EU Today Podcast 10 Transcript

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[Intro music in theme of piano playing Ode to Joy]

Katie Lindner: Hello, and welcome to EU Today, a podcast from the Center for European studies, a Jean Monnet Center of Excellence at the University of North Carolina at Chapel Hill.
Thank you to the Erasmus+ program of the European Commission, the EU Delegation to the U.S., and the U.S. Department of Education for supporting our center and its programs. On this podcast, we sit down with scholars and policy leaders to discuss pressing issues facing the EU. We hope you enjoy it.

Brett Harris: Hello, and welcome to EU Today. My name is Brett Harris, and I am a Contemporary European Studies major at the University of North Carolina at Chapel Hill. In this episode, I will be interviewing the Jean Monnet Center of Excellence Key Staff Members and UNC faculty Dr. Evelyne Huber and Dr. John Stephens.

Evelyne Huber is the Morehead Alumni Distinguished Professor of Political Science at UNC. She has contributed articles on social policy and political economy in the EU and Latin America to leading journals in political science and sociology. She received an Honorary Doctorate from the University of Bern in 2010.

John D. Stephens is the Gerhard E. Lenski, Jr. Distinguished Professor of Political Science and Sociology at UNC. He is also the Director of the Center for European Studies, a Jean Monnet Center of Excellence, which houses Transatlantic Master's program. He is also the Chair of the Contemporary European Studies Major at UNC. His main interests are comparative social policy and political economy, with area foci on Europe, North America, and the Antipodes.

Together, Drs. Huber and Stephens are authors and Co-authors of five books, including *Capitalist Development and Democracy* (with Dietrich Rueschemeyer); *Development and Crisis of the Welfare State*; and *Democracy and the Left: Social Policy and Inequality in Latin America*, all winners of book awards.

In this episode, Drs. Stephens and Huber discuss different models and outcomes of welfare states, as well as their ongoing project, *Increasing Inequality in Post-Industrial Knowledge Economies.*

[Ode to Joy fades back in and plays for appx. 4 measures]

Brett Harris: Hello and welcome to EU Today! My name is Brett Harris, and today we are welcoming Dr. John Stephens and Dr. Evelyne Huber from the University of North Carolina at Chapel Hill. Thank you both for joining us today! So, you both have been working on this project, *Increasing Inequality in Post Industrial Knowledge Economies*, for quite some time now. What is the state of the research now and what are your preliminary conclusions?

Dr. John Stephens: I'd like to start by defining the states that we're looking at. It's the universe of economically advanced democracies in North America, Europe, Australia, New Zealand, and Japan, so 21 countries altogether. In these countries, inequality fell from a high in the late 1920s, to a low in the mid 1980s, and then it's begun to increase again, in some countries modestly and others like the US more steeply. We are trying to figure out both why these countries all moved in the same direction at the same time, and why they do so at varying speeds—some with greater increases in inequality, and others with only modest increases in inequality.

Dr. Evelyne Huber: So, when we study income inequality, we have to look at wages and salaries and capital income on the one hand, what we call market income, and at redistribution through taxes and transfers, or what we call the welfare state.

Brett Harris: Great, thank you! So, in your research, you mention different types of welfare states. Could you elaborate on what defines a welfare state, and what variations differentiate the different models you're interested in?

Dr. Evelyne Huber: Right. This could take an hour, but we'll try to make it pretty concise! So, the welfare state: it is the totality of transfers—money transfers—and free or subsidized social services provided by the state. So, it includes pensions or what we know as social security [in the US], social assistance, food stamps, public housing, but also health care and education. Now, all affluent post-industrial democracies have welfare states, but they differ significantly in their types of welfare states. We generally distinguish four different types:

(1) There are Social democratic or Nordic welfare states; (2) Christian democratic, or Bismarckian, or Continental welfare states; (3) Liberal, or residual, or Anglo-American welfare states; and (4) fourth, Southern European welfare states. Now, they differ in generosity and in the redistributive profile—that is: how egalitarian they are in their benefits— and in how much they provide in terms of social services. So, the most

generous and redistributive and service-oriented welfare states are the Nordic, or Social Democratic welfare states. Their benefits are universalistic in the sense that they cover everybody, and they do so with generous pension systems, for instance; they have generous unemployment insurance; they have free health care for everybody; they have free education at all levels; and they have free or subsidized child care and elder care. So, they really have taken on a bunch of care responsibilities which makes it much easier for parents, particularly mothers, obviously, to combine work and family.

