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# ISEO Summer School 2016

THE WELFARE STATE

The Welfare State, Redistribution & The Crisis

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# Agenda

Back to Redistribution Debate

The Welfare State & Redistribution

The Welfare State and the Crisis



# The Welfare State & Redistribution

- Together with social inclusion, poverty alleviation, employment promotion and overall protection against the ‘five giants’, welfare states have aimed at reducing income disparity (especially in Europe).
- Hence, in a context of growing income and wealth inequalities, it is important to go back to the basics and clearly understand the mechanisms through which different welfare states redistribute (opportunities and outcomes).
- We move beyond the traditional comparative social policy literature by also considering the economic analysis of Piketty and the ‘rational’ ground in favour of equality provided by Wilkinson in *The Spirit Level*.
- In the last part of the lecture we will also analyse the effect of the current crisis on the welfare state



# Agenda

Back to Redistribution Debate

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# Back to the Redistribution Debate (1/2)

- The distribution of income & wealth is a hotly debated topic
  - Moral ground
  - Rational ground
- In this big debate, Piketty's work has been the main collector of attention, however other important works have been proposed by scholars such as Stiglitz, Krugam & Wilkinson (*The Spirit Level*)



## Back to the Redistribution Debate (2/2)

- The discussion on the ‘proper’/‘right’ distribution of income & wealth is too important to simply be left to academics
- Increasing inequalities in the western world are due to political, economic & financial changes (a sort of great transformation to use Polanyi’s jargon)
- Too much micro-analysis in academia (methodological individualism) and we forgot the macro-context, and the man that inhabits it
- Talking about inequalities is in a way a means to re-humanize the social space



# The Four Questions Proposed by Piketty

- (1) What do we know about income and wealth distribution over the last 200 years?
- (2) Have the dynamics of capital accumulation really led to the concentration of wealth in few hands as Marx postulated in the 19<sup>th</sup> century?
- (3) Or, are the forces that counter-balance this trend such as growth, competition and technological progress, bringing down inequalities and increasing harmony among social classes as argued by Kuznet in the 1950s?
- (4) What lessons can we draw from the evolution of the concentration of income and wealth, in order to understand the world in which we live in?



# Piketty's Provisional Answers

- Massive collective data collection
- Credit to Marx (without going within Marxist theory at all)
- Proposition of a global wealth tax to reduce the polarization of wealth





# The Mechanisms of Wealth Polarization (1/5)

- According to Piketty the ‘Marxist apocalypse’ has been avoided thanks to economic growth, social mobility & the rapid diffusion of knowledge
- After the 1970s the scenario has changed because:
  - The rate of return of capital is constantly higher than GDP and wages growth
- Similar situation to the 19<sup>th</sup> century
  - > A situation which is conducive to more and more inequalities



## The Mechanisms of Wealth Polarization (2/5)

- If the rate of return of capital is superior to economic growth, the investments will continue to concentrate on financial speculation and not on the economic sectors which create new jobs
- Capital owner will cumulate more wealth and people that live simply of their salary will struggle more and more
- What about democracy? What about political legitimacy? What about merit and the incentive to work?
- We are going back to a stage of capitalism in which the rent dominates work



# The Mechanisms of Wealth Polarization (3/5)

- When economies grow slowly, the wealth cumulated in the past acquires more relevance, because only a limited flux of new savings can increase the stock of wealth available
- Political choices have reduced the importance of the forces that were reducing income and wealth polarization



# The Mechanisms of Wealth Polarization (4/5)

The Great transformation:

- Individualism & neoliberalism
- A monetary integration without solidarity
- The lack of adaptation of the WS
- The position of social democratic parties



# The Mechanisms of Wealth Polarization (5/5)

- Proposition of the wealth tax (simplistic)
- What about the other types of inequalities?
- What about the welfare state?



