SOCIAL INVESTMENT: THE NEW PARADIGM OF EU SOCIAL POLICY?[1]

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1. THE SOCIAL AND POVERTY IMPACT OF THE CRISIS

In the past five years, the European Union underwent unprecedented financial, economic and social turbulence. GDP per capita decreased by almost 5% in the EU27 in 2008-2009; after a fragile recovery (+ 3% over the two-year period 2010-2011) growth rates became negative again in 2012. The absence of tangible recovery has put household incomes under pressure in the majority of EU countries and the risks of long-term exclusion increased. Between 2008 and 2012, real GDP declined in the majority of the Member States.[2] The largest drops were observed in Greece (22%), Latvia (11%), Croatia (9%), Italy (7%), Ireland (7%), Hungary (5%) and Spain (5%). This evolution was in sharp contrast with the situation observed in Germany, Sweden, Austria, Slovakia and Poland where welfare systems and more resilient labour markets have allowed overall incomes to continue rising during the crisis.

Beyond the aggregates, more unequal effects can be observed between social groups. In what follows, we attempt to sketch an overall picture of the social and poverty impact of the crisis in particular.

1.1. EFFECTS ON THE LABOUR MARKET

The most evident and documented effect of the crisis was the upsurge of unemployment rates in the European Union. While unemployment seems to have peaked by mid-2010 or even begun to fall slightly in some countries, in other countries it has continued to rise (Frazer et al., 2011). In 2012, the average unemployment rate stood at more than 10% in the EU27. Even more worrisome was the dramatic increase of youth unemployment, with young people twice as likely to be unemployed than the adult population (European Commission, 2012a). The youth unemployment rate amounts to 24% on average across the EU, and even exceeds 40% in countries like Spain, Greece and Croatia (EC, 2014).

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(2) Source: Eurostat database (http://epp.eurostat.ec.europa.eu/portal/page/portal/eurostat/home).

The 2013 Employment and Social Developments in Europe Review furthermore confirmed a new pattern of divergence, which is most striking between the North and the South of the Eurozone. The unemployment gap between these two areas was 2.3 percentage points in 2000, fell to zero in 2007 but then widened quickly to more than 10 points in 2012. This points to an urgent need for more effective, differentiated mechanisms of macroeconomic stabilisation (European Commission, 2014).

In the absence of reliable figures concerning income losses incurred by employees who were laid off, the net replacement rate of unemployment benefits can be used to estimate them. In many EU-countries, the average net replacement rate of unemployment benefits is between 60 and 70%. This corresponds with an estimated income loss of at least 30% in the event of unemployment.

Another consequence of the crisis in several countries appears to have been the reinforcement of labour market segmentation with a general tendency for those at the bottom of the labour market (i.e. those in low skilled and precarious employment) to be hardest hit. With the crisis, the downward pressure on wages has become more prevalent resulting in an increase of the number of working poor, particularly among temporary workers and women. In some Member States, insecure and illegal employment boomed as well (EuroMemo Group, 2010). Taking into account the overrepresentation of vulnerable groups in precarious job positions, they were most likely to become the victims in case of business restructuring activities (Françon et al., 2010).

1.2. EFFECTS ON THE INCOME AND POVERTY LEVEL

As far as income inequalities between income quintiles are concerned, at first sight, no general pattern of a widening gap during the crisis emerges at EU level. Table 1 shows the inequality of income distribution in the EU27 on average as the ratio of total income received by the 20% of the population with the highest income (top quintile) to that received by the 20% of the population with the lowest income (lowest quintile).

TABLE 1: INEQUALITY OF INCOME DISTRIBUTION – INCOME QUINTILE SHARE RATIO

	2007	2008	2009	2010	2011	2012
EU27	5	5	4.9	5	5.1	5.1

Source: EU-SILC, Eurostat.

The measured income inequality level remained relatively stable in the EU as a whole. However, the evolution of the income inequality varied greatly across Member States. In some EU Member States, income inequality declined between 2008 and 2012. Spain, Italy, Denmark, Ireland, Hungary and Slovakia, on the contrary, experienced a considerable rise in income inequality in that same period (EC, 2014).

Despite the exceptional severity and duration of the economic crisis, it appears difficult to provide hard evidence about its social and poverty impact. The evolution of the risk of poverty and exclusion (AROPE-indicator) at EU level since the outbreak of the crisis in 2008 can be found in Table 2.[3] Rather surprisingly, according to official statistics, the proportion of the people at risk of poverty or social exclusion in the European Union seems to have increased only slightly, from 23.7% in 2008 to 24.8% in 2012. In absolute terms, the increase is more impressive: 6.5 million people – whereas the ambition of Europe 2020 was a reduction by 20 million. Moreover, as will be demonstrated in Section 1.2 below, the figures tend to dissimulate part of the impact on poverty because the overall decline of the living standard was reflected in a decline of the (relative) poverty thresholds in many EU countries.

TABLE 2: PEOPLE AT RISK OF POVERTY OR SOCIAL EXCLUSION (IN %)

	2008	2009	2010	2011	2012
EU27	23.5	23.1	23.6	24.2	24.8

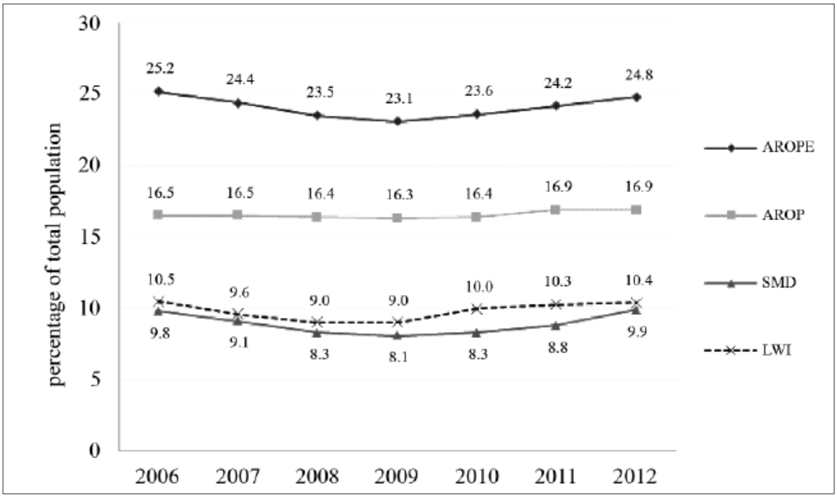
Source: EU-SILC, Eurostat.

While relative poverty did not increase substantially in the EU and in most countries, the poverty threshold itself declined dramatically in a number of countries, reflecting the general decrease of household incomes. Between 2008 and 2012, the threshold fell by 22% in real terms in Greece, 16% in Latvia, 14% in Ireland, 12% in the UK, Romania and Spain, 10% in Hungary, 9% in Lithuania and 6% in Italy.[4] This shows that even at constant relative income positions, people living on low incomes are facing considerable reductions of their resources that were already considered insufficient to maintain a decent living standard before the crisis.

(3) The official definition of 'poverty' has been revised in 2010. Until then, the 'at-risk-of-poverty' (AROP) rate was based on financial income only, using 60% of the median disposable equivalised income as the poverty threshold. Since 2010, two criteria have been added to make up the 'at-risk-of-poverty-or exclusion' (AROPE) rate: severe material deprivation (at least four items from a list missing in the household) and very low work intensity (less than 20% of the available time of all adults in the household worked).

(4) Estimates based on Eurostat data AROP thresholds and harmonised indices of consumer prices 2008-2012. For Ireland, we used the 2011 threshold as a proxy for 2012. Drops of 5% or less are not reported.

FIGURE 1: TREND IN NUMBER OF EU INHABITANTS AT RISK OF POVERTY OR EXCLUSION



Source: Eurostat, EU-SILC (ilc_peps01). Eurostat provisional estimates for 2012.

Using a financial poverty (AROP) threshold 'anchored'[5] in 2005, the poverty rate in the EU15 increased by 1.8% rather than 1.1% between 2008 and 2012. Even if we assume a strong overlap between anchored poverty and the other components of the AROPE index, this would mean that the increase in the absolute number of inhabitants at risk of poverty or exclusion has increased by *10 to 13 million* rather than 6.5 million in four years.

Even more worrisome is that the poor are getting poorer as the gap between the average income of the poor and the 60% of the median income threshold is increasing. Between 2008 and 2012, the poverty gap widened for all but a few Member States and with particularly strong rises in high-poverty countries such as the Baltic States, Slovakia, Italy and Spain (European Commission, 2014).

All in all, drawing unambiguous conclusions with regard to the distributional impact of the crisis is difficult. The impact of the crisis on income inequality depends precisely on who is affected by the crisis and where they are located in the distribution in the first place. A second reason for the difficulties in finding evidence may be the time lag of the official statistical material (such as EU-SILC), and indeed time lags between different groups in income shifts. While the median incomes are mostly affected during the first phase of the crisis, social benefits may remain

(5) The anchored poverty threshold is held constant at the level of a reference year and adjusted only for inflation.

