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The Crisis of the Welfare State in Northern Mediterranean Countries

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The Great Recession has put Welfare States everywhere under considerable strain. In particular for social protection systems in the northern Mediterranean, relative latecomers in Welfare State building, the current situation represents a severe test of their capacity to play the role they were created for: preventing an economic crisis from turning into a social catastrophe.

The Great Recession

How severe this test has been is there for all to see. In 2013, according to official estimates, the size of the economy has shrunk since 2007 by 5.5% in Spain, 7.4% in Portugal, 7.8% in Italy, and as much as 23.5% in Greece. In the European Union (EU) as a whole, the cumulative contraction over the same period was 1%.

The rise in unemployment has been the most visible effect of the recession. In the EU, the unemployment rate in 2012 had climbed to 10.5%, its highest level for well over a decade. However, in the northern Mediterranean the climb was faster and steeper: in 2012, the number of jobless workers as a share of the workforce was 10.7% in Italy, but had reached 15.9% in Portugal, 24.3% in Greece and 25.0% in Spain (from 8.3% in 2007).

International organisations are predicting a return to positive rates of growth in Europe in the course of 2014. However, the growth that is forecast will be sluggish at best, and may not materialise at all: revis-

ing growth estimates downwards has become something of a rule over the last few years. Even when the economy stabilises for good, given previous patterns of “jobless growth,” it may take many years for unemployment rates in Greece, Spain and elsewhere in the northern Mediterranean to fall to the prevailing levels before the Great Recession.

In other words, the social emergency is here to stay.

The Distributional Impact of the Crisis

The Great Recession is widely thought to have caused poverty and inequality to increase. Nevertheless, predicting the distributional impact of a crisis is less straightforward than may appear at first sight. Its effects on family incomes vary substantially, depending not only on the earnings and employment status of workers directly affected, but also on those of other members of the households in which they live, as well as on the capacity of the tax and benefit system to absorb macroeconomic shocks.

Moreover, the distributional impact of a recession may vary depending on the dimension considered: average living standards may decline, but inequality need not rise, whereas the estimated effect on poverty will be less pronounced when the relevant threshold is set as a proportion of average (or median) incomes than when it is held constant in purchasing power terms.

Generally speaking, the distributional effects of a recession take time to materialise. For instance, poverty continued to fall throughout Europe until 2009, while the economy had been in trouble since 2007. On the other hand, income data (whether from national household budget surveys or cross-national statistics like EU-*Statistics* on Income and Living Conditions [EU-SILC]) tend to become available

two or three years after their reference period. Hence, the latest results currently available refer to the year 2011. In other words, for the time being, official data only cover a limited sub-period of the Great Recession.

Official Figures on Poverty and Inequality

Perhaps paradoxically, Eurostat statistics show that the poverty rate in the EU has barely budged at all, from 16.5% in 2007 to 16.9% in 2011. In the northern Mediterranean, the poverty rate in Italy and Portugal was actually lower in 2011 than it had been in 2007, while in Greece and Spain it had gone up to 21.4% and 21.8% respectively.

Part of the explanation is, of course, that poverty is defined with respect to a relative threshold (60% of median income), which in good times goes up, and in bad times down. The assumption behind relative poverty is that people compare their material condition with that of others in the society in which they live. This seems reasonable enough, until we remember that in times of rapid change people also tend to compare their current standard of living with the one they enjoyed in the recent past.

This is why having the poverty threshold anchored at a moment in time can also be useful. As a matter of fact, Eurostat does just that, publishing figures on the proportion of people with an income below 60% of the 2005 median (in real terms). Between 2009 and 2011, in the EU as a whole that proportion went up by 2.1 percentage points, while the magnitude of change in the northern Mediterranean ranged from 0.8 percentage points in Portugal, 2.4 in Italy, through to 6.4 and 6.7 percentage points in Spain and Greece respectively.

Changes in inequality were even less dramatic, whether on the basis of the Gini coefficient or the S80/S20 ratio (showing the income of the richest 20% of population as a multiple of that earned by the poorest 20%). On the whole, relative to 2007, inequality in 2011 seemed to have risen considerably in Spain, slightly in Greece and Italy, and to have actually declined in Portugal (though it was rising even there).

On the basis of the above, one is tempted to conclude that recent changes in the distribution of incomes are much less significant than they are usually made out to be.

Other evidence

As a matter of fact, even official statistics provide plenty of cause for concern. According to Eurostat, the proportion of those in arrears on mortgage or rent payments in the EU as a whole has gone up, from 3.8% in 2007 to 4.4% in 2011. In Greece, it has doubled, from 5.5% to 11.0%, while elsewhere in the northern Mediterranean it has fluctuated around the 5% mark. Focusing on households with children and incomes below the poverty line, the share of those affected ranged from around 10% in Spain, 15% in Italy (near the EU average), almost 18% in Portugal, and as much as 30% in Greece.

The amount of medical care that was not given because it was too costly offered another insight to the hardship faced by ordinary people. Among the poorest 20% of the population, that indicator was clearly on the rise in Greece and Italy, standing at 10.2% and 11.3% respectively (in 2011). However, in Portugal it was declining (to 2.2% in 2011), while in Spain it remained consistently under 1% – which was well below the EU average, and an excellent performance by any standard.