# Defining inequalities

- Inequality of treatment, i.e. NSR and old welfare
- Inequality of opportunity, i.e. education
- Inequality of condition, i.e. income & wealth (Piketty's discussion focus solely on this aspect)



# Agenda

Back to Redistribution Debate

**The Welfare State & Redistribution**

The Welfare State and the Crisis



# Why redistribution is important?

- (1) Piketty's argument: accumulation of wealth destroys the incentive to work
- (2) Socio-political mechanisms: stability and efficiency of governments, legitimacy
- (3) Educational Mechanisms
- (4) The Spirit Level Argument: equality = better socio-economic outcomes
- (5) Increase social productivity
- (6) Facing the crisis (beside austerity): redistribution within and across countries





# The Welfare State & Redistribution (1/6)

- Because it taxes and spends, the welfare state is by definition redistributive, but this does not automatically entail that it creates more equality
- The Welfare State: insurer & redistributor
  - According to Barr the Welfare State is a piggy bank designed to insure against social risks and therefore not a vehicle for equality
  - and a Robin Hood to the extent that it aims to ameliorate need and poverty or, more generally, reduce welfare disparities
- The balance between the two functions dictates in great measure the equalizing impact of redistribution



# The Welfare State & Redistribution (2/6)

- Distinction between: (1) horizontal, (2) vertical & (3) between-group redistribution
  - (1) Social insurance is primarily designed for horizontal redistribution, seeking to reallocate income across the life-cycle
  - (2) Vertical redistribution is the Robin Hood role, taking from the rich to give to the poor
    - The degree of vertical redistribution is given by the progressivity of the tax system, and by the degree to which social expenditures go disproportionately to the least well off (social assistance is a typical example)



# The Welfare State & Redistribution (3/6)

(3) An example of inter-group redistribution is the national health care (which implicitly redistributes between the healthy and the ill)

- All three dimensions are based on how the welfare state alter the market-based income distribution
- However, no country with a welfare state has a ‘true original income distribution’ because policies affect directly and indirectly its shape



# The Welfare State & Redistribution (4/6)

- They do so in two ways:

(1) The welfare state artificially creates substantial inequality because it produces large populations with zero market income

- i.e. pensioners or women on maternity leave
- i.e. Social protection and tax systems may affect work incentives and earnings

“To really estimate redistribution one would need to invent a counter-factual ‘virgin’ distribution that was unaffected by social policy altogether. In absence of pensions, would the elderly continue to work and thus receive market income?” (see EA & Myles)



# The Welfare State & Redistribution (5/6)

(2) Welfare states provide resources to citizens that affect their earnings potential.

- These derive primarily from services, such as education, health care, training programmes or support to working mothers
- In this regard the welfare state plays an important social investment function and the design of such policies will dictate inequalities in people's lifetime earnings power
- There are powerful countervailing welfare state effects that influence market inequalities



# The Welfare State & Redistribution (6/6)

- Considering these elements there are three basic issues in the measurement of the redistributive power of the welfare state
  - (1) Different WS do embrace different redistributive principles (more equality of outcome or equality of opportunity)
  - (2) The income data traditionally used pick only a part of the overall welfare state effect
  - (3) The most interesting impact of welfare states may be their influence on the ‘virgin’ primary distribution

# Theories of Welfare State Redistribution (1/10)

- Economic theories tend to see the welfare state as replacing insurance markets to compensate for market and information failures
  - Government may be more efficient insurer of risks, in particular under conditions of strong information asymmetries, credit constraints and adverse selection
  - Economic vulnerability in global markets intensifies social risks. This should explain why welfare states are exceptionally large in very open economies



# Theories of Welfare State Redistribution (2/10)

- If the welfare state is primarily an insurer, its role in creating equality would appear irrelevant
- However, there are three kinds of social risks, each with its redistributive logic:
  - Life course risks, inter-generational risks, and class risks (i.e. specific groups like miners)
- Risk pooling can produce a complex combination of redistributive logics and cannot, as economic theory often assumes, be equated with horizontal redistribution



# Theories of Welfare State Redistribution (3/10)

- The Robin Hood theory typically assumes that targeting benefits to the neediest will yield the strongest possible redistributive result
- This has been challenged by the ‘Paradox of redistribution’ thesis (Korpi/Palme) (more in the last part of the lecture)
- The argument is that narrowly targeted policies are typically ungenerous and potentially stigmatizing due to the lack of broad electoral support
- In contrast universal benefits marshal broad citizen support and will, hence, offer more generous benefits that additionally will reach the needy with greater certainty
- Hence, we should expect that pro-targeting welfare states (i.e. US/UK) produce less income equalization than universalist ones



# Theories of Welfare State Redistribution (4/10)

- Political theories offer a second range of arguments
- One tradition (see lecture 3) links redistribution to the legislative power of the left parties
- The straightforward argument is that left parties represent the less well-off, and if they gain sufficient political power they will redistribute in their favour (strong evidence, i.e. Korpi, Huber/Stephens)



