STUDY

Budget Consolidation and the European Social Model

The Effects of European Austerity Programmes on Social Security Systems

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- The financial and economic crisis is intensifying the pressure for budget consolidation, increasing the likelihood of cuts in social services throughout Europe. One government after another is bringing forward a budget consolidation programme. Cuts are envisaged above all in social services and so the question arises of what effects this will have on welfare states in EU member countries and on Social Europe in general.

- In this study cuts in social systems are analysed and compared, both planned and already undertaken. Regardless of the different magnitudes of the austerity efforts and the policy fields concerned there can be no doubt that all austerity programmes are regressive in nature and that the option of raising incomes is being exercised far less frequently than spending cuts – and this applies especially in the social realm.

- Summary: The relatively close connection between economic development and the level of social security in Europe is continuing to dissolve. At the same time, social policy at the European level remains the Achilles heel of European integration. There is neither a uniform European Social Model nor has there been any attempt to rectify the legitimacy deficit of European integration by including social security systems in the EU governance system beyond mere lip service. Now the austerity policies of European states are increasing the risk of further social dumping processes.

Content

1. Social Policy in the European Unification Process

It is an open secret that the welfare state has become a basket case and must therefore be reformed or at least reconstructed and modernised. Globalisation and European integration, demographic change and individualisation processes in society have, slowly but surely, eroded the welfare state foundations of EU member states. If the renovation work does not start soon, according to the conventional wisdom, the welfare state will collapse under the weight of its costs and the burden of redistribution: »rebuilding means preservation«, in other words. The German Social Democrats, within the framework of their debate on the »preventive welfare state«, have already found a new label for a concept that has not yet been clearly defined, while in the social science debate one talks about the »activating« or »social investment« welfare state in order to distinguish it from the »active« and »structurally and socially conserving« welfare state of the past and present (see Heinze 2004; Behrens et al. 2005).

Before we turn to the development trends of European welfare states – the »European Social Model« – in particular under conditions of the general need for consolidation in the face of soaring public debt due to the recent global financial crisis, first a few taxonomical remarks.

1.1 Social State or Welfare State?

In general usage, but also in the social science literature, the terms »social state« (»Sozialstaat«) and »welfare state« (»Wohlfahrtsstaat«) are virtually synonymous. By contrast, we shall use the term »welfare state« only when state intervention involves not just social adjustment or social protection but broader social and economic policy change to increase societal welfare. »Social policy« in the strict sense is to be reserved for protection against the five basic life risks – old age, illness, unemployment, accident and poverty – and »social state« refers to this core. Welfare state policy, by contrast, requires, besides the instruments of »social policy« in the strict sense, collectively determined and democratically legitimised objectives (for example, the degree of redistribution, possible limits to be imposed on the market or a willingness to pursue »decommodification«) and a broad-based embedding of social policy, ranging from macroeconomic control through family policy to education policy as the basis of participation and inclusion which is not exclusively market-oriented.

Within the framework of this distinction we shall be concerned here only with the social state in the EU – and the European Social Model will refer precisely to that – not the welfare state in the broader sense. This is owing, on the one hand, to a necessary limitation of the object of investigation, while at the same time reflecting the abovementioned change of perspective with regard to the allocation of »social policy« tasks after the end of the »Keynesian welfare state«. Three objective processes:

- globalisation/European integration
- individualisation
- population ageing

have led, against the background of the neoliberalism which has dominated for the past three decades, to social policy being understood almost exclusively in supply-side terms as a distortion of allocation due to adverse incentives. In this view, the collective redistributive – justifiable in demand-side terms – content of social policy needed to be scaled back in favour of greater individual equivalence and, where possible, provided privately so that both in supply-side terms and as regards competitiveness the greatest possible efficiency and financial sustainability (economisation) would be ensured. The scaling back of the redistributive component of social policy within the framework of the welfare state whose origin, besides its demand theory justification, also included[1] a symmetrical understanding of social security and thereby the recommodification of the object of social policy, is justified, at least in the field of labour market policy, by the »inclusion« of those who otherwise would be »forced« into inactivity by the caring welfare state. »Inclusion« no longer means, in accordance with the change of perspective from the welfare state to the social state, participation in society by means of relative income insurance and social policy backing but increased pressure towards (labour) market participation.

1. Reisz (2004) talks about »symmetrical solidarity« which is based on equivalence and mutuality. It is contrasted with the »asymmetrical solidarity« of the new approach which is based on caring, but paternalistic giving on the part of the strong and one-sided receiving on the part of the weak.

It will also be demonstrated by means of the distinction between welfare state and social state that the outcome of the »social policy modernisation efforts« will not be the end of the social state, but does involve a clear-cut change in its substantive arrangements, the balance between collective and individual contributions, funding and also benefit eligibility and legitimacy. In this sense the former contrast between Europe, with its developed *welfare states,* and the USA, with its limited *social state,* is brought out more clearly. And if one takes the development outlined above into account,[2] it is obvious why Jens Alber (2006) no longer recognises any systematic difference between Europe and the USA which would justify a special emphasis on a »European Social Model«.

1.2 Different Models of the Social State in the EU, or: Is There a European Social Model?

Although social policy has played some role[3] since the beginning of the institutional process of European integration and, within the framework of the EU's Lisbon reform treaty even became part of the treaty with the incorporation of the Charter of Fundamental Rights, nevertheless, it is fair to say that there is a »social deficit« (Joerges/Rödl 2004). This assessment stems, on the one hand, from the largely economic motivation of the European integration process and, on the other hand, from the fact that the hopes that advancing economic integration would almost inevitably lead – both in functional terms and as a matter of legitimisation – to the enhancement of the social component have not been fulfilled (see Aust 2004: 128ff). Since the substantive underpinning of social policy remains exclusively a national affair, »European social policy« remains limited to the regulation of health and labour law.

European social states have not only developed fairly disparately in historical terms, but they also correspond to the variety of European economic models (cf. Strünck 2008). This relates to the extent of the provision of social security, the level of decommodification, the manner of funding, the structural allocation of social security needs in terms of the various exigencies and their institutionalisation. According to the well-known categorisation by Esping-Andersen (1990) we can therefore distinguish between at least three types of social state in the EU:

(i) the social democratic or Scandinavian type
(ii) the social conservative or continental type
(iii) the liberal or Anglo-Saxon type

With eastern enlargement this variety is likely to have increased (see Busch 2005: 24): for the time being, therefore, one cannot talk of one or *the* European Social Model. To be sure, the abovementioned transformation and modernisation process of the various social states in the EU may converge into a common model; on the other hand, the »European Social Model« can also serve as an ideal model for a (new?) form of integration capable of distinguishing itself more clearly again from the US model.

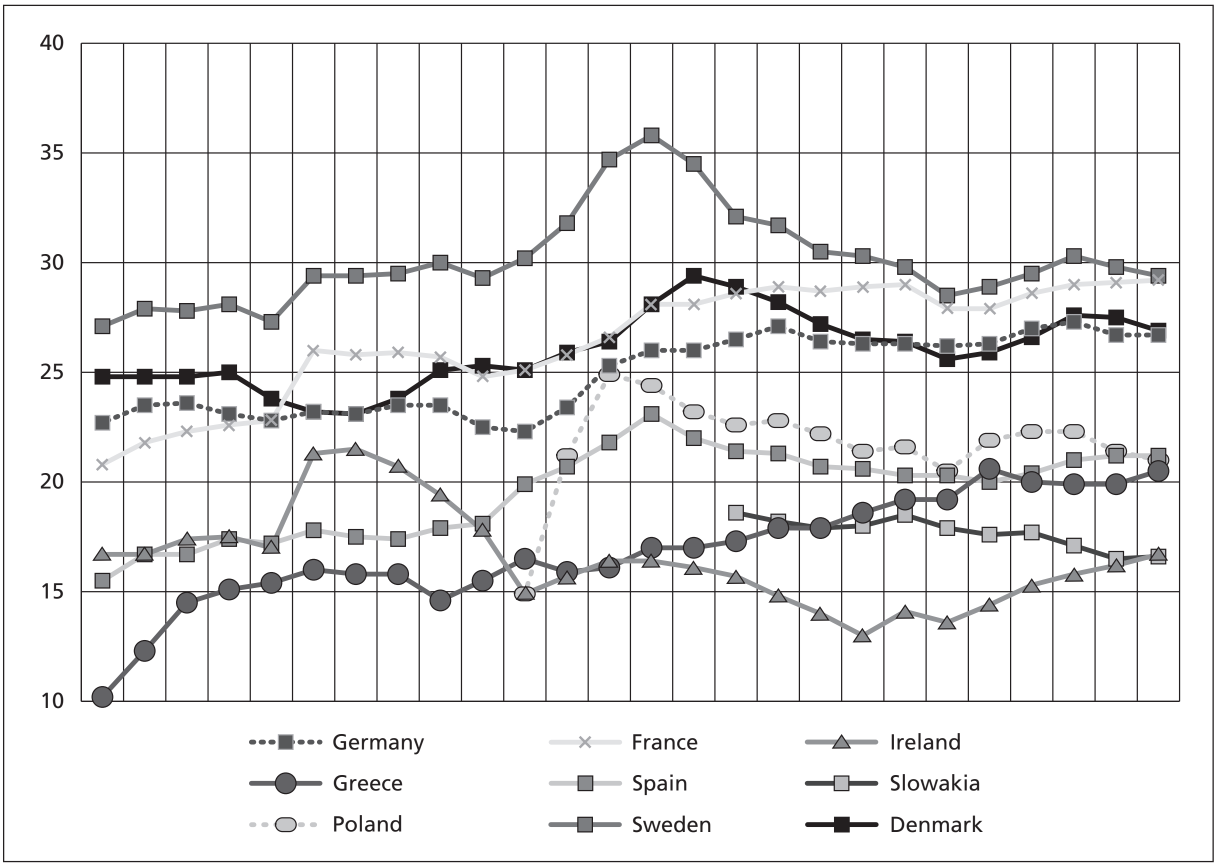
1.3 European Integration as Motor of Convergence?

The literature on the future development of the social state in the EU is voluminous and inconclusive. Although the abovementioned objective factors and, in particular, the requirements of European integration affect all member states, national adaptation paths can vary considerably: On the one hand, one may agree with Sapir (2005) and Sapir et al. (2003) who, against the background of neoliberal ideologising and the EU integration architecture, take the view that only the liberal model is capable of surviving and, therefore, predict a corresponding convergence; on the other hand, however, one might share Strünck's (2008) assessment that not only is the social state model shaped by the underlying economic model, but also the relevant modernisation and adaptation paths are fitted to the economic model and, consequently, divergences will remain and, at best, over the long term various hybrid models will emerge. To some extent between these positions lies Busch (2005; 2009) who claims to recognise a convergence towards a hybrid model in the system of market states – which is the result of the EU's neoliberal architecture (see also Streeck 1996) – which takes account of the fact that social systems have become significant factors in competitiveness, in particular in the single currency area (that is, EMU). Within the framework of the method of open

2. Which Lamping (2008: 120) outlines as follows: »Western Europe is heading towards post-heroic social states which have it in common that they are withdrawing – as in Germany – their promises of security, reducing aspects of social equality and consolidating the role of the (regulated) market as unreliable producer of social security«.

3. For example, in the still very homogenous European Economic Community (EEC), which consisted of only six member states, the harmonisation of social systems was considered so that freedom of movement (worker mobility) should not be impaired.

Figure 1: Social Spending as a Percentage of GDP (1980–2005)



Source: OECD, Country statistical profiles 2009.

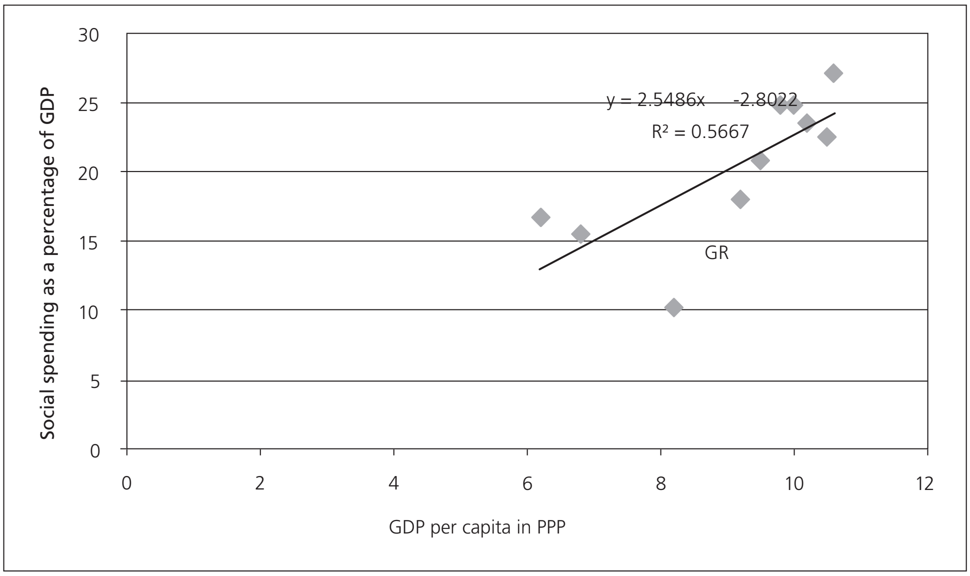
coordination – the soft form of governance which characterises EU social policy – forms of recommodification, privatisation and cuts in social security may be discerned practically everywhere. He therefore comes to the conclusion that: »To summarise, we can say that reforms of the welfare state in the EU exhibit considerable convergence in the East and the West. Given the common objective problems … this is not surprising. However, there are national differences and diverging political constellations at the level of the member states, which in the system of market states could reinforce the danger of dumping and downward spirals.« (Busch 2009)

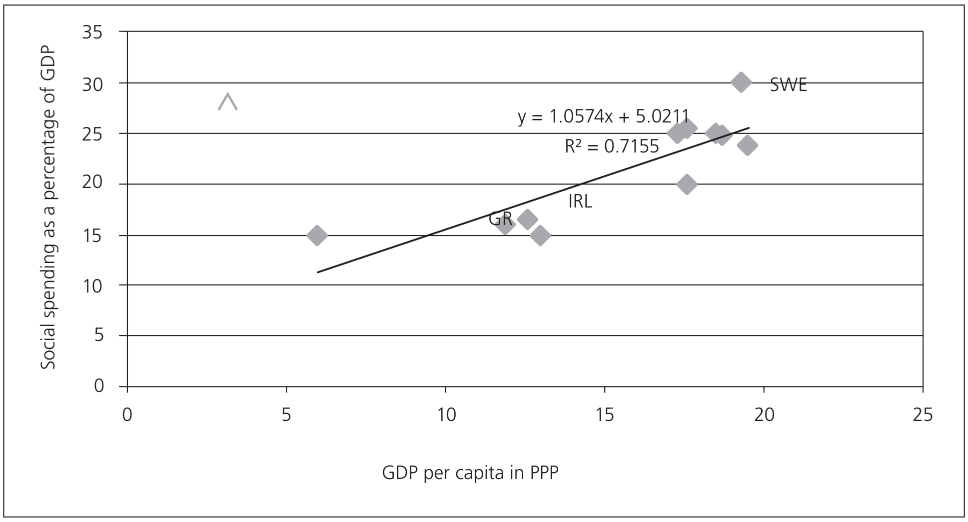
Similarly, Lamping (2008: 116) argues that: »In the rift between (European) trade and competition regimes and (national) social policy European market policies have developed which endanger the social achievements of the member states to a considerable degree«. He is referring here, alongside social policy as a competitiveness factor, primarily to the role of »negative (market creating) integration«, which with the (over)emphasis on the four economic freedoms grants the European Court of Justice (ECJ) a lot of leeway for law-making likely to undermine the social state.