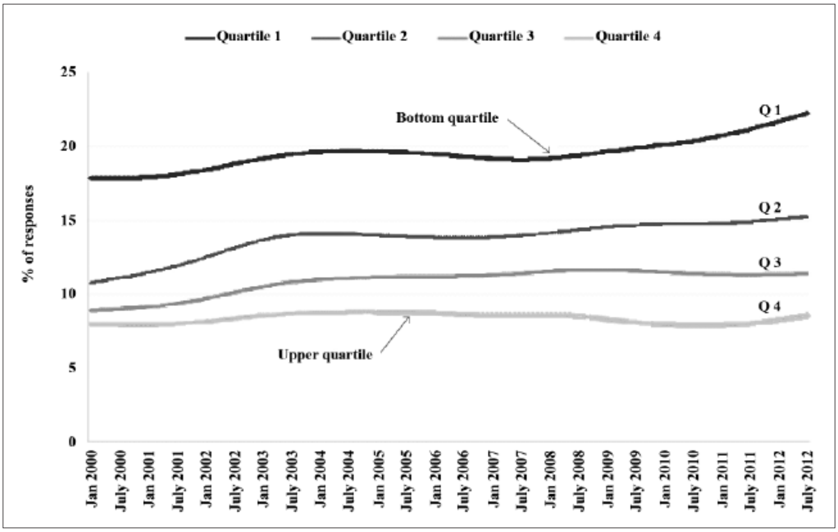
at the pre-crisis level for a while, due to the combination of 'automatic stabilizers' and counter-cyclical reactions of governments (see EC 2014, pp. 57-58). This may indeed explain the slight decline of the relative poverty rate in the first phase of the crisis. Because of the time lag between the decline of the median and the lowest incomes, it is possible that poverty statistics are flattered in this first phase of the crisis. Another problem in drawing general conclusions is the diversity of experience across countries. This is related to the specific effects of the crisis in each country as well as to variation in systems of social protection, labour market institutions and so on (Jenkins et al., 2011).

Nevertheless, the impact of the crisis on the social situation has now become more acute as the initial protective effects of lower tax receipts and higher levels of spending on social benefits (automatic stabilizers) have weakened. A new divide is emerging between countries that seem to be stuck in a downward spiral of falling output, fast rising unemployment and eroding disposable incomes and those that have so far shown good or at least some resilience. In general, the latter tend to have better-functioning labour markets and more robust welfare systems (EC, 2014). Besides the considerable inter-country differences, the crisis contributed to social polarisation within each Member State by worsening the position of at-risk groups. Young people have been particularly hard hit with nearly one in four active Europeans aged 15-24 being unemployed. Non-nationals, the low-skilled and men were also badly affected by the deteriorating labour market conditions (European Commission, 2013c). Jobless households are an extremely vulnerable category, with financial poverty risks ranging between 40% in Denmark and 76% in Bulgaria. Moreover, those poverty risks have increased between 2008 and 2012 (EC, 2014).

In order to get the complete picture, it is also necessary to look beyond the traditional statistics. The 2012 European Quality of Life Survey looks at the relation between subjective and objective measures. One of the key findings was that unemployment –and long-term unemployment in particular- has a huge impact on subjective well-being. Furthermore, it was found that the most vulnerable groups (the lowest income quartile, the long-term unemployed and older people in Central and Eastern Europe) showed the greatest decline in subjective well-being in recent years. The results furthermore indicate that these vulnerable groups are expected to swell even more given that over one in three respondents said that their financial situation was worse than 12 months before (Eurofound, 2012).

The most up-to-date proxy for trends in poverty and inequality is the indicator of financial distress among households, derived from the six-monthly consumer surveys of the EC, as reproduced in Figure 2. The figure shows a clearly diverging trend in financial distress between the bottom and top quartiles of the income distribution, especially since the Summer of 2008. A similar graph relating exclusively to Spain shows an increase of the percentage of households reporting financial distress in the bottom quartile from 5% in 2000 to 37% in 2012.

FIGURE 2: PERCENTAGE OF HOUSEHOLDS REPORTING FINANCIAL DISTRESS, PER QUARTILE OF THE INCOME DISTRIBUTION (2000-2012)



Source: EC 2013c, p. 22.

1.3. BEYOND WORK AND INCOME

In addition to unemployment and income losses, companies and households were also confronted with debt crises. Because banks became reluctant to lend as a result of the sovereign debt crisis, more and more enterprises ran into difficulties in borrowing the cash they needed or to pay off debts and went bankrupt or were forced to take drastic action. A survey released by the European Central Bank (ECB) showed that the financial institutions reduced the credit available to companies in the third quarter of 2011. Instead of being more lenient towards the credit-starved companies, banks preferred to deposit the cash with the central bank for safekeeping (Scott, 2012). Similar reactions are seen with respect to the lending conditions of banks to individual consumers, and low-income families in particular. The conditions linked to liquidity and credit facilities were tightened, resulting in a decrease as well as tougher lending opportunities for private borrowers – including personal bankruptcies, households losing their homes and becoming homeless (Carpenter et al., 2011). At the same time, the debt accumulation in the lowest-income groups led to the emergence of a ‘debt class’ which in some countries has destabilised credit markets and indeed triggered the crisis.

The peripheral countries of the eurozone, and particularly the so-called "PIIGS" (Portugal, Ireland, Italy, Greece and Spain – later joined by Cyprus), suffered significantly more than other EU countries following the global economic downturn (Caritas Europa, 2013). Because of the enormous unemployment rates for young people in the peripheral countries, many young people decided to emigrate, looking for work in countries such as Germany, France and Poland. Other youngsters even found better employment opportunities in South-America. This resulted in a loss of around 300,000 (often well qualified) young people in recent years in Spain (Tremlett, 2011). Even more alarming effects are reported on (mental) health and mortality. Karanikolos et al. (2013) analyse the complex and sometimes ambivalent relationships between economic recessions and various types of health outcomes.[6] They report that the correlation between economic crises, depression and suicide rates is well documented for previous recessions, and therefore the rise since 2008 should not come as a surprise. However, experience also shows that the impact of adverse economic circumstances also varies with the resilience of welfare provision. Ireland saw a 13% increase in suicides among people under 65 between 2007 and 2008 (Von Hoffman, 2012). In Spain, suicide rates have increased by one-third since 2008, from 6 to 8 per 100 000 inhabitants. Whereas the majority of recent suicides were committed by unemployed youngsters, a substantial number also concerned people who had been evicted from their homes (Burgen, 2013). Before the financial crisis began, Greece had the lowest suicide rate in Europe at 2.8 per 100 000 inhabitants. Since then, this figure has almost doubled and keeps rising at an alarming rate (Eurostat, 13.12.2012). The incidence is clearly concentrated among groups experiencing serious economic hardship. Similar increases were reported across other hard-hit areas of Europe. In Bulgaria, seven consecutive cases of men burning themselves in public (and several others prevented by the police) in the Spring of 2013 reflected a wave of despair and protest among the population (De Koning, 2013). Similar stories were reported in Romania (Ciobanu, 2011).

In several Member States, the crisis led to a growing sense of insecurity, helplessness, hopelessness and fear among vulnerable segments of the population. This resulted in rising social tensions and the erosion of social cohesion. The 2010 Amnesty International (AI) report suggests that the economic downturn has led to a rise in discrimination, racism and xenophobia throughout Europe, particularly in countries such as Italy, Slovakia and Hungary (Amnesty International, 2010).

Besides an increasingly negative attitude towards immigrants, there also appears to be a loss of confidence in the capacity of governments to take the necessary steps

(6) For example, rising unemployment appears to go in pair with a lower incidence of road traffic deaths but higher rates of alcohol-related deaths, suicides and murders. Whereas average health seems to improve in times of economic downturn, there is a clear adverse effect on physical as well as mental health of unemployed people.

to reduce poverty and social exclusion. A recent study showed that the electorate often punishes the party in government in bad economic times. This was clearly the case for Greece. The statistical model showed that the evaluations of the economy correlate with support for the governing party, even when other powerful predictors of party choice (such as ideology) were included (Nezi, 2012). Unsurprisingly, according to the Eurobarometer of the Autumn 2013, the percentage of European citizens who 'tend not to trust the EU' has nearly doubled (from 32 to 58 per cent) between 2007 and 2013. Citizens' distrust in national governments is even higher, with an average of 72% in the EU28 and peripheral countries reaching peaks above 85% (EC, 2013f). Supplementary support for the relation between socioeconomic debacles and legitimacy crises can be found in the results of the Edelman Trust Barometer. This indicator shows that the citizens' trust in their national governments has reached a historic low (Edelman, 2014).

2. EU ANTI-CRISIS POLICIES AND THEIR IMPACT ON POVERTY

In March 2010, the EU launched its growth strategy for the coming decade. This Europe 2020 strategy included five headline targets in the areas of employment, R&D, climate and energy, education and the fight against poverty. For our purpose, reducing the number of people at risk of poverty or social exclusion by 20 million by 2020 is the most noteworthy of these headline targets. Within the Europe 2020 strategy, two key leverages were put forward: the reduction of early school leaving and the increase in employment rates.

As such, the Europe 2020 blueprint looks coherent and shows a fair balance between economic, social and environmental objectives. However, the strategy was soon overshadowed by the Euro-crisis, which led to a series of drastic measures imposing a neoliberal macroeconomic agenda on Member States, combining internal competition with austerity – to the detriment of the social objectives. This section will give an overview of how the EU and the Member States tried to tackle the negative consequences of the crisis. Often, there will be a direct link between these two policy levels given that the Member States had to comply with the agenda negotiated at EU level. Nevertheless, some differences can be observed between different Member States.

The European Union has created a variety of instruments to tackle the negative consequences of the crisis. The first section will give a brief overview of the most important initiatives taken at EU level. In the following section, it will be demonstrated that the internal competition between the Member States constitutes an obstacle to an unambiguous and strong reaction. Finally, the effects of the European anti-crisis policy on poverty and inequality will be discussed.