# Theories of Welfare State Redistribution (5/10)

- Another tradition applies median voter models:
  - High levels of earning inequality fuels demand for redistribution, in particular if median earnings fall below the mean
- Contrasting empirical evidence on this argument:
  - Milanovic concludes positively, while Moffitt et al. argue that the more unequal is the primary income distribution, the less support for the poor
  - Moene & Wallerstein offer an explanation for the different findings. On the one hand increasing demand for redistribution and, on the other hand, rising demand for insurance (non-redistributive)



# Theories of Welfare State Redistribution (6/10)

- Much research has been influenced by the derivatives of Wagner's law
  - Enunciation: public expenditure will grow disproportionately faster than GDP growth once a certain stage of developed is reached.
  - The upshot is that welfare state expansion and more redistribution is intrinsic to advanced economics (i.e. modernisation theory by Wilensky)

# Theories of Welfare State Redistribution (7/10)

- The origin of welfare states can be dated back to the late 1800s, but social expenditure grew originally very slowly
  - Social expenditures in Europe rarely exceeded 3% of the GDP before World War II
  - The concept of WS emerged only after WWII: by 1960 10% of spending as % of the GDP in the OECD
  - The real take-off took place over the 1970s
  - By the mid-1990s the median level of social expenditure had risen to 24% of GDP (big dispersion from 15% US to 30% Scandinavian countries)
  - Except Mediterranean countries consolidation, no growth since mid-1990s



# Theories of Welfare State Redistribution (8/10)

- Since income inequality declined in tandem with welfare state consolidation, and since there is a fairly strong cross-national correlation between welfare state size and equality, the 'size-redistribution thesis' appears credible
- However, this thesis has been questioned on many grounds
  - Maybe a non-linear relation?
  - A large growth might actually bring the WS to be more generous with the upper-middle class (i.e. Italian case)
  - Problem with the use of Gross spending volume



# Theories of Welfare State Redistribution (9/10)

- Gross figures do not adjust for the taxation of benefits that then flow back into the government treasury
- Countries differ hugely in terms of how much they tax social transfer payment:
  - Very large welfare states, as Nordic countries, tax back far more than the leaner spenders



# Theories of Welfare State Redistribution (10/10)

**Table 1. Expenditure Profiles in Three Welfare regimes.**

	Public social spending (% GDP) <sup>1)</sup>	Private as % Total Social spending	Non-health services as % of Total Public Spending	Targeting: % of transfers to bottom Quintile <sup>2)</sup>
Nordic	25	5	18	34
Anglo	19	19	4	43
Continental Europe	26	8	5	30

Source: calculations from Adema and Ladaique (2005: Table 6) and from Forster and d'Ercole (2005).

1) Data refer to *net* social spending. 2) excludes retired households.



Source: EA/Myles

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# Welfare State Outcomes: Poverty and Inequality

**Table 1: Welfare state outcomes: Poverty levels and inequality across the EU 14 (pre-2004 EU members) in 2012.**

Country	Poverty level (all ages)*			Gini Coefficient			Difference in change (Gini%-Poverty%)
	Before	After	Change	Before	After	Change	
Austria	44.2	14.4	-67.4	47.1	27.6	-41.4	26.0
Belgium	42.3	15.0	-64.5	47.7	26.6	-44.2	20.3
Denmark	41.2	13.1	-68.2	53.4	28.1	-47.4	20.8
Finland	41.3	13.2	-68.0	46.4	25.9	-44.2	23.9
France	43.7	14.1	-67.7	49.8	30.5	-38.8	<b>29.0</b>
Germany	43.3	16.1	-62.8	54.4	28.3	-48.0	14.8
Greece	49.8	<b>23.1</b>	-53.6	56.9	34.3	-39.7	13.9
Ireland	<b>50.4</b>	15.7	-68.8	53.5	29.9	-44.1	24.7
Italy	44.5	19.4	-56.4	47.5	31.9	-32.8	23.6
Netherlands	<b>36.7</b>	<b>10.1</b>	-72.5	<b>46.1</b>	25.4	-44.9	27.6
Portugal	45.4	17.9	-60.6	55.9	34.5	-38.3	22.3
Spain	46.2	22.2	-51.9	52.8	<b>35.0</b>	-33.7	18.2
Sweden	41.8	14.1	-66.3	52.4	<b>24.8</b>	-52.7	<b>13.6</b>
United Kingdom	45.4	16.2	-64.3	<b>57.3</b>	32.8	-42.8	21.6

