

Chapter 8 Employment relations, welfare and politics

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INTRODUCTION

The employment relationship and the welfare state are intricately linked.¹ Formal employment is the welfare state's main source of funding. The main share of income taxes derives from formal employment and in many countries the welfare state is funded by additional pay-roll taxes. Entitlements to social transfers as well social insurances are tied to formal employment relationships. In particular, pension schemes and unemployment insurance schemes are generally designed for employees rather than for all citizens. In turn, the welfare state shapes the labour market by providing employees with different kinds of skills, education and protection. The level of transfer payments, their conditionality on length of employment and job seeking behaviour influence the way individuals are integrated in the labour market. If transfer payments are too high, labour market participation might be low; if they are too low, investments in skills might go down because individuals may not be able to bear the costs of training. Social policies and labour market policies are all centred around the way private business hire, train and employ staff.

During the golden years of welfare state development, employment and welfare had reached a high level of functional and normative integration which was additionally linked by family patterns (Hassel 1999). Each segment was closely tied and complemented, leading to a highly integrated framework. The gender division defined the complementary link between family and employment, the employment based funding of social protection characterised the link between

¹ I would like to thank Bettina Wagner for superb research assistance and the editors for very helpful comments. All remaining errors are mine.

employment and welfare and population growth and birth rates were the basis on which the link between welfare and the family was defined. The social model of post-war employment was based on a family with one permanently employed breadwinner, whose employment generated income for the whole family and also accumulated sufficient funds for social protection and welfare expenditures. Today, the relationship between welfare and employment faces fundamental challenges from changes in family and employment patterns as well as the fiscal crisis of the state. Decreasing wage levels, combined with growing job insecurity, no longer allows for traditional, one breadwinner, family models. Increased female employment undermines the traditional division of labour within families. Persisting high levels of unemployment and underemployment put pressure on social security budgets and unemployment funds. Social spending however remains at high levels. Almost all advanced industrialized countries face a fiscal crisis.

There has long been a debate whether the welfare state is a precondition or a burden for the success of business. There is a clear correlation between the size of the welfare state and the wealth of a nation. While some assume the welfare state's expansion occurred as nations grew wealthier and were able to afford extensive social insurance programmes (Alber 1980), others maintain that the modern social insurance system provided a foundation for the economic growth of the 20th century. Both processes therefore feed each other: investing in education and social services facilitate skills, which in turn maintain innovation and competitiveness. Crucial questions are how much social protection does a family need in order to invest in the skills needed by a modern economy? And how much social spending can a modern government afford in the light of the current fiscal crisis?

However, experiences between countries are mixed; and there is no one way to organize the labour market or the welfare state. Labour market institutions, such

as employment protection legislation and collective bargaining structures as well as social protection schemes of the welfare state are subject to long-term historical and path-dependent developments under intense political contestation, countries have developed their very individual configurations of regulations, provisions and institutions. The variety of combinations of different labour market institutions and welfare state types have developed complementarities and interdependencies and in general been stable over time.

At the same time, advanced industrialized countries all face similar challenges: globalization, the rise of the service economy, feminization and dualization are phenomenon that can be found in the majority of countries. The relationship between employment and welfare is characterized by parallel processes of adjustment in many countries under very different local settings. During the last decades, welfare provisions have been restructured in many countries in order to provide sufficient incentives to take up employment. Labour market policies have encouraged greater levels of flexibility. This has been accompanied by increasing divisions between labour market insiders and outsiders.

VARIETIES OF WELFARE REGIMES AND THE EMPLOYMENT RELATIONSHIP

Cross-country comparisons between industrialized countries have highlighted significant differences in welfare and employment regimes. In some countries, employment is flexible and fluid; there are few rules to be followed when hiring and firing and people move between jobs frequently. In other countries, employment is far more rule-bound and rigid.