While official statistics and other hard data lag behind, impressionistic accounts and soft data paint a starker picture. Civil society organisations, such as Caritas (Leahy et al. 2013), in touch with harsh realities on the ground, are raising the alarm. In countries most affected by the crisis, and that includes all of the northern Mediterranean, low-income families are struggling to make ends meet, as jobs and earnings have been hit by the recession, prices (and taxes) are rising, and access to essential services such as health care is not always what it used to be. The above examples, among many other things, show that it is still too soon for the full implications of the crisis to emerge (let alone to register on the radar of official statistics). They also show that policy responses matter.

The Welfare State as an Automatic Stabiliser

Helping individuals cope with job loss and income loss is the “core business” of the Welfare State (Castles 2010): its role is to support those affected with benefits in cash and in kind. As a result, well-functioning systems of social protection increase

spending when the economy goes into recession, and scale it back again as it recovers. In other words, the Welfare State can be an effective “automatic stabiliser” (Basso et al. 2012).

Available data show that, at least in the first stage of the current crisis, European welfare states performed that role quite well. Expenditure on social protection as a share of GDP went up in the EU, from 26.1% in 2007 to 29.4% in 2010 (latest available data). If anything, social spending in the northern Mediterranean increased by even more: to 29.9% in Italy, 29.1% in Greece, 27.0% in Portugal and 25.7% in Spain (even in the latter case, a sharp rise from 20.7% in 2007).

There are signs, however, that more recent policies have begun to roll back social expenditure (Guillén et al 2012). This could be thought of as something normal, part of the “automatic stabiliser” role of the Welfare State; except for the fact that projections for 2011-2014 (SPC 2013) show that social protection expenditure in all four countries considered here is forecast to decline (or, at best, as in Italy, to level off), even as unemployment is expected to increase (or, at best, as in Greece, to remain at very high levels).

The Welfare State in the Era of Austerity

The contraction in social spending is, of course, directly linked to the fact that northern Mediterranean countries have been subject to an austerity regime, at varying degrees of harshness. Rising fiscal deficits and/or high levels of sovereign debt in the previous decade have raised the cost of lending for these countries. In the cases of Greece (since May 2010) and Portugal (since May 2011), the resulting fiscal adjustment is being attempted under the joint supervision of the EU, the European Central Bank and the International Monetary Fund, which means national governments have effectively lost much (though not all) control over budgetary decisions. In the case of Spain, whose request for financial assistance was approved by the EU in July 2012, “conditionality” is less strict. Finally, while Italy (unlike Greece and Portugal) is not a “programme country,” and (unlike Spain) has not requested financial assistance, austerity there is dictated by the need to appease markets, whose nervousness at the country’s high public debt takes the form of large “spreads” on Italian

bonds (i.e. interest rate differentials relative to more secure investments such as German bonds).

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In this context, the Welfare State has been identified as a possible source of fiscal savings. In Italy, Spain and Greece, the age of retirement has been raised and the pension formula has become less generous. Social benefits (especially in Greece and Portugal) were cut, or abolished altogether, while eligibility conditions were made stricter. Cost containment in health care was introduced to eliminate waste and inefficiencies, e.g. as regards spending on pharmaceuticals. However, funding cuts often disrupted services, while co-payments and other user charges raised barriers to access.

As the recession deepened, austerity policies seemed to become harsher. In Greece, under the 2013–2014 spending review, aimed at saving 5% of GDP in 2013 and a further 2.25% of GDP in 2014, massive cuts in social spending and increases in social contributions were identified as a key source of fiscal consolidation, providing 45% and 5% of total savings respectively (Matsaganis 2013). In Portugal, changes affected the guaranteed minimum income programme, one of the greatest innovations in southern European social policy in recent decades: changing eligibility rules (mainly by adopting a less generous equivalence scale), while keeping the minimum threshold unchanged in nominal terms (as in 2008), was estimated to reduce both the number of people claiming benefit and the mean transfer per person, resulting in a 45% reduction in the total cost of transfers under the programme (Rodrigues 2013).

The Future of the Welfare State

Reports of the Welfare State’s imminent dismantlement seem greatly exaggerated: after all, this is an

institution absorbing between one quarter and one third of national income in all Europe, including the northern Mediterranean where social spending in recent years rapidly converged to the European average. Nevertheless, there is little doubt that the austerity has reduced the supply of social protection, just as the recession has raised the demand for it to historical highs.

Furthermore, even though the “retrenchment” of some social programmes can certainly be viewed as necessary to eliminate inequalities in treatment, and hence to “recalibrate” the Welfare State towards new social risks and in favour of less protected categories, a certain asymmetry can easily be identified. Cuts have been deep and systematic, but reforms that restore equity as well as efficiency have been pursued less consistently, while measures to strengthen the social safety net have been rare (Ascoli & Pavolini 2012).

With the IMF acknowledging the need for policies to encourage growth, enthusiasm for austerity seems to be waning. But countries like Greece stand little chance of returning to the carefree days of “borrow and spend.”

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In any case, the survival of the Welfare State in the northern Mediterranean, as everywhere else, will depend on the capacity of domestic actors to design social policies that can meet the “traditional” needs of the poor, the unemployed, the sick, the old, as well as the “new” needs of youth, women, immigrants, non-standard workers and others; and at the same time to convince taxpayers (and voters) that helping pay for such policies is consistent with the “common good,” and the requirements of a prosperous and dynamic economy.

This is likely to prove far from easy – but is certainly not impossible.

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