Source: Gini coefficient of equivalised disposable income (source: SILC)[ilc\_di12]; Gini coefficient of equivalised disposable income before social transfers (pensions included in social transfers)[ilc\_di12b]

\*Gross and net household income <60% median income



# Welfare State Outcomes: Poverty for Different Social Groups

**Table 2: Detailed welfare state outcome indicators: Poverty levels by social group after social transfers (and change compared to before transfers levels)**

Country	New Risks						Old Risks			Unemployed
	Total poverty		Children (<16)		Youth (16-24)		Male Worker <sup>1</sup>		Old (75+)	
	Level	Change	Level	Change	Level	Change	Level	Change	Level <sup>2</sup>	
Austria	14.4	(-67.4%)	18.3	(-56.8%)	17.3	(-41.9%)	12.5	(-47.2%)	16.6	44.9
Belgium	15	(-64.5%)	16.6	(-49.5%)	16.7	(-49.2%)	12.5	(-50.6%)	18.4	34.5
Denmark	13.1	(-68.2%)	10.0	(-59.0%)	39.4	(-27.3%)	12.1	(-49.2%)	22.4	26.9
Finland	13.2	(-68%)	11.2	(-64.1%)	24.9	(-39.7%)	10.7	(-44.8%)	27.6	45.3
France	14.1	(-67.7%)	18.8	(-46.3%)	23.0	(-41.2%)	12.0	(-47.8%)	11.4	36.2
Germany	16.1	(-62.8%)	14.9	(-53.0%)	20.7	(-36.7%)	13.7	(-60.9%)	12.6	69.3
Greece	23.1	(-53.6%)	26.5	(-15.9%)	33.1	(-26.4%)	21.9	(-60.8%)	20.0	45.8
Ireland	15.7	(-68.8%)	16.7	(-63.4%)	23.3	(-60.2%)	13.9	(-36.4%)	13.0	34.1
Italy	19.4	(-56.4%)	25.9	(-25.8%)	25.4	(-31.4%)	17.5	(-61.2%)	17.9	44.7
Netherlands	10.1	(-72.5%)	13.6	(-43.8%)	19.8	(-45.0%)	8.5	(-47%)	5.9	34.0
Portugal	17.9	(-60.6%)	21.1	(-34.7%)	22.2	(-42.2%)	15.3	(-51.2%)	21.5	38.5
Spain	22.2	(-51.9%)	28.9	(-22.7%)	28.4	(-35.7%)	22.0	(-63%)	15.9	46.4
Sweden	14.1	(-66.3%)	13.9	(-57.9%)	27.4	(-34.3%)	11.6	(-46%)	25.3	42.3
United Kingdom	16.2	(-64.3%)	18.1	(-60.1%)	24.1	(-40.9%)	13.0	(-49.4%)	18.9	52.2

Data: At-risk-of poverty rate by most frequent activity status (source: SILC) [tessi124] & At-risk-of poverty rate by detailed age group (source: SILC) [tessi120]. [http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc\\_li02&lang=en](http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_li02&lang=en), extracted 2014, June 23<sup>rd</sup>.

<sup>1</sup>25-54 years old.

<sup>2</sup>No before-transfers risk-of-poverty levels available, hence no information on change.

Source: Ferragina, Seeleib-Kaiser & Sprekelsen 2015



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**Table 3. Poverty Reduction in Families with Children. Mid-1990s. 1)**

	Market Poverty	Post-redistribution poverty	Percent reduction of poverty
Denmark	30	6	80
Finland	18	3	83
Norway	29	5	83
Sweden	39	4	90
<b>Regime Mean</b>	<b>29</b>	<b>5</b>	<b>84</b>
Australia	32	17	47
Canada	29	16	45
Ireland	28	15	46
UK	39	21	46
US	31	26	16
<b>Regime Mean</b>	<b>32</b>	<b>19</b>	<b>40</b>
Belgium	31	6	81
France	40	10	75
Germany	31	12	61
Italy	37	21	43
Netherlands	25	8	68
Spain	30	13	57
<b>Regime Mean</b>	<b>32</b>	<b>12</b>	<b>64</b>

1) poverty is less than 50% of median equivalent income

Source: LIS-based estimates, from Bradbury and Jantti (2001: 83)