One way to classify the flexibility of labour markets is the employment protection index produced by the OECD.² It covers three different aspects of employment protection: Individual dismissal of workers with regular contracts; additional costs for collective dismissals and the regulation of temporary contracts. For each of these aspects several indicators are used. For example, individual dismissal of workers with regular contracts incorporates three aspects of dismissal protection: (i) procedural inconveniences that employers face when starting the dismissal process, such as notification and consultation requirements; (ii) notice periods and severance pay, which typically vary by tenure of the employee; and (iii) difficulty of dismissal, as determined by the circumstances in which it is possible to dismiss workers, as well as the repercussions for the employer if a dismissal is found to be unfair (such as compensation and reinstatement). Based on these indicators an index ranging from 0 to 4 is constructed. The United States has the most flexible labour market among the OECD countries whereas employment protection is strongest in Turkey.

Strong employment protection often goes hand in hand with representation of trade unions within firms. Employers need to have valid reasons to make employees redundant and must consult trade unions or elected representatives of their employees. Protection and trade union representation require a far greater deal of negotiation but also cooperation between management and employees in order to remain competitive. Union representation and employment regulation have a profound effect on work organization, innovation patterns and productivity. Comparative studies on production regimes have long established that cooperative workplace relations are related to higher degrees of functional flexibility and productivity (Maurice, Sellier and Silvestre 1986). The decline of

²<http://www.oecd.org/employment/employmentpoliciesanddata/oecdindicatorsofemploymentprotection.htm>

British and US American manufacturing industries is in part due to hostile relations between management and employees at the plant level.

These differences between employment relationships in different countries correspond to big differences in welfare regimes. Again, the extent to and the way in which governments protect their citizens from economic hardship varies substantially. For instance, government expenditure for social protection in 2009 ranged from 9% of GDP in the United States to 25% in Denmark.³ The understanding of social risks and the responsibility of government to cover these risks can take many forms: In some countries risks are defined in a minimalist way and in some cases not seen as risks at all. For instance, in the United States unemployment and old age risks are only minimally covered by government schemes. On the other hand, the awareness of social risks in Europe is very high and politically salient.

Moreover, social risks can be insured by both the state and the individual. In the US the private insurance of risks is supported through tax credits, which does not take the form of direct spending. Finally, there is also a very different understanding of the role of the state for delivering social services. In particular, in Scandinavian countries welfare provisions include extensive childcare and training services, which are part of the welfare state in other countries.

Both, employment relations and welfare regimes are not only characterized by national variety and difference but also systematically linked. For the understanding of these systematic linkages, we can draw on two main academic approaches.

³ OECD Data Set National Accounts at a Glance 2011. data extracted on 30 May 2012 20:12 UTC (GMT) from OECD.Stat.

Welfare Capitalism

In Gosta Esping-Andersen's seminal studies on the worlds of Welfare Capitalism, three welfare regimes were identified (Esping-Andersen, 1990).⁴ Welfare regimes were classified by the level of 'decommodification', which describes the "degree to which individuals, or families, can uphold a socially acceptable standard of living independently of market participation" (Esping-Andersen 1990:37).

Decommodification is strongest in the social-democratic regime with universal provision of a wide range of entitlements. Social-democratic welfare states were designed to secure high standards for all, not just to support those in need. Their political project was equality between the classes. Status differences between blue collar and white collar workers were eradicated within a universal insurance system, although benefits continued to be based on accustomed earnings. Exemplary cases are the Scandinavian countries of Sweden, Norway, Finland and Denmark. At the other end, a liberal welfare regime developed in the Anglo-Saxon countries and in other countries such as Switzerland. Here welfare provisions are minimal and means-tested, and the state encourages market solutions by subsidizing private welfare schemes; public schemes are universal but provisions are too low for maintaining the income levels that were achieved during employment.

Third, in conservative welfare states, social security is provided mainly by the state and the share of the market is minimal. Provisions and entitlements are, however, not as comprehensive as in the social-democratic welfare regime; the emphasis is not on equality but on the preservation of status differentials.