2.1. THE INSTRUMENTS: INTERNAL COMPETITION AND AUSTERITY

According to De Grauwe (2013), the *unequal geographical impact* of the crisis (mainly on the PIIGS countries) has actually been aggravated by the architecture of the European monetary union, which transferred traditional monetary policy instruments (such as exchange rate or interest rate policies) from the Member States to the EU level. As Ireland, Greece and Spain were booming in the 2003-2008 period, these countries were unable to counter inflation and were 'forced' to live with the same low interest and hard currency rates as other Member States. This may have contributed to the bubbles experienced by these countries. At the same time, their trade deficits could not be corrected by devaluation, thereby spurring the accumulation of debts and the resulting liquidity crises. The lack of stabilising instruments at national level also necessitated alternative, 'internal devaluation' strategies after the outbreak of the crisis. Internal devaluation strategies include austerity in public budgets and wage cuts. This explains the fast-growing North-South divide in the Eurozone in terms of income, unemployment and poverty (EC, 2014).

In 2011, 23 Member States also agreed on the Euro Plus Pact in order to step up coordination of reforms in areas not fully covered at EU level. The participating countries committed themselves to far-reaching reforms with respect to competitiveness, employment, sustainability of public finances and the reinforcement of financial stability (Duffy, 2012). In order to reinforce the monitoring of Member States' economic and fiscal policies, the EU authorities also agreed on a 'Six-Pack' of legislation on economic governance. Through this initiative, the stability and growth pact was amended to strengthen collective surveillance of national policies, including a much stricter monitoring of national government deficits and debt ratios, but also international competitive positions, wage costs, unemployment and private debts. The surveillance framework was extended with a control mechanism on national budgets (Two-Pack). This procedure ensures that corrective actions (including sanctions on member states) are taken in the event of imbalances.

The main EU policy vehicle has become the 'European Semester' of policy coordination. This cycle was designed to bring together all of the aforementioned commitments, leading to a better ex-ante coordination and follow-up of the decisions. The European semester is launched at the beginning of each year with the Annual Growth Survey and is delivered at national level by Stability Programmes and National Reform Programmes (European Commission, 2012a). Country-specific recommendations are made to each member state, including e.g. austerity measures or cutbacks in social regulations, if these are deemed necessary to restore macro-economic imbalances. These recommendations are subject to prior negotiation procedures but can be enforced through sanctions.

Most importantly, the so-called Troika (EC, ECB and IMF) also insisted on the organisation of specific bailout terms in order to tackle the sovereign debt crises in the PIIGS-countries. These reforms included severe public sector cuts, state asset sell-offs and the weakening of labour market regulation. Despite all good intentions to support weak economies and help restore macroeconomic balances, the Troika's approach illustrates how financial power relations have completely overruled democratic decision-making in these countries as well as relations of reciprocity between member states. It is worth investigating to what extent these shifts in political balance explain the historical low in confidence in the EU in these countries.

The aforementioned initiatives also demonstrate that the EU authorities' main reaction to the crisis was to streamline the macroeconomic policies of the Member States, according to an orthodox neoliberal doctrine. While these measures clearly limited the freedom of movement of the weakest EU countries, the organizational structure of the EU still allows the stronger member states to pursue national policies without taking into account the negative effects on other Member States.

2.2. MACROECONOMIC EFFECTS

For an economic and monetary union to function well, it must have some means of dealing with divergent developments among its Member States. Some coordinated or centralised budgetary powers are indispensable in this respect. This necessity had been ignored when designing the monetary union. As a result of the absence of a coherent budgetary policy, an effective macroeconomic response to the recession was not possible. This deadlock in European integration of the macroeconomic policy mix favours the resort to non-cooperative strategies among member countries, such as competitive wage reductions, social dumping and fiscal competition (EuroMemo Group, 2010).

The non-cooperative strategy of structural reforms carried out mainly in Germany since 2003 was important in this respect because it had a significant impact on the orientation of macroeconomic policies throughout Europe. The German economic policies have led to inflation rates well below the ECB's norm, resulting in serious losses of competitiveness for the other Member States. Consequently, they could only restore their competitive position by using non-cooperative strategies themselves. Some Member States, and the PIIGS-countries in particular, were forced to engineer so-called 'internal devaluations'. This implies reducing prices, social benefits and wages relative to Germany (as an alternative for devaluation of national currencies).

The idea behind these internal devaluations was that a wage reduction would lead to an enhanced competitiveness, resulting in an increase of exports. In an open economy, the 'export-driven' strategy is more likely to be successful given that exports represent an important share of the economic activity. However, because the euro-area as a whole is a relatively closed economy, with extra-EU exports making up less than 15 per cent of GDP, wage moderation in the euro-area can only have a contractionary effect on demand (Stockhammer, 2007). This leads to a decline in aggregate demand and domestic production, resulting in turn in increased government budget deficits and a deterioration of the fiscal position of those countries. Moreover, the mere decline of GDP automatically translates into an increased debt/GDP ratio, necessitating further cutbacks in public expenditure.

In contrast with this 'social dumping' strategy, a growth strategy based on domestic demand would imply that higher wages and benefits are *favourable rather than detrimental* for the economy. In a relatively closed economy such as the EU, such a strategy would lead to a higher demand, and thus more economic growth – while its depressing effect on the balance of payments and investments remains relatively modest. For example, considering that a 1 percentage point increase in the wage share leads to a net increase in aggregate (private) demand by approximately 0.2 percentage points of GDP, it is obvious that the EU as a whole would benefit from higher wages and benefits, whereas wage moderation and cutbacks on benefits are to be avoided (Stockhammer, 2007; 2012). The problem is that this requires more European solidarity, whereas the current climate tends to evolve in the opposite direction.

As such, the situation within the EU can be compared with the prisoners' dilemma. This concept is used to explain a paradox in decision analysis in which two individuals acting in their own best interest pursue a course of action that is detrimental to their common welfare. In the case of the EU, the best option would be that all European countries pursue policies aimed at stimulating demand (e.g. by keeping wages and benefits high). The worst situation occurs when the opposite situation takes place: if all Member States opt for wage moderation, overall demand tends to implode, leading to the aforementioned negative effects. Wage moderation strategies can be beneficial for some Member States only on condition that the other countries do not follow the same path. This European prisoners' dilemma clearly shows that a eurozone with insufficient coordination threatens to end up in the worst scenario of collective impoverishment (De Grauwe, 2013).
Another key element of EU anti-crisis policy is austerity in government spending, as a means to consolidate government budgets, break the debt spiral and restore the equilibrium on financial markets. Nobel prize laureate Paul Krugman was one of the main critics of European austerity policies. He claimed that the austerity programmes imposed on the PIIGS countries in particular would do more harm than good, by dragging these countries along into a negative spiral of deflation, reduced tax revenues and further government deficits. A key argument in the debate was pro-

vided by a meta-analysis of 133 IMF-led austerity programmes, carried out by the IMF's Independent Evaluation Office (2003), which concluded that the pursued deflationary fiscal policy – reducing spending and increasing taxes – in the Member States had detrimental effects. These austerity measures have led to sharp falls in the rate of economic growth, suggesting the negative multiplier effect is larger than may be expected in usual situations. In all countries, a fiscal consolidation is considerably more contractionary if made during a recession than during an expansion. Spending multipliers when the economy is in a recession are up to 10 times larger than spending multipliers during an expansion.

The IMF-study showed that withdrawing fiscal stimuli too quickly in economies where output is already contracting can prolong recessions, without even achieving the expected budget balance. This is particularly the case if the size of the consolidation measures is large and if they are centered around cuts to public expenditure, as the reductions in public spending have powerful negative effects on the purchasing power of financially-constrained agents in the economy. Instead, smooth and gradual consolidations are to be preferred, particularly for economies in recession facing high risk premia on public debt. In these cases, sheltering growth is key to the success of fiscal consolidation (Battini et al., 2012). The European Federation of Public Service Unions concludes that, as a result of austerity measures amounting to 7% of GDP across the EU in the past five years, the reduction of public deficits from 7% to 4% of GDP is a poor achievement. Moreover, in the same period, debt ratios have kept rising and a 'second recession' has been triggered between 2010 and 2012. The corresponding effects on countries such as Portugal, Greece and Spain are even more counter-productive (EPSU, 2013a).

2.3. EFFECTS ON INEQUALITY AND POVERTY

The severity of the implemented austerity policies varies greatly across Member States. While in a few countries a relatively limited social impact is expected, policies of other Member States are likely to hit the most marginalised worst and tend to boost long-term unemployment (Duffy, 2012; EC, 2013a; EC, 2014). Unfortunately, very little empirical evidence is available on the impact of anti-crisis policies on poverty. The 'horizontal social clause' (Article 9 of the Treaty on the Functioning of the EU) states explicitly that "*In defining and implementing its policies and activities, the Union shall take into account requirements linked to the promotion of a high level of employment, the guarantee of adequate social protection, the fight against social exclusion, and a high level of education, training and protection of human health*." The systematic use of ex-ante Social Impact Assessment as a tool to ensure coherence between social and economic (or any other) objectives has been generally accepted as a principle of good governance. Although the EC has widely advocated the implementation of social impact assessment at all levels of government, we are not aware of any examples where either country-specific recommendations or Troika prescriptions have been accompanied with such analyses. At the level of member states, ex-ante impact assessments do exist in some countries – sometimes commissioned by the government, and sometimes initiated by non-governmental bodies or researchers – but they remain exceptional (examples are discussed in Brewer, 2012).

Incomes of the poor have been squeezed from different sides. Germany's response to the crisis was to keep *wages* down in order to encourage export-led growth and thus safeguard German jobs. Other European countries took the same path. While for the majority of the working population, low or no wage growth may not push them into poverty, it does increase poverty risks for marginal workers (Salais, 2012). Some Member States also introduced far-reaching reforms of their labour market aimed at enabling more flexible forms of contract and working arrangements. While these measures proved to be effective in several countries in preserving employment at the peak of the crisis, particularly in the manufacturing sector, they also led to more insecurity (European Commission, 2012a).