# Agenda

Back to Redistribution Debate

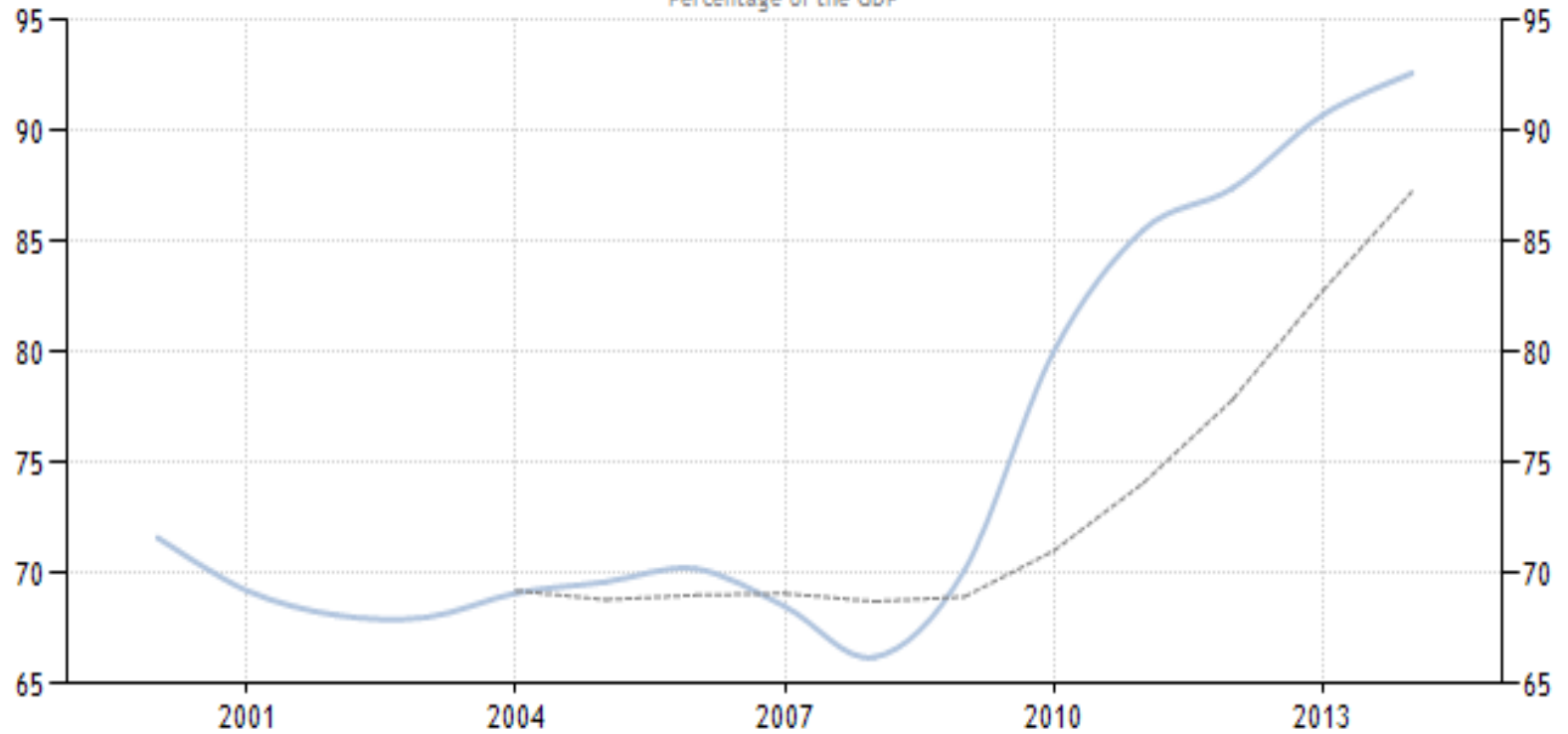
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## EURO AREA GOVERNMENT DEBT TO GDP