There is no room here to go into detail concerning the individual structural features of the putative convergence process. Ultimately, however, »economisation« is tied up with a scaling back of the level of social security with a view to reducing alleged problems of allocation and competitiveness. If one looks at the relative social spending of various countries representing different models (Figure 1), however, a general downward spiral of levels of social security is not apparent.[4]

4. Certainly, it should not be overlooked that a constant rate of social spending does not necessarily mean a constant level of social security if the number of benefit recipients increases due to population ageing, rising poverty or unemployment.

Figure 2a: Correlation between Social Spending and Per Capita Income (1980 and 1990)

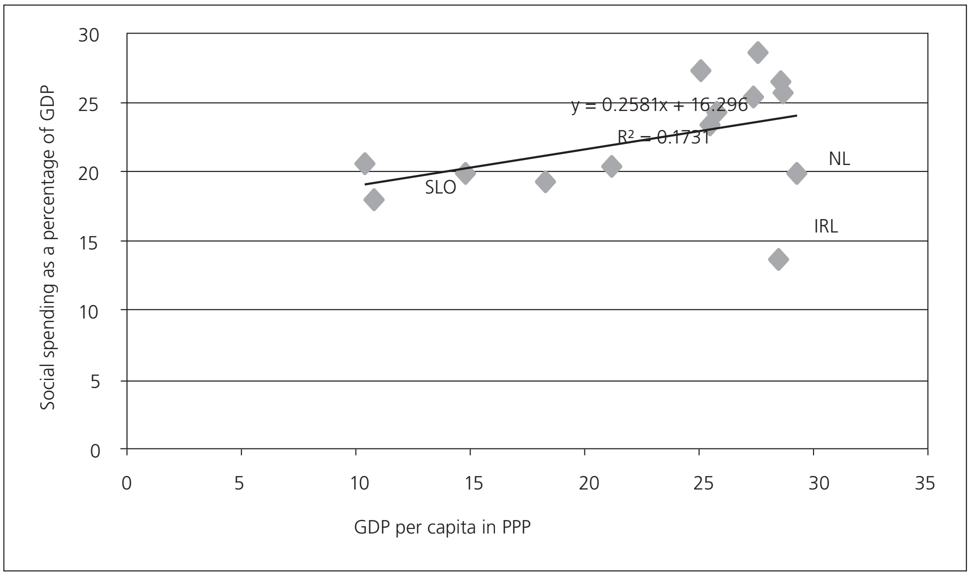


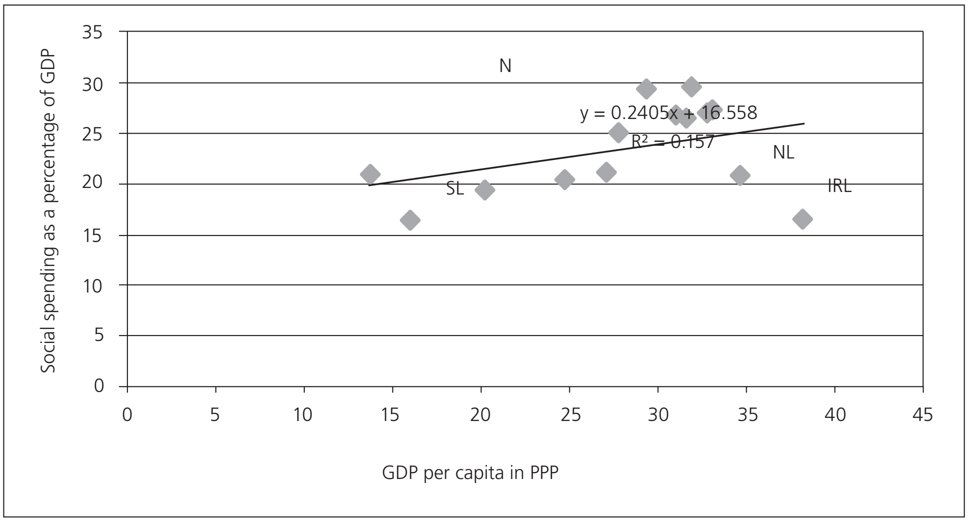


Some member states, regardless of their social security model (France as an example of the continental model, Denmark as an example of the Scandinavian model and Poland as representative of the CEE countries), even register increasing social spending rates and only in a few countries – for example, Ireland as representative of the liberal model, Slovakia as representative of the CEE states and Sweden as representative of the Scandinavian model – is there a falling trend with regard to social spending rates, and in all cases in terms of a more up-to-date time horizon stagnation can be discerned rather than a clear (downward) trend.

If, therefore, convergence towards a generalisable »European Social Model« is to be linked to serious endangerment of social achievements in the EU other evidence has to be produced. In Figures 2a and 2b, therefore, not only the development of social spending rates is taken into account but also the state of development of the national economy (GDP per capita). Social security,

Figure 2b: Correlation between Social Spending and Per Capita Income (2000 and 2005)





Note: The following countries were selected: DE, FR, NL, DK, IT, GR, ES, BE, SWE, A, IRL, SLO, CZ, PL.

Source: OECD, Country statistical profiles 2009.

after all, is a public good demand for which on the part of consumers (citizens) increases with rising incomes (positive income elasticity).

It would be evidence of dumping not only if social benefit rates are falling in absolute terms but also if these rates do not correspond to economic development, as long as a positive correlation can be determined between the two. Figures 2a and 2b identify this correlation at various time points: with regard to 1980 and 1990 we can talk of a high and even increasing coefficient of determination, regardless of variations in terms of social state models. The level of the rate of social spending (57 per cent and 71 per cent, respectively) is explained, on this basis, by the state of economic development: the increase in the coefficient of determination can be understood primarily as a result of the fact that Greece implemented an above-average increase in social spending after EU accession and sought to adapt to Europe's (material) development path. The picture changes, however, when we look at

2000 and 2005: now the close correlation is largely dissolved – only around 16–17 per cent of social spending can be explained on the basis of the state of development of member states' economies. Responsible for this is at least relative dumping in countries of the liberal (Ireland) and CEE (Slovakia) type which did not develop their social states in accordance with their growing economies, but countries of the continental type (the Netherlands), too, contributed – by scaling back their social states – to making social policy in the EU increasingly a location and competitiveness factor.

1.4 The European Social Model under Pressure

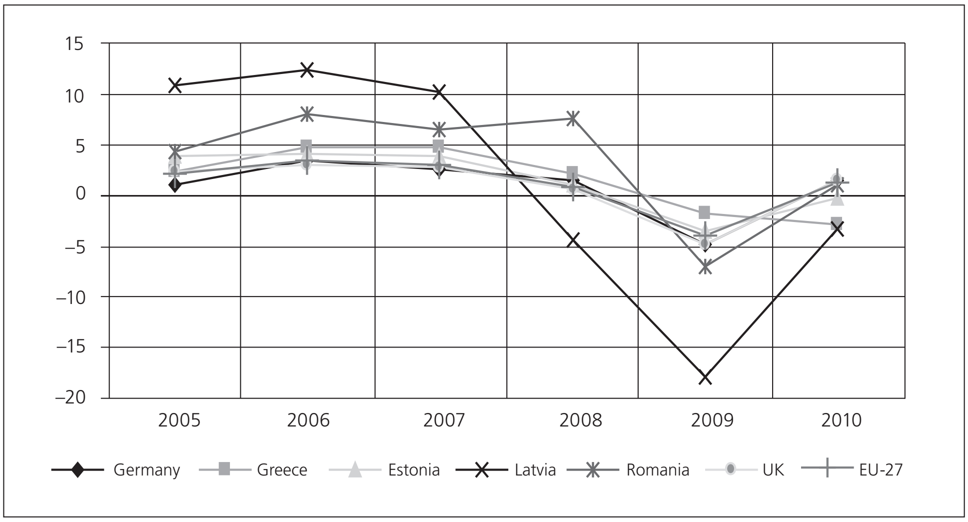
The developments in social states depend on a variety of real political power constellations; they do not depend on economic-functional or ideological considerations alone. Despite numerous objective and subjective negative factors the European modernisation process is not simply a matter of a race to the bottom with regard to social standards. On the other hand, the data suggest that the material development path discernible in the 1980s and 1990s is being abandoned or at least will no longer shape the frame of reference. The bigger the objective negative factors and the change of perspective with regard to the welfare state in the direction of »economisation« the sooner a corresponding development is to be expected. To that extent it is important whether the »European Social Model« – in particular after the sobering experiences of European political actors with the at least sceptical, if not hostile attitude of EU citizens,[5] which also manifested itself in the failed attempt to obtain agreement on a European Constitution – is developed as a positive vision of a social or welfare state which differs from the US model.

The strategy of former Commission President Jacques Delors consisted precisely of this attempt to reduce the »social deficit« by paying closer attention to the social component. Delors is associated not only with further economic integration within the framework of the single market and monetary union, but also with the shaping of the »European Social Model«. Delors was convinced that market creating integration measures alone would not be sufficient to overcome the Euro-scepticism of the 1980s (»Eurosclerosis«); in particular, the increasing incongruence of the reach of the market and market regulation threatened to put national social standards under pressure revealing the limits of »semi-sovereign nation states« (see Leibfried/Pierson 1995). For the socialist Delors, therefore, economic and social integration still presupposed one another and his vision of the »European Social Model« may still be regarded as a serious attempt to defend Europe's welfare state traditions and to understand it as a source of legitimation for European integration. Later European Commissions, therefore, must be regarded as important motors of the change of perspective which Peck (2001) describes in the abovementioned sense as a transition from welfare to »workfare« (see, for example, Aust 2004; Hofbauer 2007). In this way those forces in the European Commission have won through »in the struggle concerning European integration« which in the Delors Commission were still kept in check by the white paper »Growth, Competitiveness and Employment« (European Commission 1993), sometimes described as »neo-Keynesian« (Schmid 1995: 258). This occurred, astonishingly, at a time when a window of opportunity was opened up by the coming to power in many – and indeed the most important – EU member states of Social Democratic governments for establishing or restoring a genuinely »Euro-Keynesian« development path. The major discord which arose in the SPD during the first Schröder government with Oskar Lafontaine's resignation from all Party and government posts to become a »left-wing supply side politician« (Priddat 2001) exemplifies the uncertainty about the future economic and social policy course of European social democracy (see Aust 2004) and explains why this window of opportunity soon closed again, having been missed.[6] It also explains why the European Commission found it easy to assert its ideas on the »social investment state« and the human capital-oriented and incentive-compatible notion of employability in place of the quantitative (level of) employment as the connotative basis of the »European Social Model«, as well as the employment policy incorporated in the Amsterdam Treaty as further source of legitimation. For Hofbauer (2007) the Commission has taken advantage of ideas which the general public view positively – such as the European

5. Deppe/Felder (1993) spoke early on of a »Post-Maastricht crisis« which even the subsequent Treaty reforms were unable to overcome.

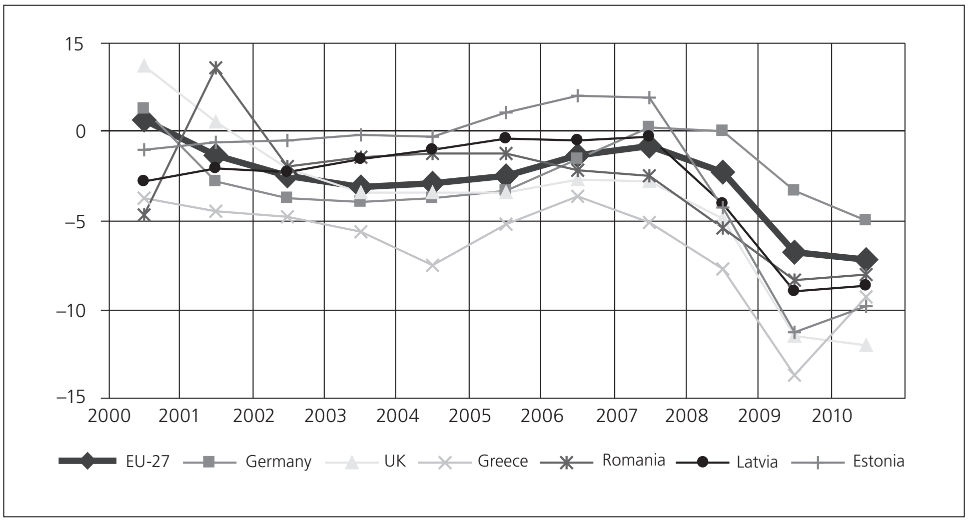
6. In fact, at the Cologne EU summit in 1997 it was still possible to extend the European governance system to encompass the »European Macro-dialogue«. This attempt to improve coordination of macroeconomic policy – virtually the necessary macroeconomic embedding of a European welfare state and largely contrary to the previous governance system – never really become operational (see Heise 2001).

Figure 3: Development of Growth in Selected EU Countries



Source: European Economy, Statistical Annex, spring 2010.

