

# Economic Governance in the Eurozone and the EU: Drawing lessons from the crisis

Cape Sounio, Athens, Greece, 10-13 June 2010<sup>1</sup>

## Session 4: Political and social consequences of the crisis

### Social policies after the crisis

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#### Questions addressed at the request of ELIAMEP:

Does the crisis necessitate a renegotiation of the domestic social contract in individual member states?

If so, then what may be the role of the EU in all this?

#### Background

It is already abundantly clear that the aftermath of the crisis will pose profound questions about the future of social policies. On the one hand, intensifying pressures on public finances will lead many finance ministers to demand sizeable cuts in budgets and it is inevitable that welfare spending, especially, will face uncompromising scrutiny. On the other hand, the severity of the economic downturn must be expected to aggravate many social problems, reverse some of the achievements of recent years and give rise to new difficulties. In addition, long-run societal and demographic changes are occurring which, while well-known, have been only inadequately addressed hitherto, and will demand action sooner rather than later.

There are manifestly different economic, social and employment models in the EU, yet many of the challenges that have to be confronted are common to all Member States, so that an EU role in analysing and co-ordinating policy responses is warranted. However, there are also big differences in what is in need of reform, raising questions about whether there should be a common reform agenda. In some cases, components of national models have been stretched to breaking point and will

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<sup>1</sup> With the support of the Lifelong Learning Programme, Jean Monnet Actions of the European Union Education, Audiovisual & Culture Executive Agency. This project has been funded with support from the European Commission. This publication reflects the views only of the author, and the Commission cannot be held responsible for any use which may be made of the information contained therein.

need to be reconfigured. Elsewhere, the problems are of a much lesser order of magnitude and the targets of, notably, the Lisbon strategy (and, now, Europe 2020) are either already attained or close.

In addition, capacities to change, systems of governance and receptiveness to reform differ substantially because of the way in which economies and the configurations of interests within Member States have evolved over many decades. It follows that care will be needed in defining an EU role, implying a mix of leading, monitoring and supporting what national actors do, while recognising the primacy of the national level.

A general presumption is that the average skill needs of the jobs of the next decade will increase, but the distribution of skill demands may shift. At the top end of the range, knowledge-related skills will be in high demand, but so too will a large raft of relatively low-skilled jobs in areas such as personal care, security and retailing. Education and skills policies have to be responsive to these emerging shifts in demand and a shift in thinking that will be required is away from the conceptualisation of the median job as one filled by a full-time male in an industrial occupation. Rather, the median employee ten or twenty years hence could well be a woman working part-time in the care sector.

### **Must national social contracts be renegotiated?**

The interactions of short and long term trends will have uneven effects on different Member States of the EU. These will depend, initially, on the ‘shape’ of the recovery from crisis: will it be the favoured ‘V’ in which the rebound rapidly restores business-as-usual; the ‘U’ with a more extended period of stagnation or its cousin the ‘W’ with a brief double-dip before recovery materialises; or the more debilitating ‘L’ with its connotation of a Japanese-style lost decade. How soon ageing kicks-in will be pivotal, since it entails not just review of pension and care funding, but also some delicate choices on labour supply, while the need to reverse the decline in competitiveness in many Member States is going to require tough decisions on pay and on means of bolstering productivity.

Many of the immediate social effects of the crisis appear to represent an undoing of a decade of national social policy efforts, subject to EU policy co-ordination. Employment rates (which had been rising, if not quite to the Lisbon strategy’s 70% target level) have fallen, youth unemployment has soared, social exclusion is being accentuated and the risk of poverty is again rising. A direct policy challenge is how to forestall segmentation of labour demand that exacerbates some of the adverse effects of the downturn on target groups such as youths and older workers. The answers are known: avoid long-term unemployment and the debilitating detachment from the labour that it engenders; ensure that those most remote from a job have pathways towards one; and equip the individuals affected with the attributes that will make them employable.

In addition, reining-in of the public sector will mean that many cherished areas of social spending will face cuts and demands for new means of delivery. Where sizeable reductions in public debt are required, the extent of the renegotiation of social contracts will inevitably be greater because existing entitlements will have to be clawed-back. The swingeing public sector pay cuts already imposed in Ireland, Greece, Latvia, Portugal and Spain (and increasingly in the pipeline for many other Member States), together with measures to curb pensions, have largely been presented

as devices to achieve deficit reduction, but they will have to be entrenched to restore the long-run sustainability of public finances, especially under the shadow of ageing. In both employment and social policy, there will be strong pressures to do more with fewer resources. This will mean, notably, that cost effective measures will be sought, and that careful judgments will be needed about the virtues of different approaches. It also implies that administrative or regulatory solutions will seem more attractive than spending.

There is still unfinished business in many Member States in undertaking reforms of the welfare state, partly because the years of plenty prior to the crisis allowed vested interests to resist change, but also because the necessity of change was less apparent. It is hard to see how an intensification of social reform can be avoided as countries have to make up for lost time.