The Continental welfare states, which we call Christian Democratic welfare states—and we'll get to why they got these names in a little bit—those welfare states are about as generous on transfers and they spend roughly equal amounts, but the transfers are less universalistic and redistributive. Different groups get different types of benefits, and in particular, they provide fewer services; they finance a number of social services, but those are typically privately provided. So particularly childcare is a very important example.

Then we have the Liberal, or what we call residual, Anglo-American welfare states. They are called residual because they really just take care of the very needy that are not taken care of by family or the market. Now that is not entirely true for all programs in all countries. For instance, in the US, social security is the most generous part of the welfare state, and in Britain, of course, we have universal healthcare. But as a group, they spend the least, and they are the least redistributive. A lot of their benefits are actually means-tested, and as I said, they neither finance nor provide many social services but leave them to the market, and private education plays an important role.

And finally, we have the Southern European welfare states, which were most of the late-comers—particularly Spain, Portugal, and Greece—they really only developed their welfare states to a meaningful extent after they became democracies. They show a mixture of the Continental pattern in their transfers and the Nordic pattern in their health services. Several of them have universal public health services. In terms of care services, they continue to rely very heavily on the family for care services. So, we sometimes also call them familialistic welfare states.

Brett Harris: Thank you. So, there's a lot of variation between those—what reasons are there for these differences and variations between welfare states?

Dr. John Stephens: These welfare states were constructed over a long period of time—the first modern social policies were passed in Germany in the 1880s, but if we look at their overall development, you can say the three or four decades after WWII were the period of rapid development of these welfare states across the groups of countries. And if you look at the dominant political force, then you will understand what kind of welfare state they have. The reason we call the Nordic welfare states the social democratic welfare states is because the Social Democrats and their allies were the dominant political force in those countries between 1945-1985. In continental Europe, it's the Christian Democratic parties that were dominant, in most cases. Sometimes Christian Democratic/Social Democratic alliances were often in government, but it's mostly the Christian democratic or Catholic ideology that shaped their welfare states and implemented these policies. In the Anglo-American countries they were governed by primarily center right and centrist secular parties, and so these broad party families are what really imprinted and led to the variation. So, if you look at the variation of these welfare states in 1950; they were not very different from one another, and then if you look at them in 1985, they're very different.

Brett Harris: In what ways does the type of welfare state impact how inequality manifests in that state?

Dr. John Stephens: So, as we just discussed, the welfare state is there to reduce poverty and inequality resulting from market income via taxes, transfers, and the provision of public services. Now, the welfare state has a big role in shaping market income inequality to begin with, largely through support for education and training—that is, skill training. The other factors that shape market outcomes are labor market institutions.

Dr. Evelyne Huber: Right, so let's have a closer look at labor market institutions. The central role is played by unions and the collective bargaining system, and these vary greatly between countries and the patterns roughly correspond to the welfare state types. In the Nordic countries, unions are very strong, organizing still more than 60% of the wage and salary earners — so, it is not surprising that unions have historically been—and still are—a major voting block for social democratic parties. So, it's that alliance that has both built the welfare state and the system of industrial relations, and they work in tandem, basically, to produce more egalitarian outcomes. In the Continental countries unions organize between 20 and 30% of the wage and salary earners; and in the US, for instance, only about 11%, so those are really enormous differences. Now, historically, in all these countries, unions were stronger forty years ago. There was a time when unions were relatively strong in the US as well. So, unionization has declined everywhere, but very important differences persist.

A second important aspect in a labor relations system has to do with legal contract extension—in other words, contracts negotiated by unions and employers are extended to non-union members. Contract coverage in the Nordic countries reaches between 80% and 90% of the wage and salary earners. So, that's the overwhelming majority, and people who are eligible to be covered by a negotiated contract—they are covered. In the Continental countries it varies from 60% to 90%.