Figure 4: Budgetary Balances in the EU (as a percentage of GDP)

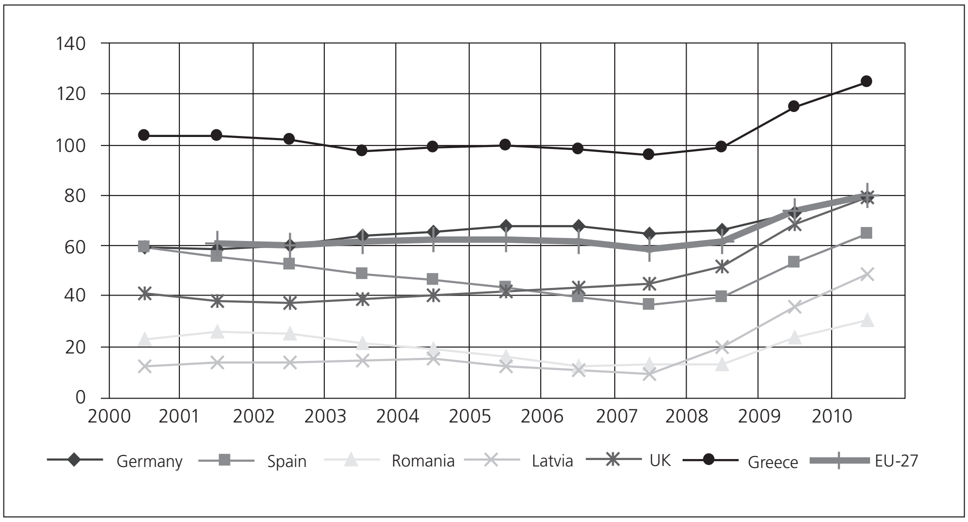


Source: European Economy, Statistical Annex, spring 2010.

Social Model and employment policy – to enhance the legitimacy and acceptance principally of economic integration, hiding and reinterpreting the »economisation« of the social behind the apparently familiar. Aust summarises as follows: »This strategy represents a conscious break with the traditions of the European Social Model, something which it also signals by its call for a ›new‹ model … Characteristic of this dominant integration strategy is that it largely dispenses with binding regulations at the European level. Europeanisation in the sense of institution building does not play a major role in the ›new‹ ESM« (Aust 2004: 142).

Whether the recent world financial crisis will lead once again to the kind of »violent social conflicts … through which emancipatory forces will set the agenda and the

Figure 5: Public Debt in the EU (as a percentage of GDP)



Source: European Economy, Statistical Annex, spring 2010.

currently dominant projects will be rejected« (Brand 2006: 169) remains to be seen. Besides the temporary loss of legitimacy of orthodox neoliberal economic and financial ideas at the ideological level (Heise 2009), at the level of political practice the global financial crisis has, for the time being, imposed an enormous strain on public-sector budgets.

Figures 3 and 4 present the sometimes dramatic rise in new public borrowing and the underlying development of growth in the EU. Almost in parallel in 2009 the whole of Europe entered a deep depression of a magnitude – and extent – not seen since the world economic crisis at the beginning of the 1930s. Different from the 1930s, however, has been the level-headed reaction of governments and the positive effects of social security: by means of discretionary economic stimulus packages, far-reaching financial market stabilisation programmes and socially responsive »automatic stabilisers«, further destabilisation of the real economy and the complete collapse of the international financial markets have been prevented – although with significant consequences for state budgets. Structural new borrowing everywhere has exceeded the level of the balanced budget foreseen by the Stability and Growth Pact and the »automatic stabilisers« are everywhere adding several percentage points to this. Germany, although affected slightly more than average by the financial crisis, is experiencing only mild upheavals. This shows the two faces of Germany's strong export orientation: the major economic downturn has been countered less by discretionary measures (see Heise 2010a) than by trust in the competitiveness of the German economy in the surprisingly strong upswing of, in particular, some emerging countries in 2010. Other countries – especially Greece, Spain and the UK – have relied more on their own economic stabilisation measures or need more financial resources to stabilise the banks.

Figure 5 depicts the effects of budget deficits on the level of public borrowing. Everywhere, public debt is rising sharply, thereby cancelling out a decade of – albeit modest – consolidation. This demonstrates the level of consolidation needed if the debt limit of 60 per cent of GDP laid down in the Stability and Growth Pact is to be maintained as the measure of sustainable finance policy: only Romania and Latvia, which started out from very low levels of debt in the wake of their social and economic transformations, will manage to keep below the threshold in 2010. But even on the basis of this fact it cannot be called into question that the structural deficits in relation to economic growth must be cut considerably if a permanent increase in public debt is to be prevented. The perennially sensitive issue for finance policy is whether this is to be achieved through tax rises or tax cuts, or through cuts or increases in (social) consumption or investment. The conventional view that cuts in (in particular social) consumption are to be preferred to tax increases is controversial, to say the least (see Heise 2004).

2. Budget Consolidation in Selected European Countries

Having concerned ourselves in the previous section with a theoretical reflection on the classification and development of social security systems in European countries, in this section we shall take a detailed look at the effects and changes which accompanied the recent economic crisis. At the end of 2008, economic growth in Europe collapsed, unemployment increased sharply in many member states and, in an attempt to prevent a long-lasting recession, the member states introduced a variety of measures to stabilise the banking system and stimulate the economy. The automatic stabilisers also increased public deficits so that virtually no country was able to adhere any longer to the Stability and Growth Pact. After these short-term rescue actions the focus has shifted to the rising debt burden of state budgets which has resulted from the crisis.

In October 2009, the member states commenced a fiscal policy »exit strategy« in order to reduce the public borrowing which had increased enormously since the outbreak of the economic crisis. This exit strategy is supposed to continue beyond the scaling back of economic stimulus packages and to be supported by means of further savings and structural reforms, without restricting growth potential. While the European Commission suggests that consolidation measures be implemented at the latest in 2011 most states adopted far-reaching cuts and reforms in 2010 and some, such as Latvia, began the consolidation process as early as 2009. But what kind of savings have the member states implemented? And what have been the effects of austerity programmes on social security systems?

While no EU member state has been spared the need to take consolidation measures, the extent and nature of the measures involved and their effects on social security systems have not yet been examined systematically and comparatively. The analysis which follows constitutes a contribution to that and an attempt to discover whether and how member states' social security systems have been affected by the cuts and the structural reforms. We shall also evaluate whether the crisis has functioned as a motor of social policy convergence among the member states. Building on the previous theoretical discussion of the development of social security systems in Europe we shall assume that there are both similarities between countries and types of system and specifically national, path-dependent developments with regard to social security systems. In particular, it is assumed that the crisis has triggered further convergence towards a »social investment« system which is largely undoing the decommodification of social policy.

In what follows we shall examine in some detail the consolidation programmes of seven European countries and their effects on social security systems. In the foreground are a number of states which were particularly hard hit by the crisis and which also reflect the plurality of types of social state in Europe. While Germany represents the continental type, the UK represents the liberal model, Greece and Spain the Southern European type, Latvia and Romania the Central and East European type and Iceland can be assigned, in the broadest sense, to the social democratic model.

In a first step the country analyses will show how economies were affected by the crisis and, in a second step, what the reactions – in other words, the consolidation measures – were. Both short-term, transitory social policy cuts and long-term structural reforms will be considered, which are supposed to promote the development of sustainable structurally balanced state budgets. Finally, the responses to the crisis will be examined within the framework of a wider social policy discourse. How were the austerity programmes legitimised? And what counter-ideas or movements have formed? Particular attention will be paid here to whether a European pattern of argumentation has emerged which, taking its cue from the European Commission, emphasises the social investment and economic dimension of social states.

2.1 Germany and the Economic Crisis

Is Germany really an international *wunderkind?* The country appears to be overcoming the biggest crisis of the post-War period as if nothing had happened. Although growth fell by 4.7 per cent in 2009, the most severe recession since the founding of the Federal Republic, in the third quarter of 2010 the German economy registered its highest rate of increase for a long time with 3.9 per cent (Eurostat 2010). And not only is growth doing well, but unemployment is falling. Pragmatic measures such as the extension of short-time working and economic stimulus programmes, as well as Germany's pronounced export orientation stabilised the economy. Although pre-crisis GDP has not yet been restored, nevertheless, the crisis is a fading memory and the mood in the country is improving.

The public are even contented with the budget consolidation reforms of the conservative-liberal government. With the apparent end of the crisis political and public attention has shifted to rising public borrowing. Although with a funding deficit of –3 per cent and a debt level of 73.4 per cent in 2009 (Eurostat 2010) Germany is doing comparatively well, the Merkel government – in the form of the Supplementary Budget Act (2011) and the medium-term Financial Plan (2010–2014) – has passed one of the biggest austerity plans in the history of the Federal Republic. Besides reductions in subsidies and savings in public administration, social benefit cuts are also planned, aimed in particular at boosting personal responsibility and work incentives for those without a job.

The German government's austerity programme – the so-called »Package for the Future« (»*Zukunftspaket*«) – is in keeping with the basic principle: »consolidation to promote sustainable growth« (Federal Ministry of Finance 2010). Budget consolidation is supposed to lead to more employment and thus contribute to lower social spending and rising tax revenues. Social policy is largely subordinated to growth targets. This is because in order to »reduce high budget deficits and thus to halt rising public borrowing every measure must be taken towards sustainable consolidation« (Federal Ministry of Finance 2010a). This basic idea is being used to legitimise the German government's rigorous approach: the cuts have not fallen upon the causes and instigators of the crisis, but on those on low incomes and social benefit recipients, making them the main victims of the debt crisis. In what follows we shall analyse the consolidation measures in detail, particularly within the framework of the current development of German social policy.

2.1.1 Cornerstones of the German Austerity Programme

With its Financial Plan up to 2014 and the Federal Budget 2011 the Merkel government laid down the basic pillars of German consolidation policy: by 2014, 80 billion euros are to be saved, representing an annual 0.8 per cent of GDP. In this way by 2013 the deficit limit of the Stability and Growth Pact is to be maintained and by 2016 the structural deficit is to be brought down to 0.35 per cent of GDP, as prescribed by the new debt regulation in the Constitution. The focus of the German austerity package is spending, the idea being to make a start »where savings and higher revenues are possible without endangering the growth potential of the economy and the social balance« (Federal Ministry of Finance 2010a). Nevertheless, the German government also plans substantial cuts in the social budget, making up 30 per cent of the whole consolidation programme. This is because sustainable budgetary restructuring can succeed only »if this sector also makes a targeted and fair contribution« (Bundesregierung online 2010a). But what does »fair« mean? And who gets to decide what measures of fairness and social balance will be used?

The conservative-liberal government plans, besides cuts in parental benefits for recipients of so-called »unemployment benefit II« (which consists of the former unemployment benefit and transfers from the social welfare system), to transform statutory benefits into discretionary benefits and to abolish subsidies for heating and the state pension contribution for this group. At present, persons receiving unemployment benefit II for a year receive an additional pension entitlement of 2.2 euros a month. Since this sum is insufficient to obtain an adequate pension, according to the government, the coalition is now abolishing it completely. Besides these measures, which affect the most needy, the government plans cuts in parental benefits and structural changes in health care policy. Even in the latter two areas, in which it would be possible to incorporate an element of progressive redistribution, the government's consolidation policy is affecting those on the lowest incomes.

Parental benefit is the successor of the previous child-raising benefit, which was paid irrespective of whether the parents had a job or not. Hartz IV recipients also received 300 euros a month which is being abolished within the framework of budget restructuring since in this instance basic needs are covered by the standard rates and supplementary benefits. In addition, according to the conservative-liberal government, the additional parental benefit reduces the wage gap and thus the incentive to get a job. As in the case of child benefit, parental benefit will in future be taken into account with regard to Hartz-IV benefits. Furthermore, the wage replacement rate of parental benefit in relation to net incomes of over 1,240 euros a month has fallen from 67 per cent to 65 per cent, while the maximum amount of 1,800 euros a month is retained; the government estimates that around 25 per cent of parental benefit recipients will feel the effect of this. The new parental benefit regulations thus affect in particular Hartz-IV recipients and middle income groups, with better-off families still receiving 1,800 euros and being spared the ill-effects of these measures.

Unlike in most European countries the government in Germany does not adjust old age pensions. However, in previous years the pension level fell due to a number of reforms and the role of private and company pensions increased (see Hegelich and Meyer 2008). Furthermore, the consolidation measures also concerned the health care system (Federal Ministry of Finance 2010c): besides drug companies, doctors and hospitals, in particular those with statutory health insurance have to bear the cost of rising health care spending. Under the health care reform of 2011 health insurance companies can levy an additional contribution from members with the professed aim of »promoting transparency and competition« (Bundesregierung online 2010c). However, the contribution is not income-related and can be regarded as an increase in the flat-rate premium. Given the regressive effects of flat-rate premiums low incomes are comparatively harder hit despite the solidarity surcharge (Leiber and Blank 2010). The reform also abolishes parity of contributions between employers and employees, hitherto a basic principle of German health insurance.

The German government's budget consolidation programme and the social state reforms are relatively low in terms of GDP in comparison to those of other European countries (see also Table 1). This is certainly because of Germany's favourable current economic and thus also budgetary development. Despite the relatively low level of restructuring the reforms are clearly directed towards social policy: the measures have affected the neediest in society – safeguarding or reinforcing social benefits for the unemployed and low earners does not come into it. On the contrary, all »additional« emoluments have been cut in order to boost incentives to get a job and personal responsibility, according to the government. The basic idea of »social balance«, as advanced by the conservative-liberal coalition, can thus be understood not in terms of social inclusion and ensuring incomes, but rather as a turning away from high social benefits and towards individual responsibility and private provision. But is this really a renunciation of existing values or does this development represent a consolidation of the German social model?

2.1.2 The End of the Social Market Economy?

The basic principles of the German social state are oriented towards the notions of so-called Rhenish capitalism and the social market economy. In the welfare state debate the German social state is also categorised as conservative (Esping-Andersen 1990; Schmid 2002): the level of decommodification is not so pronounced as in social democratic states and benefit entitlements are based predominantly on the equivalence principle. Access to social benefits is for the most part organised with regard to employment so that contribution payments and benefits largely correspond and contribute to a status-maintaining system. Nonetheless, the solidarity principle is also significant, requiring mutual responsibility and represents a redistributive element. There is, for example, income support which is not contribution-related and is supposed to guarantee minimum subsistence. The question of how high this minimum should be so that it does not act as a disincentive to work has been high on the agenda in the German debate for several years.

