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SCIENTIFIC COUNCIL FOR GOVERNMENT POLICY



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WRR lecture 2005

Towards A New Welfare State

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INTRODUCTION

While the welfare states of rich democracies are widely discussed, at the same time they appear to be doing well. Some take it that in the decades to come they will go on doing so, adapting to new challenges, while others hold that things will shortly change in dramatic ways. The two contributions in this book reflect these different positions. They were presented by their authors on the occasion of the Annual Lecture of the WRR (the Dutch Scientific Council for Government Policy) on December 8th in The Hague.

The various systems of state organised social protection that were created during the first half of the twentieth century, to greatly expand during the third quarter of this century, all came under pressure in the fourth quarter. During the 1980s and 1990s, the generosity of benefits was reduced, the eligibility of programs tightened, while cost control in service delivery was put into place. However, it is important to note that these retrenchments were modest in nature. What is more: in some of the 'poorer' welfare states the amount of money spent on social policy actually kept on increasing. At the end of the twentieth century, Europe showed a remarkable convergence: the late comers were catching up, the most generous welfare states were slightly diminishing their expenses.

A variety of reasons was given for the necessity of retrenchment. Some arguments were of *moral* kind: welfare states were said to make their inhabitants too passive. Some arguments were primarily *financial*: welfare states were spending too much on welfare and their economies could no longer afford this. And then there were arguments evoking *globalization*: this social trend, that started out with the post-1960s rise in the international mobility of capital, was bound to make it impossible to sustain a system of social security and of social services in any well-defined, bounded territory. As economies would become more international, nation states would lose much of their power. Both neoliberal and Marxist analysts have argued that the ability of international firms and financial institutions to shift assets across national borders forces elected governments, regardless of their ideology, to reduce social welfare

expenditure. This development might be enhanced by the ability of large firms to rapidly displace industrial production to low wage countries; or to spread their organization over different countries (marketing in one country, R&D in the next and production in yet another). This would then soon be followed by social dumping; while corporate taxes would drop in a race to the bottom. Until now, there is not much evidence that this is actually about to happen. Welfare states have indeed lowered corporate taxes, but they also succeeded in broadening the tax-base and in imposing strict rules to prevent tax-evasion. Minimum wages have, on the average, not been lowered. Some theorists suggest a deadlock has been reached. On the one hand, the international dimension of the economy reduces the financial capabilities of nation states to respond to internal pressures – especially since the establishment of the European monetary union. Nation states have less freedom to act on their own. However, on the other hand the internal pressures within these states make radical changes very difficult. The failure of EU countries to implement the Lisbon-agenda is a clear sign of this deadlocked situation.

What does this deadlock mean for development of the modern welfare state? If, at least so far, globalization does not lead to retrenchment, but limits the nation states' capabilities for change, to what extent might we still have huge ambitions?

Gøsta Esping-Andersen argues that we should change the focus of our ambition: our main objective should not be to sustain our social security system, but to invest in our children. Demographic as well as economic reasons force us to bring out the best in the next generation: our welfare state should be an investment state. Globalization does not prohibit nation states to pursue that goal, but make it all the more urgent. Saskia Sassen raises the question whether nation states can go on to function in the same way as they used to do. She argues that globalization does not only impose external threats, but also changes the way institutions (can) function.

Wim van de Donk
Chairman WRR

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1 THE STATE AND GLOBALIZATION: DENATIONALIZED WORK AND INTERNAL POWER SHIFTS¹

Saskia Sassen

In the larger worldwide debate about the so-called “welfare state,” most attention has gone to its changed conditions for survival and to its changed contents (its objectives, policies, and budgets). The critical question has been: Can it survive?

Can it? Two leading experts argue that yes, but it will take some sharp transformations in the organizing of public welfare. Esping-Andersen argues that the welfare state is not only about the state. We need to recognize the multiple locations needed for advancing public welfare—state, family, communities. This helps us expand the institutional domain within which to place the project that is the welfare state. To use the British locution, we might say such changes would move us away from the “nanny” state version of public welfare and towards peership between the state and the citizen. And Hemerijck (2002) finds that we need to recalibrate the mix of objectives and resources of the welfare state; the welfare state is dynamic, and thus can consist of a range of combinations.

From the perspective of research about the state and globalization, rather than the welfare state per se, there are two critical facts that come into the picture though they are not part of the welfare state debate.² One of these facts strengthens the viability of Esping-Andersen’s and Hemerijck’s proposals. The other throws some sand in the state machinery we need in order to carry out those proposals.

The first, more familiar of these two facts is, ironically a consequence of the increasingly institutionalized character of the global economy. This includes the formalizing of a growing range of “rights” of global firms and global markets. One might ask how this could possibly help in revising rather than eliminating the welfare state.

To understand what democratic options arise out of this growing institutionalization of the global economy, in my research I have sought to establish the extent to which these powerful global actors actually *need* national states, especially in the highly developed world. In other words, regardless of the facts of increased global mobility, global firms and markets need a global operations space that is at least partly inserted in the countries that comprise the global economy. They need private property protections and guarantees of contracts from each of the states involved.

One question then is: Does such “need” translate into a possibly novel type of authority of national states in the context of an increasingly formalized global economy. This would indicate that the liberal state has more options when confronted with global actors and pressures than the rhetoric of state powerlessness suggests. Further, it would also indicate that the role of the national state around questions of welfare may be less constrained and more open to genuine innovation (rather than pressures to cut spending) than is the common understanding of a somewhat powerless national state in economic matters given global firms and markets. Finally, it suggests that if the state actually gains particular types of authority from its participation in the implementing of formalized global systems, it could also use this authority for projects other than strengthening the rights of global corporate actors – for instance, strengthening the welfare state through various revisions.

But the second fact that comes out of my research on the state and globalization is more troublesome, and partly undermines the above mentioned possibilities (especially in the US). It is the marked redistribution of power inside the national liberal state. The power of the executive branch (or Prime minister’s office) has grown sharply since the 1980s, and especially in the 1990s. But the same processes that feed executive power are partly hollowing out the powers of the legislative branch. This internal redistribution of power can also alter, in multiple and often highly specialized ways, the formal relationship of the state to people. These power shifts are grounded in major changes in the organizational architecture of the state apparatus and to some extent transcend party politics. They also signal that speaking of states losing power in a global economy obscures these critical shifts.

These shifts have often been highly specialized and hence not particularly visible or self-evident. The tendency has been for this power shift to consist of multiple specific technical changes that are usually seen separately, in terms of the specific domain (commerce, finance, citizens rights) within which they take place. One of the reasons this power shift inside the liberal state has received little attention is that it is an emergent trend, becoming legible in some liberal states (especially the US and, to some extent the UK, Australia, and Italy among developed countries, and in a large number of states in developing areas, notably in Latin America) but barely so in many other states. A second reason this power shift has received little attention is that it has been obscured by the larger image of “the state” as losing power in a global economy.

The first part of this paper focuses on how the global is partly constituted inside the national, thereby blurring the distinction global/national and signaling that the national state participates in the implementation of globalization. The second part of the paper focuses on what this implies for state work and public policy. One interpretation is that it partly, and often in highly specialized ways, denationalizes state work.

I THE GLOBAL IS PARTLY CONSTITUTED INSIDE THE NATIONAL

The effort here is to recover the ways in which the state participates in governing the global economy in a context increasingly dominated by deregulation, privatization, and the growing authority of non-state actors. A key organizing proposition, derived from my previous work on global cities (2001) is the embeddedness of much of globalization in national territory, that is to say, in a geographic terrain that has been encased in an elaborate set of national laws and administrative capacities. The embeddedness of the global requires at least a partial lifting of these national encasements and hence signals a necessary participation by the state, even when it concerns the state’s own withdrawal from regulating the economy. One question this raises is whether this participation might entail the formation of a specific type of authority/power for the state in

global systems – both for the state as such and/or for the particular state institutions involved. Does the weight of private, often foreign, interests in this specific work of the state become constitutive of that authority and indeed produce a hybrid that is neither fully private nor fully public? My argument is that, indeed, we are seeing the incipient formation of a type of authority and state practice that entail a partial denationalizing of what had been constructed historically as national.

This denationalizing consists of several specific processes, including importantly, the re-orienting of national agendas towards global ones, and the circulation of private agendas dressed as public policy inside national states. Such a conceptualization introduces a twist in the analysis of private authority because it seeks to detect the presence of private agendas inside the state, rather than the more common focus on the shift of state functions to the private sector, including private forms of authority. It differs from an older scholarly tradition on the captured state which focused on cooptation of states by private actors. In contrast to this older tradition, I emphasize the privatization of norm-making capacities and the enactment of private norms in the public domain.

The purpose here is, then, to understand and specify a particular aspect of globalization and the state which is lost in what are typically rather dualized accounts of this relation; in such accounts, the spheres of influence of respectively the national and the global, and of state and non-state actors, are seen as distinct and mutually exclusive. Even if many components of each of these spheres are separate and mutually exclusive, I argue that this still leaves a specific set of conditions or components that does not fit in this dual structure. Key among these are some components of the work of ministries of finance, central banks, and the increasingly specialized technical regulatory agencies, such as those concerned with finance, telecommunications, and competition policy. In this regard then, my position is not comfortably subsumed under the proposition that nothing has much changed in terms of sovereign state power, nor can it be subsumed under the proposition of the declining significance of the state.

An important methodological assumption here is that focusing on economic globalization can help us disentangle some of these issues about the state today precisely because in strengthening the legitimacy of claims by foreign investors and firms it adds to and renders visible the work of accommodating their rights and contracts in what remain basically national economies. However, these dynamics can also be present when privatization and deregulation concern native firms and investorspace the fact that in much of the world, privatization and deregulation have been constituted through the entry of foreign investors and firms.

Using a multi-scalar analytics allows us to see that sub-national processes and institutions are also critical sites for globalization. Accepting the proposition that the global is multi-scalar leads to its conceptualizing as at least partly consisting of the denationalizing of specific forms of state authority insofar as particular components of global processes are actually located in national institutional orders. This multi-scalar conceptualization diverges from the mainstream scholarship on the state and globalization, where these are seen as distinct and mutually exclusive domains. It helps us see the particular substance and institutional insertions of what I argue is a new mode of state authority that remains insufficiently recognized and theorized. Though housed or located in national state capacities and institutions, this mode of authority is not national in the way we had come to understand this feature of states over the last century.

II GLOBALIZATION AND DENATIONALIZATION

What is it we are trying to name with the term globalization? In my reading of the evidence it is actually two distinct sets of dynamics. One of these involves the formation of explicitly global institutions and processes, such as the World Trade Organization, global financial markets, the new cosmopolitanism, the War Crimes Tribunals. The practices and organizational forms through which these dynamics operate are constitutive of what are typically thought of as global scales.

But there is a second set of processes that does not necessarily scale at the global level as such yet, I argue, is part of globalization. These processes take place deep inside territories and institutional domains that have largely been constructed in national terms in much, though by no means all, of the world. What makes these processes part of globalization even though localized in national, indeed subnational settings, is that they involve transboundary networks and formations connecting or articulating multiple local or “national” processes and actors. Among these processes I include particular aspects of the work of states. These include specific monetary and fiscal policies critical to the constitution of global markets that are hence being implemented in a growing number of countries as these become integrated into global markets. The bundle of policies involved in the project of making liberal states “competitive” is another important instance. But it also includes a range of very different types of instances that are not the focus in this paper – though I have dealt with them at length elsewhere (Sassen 2006). Examples are cross-border networks of activists engaged in specific localized struggles with an explicit or implicit global agenda, as is the case with many human rights and environmental organizations; the use of international human rights instruments in *national* courts; non-cosmopolitan forms of global politics and imaginaries that remain deeply attached or focused on localized issues and struggles yet are part of global lateral networks containing multiple other such localized efforts.

