Social security and inequality

Introduction

Welfare states, and more particularly tax-benefit systems, are regarded as one of the main instruments in mitigating and correcting inequality. And yet the original purpose of social protection systems was in fact not to redress inequality but rather to reproduce the prevailing social hierarchy (Esping-Andersen and Myles 2009). The question of these systems' ability actually to *reduce* inequality thus remains open and it comes as no surprise that the currently found varieties of welfare system display varying degrees of ability in this respect: some countries have neither created the appropriate institutions nor set aside the requisite financial resources; others have set up welfare systems that are designed mainly to operate as piggy-banks (e.g. Continental Europe); some, finally, have set up welfare systems intended to play a Robin Hood role (e.g. Denmark), deliberately aimed, in other words, at narrowing the gap between rich and poor (Barr 2001).

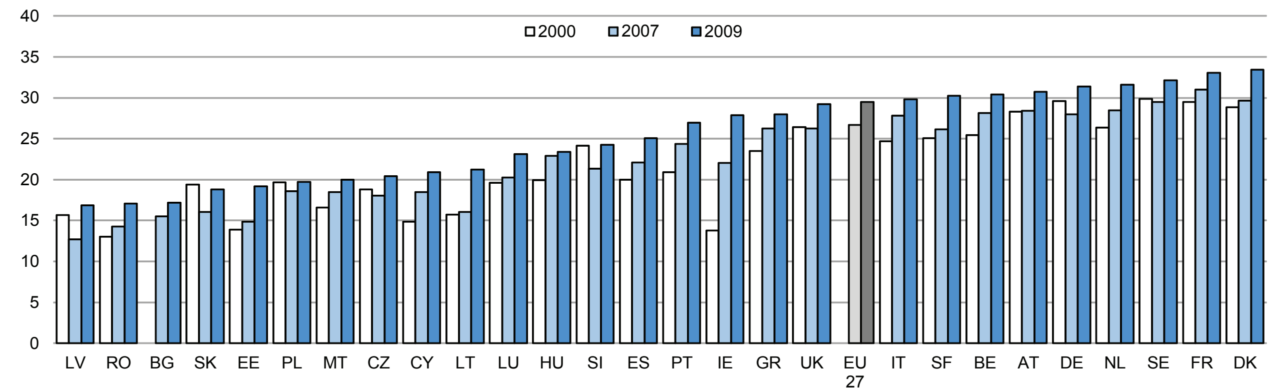
The varying ability of welfare systems to reduce inequality and the efficiency with which they succeed in doing this notwithstanding, there remains an entrenched belief that social protection and tax systems should, to some extent, contribute to mitigating and containing the various forms of inequality created by the market. This is all the more important in a context characterised, as at present, by rising inequality and persistent recession.

This chapter will first of all look at how social protection spending is evolving, after which it will investigate developments in income inequality and how they relate to the variety of social protection systems found in the European Union.

Topics

Social protection spending

Figure 5.1 Social protection spending as a percentage of GDP (2000, 2007, 2009)



Source : Eurostat (2011k).

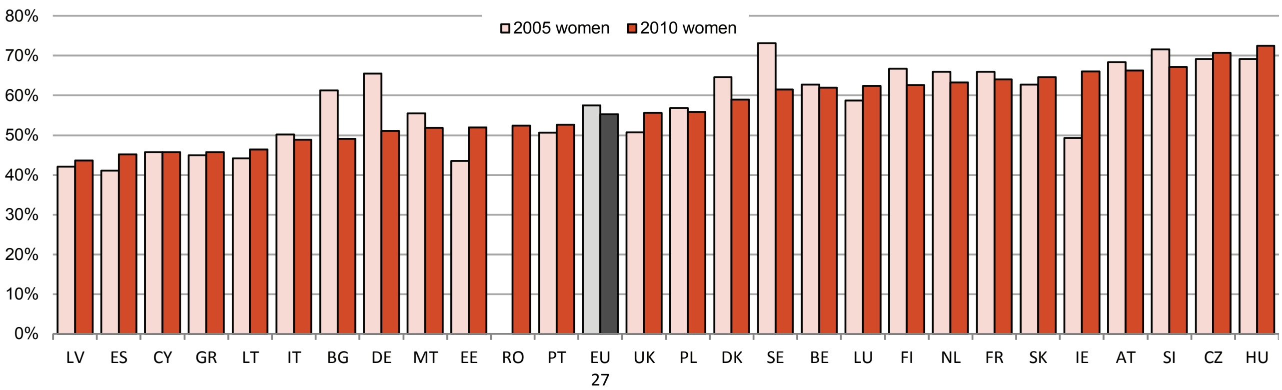
Social protection systems as automatic stabilisers

