area in European politics, such as a Eurozone stabilisation capacity and fiscal transfers.

“ WITHIN MANY OF OUR COUNTRIES, WE ARE WITNESSING INCREASING SOCIAL INEQUALITIES AND CONCOMITANT SOCIAL DISTRUST ”

Factual developments and distrust now threaten to erode the basis of solidarity itself, both national and pan-European. Within many of our countries, we are witnessing increasing social inequalities and concomitant social distrust. Between countries, the Eurozone has displayed the exact opposite of convergence: increasing divergence, which saps the legitimacy of the European project. We risk being caught in a trap: we badly need more European solidarity at a time when it is becoming more difficult to achieve. We are at risk of experiencing a vicious rather than a virtuous cycle. *How can we create a virtuous circle whereby both pan-European cohesion and national cohesion*

are enhanced? That is the main focus of this contribution to the *Vision Europe Summit*.

2. Convergence, well-being and equality: how to define a ‘Social Triple A’ Europe?

Suppose, for the sake of simplicity, that we focus only on incomes when assessing social inequalities in Europe. The inspiration of the European project’s founding fathers, as described in Section 1, could then be summarised as follows: our aim is the *simultaneous pursuit of convergence towards higher levels of national median income across the member states and convergence towards less relative income poverty within the member states*.⁶

Admittedly, prosperity and well-being are about much more than income; and relative income poverty is only one indicator in a diverse set of well-known inequality indicators. Broadening the scope of our assessment beyond income indicators (let alone, GDP) is an important challenge, if we want to revamp the notion of a European social model. In Sections 3 to 5, we will start with an analysis of income data, but in the following sections we will move on to other parameters, such as education, skills, health and the environment in which people live. The benchmark for assessing the success of the European social model should be framed in terms of the aggregate levels of well-being member states can achieve (measured at the member state level) and inequalities in well-being within the member states.⁷

The President of the European Commission launched the idea that the EU should be characterised by a *Social Triple A*.⁸ So far, this notion has not been defined. **We propose the following framework: the Union deserves a Social Triple A if it actively supports upward convergence in relevant dimensions of well-being across the member states, and convergence towards less inequalities in those same dimensions of well-being within the member states.** Obviously, this is a framework to conceptualise a *Social Triple A* Europe, rather than a precise definition. It raises questions which we cannot discuss in this paper for reasons of space, but which need careful thought. We briefly indicate them in the remainder of this section.

As much as there is an important debate taking place today on the way in which one should move ‘beyond GDP’ and measure well-being,⁹ there is also a long-standing debate on the notion of equality which asks the question: are we in favour of ‘equality of opportunity’ or ‘equality of outcome’? Philosophical proponents of equality of opportunity argue that one should make a distinction between circumstances for which we cannot hold people responsible (for instance, their family background, innate talents) and choices for which we can hold them responsible (for instance, the effort with which they valorise their talents). The philosophical case for equality of opportunity, as understood by authors such as Roemer and Trannoy (2013), is robust; it is not a superficial meritocratic approach, which is not to say that it is uncontroversial.

Roemer and Trannoy (2013) also argue that there is an important and relevant divide between European countries with regard to equality of opportunity, which is not captured well by the usual statistics on outcome inequalities. For instance, there is stark contrast between equality of opportunity in Denmark and in Hungary; the impact of the family’s educational background on an individual’s later earnings is much larger in Hungary than in Denmark.¹⁰ Moreover, it seems easier to build a broad consensus on equality of opportunities – understood as meaning that all should have the same life chances, regardless of their initial conditions – than on equality of outcomes. Also, the turn to activation and activating social investment in social policy over the last

6. Space forbids elaborating on this ‘dual’ normative benchmark and relating it to a broader philosophical debate on international distributive justice. An alternative normative approach would be to start from pan-European indicators that directly (and only) apply to individual European citizens; from a philosophical perspective, a case can be made for a single pan-European income poverty objective based on a single, pan-European poverty threshold. The dual benchmark which we formulate here could then be interpreted as a pragmatic approach to a more fundamental pan-European objective of this nature.

7. This formulation is a starting point and would need further elaboration. It leaves open how one should aggregate well-being at the member state level, and whether or not cross-country differences in preferences are taken into account. One should note that it is possible to take into account the distribution of well-being in the aggregation, for instance, by giving more weight to those who are worst off. The second prong of the benchmark also presupposes a consensus on how one should weight individuals (in the assessment of internal inequality) and on the treatment of differences in individual preferences. Whether or not the two dimensions of the benchmark can be reduced to one dimension is a question which we will not develop here.

8. Speech by President Jean-Claude Juncker to the European Parliament upon his election: “I want Europe to be dedicated to being triple-A on social issues, as much as it is to being triple A in the financial and economic sense”, Strasbourg, 22 October 2014.

9. See Stiglitz, Sen and Fitoussi (2009), Fleurbaey and Blanchet (2013), the OECD *Better Life Initiative*; Hellström et al. (2015), Hämäläinen (2014).

10. See Roemer and Trannoy (2013) for details.

“THE EUROPEAN SOCIAL MODEL SHOULD BE BOTH ABOUT REAL EQUALITY OF OPPORTUNITY AND EQUALITY OF OUTCOMES”

20 years is linked to a normative recalibration, in which the emphasis is on life chances rather than outcomes ‘here and now’ (Hemerijck, 2014). Finally, as argued in Section 1, historically the pan-European ‘social space’ was conceived of as an opportunity structure for mobile people; it was not about the redistribution of outcomes. All this means that *real* equality of opportunity has a lot of traction, if we set out normative benchmarks for the European social model: equality of opportunity cannot easily be dismissed as a notion that is ‘in retreat’ vis-à-vis a traditional European understanding of social equality. However, both the OECD (2015) and Atkinson (2015) argue that the distinction between opportunities and outcomes is not straightforward. *“Higher inequality of incomes of parents tends to imply higher inequality of life chances of their children. To achieve greater equality of opportunities without tackling increasing inequalities in outcomes will be very difficult.”*¹¹ With a simple algebraic decomposition, Lefranc, Pistoletti and Trannoy (2007) show that changes in ‘inequality of income opportunity’ can be understood as the product of changes in the intergenerational elasticity of income (which capture the transmission of inequalities from parents to children), on the one hand, and changes in parental income inequality, on the other hand. This raises important normative questions which we cannot settle here, but the practical conclusion, so it seems, is that the European social model should be *both about real equality of opportunity and equality of outcomes*.

A next question relates to the potential tension between the legitimate diversity of welfare states across the EU – legitimate, as it corresponds to different national histories and different national preferences – and the aspiration of convergence which we see as part and parcel of the European project. The convergence we argue for is about outcomes and opportunities. It is – in principle – not about the ways and means to achieve those outcomes and opportunities: subsidiarity remains an important principle. However, there is a limit to the institutional diversity that can be accommodated in the EU if convergence is our aim (Vandenbroucke, 2015a, b).

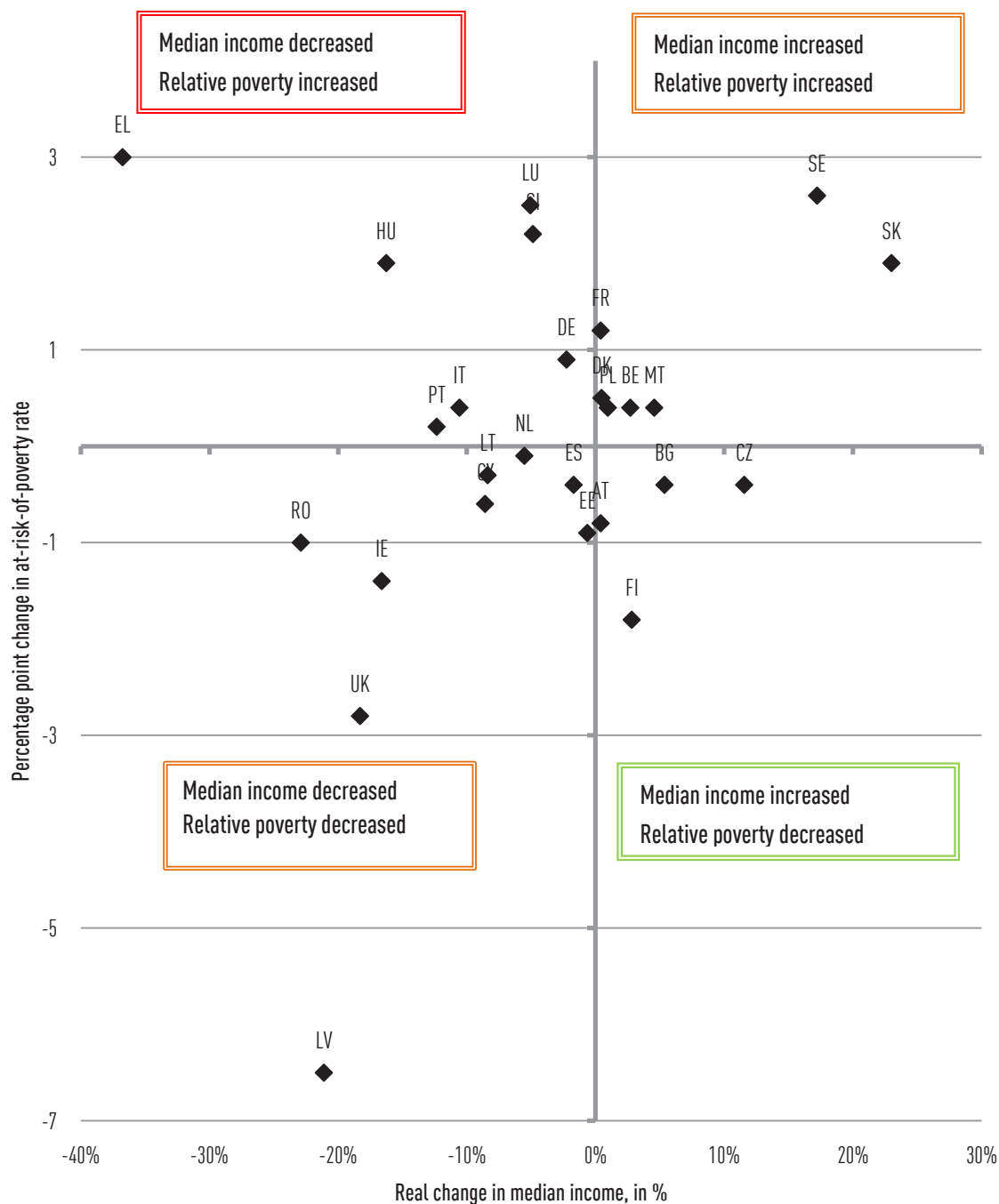
A further difficult question concerns democratic accountability. Traditionally, national governments in nation-states could be seen as accountable for the performance of their welfare states and the well-being of their citizens. Today, the location of democratic accountability is less straightforward: in many European countries, regions (or local municipalities) have taken over important responsibilities, with a huge impact on the well-being of individuals and the performance of the welfare state at large. In a country like Belgium, for instance, accountability for the performance of the welfare state cannot be attributed in a one-sided way to either the federal government or the regional governments: all of them share in that responsibility. The ‘active support’ role which we propose for the EU adds to that complexity: on the one hand, one cannot hold the Union responsible for everything that goes wrong in member states in social terms; on the other hand, if a *Social Triple A* is a stated ambition of the Union, it cannot hide from its responsibility for the eventual outcomes. Shared responsibilities make democratic accountability complex. But there is no return to the ‘good old days’ of national sovereignty and the concomitant, simple understanding of democratic accountability.

11. OECD (2015), p. 27.

3. Median incomes and relative income poverty

Would we award today's EU a *Social Triple A*? In answering that question, we first focus on the most traditional 'outcome' yardstick: monetary incomes. In Figure 1, we combine changes in the member states' median income with changes in the income distribution within the member states.

Figure 1 ► Change in Real Median Income and Percentage Point Change in Poverty (with floating threshold), SILC 2008 – SILC 2013



Source: EUROSTAT, EU-SILC [ilc_di03] and [ilc_li02], authors' calculations.

“ SINCE THE OUTBREAK OF THE CRISIS, WE HAVE BEEN FAR REMOVED FROM A SOCIAL TRIPLE A SCENARIO”

On the horizontal axis of Figure 1, we show the growth rate (or reduction) of real median income between 2007 and 2012;¹² on the vertical axis, one finds the percentage point change in the conventional at-risk-of-poverty rate between 2007 and 2012. The poverty rate measures the share of people living below the national poverty threshold; we apply a floating poverty threshold (60% of the 2007 median incomes to measure poverty in 2007; 60% of median incomes in 2012 to measure poverty in 2012). Hence, the north-eastern quadrant of the graph shows countries in which median incomes increased in real terms, but the income distribution deteriorated at the bottom end, e.g. Sweden and Slovakia. The south-western quadrant shows countries in which median incomes decreased in real terms, but the relative income distribution improved at the bottom end, as is the case with the UK, Ireland and Romania. Greece, in the north-western quadrant, experienced both a drastic reduction in median incomes and a worsening income distribution. Very few countries are in the south-eastern quadrant where median incomes increased in real terms and relative poverty decreased. Obviously, the pattern shown in Figure 1 reflects the crisis, notably within the Eurozone; if we were to look at a longer time span, for instance starting in 2004, the picture with regard to the growth of median incomes would be more favourable for a number of countries. However, since the outbreak of the crisis, we have been far removed from a *Social Triple A* scenario.

We now zoom in on a single indicator which captures the growth in incomes and the distribution of incomes; that is, we examine, both for 2007 and 2012, the share of individuals living in a household in which household income is lower than 60% of the median household income in 2007.¹³ For 2007, this is simply the conventional at-risk-of-poverty rate. Applied to 2012, this indicator is called the ‘at-risk-of-poverty rate anchored in time’, because the poverty threshold is kept constant at its 2007 level, adjusted for inflation. The at-risk-of-poverty rate anchored in time reflects the combined impact of income growth and changes in the distribution of incomes. If all incomes decrease (increase) at the same rate, and the relative distribution of income remains unchanged, the at-risk-of-poverty rate anchored in time increases (decreases): in 2012, more (less) people will have an income below (above) the poverty threshold of 2007. If median incomes remain unchanged, but the income distribution worsens (improves) at the bottom end, the at-risk-of-poverty rate anchored in time increases (decreases). In practice we see a mixture of these scenarios. Figure 2 compares the conventional at-risk-of-poverty rates in 2007 with the anchored poverty rates for 2012. Countries are ranked from left to right by their 2007 poverty rates.