Again, by contrast, in the United States contract coverage is less than 15% of wage and salary earners. So clearly, that makes for very different dynamics in earnings distributions. Also, in many Nordic and Continental countries there are works councils—that is, there is legislation that establishes work councils—that represent labor interests at the enterprise level. The powers of works councils vary depending on the country. In some countries they are mainly consultative, but in others they actually have codetermination rights on things such as wages and working conditions, for instance if there have to be adaptations to economic downturns, such as short work weeks, and so on and so forth. At any rate, we're talking about an institutional co-representation of labor which clearly represents the interest of labor vis a vis top management and basically shareholders.

So, let's look at some figures as to what has happened to poverty and inequality since 1985.

Dr. John Stephens: Now, if this was a video, we could show you a bunch of graphs and tables, but its not. So rather than showing you what's happening in all of these countries in so many measures, we're just going to give you a few examples.

And so, let's start with the US. This is the country where you had the biggest increase in inequality. All these figures I'm going to give you are for 1985 and 2015. In that period, the share of US income that accrued to the top 1% of income earners in the US rose from 12% to 20%. In terms of poverty, the market income poverty (pre tax and transfer poverty) rose from 17% to 21%, and poverty after taxes and transfers, so after the welfare state, rose from 11% to 15%. So, in this whole period of 30 years, real median household income increased only .5% per annum. At the same time, economic growth was 1.7% per annum. So, this means that the upper income earners were reaping most of the benefits of economic growth in the US over that period of 30 years. I just gave you the top 1%, but overall measures of inequality like the Gini index have the same patterns.

We can contrast this to a couple of European countries. The top 1% in Sweden increased from 5% to 8.5% in the period 1985-2015. In Germany, the top 1% income share increased from 10% to 13% of national income. So still increasing, but much less. In Sweden, the annual average increase in median household income was 2.6% (compared to 0.5% per annum in the US). So, the average Swedish household was getting better and better off every year, in contrast to the average American household, which was practically stagnant. The medium income growth in Germany was much lower than in Sweden. Now, a lot of this is due to the fact that our first date was in 1985, and then you had reunification of the much poorer East Germany with West Germany, but you still had 0.9% per annum increase in median real household income, which is almost twice that of the US. Post tax and transfer income poverty increased from to 5% to 11%. So, in Germany, the big increases in inequality are really at the bottom, so the low-wage market expanded quite a bit, which is why you have that increase.

Brett Harris: So, across the board, like you mentioned, we see these increases—what are some of the underlying reasons for these increases?

Dr. Evelyne Huber: So, we have several. We have structural economic changes, we have demographic changes, and then we have declines in labor strength, and particularly in unionization. So, let's start with structural economic changes. All of these countries experienced deindustrialization and thus the loss of well-paying jobs for people with low or medium skills. Now, deindustrialization is partly due to technological change, and partly due to import competition. So, if we look at technological change, or the transition to the knowledge economy, what we see is increasing demand for people with high skills. And basically, few jobs are created in advanced branches of the economy for people with low skills. In other words, the jobs are being created in personal services: restaurants, beauty parlors, bars, you name it. So, low-skill/ low-wage jobs are being created in sectors where people spend their money who are participating in the knowledge economy in high-skill/ high-income jobs. If you have increasing demand for people with high skills, then they will be able to command a greater remuneration, a greater return on their skills, unless the supply increases at the same rate. And that then would require—and we will come back to this in a little bit—a lot of investment in education. There is a widely cited book by Claudia Goldin and Lawrence Katz which makes precisely that argument—that the US has been losing the race between technology and education; that is, for the past five decades the US has not invested enough in education to keep up with the rising demand for education in the labor market, and therefore we have this increasing inequality. That's really part of the story, but it's not the whole story.

So, as I said, there are a lot of jobs being created in the service sector, but those jobs are notoriously unstable and low-paying. So you have what we call a dualization of the labor market. On the one hand you have people with stable, relatively well-paying jobs, and on the other hand, you have people with a precarious attachment to the labor market—temporary jobs, part-time jobs, typically without benefits, poorly paid, and so on and so forth.

So, a lot of people also point to globalization, particularly trade competition, outsourcing, and immigration. And we clearly know that these things are going on, but the results of our econometric analyses are not really robust for these variables, meaning that technological change and deindustrialization are the key factors.

Then we have demographic changes. We have a greater proportion of single-mother families. And single mother families are notoriously vulnerable to poverty.