⁴ The approach has been criticized for its incompleteness regarding other basic factors for stratification such as race, gender. Other authors have proposed additions forms of welfare capitalism in order to include misfitting countries (Kangas 1994; Leibfried 1992).

Redistributive effects are therefore negligible. Conservative welfare states are primarily to be found on the European continent.

Many countries combine elements of different welfare regimes. The Danish welfare state combines both liberal and social –democratic elements. In the less wealthy countries of southern Europe, a mix of liberal and conservative elements can be found. Different combinations indicate different relative importance of conflicting goals in social security provision: equality, the maintenance of status differentials, and market reliance. In Italy for instance, employment protection is strong while social benefits are low.

Ultimately, however, three worlds of welfare capitalism depict different types of welfare regimes whose relevance do not lie in the ranking but in the contrast of different structures of welfare provision (Esping-Andersen 1990). The biggest difference between the social democratic and the conservative welfare state “lies not so much in their de-commodifying income- maintenance guarantees as in their approach to services and sponsoring women’s careers” (Esping-Andersen 1999:88).

Decommodification protects the individual from market fluctuations during the business cycle; unemployment will not decrease the living-standards as much, and old age is less of a social risk. However, decommodification comes in different forms. The labels ‘social democratic’ versus ‘conservative’ describe the distinction between the universal characters of the Nordic welfare state versus the ‘status-oriented’ nature of benefit provisions in the conservative states. The distinction between social democratic and conservative helps to understand welfare production regimes by pointing to the administrative logic of welfare provisions in countries with specific skills. A status oriented welfare state provides special benefits to particular groups of employees, particularly employees in the manufacturing sector with very specific sets of skills. The insurance based nature of the benefit system ensures via its ‘equivalence-

principle' that benefits are tightly coupled to contributions. Social democratic welfare regimes, such as the Nordic countries provide services and insurance for coping with change. Rather maintaining the status of individuals they assist in changing a status. While social spending might be as high or even higher in social democratic welfare regimes, the focus is not on the protection of a particular job but on the income level of a household.

Welfare production regime

The second approach is based on the concept “welfare production regime” (WPR) introduced by Estevez-Abe et al. (2001). Welfare production regimes aim to capture the ways in which social protection regimes, skills regimes, and production regimes are interconnected. As Estevez-Abe et al. put it, “welfare production regimes are the set of product market strategies, employee skill trajectories, and social, economic, and political institutions that support them” (ibid:146).

Starting point of the welfare production regime literature is the idea of different business systems or varieties of capitalism (VoC). Hall and Soskice (2001) distinguish between two opposing forms of production regimes: coordinated market economies (CMEs) and liberal market economies (LMEs). They can be distinguished based on five spheres and their respective attributes. They relate the workings of national institutions with firms' behaviour. The first sphere is the level of *industrial relations* where the working conditions as well as the wage level are coordinated by companies in cooperation with labour, labour unions as well as other employers. Industrial relations can be either highly centralized and organized, as in many European countries, or highly decentralized as in many Anglo-American countries. *Vocational training and education* is the second sphere in which companies contribute on the production

of either specific or general skills of their workers which in turn shapes their production strategies. The *corporate governance* sphere determines the ability of firms to draw on patient capital. The fourth sphere refers to the *inter-firm relations*, in which standards regarding technology and supplier relations are organized. The fifth sphere is the relationship with the *employees* and coordination with regard to the employees' commitment and work motivation within the firm (Hall and Soskice 2001:6). Based on these five distinguishing spheres and their respective indicators, a distinction between two types of production regimes is possible.