The at-risk-of-poverty rate anchored in time increased in the majority of EU countries between 2007 and 2012¹⁴, with dramatic increases in Greece (from a poverty rate of 20.1% in 2007 to a poverty rate, anchored in 2007, of 44.3% in 2012), Ireland (an increase of 9.9 percentage points), Cyprus, Latvia and Italy. It also increased in countries which we consider successful such as Germany (an increase of 1.6%). It decreased significantly in Poland and more moderately in Slovakia, Romania, Bulgaria, Sweden, Finland, Belgium and Austria.

The pattern shown in Figure 2 is one of dramatic divergence, driven mainly by what happened in the Eurozone.¹⁵ Notwithstanding some important exceptions (notably Poland, but also Slovakia), the much heralded European ‘convergence machine’ of the past stopped working.

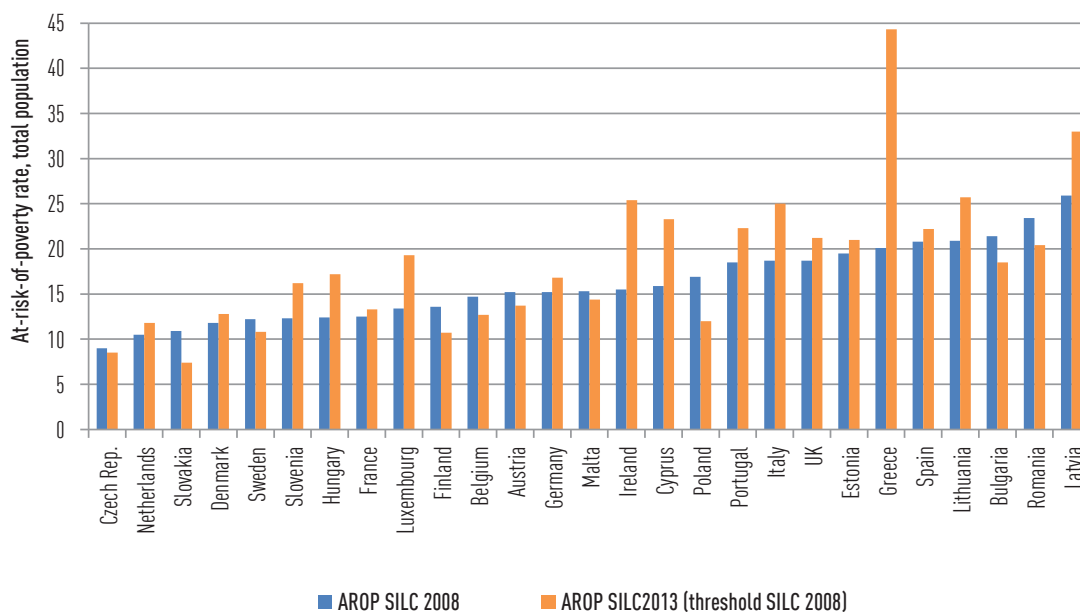
12. We use ‘median income’ as a short cut for ‘net disposable equivalised household income’, as registered in EU-SILC. This indicator pertains to individuals and takes into account taxes and transfers and the size and composition of the household in which the individual lives. Incomes perceived in 2007 are registered in EU-SILC 2008 and incomes perceived in 2012 are registered in EU-SILC 2013 (except for the UK and IE: for these countries we compare incomes perceived in 2008 and incomes perceived in 2013). Increases in nominal incomes are corrected for inflation.

13. The median income is adjusted for inflation between 2007 and 2012. We use EU-SILC 2008 and 2013 for this comparison; for the UK and IE we compare 2008 and 2013, for the other countries 2007 and 2012.

14. As mentioned, with the exception of Ireland and the UK, EU-SILC 2008 and 2013 refer to incomes in 2007 and 2012.

15. If we were to analyse the non-Eurozone countries alone, we might discern a minor tendency towards convergence in that small subset of countries.

Figure 2 ▶ At-Risk-of-Poverty Rate Anchored in Time, EU-SILC 2008-2013¹



Source: EUROSTAT, EU-SILC [ilc_li22b] and [ilc_li02].

1. At-risk-of-poverty rate (AROP) is the share of individuals living in households in which net disposable equivalised household income is lower than 60% of the median net disposable equivalised household income. AROP SILC 2013 (threshold SILC 2008) are the poverty rates 'anchored in time'. Data refer to total population.

A corollary of the observations shown in Figure 2 is that severe material deprivation,¹⁶ a standard 'absolute' measure of poverty, decreased in Poland, Slovakia and Sweden (it was already very low in the latter country), whilst it increased significantly in Ireland and the UK and dramatically in Greece. In the EU15 taken as a whole, severe material deprivation was larger in 2012 than in 2007, a regressive development probably never seen in the history of the European project;¹⁷ in the new member states, severe material deprivation decreased from its initially high level, as the impact of economic growth (notably in Poland) dominated adverse evolutions in the relative income distribution in some new member states. On balance, in the EU27 taken as a whole, severe material deprivation was marginally higher in 2012 than in 2007. Hüttel, Wilson and Wolff (2015) provide data on the intergenerational divide with regard the evolution of material deprivation.

Severe material deprivation, poverty rates anchored in time and poverty rates with floating thresholds give conflicting signals about what happens in our societies. Therefore, we should take them all into consideration. The time perspective is important here. In the short and medium term, material deprivation and anchored poverty provide the best indication of the social stress societies experience. In the longer term, anchored poverty becomes an anachronistic indicator in growing economies, as more and more people will acquire incomes above the anchored poverty threshold. In the very long term, material deprivation, as we measure it, becomes a yardstick of the economic and technological development of societies, rather than a yardstick of social justice in societies.¹⁸

Therefore, relative inequality indicators, such as poverty rates with floating thresholds, GINI-coefficients or quintile shares are indispensable for assessing the evolution of social justice in our societies, notably in the medium and longer term. In the next section, we focus on the development of poverty using a floating poverty threshold, i.e. we focus on the relative position of people at the bottom end of the income distribution.

16. Severe material deprivation refers to a state of economic strain defined as the enforced inability to pay for at least four of the following nine items: i) rent, mortgage or utility bills; ii) adequate home heating; iii) unexpected expenses; iv) meat or proteins or regular meals; v) a holiday; vi) a television; vii) a washing machine; viii) a car; ix) a telephone.

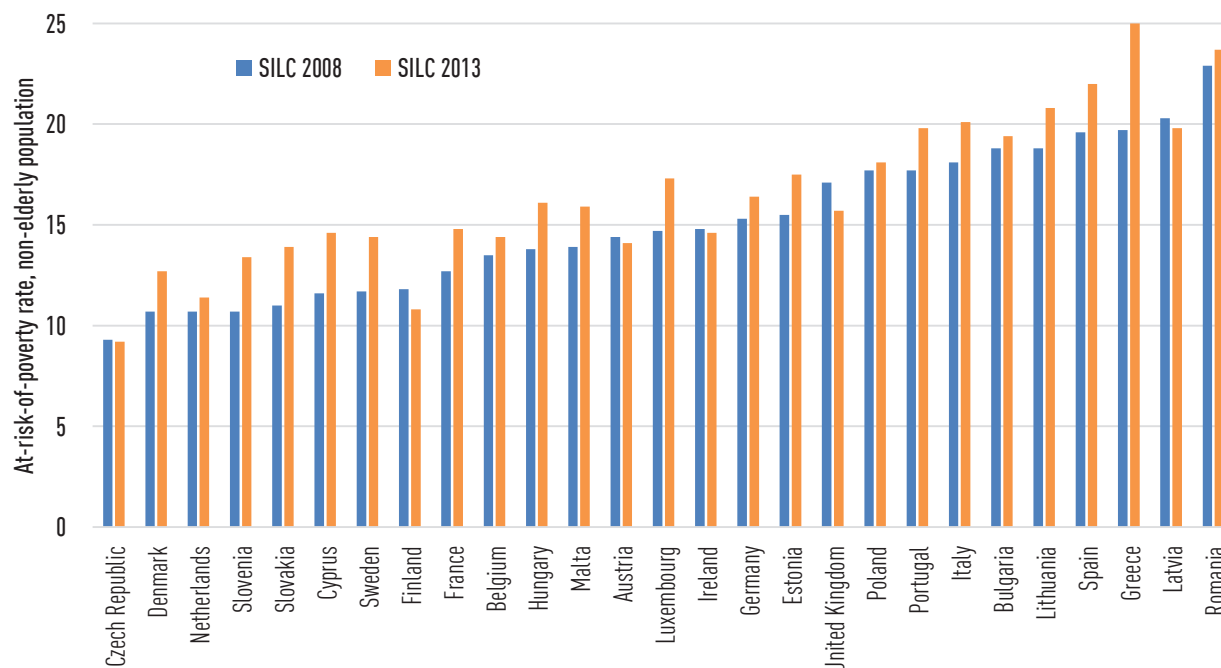
17. This statement can only be intuitive, since we do not have comparable statistics for the past; moreover, the EU of the 1980s was not the EU of the 2000s. However, it seems implausible that such large scale, simultaneous increases in material deprivation happened before in countries constituting the European Communities or, later, the EU.

18. This sentence should be understood with respect to indicators of material deprivation that remain unchanged.

4. Income poverty, pensions and non-pension transfers

The poverty rates in Figures 1 and 2 concern the whole population. In Figure 3 instead, we show conventional at-risk-of-poverty rates for the non-elderly, i.e. people younger than 65 in 2007 and 2012, using a floating poverty threshold.

Figure 3 ▶ At-Risk-of-Poverty Rates, with floating threshold, SILC 2008 – SILC 2013, non-elderly population¹



Source: EUROSTAT, EU-SILC [ilc_li02].

1. At-risk-of-poverty with floating threshold set at 60% of median net disposable equivalised household income. Data for population below 65 years old.

Figure 3 reveals that most countries experienced an increase in poverty in the non-elderly population (on average, we see an upward shift), whilst the picture for poverty in the total population is more mixed. For the non-elderly, at-risk-of-poverty increased in as much as 18 member states, it remained relatively steady in 7 member states, whilst it only decreased significantly in Finland and the UK. The picture for poverty in the total population is more mixed because elderly poverty diminished significantly in a number of countries. Over the years 2004-2006, on average, elderly poverty in the EU15 was about 4 percentage points higher than non-elderly poverty; by 2012, the situation had changed completely: non-elderly poverty was 3.3 percentage points higher than elderly poverty. In the new member states, the initial situation was different: elderly poverty was lower than non-elderly poverty in 2004-2006; the gap between poverty rates of the non-elderly population and the elderly population narrowed, but then increased again after the crisis so that, today, it is even higher than in 2004-2006.¹⁹

The explanation of this remarkable reversal in the relative poverty risks of the elderly and the non-elderly include both long-term sociological trends (such as the rise in dual earnings and the increasing numbers of female pensioners with a substantial employment record, which steadily reduced poverty in the elderly population) and the short-term impact of the economic crisis. From the point of view of individuals, pensions provide a much more robust 'automatic stabiliser' in times of economic crisis than unemployment insurance. Pension

19. In this paragraph, 'elderly' refers to individuals aged 65 or more; the 'non-elderly' are individuals below the age of 65. The average over the years 2004-2006 is a weighted average of the data registered in EU-SILC 2005-2007.

incomes were relatively well protected during the crisis; unemployment insurance, in contrast, is patchy in a number of countries, notably in countries that were hard hit by the crisis, like Italy and Spain. Moreover, in the context of austerity policies, some countries had to switch off their automatic stabilisers (too) rapidly, and were forced to take measures that may have affected pension incomes less than other incomes.²⁰ As a matter of fact, from a short-term Keynesian point of view, the relative stability of pension incomes was not necessarily bad; the problem was, rather, the limited stabilisation impact of working age benefits in a number of countries (Dolls et al., 2012). Economically, pension spending acted as a short-term buffer, albeit not a very efficient one. But also from a social point of view, there is a tension between the long-term need to reduce the structural ‘pension heaviness’ of some welfare states (such as Greece), on the one hand, and the short-term observation that children are to a significant degree protected against poverty by pension incomes in those welfare states, due to the extended family model (Diris, Vandenbroucke and Verbist, 2014). Hence, the transition from a pension-heavy welfare state to a welfare state that provides adequate protection for working-age families and children needs careful consideration: in countries like Greece, governments have to build a new welfare state, with new and adequate transfer systems for working-age families and children, whilst reducing the pension overload of the old welfare state.

“ PENSION REFORM SHOULD BE BASED ON A NOTION OF INTERGENERATIONAL FAIRNESS ”

In the long term, pension reform should be based on a notion of intergenerational fairness, as embodied in the so-called Musgrave rule. Simplified,²¹ this means that the pension benefit ratio (the ratio of average pension incomes on average incomes in the active population) should be stabilised on a target value. In other words, it means that pension systems should be guided by²² a principle of ‘defined ambition’ with regard to the income distribution between pensioners and non-pensioners (in contrast to principles of ‘defined contribution’ or ‘defined benefit’, which put the burden of adjustment in periods of demographic change unilaterally

on future pensioners or the future active population). Such a principle of ‘defined ambition’ is absent from pension reform in most of the EU member states. In some countries, pension benefit ratios are set to decline considerably in the long term, which means that today’s young people will enjoy pension systems of lesser quality than today’s pensioners; this is documented in Hüttl, Wilson and Wolff (2015). On the basis of realistic hypotheses about future developments, ‘defined ambition’, so conceived, is only attainable if working careers become longer.²³ We briefly return to this challenge in the next section.