In several Member States, the austerity policy of the European Union had a direct effect on *minimum wages*. In particular in those countries suffering most acutely from the economic crisis, the Troika (European Commission, European Central Bank and IMF) have more or less directly influenced the development of the minimum wages. The extreme case was Greece, which was forced to reduce its minimum wage by 22%. But other countries also cut back their minima. In Lithuania and the Czech Republic, they remained constant in *nominal* terms for 4-5 years. In 2011, minimum wages decreased in real terms in 15 out of the 22 countries examined by the European Trade Union Institute (ETUI). In most other EU-countries, the upgrading of minimum wages was also restricted to the legally stipulated minimum rate. Currently, minimum wages are at critically low levels (sometimes below the AROP threshold), leading to increasing levels of in-work poverty. Schulten (2012, p. 7) concludes that "although there is no direct economic link between the current debt problems and the development of minimum wages, a restrictive minimum wage policy has, nonetheless, under pressure from the EU, come to be regarded as a fixed component of the currently prevailing austerity policy".

Another reaction to the crisis was the weakening of the social and *legal protection of labour*. This led to the proliferation of insecure jobs in atypical contracts, with reduced or no employment protection. In the context of the current economic downturn, workers faced substantial reductions in working hours. Given that underemployment appears to be a key determinant of in-work poverty, the rate of in-work poverty may rise significantly in the coming years (OECD, 2009). Following complaints from trade unions, the European Committee of Social Rights, the body within the Council of Europe responsible for monitoring compliance with the European Social Charter, decided that parts of the Greek labour market reforms induced by the EU were in violation of the European Social Charter. The difference in labour and social protection between older and younger workers and the absence of any dismissal protection during the first year of employment infringed with the charter. Similarly, the ILO Committee on Freedom of Association is dealing with complaints lodged by Greek trade unions on the potential violation of the core labour standard conventions on freedom of association and collective bargaining. The Committee found that there were a number of repeated and extensive interventions into free and voluntary collective bargaining and an important deficit of social dialogue. As a result, the Committee insisted that the social partners should be fully involved in the determination of any further alterations within the framework of the agreements with the Troika (International Labour Organization, 15 November 2012). Clauwaert and Schömann (2012) mapped a range of country-specific recommendations from the EC and conditions 'negotiated' by the Troika with the aim of flexibilising labour markets in the member states, and identified a number of cases where they interfere with the freedom of association, other basic social rights, collective bargaining agreements etc. Although the erosion of labour protection may in some cases contribute to new employment opportunities, it also undermines the role of work as a leverage against poverty. In its 2013 issue of 'Employment and social developments in Europe', the EC acknowledges that non-working adults taking up work between 2009 and 2010 had only one chance out of two to leave poverty. Among the potential (work-related) explanations, the Commission mentions temporary and part-time work, as well as a remarkably high share (40%) of wages below the poverty threshold (EC, 2014, p. 154 ff.).

Whereas *social protection* schemes have played an important role in mitigating the impact of the crisis, the pressure to limit social transfers has strongly increased. In some EU countries, this led to cutting the level of payments and/or restricting access while in others indexation and uprating arrangements came to a halt. The impact of the social transfers in reducing the risk of poverty strongly depends on the type of social protection scheme. Given the wide disparities between the social protection systems in the different Member States, the effects of social transfers in reducing the poverty risk also vary strongly. While the social transfers in Sweden reduce the proportion of people at risk of poverty by more than half, they have a limited impact in Spain (Françon et al., 2010).

Cuts in the *health care sector* also triggered national governments to shift part of the costs to the users while reductions and subsidies for vulnerable groups were being reviewed (Duffy, 2012). As was demonstrated by Karanikolos et al. (2013), the effect of the crisis on health and mortality outcomes can be attenuated or reinforced, depending on the social protection measures adopted in the health sector as well as related social services. The authors show, for example, that the health impact of the financial crisis was much weaker in Iceland where the government ignored IMF prescriptions and decided to maintain the level of health and social protection. In Greece, due to the closure of many health care centres and cutbacks in preventive care (including e.g. distribution of condoms and sterile needles to drugs addicts) have led to fast-rising HIV incidence and the spread of infectious diseases such as malaria and tuberculosis. The reduced coverage of public health insurance, combined with cutbacks in public health services and a genuine crisis in the pharmaceutical sector have caused waiting lists in hospitals and a dramatic reduction in the use of health services, resulting in turn – among other things – in a 43% rise of child mortality between 2008 and 2010.

In several countries the cuts in *other services* were unevenly spread and had a more severe impact on people who are experiencing poverty and social exclusion. The cuts in benefits and services have enhanced their risk of long-term exclusion, particularly among women, children, young people, the Roma, migrants and temporary workers. Whereas these vulnerable groups often rely on the support from NGOs, local and central funding to NGOs has also been cut, curtailing their ability to the increased demand (Frazer et al., 2011; Caritas Europa, 2013).

Despite the general tendency within the EU to pursue austerity policies, the case of Latvia demonstrated that those restrictive policies should not be seen as an unavoidable dogmatic recipe. The fiscal adjustment programme imposed by the IMF had devastating effects. Economic activity contracted by close to one-fifth in 2009. Instead of sticking to overambitious and tight fiscal objectives, the Latvian authorities found a way to abandon this austerity policy by substantially loosening the fiscal straightjacket. The consequence was that the economy ended its free fall and economic activity stabilised in the course of 2010. It was the rebound in domestic demand that supported growth in Latvia from 2010 onwards. This renewed growth was only possible by handling the deficit targets in a flexible and realistic way (Janssen, 2012).

Although the EU seems to be holding on to its strategy, the anti-crisis measures are heavily criticised by other instances as well. According to the European Anti-Poverty Network, the Europe 2020 strategy has been narrowed down to an instrument of economic governance. The priorities presented in the six pack legislative package appear to override any commitment to inclusive growth and the poverty target. The Network believes that the latter are only viewed as secondary concerns (Duffy, 2012). The European Economists for an Alternative Economic Policy in Europe (EuroMemo Group) agreed that the neoliberal bias of the Union's policies is evident, referring to EU recommendations regarding employment flexibility, reductions in employers' social contributions for those on lower incomes and the increase in the retirement age, along with cutbacks in public expenditure, welfare and wages (Euro-

Memo Group, 2010). Furthermore, Europe's political and economic elites are being blamed for the absence of a coherent diagnosis of the crisis. This led to a chronic underestimation of the challenges represented by the 'collapse of financialised capitalism' (Leaman, 2012).

3. SOCIAL INVESTMENTS: A NEW PARADIGM FOR EUROPEAN WELFARE STATES?

Whereas cutbacks on social expenditures in general were met with mixed feelings, many key actors, institutional as well as non-governmental, criticised the cuts in sectors such as education and health care. The European Anti-Poverty Network (EAPN) believes that a major programme of social investment in education, health and social services, as well as the provision of strengthened social protection is essential to restore business and consumer confidence in the short and medium term (Duffy, 2012). The OECD agrees that investments in the human capital of the workforce are key for reversing the growth in inequality as a result of the crisis. Policies that promote the up-skilling of the workforce -for the low-skilled in particular- would help to boost their productivity potential and future earnings (OECD, 2011a). According to Eurochild (2012), many Member States have made solemn commitments but failed to improve the quality and accessibility of early childhood services. Other NGOs and trade unions supported these demands (see e.g. Confederation of German Trade Unions, 2012).

In its call for a 'Social Investment Pact', the Committee on Employment and Social Affairs of the European Parliament advocated social investments as part of the EU's responses to the crisis. According to the Committee, a better implementation of the employment, social and education goals is required for a re-balancing of the Europe 2020 strategy. The reason for this emphasis on social investments is their potential to reconcile social and economic goals. Therefore, they should not only be treated as spending but also as investments that will yield significant returns in the future (Committee on Employment and Social Affairs, 2012).

The European Commission echoed this report with a Communication on the *Social Investment Package* in February 2013. Recalling the inclusive dimension of the European growth strategy, the Commission advocates intensified investments in human capital through early childhood education, the New Skills Agenda, active labour market policies (including youth guarantee schemes), the social economy, preventive health policy as well as rehabilitation, active ageing, a more targeted and smarter allocation of social expenditure. The Communication refers explicitly to the 2008 Recommendation on Active Inclusion as part of the social investment agenda. While urging Member States to maintain social expenditure levels, the EC also commits itself to earmark 25% of all support from the Structural Funds to social investment, and 20% of the European Social Fund budgets to the fight against poverty.

This was followed in October 2013 by another Communication (2013e) announcing that the Commission would devote more attention to the social dimension of the EMU. Additional social indicators would be included in the dashboard for the European Semester; the social partners would be consulted more frequently; and the Structural Funds would focus more on the fight against poverty and the mobility of job seekers within the EU.

The Social Investment Package integrated some earlier and new EC initiatives into a coherent framework. In what follows, we will focus on three key policy areas where the synergies between economic and social inclusion effects are most obvious: early childhood education and care (ECEC), education and training, and active labour market policies. Our focus will be on scientific evidence about the effectiveness of these strategies.

3.1. THE FIGHT AGAINST CHILD POVERTY

The long-expected EU Recommendation on child poverty was issued at last as part of the Social Investment Package (EC, 2013d). The recommendation builds on three pillars, two of which co-incide with the 2008 Recommendation on Active Inclusion:

- access to adequate resources;
- access to affordable quality services;
- the third pillar, the children's right to participation, can be seen as the counterpart of the 'inclusive labour markets' pillar in the Recommendation on active inclusion.