In 2009 (latest available data) average spending on social protection in the EU as a percentage of GDP stood at a high of 29.5 %, up from 25.7 % in 2007. Over the 2000 to 2007 period, social protection spending had, in a majority of cases, decreased or remained stable, as economic growth had been boosting labour markets and member states were reforming their social protection systems to become leaner (exceptions being Romania, Malta, Cyprus, Hungary, Portugal, Greece, Italy and The Netherlands). As from the onset of the financial crisis in 2008, however, social protection spending rose as a percentage of GDP because the systems had begun to play their role of automatic stabilisers and to provide income security to workers who lost their jobs or saw their working time – and hence their wages – reduced. Accordingly, between 2007 and 2009, social security spending as a percentage of GDP in the EU jumped by 3.8 % points. In the countries hardest hit by the crisis (the Baltic states and also the UK and Ireland), however, the increase in spending was above 5 percentage points as GDP contracted dramatically and spending rose (or in some cases decreased). In Hungary alone did spending as a percentage of GDP rise by less than one percentage point (such a small increase may be attributable either to higher spending, or to a drop in GDP, or to a combination of the two). When examined in absolute terms (i.e. in euros), spending on social protection rose in most EU members states between 2007 and 2009, the exceptions being Hungary, Poland, Sweden and the UK where spending in euros decreased between 2007/2008 and 2009. This decrease may be due either to a pick-up in the labour market (see Chapter 2) or to reforms aimed at cutting spending, the latter being clearly the case in both Hungary and the UK.

Social protection spending continues to vary greatly across the EU member states. About 10 EU member states, mostly central and eastern European countries, spend around or less than 20% of their GDP on social protection (the three Baltic states, Romania, Bulgaria, Poland, Slovakia, Czech Republic, Cyprus, Malta); 9 member states, southern European and English-speaking countries, spend between 20 and 30 % of GDP on social protection (Spain, Portugal, Greece, Italy, Luxembourg, Hungary, Slovenia, the UK and Ireland). The continental European Union and the Nordic countries all spend around 30% of their GDP on social protection, demonstrating thereby the importance attributed by these countries to ensuring security for their population, especially in the case of social risks. The differences in spending may be expected to widen in the coming years as austerity measures will put pressure on social protection spending in the southern European countries.

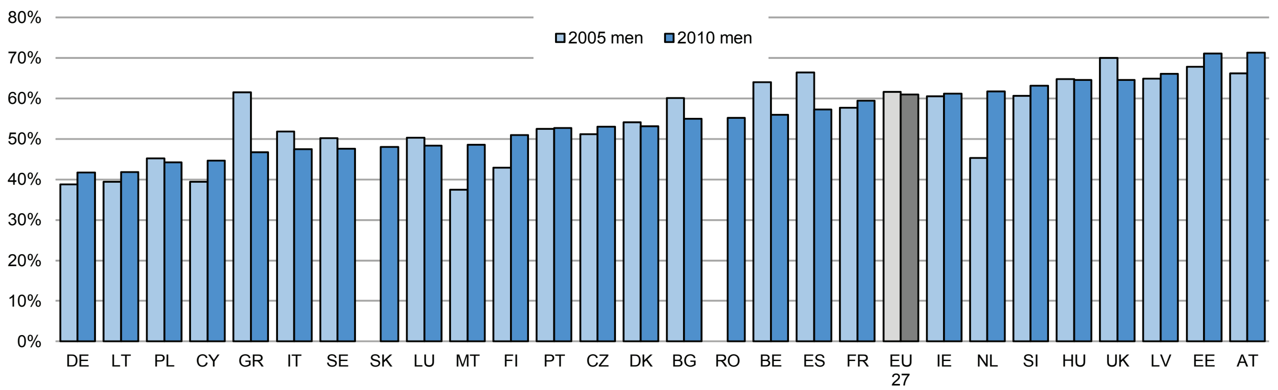
Efficiency of the welfare state

Figure 5.2 Efficiency of tax benefit systems in reducing poverty, women 18 to 64 years, 2005 and 2010



Note: Efficiency of social protection = (poverty before transfers - poverty after transfers) / poverty before transfers.
Source: Eurostat (2011k).

Figure 5.3 Efficiency of tax benefit systems in reducing poverty, men 18 to 64 years, 2005 and 2010



Note: Efficiency of social protection = (poverty before transfers - poverty after transfers) / poverty before transfers.
Source: Eurostat (2011k).