We now turn our attention to the evolution of non-pension transfers (or ‘transfers’, as a short cut). Figure 4 shows the evolution of an indicator which is commonly called ‘poverty reduction by transfers’: it is equal to the difference between a ‘post-transfer poverty rate’ and a ‘pre-transfer poverty rate’. The post-transfer poverty rate is simply the at-risk-of-poverty rate one can observe in reality; the pre-transfer poverty rate is a theoretical counterfactual, based on a manipulation of the data in which non-pension transfers are eliminated from the household incomes registered in the survey. This theoretical counterfactual should be interpreted cautiously (Vandenbroucke, Diris and Verbist, 2013); rather than showing the level of poverty that would obtain if there were no transfers, it indicates in a mechanical way the ‘amount of work done’ by non-pension transfers to reduce poverty. However, bringing together levels and changes over time in this indicator, as we do in Figure 4, illustrates much of the predicament of European welfare states.

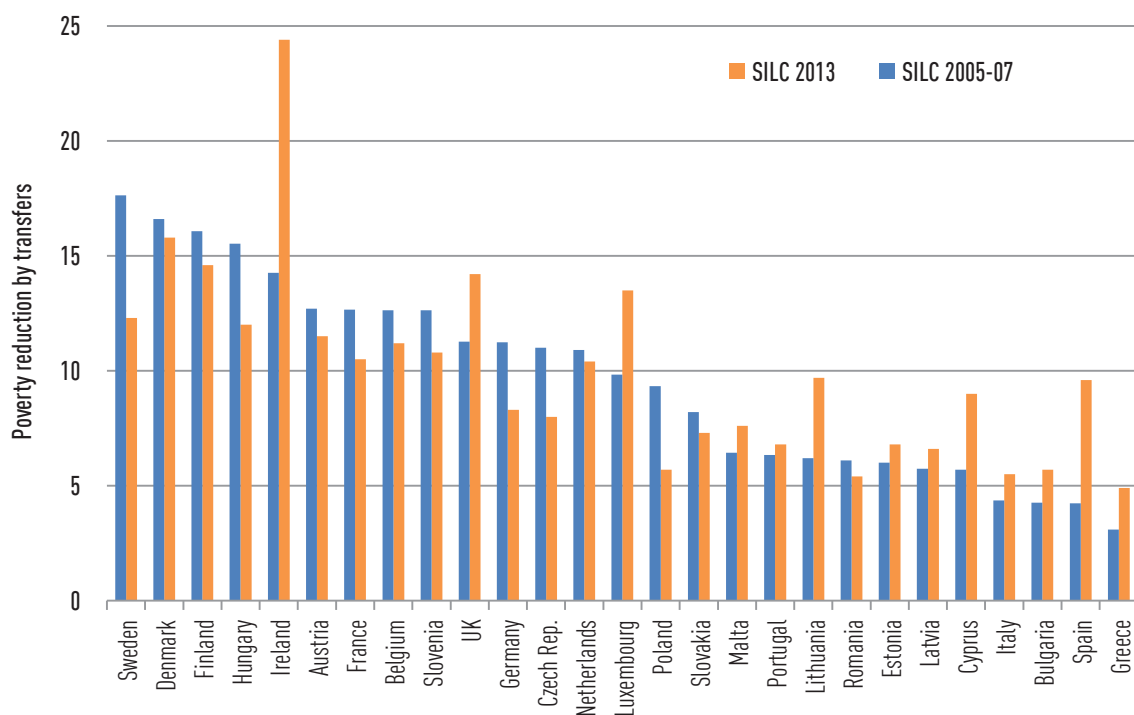
20. Our reading of what happened is also influenced by the statistics we use to measure poverty. These indicators only take income into account; they are not affected by increases in indirect taxes, increases in tariffs for services, etc.

21. The translation of the Musgrave rule into a stable pension benefit ratio is a simplification for different reasons. It does not take into account structural (sociodemographic) changes in the population of pensioners, which may justify changes in the pension benefit ratio. Also, the Musgrave rule does not, in itself, determine the selection of a pension policy; normative judgements on the optimal ‘leisure-consumption trade-off’ and the desirable degree of consumption smoothing also inform the selection of a pension policy. The Belgian Commission on Pension Reform 2020-2040 has proposed a thorough pension reform for Belgium, based on the Musgrave rule. The Annex 1.4 of the Commission’s report presents a formal algebraic presentation and a translation of such a principle into a ‘point system’; see www.pensioen2040.belgie.be (Dutch) or www.pension2040.belgique.be (French).

22. The expression ‘guided by’ is deliberately vague. A case can be made for adjustment mechanisms that are built into pension systems to keep them ‘on course’ (towards the defined ambition), whatever the structural demographic and economic changes societies experience.

23. This condition is necessary, but maybe not sufficient. Additional financing which does not rely on earned income may be necessary; cf. Annex 1.4. to the Belgian Commission on Pension Reform.

Figure 4 ► Poverty Reduction by Non-Pension Transfers: SILC 2013 compared to SILC 2005-2006-2007¹



Source: EUROSTAT, EU-SILC [ilc_li02] and [ilc_li10], authors' calculations.

1. Poverty reduction is the difference between the at-risk-of-poverty rate and the at-risk-of-poverty rate before transfers (pensions excluded from transfers). For the start of the period (left bars), we provide the average value of the data registered in SILC 2005, SILC 2006 and SILC 2007.

We compare the value of 'poverty reduction by transfers' over the years 2004-2006 with the value of 'poverty reduction by transfers' in 2012.²⁴ Over this period, the *average* value of poverty reduction by transfers across the EU member states was stable; the pattern shown in Figure 4 is one of convergence, which is neither upward nor downward. Where poverty reduction by transfers was higher than average, it diminished (except for Ireland, the UK and Luxemburg); where it was lower than average, it increased (except for Poland, Slovakia and Romania).

One should note that a high level of poverty reduction by transfers is not *per se* 'good': a high level of employment with fair access to decent jobs and a low level of poverty reduction by transfers may be preferable and generate *less* post-transfer poverty, than the opposite situation of high unemployment, leading to a high level of pre-transfer poverty and large-scale transfers. If pre-transfer poverty diminishes because employment increases, a decreasing 'poverty reduction by transfers' is not necessarily an indication of a reduced capacity to fight poverty (Vandenbroucke and Diris, 2014). When both post-transfer poverty and poverty reduction by transfers decrease simultaneously, we may be witnessing a normal, 'endogenous' adjustment mechanism of a well-functioning welfare state where employment is increasing and/or pre-transfer (market) income inequality diminishes. However, that benign scenario is not what happened in a number of countries. In Belgium, France, Austria, Germany, Sweden, Slovakia, Denmark and Slovenia post-transfer poverty increased among the non-elderly population whilst poverty reduction by non-pension transfers diminished. This parallel development signals a worrying reduction in the redistributive capacity of those welfare states. In Section 5 we elaborate upon this observation, but first we return to the general pattern shown in Figure 4.

Before the crisis, poverty reduction by transfers was, on average, relatively high in Western and Northern European countries (Sweden, Denmark, Finland, Austria, Belgium, for instance), as well as in Anglo-Saxon

24. We take the average value EU-SILC 2005-2007 (which correspond to 2004-2006), rather than 2007 as in the previous graphs, because we want to show a somewhat longer period. Given the fact that for some countries the EU-SILC results for those years yield changes in indicators that are hard to explain (next to instability in the survey itself) and that for some countries EU-SILC only starts in 2006 or 2007, we use average values for the beginning of the period. As mentioned earlier, for the UK and Ireland, the EU-SILC years correspond to the years in which the incomes were perceived.

Europe (Ireland and the UK); it was very low in the Southern Eurozone countries (Greece, Italy, Spain, Cyprus, Portugal), which are pension-heavy and have patchy benefit systems for working-age families and children. With regard to poverty reduction by non-pension transfers, the new member states were and remain very heterogeneous; on average, their position is between the EU West and North cluster and the Southern Eurozone countries. During the crisis, poverty reduction increased in the Southern Eurozone countries, but not very much (except for Spain, where the increase was considerable); the ‘automatic stabilisation’ effect one should expect from transfers in such a deep crisis remained limited. In Poland, poverty reduction by transfers was less at the end of the period, but so was post-transfer poverty among the non-elderly; this particular trajectory is explained by a considerable increase in employment.

“ WELFARE STATE
CAN BE A COMPETITIVE
ASSET WHEN IT
COMES TO ECONOMIC
COMPETITIVENESS”

Prima facie, the converging pattern shown in Figure 4 is congenial to an observation by Bénassy-Quéré, Trannoy and Wolff (2014) over a much longer time span (1985-2010), encompassing both taxes and transfers, but focusing on a more limited number of countries. They conclude that the tax and transfer system has not become less redistributive, but that there seems to be “a convergence amongst EU Member states on the extent of redistribution” during this long period.²⁵ This prompts a discomfiting question: are we witnessing the irresistible impact of globalisation and/or European integration, which forces mature welfare states to cut back on transfer systems? Atkinson

(2015) convincingly argues, on the basis of much academic research, that globalisation does not force nations to cut back their welfare states. **As a matter of fact, a number of mature welfare states with a high level of social spending rank high in the World competitiveness index. The welfare state is not *per se* the problem, when it comes to economic competitiveness; on the contrary: if it is well-organised it can be a competitive asset** (Vandenbroucke and Vanhercke, 2014).

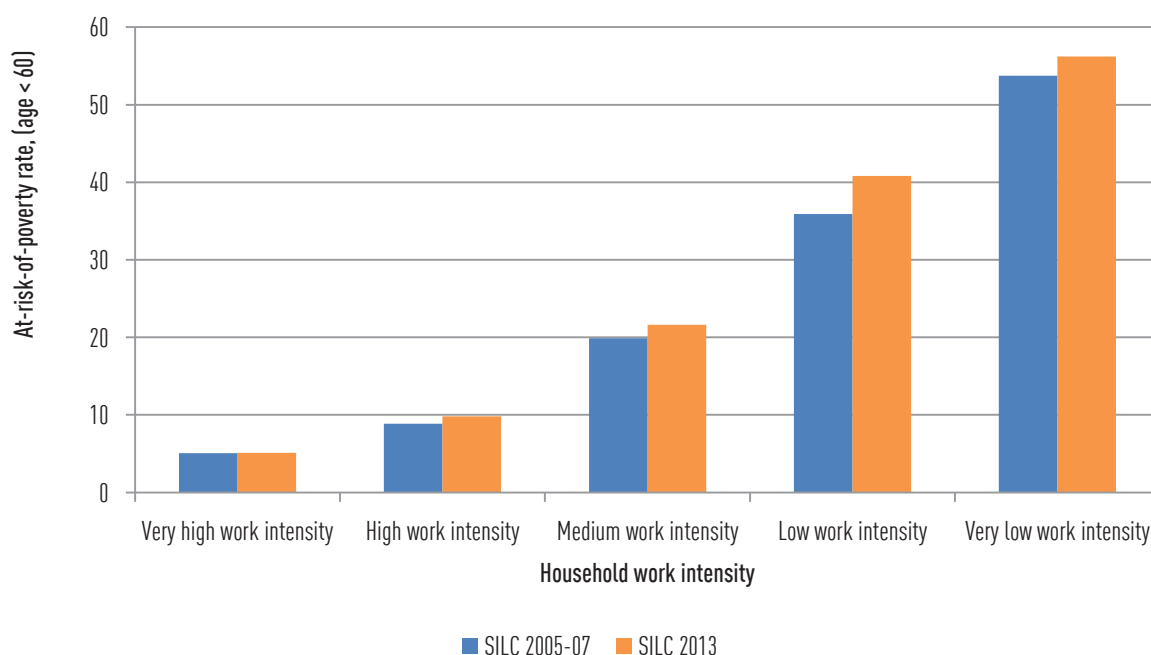
With relatively high levels of social spending, countries like Sweden, the Netherlands and Denmark achieve high employment rates, a good score in the competitiveness index and relatively low levels of poverty (although poverty is now increasing in the Nordic countries); in contrast, a country like Italy, which has more or less the same level of social spending, performs worse on all these counts. In order to understand these cross-country differences, we should broaden our examination of welfare states beyond transfer systems. The strong historic record of Northern welfare states with regard to employment, poverty and competitiveness has been linked to their long-term orientation towards *social investment*, i.e. activation, investment in human capital, and capacitating social services such as child care (Hemerijck, 2014). Obviously, investment in education and child care are no panacea; welfare states also differ with regard to the effectiveness of their social protection systems, as already indicated on the basis of Figure 4; moreover, the impact of social protection seems to change over time. Welfare state performance depends on the complementarity of effective investment in human capital – by means of education, training and child care – and effective protection of human capital – by means of adequate transfer systems and health care. The redistributive role of social protection remains important *per se* (Cantillon and Vandenbroucke, 2014). We dig a little deeper into recent evolutions in the redistributive role of social protection in the next section (Section 5), and focus on human capital in Section 6.

25. Bénassy-Quéré, Trannoy and Wolff (2014) state that “the system has become less redistributive in Nordic countries but more so in Italy. In France and Germany, the tax-and transfer system seems to have delivered similar amount of redistribution along the period”, p. 8. In contrast, the OECD finds that tax and benefit systems have become less redistributive in the countries they examine.

5. Work-poor and work-rich households in the EU and the changing nature of employment

We measure individual incomes and poverty on a household basis. A crucial determinant of the poverty risk of individuals is the labour market participation of the members of the household in which the individual lives. We measure this by an indicator called 'household work intensity'. On this basis we can distinguish five sub-groups of households: households with a very high, high, medium, low, and very low work intensity.²⁶ The lower the work intensity, the higher the poverty risk for the individuals in the household. Figure 5 illustrates this, with average observations for the EU27.

Figure 5 ► Poverty Risks by Work Intensity of Households for EU-27, SILC 2013 – SILC 2005-2006-2007¹



Source: EUROSTAT, EU-SILC [ilc_li06], authors' calculations.

Note: The at-risk-of-poverty rate is the weighted average for the EU-27, with cut-off point set at 60% of median net disposable equivalised income. We compare data registered in EU-SILC 2013 with the average value of the data registered in SILC 2005, SILC 2006 and SILC 2007.

In Figure 5, we show the poverty risk by work intensity of the household, comparing the average values in 2004-2006 with data for 2012. Around the middle of last decade, people living in households with a very low work intensity were confronted with a poverty risk of 53.7%, whereas people living in households with a very high work intensity were confronted with a poverty risk of only 5.1%. This sizable divide has further heightened. By 2012, the poverty risk of individuals living in households with low and very low work intensity had increased considerably; conversely, the poverty risk of individuals living in households with very high work intensity remained the same. What we see in Figure 5 is a polarisation in poverty risks. Using the terminology we applied earlier, one could also say that it instantiates divergence, not between countries but between different groups of people across Europe – differentiated on the basis of the labour market attachment of their household.