Traditionally, the German welfare state, despite its intermediate level of decommodification, is known for its comprehensive provision. However, statistics show that in recent years social spending has conformed rather to the EU average. While in 2002 it was still about 30 per cent of GDP and thus three per cent above the EU average, by 2007 it had fallen to 27.7 per cent of GDP. Furthermore, the current debate on the national debt has helped to legitimise further cuts in social benefits: according to the government, since social spending »accounts for more than 50 per cent of total spending this sector could not be spared«. Around one-third of the consolidation package will therefore be achieved by cuts in social spending (Bundesregierung online 2010b).

Although the conservative-liberal government promises to preserve the social balance within the framework of its austerity programme, the measures are affecting mainly social benefit recipients and thus constitute redistribution from the bottom up. The measures reduce benefits to a minimum basic income which cover the needs of benefit recipients. The German social state no longer wants to provide additional benefits, such as heating costs and parental benefits. Since the effects of the crisis and Germany's need to consolidate are relatively modest the European debt debate seems to be being used to legitimise cuts in social security at national level. Those who are being asked to pay, therefore, are not those who caused the crisis and are now making large profits and receiving high bonuses again.

Besides the social policy cuts which target the neediest the current reforms also constitute a creeping economisation of the social dimension: the current government's key idea is to create more employment incentives. Among other things, this is being achieved by reducing social benefits in order to activate the unemployed by increasing the wage gap in relation to employment with full social benefits. In addition, everyone has to help to pay down the national debt in order to »maintain the foundations of a solidaristic community for future generations and also to continue to help those who cannot help themselves« (Bundesregierung online 2010b). The political and public debate, therefore, no longer concerns so much what effects social policy is having on direct recipients and their living standards, but rather its overall economic effects with regard to economic growth and the labour market and whether »it advances the use of resources in our country« (Bundesregierung online 2010b).

The »social dimension« of the German market economy is thus being markedly reduced and personal responsibility is being increasingly emphasised. The dominant view seems to be that high and universal benefits are not compatible with an innovative, flexible and employment-promoting policy. This conclusion corresponds to our initial hypothesis that the crisis in Germany has triggered further development towards a social investment oriented social security system. To be sure, there are voices which oppose this dominant liberal paradigm; among others, the trade unions have warned that the austerity package will further exacerbate Germany's social difficulties (ver.di 2010). Whether in future this will lead to a turning away from the path currently being pursued appears doubtful.

2.2 Spain and the Economic Crisis

With the outbreak of the crisis Spain suffered its worst economic setback since its EU accession in the 1980s. The real estate and construction boom came to an abrupt end; investment fell by about 25 per cent; and consumption and the export economy were severely weakened. For example, Spanish GDP registered a fall of 3.6 per cent in 2009, although in the first quarter of 2010 there was positive growth again of 0.1 per cent (Eurostat 2010). The most devastating effects of the economic crisis, however, were on the Spanish labour market: since the end of 2008 unemployment in Spain has risen by around one million, hitting hardest the poorly qualified and those without permanent contracts. At the moment, the unemployment rate is 20 per cent and the youth unemployment rate is estimated at 40 per cent (Kellner 2010).

With this increase in unemployment social spending doubled in Spain, while tax revenues fell dramatically in the course of the crisis. In addition, the government, in cooperation with the other EU member states, adopted a stimulus package, as a result of which Spain's national debt grew: the budget deficit grew from 4.1 per cent of GDP in 2008 to 11.2 per cent in 2009 (Banco de Espana 2010) and public debt grew from 36 per cent in 2007 to 53.2 per cent in 2009, although that is still relatively low in comparison to the EU27 average of 73.7 per cent (Eurostat 2010). However, there is media speculation about whether or when the country will apply to the Euro rescue fund. Spain's main problem appears to be not only its debts but also its extremely high unemployment.

After the social democratic government under Prime Minister José Luis Rodriguez Zapatero adopted yet another anti-cyclical financial policy in 2009 in order to stimulate demand through public investment and incentives, with the adoption of the 2010 budget a strict consolidation process commenced. The government is focusing in particular on spending cuts to be achieved through structural reforms in the pension system and on the labour market, as well as through child benefit and civil service cuts. In what follows we shall analyse the social democratic government's austerity programme and its effects on the Spanish social state in more detail. The aim is to find out whether the crisis served as catalyst and legitimation for structural reforms and social security cuts and whether the reforms represent a turn towards a social investment welfare state.

2.2.1 The Spanish Austerity Programme

With the budget plan for 2010 the Spanish consolidation process commenced with the aim of reducing the deficit to three per cent of GDP by 2013 (Stability Programme ES 2010). However, on top of this package the government ratcheted up its economy drive in the course of the year: besides the austerity plan (2011–2013) and the Action Plan (2010) considerable spending cuts were earmarked for the public sector, and the government passed laws on structural reform in the pension system and the labour market, as well as additional economies totalling 15 billion euros (Additional Measures Act 2010). These extensive reforms are supposed to tighten the Spanish budget while boosting economic growth and ensuring basic social care. The Spanish strategy is thus concentrating on a mixture of spending cuts and revenue increases (Stability Programme ES 2010, see also Table 1).

With its first consolidation wave, the 2010 budget plan, the government decided to reduce the deficit by 2.1 per cent of GDP, whereby no significant cuts in social services were envisaged. The government increased VAT, tax on interest and some consumption taxes. In addition, incentives were laid down to stabilise jobs, within the framework of which corporate tax was to be reduced from 25 per cent to 20 per cent for SMEs which maintain or increase their employment rate. On the spending side, the government planned a public sector pay and pension freeze. Substantial reforms and cuts in the Spanish social state were not foreseen. However, the social democratic government implemented additional austerity measures which envisage cuts in the pension system and other areas of social policy.

Within the framework of the »Strategy for a sustainable economy and budget position« the Spanish government implemented a number of structural reforms in relation to pension and labour market policy (Stability Programme ES 2010). The latter is supposed to introduce more flexibility into wage negotiations and employment protection, but at the same time to reinforce the employment rights of those on temporary contracts (Labour Market Act 2010). The aim is to stabilise the employment situation in Spain, where the main problem is the large proportion of temporary and provisional jobs, accounting for around 30 per cent of all employment contracts, well over the European average of 14 per cent (Eurostat 2010). The lack of employment policy stabilisers undoubtedly also explains the sharp increase in the unemployment rate since the beginning of the economic crisis. The belief that more flexibilisation will contribute to stabilisation may be explained historically: since the end of Francoism neoliberal approaches have had considerable weight in Spain (Lessenich 1997).

The Toledo Pact (2010), which envisages extensive pension reform and is supposed to achieve cuts to the value of four per cent of GDP by 2030 (El Mundo 2010), is also part of the strategy for a sustainable economy and budget position. Pension reform includes measures in accordance with the OECD trend (Hinrichs 2008): a uniform pension system has been established, individual equivalence has been reinforced, the retirement age has been raised and the minimum contribution period has been increased from 15 to 25 years. Furthermore, part-time work for those approaching retirement has been temporarily abolished and the 2011 pension increase suspended, although the social security pension is exempt from the latter two measures (Additional Measures Act 2010). The aim of the reforms is to create incentives for regular and longer payment of pension insurance contributions. However, in particular the strengthening of individual equivalence, which is supposed to connect pension levels more closely to contributions, leads to pension redistribution: those with low incomes and erratic employment will increasingly receive lower benefits than those with stable and high incomes. In Spain, where the unemployment rate is currently 20 per cent and the number of temporary contracts is high, this reform can be expected to exacerbate income inequality in old age.

The government also plans to abolish the so-called »baby cheque« and to reduce costs in the health care sector. The baby cheque was introduced by the social democratic government in 2007 and entitles parents to a one-off payment of at least 2,500 euros on the birth of a child. From 2011 this non-income related support will be abolished. Health care reforms are aimed at reducing costs: the state system entitles every citizen to free health care. However, expenditure on drugs is high in Spain and infrastructure is poor and out-of-date (Gil-Escoin/Vaszquez 2008). The current reforms are aimed in particular at lowering drug costs: savings of 1.5 billion euros a year are to be achieved by reducing the price of generic medicines and introducing price caps. Although the social democratic government is not levying copayments, the state health care system will cover only drug costs which are in line with the new price regulations.

The social policy cuts implemented by the Spanish government within the framework of budget consolidation are relatively moderate (see also Table 1) since no specific cuts in basic provisions for social insurance recipients are envisaged. However, the reforms must be regarded as predominantly liberal and regressive because the abolition of the baby cheque has hit low income families hardest. Pension reform, too, adversely affects in particular those with unstable and irregular work records. Taking into consideration the high unemployment and the instability on the Spanish labour market pension reform will result in significantly lower earnings for many people. In addition, the Zapatero government is not planning redistributive compensation by taxing higher incomes or property, so that budget consolidation will predominantly affect families and future pensioners on low and irregular incomes. In order to be able to contextualise the reforms within the framework of the overall development of social policy in Spain, in what follows the basic features of the Spanish social state will be examined in more detail.

2.2.2 Uncertainty about the Future of the Southern Social State

The Spanish social state is usually categorised under the Mediterranean or post-authoritarian welfare state model. This group is distinguished in a number of fundamental ways from other continental European social states: in particular, the marked fragmentation of the social security system, the importance of the family and lower benefits (Arts and Gelissen 2002). Spain's social state has both public and private components, with benefits generally dependent on contributions, with the exception of the national health service and the social assistance fund, which supports people who otherwise are not covered. Social spending, at 21 per cent of GDP, is at the lower end of the EU15 and only a little above that of the Central and Eastern European countries (Eurostat 2010).

In an attempt to throw off the legacy of Francoism, in the course of transformation in the 1980s there was massive flexibilisation and dualisation on the labour market, while social policy re-regulation remained far behind (Lessenich 1997). The result was an explosive increase in temporary contracts which have undoubtedly contributed to the high increase in unemployment since the outbreak of the crisis. However, the social security net is too weak to support this group. More than 30 per cent of the unemployed do not receive unemployment insurance and the level of benefits is very low (Gil-Escoin/Vázquez 2008: 11). In 1998, the conservative government tried for the first time to promote stable employment relations by means of an agreement on regular part-time jobs. Current labour market policy is in line with this basic consensus: while temporary employment has been re-regulated further flexibilisation of employment policy is at the forefront of the reforms.

Although the democratic Spanish state has never played a central role in social security, in other areas too there are signs of the further economisation of Spanish social policy. In response to the financial crisis the Zapatero government passed extensive consolidation measures, affecting also social expenditure. And although there is no particular emphasis on cuts in the basic pension and unemployment provisions, nor do the reforms do much to redistribute from the top down, but are rather regressive in nature. In particular, the recent pension reforms, which are intended to provide incentives to normal employment, are in line with a turn towards a social investment approach. This sent a signal that citizens must take responsibility for their old age and the state will have only a supporting role.

The expansion of the Southern social state, which even before the crisis was characterised by low benefits and fragmentation, appears to have receded even further into the future. Although the public has responded with extensive national strike action and the trade unions, the traditional allies of the social democratic party, have protested against the consolidation policy, the government has implemented reforms which appeared to it necessary to restore Spain's credibility on the financial markets (Keeley 2010). Since prosperity is jeopardised by the high deficit the interests of individual groups, such as pensioners and the unemployed, must take a step back »in the interests of all«. In this way the goals of social policy are subordinated to budgetary policy exigencies, with arguments concerning redistribution and the maintenance of social standards not playing much of a role in the public debate.

2.3 Greece and the Economic Crisis

The economic crisis hit the Greek economy – which makes up two per cent of European GDP – hard, reaching its peak at the beginning of 2010: its external debt rose to such an extent that the country's credibility and its ability to meet its interest payments were called into question. Capital inflow ground to a halt and interest on long-term government bonds rose above 11 per cent, very high in comparison to the average of 3.41 per cent for the rest of the euro area. The Greek budget deficit climbed to 12.7 per cent and the national debt exceeded 113 per cent of GDP, with annual interest repayments amounting to more than 12 billion euros (Eurostat 2010).

Although the sharp debt increase was a consequence of the economic crisis the budget situation was not sustainable even before the outbreak of the recession. Despite average economic growth of almost five per cent between 2000 and 2005, net lending/net borrowing grew annually by 6.3 per cent of GDP and government debt stood at 100 per cent, even in 2005 (Eurostat 2010). With the onset of the crisis government spending increased sharply, however, while economic activity and thus public revenues declined. Besides a fall in real growth of around three per cent in 2009, the unemployment rate rose for the first time since 1991 and currently stands at 9.3 per cent. In particular, employees in construction, the processing industry and tourism were hit by the crisis.

Although Greece did not register such deep declines in growth as other European countries in February 2010 the country was on the brink of insolvency. The plight of the budget was so great that Giorgos A. Papandreou's social democratic government had to ask the EU and the IMF for financial aid. Thus developed the Greek crisis, which has also been a crucial test of the euro area. The question was, to what extent would the EU member states show solidarity and stabilise the common currency with euro-denominated government bonds and transfer payments? Or would Greece be left to overcome the crisis all on its own? At the beginning of March 2010 the social government signed an agreement with the EU and the IMF, arranging a credit guarantee of up to 110 billion euros. As a countermove to the financial rescue package Papandreou's government committed itself to implementing an extensive austerity programme.

Besides the goal of restoring the credibility of the public finances the consolidation measures, by means of structural reforms, are supposed to boost competitiveness, a balanced current account and sustainable economic growth. Since its accession to the euro in 2001 Greece has registered higher inflation rates than the rest of the euro area, causing its competitiveness to decline constantly in relation to the other member states. In particular, the favourable credit situation for companies and households which accompanied euro accession is regarded as the cause of »too strong« domestic demand. With its austerity package the socialist government initiated a fundamental change in the Greek growth paradigm: instead of consumption and domestic demand as the main growth factors a new economic model is to be fashioned in which the emphasis is on investment and exports (Stability Programme Greece 2010a).

Greece's austerity programme is all-embracing: besides higher taxes and wage reductions the government also plans social security cuts. An extensive pension reform, which has long been on the agenda, as well as health care cuts and labour market activation policies, are aimed at fostering the sustainability of the public finances. According to Finance Minister Giorgos Papakonstantinou the severe financial situation means that »everyone must contribute in accordance with their means« (Die Zeit online 2010a). In order to reach the government's finance policy goals the Greek social state cannot remain immune to the economy drive and the exigencies of the new growth model. Despite widespread strikes and harsh criticisms from the public the austerity package is being strictly implemented.