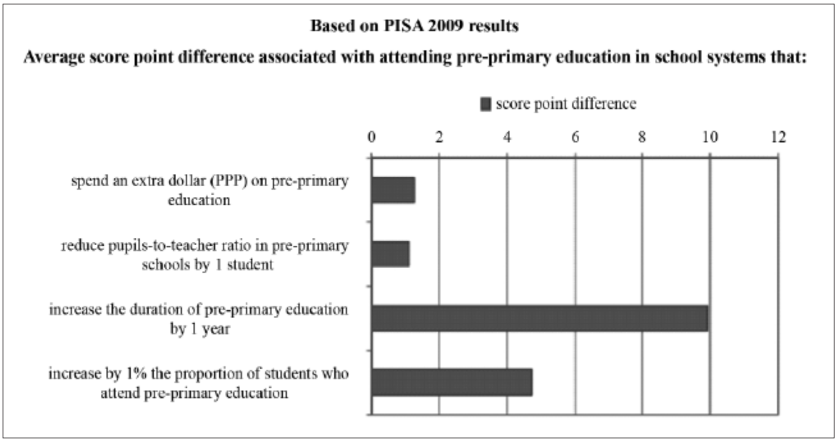
It is interesting to note among the arguments in the introduction, apart from references to children's rights and values of the EU, an explicit reference to cost-benefit arguments: "*Early intervention and prevention are essential for developing more effective and efficient policies, as public expenditure addressing the consequences of child poverty and social exclusion tends to be greater than that needed for intervening at an early age*." Indeed, whereas (social) policy often shows a tendency to cure problems, such reactive interventions in the complex process of human development are often less efficient. Instead, it is necessary to put more weight on proactive measures to tackle poverty, inequality and social disadvantage at a very young age. Research in different scientific disciplines (developmental psychology, neurology, pedagogy and economics) has proven that better results can be obtained by shifting from curative to preventive actions, at the earliest possible age.

Even before children have their first school experience, significant differences can be observed between children of a different social origin with respect to cognitive and socio-emotional skills. A longitudinal study analysed the differences in the early cognitive development of cohorts of children with a low, medium and high socioeconomic status (SES). From the age of 2, a correlation could be observed between their position in the overall distribution and the socioeconomic status of their families. Over time, the gap between the three cohorts appeared to increase. Moreover, children from high-SES families with a low score at the age of 22 months were able to catch up with their counterparts, while children from low-SES families with a low score had considerably fewer opportunities to improve their position. All this points to the importance of favourable living conditions for the development of children. It also implies that supportive investments in the development of children at a young age can make a difference in the long run (Alava et al., 2011). Evaluation studies of early intervention programmes showed that integrated approaches combining linguistic, cognitive and socio-emotional stimulation produce the best outcomes.

Longitudinal follow-up studies of various pre-school and early school programmes demonstrated convincingly that high-quality services can have a major impact on the (socio-emotional and cognitive) development of young children. Such programmes also managed to attenuate significantly the effects of social disadvantage. The most important benefits of pre-school programmes include more successful school careers, higher earnings, a better health condition, and less dependency on welfare. As a consequence, such interventions produce enormous future welfare gains through enhanced productivity and economies on public expenditures. Detailed cost-benefit estimates for the 'best practice' case in the USA, the Perry Preschool Programme, concluded that the social benefits equalled 6 to 13 times the cost of the programme (Belfield, 2006). In the context of the PISA 2009 study, the OECD (2011b) estimated the impact of participation in pre-primary education on the skills of 15-year-old students – expressed in 'score point differences'. As a yardstick for the assessment of the size of these effects, consider that a difference of 39 points corresponds with the effect of a full year of formal schooling. Despite the rough nature of the data,[7] the analysis showed various significant effects, as can be seen from Figure 3. Note that quality plays a key role, and that 'cheap' commercial child care may also have negative effects on child development (Penn, 2009).

(7) The information is based on retrospective questions included in the PISA questionnaires answered by students, combined with national data on quality indicators.

FIGURE 3: EFFECTS OF PARTICIPATION IN/QUALITY OF PRE-PRIMARY EDUCATION ON SKILLS AT AGE 15



Source: OECD, 2011b.

3.2. EDUCATION AND TRAINING

Given the key role of human capital in the Europe 2020 strategy, The European Commission launched the *New Skills for New Jobs* initiative. This policy document mainly sets out to promote better anticipation of future skills needed, develop better matching between skills and labour markets needs and bridge the gap between the worlds of education and work (Schmid and Keraudren, 2012). The initiative was echoed by a communication from DG Education and Culture, '*Rethinking Skills*', which was accompanied by an impressive analysis of trends and challenges in the field of education and lifelong learning (EC, 2012c).

Technological change, globalisation, shifts in demand patterns, ageing of the workforce, polarisation between high- and low-skilled labour market segments necessitate a number of shifts in the supply of skills:

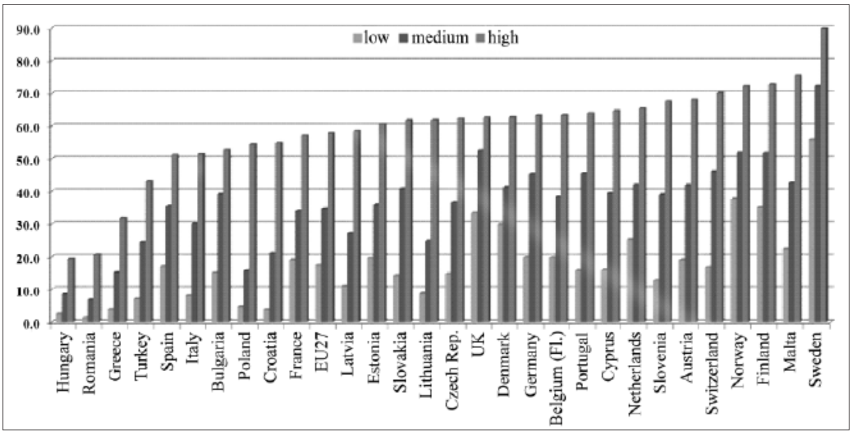
- more secondary as well as tertiary education graduates;
- a shift away from industrial to service-sector skills;
- more generic (as opposed to job-specific) skills;
- more STEM (science, technology, engineering, mathematics) graduates;
- more lifelong learning;
- more collective learning (learning organisations, learning cities/regions), and
- more workplace learning.

Despite its comprehensive nature, the Rethinking Skills agenda puts a strong emphasis on the acquisition of basic skills, among young people as well as adults. This implies strategies to reduce early school leaving, but also curriculum reforms (to foster the development of generic work-related skills such as communication, problem-solving, languages and ICT skills), and a greater priority to basic literacy, numeracy and ICT training for adults. It goes without saying that these priorities converge to a large extent with the social inclusion agenda.

Moreover, education is probably the area where economic and social interests coincide most. de la Fuente and Jimeno (2005) estimated the returns on education in 14 EU countries and concluded that the *private* rate of return was in most cases between 7.5 and 10%; analogously, the *social* rate of return (which takes into account government subsidies and revenues as well as spill-over effects on third parties) varied between 8.5 and 11.5% (de la Fuente, 2003). Endogenous growth theory has recently discovered that education does not simply enhance welfare *levels*, but also accelerates *growth rates*, by extending the learning and innovation capacity of the economy. Using an econometric model that reflects the impact of *skills* (rather than years of schooling) on economic growth in the past (controlling for other determinants), and combining a multitude of data sources, Hanushek and Woessmann (2010) estimated the impact of improved skills levels of the European workforce on economic growth. Note that the effects materialise only in the very long run, as it takes approximately 60 years for a new cohort of children to complete their careers in the labour market. However, as small effects cumulate over time and across successive cohorts of new labour market entrants, the discounted cumulative GDP gain of the EU across the period up to 2090 can be very large. Applying this model to the EU benchmark of reducing reading underperformance at age 15 in all Member States to (at most) 15% by 2020, the authors estimate the welfare gain at 23 trillion EUR – i.e. 177% of the EU's current GDP. As the achievement of this objective necessitates targeted action in favour of the lowest achievers, this also implies that the impact will be stronger in the EU countries with the weakest education systems (Bulgaria, Romania, Cyprus and Malta).

Given the delayed impact of skills upgrading strategies targeted at young people, it is certainly worth to conduct similar campaigns to upgrade the basic skills of *adults*. The latter approach may take less time and have a larger impact, as in principle the whole active population can be covered. A noteworthy example of such a comprehensive plan was the Portuguese 'Novas Oportunidades' scheme, which combined second-chance education and training with counselling and tools for the accreditation of prior (experiential) learning. Unfortunately, it seems that the crisis and the change of government have diluted this plan. At EU level, the 'Renewed agenda for adult learning' for the period 2012-2014 and beyond puts particular emphasis on learning opportunities for low-educated adults. Yet, greater political commitment is needed for a successful implementation of this agenda. Its objectives should be translated into quantitative benchmarking, beyond the aggregate 15% participation target in adult education: for example, through specific quantitative targets at national level for participation of *unqualified* adults in adult education, as well as targets relating to outcomes. As Figure 4 indicates, low-educated groups are severely under-represented among adult learners.[8] National plans should also include specific measures and budgets to encourage demand and supply and to boost the efficiency of adult learning.

FIGURE 4: PARTICIPATION IN ADULT EDUCATION, BY LEVEL OF INITIAL EDUCATION



Source: own estimates based on Adult Education Survey, 2007.