The VoC literature contrasts the working of liberal market economies (LME) based on market mechanisms for the coordination of economic actors with coordinated market economies (CME). CMEs are based on non-market mechanisms, such as organizational interaction and long-term relationships. The Nordic and Continental European countries are both classified as CMEs. In coordinated market economies, firms' product market strategies rely heavily on the availability of specific skills. Specific skills are those skills that can only be used in a particular firm or industry and cannot easily be transferred. General skills can be used in any context. In order to protect their investment in specific skills, workers demand social insurance policies that protect these skill investments, such as employment protection, job specific unemployment insurance and earnings-related pensions. Firms then pursue product market strategies based on incremental innovation or "diversified quality production" (Streeck 1991) because of the abundance of specific skills. According to this logic, skilled workers will join with manufacturing employers in supporting social protection and training policies that support this high skill equilibrium.

Key institutions in this perspective are those institutions which protect the acquisition of specific skills, either through high degrees of employment protection (dismissal protection) or specific welfare provisions for groups of

skilled employees. Highly specific skills are correlated with more welfare provisions aimed at protecting these skills and with less flexible labour markets. Demands by specifically skilled workers in manufacturing industries have led to specifically designed welfare programmes, as well as to relatively strong employment protection legislation. The strong focus on protecting specific skills has led to the adoption of systems, which – in contrast to the Nordic countries – did not ask skilled workers to change their skill sets, but rather promised life-long earning-related benefits in case of unemployment with no obligation or expectation to acquire new skills or move to new occupations.

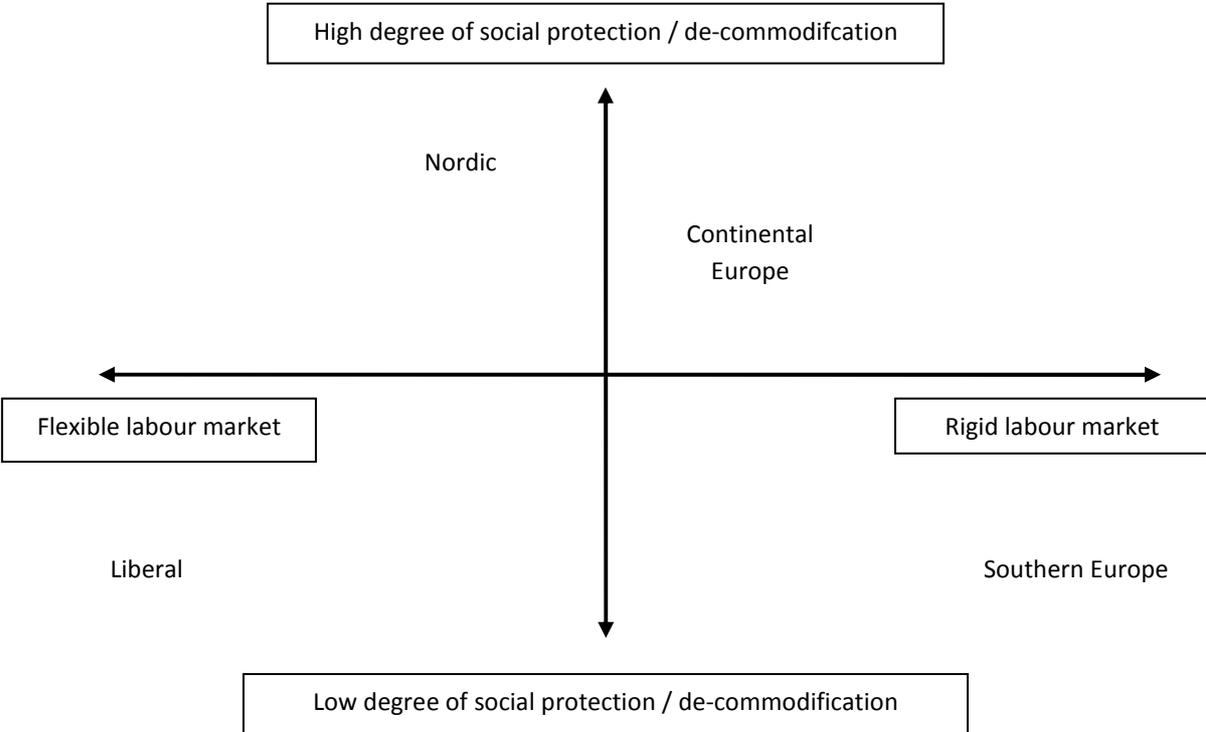
In countries with more general skill sets, the demand for skill-specific social protection is lower and programmes are more employment friendly in nature. In both liberal and Nordic countries, the benefits focus much more on moving unemployed workers into new employment rather than protecting their acquired skills. This is closely related to the training system of some of the Continental European countries, in which companies invest highly in initial skill sets (Anderson and Hassel 2013).