2.3.1 The Greek Austerity Package

The social democratic government is banking on tough austerity measures which will not leave the Greek social security system unscathed. The 2010 Stability Programme was aimed at reducing the budget deficit within the year by between four and 8.7 per cent (Stability Programme Greece 2010a). When shortly afterwards at the beginning of 2010 the danger of state bankruptcy reared its head and Greece signed an international rescue package (see above) the Papandreou government passed additional austerity measures in the amount of two per cent of GDP or 4.8 billion euros (Stability Programme Greece 2010b). The government's consolidation strategy is comprehensive and includes both tax increases and social security cuts (see also Table 1). Although the latter are not the focus of the consolidation measures essential areas such as pension provisions, labour market policy and health care have been substantially affected.

Extensive pension reforms were presented to parliament because – thus ran the argument – only in this way would Greece be able to make its public finances sustainable. The costs of pension provisions have risen in recent years from 4.5 per cent of GDP in 2005 to 6.6 per cent of GDP in 2009. According to various prognoses unless the pension system is restructured spending will even exceed 24 per cent of GDP by 2060 (Stability Programme Greece 2010). Spending is significantly above the average for European member states which could point to preferential treatment for pension recipients with regard to social spending. However, the non-contribution related social pension, with a basic monthly benefit of 228 euros (2006), is very low and the system is strongly segmented, with major differences between benefit levels, retirement ages and the contribution system. Since the mid-1990s pension reform has been high on the reform agenda, but until the outbreak of the crisis there was little to show for it.

In July 2010 Parliament assented to this extensive pension reform, which is designed to save three billion euros by 2012. A series of measures are supposed to help to rationalise pension spending and, at the same time, to provide employment incentives by boosting individual contribution equivalence. For example, the retirement age for women and men has been raised to 65 years of age, pension amounts have been adapted to GDP fluctuations, early retirement incentives have been abolished, the payment period for the minimum pension has been lengthened and the contribution assessment base has been increased, so that it no longer relates solely to the final years' income. Privileges for particular groups have been abolished and the number of pension funds has been reduced. In addition, a wage freeze has been imposed for 2010–2012, holiday bonuses have been reduced and those receiving pensions of over 1,400 euros a month will in future pay extra income tax of up to 10 per cent. The pension reforms are generally in line with those of other OECD states, putting more emphasis on individual contribution equivalence, the »living income« principle and raising the retirement age (see Hinrichs 2008). From these reforms it may be expected that state pension benefits will in future be lower and distributed much more unequally, although the 10 per cent tax on higher pensions will compensate this effect to some extent.

The Greek health care system has also been hit by the austerity measures. A reduction in state funded drugs and the introduction of price and cost caps for hospitals are intended to save at least 300 million euros. In contrast to pensions, however, even before the crisis public spending on health care was below that of other EU member states (Stability Programme Greece 2010a). In addition, the state system introduced in 1983, which is supposed to provide universal access and coverage with regard to health services, early on exhibited serious inefficiencies, funding deficits, corruption and discrimination (Davaki/Mosialos 2006; Venieris 2006). To what extent the planned reforms will rectify these problems remains unclear.

During the recession the debate on activating labour market policy measures also flared up again: the mutual obligation principle came to the fore, in accordance with which state benefits can be obtained only on a reciprocal basis. Accordingly, the unemployed are obliged to show evidence that they are looking for work and to participate in training courses on applying for jobs. Failure to comply is subject to sanctions. The reforms are in line with traditional Greek labour market policy which emphasises activation, while unemployment insurance is extremely low by international standards. Not only the benefit level, but also the entitlement period and the level of coverage are comparatively low (Papadopoulos 2006). In particular, the long-term and young unemployed are not protected, so that family networks continue to supplement the inadequate state system.

In response to public budgetary difficulties the Greek government reformed the pension and health care systems and stepped up its existing activating labour market policy. The pension and health care reforms are designed to boost the incentives with regard to »normal« employment. Both the pension reform, which has reinforced individual contribution equivalence, and the employment policy orientation more strongly emphasise incentives, with not much of a role for redistribution and income stabilisation. However, the social democratic government shied away from explicit cuts in social benefits and imposed extra taxes on higher pensions, as well as one-off payments on high profit rates and expensive real estate. The social policy reforms fit in the paradigm of the social investment welfare state, which focuses less on redistribution and income guarantees and more on incentives towards labour market participation. However, the Greek austerity programme and social policy cuts which have affected unemployment benefit recipients and low earners appear to be relatively moderate (see also Section 3, Table 1). Furthermore, the austerity package provides for additional taxes on profitable companies and expensive real estate and a banking levy, so that higher incomes and high-turnover branches also play a part in the consolidation process.

2.3.2 The Development of a Liberal Greek Social System?

As the preceding analysis shows, extensive social policy reforms have been enacted within the framework of the Greek debt crisis with a view to minimising the future costs of the health care and pension systems, as well as to provide incentives for labour market participation. But how do the reforms fit in with the development of the Greek social state? Do they represent a change of course towards a liberal social state? Like other Southern social security systems the Greek system is classified as highly fragmented and rudimentary, relying strongly on family networks as agents of social security (Papatheodorou 2008).

Although Greece's social spending, at 25 per cent of GDP, is only a little under the EU average (2008) the at-risk-of-poverty rate after social benefits is extremely high, at 20 per cent, and markedly over the EU27 average of 16.5 per cent (Eurostat 2010). This is primarily the result of inefficiencies, as a result of which the Greek social security system is frequently described as antiquated. Apart from the state health care system and a means-tested social pension the majority of benefits are contribution-based and there is no universal income maintenance, so that some people fall completely through the social safety net and have to rely on family support.

While in the 1980s a series of social security policy reforms were implemented and social spending grew, in the following years development of the social state stagnated in Greece (Papatheodorou 2008). For example, the government tried, on the one hand, to reduce expenditure by expanding its sources of revenue and, on the other hand, to better separate the contribution financed social security system and the means-tested social assistance system. That means that the very low non-contributory social assistance remains in place, while at the same time individual contribution equivalence has been raised. The responses to the debt crisis also correspond to this policy approach – in particular, pension reform, which is increasingly based on individual incentives to pay contributions. As a result, the Greek government's reforms cannot be described as egalitarian and universalistic, but rather represent a liberal and social investment turn, in which the redistributive components and the level of independence from wage labour are diminishing.

There has been widespread opposition to the government's austerity programme, in particular against the pension reforms, and there have been numerous national strikes since spring 2010. The demonstrators display placards bearing such slogans as »Capitalism must pay for the crisis« and »Nationalise the banks« (Welt Online 2010). The trade union confederation too has warned against excessive wage cuts, which could be hazardous for the paralysed Greek economy. Despite these public protests, however, the Prime Minister has stuck to the reforms as the only way of getting Greece out of the crisis and enabling it to pay any pensions at all: »We cannot afford not to take action«, Papandreou has said (Financial Times Deutschland 2010). The key notion of the government's legitimating discourse is that the austerity package represents a struggle for Greece's survival and that all must participate in the consolidation process.

Papandreou may manage to restore the credibility of the public finances and stabilise yields on Greek bonds, but the social policy prospects for the Greek population have not improved. The social investment turn of the Greek social state has increased income insecurity in old age and stepped up the pressure towards labour market participation. But this can work only if there are sufficient jobs. Greece's competitiveness in the euro area has not been restored, however, and wage policy and social policy cuts will only increase the uncertainty and choke off domestic demand. Whether the reforms have achieved the aim of sustainability or have merely ushered in a turn towards a liberal social security system remains uncertain.

2.4 Iceland and the Financial Crisis

Between 2003 and 2007, before the outbreak of the crisis, Iceland's economy boomed, with average growth of 6.7 per cent. This growth spurt was the result of increasing investment business which grew by 19 per cent a year. With an unemployment rate of only two per cent at the beginning of 2008 the Icelandic economy seemed to be running smoothly. After a slight economic slowdown in the first half of 2008, however, the Icelandic financial system suddenly collapsed in October 2008: the three biggest banks – Glitnir, Kaupthing and Landsbanki – which accounted for 85 per cent of the Icelandic banking system, had borrowed large sums in the capital markets in order to fund the expansion of investment business (OECD, 2009). Because of the low proportion of own capital, the banks' dependence on foreign credit and a general loss of confidence the Icelandic banking system crashed. In October 2008 the grand coalition of conservatives and social democrats passed an emergency law to nationalise the banks and in November 2008 imposed capital controls in order to prevent a mass exodus of investors.

The nationalisation of the banks caused the deficit to skyrocket and in October 2008 Iceland stood on the brink of state bankruptcy. The banks' credit volume amounted to ten times Iceland's GDP, so that domestic capacities were insufficient to rescue the banks. In the same month the Icelandic government signed an international credit agreement, among others with the IMF and the Nordic countries, in the amount of around five billion US dollars. The agreement is supposed to help to restore confidence in the economy and the Icelandic exchange rate in order to prevent a further increase in the national debt, establish a sustainable banking system and reduce public debt (IMF, 2008).

Before the crisis Iceland's national debt was one of the lowest among OECD states. Standing at 26 per cent of GDP in 2005, however, it rose to 57.4 per cent in 2008 (Eurostat 2010) and currently stands at an estimated 120 per cent and total external debt may be as high as 280 per cent of GDP (IMF 2010b). This enormous increase is mainly the result of bank failures and represents a budget deficit of –13.5 per cent in 2008 and –9.1 per cent in 2009 (Eurostat 2010). The Icelandic economy has also plunged into recession: the fall in domestic demand has been much more marked than in other countries and unemployment has risen from two per cent to eight per cent today. In addition, the exchange rate of the Icelandic krona has fallen and inflation climbed above 11 per cent in May 2009, though it adjusted later on (Iceland 2011).

After state bankruptcy had been averted in 2008 Iceland faced profound upheaval in terms of social policy. Large-scale strikes and street protests forced Geir Haarde's government to resign in January 2009, however. The early elections confirmed a policy shift and since February 2009 a Left-Green coalition has governed with the Europe-friendly Johanna Sigurðardóttir as prime minister. Although the new government would like to preserve the Nordic welfare state and does not want to reduce the debt at the expensive of the needy, Icelandic society cannot be protected from social policy cuts and reforms. In July 2009 the coalition published the outline of its austerity package: although it foresees social policy cuts and a renunciation of universality, nevertheless, the poorest will not be affected and to that extent it represents a retention of the Nordic social state.

2.4.1 Iceland's Austerity Package

In July 2009 the Left-Green government presented its budget consolidation package, which amounts to 179 billion krona or 12 per cent of GDP, covering a period of five years. This represents a significant moderation of the programme of the preceding conservative government, which planned cuts amounting to 16 per cent of GDP (Iceland 2010). In the period 2009–2013, 35 billion krona (around 1.17 billion euros) are to be saved annually, or 2.4 per cent of GDP. The measures are all-embracing and include both spending cuts and tax increases, aimed at achieving a positive primary balance in 2011 and positive net lending/borrowing in 2013 (Iceland 2009). Although the government takes the view that, given the continuing recession, tax increases would do less damage to economic growth, spending cuts account for the largest share of the consolidation package, at 64 per cent (Iceland 2010).

On the revenue side, the Icelandic government has adopted extensive reforms. In July 2009, it increased social insurance contributions from 5.34 per cent to seven per cent, raised VAT by half a percentage point, increased a number of consumption taxes and the capital levy on yields of over 250,000 krona from 10 per cent to

15 per cent, and introduced a temporary supplementary tax on monthly incomes above 700,000 krona (around 4,600 euros) (IMF, 2010). An increase in corporation tax is also planned, which at present stands at only 18 per cent. These tax policy measures are progressive since the government, besides tax rises across the board, is making those on higher incomes pay more.

On the expenditure side, too, the Left-Green government has tried to avoid imposing a disproportionate burden and cuts in living standards on those on low incomes. Despite this approach, however, Iceland has not been spared social cuts: particularly hard hit have been old age and invalidity pensions, as well as health insurance and child benefit. Cuts in these areas are intended to reduce spending by around 10 billion krona before the end of 2010, although minimum payments are not affected but rather those benefitting from universal benefits despite higher incomes.

The current policy approach, which leaves low incomes untouched, represents a move away from previous social policy reforms in Iceland. In the 1990s, Iceland increased the proportion of individual user funding of public services, as well as the link between individual benefit payments and benefits. In the pension system, besides the state and company pensions, an additional private provision was introduced and tied to tax policy incentives. The basic pension, which originally was independent of earnings, was adapted to individual payments. The current pension reform partly severs the link between contributions and claims. Earnings in addition to the basic state pension have been cut: in future, earnings from employment and other pension funds that are above 10,000 krona will be credited against the basic pension. As income increases, therefore, benefits will be cut back and from an income of four million krona a year completely abolished. The Icelandic measures thereby represent a deviation from the OECD trend, which emphasises the correlation between individual contributions and claims.

The consolidation package also affects the national health care system which, as in most Nordic states, is largely organised by the state. Health care costs in Iceland are traditionally significantly higher than the EU average, because the system is extensive. However, since the 1990s there has been a move away from universal and free services in this area. Access to free health care has been restricted, fees introduced for all services and co-payments for drugs increased (Jonsson 2001). The current health care reforms are in line with these developments: co-payments for medicines have been raised in order to boost demand for generic drugs, with a view to reducing costs by 10 per cent. Much like in the pension system, basic care is maintained by means of free generic drugs. However, this development could also lead to social division in the sense that only a few will be able to afford some special drugs.

Besides pensions and health care costs child benefits and parental benefits have also been affected by the austerity measures. While child benefit is at present paid to families with children below six years of age regardless of income, from now on benefits will be at least partly income-related, with the aim of saving one billion krona. In addition, the government is cutting parental benefit which has an income replacement rate of 80 per cent and at present may amount to a maximum 400,000 krona a month. Within the framework of the austerity package the highest payment is being reduced to 350,000 krona a month, so that in particular higher and medium incomes are affected by this measure. Parents who earn less than 437,500 krona (around 2,900 euros) will continue to receive 80 per cent of their income. The government estimates that this measure will save 70 million krona and adversely affect 15 per cent of parents (30 per cent of men and 10 per cent of women). Much the same as with regard to pensions and health care these reforms represent a move away from universal provisions and put the emphasis on means-tested payments.