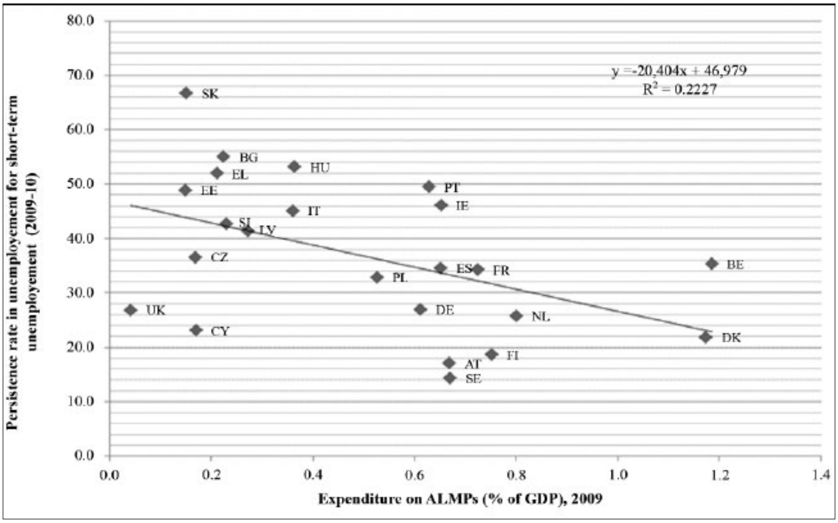
The achievement of the EU targets (expressed in terms of reduced early school leaving, reduced underperformance or second-chance education) will not be easy. It requires strong political support and resistance against the temptation to prioritise the privileged, high-performing learners. It also requires sustained investments over a long period. But it is not less efficient: on the contrary, the benefits in terms of welfare as well as social inclusion will last for generations. It is therefore regrettable that no less than 20 countries or regions have reduced their education budgets in 2011-2012 (Eurydice, 2012).

(8) Note that the 15% target is expressed on a monthly basis, while the rates reflected in Figure 4 are calculated on a yearly basis.

3.3. ACTIVE LABOUR MARKET POLICIES

Active labour market policies (ALMP) can be seen as investments in the employability of individuals, to the extent that they enhance their human and social capital. We need to distinguish between mere 'activation' (which often boils down to exerting pressure on job seekers or just offering short-term work experience) and genuine investments that combine decent work placements with training, counselling and other services. Figure 5 below shows a negative correlation between expenditure on active labour market policies in general and the risk of transition from short-term to long-term unemployment in EU Member States. As regards the relative performance of different types of ALMP, Kluve (2006) reviewed a large number of evaluation studies and concluded that public employment schemes tend to have negative effects, whereas recruitment subsidies and services to job seekers are generally effective in enhancing the employment probability of beneficiaries.

FIGURE 5: ACTIVE LABOUR MARKET POLICIES AND RISK OF TRANSITION INTO LONG-TERM UNEMPLOYMENT



Source: EC, 2012b, p. 96.

A key element of the EC's Social Investment Package is the *Youth Opportunities Initiative*, i.e. a set of measures to combat youth unemployment. In particular, it aims to reduce early school leaving and to foster the school-to-work transition. In eight countries with youth unemployment rates above 30% (in 2011: Greece, Ireland, Italy, Latvia, Lithuania, Portugal, Slovakia and Spain), the Commission participates in Youth Action Teams, providing policy advice including suggestions on how to use unspent money from the Structural Funds (6 billion EUR). Seven other countries with youth unemployment rates exceeding the EU average also get support. The idea of youth guarantee plans is being actively promoted in other Member States. Such guarantee plans aim to ensure that every young person is offered a job, training, apprenticeship or combination of those within four months of unemployment (European Commission, 2012c).

The idea of guarantee schemes for young people (or other target groups such as the long-term unemployed) is not new. The Nordic countries and the UK have introduced them in the 1980s and 1990s, while Austria, Germany, The Netherlands and Poland took the first steps more recently. Although these initiatives were not identical, they share the same key objective, i.e. to prevent young people from being trapped in unemployment and inactivity. In the Nordic schemes, a central role is played by the public employment services in offering the young job seeker a personalised needs assessment and an employment plan, followed by a package of guaranteed tailor-made services.

Accurate targeting of the guarantee scheme is essential, because the cost efficiency depends crucially on the avoidance of deadweight and substitution effects. Deadweight occurs whenever beneficiaries would have found jobs even without subsidies or services. As *all* school leavers enter the labour market as job seekers, it is difficult to target support at those who have the lowest probability of finding work, without discriminating. Substitution effects occur when support for one target group simply reshuffles the queues of job seekers, favouring young people at the expense of other groups that may be equally or more disadvantaged (such as disabled people, migrants, low-skilled unemployed, etc.). Research indicates that the risk of deadweight and substitution effects is higher in active labour market programmes targeted at young people.

Evaluations of early youth guarantees such as the UK's Youth Training Scheme and the Danish Law on Active Labour Market Policy showed negative effects on the employment chances of participants, mainly because of the rigidity and lack of quality of services. Later reforms drew lessons from these evaluations: more emphasis was put on personalised pathways, combining a variety of services and offering more choice (Nicaise, 2001; Mascherini, 2012). Before the crisis of 2008, the Nordic youth guarantee schemes proved to be very successful with unemployed young people participating in the scheme managing to find a job quicker than older people. During the economic crisis, the public employment services had difficulties in delivering the promised servicing within the time frames. The workload of many counselling services became almost unmanageable. However, they are performing significantly better now as the demand for their services has started to slow down recently (Mascherini, 2012).

Equally importantly, economic cost-benefit estimates of guarantee schemes for the long-term unemployed showed that in smart employment guarantee schemes (i.e. work experience combined with training and personal counselling), the initial additional cost for the government is recovered within 3-4 years through economies on unemployment benefits and increased tax and social security revenues. The *social* cost-benefit balance (which takes into account costs and benefits for all stakeholders) turns out positive after 2-3 years, even if leakages such as dropout, deadweight and substitution effects are taken into account (Layard and Philpott, 1997; Nicaise, 1999).

3.4. LIMITATIONS OF THE EU'S SOCIAL INVESTMENT PACKAGE

Overall, the Social Investment Package can be seen as a milestone in the evolution of European welfare states. Hemerijck (2013) considers social investment as a new paradigm in social policy, with the emphasis shifting from "compensating income equality" (Rawls) towards "capacitating fairness" (Sen/Dworkin). Although trajectories diverge between countries, the global financial crisis appears to spur reforms into the same direction.

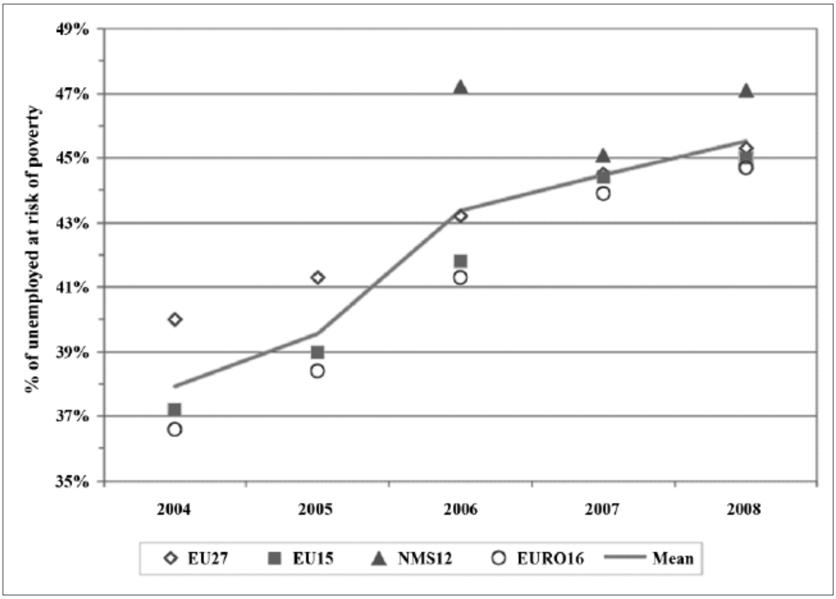
For the time being, admittedly, the shift in emphasis is observable in the policy rhetoric rather than in the effective policy making which is reflected in the allocation of budgets. The EU itself disposes of a budget which is so marginal (1% of its GDP) that it can in no way finance the advocated social investment package on its own. Nor can the Union exert any pressure on Member States in the area of social expenditure, due to the subsidiarity principle. The chances of a genuine paradigm shift will therefore depend on the extent that member states can be convinced by the new discourse.

Our three 'case studies' in the previous subsections suggest that economic and social objectives may converge in practice, provided that social policies are conceived in a more efficient and proactive way. Whether the analysis can be generalised to other policy areas such as health, housing, family policy, elderly care… also remains to be demonstrated. Yet, some other major issues relating to the social investment agenda have barely been addressed in the EU's documents on the Social Investment Package.

3.4.1. Social protection: investment or not?

A first weakness of the Social Investment Package relates to the vision underpinning social protection, which is most visible in the background document 'Staff Working Document on demographic and social trends' (EC, 2013c). It is to some extent understandable that social transfers are not commonly seen as investments, because their role is to compensate victims of realised social risks, whereas social investments are mainly supposed to prevent such risks. Nevertheless, in our view, the dividing line between compensation and prevention is often not clear-cut. Social benefits also serve to enable beneficiaries to keep investing in themselves and their families. Our feeling is that in the Commission underestimates the latter role in the documents relative to the Social Investment Package. The Staff Working Document mentioned above clearly sticks to the 'making work pay' paradigm as it continuously refers to the dilemma between generosity and work (dis)incentives of benefit systems: indeed, the making-work-pay paradigm prescribes low levels of benefit and strict conditionality rules in order to safeguard incentives to take up work.[9] The social investment view, on the contrary, advocates generous benefits in order to sustain investments in the beneficiaries' health, human capital, family and social participation. The dominance of the (neoliberal) 'making work pay' paradigm, reflected in strong public concern about financial work (dis)incentives, has undoubtedly weakened the support for redistribution through social security in general, and unemployment benefits in particular. This explains why the latter have been systematically eroded in the past decade(s), resulting in increasing poverty rates among the unemployed.