A particular challenge in the work of identifying these types of processes and actors as part of globalization is the need to decode at least some of what continues to be experienced and represented as national. While seeming national, these types of practices and dynamics are actually constitutive of global scalings we do not usually recognize as such. When the social sciences focus on globalization it is typically not on these types of practices and dynamics but rather on the self-evidently global scale. And although the social sciences have made important contributions to the study of this self-evident global scale by establishing the fact of multiple globalizations (e.g. Appadurai 1996; Eichengreen and Fishlow 1996; Aman 1998), only some of which correspond to neoliberal corporate economic globalization, there is much work left. At least some of this work entails

distinguishing: a) the various scales that global processes constitute, ranging from supranational and global to subnational (Taylor 2000; Brenner 2004; Swyngedouw 1997; Amin and Thrift 1994), and b) the specific contents and institutional locations of this multi-scalar globalization (e.g. Massey 1993; Howitt 1993; Jonas 1994). It is the latter two that concern me in this lecture. Geography more than any other of the social sciences today has contributed to a critical stance toward scale, recognizing the historicity of scales and resisting the reification of the national scale so present in most of social science.

III THE SUBNATIONAL: A SITE FOR GLOBALIZATION

Studying the global, then, entails not only a focus on that which is explicitly global in scale, but also a focus on locally scaled practices and conditions articulated with global dynamics and a focus on the multiplication of cross-border connections among various localities. Further, it entails recognizing that many of the globally scaled dynamics, such as the global capital market, actually are partly embedded in subnational sites and move between these differently scaled practices and organizational forms. For instance, the global capital market is constituted both through electronic markets with global span, and through locally embedded conditions, i.e., financial centers.

A focus on such subnationally based processes and dynamics of globalization requires methodologies and theorizations that engage not only global scalings but also subnational scalings *as* components of *global* processes, thereby destabilizing older hierarchies of scale and conceptions of nested scalings. Studying global processes and conditions that get constituted subnationally has some advantages over studies of globally scaled dynamics, but it also poses specific challenges. It does make possible the use of long-standing research techniques, from quantitative to qualitative, in the study of globalization. It also gives us a bridge for using the wealth of national and subnational data sets as well as specialized scholarships such as area studies. Both types of studies, however, need to be situated in conceptual architectures that are not quite those held by the researchers who generated these research techniques and data sets, as their efforts mostly had little to do with globalization.

One central task we face is to decode particular aspects of what is still represented or experienced as “national” which may in fact have shifted away from what had historically been considered or constituted as national. This is in many ways a research and theorization logic that is the same as that developed in the economics of global city studies. But there is a difference: today we have come around to recognize and code a variety of components in global cities as part of the global. What I am trying to focus on here engages a range of conditions and dynamics that are to be distinguished from those global city components in that they are still coded and represented as local and national; further, my concern in this lecture is largely the realm of the political rather than economic.

One important focus for research is the specific set of interactions between global dynamics and particular components of national states. My main argument here is that insofar as specific structurations of the global inhabit what has historically been constructed and institutionalized as national territory, this engenders a variety of negotiations. One set of outcomes evident today is what I describe as an incipient, highly specialized, and partial denationalization of specific components of national states.

With few exceptions, most prominently among which is a growing scholarship in geography, the social sciences have not had critical distance, i.e., historicized, the scale of the national. The consequence has been a tendency to take it as a fixed scale, reifying it, and, more generally, to neutralize the question of scaling, or at best to reduce scaling to a hierarchy of size. Associated with this tendency is also the often uncritical assumption that these scales are mutually exclusive, most pertinently for my argument here, that the scale of the national is mutually exclusive with that of the global.

Finally, the notion of processes that denationalize the national goes against those assumptions and propositions that are now often captured through the concept of methodological nationalism. But they do so in a distinct way. Crucial to the critique of methodological nationalism is the need for transnationalism because the nation as container category is inadequate given the proliferation of trans-

boundary dynamics and formation (e.g. Taylor 2000; Beck 2001). What I am focusing on here is a set of reasons other than transnationalism for supporting the critique of methodological nationalism: the fact of multiple and specific structurations of the global inside what has historically been constructed as national. Because the national is highly institutionalized and thick, structurations of the global inside the national entail a partial, typically highly specialized and specific denationalization of particular components of the national.³

IV TOWARDS A NEW TYPE OF STATE AUTHORITY

How do the analytics briefly developed above map onto the main scholarship on globalization and the state, much of it coming from political science. At what points do these analytics deborder or contest propositions in that scholarship. The literature on the state and globalization is large and growing. A number of scholars have addressed various dimensions of the particular issue that concerns me here, participation by the state in global processes. For some states remain as the key actors and hence not much has changed for states and the interstate system (e.g. Krasner 2003; Pauly 2002; Helleiner 1999; Hirst and Thompson 1996). For others, even if states remain important there are today other key actors, and globalization has changed some important features of states and the interstate system (e.g. Cerny 1990; 2000; Strange 1996; Cutler et al. 1999; Ferguson and Jones 2002; Dark 2002; Palan 2003). For what is probably the most comprehensive mapping of the main strands in the scholarship on globalization and the state, see Held et al. (1999). They categorize the two major emerging strands as “hyperglobalists,” who posit that national states are becoming weak and are on their way out, and “transformationists,” who contend that globalization has brought about significant changes in state authority and the work of states. My particular argument is that we are seeing the incipient formation of a type of authority and state practice that entail a partial denationalizing of what had been constructed historically as national. Even if we accept that the present era is, at a very general level, a continuation of a long history of changes that have not altered the fundamental fact of state primacy, it still leaves us with the need

for detailed research about the specificities of the current changes.⁴ In this conceptualization I introduce a twist in the various analyses on the broader subject. First, it needs to be distinguished from analyses of private authority because these emphasize the shift out of the public domain and into the private domain.⁵ I seek to detect the presence of private agendas and authority inside the public domain represented by the state.⁶ Second, I emphasize the privatization of norm-making capacities which were once in the public domain, and today's enactment of these private norms in the public domain—where they look “public”. This perspective also differs, then, from a literature that emphasizes the decline and obsolescence of the state.⁷ It comes close to the scholarship that emphasizes state transformation⁸ even though this literature tends to discard the specificity of the current phase of globalization.⁹

One of my efforts here is, then, to blur some longstanding dualities in state scholarship, notably, those concerning the distinctive spheres of influence of respectively the national and the global, of state and non-state actors, of the private and the public.¹⁰ While it may indeed be the case that mostly the two sides of the duality are separate and mutually exclusive, I argue for the critical importance of recognizing and deciphering conditions or components that do not fit in this dual structure (e.g. Zacher and Sutton 1996; Bermann, et al. 2000). In the case of US law, one domain where this debordering plays out in what I find intriguing ways is the relation between Federalism and several new global regimes.¹¹ An important methodological assumption here is that focusing on economic globalization can help us disentangle some of these issues.¹²

The embeddedness of the global requires at least a partial lifting of these national encasements and hence signals a necessary participation by the state, even when it concerns the state's own withdrawal from regulating the economy. Does the weight of private, often foreign, interests in this specific work of the state become constitutive of a particular form of state authority that does not replace but works alongside older well-established forms of state authority?¹³ My argument is that the mix of processes we describe as globalization is indeed producing, deep inside the national state, a very partial

but significant form of authority, a hybrid that is neither fully private nor fully public, neither fully national nor fully global.¹⁴ As states participate in the implementation of crossborder regimes, whether the global economic system or the international human rights regime, they have undergone at times significant transformations because this accommodation entails a negotiation. In the case of the global economy, this negotiation entails the development inside national states – through legislative acts, court rulings, executive orders, policy – of the mechanisms necessary for the reconstitution of certain components of national capital into “global capital”, and necessary to develop and ensure new types of rights/entitlements for foreign capital¹⁵ in what are still national territories in principle under the exclusive authority of their states.¹⁶ And it involves developments aimed at making states more competitive, notably the shrinking of welfare programs.

These particular transformations inside the state are partial and incipient but strategic. Such transformations can weaken or alter the organizational architecture for the implementation of international law insofar as the latter depends on the institutional apparatus of national states. Further, they have also created the conditions whereby some parts of national states actually gain relative power as a result of that participation in the development of a global economy. As particular components of national states become the institutional home for the operation of some of the dynamics that are central to globalization, they undergo change that is difficult to register or name. This is one instantiation of what I call a process of incipient de-nationalization.

This partial, often highly specialized or at least particularized, denationalization can also take place in domains other than that of economic globalization, notably the more recent developments in the human rights regime which allow national courts to sue foreign firms and dictators (Stephens 2002) or that grant undocumented immigrants certain rights. Denationalization is, thus, multivalent: it endogenizes global agendas of many different types of actors, not only corporate firms and financial markets, but also human rights objectives.

The question for research then becomes: What is actually “national” in some of the institutional components of states linked to the implementation and regulation of economic globalization? The hypothesis here would be that some components of national institutions, even though formally national, are not national in the sense in which we have constructed the meaning of that term over the last hundred years. One of the roles of the state vis-à-vis today’s global economy has been to negotiate the intersection of national law and foreign actors – whether firms, markets, or supranational organizations. This raises a question as to whether there are particular conditions that make execution of this role in the current phase distinctive and unlike what it may have been in earlier phases of the world economy.

We need to understand more about the nature of this engagement than is represented by concepts such as deregulation. It is becoming clear that the role of the state in the process of deregulation involves the production of new types of regulations, legislative items, court decisions (e.g. Cerny 1997; Picciotto 1992; Picciotto and Mayne 1999), in brief, the production of a whole series of new “legalities.” It also is evident in the proliferation of specialized, often semi-autonomous regulatory agencies and the specialized cross-border networks they are forming which are taking over functions once enclosed in national legal frameworks.¹⁷ The background condition here is that the state remains as the ultimate guarantor of the “rights” of global capital, i.e., the protection of contracts and property rights, and, more generally, a major legitimator of claims.¹⁸ It is in this sense that the state can be seen as incorporating the global project of its own shrinking role in regulating economic transactions and giving it operational effectiveness and legitimacy. The state here can be conceived of as representing a technical administrative capacity which cannot be replicated at this time by any other institutional arrangement; furthermore, this is a capacity backed by military power, albeit not an option in many countries, and with global power in the case of some states. To some extent this work of states is becoming privatized, as is signaled by the growth of international commercial arbitration (Dezalay and Bryant 1996; Salacuse 1991), and by key elements of the new privatized institutional order for governing the global economy.

Legislative items, executive orders, adherence to new technical standards, and so on, will have to be produced through the particular institutional and political structures of each participating state. Even when imposed from the outside, there is specific work that individual states need to do.¹⁹ The emergent, often imposed, consensus in the community of states to further globalization is not merely a political decision: it entails specific types of work by a large number of distinct state institutions in each of these countries. Clearly, the role of the state will vary significantly depending on the power it may have both internally and internationally.²⁰ It is in fact some states, particularly the US and the UK, which are producing the design for many of these new legalities, i.e., items derived from Anglo-American commercial law and accounting standards, and are hence imposing these on other states given the interdependencies at the heart of the current phase of globalization. This creates and imposes a set of specific constraints on the other participating states.²¹

There is in this dynamic an interesting dialectic. These types of state participation can contribute to strengthen the forces that can challenge or destabilize what have historically been constructed as state powers (Arrighi 1994; Davis 1999). In my reading this holds both for the US and for other countries. The US government as the hegemonic power of this period has led/forced other states to adopt these obligations toward global capital and, in so doing, contributes to globalize conditions that reduce particular forms of state authority in more and more countries around the world. One way in which this becomes evident is in the fact that while the state continues to play a crucial, though no longer exclusive, role in the production of legality around new forms of economic activity, at least some of this production of legalities is increasingly feeding the power of new emerging structures, whether global markets for capital, WTO, or the international human rights regime.