Efficiency of the welfare state

Welfare state efficiency reduced, especially for women

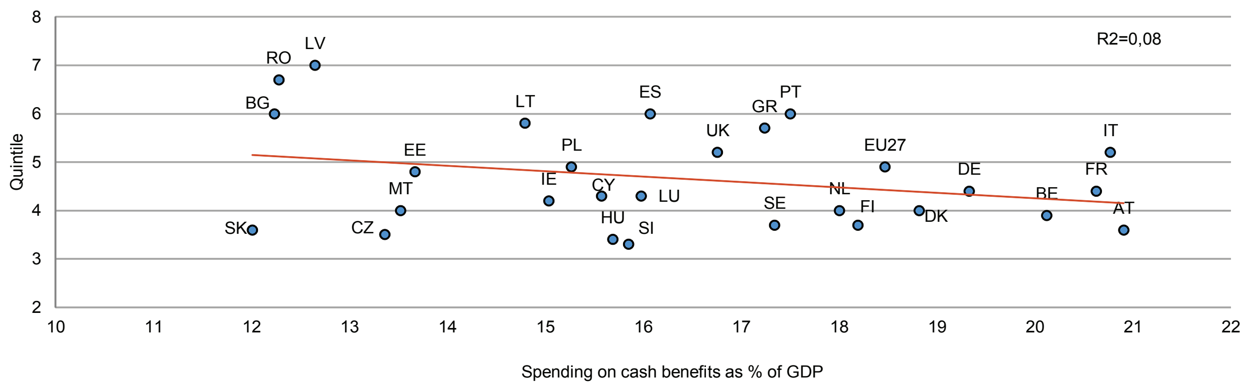
As will be developed in the section on inequality in this chapter (Figure 5.6), inequality has risen across most European Union member states, the reasons for this being manifold. The OECD (2011b) analysis shows that market inequality has been the dominant trend and that, at the bottom end of the income distribution, the main causes have been joblessness, as well as precarious employment conditions, while at the higher end of the income distribution the most important factor has been the increase in capital income. As market-based inequality rises, governments might be expected to 'stem the tide' and use the tax-benefit system to compress and contain inequality. The same study, however, shows that this has not been the case. In seeking to gain an idea of how EU member states have fared in terms of welfare state redistribution, the ability of each member state to reduce poverty emerges as a relevant form of measurement.

Figures 5.2 and 5.3 show us that the capacity of tax-benefit systems to reduce poverty diminished between 2005 and 2010, and that this was especially the case in relation to women. In 2005, the EU27 average for men stood at 62% and in 2010 it was down to 61%, indicating that the tax-benefit system was able to reduce market poverty by one percentage point less. For women the EU27 average was lower and stood at 57% in 2005 and 55% in 2010. Some countries (Hungary, Czech Republic, Latvia, Lithuania, Estonia, Portugal), however, stand out in that their efficiency has increased. From a gender perspective, a worrying trend is appearing as countries – for example, Bulgaria, Denmark and Sweden – that formerly had efficient systems to prevent female poverty have seen large decreases in this efficiency. Furthermore, some of the countries that have increased the efficiency for men have actually decreased the efficiency for women, such countries including Germany, Austria and the Netherlands.

This general trend of becoming less efficient in reducing poverty is attributable to numerous factors; however, it should be noticed that the trends are not necessarily the same for men and women in the respective member states. As permanent austerity seems to be the framework within which welfare states will operate in the medium term, the above observations clearly hint that there is a risk that the current restrictive reforms could lead to far less efficient systems, and particularly in the case of women.

Efficiency of the welfare state

Figure 5.4 Correlation between income inequality for women and cash benefits



Source: Eurostat (2011k).

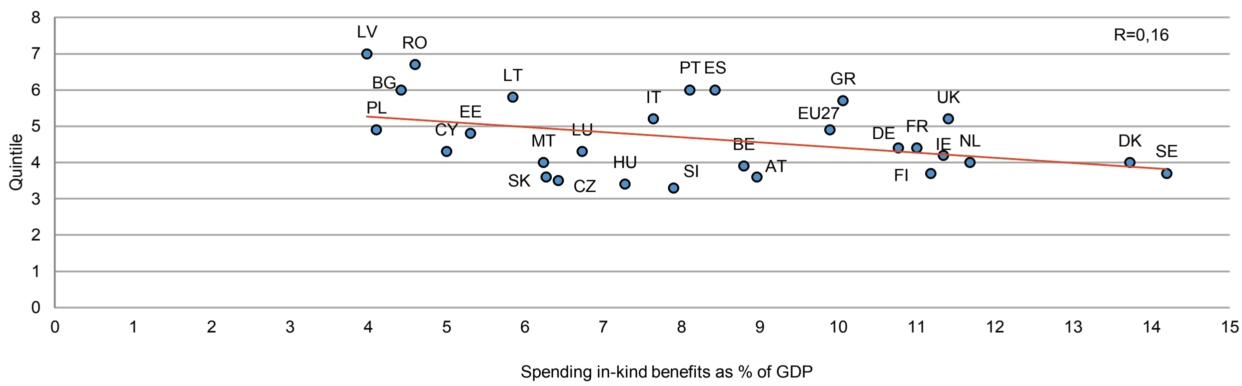
Not only cash benefits matter. Goods and services vital for female inequality