FIGURE 6: TRENDS IN FINANCIAL POVERTY (AROP) RATES AMONG UNEMPLOYED PERSONS



Source: Cantillon, 2011.

(9) According to the making-work-pay paradigm, while admittedly the risk of losing one's job is exogenous, the duration of non-employment is treated as the result of a rational choice process between leisure and income, with people getting stuck in inactivity if the income difference between work and non-work is not large enough.

Yet, the empirical basis for the 'making work pay' approach remains weak. The 2012 as well as 2013 issues of the European Commission's 'Employment and social developments in the EU' reports provide interesting empirical evidence as well as references to the literature, showing that receipt, duration, and generosity of benefits have no clear-cut effect (and indeed sometimes a positive effect) on the probability of getting back into work (EC, 2012b; EC, 2014, Chapter 2). This can be explained by another role of social benefits, namely, allowing individuals to invest in their employability (through expenditures on mobility, training, social participation). The social investment perspective on social protection therefore prescribes decent benefits, combined with supporting services enhancing the employability of the individual. Curiously, the Social Investment Package does not seem to have fully integrated these lessons.

3.4.2. Social investment in a context of social dumping?

Promoting social investments as a key element of an alternative macro-economic strategy appears unfeasible in a climate of excessive intra-EU competition, which actually leads to social dumping. The need for *social minimum standards* was put on the agenda by social movements across the EU as a response to the liberalisation of the public services such as telecom, energy, public transport – and, more importantly, social services such as child care, elderly care, labour market re-integration, etc. As the EU's liberalisation policy went in pair with privatisation, competition and commercialisation, there was a great fear that this would result in low-quality services, social dumping and exclusion of vulnerable clients. Under the EU's Services Directive, any kind of government intervention, through price setting, quality regulation or subsidisation was in principle considered as a market distortion and needed to be justified 'from scratch' or suppressed. Following strong protest from the public and non-profit sectors, the European Commission developed a 'Quality framework for services of general interest' in order to safeguard the highly regulated and subsidised (initial) education, social and health care sectors from commercialisation (EC, 2011).

A related aspect of the social minimum standards agenda concerns the introduction/strengthening of guaranteed minimum income (GMI) schemes (and minimum wages) across the EU. The objective would be to lift minimum benefits to the at-risk-of-poverty threshold (60% of the equivalised median disposable income) by 2020 (Van Lancker, 2010 – on behalf of EAPN). An *EU framework directive on minimum income* has been advocated for several reasons:

- the arguments relating to equity and human dignity are the most obvious ones, bearing in mind Art.137 (fight against social exclusion) and the inclusion of the right to social assistance in the European Treaty, as well as the 2008 Recommendation on Active Inclusion;

- from an economic perspective, more generous GMI schemes can be expected (a) to support consumption demand and (b) to put a break on social dumping, particularly in the services sector. The productive role of social protection and minimum income (c) in preventing long-term social damage such as ill-health and social tensions should also be recognised;
- in sum, it is clear that harmonised minimum income schemes will yield economic as well as social benefits.

The budgetary cost of EAPN's proposal was estimated by Cantillon et al. (2014) at 82 billion EUR.[10] This is less than 1% of the EU's GDP; and the 'burden' of the operation would obviously be shared between governments and employers (as minimum wages would need to rise as well). By way of comparison, the cost of the first wave of bank bailouts in 2008 and 2009 costed the European economies 36 times that amount (2.99 trillion EUR). Admittedly, the cost of a minimum income guarantee could turn out relatively higher in countries where the present schemes are weakly developed. Some form of European redistribution mechanism would therefore be useful to support the weaker Member States in implementing the scheme.

A boundary condition for increasing minimum benefits is of course the necessity to maintain some tension between minimum wages and benefits. Vandenbroucke et al. (2012) calculated that the Europe-wide introduction of a minimum income equal to 60% of national median equivalent income could create a financial inactivity trap in at least eleven EU Member States. Therefore, the proponents of co-ordinated EU-wide GMI policies also propose to set appropriate standards for minimum wages. Admittedly, the problem is that minimum wages are not designed to address specific family situations or specific employment conditions, such as part-time work. Actually, minimum wages are not sufficiently targeted as a direct anti-poverty tool (OECD, 2009). However, a co-ordinated minimum wage policy might prevent further damage from competitive wage dumping within the EU and thus also have a beneficial indirect effect on poverty.

3.4.3. Financing social investments

Perhaps the largest gap in the Social Investment Package is that the Commission does not seem to take an explicit position as regards potential budgetary implications. Although references to 'selectivity' in the document may raise some suspicion among social organisations about further cuts in social spending, the intention is not to make existing provision more selective - rather to extend it selectively. On the other hand, the Commission does not make any statement about financing of this extension either. This is cautious but leaves a critical issue unsettled. All in all, the

(10) Estimate for 2008.

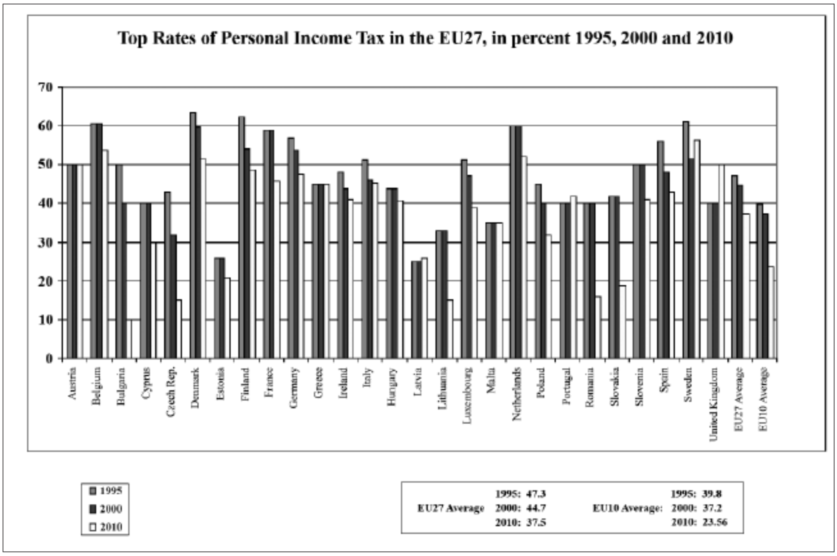
document misses an overall strategic view on how to actively promote social investment amidst the crisis. Yet it is obvious that, if the EU wants to make a 'qualitative leap forward', this will inevitably require additional funding in the short run. It would be more courageous to state explicitly that additional government revenues are needed, and to examine the opportunities to raise taxes selectively on high-income groups, on wealth, transnational corporations, financial speculation etc.

The EuroMemo(random) Group is more explicit on these issues. This group of 350 economists and social scientists advocates an alternative fiscal policy for the EU, focussed on equity and the fight against unemployment rather than austerity. Key prescriptions of the EuroMemo Group include:

- a proper EU fiscal policy margin in the order of 10% (instead of the present 1%), aimed at combating unemployment, conducting an industrial policy and redistributing between rich and poor regions in the EU;
- a requirement for surplus countries (such as Germany) to expand demand;
- alternative labour market policies based on redistribution of work (through shorter work weeks) and investment in skills instead of wage competition;
- the power for the European Central bank to issue euro-bonds in order to finance major investment programmes;
- strict regulation of investment banks, hedge funds and private equity funds, and establishment of a public European rating agency; generalisation of the financial transaction tax;
- above all, breaking the downward spiral of tax competition through harmonisation of national tax policies, restoration of progressive taxation, strengthening of taxes on wealth, and elimination of tax havens (EuroMemo Group, 2013).

According to the EuroMemo Group, a key precondition for improving the fiscal health of the European Member States is to establish, through regional and international agreements, clear principles of fair taxation. Such an agreement would involve the elimination of so-called 'tax havens', the prevention of destructive tax competition, a standardised tax base for corporations and non-incorporated companies and the reestablishment of effective systems of progressive taxation (EuroMemo Group, 2010). The erosion of the progressiveness of income taxes in the EU in recent years is illustrated by Figure 6 below.

FIGURE 7: EROSION OF PROGRESSIVENESS OF PERSONAL INCOME TAXES IN THE EU, 1995-2010



Source: Eurostat, Taxation trends in the EU.

Although the EuroMemo agenda looks radically different from present macro-economic policies in the EU, it is certainly coherent, scientifically sound and compatible with monetary consolidation. The main difference with current EU policies is its balance between social and economic objectives. Europe is capable of funding a generous welfare system and investing in social progress, provided that unfair fiscal competition is stopped.

The OECD also favours tax reforms that increase the average rate of tax paid by top earners. Possibilities include aligning the taxation of owner-occupied residential property more closely to actual market values and returns, while also applying a progressive rate structure to those returns. Another option is to abolish or scale back a wide range of tax expenditures which tend to benefit high income recipients disproportionately (OECD, 2011a). The additional proceeds resulting from these tax reforms could be used to reconcile a balanced budget with increased social investments.