CONCLUSION

In sum, a crucial part of the argument is, then, the fact of the institutional and locational embeddedness of globalization inside the national, including the state apparatus. In terms of the concerns in this lecture, it is crucial for two reasons.

First, because it signals that the global economy needs states and hence the possibility of states gaining a specific type of authority, one still dressed in the same old national clothes but actually substantively different. It is possibly a new hybrid base from which states can act. Second, it signals that the range of ways in which the state *could* be involved is conceivably far broader than what it is today, largely confined to furthering economic globalization. States have more playing room than the typical dualized analyses of the global and the national suggest. They could contest pressures to becoming neoliberal competitive states.

One problem is that the playing room states derive from the fact that their work is critical to the corporate global economy is obscured precisely because it is located inside the national state apparatus and the nation-state generally. This playing room has a hybrid quality – it is neither national as historically understood nor global as this term is understood today, that is mutually exclusive from the national. This hybridity renders it invisible. But it is important to recover the fact that there is in this playing room a new kind of authority for the state. And its character goes well beyond the actual uses states have made of this hybrid authority (mostly ensuring the rights and guarantees of global firms and markets). State participation creates an enabling environment not only for global corporate capital but also for those seeking to subject the latter to greater accountability and public scrutiny.²² But unlike what has happened with global corporate capital, the necessary legal and administrative instruments and regimes have not been developed that would allow citizens to participate in global governance through state institutions. The trade-offs and the resources that can be mobilized are quite different in the case of citizens seeking to globalize their capacities for governing compared to those of global capital seeking to form regimes that enable and protect it.²³ Drawing the implications of this type of analysis for the welfare state is a task that I will have to leave with those who are experts on the welfare state. Very briefly we might indicate three issues.

One is that in terms of welfare reform, these shifts spell out a challenge that goes beyond the details of such reform. The conditions within which such reform is to be enacted have changed signifi-

cantly. It is not just a matter of the “welfare state” needing reform. It is also a question of an increasingly sharp change in the conditions under which the liberal state functions. The analysis above points to sharpening divisions inside the national state. While the state has always been marked by internal heterogeneity and conflicting interests, the changes taking place today are of a different order. The gain in executive power and the hollowing out of legislatures is significant since democratic representation is largely enacted through the legislature. This is also the branch of government that is most public and that slows down politics, allowing citizens to catch up and engage. How can a weakened legislature ensure execution of, and democratic participation in, the enactment of welfare reform that ensures a people oriented outcome, rather than for instance as in the US, an outcome that fits the Executive branch’s agenda. There is today a growing alignment between the interests of the executive (or Prime minister’s office) and the global corporate and political agenda, and a growing disalignment with the larger public agenda enacted through legislatures and democratic representation. This is well illustrated by the fact that when a country becomes an IMF “program country,” the IMF will only deal with the executive branch; it will not deal with legislatures. One important question for welfare reform is then what does this redistribution of power *inside* the state – and not only, as typically noted, between the state and global actors – entail for the viability of a peoples’ needs oriented welfare regime.

A second implication is that the fact that the global corporate economy and the supranational regulatory system “need” national states to implement their aims, translates into a possibly novel type of authority of national states in the context of economic and increasingly political globalization. This would indicate that the liberal state has more options confronted with global actors and pressures than the rhetoric of state powerlessness suggests. This points to the possibility that the role of the national state around questions of welfare may be less constrained and more open to genuine innovation (rather than pressures to cut spending) than the typical view of the state today as somewhat powerless in economic matters given global firms and markets.

NOTES

- 1 This paper is part of the author's larger multi-year research project (see Sassen 2006).
- 2 For a full analysis of these trends please see Sassen (2006: chs 4, 5 and 6).
- 3 I have developed this at greater length in Sassen (1996; 2006). I should clarify that when I first developed the construct "de-nationalization" (1996) I intended it to denote a specific dynamic. I did *not* intend it as some general notion that can be used interchangeably with post-national, global, or other such terms.
- 4 Along these lines of analysis, I argue that economic globalization is in fact a politico-economic system partly located inside national states (Sassen 1996: chapters 1 and 2; 2006: chs 4 and 5), thereby having the effect of partly denationalizing specific, often highly specialized components of state work.
- 5 A growing literature that often overlaps with particular parts of the above cited strands in the scholarship emphasizes the relocation of national public government functions to private actors both within national and transnational domains (see Cutler et al. 1999; Aman 1998). For a state of the art elaboration of the rise of private authority see generally Hall and Biersteker (2002). For the emergence of cross-border governance mechanisms see generally Ferguson and Jones 2002.
- 6 A good examination of these issues as they materialize in specific institutional settings can be found in Aman (1998). An excellent collection of essays that seeks to capture these types of dynamics can be found in Likosky (2002). For an analysis of the influence of US criteria regarding welfare state reform in the Dutch case see Huygens (2000).
- 7 Perhaps the best known, though not necessarily the most precise, authors here are Ohmae (1995) and Wriston (1992). See also Kobrin (1998); (Cohen 2001).
- 8 There is today a growing literature (Cox 1987; Panitch, 1996; Gill 1996; Mittelman 2000) that interprets deregulation and privatization as the incorporation by the state of its own shrinking role; in its most formalized version this position emphasizes the state's constitutionalizing of its own diminished role.
- 9 Perhaps the best example is Helleiner (1999), who examines the regulatory changes brought on by the emergence of global financial systems and shows how states remain as key actors.
- 10 A good source in this regard is Mansfield and Sisson (2004), containing papers by major scholars in international relations addressing key issues about the state and the current features of the interstate system, with responses by critics from other disciplines.
- 11 In this context, I find interesting parallels in a specific type of legal scholarship focused on the construction of jurisdictions and the locating of particular issues in jurisdictions that may today be less and less adequate; see, for instance, Bermann (2000); see also the analysis in Resnik (2001).

- 12 Beyond issues pertaining to the global economy, the question of state participation is also at the heart of a far broader debate about globalization and the state. There is an older scholarship on world-order systems (e.g. Falk 1992; 1993) recently invigorated by debates about cosmopolitanism (Held 1995; Held et al. 1999). It examines and theorizes the possibilities of transcending nationally oriented state authority and instituting world-level institutional orders. This literature often includes partial world-level orders such as the international human rights regime (e.g. Brysk 2002) or certain features of international environmental treaties (e.g. Lipschutz and Mayer 1996), and, quite prominently, discussions about the possibility of a global civil society (e.g. Held et al. 1999; Kaldor et al. 2002).
- 13 Several scholars have focused on the nature of this engagement (e.g. Strange 1996; Scholte 1997; Cerny 2000; Dark 2002; Doremus et al. 1999; Kagarlitsky 1999). One way of organizing the major issues is to ask whether the role of the state is simply one of reducing its authority – e.g., as suggested with terms such as deregulation and privatization, and generally “less government” – or whether it also requires the production of new types of regulations, legislative items, court decisions, in brief, the production of a whole series of new “legalities”. I use this term to distinguish this production from “law” or “jurisprudence.” (Sassen 1996: chapter 1).
- 14 Among the issues raised by this type of analysis are the increased autonomy and influence of a whole variety of types of processes and actors, including non-state actors. The literature on non-governmental organizations (NGOs), including transnational ones (TNGOs), and the associated forms of activism, has also generated a series of interesting insights into the changed position of states in a context of multiple globalizations (e.g., Keck and Sikkink 1998; O’Brien et al. 2000; for a critical account that partly rejects the notion that these non-state actors actually represent a politics that undermines existing forms of authority, including that of the state, see Drainville 1995). I would also include here a variety of emergent global networks that are fighting equally emergent global agents such as trafficking gangs (e.g. Global Survival Network 1997; Coalition to Abolish Slavery and Trafficking, Annual); but see also Hopkins (2005) on the importance of not grouping all forms of trafficking as criminal. Along these lines a new set of concrete instances has come about with the September 11, 2001 attack on the World Trade Center, i.e., the use by international organized terrorism of the global financial system and the international immigration regime (see, for a variety of analyses Calhoun et al. 2002).
- 15 Seen from the perspective of firms and investors operating transnationally, the objective is to enjoy the protections traditionally exercised by the state in the national realm of the economy for national firms, notably guaranteeing property rights and contracts. How this gets done may involve a range of options. See, e.g. Cutler et al. (1999); Hall and Biersteker (2002).
- 16 Two very different bodies of scholarship which develop lines of analysis that can help in

- capturing some of these conditions are represented by the work of Rousenau, particularly his examination of the domestic “frontier” inside the national state (Roseneau 1997) and by the work of Walker problematizing the distinction inside/outside in international relations theory (Walker 1993). An interesting variant on this subject is Callaghy et al. (2001), who examine the proliferation of global non-state-centered networks in the case of Africa.
- 17 We can see this in particular features of a variety of domains: for instance, competition policy (Graham and Richardson 1997), specific aspects of international business collaboration (Dunning 1997; *Indiana Journal* 1998), in networks among members of the judiciary (Slaughter 2000) and, in a very different domain, the new opening among the top leadership in a growing number of unions to organizing immigrants (Haus 2002). One particularly acute case where the contradictions and tensions inside the state become legible is the way immigration, especially illegal immigration, is handled to day (see Stichting BMP 2005 for a detailed analysis).
- 18 While it is well-known, it is worth remembering that this guarantee of the rights of capital is embedded in a certain type of state, a certain conception of the rights of capital, and a certain type of international legal regime: it is largely embedded in the state of the most developed and most powerful countries in the world, in western notions of contract and property rights, and in new legal regimes aimed at furthering economic globalization, e.g., the push to get countries to support copyright law.
- 19 In terms of research and theorization, one of my concerns, this is a vast uncharted terrain: it would mean examining how that production takes place and gets legitimated in different countries. This signals the possibility of cross-national variations (which then would need to be established, measured, and interpreted).
- 20 See also the development of the argument focusing on private rather than state actors in Sassen (2001).
- 21 This dominance assumes many forms and does not only affect poorer and weaker countries. France, for instance, ranks among the top providers of information services and industrial engineering services in Europe and has a strong though not outstanding position in financial and insurance services. But it has found itself at an increasing disadvantage in legal and accounting services because Anglo-American law and standards dominate in international transactions. Anglo-American firms with offices in Paris do the servicing of the legal needs of firms, whether French or foreign, operating out of France. Similarly, Anglo-American law is increasingly dominant in international commercial arbitration, an institution grounded in continental traditions of jurisprudence, particularly French and Swiss (Dezalay and Garth 1996).
- 22 There are several types of analyses that address particular forms of this question. See e.g. Aman (1995; 1998) on how states could participate in global governance; Ferguson and Jones (2002) on how to rethink political space; Brysk and Shaffir (2003) on the citizenship

gap in a global world and what states could do; for a very particular angle on these issues see Calhoun et al. (2002).

23

Elsewhere (2006: chapter 6) I examine some of these issues from the perspective of the institution of citizenship. This produces a domain for global politics that can be distinguished from the notion developed above that state participation in the global economy should function as a bridge for a country's citizens to participate in global governance. However, I see an emergent institutional resonance between the features of the state discussed here and the features of an evolving institution of citizenship.

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2 PUTTING THE HORSE IN FRONT OF THE CART: TOWARDS A SOCIAL MODEL FOR MID-CENTURY EUROPE

Gøsta Esping-Andersen

Introduction. How to analyze welfare futures

The debate on a social model for the future is treading water. Perhaps this is because we have been overly focused on the issue of financial sustainability and have accordingly relied too much on the wisdom of our accountants. Allowing actuarial concerns to define the agenda is like putting the cart before the horse. It is a bit pointless to forecast expenditures if we have no clear idea where we wish to go. My contribution, therefore, aims to put the horse back where it belongs.