Simultaneously, we witnessed a polarisation of employment across households in Europe: the share of individuals living in households with very high work intensity was reduced by the crisis, but it is today again higher than in 2007.²⁷ The share of people living in 'work-poor' households (by which we mean households with low

26. Eurostat defines work intensity of a household as the ratio of the total number of months that all working-age household members have worked during the income reference year and the total number of months the same household members theoretically could have worked in the same period (the indicator also takes into account the number of hours worked per month).

27. EU-SILC years correspond to observation years for work intensity.

and very low work intensity)²⁸ increased and is – as yet – not returning to its pre-crisis level. Simultaneously, there was a hollowing out of the middle: the share of people living in households with medium and high (but not very high) work intensity is lower than before the crisis. Compared to 2007, more people live in a household that is ‘very rich’ in terms of work intensity, and more people live in households that are ‘very poor’ in terms of work intensity. This is shown in Table 1.

Table 1 ▶ Structure of population below 60 years on the basis of household work-intensity

	2007	2008	2009	2010	2011	2012	2013
Very high work intensity	42,2	44,1	43,9	42,9	42,5	43,5	43,1
High work intensity	22,3	22,5	22,7	22,1	22,3	21,5	20,9
Medium work intensity	18,2	17,4	17	17,4	17,3	17	17,2
Low work intensity	6,9	6,3	6,7	7	7,1	7,1	7,6
Very low work intensity	9,7	9,1	9,1	10	10,3	10,4	10,7

Source: Eurostat. Note: years refer to EU-SILC years.

The combination of Figure 5 and Table 1 goes a long way in explaining why non-elderly poverty increased in Europe. Two mutually reinforcing factors are at play: more people are living in work-poor households; these households experience higher poverty risks than before the crisis. The latter trend started before the crisis: in a number of countries, the poverty risk of work-poor households has been increasing since EU-SILC began. Even before 2008, it increased considerably in mature welfare states such as Germany, Sweden, Austria and Finland. This explains why ‘employment successes’ before the crisis were, in a number of countries, not converted into ‘inclusion successes’ (Cantillon and Vandenbroucke, 2014). In fact, the pattern of change was far from homogeneous across Europe. Since 2004, some countries have combined increasing employment with decreasing non-elderly poverty, notably Poland. In other countries, poverty increased despite increasing employment. These diverse trajectories cannot be explained by one single driver; rather, a set of drivers is at play and the role and impact of the drivers differs from country to country.

An economic crisis reduces employment, but the long-term trend towards polarisation of jobs across households is a phenomenon that is not well understood (Corluy and Vandenbroucke, 2015). We have more indications with regard to the reasons for the increasing poverty risk of work-poor households. In principle, three sets of factors can have an influence:

1. tax-and-transfer systems may have become less generous for people without work, compared to people in employment;
2. changes in household structures can also play a role: a lone-parent household with a medium or low work intensity (say, a lone mother who holds a part-time job), is confronted with a higher financial poverty risk than a couple with children with the same medium or low work intensity (say, a couple where both partners work part-time or where one partner works full-time and the other is not employed);
3. if households with lower work intensity (but not *zero* work intensity) are dependent on a segment of the job market where the quality of jobs is lower, both in terms of contractual security and earnings, they lose out in terms of earned income compared to other households.

28. ‘Work poor’ is about work intensity, not about incomes earned; hence, it is not to be confused with ‘in-work poverty’.

The first factor, tax-and-transfer systems, may be associated with the activation turn, which emphasised that financial incentives to take up employment had to be increased: if enhanced financial incentives are not accompanied by success in activation in the segment of work-poor households, relative poverty can increase because the income gap between employed and unemployed people grows.

However, apart from deliberate changes in policy, there may also be an increasingly difficult structural constraint on the social adequacy of benefit systems. In societies where the standard of living of work-rich *dual-earner* households determines what is necessary for a decent standard of living for *any* household, social policy is confronted with a dilemma. It is not just the case that most work-poor households cannot reach this standard, whatever the number of working-age adults in the household; differences in the constellation of households create a dilemma that is structural. On the one hand, individual income replacement benefits are constrained, since they must not create employment disincentives, notably in comparison with the level of minimum wages; and the level of minimum wages is in turn constrained by considerations of cost competitiveness. On the other hand, income replacement benefits are insufficient to protect single-adult households against poverty (and even a comparatively decent minimum wage, as the Belgian one, is insufficient to protect single-adult households against poverty risks if the parent cannot work full-time, or if there are more than two children). Hence, the challenge is to improve social protection *at the household level*, whilst avoiding ‘work poverty traps’ at the household level, both for lone parents and for other households with children. **Therefore, we should reconsider the need for schemes designed to alleviate ‘household costs’ facing singles and single-income households as well as dual earners, including the cost of child-rearing, healthcare or housing. This would imply that, within the social security toolset, greater weight is assigned to so-called ‘cost-compensation’ benefits as supplements to individual replacement incomes, and intelligent and nuanced principles of household income selectivity are applied to those supplements. Simultaneously, the development and design of social services in support of families is of utmost importance.**

“ THE EU WOULD BE
WELL ADVISED TO DEVELOP
A FRAMEWORK ON
MINIMUM WAGES ”

These observations underscore the role of minimum wages, which we should understand correctly. To a certain extent (and with considerable heterogeneity across countries) minimum wages function as a ‘glass ceiling’ for the generosity of transfer systems. In countries where minimum wages are under pressure, the generosity of benefit systems will in the end also be under pressure.²⁹ Apart from their role as a (potential) glass ceiling for systems of minimum income protection, the direct impact of minimum wages on poverty is rather limited (OECD, 2015; Eurofound, 2015). Fundamentally, minimum wages underpin a notion of ‘fairness’ with regard to the compensation for work: their prime objective is not poverty alleviation. However, the OECD (2015) notes that minimum wage settings can help supporting low-wage workers and low-income families while avoiding significant job losses, if they are well designed and embedded in appropriate tax-and-transfer settings. Minimum wages are increasingly seen as under pressure because of cross-border mobility: part of the fears of social dumping may be unwarranted, but in specific sectors competitive pressure from ‘low-wage’ employers within the EU cannot be denied. In addition, there are problems with enforcement of minimum wage standards, in the context of posting of workers. **All these considerations support the idea that the EU would be well advised to develop a framework on minimum wages. A European framework could put pressure on all member states to have a system of minimum wages with universal coverage of the workforce, whatever the nature of the system (statutory, or based on collective bargaining).**

The direct impact on poverty of the third factor in our list, the changing nature of employment, is difficult to assess empirically. However, the OECD (2015) notes that, since the mid-1990s, more than half of all job creation was in the form of non-standard work and discerns important links with the trend toward income inequality in a number of countries. Non-standard work can be a ‘stepping stone’ to more stable employment – but it depends on the type of work and the characteristics of workers and labour market institutions. In many countries, younger workers, especially those with only temporary work contracts, have a lower chance of

29. The idea of a ‘glass ceiling on poverty reduction’, linked among other factors to the development of the wage floor, is explored in Cantillon, Collado and Van Mechelen (2015).

moving on to a more stable career job. Many non-standard workers are worse off in many aspects of job quality, such as earnings, job security or access to training. In particular, low-skilled temporary workers face substantial wage penalties, earnings instability and slower wage growth. Households that are heavily dependent on earnings from non-standard work have much higher income poverty rates, and the increase in the number of such households has contributed to higher overall inequality, according to the OECD.³⁰

With regard to job quality, we are confronted with contradictory demands. Voluntary part-time work can match preferences of individuals; part-time jobs can improve the distribution of work over households. Part-time jobs can allow older workers to remain active. So conceived, the development of a part-time labour market is positive. Simultaneously, many individuals need full-time employment to earn a decent living and to secure an adequate pension, i.e. a sufficient supply of full-time jobs remains necessary. The development of zero-hour contracts, which undermine the very notion of the employers' responsibility to secure an income (and concomitant entitlements in the social security system), raises even more difficult questions: for some individuals, zero-hours contracts may be an attractive option; but for many others it may be a cul-de-sac. The rise of 'marginal employment' in the form of mini-jobs, as in Germany, also implies fundamental long-term problems with regard to the social security coverage of those individuals who would only rely on such mini-jobs.

The European Commission's *Employment and Social Developments in Europe* report for 2014 contains an informative chapter on job quality and work organisation in Europe, to which we refer the reader. Their analysis signals the increasing prevalence of temporary short-term contracts and other forms of precarious work; it also emphasises that job quality can enhance labour productivity. In other words, there need not be a contradiction between a choice for job quality and economic progress. (ESDE, 2015)

“EUROPE NEEDS A COMBINATION OF ADEQUATE SOCIAL INVESTMENT AND ADEQUATE SOCIAL PROTECTION”

Job quality is not only about contractual arrangements; it is also about 'job control' and autonomy, as also highlighted in the *Employment and Social Developments in Europe* report. 'Job control' and autonomy are key to sustaining the drive for longer working lives. Nordic countries, in which people work longer than elsewhere in Europe, have more jobs that are characterised by job control and autonomy: that correlation is not happenstance.

The key message that emerges from these analyses is the following:

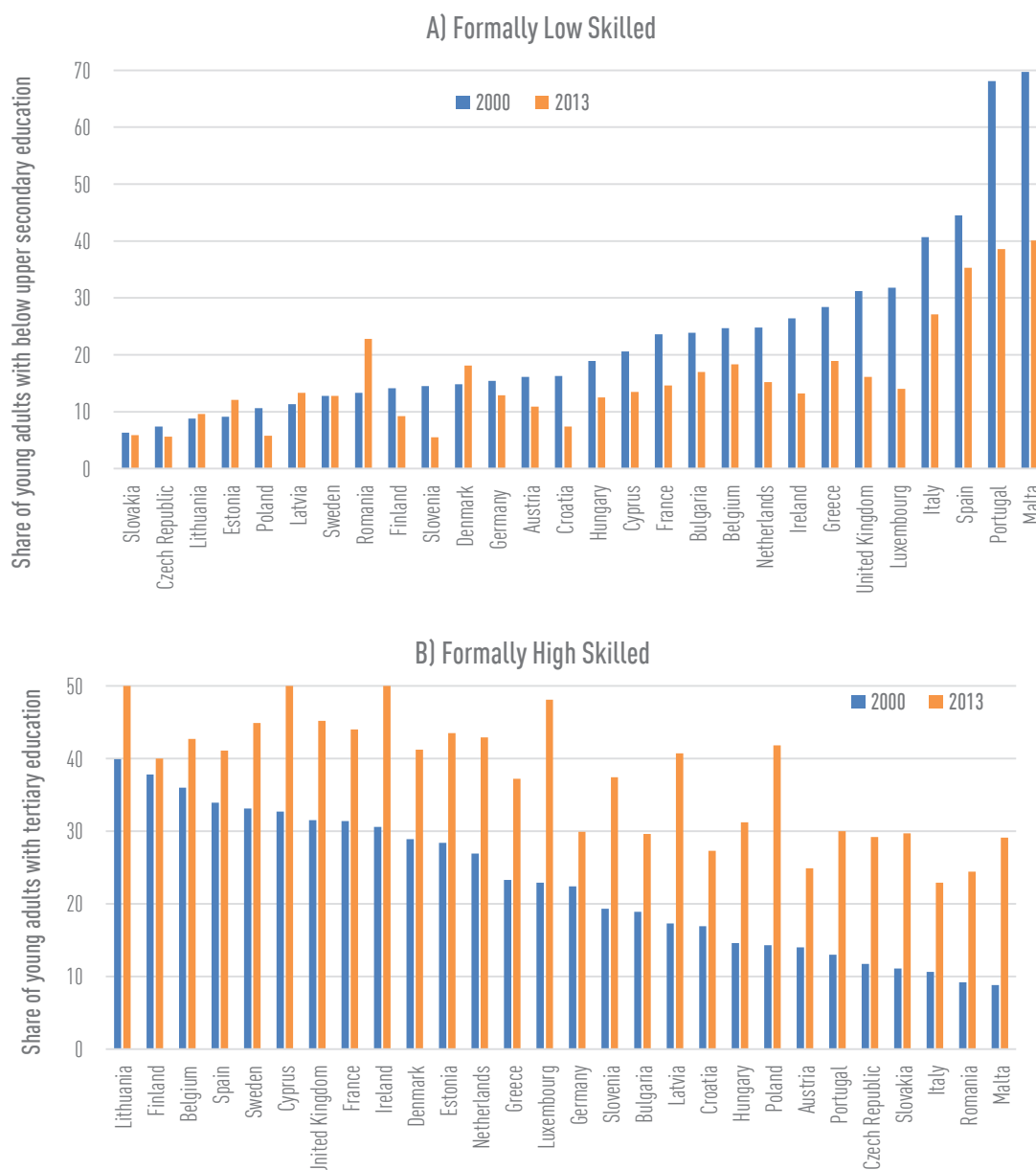
1. **The need for activation and for financial incentives to take up jobs should not be questioned. First, however, activation must be based on a 'high road' to quality jobs and real investment in human capital.** In other words, both the quantity and the quality of jobs count; the quality of employment should actually be seen as a condition for a full valorisation of human capital.
2. **Europe needs a combination of adequate social investment and adequate social protection;** they cannot be substitutes for each other. For instance, adequate unemployment benefit systems serve a dual purpose, apart from protecting individuals: they are a corollary to flexible labour markets and they act as macro-economic stabilisers. The emphasis on 'investment' in human capital should not ignore the need for protection of human capital, i.e. the traditional 'protective' functions of welfare states. Traditional instruments of social policy, such as activation, training, social benefits and minimum wages, remain important; but there is no denying that social protection systems are confronted with new challenges for which new and innovative solutions are to be found.
3. **The changing nature of employment raises issues with regard to the architecture of our social protection systems, issues which need to be addressed.** These are difficult questions, but the EU could provide a unique learning environment for policy-makers on how to tackle them (Hellström and Kosonen, 2015).