Four models of employment and welfare regimes

The combination of the two theoretical perspectives – one based on welfare decommodification and the other on the production regime – can be used as two axes for classifying countries in the way they link welfare and employment (Graph 1). While the liberal countries score high on the degree of labour market flexibility compared to Continental and southern Europe. The Nordic and Continental European countries score considerably higher with regard to the degree of social protection / decommodification compared to both liberal and southern European welfare states. Both country groups are similar with regard to income maintenance.

In this perspective, countries are situated on a continuum of flexibility of labour markets and the character of the benefit system under the assumption that these two categories correspond.⁵ In liberal countries with education systems that focus on school based rather than vocational education, the regulation of labour markets is loose and benefits are aimed towards high employment levels.. The group of coordinated market economies is broken up into three different groups: the Nordic countries are closest to the liberal model with regard to the measure of the benefit system’s universality and the degree of flexibility in the labour market. In comparison, Continental European and southern European countries have more strongly regulated labour markets. Southern Europe combines a strongly regulated labour market with a meagre welfare regime. Employment protection often takes the place of social security as income maintenance is guaranteed with a permanent job.

Graph 1: Degree of social protection by type of welfare production regime



⁵ This conceptualization therefore moves away from the standard assumption of the VoC literature, which is organized around two poles.

An important implication of this approach is that it removes the traditional stark contrast between liberal and Nordic models and puts both groups of countries on the same level. Both models are similar not only regarding employment levels and the role of women in the labour market, but also in terms of education levels and the importance of general skills. The Nordic countries are closer to the Anglo-Saxon world than to their Continental European counterparts.

Critics might take issue with the notion of the Nordic countries as being more flexible in terms of labour market regulations. Standard measures of employment protection for regular employment (EPL) by the OECD give most of the Nordic countries (with the exception of Denmark) a similar score compared to standard Continental European countries (see Table 1). Scholars of the region frequently disagree with the notion of labour market flexibility as a Nordic trait.

However, the practice in the Nordic countries prefers activation over preservation as high employment rates are a precondition for high taxation. Though all CMEs are characterized by high social spending, countries with strong Social Democratic incumbency differentiate themselves with regards to the employment-friendly nature of their social policies (Huo, Nelson and Stephens 2008). As a case in point, Social Democratic welfare state regimes are characterized by high spending on active labour market policies and generous short term unemployment replacement rates, which relate to higher employment levels (Bradley and Stephens 2007); Christian Democratic states, in contrast, demonstrate strong employment protection, high social security taxes, and generous long-term unemployment replacement rates, which relate to lower employment levels (Bradley and Stephens 2007). In Sweden, the Rehn-Meidner model recognised in the 1950s that workers benefit from mobility between jobs rather than fighting for the stability of existing workplaces. Therefore, active

labour market policies were combined with early investment in education, good child care facilities, centralised wage bargaining and a large public sector. Today, Denmark excels at achieving high growth rates, high employment levels, high levels of labour turn-over and high degrees of worker mobility.

This also becomes apparent when looking at job tenure rates. Tenure rates in the Nordic countries are considerably shorter than in Continental European countries and fall exactly between the high turn-over rates of liberal market economies and the substantially lower rates of Continental Europe (Table 1).