Percentage of the GDP



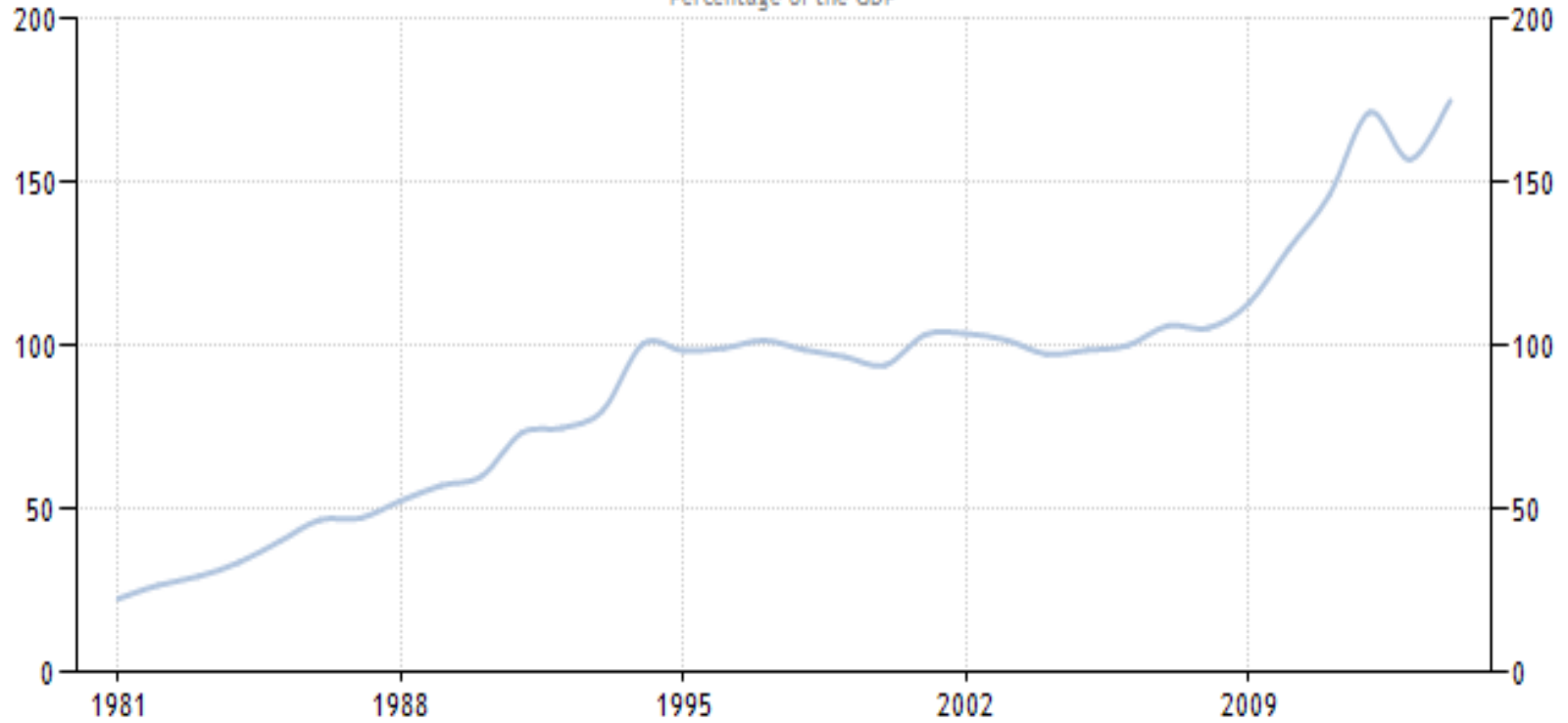
SOURCE: WWW.TRADINGECONOMICS.COM | EUROSTAT



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## GREECE GOVERNMENT DEBT TO GDP

Percentage of the GDP



SOURCE: WWW.TRADINGECONOMICS.COM | EUROSTAT



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### GREECE GOVERNMENT SPENDING



SOURCE: WWW.TRADINGECONOMICS.COM | NATIONAL STATISTICAL SERVICE OF GREECE



# The Advent of the crisis (1/4)

- Employment growth across the EU has been wiped out as a result of the banking crisis
- Necessary investments in countries' future productivity and participation in the areas of early childhood development, training, education, and lifelong learning are under siege
- The downfall of the Euro would have most dramatic social and distributive implications
- Maybe the real retrenchment era has begun





## The advent of the crisis (2/4)

- Economic turmoil polarizes political debate and economic analysis
  - i.e. extreme right
  - The diktat of austerity
- After the credit crunch in 2008 despite the strong support for the WS all parties have taken a strong stance in reducing its size



## The advent of the crisis (3/4)

- In the immediate wake of the bankruptcy of Lehman brothers, all advanced economies intervened with Keynesian stimulus measures for ailing banks through monetary easing and temporary social policy expansion
  - In order to sustain demand and save jobs and skills
- Since 2010, a more conservative macroeconomic policy reform platform has appeared
  - Bent on bringing down budgets deficits and public debt