Any rigorous discussion of welfare reform needs minimally to consider four questions. One, how are social needs and risks evolving; what are the challenges that lie ahead? Two, which instruments are best suited to address our priorities? Three, can such instruments deliver efficiency and equity simultaneously; will they help us attain a superior Pareto frontier? A reform that fails on either efficiency or equity grounds must obviously be shelved. Four, what, if any, egalitarian aspirations should we saddle welfare policy with?

A sound diagnosis of the challenges that lie ahead requires a suitable analytical method. In the first place, we need to move from the standard, and overly myopic, focus on the welfare *state* to a *welfare regime approach*. We will not see the world clearly unless we examine the interplay of family, markets and government in the production (and consumption) of the total welfare pie. These three cornerstones of welfare have reciprocal effects on each other. Markets may fail and this will necessitate recourse to either the family or to government. Similarly, families can fail and this means greater reliance on markets or government. And what if markets and families fail in tandem? Care for the frail elderly is susceptible to double failure since commercial services are expensive while families' caring ability is eroding. Any given welfare mix will inevitably

produce second-order distributional and behavioural consequences that influence equity and efficiency. To illustrate, if childcare is unaffordable prospective parents may reduce fertility or the mother may decide to curtail employment. The former generates a societal child gap; the latter lowers employment levels and, hence, tax-revenue and it reduces income among the families that most need it.

Secondly, we need to move beyond the traditional categorical client perspective that usually underpins welfare analysis. By this I mean the practice of defining policy around discrete groups, be they the 'elderly', the 'working class', or the 'excluded'. This leads to very ineffective policy; it places too much decision power in the hands of vested corporative interests that lobby on behalf of their clients or their own jobs; and it easily nurtures counter-productive equity conflicts. Adopting a life course perspective permits us, in contrast, to identify the inter-connectedness of citizens' risks and needs. Social exclusion or old age poverty are not events that suddenly befall an individual but are usually the end-result of a problematic biography. More often than not, the triggers of a social problem are deeply buried in the early stages of peoples' life course. An effective response to welfare needs requires us to identify when and how in the human life course we might best invest resources so as to minimize the need for later, costlier and often ineffectual remedial policies.

The evolving structure of risks and needs

Ongoing societal transformation is spearheaded by a set of endogenously driven *structural* trends. They are structural in the sense that a) they affect the *modus operandum* of our society as a whole, and b) for good or bad, they are here to stay. The way we – and our children – will live tomorrow depends on how we adapt now.

Population aging is undoubtedly the best-documented trend. By mid-century the typical EU country will experience a 50% increase of its elderly population while the new youth cohorts are very small. The EU old age dependency ratio will, in 2050, edge towards 50 percent. Meanwhile, the EU working age population will be 40 million fewer than today. There is widespread fear that this will make us financially insolvent and unleash a major generational clash.

Aging is driven by low fertility but also by rising longevity, and the latter occurs at an especially rapid pace. Roughly speaking, the ‘ultra-aged’ population (80+) doubles every 20 years and this signals a rapid growth of frailty and dependency. At the EU15 level, it is projected to grow from 15 million now to 38 million in 2050.²² Our policy menu is unlikely to include euthanasia, most families are priced out of the elderly care market, and the stock of available family carers is disappearing. Hence, we must urgently devise a workable formula to meet coming caring needs.

The *second* trend comes from the ‘revolution’ of women’s roles, which is arguably the most dynamic source of change in contemporary society. At present, female employment ranges from less than 50% in Southern Europe to 75+% in Scandinavia. This gap may narrow sooner than we think since young Italian and Spanish women’s activity rates are catching up rapidly. We should also anticipate greater convergence around the ‘full-time, lifelong’ employment model. Already the norm in the Nordic countries and the US, this may very likely spread to countries like the Netherlands, too. This has major repercussions for labour and product markets and constitutes a vital ingredient in any long-term sustainability scenario. It also implies that families’ ability to internalize caring responsibilities will diminish and, hence, the familialistic welfare tradition must be reconsidered. The challenge is to reconcile women’s new preferences with our continued desire to form families. Failure to do so will produce either of two evils: a ‘childless’ society or a ‘sub-employment’ economy.

The *third* trend stems from the new family demographics that are, incidentally, very much a bi-product of women’s changing roles. These include rising marital homogamy, postponed family formation, fertility levels that are far lower than what citizens desire, increased marital instability, and the proliferation of ‘a-typical’ families – many of which are economically vulnerable. Women’s new economic role is generally good news but it also heralds the arrival of mounting welfare problems. The hardening of assortative mating can be polarizing as is evident in the widening gap between work-poor and work-rich households. Delaying marriage and births is an

expression of citizens' new life priorities (such as more education) but also of constraints (women hesitate to have children until their job situation is secure). Postponement lowers the chances of attaining the 2+ child goal that most adults pursue; catch-up is certainly not precluded but it requires very favourable conditions. Partnerships are far less stable and this trend is likely to continue in tandem with women's enhanced autonomy. In Scandinavia, as in North America, just about half of all children will not grow up within an intact biological family. Divorce has adverse consequences for children and parents alike, and single parenthood can be harmful for children's achievements (Kamerman et.al., 2003).

The *fourth* trend stems from the emerging knowledge economy and, in particular, from the centrality of skills for citizens' life chances. In the past, even a low skilled male breadwinner would be able to ensure adequate living standards for his family. Job protection legislation helped consolidate this assumption. We can no longer count on the male breadwinner model and must assume that two incomes are required to insure family welfare. High school dropout rates provide a pretty good indicator of the problems we will face. The rate is above 30% in Spain, almost 25% in the Netherlands, and less than 10% in Sweden. The size of the dropout population will affect future productivity and welfare burdens. The distribution of skills among today's youth will determine the quality of tomorrow's working age population and, further ahead, the well-being of the retirement population. Since future pension benefits will depend more on lifetime contributions, those with a career of low earnings and frequent unemployment are very likely to end up poor.

To provide an idea of the social challenges we may face, Table 1 exhibits three 'warning signals' in the form of 1) the incidence of 'cognitive dysfunctionality' among youth, 2) the degree of cognitive inequality, 3) the share of lone mother families and, 4) jobless households (the latter including of course also jobless single parents).

Table 1. Early Warning Signals

	% below PISA minimum 1)	Literacy inequalities 2)	Lone mothers	Trend in lone mothers	Jobless households	Trend in jobless households
Denmark	15	88	14	+2	9	+2
Germany	21	109	13	+4	16	+3
Netherlands	10	85	8	0	11	-2
Spain	19	95	7	+2	13	-1
Sweden	12	96	18	+4	6	+1
UK	13	100	22	+6	13	0
US	18	101	20	-1	5	-2

Note: Trends are based on past ten years. 1) Percent 15 year olds that score below 400 (level 1 and below) on PISA's 2003 reading test. Falling below the 400 score implies a dysfunctional skill level. 2) standard deviation on PISA reading test. Note that UK data refer to PISA 2000. Sources: Jobless household data are from OECD's social indicator data base; Lone mother data are from US.

Reform priorities

The contemporary debate is almost exclusively concerned with retirement reform. Yet, the nature of structural transformation tells us that our first priority must be to invest far more in children. It is no secret that school success and subsequent life chances are powerfully dictated in early childhood. The ability of schools to equalize children's opportunities and to rectify a bad start is, at best, very limited. The mainsprings of child outcomes lie in the family of origin. To ensure a good life, today's youth will not only require more education but also the pursuit of continuous life-long learning. This presupposes strong cognitive skills to begin with. Considering the looming demographic imbalances we can ill afford large skill deficits within the population. Large-scale immigration adds to the urgency of homogenizing children's learning abilities.

The second upshot is that we need to redesign family policy. Unless we 'de-familialize' welfare responsibilities we will never succeed in reconciling motherhood with employment. Low fertility is not a signal that citizens do not want children but rather that the cons-

traints of family formation are mounting. The family remains the key institution of society and the challenge is to forge policies that support it. The family, in its increasingly varied manifestations, is also the key to children's well-being and, hence, policy that ensures children against economic deprivation is *sine qua non*. More generally, the cost of children is rising – and so is the positive externality of children. We need to design an equitable sharing of the costs and benefits of children.

The third upshot is that we need to minimize the child penalty of motherhood. This implies a reconciliation of motherhood and careers but we are mistaken if we believe that the standard menu of 'mother-friendly' policy will suffice. Some of the major obstacles are hidden in the labour market, especially with regard to job security. Policy that addresses this problem will easily provoke new dilemmas. At the end of the day we will almost certainly have to conclude that a positive equilibrium necessitates a 'feminization' of the male life course.

The fourth upshot is that we need to redefine the nexus between working life and retirement. The really difficult challenge of aging is not so much to finance it as to ensure *equity*. It is a pretty safe bet that earnings will become increasingly unequal and that a sizable group will find itself locked into a carousel of low wages and unemployment, possibly passing through any number of activation measures. This will spill over to the distribution of household income. Stable high-educated couples will accumulate a formidable retirement wealth, but this is less likely for the low educated and the divorced.

It is easy to envision a retirement regime that is sustainable while equitable in inter-generational terms. It is far more difficult, and also far more urgent, to design one that delivers *intra-generational* equity. The current system is, almost everywhere, inherently inequitable and replete with ineffectual stop-gap measures. As the retirement population and caring needs grow, the inbuilt financial inequities will provoke growing tensions. I shall argue that a positive equilibrium necessitates some form of basic pension guarantee and a far more progressive system of financing aging and dependency.

The fifth, and final, upshot is that current social accounting systems fail to provide us with a clear and relevant picture of the financial implications of welfare reform. We need to move towards consolidated *welfare regime* accounts and we need to be able to identify the investment character of key social policies.

Work, retirement and old age

If we are genuinely committed to the well-being of tomorrow's elderly, simple arithmetic tells us that pension expenditure will grow by – roughly speaking – an *additional* 50%. For the average EU country this means another 5% of GDP by mid-century. Health care (which is very old age biased) together with frailty and caring needs will, realistically speaking, require yet another 3 or even 4% of GDP. All told, the total *additional* cost of aging edges towards 10% of GDP, a figure that equals a third of current average EU public social expenditure. This burden will not ease by privatizing either pensions or care.

Small cohorts imply that we may need fewer teachers or pediatricians and, hence, some costs savings at the youth end of the life course. But these are unlikely to offset the aging cost by much – perhaps by 1% of GDP or so (European Economy, 2005). We know that neither immigration, nor a sudden spurt of fertility, will do much to re-balance our demography in the medium term. All the best simulations conclude that we would need to quadruple current immigration rates in order to balance the books. This means that the best-case scenario necessitates maximum mobilization of our labour reserves, primarily women, and a non-trivial postponement of retirement age. OECD estimates suggest that a return to *de facto* retirement at age 67 would go a long way to ensure sustainable finances.

Aging can unleash two kinds of divisive equity conflicts. The first – and most debated – has to do with generational burden sharing. If we continue unabated with a pay-go system, the entire additional cost will fall on workers; if we were to move towards a funded regime, it will fall on the aged themselves. Neither would appear socially desirable or politically viable. In most EU countries, pensions (and sometimes also elderly care) are financed via the payroll which is not only a relatively narrow tax base, but also harmful for jobs.

As previously argued (Esping-Andersen et al., 2002; Esping-Andersen and Myles, 2006) a Musgrave-type fixed relative proportions model would guarantee equitable burden sharing across generations. And, most importantly, the burden will diminish in tandem with rising retirement age. Delaying retirement is both effective and equitable. It is effective because it operates simultaneously on the nominator and denominator: more revenue intake and less spending at the same time. It is inter-generationally equitable because retirees and workers both sacrifice in equal proportions. In any case, inter-generational fairness requires a substantial reduction of public debt. If this does not happen, we will face inequity in another form because the (small) future working age population will be saddled with the debt we have incurred to pay for present and past retirees.