Other stakeholders also focussed on the need to change the fiscal regulations within the EU. The European Federation of Public Service Unions (EPSU) launched a campaign against tax fraud and avoidance in the EU. They criticize certain EU Member States for suppressing jobs in tax services instead of being tougher on tax dodging and investing in tax services that bring in much revenue. The union refers to the fact that each year 1 trillion euro of public revenues are lost in tax fraud, which is illegal, and tax avoidance, which may not be illegal but nevertheless is unacceptable. Closing the tax gap between what governments expect to raise and what they do raise, is essential to tackle public deficits. Hence, it is vital to invest more into tax administration because it more than pays for itself and will combat tax evasion directly (EPSU, 2013b). Note that the estimated loss of 1 trillion EUR is equivalent to 7.5 times the poverty gap in the EU (i.e. the budget cost of the establishment of EU-wide GMI schemes as explained above).

Another popular demand with respect to fiscal measures was the introduction of a generalised financial transaction tax. The levy is designed to prevent a repeat of the conditions that stoked the credit crunch. In the mean time, the European Commission agreed to this idea by proposing the creation of such a tax at EU level. In line with its proposal, the proceeds of such a tax could be used to finance growth enhancing investments (European Commission, 2012d). The EU's effort to introduce a tax on financial transactions was given new life recently. Concretely, Germany, France, Belgium and eight other Eurozone countries have been given the green light to impose the financial transaction tax, using the 'enhanced co-operation' mechanism that allows groups of EU countries to move forward without the agreement of all 27 members. It is expected that the levy could raise as much as 35 billion EUR a year for the 11 countries. Following go ahead for the EU Finance Ministers, the levy could be introduced within months (Inman,2013).

EAPN furthermore criticized that the 2007-2013 *Structural Funds* have fallen far short of their potential to promote social inclusion. In particular, the network criticized the way the 2007-2013 Structural Funds have been implemented. A non-satisfactory involvement of social inclusion NGOs in monitoring is considered to be one of the main reasons for this deficit. As a result, EAPN created a toolkit in order to help social NGOs to prioritise the new social targets of Europe 2020, and especially the poverty reduction target. Given their knowledge of the needs of the most vulnerable groups of people and how to reach them, social NGOs should participate in all stages of the processes of Structural Funds (preparation, implementation, monitoring and evaluation) (EAPN, 2012). Meanwhile, as mentioned earlier, the Commission decided to introduce a double quota system for the period 2014-2020, with at least 25% of the resources being dedicated to social investments and at least 20% of the ESF funding to the fight against poverty.

3.4.4. The redistributive effect of social investments

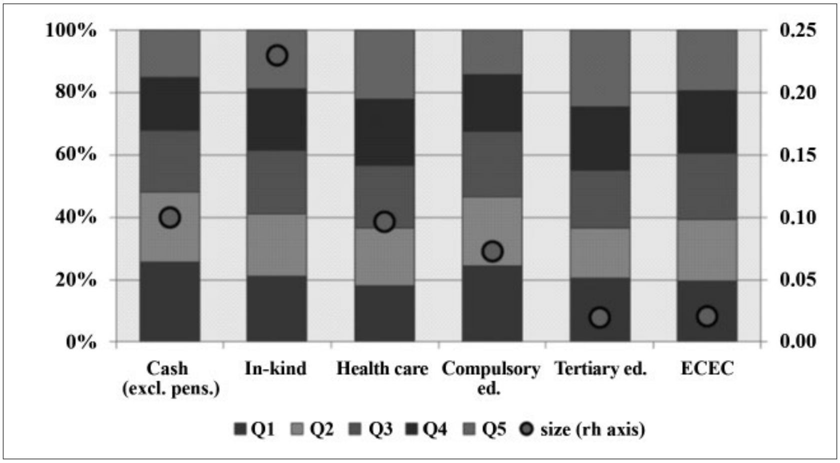
A fourth problem with social investments relates to their limited effectiveness in the fight against poverty. In this context, Cantillon (2011) refers to the 'paradox of the social investment state': in the past decades, social investments have gradually absorbed a greater share of public expenditure, partly at the expense of social security cash transfers. Whereas social benefits were increasingly targeted at the lower income groups, social investments (in education, health care, public housing and child care) kept suffering from severe Mathew effects. According to Cantillon, this explains – at least, partly – why the efforts to reduce poverty in the EU failed to produce any substantial impact on the poverty risk.

Verbist and Matsaganis (2014) qualify this picture. On the basis of a detailed analysis of the use of various types of social services among the non-elderly population, they conclude that the overall volume of social investments in EU countries appears to be distributed more or less equally across all welfare quintiles of the population (see Figure 7).[11] Compulsory education tends to redistribute resources towards the lowest quintile, whereas tertiary education and health care are used disproportionately by the upper quintiles. More surprisingly, Verbist and Matsaganis also find that the poverty-reducing effect of social services (-15 percentage points at EU-level) is much larger than that of cash transfers (-8 percentage points). However, this is due to the higher aggregate value of social services, rather than their redistributive impact per se: in other words, each euro spent on cash transfers has a stronger pro-poor effect than a euro spent on services.

All in all, this means that the shifting emphasis towards social investments necessitates simultaneous efforts to target them at disadvantaged groups better than in the past. Without such accompanying efforts, Cantillon's criticism that the new paradigm may fail to reduce poverty remains valid. The present strong variation in pro-poor effectiveness between national systems of social services shows that there is a wide margin for improvement.

(11) See Verbist and Matsaganis (2014) for a precise definition of 'welfare quintiles'. The criterion used is disposable equivalent household income, where the equivalence scales have been corrected to account for differences in economies of scale between cash income and the take-up of public services.

FIGURE 8: DISTRIBUTION OF VARIOUS TYPES OF SOCIAL EXPENDITURE ACROSS THE POPULATION, BY WELFARE QUINTILE



Source: Verbist and Matsaganis, 2014.

CONCLUSION

The ongoing financial and economic crisis has taken a high social toll on Europe's citizens. Paradoxically, the poverty impact is hard to assess precisely. In relative terms, the number of Europeans at risk of poverty or social exclusion has increased by 6.5 million between 2008 and 2012. However, using 'anchored' poverty thresholds, this number may well be twice as high. Traditional parameters such as a rising (youth) unemployment rate and an erosion of the income level also clearly demonstrate the detrimental impact of the crisis on the social situation of many Europeans. Apart from its impact on income and unemployment, the economic downturn also strongly affected social ties and psychological well-being – particularly in the peripheral regions of the EU.

In order to tackle the negative effects of the crisis, the EU authorities developed a fiscal consolidation strategy with a tight control over the budgetary policies of the Member States. Meanwhile, it has become clear that the deflationary effects of the (imposed) austerity measures actually tend to aggravate the impact of the crisis. The lack of co-ordinated budgetary policy in the EU furthermore hindered an effective macroeconomic response to the recession. Instead, it led to the use of non-cooperative strategies among the Member States, such as competitive wage reductions, social dumping and fiscal competition. Whereas the majority of EU citizens may be affected, there are indications of particularly harmful effects on the poorest. Despite strong pledges of the European Commission, there seems to be a glaring lack of political will to carry out ex-ante as well as ex-post social impact assessments of anti-crisis policies.

While the EU is still following the same austerity line,[12] a consensus seems to emerge among a number of European stakeholders about the necessity of re-orienting the current strategy in favour of renewed social investments. This strategy covers a wide range of areas and may benefit the entire population, but it is particularly relevant for the poorest segments of society who have traditionally survived on social benefits. Investments in the fight against child poverty, in education and training and in active labour market policies (youth guarantee schemes in particular) were taken as examples of such social investments. By strengthening the capabilities of excluded people, such investments may produce lasting social inclusion effects and may indeed break the inter-generational cycle of poverty.

However, if the EC's ambition is to promote the Social Investment Package (SIP) as a key element of its macroeconomic policies, some conditions need to be met. The main challenge undoubtedly relates to the financing issues. Without additional resources, it is improbable that the package will produce any substantial impetus in the short run. Hence, continued efforts to extend and co-ordinate tax policies at the EU level are indispensable. The introduction of the tax on financial transactions (FTT) could be a hope-giving step forward in this respect.

Secondly, the EC's discourse about social protection remains rather ambiguous. The SIP documents still refer extensively to the problem of work incentives and thus appears to be strongly rooted in the 'making work pay' logic, which is the opposite of the social investement approach. Other EC documents have more clearly embraced the latter approach, emphasising the positive effects of generous protection combined with reintegration services.

Thirdly, it would be very hard to implement a large-scale social investment agenda in a climate of fiscal and social dumping. For this reason, a solid framework of social minimum standards needs to be (further) developed. In this context, the EU's Quality Framework for services of general interest is definitely a step forward, but its impact will be constrained a priori to these services, whereas social dumping is a pervasive mechanism affecting all sectors of the economy. EAPN's claim for an EU framework directive on guaranteed minimum income-schemes (GMI) should also be taken more seriously, not just for its direct relevance in the fight against poverty, but also for its beneficial role in correcting markets. It should moreover be accompanied with similar measures in relation to minimum wages. Although this may be

(12) Hemerijck (2013) argues in this regard: 'unlearning is the most difficult part of policy learning'.

hard to achieve overnight, a co-ordinated set of GMI- and minimum wage schemes will produce ‘automatic stabiliser’ effects on consumption demand and put a break on social dumping.

Fourthly, Member States still need to go a long way to achieve a better distribution of their social investments across various sections of society. At present, this distribution appears to be ‘neutral’ on average: i.e. the poorest do not benefit more than any other group in society from social investments. A stronger redistribution effect can be achieved through gradual implementation of the principle of ‘progressive universalism’: this means that, while the access to public services remains universal, positive action should be taken in favour of target groups with the highest needs through a combination of outreaching, sensitization, as well as preferential access and treatment.

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