To depict the Nordic countries as in between those of Continental Europe and those of more liberal economies has important implications in judging reform movements. A movement towards the Nordic model by the Continental European countries is, at the same time, a move towards liberalization. In other words: approaching the Nordic model from a Continental European viewpoint would entail a dose of liberalization, even if policy-makers have a ‘social-democratic’ model in mind.

In this perspective, countries are situated on a continuum of flexibility of labour markets and the generosity of the benefit system under the assumption that these two categories correspond. In liberal countries with general education systems, the regulation of labour markets is loose and benefits are aimed towards high employment levels. The group of coordinated market economies is broken up into three different groups: the Nordic countries are closest to the liberal model with regard to the measure of the benefit system’s universality and the degree of flexibility in the labour market. The other two groups, the Continental European and southern European have, in comparison, more strongly regulated labour markets and an increasingly inactivity prone benefit system.⁶

⁶ Anderson and Hassel (2013) propose a similar typology based on training regimes.

Table 1: Employment protection and social expenditure in four types of welfare regimes

	Employment Protection Index	Government expenditure for social protection (% of GDP)	Average Job Tenure (in Years)*
LME	1.12	14.52	9.93
Nordic	2.23	22.57	10.00
Continental	2.71	20.62	11.54
Southern Europe	2.88	17.9	12.56

*Source: OECD Statistics, latest available year (2009/2010). Note: LME = UK, USA, New Zealand, Australia, Ireland, Canada; Nordic = Sweden, Denmark, Norway, Finland; Continental = Germany, Austria, Belgium, Netherlands, France; Southern = Portugal; Spain, Italy, Greece. *USA, New Zealand and Australia missing; Greece data for 2001.*

Mapping the advanced industrialized countries like this provides us with a set of important dimensions which are useful in assessing policy reforms and the trajectory of change. It also fits neatly in with the policy debate on ‘flexicurity’, as of now the most sophisticated policy approach that aims to combine change, flexibility and the protection of workers. Flexicurity has been discussed within the European Union for about the last decade and has in 2007 moved high onto the agenda of the European Commission.⁷ The European Commission described flexicurity as an optimal balance between labour market flexibility and security for employees against labour market risks.⁸ Rather than protecting jobs, the notion is now to protect people. Denmark, in particular, has been used as a case for flexicurity, but in this analysis the Nordic countries combine a comparatively high degree of flexibility in the labour market with a certain high degree of social protection, i.e. high levels and generous conditions of social benefits for the unemployed.

⁷ The concept was endorsed by the European Council of Ministers in December 2007 and has informed the discussion on revitalizing the Lisbon Agenda.

⁸ EU Commission: Employment in Europe Report 2006. Brussels.

POLITICS: POLITICAL INSTITUTIONS; CLASS STRUCTURES AND VOTING PATTERNS

Research on the relationship between voting behaviour and redistribute welfare policies starts from the assumption that the positioning of the median voter will affect the redistributive focus of governing parties. In general it was assumed that the lower the income of the median voter and the higher his exposure to risks, the more probable are redistributive policy programs of the governing party. However, voting results indicate that low-income workers in precarious labour situations are less likely to vote than high-income workers in more stable positions, leading to a distorted picture of the median voter (Lijphart 1997).

Political institutions play a major role when explaining differences in redistribution between countries. Iversen and Soskice (2006) claim that the electoral system has key influence on electoral support for redistribution. Electoral systems shape the electoral success of parties which are formed along socio-economic cleavages. Majoritarian electoral systems favour centre-right parties, which are against redistribution, whereas centre-left parties, generally in favour of redistribution, fare better under regimes based on proportional representation (Iversen and Soskice 2006).