Consequently some renegotiation of social contracts is inevitable just for budgetary reasons. However, there are wider imperatives that will also impinge on social contracts. The most significant concerns the shift from social protection to social investment in the underlying thrust of the welfare state. There are several watchwords in this shift: active supplants passive; rights are balanced by responsibilities and obligations, notably to accept training positions or less attractive jobs; and there may also be a switch from unquestioning solidarity to greater conditionality and means-testing.

### **The EU's role**

Despite the many governance and policy innovations of the last decade, the role of the EU in shaping national social policies remains tentative. According to scholars such as Fritz Scharpf, the lack of a genuine social Europe can be explained by the reluctance of governments to cede powers to regulate the market or to shape welfare provision. Indeed, Scharpf argues that once the choice was made in the 1950s to opt for 'negative', market integration rather than the politically more difficult path of 'positive' integration, the prospect of social integration was killed-off. Yet others, such as Maurizio Ferrera and Stefano Sacchi see justifications for a more social EU because it would help to legitimate European integration, as well as for reasons of social justice and economic efficiency. But it is not enough just to find a rationale, as the case for a social Europe also depends on why and how it is advanced.

The incorporation of a social pillar in the EU approach to sustainable development points to a possible new approach to establishing a social Europe, . A key consideration is that a delicate political and policy balance is needed, especially for social market economies, in adapting to the rapid and extensive shifts in the economic and social environment. However, although climate change and wider environmental concerns are increasingly in the mainstream, 'social' sustainability is more complex.

Prior to the onset of the crisis in 2008, flexicurity had been pushed as both a model for EU Member States in recasting their social agenda and as a toolkit for change. The rise of flexicurity coincides with an intellectual debate on the role of welfare systems, in which a shift of emphasis from a protective role towards an emphasis on social investment became increasingly pervasive in the functioning of welfare states. Indeed, Peter Taylor-Gooby maintains that in its idealised form, the social investment approach to welfare can bring together economic and social objectives in a self-reinforcing manner. However, he also notes that the practice falls short of the rhetoric,

implying that rather than social investment, what has happened is ‘negative activation’.

The question post-crisis is whether this reorientation was a brief flourish based on ‘neo-liberal’ ideas that have now been debunked and discredited, or whether instead it is here to stay. Judging by what is in the Europe 2020 proposals, the latter is the answer, though with some rebalancing between the protective and investment functions. Central to the approach is how extended periods of unemployment or (increasingly in some models) inactivity can be avoided, and there is considerable interest in the means by which countries like Denmark and the Netherlands have achieved sustained increases in employment rates. In addition, the investment focus can be seen as consistent with the contention that employment is the best route out of poverty, with human capital as the key variable. Countering persistent poverty and its inter-generational transmission are also part of the narrative.

Soft law processes such as those that have been applied to employment and social policies over the last decade have often been criticised, but perhaps because of unrealistic expectations and a misunderstanding of their aims. Their advantage is that they provide orientations to national policies without the heavy-handed application of legal restrictions, yet their impact may still be profound in shifting the thrust of social policy and the architectures of social systems. These impacts are cognitive as well as procedural. The flexicurity turn in policy, for example, can be seen as a template and a goal for Member State policies: while the logic of the open method leaves implementation firmly with Member States, it suggests an ideal-type towards which Member States should gravitate, with the implicit corollary that those which make the least progress, need to do most to shift towards the model.

Prospective EU roles can be defined telegraphically as follows:

- Establishing the broad contours of a modernised social model, though with all the usual caveats about the need to respect diversity and national traditions.
- Facilitating policy learning through the toolkit of the open method of co-ordination, while also stimulating experimentation. Relevant instruments and processes include benchmarking and targets, as well as structured procedures for mutual learning. Where possible these processes can help to identify bad as well as good practice.
- Monitoring and scrutiny of Member State policies, leading to recommendations about remedying shortcomings.
- Supporting approaches to governance that underpin reform. It is important to stress that these can be at both EU and national levels and will entail a mix of hard law and co-ordination.

The widespread experimentation with schemes to preserve jobs over the last two years and to put in place imaginative approaches to activation and job creation points to the importance of redoubled efforts to share and draw on the knowledge that is being generated. But co-ordination is only as good as the willingness of governments to listen and to be receptive to new approaches. Several areas of EU policy are ripe for a fresh approach, including an EU-wide policy on immigration, the refinement of flexicurity and renewed drives to promote quality of work and equal opportunities.

## **Concluding remarks**

The budgetary arithmetic, the emergence of new demands on social policy and the likely legacy of the crisis mean that the status quo in social policy will not be an option. It follows that domestic social contracts will have to evolve, in some cases quite radically.

The EU can play an important enabling role, both in setting directions and in encouraging change, but its role will remain an arms' length one and it is still hard to see circumstances in which it becomes a direct provider or funder of social policy.

A template around flexicurity is the likely way forward, but considerable sensitivity is needed in fitting the model to the circumstances of Member States. It also needs to be developed to take more account of flexibility from the standpoint of the worker as well as the employer, while reconciling the redistributive and security-orientated aspects of social protection with the social investment role.