The austerity package of Iceland's Left-Green coalition is predominantly progressive and aimed at preventing growing income inequality. The government has reduced benefits primarily for those on higher incomes, while low earners remain untouched. Benefits are therefore reduced as income increases and pensions have been completely abolished for those with incomes above four million krona a year (Iceland 2009). This means that, although there has been a move away from non-income related benefits, minimum benefits and the living standards of those on low incomes are ensured.

2.4.2 Iceland and the Survival of the Nordic Welfare State

The welfare state literature usually categorises the Icelandic social state as a Nordic and thus a social democratic regime (Jonsson 2001; Einhorn/Logue 2003). Given Iceland's history and its close relations with its Nordic neighbours this cultural and social kinship is hardly surprising. These close relations have contributed to similar welfare state reforms and developments: the principle of universalism, tax-financed benefits and a state health system also characterise Iceland's social security system. Besides these similarities, however, Iceland's social state has specific features of its own.

In comparison to the other Nordic systems, Iceland's welfare state services can be described as backward and underdeveloped, with the emphasis on market liberal solutions, individual protection and family support, and services are lower than in the other countries. This is also evident from the relatively low social spending. While in the 1950s Iceland's social spending was similar to that of its neighbours – between six and eight per cent of GDP – in the 1970s a gap began to open up: Icelandic social spending was only 10 per cent of GDP in contrast to 19 per cent in Denmark and 16 per cent in Sweden. In 2008, too, social spending was only 22 per cent, below the EU average of 26 per cent. While the costs of the health care system are similar to the EU average, in other areas – such as pensions, unemployment benefit and child and parental benefit – costs are markedly below the EU average.

Between 1988 and 199, however, Iceland implemented a series of welfare state reforms and cuts which can be considered a move away from the social democratic regime. As mentioned in the previous section, the government emphasised user funding of services and strengthened the relationship between payments and benefits. This represents a turning away from the universal principle of the welfare state and stresses individual equivalence, which is often justified in terms of incentives for labour market participation. Despite the low social spending as a proportion of GDP and the reforms which increasingly relied on personal responsibility the Icelandic social state is still characterised by one of the lowest at-risk-of-poverty rates and income inequality levels in the EU (Eurostat 2010). The low spending might also be the result of, among other things, a different population structure, characterised by a high birth rate, few pensioners and, up to 2008, a low unemployment rate (Jonsson 2001).

After the cuts in the early 1990s the upturn in the Icelandic economy, with high employment and a budget surplus, was accompanied by many improvements in the welfare state. Benefits were increased and individual equivalence in that regard was strengthened, so that this phase can be regarded as one of decommodification. The financial crisis and the failure of Iceland's three biggest banks, however, dragged the national economy to the brink of insolvency and deep economic recession. The high national debt, which currently stands at over 120 per cent of GDP, must be reduced and international loans paid back. In addition, in particular with regard to Iceland's future EU accession, a robust budgetary position is indispensible.

The Icelandic government's austerity package envisages massive cuts, making up 12 per cent of GDP by 2013. Besides tax policy reforms the government will realise the bulk of consolidation through economies, also affecting social spending. However, in contrast to a number of EU states, the Icelandic population and the Left-Green government have not reacted with sweeping cuts in social spending or by stepping up the pressure with regard to employment participation and activation. While it does represent a move away from universal benefit entitlements for all population groups, it has a progressive orientation, thereby maintaining the still very low income inequality. The public reaction which forced the coalition to take a step back brought Iceland onto a welfare state path which appears to differ considerably from those of other countries.

2.5 Latvia and the Economic Crisis

In 1991, the transition commenced from a socialist to a market economic system in Latvia. Since, in the wake of this transformation, the Russian market was separated from the Baltic region and in the West demand for Latvian goods was insufficient there was a fall in industrial production. Latvia's transformation process was therefore characterised by substantial falls in growth. Latvia was long the poorest country in the EU in terms of real income per capita. Today, it is still near the bottom of the EU27. The fact that Latvia seems to be doing so poorly is astonishing, however, given that during the pre-crisis years – 2005–2007 – Latvia registered average growth of around 10 per cent. While real income grew from 37 per cent of the EU average in 2000 to 56 per cent in 2007, income inequality also grew during this period, as did the at-risk-of-poverty rate (Eurostat 2010).

After several boom years Latvia was plunged into one of the deepest recessions in Europe on the outbreak of the financial crisis: the huge growth rates turned negative, the high demand for credit morphed into a credit crunch, high inflation became deflation and the relatively low unemployment shot up. With a –4.2 per cent decline in growth already in 2008 the Latvian economy registered an EU-wide record fall in 2009 of –18 per cent. Lending juddered to a halt, construction and trade stagnated and public optimism turned into pessimism. The fall in growth had horrendous consequences not only for the country's credit-worthiness, but also for employment. The unemployment rate shot up from six per cent in 2007 to 20 per cent in 2009. The crisis affected Latvia to such an extent that the economy today is back to where it was in 2004.

In the course of the crisis the Latvian government got into financial difficulties and at the end of 2008 applied for an international rescue package: the international credit crunch and the lowering of Latvia's credit-worthiness by the rating agencies made it more difficult for the country to borrow adequately on the market. This was accompanied by the losses incurred by Parex Bank, Latvia's largest, which required a capital injection to stave off insolvency. Latvia's budget deficit rose from –0.3 per cent in 2007 to over –10 per cent in 2009. Government debt, although below the agreed 60 per cent limit of the Stability and Growth Pact, registered an increase from nine per cent in 2007 to around 36 per cent in 2009. At the end of 2008 Latvia had problems obtaining more credit on the international market and was granted an international rescue package of around 7.5 billion euros up to 2011.

International loan payments are dependent on Latvia's progress with consolidation and are intended to support the »Programme for Economic Stability and Growth«, adopted by the Centre-Right government in 2008. The aim is to stabilise financial sustainability, the banking system and the exchange rate in order to safeguard the introduction of the euro by 2014. While the first consolidation programme envisaged no cuts in social spending, in June 2009 the Latvian government passed another austerity package with severe welfare cuts, which hit the poor hardest, those who even during the boom had not benefited much from economic growth. Surprisingly, Latvians reacted positively to the Centre-Right government's consolidation course: at the national elections in January 2009 and in October 2010 the coalition achieved a clear victory.

2.5.1 The Latvian Austerity Package

The Latvian government passed two consolidation rounds, one in December 2008 and another in June 2009. The first austerity package concentrated on wage and job cuts in the public sector, as well as on increases in VAT and consumption taxes, aiming at cuts worth seven per cent of GDP. Due to the sharp fall in growth, however, the effects of consolidation fell short of expectations and so the second round is supposed to achieve cuts of around four per cent of GDP. The consolidation measures were aimed at reducing the budget deficit to below 8.5 per cent of GDP in 2010. Future deficit reductions are planned, to bring it down to six per cent in 2011 and below three per cent in 2012 (Stability Programme Latvia 2010).

While the first consolidation package represented a mixture of spending cuts and revenue increases, the second concentrated – 72 per cent – on cuts, one-third of which affected the welfare system (Latvian Ministry of Finance 2009), alongside wage and job cuts totalling 15 per cent in the public sector, and rises in VAT and consumption taxes, personal income tax and social security contributions. In addition, the government hopes for a revenue increase by means of a reduction in the personal income tax allowance from 95 to 34 lats a month. Those on low incomes will be disproportionately affected, in particular because tax rates in Latvia are not income-related. The flat tax rate introduced in 1997 contributes less than a progressive system to income redistribution.

On the spending side, the government is implementing sweeping social spending cuts: besides cuts in child and parental benefits, unemployment and invalidity entitlements above 11.51 lats a day are also being cut by 50 per cent. These reforms will lead to income losses in particular for social benefit recipients and reduce all social benefits to a minimum basic provision. In addition, the government plans massive cuts in the pension and health care systems.

The government cut pensions by 10 per cent in July 2010. In February 2010, however, the Office for the Protection of the Constitution issued a complaint, so that these measures had to be revised. In response, the government announced a further raising of the retirement age (Latvia 2009). The Latvian government had already implemented extensive reforms at the beginning of 2000.

Among other things, a three-tier system was introduced, embracing a funded and a private system alongside the state contribution-financed pensions. In addition, the retirement age was raised to 62 and the basis of assessment extended to a person's whole working life (Rajevska 2008). This represents a turn towards more individual and private provision, as well as towards a reduction in pension benefits for those with irregular employment histories.

Due to population ageing the government expects an increase in health care costs (Stability Programme Latvia 2010). The reforms in this sector focus in particular on reducing in-patient treatment as well as service providers in order to contain costs. For example, over half of all hospitals – at present numbering 56 – are to be closed and daily co-payments are to be increased. For many pensioners and minimum wage recipients, however, that is not viable (Wolf 2009). Latvia's state health system was reformed in 2005: a capitation model was introduced for the funding of basic medical care; insured persons had to pay a larger proportion of treatment costs; and stricter rules for emergency services and the introduction of competition between doctors was pressed ahead with. Much as in pension policy, a turn towards more individual responsibility can be observed, either through higher out of pocket payments, as in the health care system, or through the adjustment of contributions and benefits.

The Latvian consolidation programme affects virtually every part of the social security system; cuts are envisaged in child and parental benefits, as well as in unemployment and health insurance, and structural reforms are planned in the pension and health care systems. The government expects that through these reforms in particular work incentives and personal responsibility will be reinforced. Besides social policy cuts and the expansion of private provision and personal responsibility, which particularly affect the needy, tax reforms are not contributing to income equality: an increase in flat-rate taxes and the reduction of the tax allowance to 35 lats a month affects especially low earners. Given Latvia's existing substantial income inequality and at-risk-of-poverty rate it is not apparent how the reforms are supposed to contribute to healing social divisions.

2.5.2 Rolling Back of the Latvian Social State

After regaining its independence from the Soviet Union the Latvian state took over responsibility for the welfare state. The basic principles are derived from the Social Security Act of 1995 which represented a radical change for workers and emphasised personal responsibility for welfare (Rajevska 2008). During the transition to the market economy and a democratic political system Latvia's social spending was high, in particular because of the decline in production and rising unemployment. Initially extensive unemployment benefits were drastically cut and redesigned as an incentive to find a job as soon as possible. For example, as unemployment continues benefits fall from 100 per cent to 50 per cent, with no lower limit. Social spending has fallen steadily, from 17.2 per cent of GDP in 1999 to 11 per cent in 2007: this falls far short of the EU27 average of 26 per cent in 2007. The growth boom in the pre-crisis years did not lead to an expansion of the Latvian social state either.

Although Latvian social legislation and the corresponding institutions are extensive, income inequality and the at-risk-of-poverty rate after social transfers are extremely high. Latvia has both contributory and means-tested benefits: besides the state social security system, in which payments are linked to contributions, public assistance comprises universal state benefits which are provided on the basis of membership of certain population groups or of need. However, benefits in general are extremely low: for example, for 80 per cent of recipients pensions are below the subsistence minimum and there is no lower limit with regard to unemployment benefit. As a result, Latvia is one of the poorest countries in the EU with severe social inequalities. The imbalances with regard to income distribution and the at-risk-of-poverty rate have both increased significantly over the past decade and are far above the EU27 average (Eurostat 2010).

The public is still dominant in the provision of social services. In all areas, however, the share of the private sector and individual responsibility is increasing significantly. This affects not least pensions and health care, in which fundamental reforms have been implemented over the past decade. Valdis Dombrovski's consolidation policy represents an additional withdrawal of the state from social policy: Latvia's social benefits, already low (frequently below the subsistence minimum), are being cut back even further. As a result, Latvian social policy contributes neither to status maintenance nor even to ensuring basic needs. Given the increasing poverty and income inequality, as well as the high unemployment, this is alarming.

Nevertheless, the government is holding firm to its market liberal reforms: Dombrovski justified his course of action in an interview as follows: »There is no alternative – in particular if one is in the Eurozone – to cuts if the aim is to restore competitiveness. Implementation must be rapid, brutal and unhesitating« (sueddeutsche.de 2010). Consolidation and social redistribution, consequently, are subordinate to future entry to the euro, still planned for 2014. Robust finances and international competitiveness are being implemented with a clear liberal orientation, however, preferring predominantly market solutions and allocating a very active role to the private sector.

However, the liberal consensus does not appear to be limited to the political elite: the Centre-Right government's austerity programme has been confirmed by two elections. Although in February 2009 there were thousands of demonstrators on the streets protesting against the government's economic and austerity policy and calling for new elections, and Prime Minister Ivars Godmanis resigned in response to the sometimes violent protests in February 2009, the coalition was returned in the subsequent elections; the electorate also supported the government's austerity policy in the national elections in October 2010. The reason for the weak opposition, besides widespread support for the liberal social policy, is undoubtedly also the lack of organisation on the workers' side, resulting in a lack of pressure from below and a largely free hand for the political elites in the implementation of social policy.

2.6 Romania and the Economic Crisis

Although Romania's transformation into a market economy in the 1990s was characterised by falling growth and incomes and high unemployment, as the twenty-first century got under way the country seemed to have developed into a regional model (see Moser 2010): with average growth rates of 6.7 per cent and increases in real income of 12 per cent a year between 2004 and 2007 the Romanian economy experienced an enormous upturn. In 2007, real income grew for the first time above the 1990 average and unemployment stood at a mere 5.8 per cent in 2008 (Eurostat 2010). Romania's accession to the EU in 2007 appeared to boost the economy and it seemed that the country had found an exemplary path to growth and prosperity.

Despite the marked economic upswing Romania's national debt rose continuously. In 2008, when growth and employment reached a high point, the budget deficit stood at 5.5 per cent of GDP. Because of the economic boom, however, the structural deficit was not heeded and only with the outbreak of the crisis did the pro-cyclical finance policy develop into a problem. Romania's role model status came under strain with the onset of the global economic crisis: domestic demand fell by 13.7 per cent, exports by 10.1 per cent and capital inflows fell by 20 per cent, as a result of which unemployment rose to 7.8 per cent at the end of 2009. Since state revenues slumped and spending rose steeply the deficit grew to eight per cent of GDP in 2009, well over the threshold laid down in the Stability and Growth Pact. Although public debt was only 25 per cent of GDP the burden doubled virtually in the course of a year (Stability Programme Romania 2010).