A far greater – but frequently ignored – challenge lies in securing *intra-generational* equity. The problem stems from strong social asymmetries in mortality. Managers and professionals live, on average, 5 or even 7 years longer than manual workers. This means that they collect far more pension income, and that they are vastly over-represented among the ultra-aged with expensive caring needs. Where financing mainly comes from payroll contributions, the relationship between taxation and benefits is very inequitable.

Equity would be enhanced were we to finance aging more progressively. One way to do this would be to introduce steeper progression in the contribution system. Another would be to index (positively) retirement age to lifetime income. And a third would be to build a general revenue financed, first-tier basic pension guarantee. A combination of all three strategies is, as I argue below, arguably superior.

There are two arguments in favour of a Nordic style first-tier basic ‘peoples’ pension. One is that it eases the payroll tax burden and this, in turn, will help promote job creation. The same reasoning applies incidentally also to financing old age care via general revenues. The other has to do with future elderly poverty risks. Can we really forecast such?

To a degree, yes. Those who now enter the workforce with few competences are likely to face a life of low paid employment and this will, subsequently, translate into sub-standard pension entitlements. If we, again, use upper-level secondary schooling as our benchmark for minimal skill needs, the EU's coming problem population may range from 10 to 30 percent. Most EU welfare states are poorly equipped to face such a scenario, in part because pension benefits depend increasingly on life-time contributions and, in part, because the weakest are not very well protected in systems that rely primarily on social insurance.

A basic 'peoples pension' is unlikely to add much to total pension spending. If we decided to eliminate old age poverty in the Netherlands today, it would cost less than one-tenth of a percent of GDP. Since private individual retirement plans are tax-subsidized and heavily biased in favour of the top quintile incomes, it would, in the name of equity, be logical to index the growth of the 'people's pension' to the growth of private plans.

The transition to retirement

Many believe that it is unfair to raise the retirement age. But not doing so would be even more unfair. It all depends, in the end, on who we are talking about. Before the 1980s, early retirement was mainly driven by health impairment among older workers. With economic restructuring emerged new motives. One was the – now discredited – idea that retiring the old would create jobs for the young. Another was to help firms shed excess manpower without attacking existing job security provisions. Firms are especially eager to shed older workers where, as in France and Germany, seniority-based wage growth is unusually strong and, hence, prices older workers out of the market. A final important impulse lay in the non-neutrality of pension accruals. In the typical EU country older workers had a clear financial incentive *not to* continue working.

Productivity among older workers is conventionally assumed to decline, both absolutely and relatively: Absolutely because aging means eroding health, and relatively because old workers possess less education than the young. Change is rapid on both fronts

because we are getting healthier and more educated. By 2050 we should expect that life expectancy at age 60 will have increased by another 5 years. At present, the average 60-year old male can expect to enjoy another 12+ disability free years and, for each new cohort, health is improving. There is also good news in terms of ‘relative productivity’. The education gap between old and young workers will begin to disappear when the baby-boomers approach retirement. In other words, the evolving health and education prospects of older workers speak in favour of delayed retirement – in particular if we adopt the principle that retirement age must be progressively adjusted to lifetime income.

Still, firms will not lose their appetite for early retirement unless we lower the relative cost of older workers. This implies weakening the seniority component of wage increases and, hence, a head-on battle with sacred collective bargaining principles. Some perspective on current practice may help. One very important initial motive behind seniority wages was that pension benefit assessments were based on the very last years of employment. As benefits become a function of total lifetime contributions, the salience of the last years’ earnings weakens.

Women in the work-retirement nexus

We should not forget that early exit is even more pronounced among women, especially when they reach midlife (after age 50) and caring obligations for the frail begin to take effect. Consider the gap in participation among women aged 55-64: 65% in Sweden compared to 23% in the Netherlands and only 16% in Italy. In practice there are no dramatic differences in terms of the share of midlife women who provide *some* care. The real variation lies in the burden of care – from a median of 5 weekly hours in Denmark, to the equivalent of a half-time job in the Netherlands and a full-time commitment in Spain (Sarasa, 2005).²³ In Scandinavia virtually no women need to curtail their career in order to care for kin; in Southern Europe it has been the norm. Exiting the labour force, say at age 50, implies major foregone lifetime income and probably inferior pension entitlements. To society it implies foregone tax revenue. But the rest of Europe is bound to converge to the Nordic pattern in the coming decades,

not only because young women have experienced a leap in educational attainment but also because their career commitments are far stronger.

Demand for non-family care will accordingly rise abruptly. This demand cannot be adequately met via commercial care markets, either in the form of residential care or home help services simply because both are priced out of the market for the majority of households. A residential place will easily cost the equivalent of median female earnings. For policy considerations Denmark offers a perfect benchmark considering that care supply meets demand (by law). Here the price tag for full coverage via home help and residential places runs to almost 3% of GDP (home help is fully government financed while patient co-payments defray about a fifth of the residence costs). The model prioritizes home help and seeks to minimize the use of residential care because the elderly prefer the former, and because it is far more cost effective. Even with daily visits, the *per client* cost of home help is less than a third of a residential place. If, on the other hand, there is a shortage of residential places families will seek recourse in hospitalization which is at least twice as expensive as residencies.

Since entitlements depend solely on need, the model is equitable in terms of access. But if we recall that need correlates with social status, financing should be progressive. The Danish system is general revenue financed and this, of course, ensures a modicum of equity that would be further enhanced were client co-payments to be levied progressively as well. A German-type social insurance is bound to be comparably inequitable, both because of income ceilings for contribution purposes and its essentially proportional tax schedule. And the Anglo model of means-tested free services to the poor, combined with (tax subsidized) commercial services for the rest, will perhaps ensure some equity on behalf of low-income citizens but at the expense of major inequities *and* welfare gaps among the rest of the population.

Denmark undoubtedly boasts the most equitable formula, but is it also efficient? It is in the sense of 'clearing the dependency market',

but many may flinch at the associated cost. If our aim is to meet demand it is, however, unlikely that the commercial alternative will entail macroeconomic savings, simply due to profits and higher transaction costs. And for most citizens it is anyhow inaccessible unless subsidized. A superior way to gauge costs is to hold them up against the added revenues to government from a boost in older women's employment. If older women remain employed ten years longer than is now typically the norm, household incomes will increase substantially. This means less poverty and need for social assistance and greater tax revenue to the exchequer.

To illustrate the point let us hypothesize that older Dutch women would double their employment rate to Danish levels if the Netherlands were to adopt a Danish-style care model. This would imply that an additional 25% of Dutch women, aged 50+, receive earnings for an additional ten years or so. Even if they were all part-timers their aggregate tax contributions would probably offset a great part of the full government cost of elderly care.

Supporting the revolution of women's roles

One does not need to be a feminist to realize that women are very much the vanguards of ongoing change – and that the conventional male breadwinner society is unworkable. There is good and bad news connected to women's embrace of lifelong employment. It will stimulate jobs because families will externalize servicing needs, from eating and cleaning to child and elderly care. The job multiplier that is created is potentially huge, especially within personal and social services. It also gives women autonomy over their life course decisions and provides an effective bulwark against income loss due to divorce, and against deprivation in old age. But it also implies greater marital instability, declining fertility, and more vulnerable households among which lone mother families loom large.

Women's altered life course preferences are very good news for welfare state finances. A back-of-the-envelope arithmetic may be illustrative of the magnitudes. If women on average earn 75% of male wages and their employment rate jumps from 50 to 75% (from Spanish to Danish levels) their additional contribution to national

income will be about 15% and, at a mean taxation rate of 30%, this would add 10 or 12% to government tax revenues.

As Hakim (1996) insists, women's preference sets are quite heterogeneous. A disappearing minority continues to cling to the traditional housewife ideal and another minority (certainly less than a fifth) puts careers before family. The vast majority, in other words, embrace a dual-role preference of combining a life commitment to work with marriage and motherhood. It is to this majority that we must address policy. If the dual preferences cannot be reconciled satisfactorily we face negative-sum tradeoffs both in terms of individual welfare and the collective good.

Failure to reconcile motherhood and careers will, for citizens, provoke a trade-off between having children, on one hand, and pursuing employment, autonomy and increasing household income, on the other hand. At the societal level this translates into one of two sub-optimal equilibria: a childless 'low fertility equilibrium' or a 'low income, low employment equilibrium'.

We must first come to grips with the low-fertility syndrome. Since survey data repeatedly show that adults desire at least 2 children, low fertility cannot be simply ascribed to 'post-materialist' tastes. The child gap is modest in some countries (the US TFR is 2.1, and the Danish, Norwegian, British and French hovers around 1.8), it is substantial in most EU countries (the Dutch is about 1.5-1.6) and, at 1.2, huge in Southern and Eastern Europe. In some regions it is as low as 0.8. For citizens, low fertility represents a welfare deficit – the inability to form families as desired. For society, even small differences in the TFR will, in the long haul, have massive consequences. Holding all else constant, a TFR of 1.3 will produce a population that is only 25 percent its present size at end of century. Italy would accordingly shrink to 13 million people, most of whom will be old. In contrast, a TFR at 1.9 will produce only a 15% population decline. Aging together with population decline will produce a society that probably no one desires and, besides, it will lower our living standards. One rather typical simulation concludes that, for the EU15, aging lowers per capita GDP by 0.4 percent annually. OECD estimates are a bit higher.

There are, similarly, major costs to both citizens and society if women's pursuit of lifelong employment is frustrated. Here we must consider the rising importance of women's earnings for family welfare. Men's earnings have eroded, especially among the young and less skilled, and the conventional male breadwinner is less and less able to guarantee sufficient income. Hence, mothers' earnings are increasingly the key to child welfare. Child poverty rates decline by a factor of 3 or 4 when mothers work. Additionally, women who are compelled to interrupt their careers either to care for small children or for dependent elderly will accumulate less pension credits and thus risk poverty in old age. Most importantly, rising female education, now surpassing males', implies that the opportunity cost of career interruptions becomes very large in terms of foregone earnings.

We need to recognize that the cost of children is rising and that, concomitantly, parents create important positive externalities. US research estimates that the social benefit of an average child runs to \$100,000, so we are not dealing with trivialities (Preston, 2004). Most importantly, the social value of children is bound to rise simply because there are so few of them. It should be evident to all that the childless are free-riders if they do not help defray the cost of children. For equity reasons, therefore, redistribution in favour of children is called for. At present, even the most generous family benefit schemes, such as the Danish, cover only a fraction of added consumption spending – although they are very effective in minimizing poverty. In any case, the major – and rising – cost of children lies in mothers' child penalty and not in the added consumption outlays. This is why the most important family support is policy that reconciles motherhood and careers.

The standard 'mother-friendly' package includes a neutral, individual taxation regime, maternity-cum-parental leave with job security, and subsidized childcare. Joint taxation penalizes wives' marginal earnings and is discriminatory. If paid child leaves are too short (or too long) they discourage employment re-entry of less educated women and fertility among highly educated women. And, as I discuss below, if mothers are compelled to return to work too soon

this can harm children's development. Access to affordable quality childcare is *sine qua non* for any workable future equilibrium.

It is important to understand that childcare costs are the equivalent of a *regressive tax* on mothers' labour supply. The typical price of full-time, full year quality commercial care approaches 10.000 euros which means that most parents are pretty much priced out of the market. Worse, the price structure has a strong social bias since low-income mothers are especially likely to curtail employment – and, yet, it is especially these mothers' earnings that are vital for family welfare. Subsidizing our way to universal coverage does not come cheap. Sweden provides what is probably the most generous system, subsidizing 85% of total cost; Denmark is somewhat less generous (66% of total cost) but is demonstrably able to furnish universal coverage, in part because low-income parents go free. The total cost to the exchequer comes to a little less than 2% of GDP.