30. This paragraph is based on the OECD's own executive summary of OECD (2015), on pp. 15-16.

6. The human capital divide

If we restrict our attention to formal education, there is evidence of upward convergence across Europe. The heterogeneity in the share of formally high-skilled individuals is still wide, with less than 25% of the 25- to 34-year-olds in Italy, Romania and Austria having earned a university degree. In contrast, in Ireland, Cyprus and Lithuania one out of two young adults attains tertiary education. Nevertheless, upward convergence in formal education is taking place, and the divide, compared with that of the year 2000, is shrinking. In Figure 6a we can observe that the share of formally low-skilled individuals, i.e. those with less than upper secondary education, has diminished over time in the vast majority of EU member states, with Romania being the only notable exception to the trend. Likewise, Figure 6b shows an encouraging convergence coupled with an upward shift in the number of young adults with tertiary education.

Figure 6 ▶ Poverty Risks by Work Intensity of Households for EU-27, SILC 2013 – SILC 2005-2006-2007¹

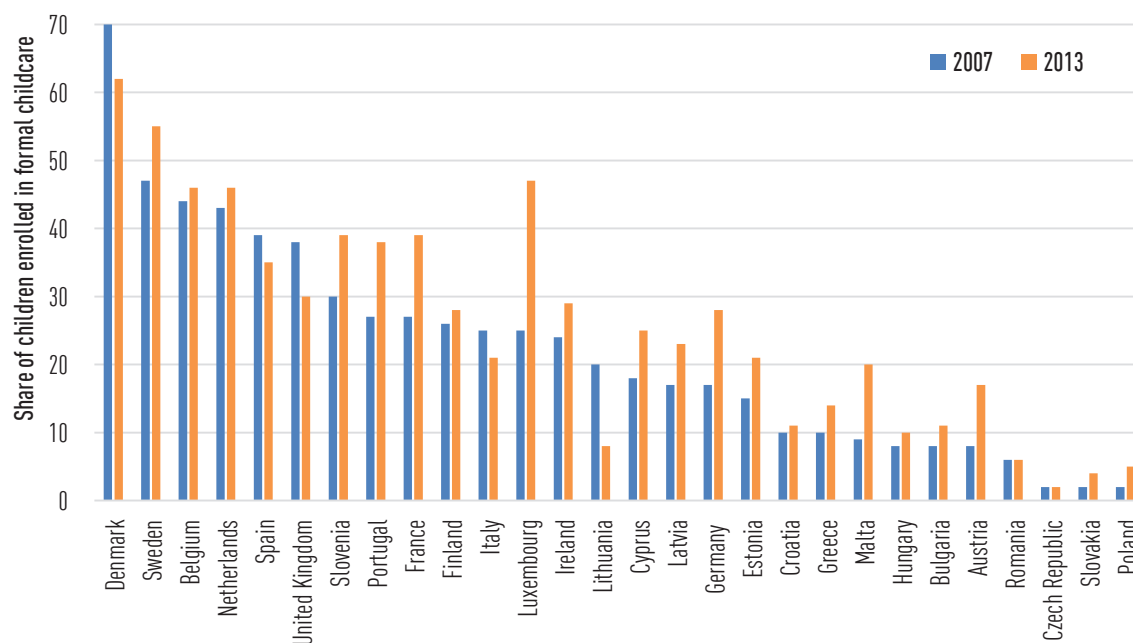


Source: EUROSTAT UOE [edat_ifse_05] and [edat_ifse_07] authors' calculations.

1. Data refer to age group 25-34 year-old. Formally low skilled refers to population with less than primary, primary and lower secondary education (levels 0-2). Formally high skilled refers to population with tertiary education (levels 5-8). Data for Croatia are for 2002 instead of 2000.

Unfortunately, formal education is only a piece of the story. Two issues are a cause of concern: first, upward convergence is less strong in formal education for children, where it would instead be mostly needed to ensure the eradication of poverty and social-exclusion transmission mechanisms; second, the divide in actual skills is growing.

Figure 7 – Developments in Early Childhood Care¹

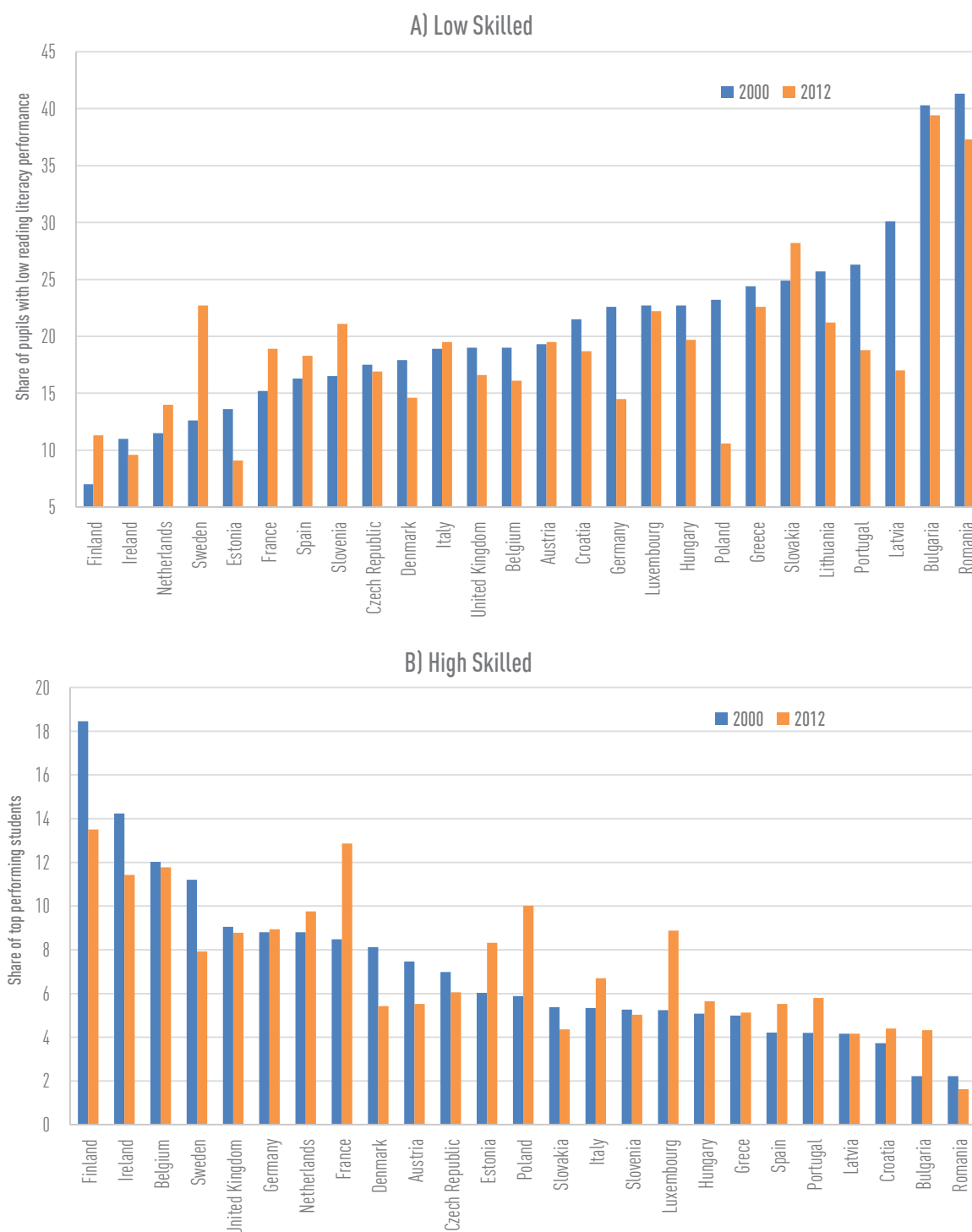


Source: Eurostat EU-SILC [ilc_caaindformal], authors' calculations.

1. Participation rate accounts for formal childcare for children below 3 years of age and refers to both part- and full-time participation. Data for Lithuania refer to 2012 and not to 2013, data for Croatia refer to 2010 instead of 2007.

In Figure 7 we can observe the development of formal childcare for children below the age of three. There is upward convergence, to some extent, but there are signs of downward shifts in Denmark, Spain, Lithuania, the UK, and Italy. In the latter country, for instance, fiscal consolidation has considerably reduced funds for regional and local welfare systems which are responsible, among other things, for primary and preschool services. Funds for Early Childhood Education and Care (ECEC) in 2015 are 3% lower than those available in 2010 and 54% lower than those available in 2008. It is therefore not surprising to see that enrolment decreases: the highest percentage of children below three years who are enrolled in ECEC services was registered in 2008 (28%); it decreased to 21% in 2013 and it is likely to contract further. Lack of investment in early childhood services is not a problem affecting Italy alone. The ESPN (2015) finds that, notwithstanding the message of the Social Investment Package (SIP) and the Commission Recommendation on Investing in Children, several countries (namely BG, CY, CZ, EL, ES, HR, IT, LT, LV, MT, PT, RO, RS, SK and TR) still have very low investment in child care and weak policies for supporting early childhood development. Moreover, as reported in Rinaldi (2015), the uptake of early childhood care in the EU is higher among wealthier and more educated parents, whereas the role of ECEC in the framework of a social investment strategy should consist in empowering disadvantaged households.

Figure 8 ▶ Developments in Skills¹



Source: OECD PISA 2012 Database and Eurostat [tsdsc450]. Authors' calculations.

1. Low reading literacy performance of pupils consists in the share of 15-year-old pupils who are at level 1 or below of the PISA combined reading literacy scale. Top performance is defined as Level 5 and above in reading proficiency. Reading literacy focuses on the ability of students to use written information in situations which they encounter in their life. When data for PISA 2000 are not available, the graph refers to PISA 2003 (Luxembourg, Slovakia and the Netherlands) or to 2006 (Croatia and Estonia).

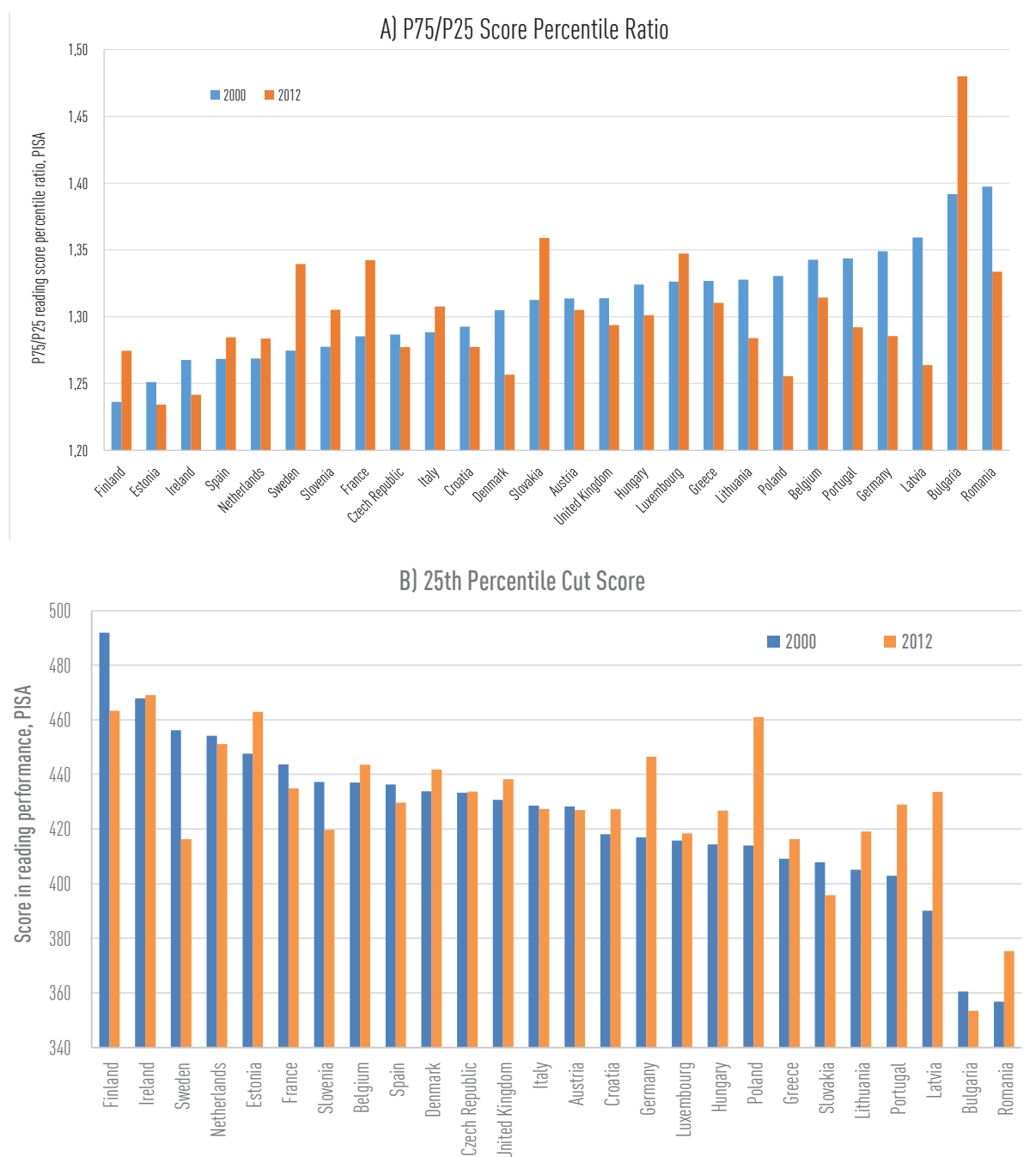
Actual skill levels are what matter, rather than formal educational attainment. To analyse the development of skills over time, we focus on the PISA scores for reading skills and compare the performance of 15-year-old pupils in 2000 and 2012, i.e. we use reading proficiency as an overall proxy for skills.³¹ The contrast between Figure 6 on formal education and Figure 8 on actual skill levels is striking. On the one hand, in terms of educational attainment almost all countries have improved, but, on the other hand, in Figure 8a, we observe that the share of low-skilled individuals increased in nine member states, including Austria for which the increase is marginal. Furthermore, in 14 countries the share of top performing pupils decreased or showed no sizeable increase. In Poland, the reduction of the share of students who are not able to meet the baseline level of reading proficiency paired with an increase in the share of top-performing students; in Sweden, Finland and Slovakia instead, the share of the high-skilled decreased and the share of the low-skilled increased. A certain degree of convergence is present but it is not due to a catching up towards higher levels of competences, it is rather due to deterioration of skills levels in those countries that were doing relatively well. Figure 8 also highlights that this mixed convergence has not been able to lessen the skills divide affecting Europe. Romania and Bulgaria with over 35% of low skilled pupils and only less than 5% of high skilled still lag considerably behind other EU member states in terms of skills.