The efficiency of social protection systems in reducing inequality and poverty does not depend only on the amount spent on social protection but also very much on the institutional setting and mix of provisions within the system. As several recent publications highlight (OECD 2011b; European Commission 2012), the tax-benefit arrangements have become less effective in offsetting market-based inequality, the previous section having demonstrated the same phenomenon in relation to poverty reduction, in particular as it affects women. The debate on what an efficient social protection system should look like is a longstanding one (Esping-Andersen and Myles 2009).

Figures 5.4 and 5.5 display the correlation between social protection spending on benefits in cash (money) and in-kind (goods and services). Both Figures display a negative correlation between social protection spending and income inequality for women; this relationship holds also for men. What the figures imply is that the higher the level of spending on social protection the lower the inequality, and this relationship is stronger for in-kind benefits than for cash. In other words, the way in which social protection systems distribute their spending between cash and in-kind benefits is an important consideration.

Efficiency of the welfare state

Figure 5.5 Correlation between Income inequality for women and in-kind benefits



Source: Eurostat (2011k).

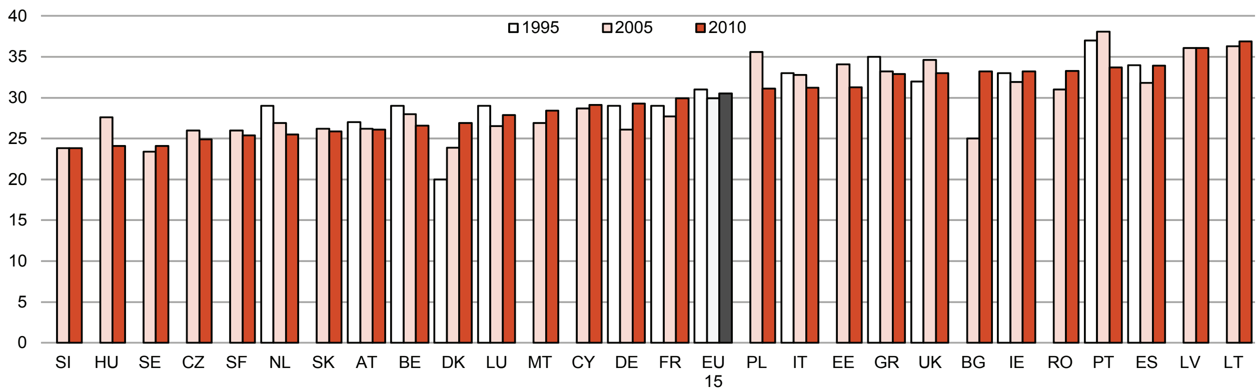
Finding the right mix

The discussion about the set-up of social protection system centres particularly on the question of universal versus targeted forms of provision. Universal forms of provision grant rights to all citizens, for example, and hence cover a large part of the population; targeted provision meanwhile grants rights to a sub-set of the population based on a set of criteria, for example, means-tested forms of benefit. The conclusion reached in Esping-Andersen and Myles (2009) is that if the aim is to reduce inequality, the universal approach is more efficient than the targeted approach, there being two main reasons for this: firstly, targeted systems tend to be less generous and voters are less prone to support high social protection spending; secondly, targeted systems are complicated and often lead to low take-up rates as access is guided by complicated rules, especially for those most in need. The universal approach gains more support from the population and has better take-up rates.

Another debate pertains to the optimal mix of cash and in-kind benefits (goods and services) within the social protection system. Very often this discussion focuses on what cash benefits should be made available, how they should be accessed and what should be their duration. However, goods and services provided by the social protection system are just as important, if not more so, for the purpose of containing as well as offsetting forms of market-based inequality. In other words, the provision of health care, child care (see also Chapter 2), housing (see also Chapter 6), education (Chapter 3), transport facilities, etc. may be said to represent a twofold contribution by, on the one hand, fostering the equal opportunities that will help to limit the formation of market inequality, and, on the other hand, correcting some of the inequality that is unavoidably bound to arise. This finding goes against the mainstream-economist conclusion, namely that cash benefits should be favoured over in-kind benefits as they increase utility.