If we again use Denmark as a benchmark, the typical mother will take leave benefits during the first year of the child's life, return to work – for a brief period on a half-time basis and then resume on a full-time basis. Research shows that the lifetime income loss is quite marginal and this means that in a *dynamic accounting* framework, mothers end up de facto re-paying (with interest!) the initial subsidy via their enhanced lifetime earnings and tax payments. See Table 2.

TABLE 2 DYNAMIC ACCOUNTING OF THE COSTS AND RETURNS FROM DAY CARE PROVISION

Assumptions:

- Mother, at age 30-35, has two kids;
- she does not interrupt employment (except one year maternity);
- her wage is 67% of APW, and;
- she will continue working until age 60;
- we apply 1.5%p.a. 'Mincer estimate' of cumulative loss for 5 year interruption.

	D.Kr.
<i>Cost to government:</i>	
2 years in creche (x2)	168.000
3 years in pre-school (x2)	342.000
Total	510.000
<i>Gains to mother:</i>	
(a) 5 years with full earnings	800.000
(b) life-time wage gain from no interruption	1.400.600
Total	2.200.600
<i>Gains to Exchequer:</i>	
additional revenue from (a)	280.000
additional revenue from (b)	490.000
Total	770.000
<i>Net return to Exchequer</i>	
On original outlay (770.000 – 510.000)	260.000

In most EU countries motherhood incurs major opportunity costs (Sigle-Rushton and Waldvogel, 2004; Rake, 2000). Estimates suggest that the lifetime income penalty for a median woman is around 40% in Germany and the Netherlands. Put differently, subsidizing universal childcare is necessary for equity and also doubly efficient because it enhances family income and government revenues. And as I discuss below, quality childcare can be a very effective

tool in the pursuit of equal opportunities and lower school dropout rates. If we were to rely on the market, as in the US, families' uneven purchasing power translates into uneven child care quality which, in turn, manifests itself in unequal child outcomes.

Within the EU there is now broad consensus in favour of the standard 'reconciliation package'. But we will fool ourselves if we conclude that this will suffice. The incompatibilities of motherhood lie also in the labour market and in the resilience of traditional familialism. Testifying to women's new life priorities, research shows that precarious jobs and also unemployment have become major impediments for women to having children. Indeed, we have evidence that being employed on temporary contracts lowers the probability of fertility by a factor of two, or more. Similarly, we know that job guarantees and flexible working schedules are key to reconciliation.

Feminizing the male life cycle

Women's fertility choices depend less and less on their partner's breadwinner potential and more and more on *their own* career prospects. This does not mean that childbearing has become purely individualized, only that the relevance of fathers is being redefined. There is strong evidence that low fertility is a manifestation of the incongruence between women's new life course preferences, on one side, and lingering traditional gender roles, on the other side (McDonald, 2000). We see this clearly in the fertility decisions of higher educated women in Scandinavia: women condition births on the fathers' expected contribution to child caring and home production.

Put differently, women have adopted a more 'masculine' life course while men have not really proceeded to 'feminize' theirs'. True, men's contribution to domestic tasks is increasing, but the sex gap remains large. Men may also experience more career interruptions but this is largely due to unwanted unemployment. Gendered life course asymmetries are obviously linked to incentive structures and constraints. Although closing, the gender pay gap remains substantial, and the typical spousal age gap also implies that the male's

opportunity cost of dedicating time to home production will be relatively greater. And to the extent that women select themselves into mother-friendly, soft-economy jobs while men are more likely to work in the hard economy, the career penalties of 'feminizing' the male life course will be substantial.

If our goal is to promote women's quest for autonomy and children we face, therefore, major obstacles in the form of gendered life course asymmetries. How might we encourage men to interrupt careers and share the domestic burden? One answer would be to design parental leaves so that fathers are encouraged to take them. This would require not only full income compensation but also that men's lifetime earnings are not harmed. How could that occur? It might if the sex-wage differential narrows towards zero and if men's and women's contribution to total household income approaches parity *on a lifetime basis*. Still, if gender job segregation is as pronounced as is the case in Scandinavia the differential penalty of interruptions will not disappear. One major obstacle to gender equalization lies in women's self-selection into protected, mother-friendly sectors.

The dilemma is aggravated because men's contribution to domestic work is socially skewed towards the highly educated. This has undoubtedly something to do with growing marital homogamy, especially at the top of the social pyramid. Highly educated women have substantial bargaining power in the partnership. We face, in other words, not simply a gender issue but a broader question of social inequalities. Marital homogamy contributes importantly to widening household income and work inequalities.

The problem is the following: Highly educated dual-earner couples have the means to embrace greater gender equality in domestic *and* work life; they are also far better positioned to reconcile careers and parenthood. At the other end of the social spectrum, low educated women are more likely to interrupt or end employment when children or, later, elderly caring obligations arrive; and both partners in such households are concomitantly far more likely to face unemployment and precarious working lives. Work-poor households are concentrated at the bottom end of society. The upshot is a growing

gap in couples' potential labour supply and hence earnings power. When we add to this the proliferation of lone parent families we see the potential for an increasingly polarized household welfare scenario.

We can remedy this the old-fashioned way by more redistribution in favour of low-income households. A more effective policy would be to equalize the *earnings potential* of households by removing the barriers to labour supply that those at the bottom face. A major barrier lies in the cost of accessing child and adult care and this would be easy to resolve via a sliding subsidy scale.

A far more formidable barrier lies in the nature of less skilled jobs in our new economy. Uneven productivity growth in services means that low-end service jobs will offer low wages or disappear. Given that families increasingly need two incomes and that marital homogeneity is hardening, low individual wages will probably go hand-in-hand with low family income. Obviously, the most effective policy is to limit the size of the at-risk population to begin with. For the medium-term we cannot ignore the fact that a substantial share of tomorrow's workforce is already handicapped by having inadequate competences. We cannot assume that activation measures will remedy such skills deficiencies – activation policies can help but they are generally ineffective for those who most need them. Hence, in the medium term it will be difficult to avoid some form of income support unless we are willing to accept rising household welfare inequalities. In this regard European countries might fruitfully learn from the Anglo work-conditional Negative Income Tax experiences, while the Anglo countries might learn from Europe's more generous support for child families.

Investing in children

The advanced societies are swimming upstream in terms of securing children a good life. The knowledge economy requires ever more competences, families are ever more fragile, and economic inequalities are widening. This means that parents' ability to invest in their children's fortunes is becoming more unequal, too. So children face an increasingly hostile environment within which they must

maximize their life chances. The knowledge economy is raising the human capital requirements needed to ensure good jobs. Of course, not all jobs require strong skills and we will inevitably see substantial growth in low-end service jobs catering to families' needs. Unless publicly provided, the latter are likely to be low-paid and precarious simply because they tend to be low value added and labour intensive.

There are good arguments in favour of such low-end service jobs. They provide a large pool of easy-entry jobs for youth and immigrants with few skills or experience. But from a life chances perspective this labour market may prove problematic if it cultivates a new 'post-industrial proletariat', condemned to lifelong low wage employment. Strong human capital is the main pre-requisite for mobility.

The question is what skills? Formal educational credentials are, as always, *sine qua non*, especially for early career moves. As mentioned, we might consider completed upper secondary equivalent education as a bottom-line requirement. But other human capital dimensions are gaining in saliency. Many employers look for social skills, initiative, and emotional intelligence. But virtually by definition it is cognitive skills that reign supreme. Firstly, cognitive abilities and the motivation to learn are the preconditions for successful schooling. Secondly, knowledge intensive production assumes that people have the skills to understand, interpret and apply information. Thirdly, life-long learning is becoming the norm but it depends on a good educational base and on strong cognitive abilities. The economic returns to cognitive skills are rising strongly (Farkas, 2003).

There is one basic rule that must guide policy on this front, namely that key competences such as cognitive skills, discipline, and learning motivation are developed very early in life (Karoly et al., 1998). This helps explain why a half century of educational expansion has done very little to diminish the impact of social origins on opportunities: the first years of childhood are decisive and this is usually when children are most 'privatized'. Inequalities in parental stimulus are simply transmitted to the school experience but schools are

typically poorly equipped to rectify differentials in learning abilities. How should we then invest in our children's life chances?

There are two sides to this coin: one has to do with raising the level of skills overall; the other has to do with homogenizing competences, i.e. ensuring more equality of opportunities. At this point it is important to note that equalization need not lower the common denominator. To illustrate, some of the best PISA performers (like Finland and Sweden) also boast very modest differentials in terms of cognitive abilities or school completion. For efficiency reasons we cannot permit ourselves to squander our human capital potential. And if the future will bring more wage inequality, the best way to prevent polarization is to equalize the opportunity structure. Our challenge is basically to bring Joseph Schumpeter's class scenario into reality: "classes are just like the omnibus, always full of people but always of different people".

Ignoring genetic transmission, child outcomes are primarily the result of parents' income and 'cultural' status. Even if education is free of charge, parental income matters greatly for health and schooling. In most countries quality pre-school enrolment depends on household income; well-off parents can give their children an edge by investing in private schools or in extra-curricular activities. At the other end, poverty and economic insecurity can have very adverse consequences. Economic insecurity breeds risk adversity, and low-income parents are therefore more inclined to pull their children out of school prematurely. There is ample evidence that parental unemployment, lone motherhood, and low incomes are harmful for an array of outcomes, such as sociability, studying, health and delinquency. US research shows that poor children will have 2 years less of schooling than the non-poor. Similar but less dramatic findings exist also for Europe. The Nederlandse Gezinsraad shows that up to 15% of children from long-term low-income families manifest poor developmental outcomes. Worse, the effects become persistent through children's lives. As adults, the same children are very likely to become poor parents. Children of lone mothers end up with incomes that are 66 percent of non-poor kids in the Netherlands and the UK; in the US the penalty is even greater (Kammerman et.al., 2003).

Here we are, once again, swimming upstream because child poverty, lone parenthood and, in some countries, workless households, are on the rise. Despite a booming economy, Dutch child poverty has doubled in the past two decades, reaching 10% today.

We must take note that the income effect is not linear. The really harmful effects begin to spiral when economic conditions are very poor, in particular when children are small. Fortunately it is both simple and cheap to combat the poverty problem. First of all, it will diminish simply when more mothers work. Secondly, generous family benefits are very effective in limiting poverty. Indeed, the added cost to the exchequer of abolishing child poverty altogether would be surprisingly modest. Adopting the 50% of median poverty line, the complete elimination of child poverty would in a typical EU country amount to 0.2 or 0.3 percent of GDP. In the Nordic countries where virtually all mothers work, the price tag is less than 0.05%.

On balance, however, the income effect is probably less salient than the 'culture effect'. Analyses of the PISA data show that children's cognitive performance (at age 15) is less connected to income than to families' 'cultural' resources. There are three types of culture effects that operate. One is related to Bourdieu's idea of class reproduction in terms of transmitting the proper 'middle class' cultural baggage to their children. A second has to do with parents' education, which can be decisive for making the best school choices on behalf of their offspring. Low educated parents easily suffer from information failure and lack the means to navigate their children through the education system. And a third refers to the family's learning environment, parental stimulation and nurturing. Analyses of the PISA data show that the number of books in the home is one of the single most powerful predictors of children's learning abilities. I use the Dutch PISA data to illustrate the point: children from a family with less than 10 books would enjoy a 9% improvement in their reading abilities if their parents arrived at the national average in terms of books in the home.²⁴

Inequalities on all three dimensions are quite huge and, not surprisingly, immigrant and lone parent families are especially disadvan-

taged. The inequalities are especially large in countries – like Italy or Spain -- where a substantial share of the parental generation had only minimal education. To illustrate, the share of women in the typical parental age bracket (35-44) with no more than compulsory schooling is 54% in Spain; 33% in the Netherlands; and only 12% in Sweden. Young women’s educational attainment is rising rapidly and, hence, part of the problem will gradually diminish. But large-scale immigration constitutes a worrisome counter-tendency. Even in Sweden, where efforts to rectify the immigrant disadvantage have been extraordinary, we find that the probability of school failure among immigrant kids is 5 times higher than for natives. In the Netherlands immigrant kids score more than 10% lower on PISA’s problem-solving tests (which are less likely to be immigrant biased than are literacy tests).