Figure 9 provides additional insights into the dispersion of reading skills *within* Member States. We report both the P75/P25 score percentile ratio (Figure 9a) and the cut-off score for the 25th percentile³² (Figure 9b). The two indicators tell two different stories, neither of which is really positive. The P75/P25 ratio shows that in ten member states internal inequality in skills distribution worsened (France, Sweden, Bulgaria and Slovakia are examples) from 2000 to 2012. The P25 level shows that the absolute performance level at the bottom end of the skills distribution increased in some countries (such as Poland, Portugal and Germany, countries in which major efforts have been undertaken to improve performance) but decreased in a number of other countries, Sweden, Finland, Slovakia, Slovenia among others.

31. European Commission (2013), by comparing PISA 2009 and 2012 results, confirms that the trend we described for reading performance is consistent with those in mathematics and science. The share of low achieving students in EU member states has remained unchanged for both math (from 22.3% in 2009 to 22.1% in 2012) and science (from 17.8% in 2009 to 16.6% in 2012).

32. The cut-off score for the 25th percentile identifies a score such that 25% of the student sample perform worse.

Figure 9 ▶ Skills Dispersion¹



Source: OECD PISA 2012 Database and OECD (2014), authors' calculations.

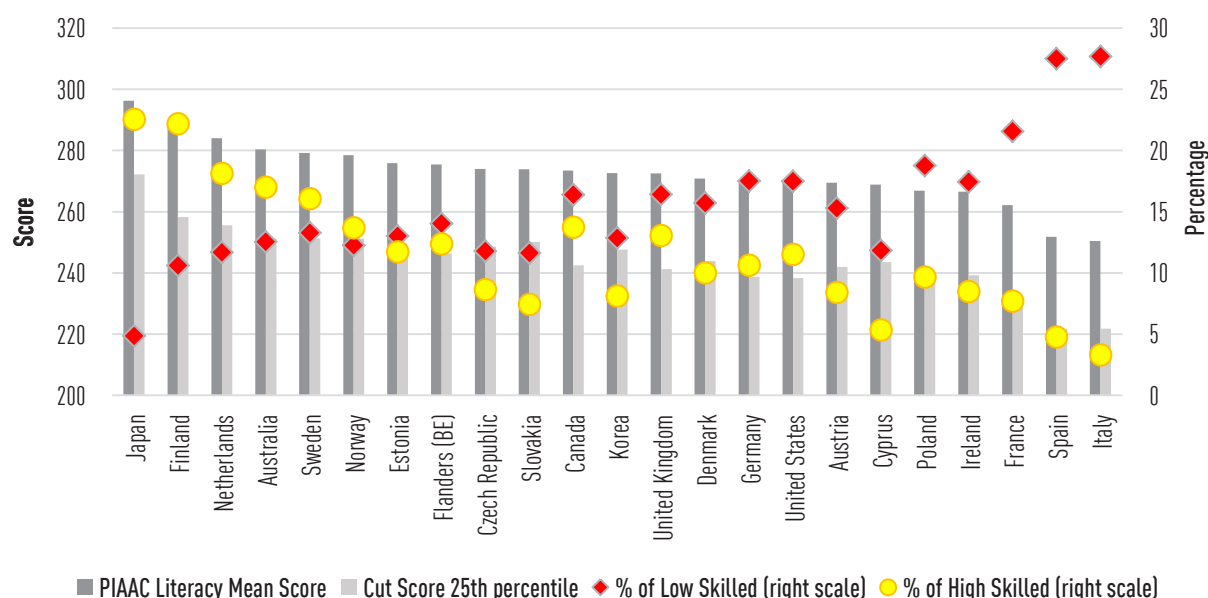
1. Cut scores of 15-year-old students on PISA reading literacy scale at 25th percentile. When data for PISA 2000 are not available, the graph refers to PISA 2003 (Luxembourg, Slovakia and the Netherlands) or to 2006 (Estonia, Croatia, Lithuania, Slovenia and the United Kingdom).

To have a better understanding of the 'stock' of skills, we also look at the skills distribution among adults. PIAAC³³ results, released in 2013, give insights into inequality in skills across countries and within countries among the working-age population. We condense the information in Figure 10, which reports scores at the

33. The Programme for the International Assessment of Adult Competencies (PIAAC) is an international survey carried out by the OECD. It assesses literacy, numeracy and problem-solving performance of people between 16 and 65 years old and thus evaluates cognitive and workplace skills. As PIAAC data are cross-sectional, it is impossible to study the evolution of adult skills over time.

mean and at the 25th percentile as well as the percentage of low- and high-skilled adults³⁴ for 23 countries.³⁵ The divide between Finland, the best-performing EU country, and Italy is alarming. With regard to literacy, more than 22% of Finnish adults are highly skilled, compared to a mere 3.3% in Italy. The mean score in the Scandinavian country is 287.5, whilst the mean in Italy (250.5) is even lower than the Finnish cut-off score for the 25th percentile (258.3). The percentage of low-skilled adults is below 10% in Japan, whilst it is above 20% in France, Spain and Italy. The worst results in terms of adult skills can be seen in those countries where social investment strategies are either non-existent or at a very embryonic stage. A weak culture of lifelong learning and training on the job is likely one of the main causes of poor skills among adults. The need for a serious investment in new skills in young people is evident in several European countries in this sample, notably France, Spain and Italy.

Figure 10 ► Distribution of Adult Skills across countries¹



Source: Survey of Adult Skills (PIAAC) (2012) and OECD (2013), [Table A2.1] and [Table A2.4], authors' calculations.

1. Scores refer to literacy performance. Adults with proficiency level 1 or below are defined as 'low skilled'; adults with proficiency level 4 or 5 are considered 'high skilled'.

34. PIAAC identifies five levels of proficiency. We define as low-skilled those who achieve proficiency level 1 or below, whereas we consider high-skilled those who achieve proficiency level 4 or 5.
35. The PIAAC sample is relatively limited for the EU, covering 16 EU countries plus Flanders, as shown in Figure 15 together with other participating countries.

“THE EU IS DEEPLY AFFECTED BY A HUMAN CAPITAL DIVIDE, BOTH BETWEEN AND WITHIN THE MEMBER STATES”

To sum up, the EU is deeply affected by a human capital divide, both between and within the member states. With regard to formal educational attainment, there are positive developments; but with regard to skills, insofar as there is convergence across the Union, there is a mixture of positive and negative developments. With regard to early childhood education and care, there are signs of upward convergence but, simultaneously, austerity policies have negatively affected ECEC efforts in many countries. The discrepancy between upward convergence in formal education and persistent inequalities in the actual distribution of competences both among and within member states is alarming. The European Commission (2015), which stresses similar results, sees this as a key threat to the achievement of a real European labour market and concludes that educational inequalities have often increased, since “educational equality has never been a policy priority in many EU countries”.³⁶ **European countries are therefore faced with a double challenge: they should consider how to boost skills and competence levels whilst also addressing the issue of how to bring high levels of competences to a broader share of the population.**

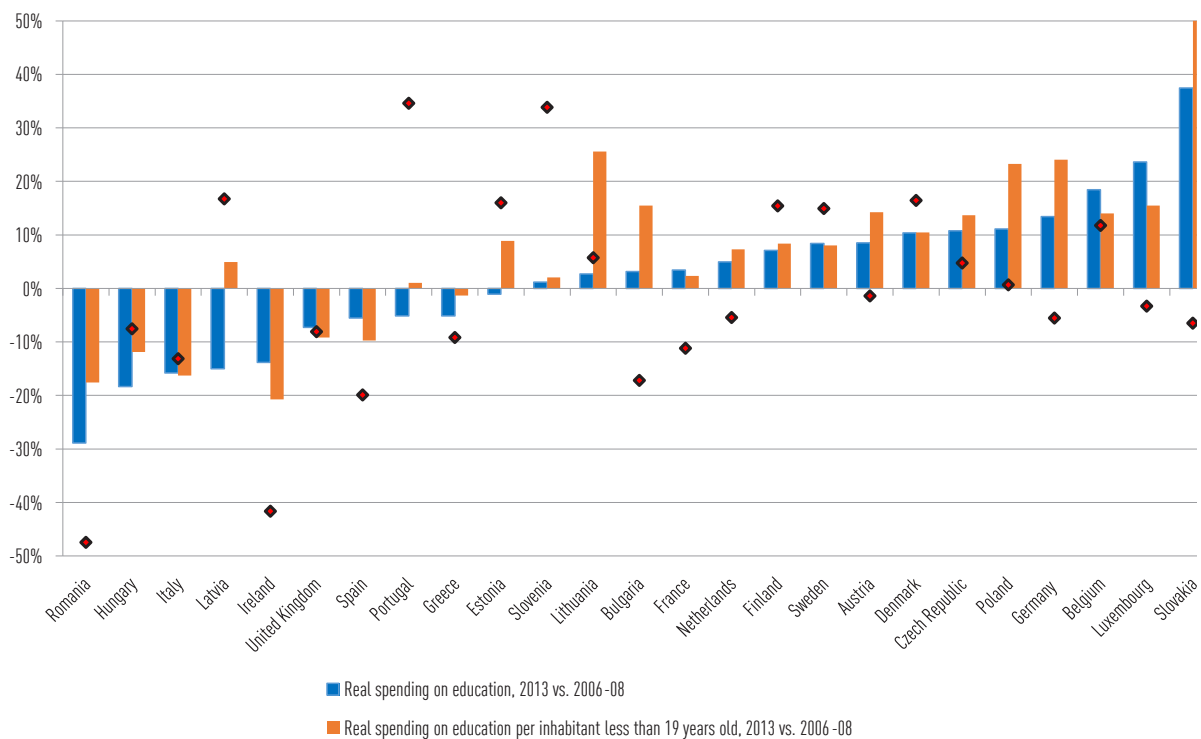
The EU certainly recognises the huge education challenge with which it is confronted and the European Commission has developed a comprehensive agenda on education, training and skills, and issued excellent recommendations on the modernisation of education systems. However, this educational agenda does not carry sufficient weight at the highest levels of European political decision-making and in the setting of budget priorities. Real public expenditure on education was lower in 2013 than before the crisis in 10 member states, including those that badly need to improve their education system.

Figure 11 displays data on the evolution of public spending on education in real terms. The black bars compare public education spending in 2013 for each country with the country’s average spending over the years 2006-2008 (deflated with the GDP deflator). In 10 of the 25 countries under review, real spending is now lower than it was, on average, in the years before the crisis. In Romania the decline is 29%, in Hungary it is 18%, in Italy 16%, in Latvia 15% and in Ireland 14%. Meanwhile, there was a significant increase in real spending, with an increase in education spending of 10% or more in Denmark, the Czech Republic, Germany, Poland, Belgium, Luxemburg and Slovakia (always comparing 2013 with the average over 2006-2008). Obviously, demography plays a role; in Figure 11 we can see that when demographic change is taken into account, by calculating real public spending on education per inhabitant younger than 19 years of age, real spending per young inhabitant decreased with 18% in Romania and 12% in Hungary; in contrast, in Ireland real spending per young inhabitant diminished with 21%. The effort in public education spending is spectacular in Germany and Poland, when taking demography in account.

The divergence in education spending across the EU may lead to more long-term divergence in productivity, instead of the convergence that is so badly needed. That is not to say that the quality of education systems can be measured in a simplistic way by the level of public spending on education; but it seems very hard to improve education systems significantly while disinvesting.

36. European Commission (2015), p. 21.

Figure 11 ► A Worrying Divergence in Public Spending on Education¹



Source: Eurostat, authors' calculations.

1. General government expenditure on education [gov_10a_exp] is corrected for inflation with price index 2005=100 [nama_gdp_p]. Spending is corrected for demographic changes [demo_pjangroup].

7. Health, health care and the environment

With regard to life expectancy, there is a large divide across European regions. Mediterranean and western countries have higher life expectancies, with Spain leading among EU member states with 82.4 years. Eastern and Baltic countries, in contrast, have shorter life expectancy, with Romania, Bulgaria, Latvia and Lithuania bringing up the rear with less than 75 years. Since 2000, there has been a remarkable upward shift: for all member states, life expectancy increased. Nevertheless, a clear distinction remains between two groups of countries: western countries, with a life expectancy of more than 75 years in 2000 and about 80 years or above now; and eastern countries, with life expectancy below 78 years, not all of which have achieved the levels that western countries enjoyed 15 years ago. The nine years' difference between Spain and Lithuania (73.4 years in 2013) is a considerable gap.

“ UNIVERSAL ACCESS TO QUALITY HEALTH CARE HAS TO BE REGARDED AS ONE OF THE CORE AIMS OF EUROPEAN WELFARE STATES”

Universal access to quality health care has to be regarded as one of the core aims of European welfare states. We can assess how the availability and affordability of health-care services have improved over time in European countries on the basis of the EU-SILC database, which registers the self-reported assessment of unmet needs for medical examinations. Medical examinations and treatment are crucial aspects of health care; high costs, long waiting lists and the distance to the service provider can be very relevant barriers to access for individuals who need health care. If we look at the year 2013 for the entire EU28, the percentage of people reporting unmet needs for medical examinations – due to services that were too expensive, distances that were too great or waiting lists that were too long – was 1.5% for the top income quintile; in contrast, it was 11% for the bottom 40% of income earners.

Inequalities in access to health care which penalise low-income households are unfortunately not a novelty. What emerges as a more striking pattern is that, with the exception of Portugal, Bulgaria, Germany and Latvia, there is no evidence of a downward trend in the share of people with unmet medical needs. Actually, Poland, France and some countries deeply affected by austerity measures, such as Greece, Latvia and Italy, have experienced a noticeable rise in unmet medical care for lower incomes. Some of the top-performing countries regressed and now have a higher share of poor individuals with unmet medical needs in 2013 than they had in 2007 (Finland +8.9%, Belgium +6.2%, France +4.3%).