Public spending grew to such an extent that the government feared insolvency. Romania was granted a 20 billion euro loan by the International Monetary Fund, the World Bank and the EU in May 2009. Approval of the loan was linked to an extensive package of measures to rein in fiscal policy and external imbalances. The democratic-liberal government laid down the goal of a structurally balanced deficit by 2014. In addition, in May 2010 President Traian Basescu announced a comprehensive austerity programme, envisaging cuts in the public sector and in welfare. The Romanian government's austerity plan can be regarded as a turning away by the state from redistribution and social policy aims, which will only exacerbate the country's severe income disparities. In what follows the austerity package is considered in detail and its quantitative and qualitative effects analysed.

2.6.1 The Romanian Austerity Programme

The Romanian government started to implement its strict austerity plan in 2009. The budget envisaged an increase in social contributions of 3.3 per cent, as well as cuts in public sector wages and jobs. On the approval of the international loan in May 2009 Romania adopted the first consolidation programme. Since one year later it was evident that, despite the reforms, the agreed deficit target would not be reached the government passed another austerity package. This provides for deep cuts in the Romanian welfare state, with sweeping cuts of 15 per cent in all social transfers and of 25 per cent in public sector wages in order to bring about a structurally balanced budget by 2014.

The government's approach is based mainly on cuts; with an increase in tax revenues not envisaged for the time being (see also Table 1, p. 31). In order to reach its budget policy targets the Romanian government planned, in the first rounds of cuts, the introduction of a law on »standard pensions«, as well as a »uniform payment system«. While the latter relies on the standardisation and efficiency of public sector pay, the former concerns comprehensive pension reform. Pension reform is to be implemented in 2011 and is intended to reduce the budget deficit by up to four per cent over the long term (Stability Programme Romania 2010).

Pension reform encompasses a number of measures aimed at reducing costs over the long term. To this end the retirement age is being raised to 65 and standardised for men and women; the minimum contribution period is being increased; and the assessment base is being extended among others to freelancers and the public sector. In addition, pensions are being tied to inflation, which over the long term will yield considerable savings because adjustment will increasingly be oriented towards consumer prices and less to increases in income. In future, pension levels will be calculated also on the basis of total contributions and no longer on earnings in the final years of insurance. These measures are supposed to establish an incentive to remain in employment longer and more constantly. However, they will also lead to lower pensions, especially for those with irregular contribution records. Besides re-orientating the state pension system the Romanian government is set on bringing the private pension system to the fore. Since 2007, people have increasingly been turning to private and capital funded provisions.

On 6 May 2010 Finance Minister Basescu announced the consolidation measures, justifying them by saying that the payment of the next IMF loan depended on them. While it is true that the IMF demanded further budgetary consolidation to the value of 2.3 per cent of GDP in 2010 there were no specific guidelines concerning the shape restructuring was supposed to take. Within the framework of the second austerity package, however, drastic cuts in the social budget and in the public sector are to the fore. The government resolved on wage cuts of 25 per cent in the public sector and cuts in all social transfers of 15 per cent. While sweeping reductions in pensions were halted by the Constitutional Court, the other areas, such as unemployment benefits and parental benefits, are affected by these deep cuts. However, the measures do not include minimum payments and thus do not protect those most in need.

Further social policy measures included the discontinuation of supplementary payments for heating costs, the suspension of early retirement and stricter controls on disabled pensions. The government also plans cuts in health care, including the cutback of hospitals, increased individual co-payments and the extension of private services. While Romania's health care system is based on a Bismarckian system, in which insurees pay in accordance with earnings and receive services independent of contributions, in recent decades there has been an increasing focus on privatisation.

While the Romanian consolidation strategy is based on massive economies virtually no tax increases are planned. Although the government raised VAT from 19 per cent to 24 per cent in July 2010 it was an emergency measure after the planned pension cuts of 15 per cent had been declared unconstitutional. Apart from that no additional taxes are being levied and the government does not envisage redistribution by means of property and inheritance taxes or the taxation of gains from foreign exchange and speculation. The government's strict austerity plan thus affects, besides the public sector, in particular pensioners, families and social benefit recipients. However, there is no differentiation between income groups; the across-the-board cuts will leave those on low incomes comparatively worse off.

The Romanian government's reforms represent a regressive policy approach in which high and stable incomes are spared. While the consolidation package affects all benefit recipients high-income and wealthy strata are exempted from collective responsibility for correcting the budget deficit. Naturally, they are affected by the VAT increase, but apart from that they do not really have to share the costs of the government's measures.

Socially vulnerable groups therefore not just relatively but also nominally have to bear more of the burden of budget restructuring. The Romanian government's austerity plan can therefore be considered a renunciation by the state of redistributive and social policy goals.

2.6.2 Cutting Back the Welfare State in Romania

At the outset of the transformation to a market economy the Romanian state had to completely restructure the social security system. Economic and social policy was oriented towards Western welfare states, which provide for freedom of employment, minimum wages, paid holidays and unemployment benefit, as well as health care and pensions. Although Romania's social policy legislation corresponds to that of a modern welfare state conditions on the ground are very different. Not only is social security spending comparatively low, but income inequality is extremely high. Social expenditure in Romania in 2006 represents only 14 per cent of GDP (Eurostat 2010) compared to an EU average of 25 per cent.

Although in legislative terms the situation in many ways resembles a modern welfare state the real situation deviates from it significantly. For example, there is a discrepancy between envisaged measures and real minimum payments. EU statistics on poverty thresholds and income inequality confirm these findings. According to them income differentials in Romania are the highest in the EU; even in the years of strong economic growth which the Romanian economy experienced before the outbreak of the crisis income inequality did not change.

In the 1990s, the social security funds experienced severe funding problems so that extensive reforms were implemented in social legislation aimed mainly at achieving a balanced social security budget. One of the biggest reforms was the restructuring of the pension system, involving increases in the retirement age and the minimum contribution period. The Romanian government adhered closely to the three-pillar model recommended by the World Bank (see Baum-Ceisig et al. 2008: 206 ff). With regard to pension levels there are marked income differences, with some groups enjoying privileged conditions. The introduction of the standardised pension system may counteract this segmentation, although the reform will certainly not lead to a convergence of pension levels. On the contrary, the reforms emphasise individual equivalence and thus bring personal responsibility for old age provision to the fore.

Romania's health care system is also undergoing a turn towards private services and individual co-payments. Although public spending on health care is extremely low and the system is markedly underfunded the government plans further cuts in collective services. The withdrawal of the Romanian state from social policy responsibilities is nothing new: for some time a shift has been taking place from the state to the primacy of the economy, with regulation and safeguarding of the social state very much subordinated to competition and individual responsibility. The intensity of the current social cuts is astonishing, however. They represent a clear opening up to market-oriented solutions, thereby exacerbating income inequality.

The Romanian government justifies its social policy cuts in terms of international pressure for debt repayments. The one-sided emphasis on cuts and the decision not to increase taxes, in contrast, is justified by the argument that such a measure would give rise to false incentives and the retreat of private investment and demand. In this way the crisis has served to legitimate structural reform and radical cuts in the social state.

In September 2010, there were protests against the austerity plan in Romania, in particular against the wage cuts as the extent of the austerity measures gradually became apparent. Reactions were belated, however, and general displeasure with the cuts in social benefits is limited. The current government does not have a stable and strong coalition in parliament. Whether this could result in a renunciation of the current social policy course is doubtful, however. The social democratic opposition and the trade unions, which are calling for the re-introduction of a progressive income tax and higher taxation of luxury goods, do not do much to shape the political debate. Although the opposition tabled a vote of no confidence it offers no alternatives to the dominant liberal policy approach.

2.7 The UK and the Crisis

The market liberal UK represents one of Europe's major financial centres: all the major banks and insurance companies are represented in London. The success of the financial sector, which accounts for more than eight per cent of GDP, rests on a liberal regulatory framework and a high level of debt financing. With the collapse of real estate prices in the USA a severe credit crunch ensued: one of the first »victims« was Northern Rock, a medium-sized British bank which applied to the Bank of England for a loan facility in September 2007. This led to a general panic and a run on the bank, which shortly afterwards was taken into public ownership.

Given the immense economic importance of the financial sector and the low level of equity financing the financial turbulence had major consequences for the national economy: although the Bank of England's base rate has stood at a historically low 0.5 per cent since March 2009, there has been a considerable loss of confidence and a credit squeeze in the private sector. Economic performance fell by five per cent and unemployment rose from 5.6 per cent to 7.6 per cent in 2009 (Eurostat 2010). At present the UK has one of the biggest public deficits in Europe: net lending/net borrowing amounted to –11.4 per cent in 2009, higher than in Spain, Portugal and Ireland, three other countries hard hit by the crisis. The national debt also rose in 2009 to 68.2 per cent; although this is still below the EU27 average of 74 per cent it represents an enormous increase in comparison to the 44.5 per cent registered in 2007. However, it is not just public debt which is high; private debt is also extremely high, at 180 per cent of GDP. The British invest significantly in housing: only 10 per cent of households do not own their home. In the wake of the crisis, however, house prices have fallen precipitately.

In response to the growing national debt the British state is scaling back: the plan is that the private sector provide the necessary growth for jobs and prosperity. In March 2010, Gordon Brown's Labour government passed a consolidation programme, and his successor David Cameron, at the head of a Conservative-Liberal coalition, took further measures. The coalition announced its tough austerity package »Welfare that works« in summer 2010, containing some of the most severe cuts in British history. Cameron – the »Iron Lord« (Zeit 2010b) – wants to save 81 billion pounds (91 billion euros) by 2014, 11 billion pounds of which are to be achieved through cuts in social spending. The media are discussing Britain's total reconstruction and the IMF talk of an extremely progressive and daring reform project. But do the current cuts really represent a turning away from the existing welfare system? Or is it merely a consolidation of the liberal social model? To answer these questions we shall examine the austerity package and its effects on the British social model in more detail.

2.7.1 »Welfare that works«: the British austerity programme

The guiding principles of the Conservative-Liberal coalition's austerity programme are personal responsibility and freedom. The five-year plan is aimed at eliminating the structural deficit by 2014–15 and reducing net borrowing from 11.4 per cent to 1.1 per cent in the fiscal year 2015–2016. Besides introducing a banking tax and raising VAT and capital taxation, the government plans to reduce the debt primarily through cuts: by 2015, 77 per cent of the consolidation programme is to be achieved through spending cuts (HM Treasury 2010). The budgets of almost every ministry are being cut, half a million public sector jobs are being eliminated, British people will have to work longer and social spending, as well as welfare fraud and misuse are to be reduced.

The aim of the British welfare reforms is to heighten the responsibility of the individual and to reinforce the incentives to take up regular employment (subject to social insurance contributions, known as »national insurance«) by way of sanctions and benefit reductions, so that »work always pays« (Financial Plan 2010). The government measures are comprehensive and affect pensioners, single parents, welfare benefit recipients and families. A switch from the retail price index to the consumer price index is to be introduced for the calculation of all benefits. The extent to which benefit recipients will lose out as a result of this switch is disputed. Some studies show, however, that it corresponds to a reduction in benefits and will provide the state with savings of around 5.8 billion pounds in 2014–15 (Browne and Levell 2010).

Besides the reorientation of pension indexation the Conservative-Liberal coalition decided to raise the retirement age again and to eliminate tax relief on pensions over 130,000 pounds a year. While the limitation of tax relief affects only higher pensions the change in indexation, which could be accompanied by a lowering of pensions in general, affects in particular the recipients of state pensions. A characteristic feature of the British pension system is the importance of private and company pensions, since the flat-rate state pension is not enough to cover basic needs (Mitton 2008). Pensioners who have no other income are therefore dependent on other benefits. However, within the framework of the consolidation strategy complementary benefits, such as housing benefit and child benefit, are being cut.

Housing benefit, which currently stands at 50 per cent of the rent, is being reduced by the coalition to 30 per cent. That means that recipients of this benefit can only choose the cheapest housing in their area. In addition, a general maximum payment is being introduced independent of local rents, with a view to saving 4.2 billion pounds over the next five years. The government also plans to restructure child benefit, linking benefits more closely to need. While child benefit, which is not income-related, is being cut, the government is boosting child credits, which are means-tested. This means that over the next few years increases in child benefit will be postponed and abolished for families on higher incomes from 2013. This is in line with the key values of the British welfare state, which traditionally emphasises benefits for the poorest and for children. In addition, single parents with children over five years of age can no longer obtain income support but in future will have to register as unemployed: this measure is intended to increase employment incentives for this group.

Besides the tax increases and welfare reforms the British government also plans to raise the personal tax allowance for all by 1,000 pounds. While the cuts affect benefit recipients most of all, those on higher incomes benefit most from this measure. The Institute for Financial Studies (IFS) therefore describes the British austerity programme as regressive, the biggest losers from the Conservative-Liberal reforms being benefit recipients. In contrast, those without children and on higher incomes are the biggest winners since they are not affected by the reforms and benefit from the raising of the tax allowance. Although the austerity package is certainly comprehensive and means severe cuts for some groups the reforms do not represent a complete reorientation of the British welfare system, but in many respects rather the consolidation of the existing model.

2.7.2 The British welfare state

Traditionally, poverty is the key issue of British social policy, going back to the Poor Law of the seventeenth century. Also during the extension of the English welfare state, state benefits were limited to the relatively poor part of the population (Kaufmann 2002). This derives from the liberal conviction that social problems can best be solved by self help and economic advance. As a result, traditionally social benefits were limited to the needy and children. The British system can therefore be characterised as one of social services, directed primarily towards avoiding poverty, not to safeguarding a certain standard of living. This means that basic rates and wage replacement benefits, as well as social spending in general – just under 24 per cent of GDP – are relatively low. In contrast, income inequality and the at-risk-of-poverty rate are above the EU27 average.

Britain built up its social system in the post-War years, but in the 1980s a series of radical cuts were implemented which were intended to restore the country's international competitiveness. Margaret Thatcher's Conservative governments sought to roll back the state and, during later periods in office, in particular the welfare state (Mitton 2008). While originally the conservatives favoured a liberal and need-oriented solution, since Tony Blair came to power there has been an increasing convergence with regard to social policy: the central idea underlying »New Labour« was the »Third Way«, in terms of which the state played less of a stabilising than an activating role through lower and private benefits. In addition, attention was directed to the social inclusion of disadvantaged groups, such as the homeless and single parents.

The British state is therefore assigned to the liberal model in the welfare state literature, characterised by low income redistribution and decommodification and the strong influence of the private sector. Within the framework of the current consolidation strategy social benefits have been reduced further and are linked to the liberal values of the British social model: besides the relatively low social benefits the focus is on benefits for the needy and children.