The spread of lone parenthood represents a second problematic trend. Coleman (1988) reports that school dropout rates are 30 percent higher among children living with a solo parent. But the negative effect largely disappears when we control for income and employment (Biblarz and Raftery, 1999). Hence, encouraging more employment among lone mothers should constitute an effective counter-measure. Research, however, warns us that outcomes for lone mother children are especially threatened unless they benefit from high quality child care (Bernal and Keane, 2005).

At first glance it would appear impossible to remedy cultural deficits via policy. How can we compel parents to read to their children or to take an active interest in their homework? The good news is that compulsion is unnecessary because early childcare programmes that help reconcile motherhood and careers can be a very effective tool for equalizing children’s cognitive stimulus and school preparedness. There are three major findings from evaluation research. One is that external care during the child’s first year can be harmful. But, secondly, from year one onwards childcare participation has very positive effects on child outcomes, especially for under-privileged children (Karoly et.al. 1998; Waldvogel, 2002; Kamerman et.al., 2003). The third is that ‘neighbourhood’ and school effects matter far less than family effects (Brooks-Gunn et.al., 1997; Farkas, 2003). In

other words, the thrust of policy must be directed at family mechanisms far more than at the education system. The key is to ensure optimal parent-child interaction during the first year and to secure strong pedagogical quality of child development thereafter.

Indirectly, evidence from the Nordic countries confirms the vast potential of high quality, universal early childcare. Denmark, Norway and Sweden demonstrate a substantial (and unique) decline in the effect of parents' education, 'cultural capital' and socioeconomic status on children's educational attainment. Most strikingly, this decline coincides almost perfectly with the universality of childcare for the under-3s – namely for children born in the 1970s onwards. The equalizing effect is especially notable for children from disadvantaged homes, i.e. parents with very low education. In Denmark, the chance of completing upper secondary education has doubled for the youngest cohorts, and in Norway even tripled (Esping-Anderesen, 2004).

There are two potential problems with the childcare strategy. One is that mothers' employment may cause children to suffer from inadequate parental interaction. The evidence suggests that such harmful effects disappear *if* children remain with the mother during their first year (Ruhm, 2004; Waldvogel et.al., 2002; Gregg, 2005); *if* mothers have quality jobs; and *if* childcare quality is high. These are three difficult 'ifs'. The first can be solved by providing adequate parental leave entitlements for *at least* the first 9 months. In the Netherlands only the first 16 weeks of leave are fully compensated while the remaining 24 weeks provide a very low benefit. This means that career minded women rush back to work very soon (60% of Dutch mothers return to work within 6 months of birth), but also that a substantial number (25%+) disappear from the workforce (Gustafsson and Kenjoh, 2004). Extending parental leave to one year is not merely a concession to women – or a means to get fathers involved – but also an investment in superior child outcomes. And as I discussed above, investing in quality childcare will largely pay for itself. The remaining dilemma we face is how to ensure that mothers are employed in quality jobs – a question that falls beyond the scope of this paper. Tomorrow's society will inevitably be far more ethnically and cultu-

rally heterogeneous, and we face a major challenge in terms of how to ensure that immigrant children do not fall behind in the knowledge economy. As noted earlier, there is a substantial native-immigrant gap not only in reading literacy but also in math and problem solving abilities. The 10% performance gap I found for the Netherlands jumps to 15% in Germany. It is undoubtedly feasible to narrow the gap since in France, Denmark and Sweden it is less than 5 percent.

Returning to the research discussed above this is, in fact, one case where ‘neighbourhood’ effects *do* matter greatly. Here we encounter a very complex interaction process that is vital to understand: An oppositional enclave culture is especially likely to evolve if the minority group a) is physically concentrated and b) sees itself systematically distanced from the economic opportunity structure. In this environment minority groups will adopt performance criteria and behavioural norms that are in opposition to the mainstream, emphasizing ‘street-smartness’ rather than study, and this can produce self-reinforcing spirals of marginalization, oppositional culture, and under-achievement (for an overview, see Portes and Rumbaut, 2001).

Enrolment in quality day care would no doubt help, but is surely an inadequate answer since disadvantages are compounded by residential segregation and economic exclusion. We can diminish segregation by more residential dispersion – a policy that has met with substantial success in Chicago – or by limiting minority concentration in the school system. Positive bussing of ghetto children is worth considering. One thing is clear: immigration is here to stay and if we do not take urgent steps to combat excessive segregation and scholastic under-performance now we will find ourselves with a major social divide tomorrow.

A new welfare mix? back to the accountants

A paradox of our times is that family well-being presupposes ‘defamilialization’. This obviously does not imply coercive intrusion in family life. The essence is to give families realistic options. Nor does it automatically threaten the quality of family life, more likely to the contrary. As I noted, the *incidence* of caring for, and interacting with, frail elderly kin is not lower in Scandinavia than in any other EU

country. Additionally, recent Danish data show that parental time dedicated to their children is actually greater today than it was in the Golden 1960s.

What, then, are the relative merits of markets or state in terms of substituting for familialism and meeting the challenges ahead? The debate on privatization frequently pits opponents, who insist that *all* private is bad, against supporters, who maintain that *all* public is bad. The truth lies in the details, not in ideology. The menu of privatization is ample, ranging from a purely commercial regime to quasi-market principles in public provision. In between exist non-profit, regulated or subsidized private providers, voucher schemes, and so forth.

The first point to hammer down is that, macro-economically speaking, total welfare costs will probably not change much however we combine markets and state. Denmark and the United States occupy the polar ends in terms of public spending but end up virtually identical when we examine total net social outlays (for details, see below). If the market is truly competitive we may expect a quality dividend and, in some cases, it is demonstrably possible to achieve cost savings via private provision. Home help services staffed by public functionaries will inevitably prove more expensive than if provided by contracted personnel. But in most commercial welfare establishments the per unit service cost will normally exceed the public sector equivalent. This is partially due to the profit margin but mainly to higher transaction costs (such as marketing or billing administration). If commercial welfare providers are pricier this does not automatically imply that government provision is the only alternative. Both protestant and catholic welfare organizations play a massive role in some countries' welfare delivery. In Denmark a third of childcare centres are established and run by parental associations, and in Sweden one-in-ten schools are independent. The real issues we should address are, instead, the distributional and behavioural second-order effects of any given mix.

Unless subsidized (say by tax concessions or by vouchers), commercial social services are typically priced out of the market for most households below the median income. The same goes for private

health insurance and retirement plans. A tragic example is health insurance in the US: 40+ million Americans have no coverage whatsoever. The important point here is that we must *always* measure any potential efficiency dividend against equity. As a rule-of-thumb the equity price we pay will almost invariably overshadow any efficiency dividend.

In terms of second-order behavioural effects, there are three kinds that especially merit attention. One kind refers to incentive effects – primarily the incentives to save and to work. Although unambiguous empirical findings are hard to come by, it is a plausible argument that a primarily publicly financed welfare model implies a level of taxation that will distort work incentives and reduce household savings. Vice versa, we should expect more savings and labour supply if citizens need to personally finance their welfare. Until we have credible estimates of the relative savings and labour supply effects of either alternative for *each and every* welfare item we will be in no position to make an educated choice one way or another.

A second has to do with information deficits and asymmetries. Competition may be very positive for quality but many welfare fields involve substantial expertise that citizens are unlikely to possess. Very few are able to choose between competing heart transplant offers and even selecting between alternative schools may pose major difficulties. Asymmetries arise because customers become captive to the sellers' expertise. Citizens' ability to inform themselves is also highly unevenly distributed. The resourceful may do well in a competitive market but the low educated can be severely disadvantaged. The weak may be additionally disadvantaged if competitive markets lead to client creaming and exclusion. Any rational private insurer would shun high-risk clients.

The third kind refers to social externalities. If a large segment of the population is priced out of welfare services this may have non-trivial societal repercussions. Take access to childcare. If low-income parents are unable to afford quality care, they may respond by placing children in sub-standard care (parked in front of a TV for example) or by withdrawing the mother from employment. The former is undeniably

harmful to children. The latter reduces aggregate employment (and tax revenues) and raises child poverty (that necessitates public income transfers). Alternatively, if childcare is inaccessible fertility may suffer.

My argument is that we must factor all such second-order and distributional effects into our accounting practices. And we must compel the advocates and enemies of either preference to furnish us such a complete kind of social accounting.

The strongest case in favour of privatization is that it enhances freedom of choice and competition; either may raise quality. The weakness of this position is, however, that the implementation of 'quasi-market' principles in public (or publicly regulated) services may yield the same benefits. Julian Le Grand makes a very persuasive argument that greater choice is fully compatible with egalitarian goals, too, if competing providers are adequately regulated and consumers are adequately informed. Empirical research is replete with good and bad practice from which we can learn a lot. If providers are permitted to cream the best risks or to set fees as they like, the result is very likely welfare segregation. The question boils down to a consistent and effective regulatory framework.

Financing the future

Now to the accountants. The welfare equilibrium that I am promoting will certainly not come cheap. The main items in my design will require an additional spending burden that, realistically speaking, may run to 10 or 12 percent of GDP.²⁵ Our Minister of Finance – having consulted with his accounting department – will surely dismiss the whole thing as frivolous.

The real problem we face is that current accounting practices are simply not up to the task of furnishing the kinds of numbers we really need. I therefore argue that we need to revamp our social accounting systems so that we can think more clearly about substance. I have already emphasized the need for accounting that explicitly factors in second-order effects. There are two additional changes that need to be considered.

Investment accounts

As I suggested in Table 1, expenditure on childcare will, in a dynamic perspective, pay for itself. Indeed, in my example the government reaps a 50% return on its initial investment. More broadly, the upshot of my future scenario is that we shall be moving towards a more *investment oriented social policy*. It would accordingly be helpful to distinguish what is of an investment character from what is current consumption and then be able to estimate the real returns. This is no mean challenge, considering that existing social accounts (dating basically to mid-20th Century) consider public social spending as purely consumption expenditure. There are good reasons why we might promote a separation of current and capital accounts in our welfare state, just as we do in private companies.

In the post-war welfare state, being exceedingly income-transfer (and especially pension) biased, the need to distinguish social investments from consumption was minor. It becomes an urgent question when spending must be redirected in favour of pro-active policies, servicing families, building life-long learning opportunities, or activation programs.

It is not easy to separate social investment from consumption. It is only modest progress to distinguish 'passive' from 'active' policies. It would appear obvious to classify income support as a passive 'consumption' that yields few economic returns. Yet, things get complicated when we consider that transfers to families may enhance child outcomes. Or, take programs in support of working mothers: once again, simply the fact that they work means sharply reduced child poverty, an implicit job-multiplier, and additional tax revenue to governments. Care for the elderly is likewise Janus-headed: taking care of the frail may not constitute an investment in our future productive potential and, yet, failure to do so implies that many women must reduce their labour supply.

Besides education and training, there are a number of social policies that are easy to identify as investments in individual productivity and collective wealth creation. Most generically, all spending towards child welfare has a potential pay-off. Cash benefits to fami-

lies with children create financial security and prevent child poverty, two factors that are crucial for child outcomes. Early pre-school programmes, and most of all universal, quality childcare, have a powerful equalizing effect on children's learning abilities.

It is more complicated to pinpoint precisely the investment component of many income maintenance programs for working-age households – such as unemployment benefits. The reasoning is more circumscribed, but it has for long been recognized that strong welfare guarantees stimulate greater risk-taking during work life. Also, workers will arguably be less resistant to change if their welfare is assured in the event of redundancies. Generally speaking, flexible and dynamic labour markets require off-setting social security.