Concerns over environmental justice are growing in Europe and it is now relatively clear that the environment and related policies have a strong impact on social conditions and well-being, notably via health, access to amenities, and consumption patterns. Despite that, a more general debate on the crossing of social and environmental perspectives has not yet emerged in all member states³⁷ and it is at an embryonic stage at the European level. Council of Europe (2013) develops an analysis that links aspects of poverty and inequality to waste and access to resources; in a study for the European Commission, Pye et al. (2008) review the numerous interlinkages between environmental and social policy and attempt to define patterns promoting synergies for mutually reinforcing policies. In this context, Laurent (2010) identifies four types of environmental inequalities: i) *inequalities in policymaking*: as certain socially disadvantaged groups have less or no impact on decision-making affecting their environment; ii) *inequalities in environmental impact*: as different social groups with different lifestyles impact the environment differently; iii) *inequalities in environmental regulation*: as individuals from different social groups or with different incomes are affected diversely by environmental policy, regulation and taxes; iv) *inequalities in exposure and access*: as environmental quality is distributed unequally across individuals and groups according to their incomes, ethnicity or social status.

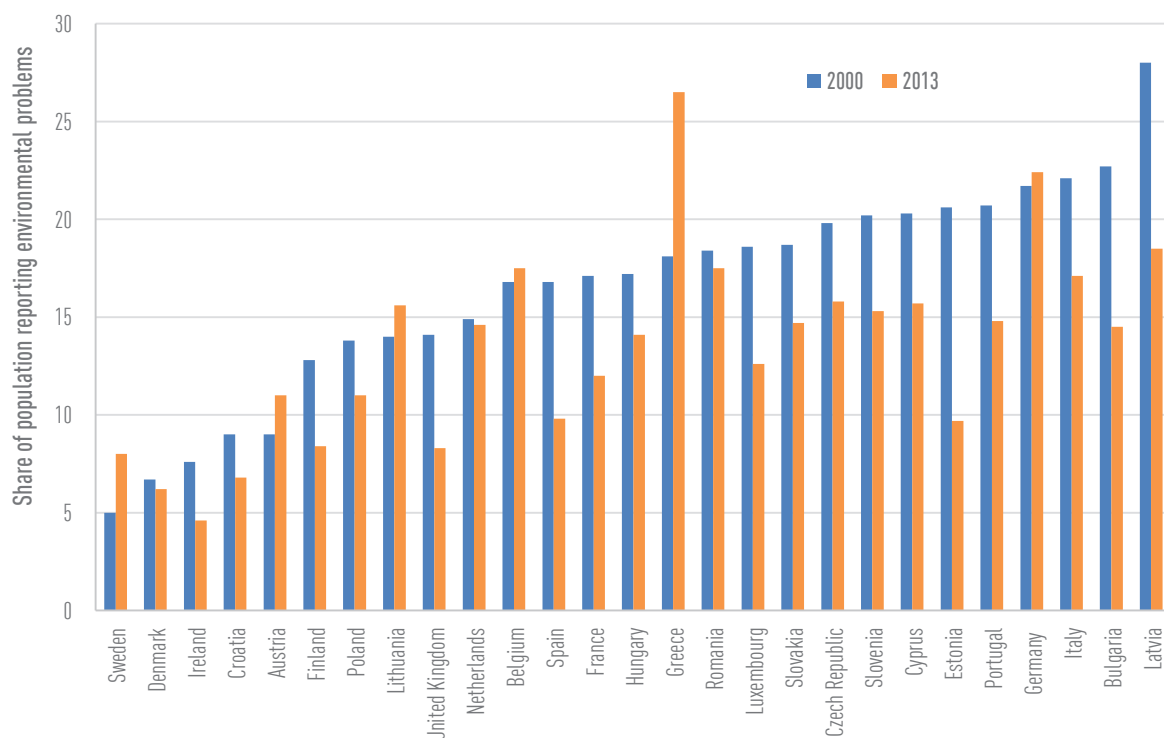
The distribution of environmental quality remains unequal, because the exposure to environmental risk and hazard is higher among vulnerable groups and because access to environmental amenities is at times limited

37. The UK leads the way with its national sustainable development strategy developed in 2005 and with the broad mandate of the UK Environmental Agency.

for disadvantaged group. Being exposed to pollution and crime and living in environmentally risky or excessively noisy areas represents a serious threat to health and well-being and can constitute a barrier to the empowerment of certain strata of society. To address social inequalities, social policy must embrace the issue of environmental justice.

To check whether Europe has made progress with regard to environmental inequalities, Figure 12 shows the share of population that reports problems linked to the presence of pollution, crime or other environment-related problems such as smoke, dust, unpleasant smells or polluted water, in the proximity of their dwelling. Over the 2005-2013 period, the only increase in reported environmental discomfort happened in Greece and Sweden; some countries remained relatively steady (Denmark, Lithuania, Belgium, Germany and the Netherlands). Nevertheless, there is evidence of downward convergence in the rate of exposure to environmental problems, i.e. an upward convergence in environmental quality.

Figure 12 ► Developments in Environmental Quality¹



Source: EUROSTAT, EU-SILC [ilc_mddw02]

1. Percentage of total population reporting exposure to pollution, crime or other environmental problems. Data are not available for 2005 for Romania and Croatia, 2007 and 2010, respectively, are reported.

Upward convergence in environmental quality has impacted both top and bottom incomes, with marginally higher gains for the former. If we look at the euro area for instance, the share of reported environmental distress decreased 3.2 percentage points for those above 60% of median equivalised income and 1.5 percentage points for those below. Marked differences between income groups are present in Bulgaria, Hungary, France, Belgium and Germany, whilst for countries such as Greece and Romania the EU-SILC survey reports that environmental problems are more of a concern for the richer.

As stressed by Laurent (2010), European social policies should deal with the impact, in terms of health and socio-economic conditions, of environmental conditions and policies. A reduction of environmental inequalities by means of social-ecological policies should be among the objectives of modern welfare states.

8. ‘Dual-use’ policy packages for convergence and cohesion and the role of the EU

In its report *In It Together. Why Less Inequality Benefits All*, the OECD (2015) emphasises that reducing the growing divide between rich and poor requires *policy packages*, mobilising a whole range of instruments, in four main areas:

1. women’s participation in economic life
2. employment promotion and good-quality jobs
3. skills and education
4. tax-and-transfer systems for efficient redistribution

Simultaneously, the OECD emphasises that there is no single best model or policy mix to adopt. “Each country will have to design its own package, depending on the key factors at the origins of inequality in the national context.”³⁸ The OECD adds a particular dimension to discussions on policy choices by demonstrating how inequality can reduce growth. The main transmission mechanism between inequality and growth, according to the OECD, is human-capital investment. While there is always a gap in education outcomes across individuals with different socio-economic backgrounds, the gap widens in high-inequality countries as people in disadvantaged households struggle to access quality education. The report suggests that it is the position of the bottom 40% that matters in particular for economic growth. It is not only the situation of the very poorest section of the population that inhibits growth, but that of a much broader group of working and lower middle class people. Policy thus needs to be directed towards the bottom 40%.

The data in Section 6 show that upward convergence in the quality of our human capital is a key condition for long-term upward convergence across the EU. Hence, *reducing background inequalities between families with children and investing in child care and education support both national cohesion and long-term EU-wide convergence*. Obviously, creating greater access to success in education for all children is not just a question of money; it also requires reforms in the education system in many member states.

“A CHILD-CENTRED
SOCIAL INVESTMENT
STRATEGY THAT
ADDRESSES INEQUALITIES
IN OPPORTUNITIES SERVES
A DUAL PURPOSE”

In other words, a child-centred social investment strategy that addresses inequalities in opportunities serves a dual purpose. Borrowing from military terminology, one may say that it is a dual-use policy package in the current European context. Governments pursuing such a strategy deserve encouragement and opportunities to learn from other EU governments, but also tangible support from the EU, notably when they are in budgetary dire straits.

Other policy orientations, put forward by the OECD, have a similar *dual-use* character in the context of the Eurozone. Adequate unemployment insurance and coordinated wage bargaining are two examples.

The OECD notes that increasing coverage of unemployment insurance is a promising avenue for promoting worker security, provided systems are designed to preserve incentives to work and meet other conditions which the OECD sets out. Inadequate coverage of unemployment insurance is an endemic problem in some European countries, notably in the Southern Eurozone. Apart from their negative social consequences, patchy unemployment benefit systems undermine the automatic stabilisation capacity of those welfare states. They also make it difficult to opt for a more flexible labour market with more balanced employment protection.

38. OECD (2015), p. 36.

Addressing labour market segmentation, promoting flexibility and improving unemployment insurance coverage should go hand in hand. Flexible labour markets are also a condition for a monetary union to function smoothly. In other words, a policy package that combines improved unemployment insurance and flexibility will serve both internal social inclusion and the future stability of the Eurozone. This is one of the reasons why some argue in favour of a European support for national unemployment insurance systems, notably in the Eurozone.

The coordination of wage bargaining has the same *dual-use* potential. This may be a surprising and more controversial statement, but it merits serious consideration. The OECD mentions the improvement of social dialogue and industrial relations as important elements of a more equitable and inclusive growth: high union density and bargaining coverage, and the centralisation/coordination of wage bargaining tend to go hand in hand with lower overall wage inequality, although there is some disagreement about the size of these effects and whether they hold for women. (OECD, 2015) Atkinson (2015) stresses the same insight, integrating it into a broader discussion of the link between equality and empowerment, and of the need to have ‘national conversations’ on pay and income inequality. From a totally different vantage point, wage coordination is also important in a monetary union – for reasons of symmetry in wage developments. What we have learned since 2008 is that exposure to market forces has not in itself produced wage discipline in the monetary union. On the contrary, monetary integration, as it has been implemented, invited ‘lack of discipline’ rather than discipline. This one of the reasons why divergence obtained, rather than convergence. Elsewhere we argue that, therefore, **the Eurozone needs a visible hand that pursues symmetry, notably with regard to wage increases (Vandenbroucke, 2015a, b). Moreover, member states need labour market institutions that can coordinate wage increases: the visible hand must be effective.**

Hence, the EU should acknowledge the positive results that come from coordinated wage bargaining within member states. Instead of encouraging the decentralisation of collective bargaining, the EU should take steps to encourage and facilitate bargaining coordination. The Five Presidents’ Report on the future of the Monetary Union³⁹ now presents a proposal which can be linked to the need to revamp systems of collective bargaining: it proposes a euro-area system of national ‘competitiveness authorities’, thereby referring to Belgium as an example of good practice. It so happens that the Belgian competitiveness watchdog is embedded in national collective bargaining institutions, and derives its authority precisely from being part and parcel of the collective bargaining system. Hence, the ‘good practice’, which the Five Presidents’ Report refers to, may be broadened to embedding such competitiveness authorities in collective bargaining systems.

Finally, EU initiatives may also be necessary to allow member states to implement certain OECD recommendations successfully. The OECD emphasises that adequately designed redistribution via taxes and transfers is a powerful instrument to contribute to more equality and more growth. According to its analysis, the effectiveness of redistribution weakened in recent decades in many countries due to working-age benefits not keeping pace with real wages and taxes becoming less progressive. The OECD leaves no doubt that policies need to ensure that wealthier individuals, but also multinational firms, pay their share of the tax burden. Without a European framework on corporate taxation, tax competition between EU countries seems to make that very difficult, if not impossible (Bénassy-Quéré, Trannoy and Wolff, 2014). In the 1980s, creating a level playing field with regard to health and safety at work was seen as a natural corollary to the deepening of market integration; in the same vein, consolidating the Union today may necessitate the creation of a level playing field in new domains, such as corporate taxation.

39. Five Presidents’ Report (2015), *Completing Europe’s Economic and Monetary Union*, 22 June 2015.

9. Solidarity and mutual trust

In the previous section, we highlighted the link between specific challenges for the EU and certain OECD recommendations with respect to inequality. These observations touch upon more fundamental issues of solidarity, mutual trust and the role of the EU. We briefly elaborate upon this in this section.

“ THE ORGANIZATION OF SOLIDARITY REQUIRES MUTUAL TRUST ”

Since 2008, we have learned that design failures of European Monetary Union made it unstable and fragile: it lacked both a banking union and a central bank that was ready to be lender of last resort, if necessary. The Five President’s Report now adds to this that the euro area also needs a fiscal stabilisation function. Indeed, both a lender of last resort and a fiscal capacity are indispensable to support Eurozone welfare states in one of their key systemic functions: stabilisation in times of economic crisis. The idea of a fiscal stabilisation function, which implies fiscal transfers in one way or another, remains at a very generic level in the Five Presidents’ Report. Admittedly, it raises complex political and technical questions, and different options can be pursued; the idea of a European support for national unemployment insurance systems, referred to in the previous section, could be one option⁴⁰. It is therefore important to clarify these ideas, which constitute a research agenda rather than a policy programme. Fundamentally, both with regard to the completion of banking union (which raises issues of mutual insurance) and fiscal stabilisation (which can also be understood as the organisation of a kind of mutual insurance against adverse economic circumstances), the Five President’s Report signals an acute awareness that we need to organise more solidarity in the Eurozone.

The organization of solidarity requires mutual trust. Solidarity on the basis of mutual insurance is a rational option, but even the most rational individuals will not engage in mutual insurance, if they do not trust each other sufficiently. European solidarity requires mutual trust with regard to the quality of the social fabric in the member states, notably with regard to their capacity to deliver on competitiveness and sound public finances.