The reforms reflect Britain's liberal roots and convictions, according to which social problems should be solved through personal responsibility and freedom for private enterprise. In its reforms the Conservative-Liberal regime emphasises the notion of »social mobility«. According to this the existing social system has led too many people into »welfare dependency«. The government's central idea is that in future work must always pay (Department of Work and Pensions 2010). The state supports growth through low corporate tax rates and investment incentives, and social benefits are to help only the truly needy and children. For everyone else employment incentives and encouragement of personal responsibility must be increased: this means that the liberal British welfare state must be made even leaner and more flexible (Stability Programme UK 2010). The capital markets reacted positively to David Cameron's cuts: interest rates on British government bonds fell after the announcement of the government's plans and the rating agencies declared that they would give Britain top ratings if the government stuck to its austerity plans. But will this extreme austerity programme be successful? Or will it nip the upturn in the bud and divide the population?

3. Brief Comparison of the Austerity Programmes

Having looked at the consolidation programmes of seven European countries individually in the previous section, embedding the reforms in the context of the relevant welfare state developments, in this concluding analysis we compare the scope of the various austerity packages. What are the similarities and differences between the member states? Is it possible to identify contrary welfare state developments or have governments reacted with similar consolidation strategies? The following analysis first compares the sizes of the national programmes before, finally, examining the social security cuts with regard to their regressive and progressive effects.

Table 1 summarises the findings of country studies and presents the sums involved in the various consolidation programmes in relation to GDP and in billions of the national currency. While Romania adopted a package worth almost 14 per cent of GDP, the German austerity programme amounts to a mere 3.3 per cent of GDP. In order to develop a solid basis for inter-state comparison it makes sense to compare the various austerity plans in relation to annual GDP. Romania – with an annual consolidation effect of seven per cent of GDP – is at the top, followed by Latvia with 5.7 per cent and Greece with five per cent. In contrast, the package of the German conservative-liberal coalition, at 0.8 per cent, lies at the bottom end, and the Spanish and Icelandic programmes are also relatively low. The magnitudes of the consolidation programmes therefore vary considerably.

The differences can be traced back to, among things, the various effects of the crisis in European countries. While Germany's economic situation appears to be rapidly recovering and the national debt is relatively low, other countries – such as Romania, Latvia and Greece – have taken up international loans linked to strict budget plans and extensive structural reforms. In these states in particular the austerity programmes are very harsh. However, there are also differences: Iceland also stood on the brink of state bankruptcy when the nationalisation of the three largest banks greatly exceeded the national finances. Although the Icelandic government applied for billions in international loans annual consolidation is quite low, at 2.4 per cent. The approach of Prime Minister Sigurðardóttir's government – which envisages cuts worth 12 per cent of GDP – is a long-term one, over a five year period, and thus low expressed as an annual average.

Table 1 presents, besides the size of the consolidation package, the relationship between revenue increases and spending cuts as a percentage of the respective austerity package. According to our calculations all states focus predominantly on cuts in spending rather than on increasing or introducing taxes or social contributions. This can be explained by the fact that the »economic literature shows that consolidation is more effective and more sustained by means of spending cuts than consolidation through tax increases«, according to the European Commission (EU Public Finances 2010: 51). However, given the extent of government debts one-sided consolidation is considered insufficient.

Although all states are relying largely on cuts considerable differences with regard to consolidation approaches can be observed. While almost half the Greek and Latvian austerity programmes are being achieved through tax revenues their proportion in the Romanian package is only one-sixth. These differences can be traced back, on the one hand, to variations in national circumstances and so to the existing scope for cuts and tax increases: for example, tax revenues in Latvia represent only 28.6 per cent of GDP, considerably below the EU average of

Table 1 Synopsis* of National Austerity Programmes

Austerity programme	Germany[a]	Estonia	Greece	UK	Latvia	Romania [b]	Iceland
% of GDP	3.3***	8.5**	10.5**	7.2**	11.7*[c]	13.9*	12***
% of GDP per year	0.8	2–3	3	1.8–2	5.7	7	2.4
Billions, national currency	80 € 2010–14	85 € 2010–13	24 € 2010–13	No data 2010–12/13	1,5 LVL 2009–10	74,6 Lei 2009–10	179 ISK 2009–13
% of the austerity programme							
1. Revenue increases	**33**	**41.2**	**42.9****	**31**	**45**	**15**	**36**
– Corporate taxes	7.5[d]	–1.6	8.5[e]	–8.5[f]	–2.4		1.4[h]
– Income taxes				–11.56[g]	9.6		32.3[i]
– VAT		11.4	23.4	44.9	27.3	10[j]	4.6
2. Spending cuts	**52**	**58.8**	**57.1**	**69**	**55**	**85**	**64**
– Social security[k]	34	5.4	No data	21.9	14.8	No data	15.6

Sources:

* Authors' own calculations, based on various IMF and EU sources, as well as national budget plans.

** EU Public Finances 2010, p. 66.

*** Germany: »Package for the Future« 2010 (Zukunftspaket); UK: Budget Plan 2010; Iceland: Financial Plan 2009–13.

a Not including revenues/spending cuts achieved through increased efficiency or a reduction in interest costs.

b The EU believes that Romania will continue to adhere to its consolidation programme over the coming years. For example, between 2010 and 2013 4.3 per cent of GDP will be achieved by spending cuts and only 0.8 per cent of GDP through tax revenues (EU Public Finances 2010: 66).

c According to the EU, Latvia's consolidation over the past two years has amounted to 15 per cent of GDP (EU 2010). Also between 2010 and 2013 Latvia will maintain the focus on consolidation through revenue increases. The EU believes that Latvia in this period will achieve 5.5 per cent of GDP through revenue increases and 1.5 per cent through cuts (EU Public Finances 2010).

d Even though no increase in corporate tax was introduced, the German government plans to introduce a transaction tax with projected revenues of around six billion euros, corresponding to around 7.5 per cent of the austerity package.

e This includes an extra tax on profitable firms, expensive real estate and banking levy.

f However, the British government introduced a banking levy which accounts for around seven per cent of the austerity package.

g In Britain the personal income tax allowance was increased by £1,000 per annum, which is regressive, not progressive in effect.

h This includes both the increase in the corporate tax rate and capital taxation from 18 per cent to 20 per cent (IMF 2010b), as well as a banking levy of one billion ISK.

i This includes a wealth tax totalling 9.8 billion ISK and an additional income tax for high earners in the amount of 47.7 billion ISK.

j Estimates for Romania are particularly difficult because of the lack of public data and the multitude of revisions, since initial consolidation effects were not achieved. However, Romania decided, alongside an increase in VAT from 19 per cent to 24 per cent, only on an extension of personal income tax and consumption taxes to medical products. The former will, according to the finance minister, amount to around 3.5–4 billion lei, corresponding to around 0.65 per cent of GDP. Total consolidation measures for 2010 amount to 6.5 per cent of GDP, so that 90 per cent of the Romanian package consists of cuts and only 10 per cent can be attributed to additional revenues. European Commission estimates confirm this finding (EU Public Finances 2010).

k Without long-term structural reforms in the health care sector and pension system.

l This amount includes the planned 10 per cent pension cuts declared unconstitutional by the Constitutional Court.

39.2 per cent (Stability Programme Latvia 2010: 33). In Greece, there are many tax exemptions, so that the system is to be simplified and consolidated through an extension of the tax base (Stability Package Greece 2010). On the other hand, there are also governments that subscribe to different values and have different national traditions, which certainly favour different consolidation approaches.

The crisis and the dire state of the public finances have served in all countries both to trigger and to justify cuts in the welfare state. In Germany, for example, about one-third of all consolidation measures involve social security reforms, while in Britain they make up one-fifth. In Spain, in contrast, the cuts represent only around five per cent and in Latvia and Iceland about 15 per cent. In other words, while some countries have focused on welfare cuts, in others they have been far less significant. In addition, findings show that an automatic uncoordinated European convergence is improbable: even countries such as Britain, Latvia and Romania, in which social spending as a proportion of GDP is already below the EU average (see Section 1), plan further reductions. The data show, therefore, that also in future there is no question of an automatic adjustment to a social security standard, but rather that European coordination is necessary.

Not only the proportion of welfare cuts but also the ways in which they are made differ considerably. In general, either the pension or the health care system are affected in all countries, in many cases both. In these areas certain tendencies can be observed: in pensions, besides increases in the retirement age, calculation bases are being extended and individual contribution equivalence is being strengthened. While most governments plan structural reforms in pension schemes Romania and Latvia originally wanted across-the-board cuts of 15 per cent and 10 per cent, respectively. Since these were struck down by the Constitutional Court similar effects are to be achieved by structural reforms. It is all the more astonishing that the Icelandic government passed a pension reform which bucks this trend. Pensions in Iceland are to be cut back with increasing incomes and individual equivalence reduced.

Besides health care systems other social spending has been affected in all countries. In health care, cuts have been made through price and cost caps, increasing resort to generic drugs, less inpatient treatment and individual co-payments. While the scope of these measures differs by country a move away from state benefits and towards individual co-payments and risk provision can be observed. Besides cuts in health care, benefits and services in other areas of social security have been scaled back. In Romania all benefits have been cut by 15 per cent; in Germany parental benefits for social security recipients has been abolished; in Britain housing benefit has been cut; in Spain »baby cheques« have been abolished; and in Latvia parental and child benefit have been cut and unemployment and invalidity benefits reduced.

While most countries are making savings at the expense of those on low incomes, only a few governments are pursuing a strategy which also involves higher earners in debt consolidation. For example, Britain and Germany are making cuts which affect the neediest and social benefit recipients with the aim of reducing the wage gap and boosting employment incentives. This represents a regressive policy, with – in effect – redistribution from low to high earners. However, programmes which plan mainly across-the-board welfare cuts, such as those of Spain, Romania and Latvia, can be categorised as regressive. In contrast, Iceland has passed welfare cuts which predominantly affect middle and higher incomes. In addition, only a few countries – such as Iceland and Greece – plan to involve higher earners through taxation of property or wealth or taxes on profitable companies. Although some other countries, such as Britain, have introduced a banking levy they have at the same time reduced corporate taxes, thereby diluting the redistributive component.

Basically, the international economic crisis and the resulting public debt situation have served in all seven countries as both trigger and justification of social spending cuts. Although their consolidation strategies share a number of similarities there are also considerable differences: on the one hand, there appear to be few countries whose approach includes a redistributive component and thus represents a progressive approach; on the other hand, most consolidation programmes – such as those of Britain and Germany – are in effect targeting those on lower incomes.

4. Brief Summary

Europe said goodbye long ago to defining social policy within the framework of a particular concept of society. Welfare states have given way to – historically differing – European social models in which social policy must follow economic and fiscal priorities. This implies both a declining solidarity component in social security and a financial commitment which declines for every successive benefit claim in pursuit of alleged incentive and allocation effects. This general assessment applies not only to the developed EU states of »Old Europe«, but also to the convergence candidates in the south and east of the EU, which have deserted the former development path with its higher correlation between economic development and social provisions.

The hope that the world financial crisis, with its social upheavals, could lead to a rethink and that the – hotly contested – European Social Model could serve as the basis for an alternative approach to European integration seems vain, given the budgetary situations in almost every EU country. Almost everywhere, even in the wake of the global financial crisis, the orthodox truths of finance policy – balanced budget within the framework of the Stability and Growth Pact – still apply or are formulated even more starkly. The belief that budget consolidation is more likely to succeed on the basis of spending cuts than revenue increases also seems unshakable.[7]

In all the cases investigated – perhaps with the exception of Iceland – regressive spending cuts predominate, regardless of the composition of the government. Revenue increases by means of progressive tax rate rises at best play a subordinate role: occasionally, regressive VAT increases are partly offset by corporate tax increases, thereby heightening the regression. Even countries such as Ireland, which have to apply to the European aid programme, appear to have been able to avoid having to raise their competition-distorting low corporate taxes.

Since almost everywhere in the EU regressive austerity measures of unprecedented magnitude have been implemented the consolidation effects are at the very least unclear: the still dominant fiscal orthodoxy is built on the notion of the »crowding in« of private investment as government spending falls. Then the growth path can remain intact or even – with corresponding expectation effects – increase and consolidation succeed alongside a trimmed social state (see Heise 2010b: 287ff). The alternative (Keynesian) view regards as naïve the hope of a compensating private »crowding in« in the event of falling consumer spending power and fears negative effects with regard to growth which – depending on the magnitude of the multiplier and accelerator effects – will at the very least hinder consolidation, if not make it impossible (see Heise 2010b: 287ff). The more widespread the cuts the less hope there is that deficient domestic demand can be compensated by external (export) demand. There is therefore a great deal of evidence of a stagnant growth scenario in the EU in which consolidation efforts will have little success and thus the pressure towards regressive measures will even increase.[8]

Considering, finally, that the EU and the European Monetary Union are characterised by increasing regional imbalances which cannot be sustained over the long term (see, for example, Dullien 2010) the danger cannot be ignored that the pessimistic convergence prognosis will become reality: if regulation at EU level does not prevent it cuts in social services as both a consolidation and a competitiveness strategy could become dominant. Given the diverse social models in the EU member states a harmonisation of social policy as a counter-strategy is not only somewhat unconvincing but also impractical. A concept which maintained national autonomy over social policy, while preventing both absolute and relative forms of dumping, however, could be accepted: this is the so-called »corridor model« (see Busch 1998; Heise 1997: 138f). On this basis the connection between economic development and social security (see Figure 2a) which prevailed in the 1990s could be institutionally safeguarded by requiring each member state to guarantee a social spending rate in accordance with its state of development within a defined corridor. Economic advancement of the kind achieved by, for example, Ireland would be linked to a corresponding expansion of the welfare state – the priorities would remain a national matter, but relative dumping would be halted. And absolute dumping in crisis periods would be prevented unless the Community, on the basis of shared responsibility, redefined the corridor.

7. And naturally there are also those who perceive in the fiscal effects of the financial crisis the opportunity finally to put the taxation and welfare systems in their place (»Tremble, Leviathan«), because »(i)n general, making government smaller is a good idea« (Micklethwait 2010).

8. There are many past instances of governments persisting with ineffective measures on the basis of a belief that they were the »correct measures, but the dosage had to be increased«.

After the billions spent on rescue packages for banks and whole countries such a European Social Model could be considered a necessary social shield which would restrict national autonomy no more than the single currency and the European Stability and Growth Pact have long done. The social protests all over Europe serve as a reminder that an EU without social foundations could, in the long term, be built on sand.

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