# The advent of the crisis (4/4)

- The economic imbalances of highly leveraged economies have been there for years
- 5 factors came together in a lethal combination:
  - (1) Internal capital market liberalization & financial deregulation
  - (2) Loose monetary policy
  - (3) Rising global trading imbalances
  - (4) Weakened safety nets, especially in the US
  - (5) Academic failure



# Lax Financial Regulations (1/2)

- Finance become truly global, however regulation remained essentially national.
- On top of it, profound deregulation from the 1980s
- Mortgages were used to secure mortgage-backed securities, and those securities in turn were used to secure a collateralised debt obligation
- Assets came to be bought not because of the rate of return on investments, but in anticipation that such assets and securities could be sold at higher prices



## Lax Financial Regulations (2/2)

- International capital flows were decoupled from the real economy, as financial industry acquired the licence to create money out of credit claims at a pace so rapid that the real economy product and labour markets could not possibly follow
- The stage was set for a global bubble of overvalued stocks to burst into a dramatic credit squeeze



# Loose Monetary Policy (1/3)

- Low interest rates in the US (Beginning of the 2000s)
- Initially it worked well to support the US during a period of crisis (end of the 1990s/early 2000s)
- However in the medium-long term a housing bubble built up
- Low interest rates created a very competitive environment for financial institutions, which could only achieve high returns if they made ever-riskier investments



## Loose Monetary Policy (2/3)

- In Europe many banks invested in large quantities of secured US mortgages and other innovative financial instruments
- Over time, European financial institutions ended up even more leveraged than their American counterparts
- The introduction of the EMU brought interest rates down in the previously high-interest southern periphery of the EU and Ireland
- This provided cheap funding for financial speculators in these countries



## Loose Monetary Policy (3/3)

- The result was an enormous housing and lending boom, especially in Ireland and Spain
- This, combined with the lack of a pan-European system of financial governance, explains why the instabilities in American financial markets contaminated Europe so quickly



# Global imbalances

- Macro imbalances in trade accelerated over the past 15 years, in part as a result of loose US monetary policy
- The emerging economies of Asia and the oil-exporting countries accumulated large current account surpluses
- These surpluses were matched by large current account deficits in the US, UK, Ireland & Spain
- High savings in Asia exacerbated the US debt burden, this further perpetuated global trade imbalances



## Weakened Safety Nets (1/2)

- Lack of welfare provision played an important role behind the growing private indebtedness in the US economy since the 1980s
- Growing job insecurity and the general stagnation of wages of the American middle class from the late 1970s were compensated by easy credit and subprime reductions
- This allowed the squeezed middle class to keep spending patterns up by reductions in household savings and mounting private indebtedness



## Weakened Safety Nets (2/2)

- In other words, access to credit and subprime mortgage loans by low-income households replaced the welfare state as the basis of the American social contract

“According to the former chief economist at the IMF, Raghuram Rajan, weak safety nets, growing inequality, and increasingly unequal access to education and privatised healthcare have, since the 1980s, deepened the fault line of the overleveraged US economy, forcing in turn consecutive American governments and the Fed to pursue extremely expansionary fiscal and monetary policies” (Hemereijck)



# Academic Failure (1/2)

- Only a small minority of academic economists (i.e. Rajan & Roubini) gave fair warning of the risk of an unchecked housing bubble in the early 2000s
- A majority in the economic profession failed to recognize the impending storm
- Rational choice theory and methodological individualism (no consideration for the different trajectory of macroeconomics)



## Academic Failure (2/2)

- The efficient-markets hypothesis fuelled the idea that free markets are self-regulating and financial innovation is beneficial for everyone
- Theoretical and mathematical sophistication moved professional economists away from empirically probing the underlying vulnerabilities of loose macroeconomics, financial deregulation, and the distorted bonus schemes in banking that exacerbated already existing instabilities
- Having bid farewell to Keynesianism in the 1980s, academic forgot one of the most fundamental elements of financial crises: animal spirits
- Left to their own devices, capitalist economies will experience manias followed by panics



# Summing up the Elements of Crisis

“The factors of financial market deregulation and liberalization, loose monetary policy, global savings and trade imbalances, weakened social protection and cognitive capture by short-sighted neoclassical economics, all conspired behind a growth model of overstimulation and overconsumption by debt-financing, which ultimately proved unsustainable and triggered the 2008 credit squeeze and the subsequent global downturn” (Hemereijck)