It's hard to take care of kids and work at the same time, particularly in countries without extensive childcare. These developments help explain common trends toward greater inequality, but other developments differ more across countries. So, as I mentioned before. Decline of union density has been universal but particularly strong in the Anglo-American countries. Moreover, other aspects that strengthen labor, such as contract coverage, which are high in the Nordic and Continental and even the Southern European countries, have not declined very much. We can see this impact very clearly in the growth of the share of the top 1% that John just talked about; strong unions and other aspects of labor strength, like works councils, in our econometric analyses are shown to reduce the income share of the top 1%. The runaway incomes at the very top are primarily a phenomenon of the Anglo-American countries, where all of those aspects of labor strength are very low.

Dr. John Stephens: I just want to make it clear here—Evelyne is talking about our econometric analyses—this is our data analysis for this book. The quantitative part, we are just about finished with.

Another key difference across these countries is the skills distribution. European education and training systems do a better job increasing skills at the bottom. So, when you have better skills at the bottom, you have better pay at the bottom. With the advent of the knowledge economy it is particularly the Nordic countries that have distinguished themselves in investing in lifelong education and training and thus have improved skills levels on the average and particularly at the bottom. We see this very clearly in the OECD's Program for International Assessment of Adult Capabilities. It shows that particularly the US and the other Anglo-American countries have skill levels at the bottom 5% that are much worse than they would be in the continental European states, which is not as good as they would be in the Nordic countries. So, one of the reasons that you have lower income inequality in the Nordic countries is investment in skills. If you add up spending on daycare, all levels of education, and active labor market policy, the Anglo-American countries spend about 5.5% of GDP on these investments skills, while the Nordic countries spend about 10% of GDP on those education and training programs.

So, market income inequality has increased in every country, but to different degrees. The same is true for market income poverty. Welfare states everywhere reduce poverty and inequality, but they have not been able to keep up with the increase in market income poverty and inequality, and as a result, disposable household income poverty and inequality have gone up everywhere, though levels continue to differ. In the European countries, the EU austerity policies have been an important brake on the ability of welfare states to counteract this increase in market income inequality; in the United States it has been domestic politics, with repeated significant tax breaks for corporations and upper income groups, and a failure to invest in the skills—that's the race between technology and education over the past four or five decades.

Brett Harris: Thank you for sharing. We're about ready to wrap up—are there any last thoughts either of you two would like to share?

Dr. Evelyne Huber: Just that, in a lot of public discourse, people say, "oh well, it's globalization; it's trends that one can do nothing about; and that's what's behind inequality: transition to the knowledge economy." Well, yes, those things are important, but there are policy choices that can be made that can mitigate the inegalitarian effects of structural changes. And in order for these choices to be made, you need to have the appropriate political alliances. In other words, you need to have the political parties, and groups in civil society that work together to push for those trends.

Dr. John Stephens: If you look at the economics literature on the increases in wage inequality and overall income inequality, what you see written all over the place is "skill-biased technological change." So, we have this transition to the knowledge economy, and we have certain semi-skilled jobs, basically assembly line jobs, which were well-paid, and they've gone away. And there's a swath of workers who fall behind. But it's important to underline, as Goldin and Katz did in their 2008 book, *The Race between Education and Technology* that Evelyne referred to previously is that for the first 75 year of the 20th century, the US was winning the race between education and technology, expanding secondary education until it became universal, and then expanding tertiary education, and then all of the sudden, around 1970, we stopped doing that. So, if you look in 1970 at the percentage of GDP that goes to education, the #1 country in the world is Canada with 8.6% of GDP. Tied for #2, were the US and Sweden at 7.2% of GDP. Now the US is at 5.5%, and Sweden is still up at 8%. So, it's a choice we made not to invest in people's skills and the expansion of public education, and that's the point of their book. And so, when people say "skill-biased technological change," they forget that there is a political side to it, and that is the supply side. If we would invest the same amount as the Nordic countries do in people's skills we would have more equal outcomes, especially for the people at the bottom.

Brett Harris: Definitely! Well, thank you very much for the very thought-provoking lecture, and thank you everyone for tuning in!

[Ode to Joy plays in the background]

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[Ode to Joy fades out]

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