Mutual trust is also at stake in the social dumping debate. In the past, the spectre of large-scale social dumping has never materialised, but in today’s enlarged EU, blatant cases of illegal working conditions and exploitation do occur, resulting from the interplay of gaps in the domestic implementation of social and employment protection in member states, their reduced legal sovereignty and the absence of common social standards in a very heterogeneous group of countries. A crucial condition for European public opinion to accept labour mobility and migration is that they should fit into a regulated social order; they must not undermine that social order. Whether or not minimum wage standards can be protected in a context of free movement of workers and services is a salient example. Reconciling mobility and the four freedoms, on the one hand, with the internal cohesion of national welfare states and industrial relations, on the other hand, is a complex challenge, but it is not an insurmountable one. It requires a ‘balancing act’, which is feasible. This balancing act is not just between economic principles and social principles. Both international openness (under certain conditions) and domestic social cohesion can be understood in terms of solidarity; we touched upon this in Section 1, when we explained that the European project implies a complex notion of solidarity. Hence, the balancing act is also between different types of solidarity.

40. See Beblavý and Maselli (2014) for a simulation exercise that compares a harmonised European unemployment benefit scheme with a reinsurance scheme and Enderlein, Guttenberg and Spiess (2013) for the alternative proposal of a cyclical shock insurance based on output gap measures.

10. Envoi

The EU deserves a *Social Triple A* if it actively supports both convergence towards higher aggregate levels of well-being across the member states and convergence towards more equality of individual well-being within the member states. In a sense, this twin ambition is not new; it means that we have to revisit what originally inspired the European project's founding fathers. The problem is less with the original inspiration than with our current capacity to deliver on it. The founding fathers optimistically assumed that growing cohesion both between and within countries could be reached by supranational economic cooperation; domestic social policies were to redistribute the fruits of economic progress, while remaining a national prerogative. **This traditional division of labour is not fit for the current challenges. As a matter of fact, the EU has already had a considerable impact on the member states' social policies. Hence, we now have to define what we expect from the EU in the domain of social policy**⁴¹.

“UPWARD CONVERGENCE
IN THE QUALITY OF OUR HUMAN
CAPITAL IS A KEY CONDITION
FOR UPWARD CONVERGENCE IN
PROSPERITY AND WELL-BEING
ACROSS THE EU”

The EU should stimulate and support the member states to develop policy packages that contribute to growing cohesion both within and between countries. Such 'dual-use' policy packages do exist: education offers a telling example. Upward convergence in the quality of our human capital is a key condition for long-term upward convergence in prosperity and well-being across the EU. Currently, the EU is deeply affected by a human capital divide, both between and within the member states. Hence, reducing background inequalities between families with children and investing in child care and education contribute both to national cohesion and to long-term EU-wide convergence.

Obviously, creating greater access to success in education for all children is not just a question of money; it also requires reforms in the education system in many member states. **Governments pursuing such a strategy deserve encouragement and opportunities to learn from other EU governments, but also tangible support from the EU, notably when they are in budgetary dire straits. We need more 'solidarity in reform'.**

There is a growing awareness that we need to organize more solidarity in the EU, as witnessed by the recent Five President's Report on the future of the Eurozone and the refugee crisis. The organization of solidarity requires mutual trust. Mutual trust is also at stake in the social dumping debate. **A crucial condition for European public opinion to accept labour mobility and migration is that they should fit into a regulated social order. Such a 'balancing act' should figure high on the European agenda.**

The EU's role in social policy can be summarised as follows. **The EU should provide a framework that reconciles openness and mobility with domestic social cohesion; it should support national welfare states on a systemic level in some of their key functions; it should guide the substantive development of national welfare states by indicating general social standards and objectives and organise mutual learning processes, but leave ways and means to the member states.**

41. See Fernandes and Maslauskaitė (2013), which provides three scenarios for deepening the European Monetary Union and Vandenbroucke (2015a, b), which make the case for a European Social Union.

REFERENCES

- Atkinson Anthony, *Inequality. What Can Be Done?*, Oxford University Press, 2015.
- Beblavý Miroslav and Maselli Ilaria, “An Unemployment Insurance Scheme for the Euro Area: A Simulation Exercise of Two Options”, CEPS Special Report, n° 98, 2014.
- Begg Iain, Mushövel Fabian and Niblett Robin, “The Welfare State in Europe: Visions for Reform”, Vision Europe Summit paper, 2015.
- Bénassy-Quéré Agnès, Trannoy Alain and Wolff Guntram, “Tax Harmonization in Europe: Moving Forward”, Les notes du conseil d’analyse économique, French Council of Economic Analysis, n° 14, 2014.
- Cantillon Bea, Collado Diego and Van Mechelen Natascha, *The Glass Ceiling of Poverty Reduction*, forthcoming, 2015.
- Cantillon Bea and Vandenbroucke Frank (eds.), *Reconciling Work and Poverty Reduction – How Successful Are European Welfare States?*, Oxford University Press, 2014.
- Corluy Vincent and Vandenbroucke Frank, « Polarisation of Employment over Households Revisited: The Belgian Case », KU Leuven Discussion Paper Series, n° DPS15.08, 2015.
- Council of Europe, *Living in Dignity in the 21st Century – Poverty and Inequality in Societies of Human Rights: The Paradox of Democracies*, Strasbourg: Council of Europe Publishing, 2013.
- Diris Ron, Vandenbroucke Frank and Verbist Gerlinde, “Child Poverty: What Can Social Spending Explain in Europe?”, KU Leuven Discussion Paper Series, n° DPS14.20, 2014.
- Dolls Mathias, Fuest Clemens and Peichl Andreas, “Automatic Stabilizers and Economic Crisis: US vs. Europe”, *Journal of Public Economics*, n° 96(3-4), 2012, pp. 279-294.
- ECB, “Real Convergence in the Euro Area: Evidence, Theory and Policy Implications”, *ECB Economic Bulletin*, n° 5, 2015.
- Enderlein Henrik, Guttenberg Lucas and Spiess Jann, “Blueprint for a Cyclical Shock Insurance in the Euro Area”, *Studies & Reports No 100*, Jacques Delors Institute, “EU & Differentiated Integration” Project, 2013.
- ESDE, *Employment and Social Developments in Europe 2014*, European Commission, Brussels, 2015.
- ESDE, *Employment and Social Developments in Europe 2013*, European Commission, Brussels, 2014.
- ESDE, *Employment and Social Developments in Europe 2012*, European Commission, Brussels, 2012.
- ESPN, *Social Investment in Europe: A Study of National Policies 2015*, Study for the European Commission, DG Employment, 2015.
- Eurofound, *Upgrading or Polarisation? Long-Term and Global Shifts in the Employment Structure: European Jobs Monitor 2015*, Luxembourg : Publications Office of the European Union, 2015.
- European Commission, *An Ever Closing Union Among the Peoples of Europe? Rising Inequalities in the EU and Their Social, Economic and Political Impacts. Outcomes of EU-Funded Research*, Brussels, 2015.
- European Commission, *PISA 2012: EU Performance and First Inferences Regarding Education and Training Policies in Europe*, Brussels, 2013.
- Fernandes Sofia and Maslauskaitė Kristina, “Deepening the EMU: How to Maintain and Develop the European Social Model?”, *Studies & Reports No 101*, Jacques Delors Institute, 2013.
- Five Presidents’ Report, *Completing Europe’s Economic and Monetary Union*, Brussels : European Commission, 22 June 2015.
- Fleurbaey Marc and Blanchet Didier, *Beyond GDP – Measuring Welfare and Assessing Sustainability*, Oxford University Press, 2013.
- Friends of Europe, *Unequal Europe. Recommendations for a More Caring EU*, Final Report of the High-Level Group on ‘Social Union’, spring 2015.
- Hämäläinen Timo, “In Search of Coherence: Sketching a Theory of Sustainable Well-Being”, in Hämäläinen Timo J. and Michaelson Juliet (eds.), *Well-Being and Beyond*, Edward Elgar Publishing, 2014, pp. 17-67.
- Hellström Eeva, Hämäläinen Timo, Lahti Vesa-Matti, Cook Justin and Jousilahti Julia, “Towards a Sustainable Well-Being Society. From Principles to Applications”, *Sitra Working Paper*, 2015.
- Hellström Eeva and Kosonen Mikko, “Governing the Welfare State and Beyond – Solutions for a Complex World and Uncertain Future”, *Vision Europe Summit paper*, 2015.

- Hemerijck Anton, *Changing Welfare States*, Oxford University Press, 2014.
- Hüttl Pia, Wilson Karen and Wolff Guntram, « The Growing Inter-Generational Divide in Europe: What Role for the Welfare State? », *Vision Europe Summit Paper*, 2015.
- Laurent Eloi, “Environmental Justice and Environmental Inequalities: A European Perspective”, *ETUI Policy Brief, European Social Policy*, n° 3, 2010.
- Lefranc Arnaud, Pistolesi Nicolas and Trannoy Alain, “Une réduction de l’inégalité des chances dans l’inégalité du revenu salarial en France ?”, *Revue d’Economie Politique*, n° 117, 2007, pp. 91-117.
- OECD, *In It Together: Why Less Inequality Benefits All*, Paris: OECD Publishing, 2015.
- OECD, *What Students Know and Can Do: Student Performance in Mathematics, Reading and Science – Volume 1*, Paris: OECD Publishing, 2014.
- OECD, *OECD Skills Outlook 2013*, Paris: OECD Publishing, 2013.
- OECD, *Divided We Stand: Why Inequality Keeps Rising*, Paris: OECD Publishing, 2011.
- OECD, *Growing Unequal? Income Distribution and Poverty in OECD Countries*, Paris: OECD Publishing, 2008.
- Oxfam, “A Europe for the Many, Not the Few – Time to Reverse the Course of Inequality and Poverty in Europe”, *Oxfam Briefing Paper*, n° 206, 2015.
- Pye Steve et al., “Addressing the Social Dimensions of Environmental Policy – A Study on the Linkages between Environmental and Social Sustainability in Europe”, *European Commission, DG Employment, Social Affairs and Equal Opportunities*, 2008.
- Rinaldi David, “A New Start for Social Europe?”, *Studies & Reports No 108*, Jacques Delors Institute, 2016.
- Roemer John and Trannoy Alain, “Equality of Opportunity”, *Cowles Foundation Discussion Papers*, n° 1921, Cowles Foundation for Research in Economics, Yale University, 2013.
- Salverda Wiemer et al., *Changing Inequalities in Rich Countries – Analytical and Comparative Perspectives*, Oxford University Press, 2014.
- Schraad-Tischler Daniel, *Social Justice in the EU – Index Report 2015*, *Social Inclusion Monitor Europe*, Bertelsmann Stiftung, October 2015.
- Stiglitz Joseph, Sen Amartya and Fitoussi Jean-Paul., *Report by the Commission on the Measurement of Economic Performance and Social Progress*, *Institut national de la statistique et des études économiques*, 2009.
- Vandenbroucke Frank, “The Case of a European Social Union. From Muddling Through to a Sense of Common Purpose”, in Marin Bernd (ed.) (forthcoming, 2015), *The Future of Welfare in a Global Europe*, Ashgate: Aldershot UK, 2015a, pp. 433-464.
- Vandenbroucke Frank, “A European Social Union: Unduly Idealistic or Inevitable?”, *European Debates*, n° 7, *European Investment Bank Institute*, 2015b.
- Vandenbroucke Frank and Diris Ron, “Mapping At-Risk-of-Poverty Rates, Household Employment, and Social Spending”, in: Cantillon Bea and Vandenbroucke Frank (eds.), *Reconciling Work and Poverty Reduction. How Successful are European Welfare States?*, Oxford University Press, 2014, pp. 1-59.
- Vandenbroucke Frank, Diris Ron and Verbist Gerlinde, “Excessive Social Imbalances and the Performance of Welfare States in the EU”, *Euroforum paper*, KU Leuven, 2013.
- Vandenbroucke Frank, Hemerijck Anton and Palier Bruno, “The EU Needs a Social Investment Pact”, *OSE Paper Series, Opinion Paper No. 5*, *European Social Observatory*, 2011.
- Vandenbroucke Frank and Vanhercke Bart, “A European Social Union: Ten Tough Nuts to Crack”, *Background Report for the Friends of Europe High-Level Group on ‘Social Union’*, 2014.

On the same themes...

REDESIGNING EUROPEAN WELFARE STATES – TIME FOR ACTION

Yves Bertoncini, Piero Gastaldo, Aart De Geus, Mikko Kosonen, Robin Niblett, Artur Santos Silva, Izabela Styczyńska, and Guntram Wolff, *Tribune*, Jacques Delors Institute / Vision Europe Summit, December 2015

THE GROWING INTERGENERATIONAL DIVIDE IN EUROPE – WHAT ROLE FOR THE WELFARE STATE?

Pia Hüttl, Karen Wilson, and Guntram Wolff, *Policy paper No 149*, Jacques Delors Institute / Vision Europe Summit, December 2015

GOVERNING THE WELFARE STATE AND BEYOND – SOLUTIONS FOR A COMPLEX AND UNCERTAIN FUTURE

Eeva Hellström, Mikko Kosonen, *Policy paper No 148*, Jacques Delors Institute / Vision Europe Summit, December 2015

THE WELFARE STATE IN EUROPE – VISIONS FOR REFORM

Iain Begg, Fabian Mushövel and Robin Niblett, *Policy paper No 146*, Jacques Delors Institute / Vision Europe Summit, December 2015

REDESIGNING EMU: WHAT AGENDA AFTER THE GREEK NEGOTIATIONS?

Eulalia Rubio, David Rinaldi and Emmett Strickland, *Synthesis*, Jacques Delors Institute, November 2015

REGIONAL INTEGRATION AND SOCIAL COHESION: THE EUROPEAN EXPERIENCE

Eulalia Rubio, *Policy paper No 138*, Jacques Delors Institute, June 2015

DEEPENING THE EMU: HOW TO MAINTAIN AND DEVELOP THE EUROPEAN SOCIAL MODEL?

Sofia Fernandes and Kristina Maslauskaitė, *Studies & Reports No 101*, Notre Europe – Jacques Delors Institute, November 2013

SOCIAL COMPETITION IN THE EU: MYTHS AND REALITIES

Kristina Maslauskaitė, *Studies & Reports No 97*, Notre Europe – Jacques Delors Institute, June 2013

Managing Editor: Yves Bertoncini • The document may be reproduced in part or in full on the dual condition that its meaning is not distorted and that the source is mentioned • The views expressed are those of the author(s) and do not necessarily reflect those of the publisher • The Jacques Delors Institute cannot be held responsible for the use which any third party may make of the document • Original version • © Jacques Delors Institute