This is not meant to be an exhaustive overview of how to set up a system of social investment accounts. The idea is simply to pinpoint the need to revise existing practice so as to construct an accounting practice that is more realistic for any 21st Century welfare model.

Welfare Regime Accounts

Our social accounts are too myopically limited to *public* expenditures. The reawakened international interest in the Nordic model is a case in point: while broadly admired, it is even more broadly rejected for its huge spending and taxation needs. In 2001, gross public social expenditures were 34% of GDP in Denmark and 35% in Sweden.²⁶ To most accountants this compares unfavourably with the US's 16%, the Netherlands' 24%, the UK's 25%, and even Germany's 30%.

The first problem is that these numbers are meaningless because they fail to consider that much spending is taxed back immediately – in particular in big-spending welfare states like the Nordic. They also ignore hidden tax-expenditures in the form of tax deductions and subsidies for social purposes. Tax subsidies loom large in 'residual' type welfare models. The second problem is that meagre public provision will stimulate market alternatives – in particular if mandated or given tax subsidies. Private (net) social spending is predictably marginal in Scandinavia (only 0.8% of GDP in Denmark) but substantial in the US (11%), the Netherlands (5%) and the UK

(4%). The Netherlands has experienced very rapid growth in private welfare in tandem with major cutbacks in public programmes. Studies that focus on pension spending come to similar conclusions, i.e. there is basic convergence in *total* GDP use for pensions however we mix markets and government. Table 3 provides an overview.

Table 3. Apparent and Real Social Expenditure as a percent of GDP

	Denmark	Sweden	Germany	Netherlands	USA
<i>Gross public</i>					
Social spending	34	35	31	24	16
<i>Net public</i>					
Social Spending	26	28	28	20	17
<i>Net private</i>					
Social Spending	1	3	3	5	11
<i>Total net</i>					
Social Spending	27	31	31	25	28

Source: Adema and Ladaique (2005: Table 6).

One lesson is that some forbiddingly heavy spenders, like Denmark, in reality are quite lean. In other words, the important issue is not so much the overall burden but rather: a) from which and whose pocket the money is drawn, and b) what are the welfare outcomes for any given level of expenditure. In Denmark and Sweden almost all the money is taken out of the taxpayer pocket; in the Netherlands and the US, a lot is taken out of the consumer pocket. At the end of the day the average Dane, Dutch and American end up paying pretty much the same. But, clearly, the non-average Dane, Dutch and American will not *receive* the same.

Not all citizens are average and this is where total welfare regime accounting becomes relevant. If a large chunk of the money must come from the consumer pocket, access to welfare will hinge on our spending power. The average American family can, by and large,

afford to purchase health insurance and care services but the same items are priced out of range for most households below median income. This is why 40+ million Americans have no health insurance whatsoever, and also why the US exhibits huge quality differentials in child and elderly care. To cite a similar example, in the late 1990s the Blair government embarked on a massive expansion of day care, establishing within few years 600.000 new places. The policy was based on commercial centres and since the public subsidy was modest, families had difficulty accessing the service. As a result, almost half of all were subsequently closed due to 'lack of demand'.

The added spending burden of 10 or 12 percent of GDP must be considered as a realistic scenario. The very simple point that needs to be driven home is that a) if we *do* want to realize such welfare goals, this added financial burden is inevitable however we combine private and public. And b) if the added spending is not forthcoming we should expect major welfare lacunae.

The added financial burden will inevitably vary across the EU. In countries like Denmark and Sweden a very large slice of the added spending needs have already been effectuated considering that child and elderly care is now virtually universal. Denmark and Sweden already commit roughly 5% of GDP to these two items. The additional outlays that will be required over the coming decades will therefore be limited to population size adjustments or to possible quality improvements. At the other extreme are countries like Italy and Spain where catch-up needs to be huge. This suggests that the Scandinavian countries are far better positioned to meet future spending requirements than are most other EU nations. In *net total spending* terms they will probably end up at the low end of the welfare spending rankings.

In short, we need a consolidated system of accounts that allows us to a) identify real (and not misleading) public spending, and b) examine the joint expenditure trends in markets and government alike. It is total GDP use that matters. The really important value of such an approach is that it puts us in a far better position to assess the distributional aspects of our social model. The relevant question is not *whether* we can afford more welfare spending because this will

happen anyway. The really relevant question has to do with *who* are the winners and losers, and what may be the second-order consequences, when we opt for one or another public-private mix. If we could also develop a credible system of measuring the implicit costs of non-monetarized family servicing, we would be able to approach a genuine system of welfare regime accounts.

Conclusion

This paper has focused on what I believe to be the three (plus one) greatest challenges to our welfare model. Since life chances are so over-determined by what happens in childhood, the flagship of our strategy must be a comprehensive child investment strategy that combines a strong accent on early childhood development with a deliberate and explicit commitment to equality of opportunities. Since the future of our family depends on how well we resolve the dilemmas associated with women's new life course preferences, it is impossible to imagine a positive equilibrium without an effective reconciliation of parenthood and careers. But the battle will only be half-won if we do not accompany standard reconciliation policies with a strategy designed to promote a 'feminization' of the male life cycle. Women – at least in countries like the Scandinavian and the US – are reaching the limits of 'masculinization' of their life cycle and it is increasingly this which provokes new disequilibria. And, thirdly, since the welfare of tomorrow's elderly depends crucially on the quality of their childhood and subsequent careers, our response to the aging challenge should "begin with babies" and focus especially on minimizing life chance inequalities.

The 'plus-one' challenge lies in the development of a superior system of social accounting and may arguably be our first priority. Accordingly it may have been premature to put the accountants behind the horse. The quality of jobs can be a major stumbling block for both our child investment and parenthood-career reconciliation strategy. We can promote more equality of opportunities in early childhood, but what if opportunities are not there when youth reaches adulthood? Likewise, even the most brilliant reconciliation policy may fail if women's job conditions contradict motherhood. And, likewise again, we will have to expect widespread old age poverty in the

future if a substantial proportion of tomorrow's workers find themselves trapped in a life of bad jobs. The quality of jobs is not normally the domain of social policy and should therefore be relegated to a different context. Suffice to say that we should most realistically assume the following scenarios. One is that labour markets will become more flexible, in particular in terms of wage setting and job protection. Two, that post-industrial job growth is highly biased in favour of 'good' jobs (that require skills). Three, that flexibilization plus the continuous rise in female employment plus aging will nurture the growth of a sizable amount of low-end (low skill) servicing jobs. Four, that income inequalities are likely to increase.

These trends, in other words, give mixed signals. Greater flexibility and widespread low-wage employment suggest a scenario of overall insecurity for possibly sizable population groups. It is unrealistic, therefore, to believe that the importance of traditional 'passive' income maintenance will disappear. Indeed, I would consider it *sine qua non* that we build a genuine unconditional anti-poverty guarantee for child families and the elderly alike.

Postscript: what about equality?

My treatment has emphasized equity in the sense of fairness not equality. Should we also pursue an egalitarian agenda? If so, which? Academics and policy makers routinely equate the welfare state with egalitarianism while, paradoxically, this is less so in the general public – for whom the welfare state represents security. In the very good old days the egalitarian promise was often framed in terms of the class divide. In the post-war era it became a more diffuse and plural idea, embracing meritocracy and equal opportunities but also a redistributive here-and-now equality of condition. Do we need a new egalitarian commitment for the Century that lies ahead? We must first recognize that ongoing structural change promotes substantial inequality, be it from widening earnings differentials, marital homogamy, immigration, or the evolving household structure. There are also counter-tendencies buried within these same trends. The gender pay gap is narrowing and female employment is becoming more universal. Household income inequalities can be held at bay when less educated women embrace the lifetime employ-

ment model. Such counter-movements are important but are, in any case, unlikely to turn the basic tide of inequality around.

There are reasons why we should not be especially alarmed by rising here-and-now inequality. Low wages or bad jobs are not *per se* problematic if they are transitory experiences. Our poverty headcounts are misleading if many of the poor are simply youth and students. The real question has to do with mobility, i.e. with life chances. When we measure inequality in terms of *lifetime incomes* we find that there is far less inequality than we were led to believe. To illustrate, the Danish Gini coefficient is reduced to half when calculated on the basis of lifetime incomes but, at the same time, now we discover that 92% of Danes have been poor at one or another moment in their lives!

But there are also reasons for alarm. There is substantial evidence that mobility is *negatively* correlated with the overall level of income inequality. The notion that inequality nurtures more mobility is simply wrong. Most comparative data show that there is substantially less mobility in the US than in many if not most European countries. Worse, the opportunity structure is adversely affected by prevailing levels of inequality. If there are strong inequalities in the parental generation this implies more unequal abilities to invest in the life chances of children.

All this considered, there are at least two fundamental principles that must underpin any future egalitarian policy. One, it should emphasize life chances rather than here-and-now redistribution. Two, it should centre on those mechanisms that lie at the heart of social inheritance and unequal opportunities. We are well-placed to identify where our egalitarian efforts should focus. We must prioritize child investments and family welfare not because children are sweet and innocent but because the key triggers of life chances lie in childhood conditions. No policy will solve all problems but guaranteeing a strong start to all children is one that surely will pay off. It is for this reason that we should consider an income guarantee and also access to quality child care to all child families. Very committed life chance egalitarians might go further and advocate affirmative action

for disadvantaged children and mobility guarantees to adults who find themselves entrapped in persistent dis-welfare.

In the end we should expect that an unchecked rise in income inequality will worsen the opportunity structure and this implies that it does, indeed, need to be checked. Government redistribution via taxes and spending is demonstrably a very effective instrument, especially if, as I advocate, we sharpen the progressiveness of old age financing and favour universalistic principles of entitlement.

To wrap it all up I present below an idea of the distance we need to travel in order to come anywhere close to the kind of Pareto improvement I advocate. To define the target towards which we can move I firstly set as our benchmark zero child and aged poverty and, for other indicators I use the best performance that can be currently identified within the EU15.

Table 4 The Distance to Travel to Reach Main Objectives. Select EU Countries, latest data. A Minus sign identifies shortfall to reach objective.

	Sweden	Germany	Netherland	UK	Spain
<i>Poverty Targets</i>					
Zero % child Poverty	-4	-9	-10	-15	-16
Zero % aged Poverty	-7	-10	-2	-21	-23
<i>Invest in Children</i>					
Minimize School Dropout 1)	0	-4	-7	-9	-23
Max average Cognitive level 2)	-45	-65	-33	-71	-96
Max Cognitive Homogeneity 3)	-13	-15	-12	-20	-1
<i>Reconciliation</i>					
2-kids on Average 4)	-0.3	-0.5	-0.4	-0.2	-0.8
Employment Of mothers W/ small Children 5)	0	-23	-8	-19	-32
<i>Equality of Opportunity</i>					
Impact of ascriptive factors on child Outcomes 6)	-6	-15	-10	-8	-7

Notes: 1) Sweden and Denmark, with a dropout rate of 8% among 18-24 years olds is reference. Dropout is defined as no education beyond lower secondary level. 2) Cognitive score levels refer to PISA's math tests, and Flemish-speaking Belgium is reference with the highest EU mean score of 562. 3) Cognitive homogeneity is derived from the standard deviation (Iceland with the lowest S.D of 73 is reference. 4) Target here is defined as a $TFR=2.0$. 5) Denmark (and Sweden) is reference with a 73% employment rate. 6) Regression estimated combined effects of parents' socioeconomic status and cultural capital (number books in the home) on PISA 2000 reading scores. I include a control for immigrant status since the relative size of the immigrant population differs substantially across nations. Finland is again reference because it exhibits the OECD's lowest family effects. The numbers reflect how much a country must reduce the percent variance explained by the family effects to reach the Finnish minimum ($R\text{-squared} = .075$).

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