# Aftershocks (1/11)

- After the crisis, no time for rational responses
- The magnitude of these fast-moving, sequentially related aftershocks has altered the range of social policy choices available to national governments and supranational institutions
- Hemereijck distinguishes seven related aftershocks



# Aftershocks (2/11)

- (1) Aftershock of financial deregulation
- (2) Aftershock of a severe real economy recession
- (3) Aftershock of a social crisis
- (4) Aftershock of a fiscal crisis of the state
- (5) Aftershock of a currency crisis
- (6) Aftershock of a protracted period of low growth
- (7) The political aftershock





# Aftershocks (3/11)

## (1) Aftershock of financial deregulation

- The result of the dramatic collapse of a regime of international finance based on deregulation for the past three decades
- Too much freedom for banks (often out of control)
- Relation between politics and economics



# Aftershocks (4/11)

## (2) Aftershock of a severe real economy recession

- The ‘real recession’ was generated by the credit squeeze in 2008
- Most worrisome was the prospect of real economy protectionism with shrinking trade and overall declines in wealth



# Aftershocks (5/11)

## (3) Aftershock of a social crisis

- The decline of the economic activity caused raising unemployment, poverty & more social exclusion
- Unemployment (especially among young people) across the EU surged to 23 million people by late 2011, averaging at 10% of the working age population
- The crisis has highlighted the vulnerability of low skilled



# Aftershocks (6/11)

- Other social effects of the increase of unemployment
- Pension crisis (due to the collapse of the financial markets) made the ageing of society a worse problem for future generations
- A painful combination of lower benefits and higher contributions is consequently inevitable if the steep rise in old-age dependency ratios is not coupled with measures to promote longer working lives



# Aftershocks (7/11)

## (4) Aftershock of a fiscal crisis of the state

- Since 2010 costly bank bail-outs and stimulus packages have drained the public budget, resulting in a double bind of raising social benefit expenditures combined with declining government revenues
- Elevated public debt-to-GDP ratios brought cut also in welfare programs
- Discussion about the necessity of these cuts



# Aftershocks (8/11)

- By mid 2010, the fiscal crises transmuted into sovereign debt problems in countries such as Greece, Ireland, Portugal, and Spain
- Stimulus programs, costly bank bail-outs, combined with deeper problems in the designing of the governance regime of the EU, set the scene for:

## (5) The aftershock of a currency crisis

- Threat to the survival of Euro
- For Europe, the spill-over from sovereign debt crisis to a fully-fledged currency crisis is surely the most serious aftershock of the global financial crisis



# Aftershocks (9/11)

## (6) Aftershock of a protracted period of low growth (potential aftershock)

- History suggests that economies take a much longer time to recover after a financial (compared to a real economy) crisis
- The magnitude of systemic debt (private + public) is delaying recovery
- Employment and growth are unlikely to return the pre-crisis levels soon
- Hence, social benefits need to be paid for at a time when public spending will be heavily constrained



# Aftershocks (10/11)

- The crisis has dismantled the most important growth driver (from the 1970s onward): easy credit and private consumption
- Is it possible to kick in growth starting from the bricks?
- Danger of a long standing crisis





# Aftershocks (11/11)

## (7) The political aftershock

- The crisis has accelerated a long standing process:
  - The large scale alienation of political elites, a growing hostility against financial capitalism, and cynicism about the EU
- Risk of national responses: welfare regimes & answers
- We do not get out without a (at least) European response



# Recap (1/3)

- Shall We redistribute? Shall we redistribute more?
- There are moral and rational grounds for redistribution
- Piketty & inequality back in the agenda
- The ‘Great Transformation’
- Marx or Kuznet?



## Recap (2/3)

- Not simply inequality of condition, but also treatment and opportunity
- Bringing the WS back in
- Piggy Bank or Robin Hood?
- Different types of redistributions enacted by the WS: horizontal, vertical & between groups
- It is difficult to evaluate the real redistributive power of different WS



## Recap (3/3)

- The advent of the crisis was associated with five main factors:

(1) deregulation, (2) loose monetary policies, (3) Rising trading imbalances, (4) weakened safety nets, (5) academic failure

- 7 aftershocks:

(1) Financial deregulation, (2) severe real economy crisis, (3) social crisis, (4) fiscal crisis of the state, (5) currency crisis, (6) low growth, (7) Political aftershock