Development of income inequality

Figure 5.6 The Gini coefficient - Inequality of income distribution



Source : Eurostat (2011k).

Europe becoming more unequal

Income inequalities can be measured in a host of ways, each entailing advantages and disadvantages (compare Chapter 4). The Gini coefficient displayed in Figure 5.6 measures the extent to which equivalised disposable household income is distributed across the population. The Gini coefficient equals zero if the income is perfectly distributed across the population and 100 if all the income belongs to one person; in other words, the higher the Gini coefficient, the greater the inequality. This measure takes into consideration the entire income distribution.

Several recently published publications (OECD 2008 and 2011b; European Commission 2012) emphasise that market as well as income inequality has risen over the past decade. The reasons for this increase, in most EU member states, are manifold, but the most important ones seem to relate to globalisation, technological change, demographic change, and changes in institutions and regulations – in other words, changes in social protection and taxation systems.

Figure 5.6 displays the Gini coefficient for 1995, 2005 and 2010. The figures confirm the above-mentioned studies, as the general trend of the Gini coefficient from 1995 to 2000 was a decrease across the then EU12. In 1995 Denmark had the lowest Gini coefficient at 20 and Portugal, with 37, the highest. In general, the Nordic countries could boast the most equal societies, followed by continental Europe, then the English-speaking countries, with, finally, the southern European countries displaying the most unequal distribution of disposable income. The period from 1995 to 2000 was characterised by a general decrease in, or stabilisation of, the Gini coefficients in all countries. The ranking did not change dramatically. However, the trend in the period from 2000 to 2005 took a quite different course as the Gini coefficient increased in nearly all countries. Especially some of the more equal countries saw a rapid rise in the Gini coefficient; Denmark rose from a low of 20 in 1995 to 24.9 in 2005, Finland from 24 to 26, and Germany from 25 to 26.1. The ranking of countries meanwhile remained more or less the same, with Slovenia, Bulgaria and the Nordic countries showing the lowest degrees of inequality and the southern European and newly joined Baltic countries the highest.

The period from 2005 to 2010 presents a less clear picture, with some countries showing a decreased degree of inequality (Finland, The Netherlands, Belgium, Italy, Poland, Greece, UK, Estonia and Portugal) while others continued to see their Gini coefficient rise. In both Sweden and Denmark income inequality continued to widen, as was the case also in France and Germany (in the latter the coefficient rose from 26.1 to 29.3). Finally, some of the most unequal countries – for example, Spain and Ireland – became even more unequal. As a result of these highly diverse trends over the most recent period, the ranking of countries with regard to their Gini coefficient has altered as compared to the past decade. Some of the traditionally equal countries, Denmark and Germany, have moved down the ranking towards the English-speaking countries, while the central and eastern European countries, in particular, have moved up the ranking. However, inequality has, on average, increased, the increase being a combination of labour-market-based inequality and the outcome of reforms that have taken place in the welfare state (OECD 2011b).

Conclusions

Not less, but more social spending is the answer to crisis

Social protection spending has risen as a percentage of GDP in all EU member states; in the countries hardest hit by the crisis this increase has exceeded 5 percentage points. However, this increase in spending expressed as a percentage of GDP did not translate into an increase in spending in absolute terms. Poland, Sweden, Hungary and the UK actually spent less money on social protection; in the latter two countries in particular, this is a clear effect of austerity measures implemented at the onset of the financial crisis. The figures on spending for 2010 and after could, as they become available, confirm this trend for most EU member states as the austerity measures start to take effect.

The pressure on social protection spending gives cause for concern on two main counts. Firstly, inequality has, generally speaking, risen right across the European Union; secondly, the welfare state has, over the past decade, become less efficient in terms of off-setting, or providing the framework for lowering, market-based inequality. This trend seems to be more marked for women than for men.

Hence, at a time when equality in its many forms is on the rise, there is tremendous pressure to decrease government spending on social protection. If social protection systems are to adapt and regain their former degree of efficiency in limiting inequality and decreasing poverty, spending cuts cannot be the answer; it is vital rather, on the contrary, that social protection be beefed up and able to provide the security for social risks as well as essential goods and services for the wellbeing of the European Union's population. Furthermore, achievement of the Europe 2020 target of reducing poverty (see also ETUC and ETUI 2011) seems very distant and difficult to attain on the basis of current trends in social protection spending and reforms. Inequality and poverty cannot be dissociated, for they go hand in hand.