Why countries have either majoritarian electoral systems or proportional representation can in turn be explained by different kinds of economic organization during key phases of democratization. Proportional representation was easier to implement in countries with locally organized skilled unions as it allowed for facilitated coordination and concomitantly preserve specific interests and build cross-class compromises (Iversen and Soskice 2006:383). Conversely majoritarian electoral regimes evolved when labour unions and their interest representation were feared (p.378). In consequence, government dominance was ensured through majority voting focusing on the median voter, independent of group-specific interests or needs.

Schneider and Soskice argue that in coordinated market economies economic institutions and consensus-based politics are complementary and were effectively a major tool for reducing inequality and reinforcing the strength and stability of a distributive welfare state. In contrast, liberal market economies characterized by competitive political systems based on majority voting, lead to welfare states based on minimal standards and higher levels of inequality (2009).

Political systems and economic institutions are complementary through the effects of partisanship and the nature of coalitions formed in order to take office (Iversen and Soskice 2006). The electoral system determines the strength of partisanship and government position of the government. Political systems characterised by proportional representation allow a variety of different groups access to the policy-making process and are hence generally biased towards centre-left governments. In political systems characterised by majoritarian voting rules, the competition over the middle-class votes usually leads to a bias to centre-right (Schneider and Soskice 2009:22). Similar to economic institutions, political systems turn out to be very stable over time. In sum, coordinated market economies are correlated to welfare regimes due to political and economic institutional factors. Business as well as wage bargaining are characterised by co-decision and involvement at all levels. Both capital and labour thus have a vested interest to politically contribute and decide over the egalitarian redistribution. In liberal market economies, the the middle-class voter is the key voter. This leads to a orientation of political parties to general provisions and minimum standards and less to protection of specific groups.

Based on this classification, we can now add to the notion of welfare capitalism and varieties of capitalism the role of political institutions (Schneider and Soskice 2009).

Table 2: System Classifications in OECD countries: Varieties of Capitalism, welfare states and political institutions

	Liberal (Anglo-Saxon): US, UK, Canada, Australia, New Zealand, Ireland	Coordinated (Northern European): Denmark, Finland, Norway, Sweden, Austria, Belgium, Netherlands, Germany, Switzerland
Variety of Capitalism (Hall and Soskice)	Liberal market economies	Coordinated market economies
Welfare State (Esping-Andersen)	Safety net	Insurance plus redistribution
Political System (Lijphart)	Majoritarian	Consensus (PR)

Source: Schneider and Soskice (2009:21)

The issue of redistribution is highly contested and again differs across government partisanship and countries. Facing the dilemma that democratic governments must respond to the needs and preferences of their citizens in order to be re-elected, the determinants of individual level support for income redistribution have to be taken into consideration. There are two different motivations behind individual support for income redistribution: the desire for equity (people aim at redistribution because of their own disadvantaged position) and the desire for insurance (individuals seek an insurance against risks) (Rehm 2007:48-49). The first motivation can either be based on purely egoistic grounds, or alternatively purely altruistic aiming for general equity in society.

The empirical evidence suggests that individuals with income above the national mean are less likely to be in favour of redistribution than individuals with income below the national mean (the difference is 7%) (Rehm 2007:60). The second is redistribution as a personal insurance against the risks of income

shocks (Rehm 2005:30). With regard to skill formation, the findings suggest that the more specific the skills of individuals, the more likely they are to support income redistribution (p.63). Women are more in favour of redistribution than men and support decreases as income increases, and self-employed are less in favour of redistribution than employees. The data confirms that both logics for redistribution are at play: “individuals are in favour of redistribution either because they are poor or because they expect to be poor in the future” (Rehm 2007:65). These findings support the claim that countries with strong specific skill-formation institutions have stronger welfare states (Esping-Andersen 1991).

WELFARE AND EMPLOYMENT REFORMS

The main challenge for welfare state politics is to keep pace with modernization i.e. to adapt policies that address new pressing problems in the globalized post-industrial society. As employment structures change, social programmes run the danger to spend resources on outdated risks (Häusermann 2010; Iversen 2005). Some of the most pressing changes and challenges as defined in the literature are the transition to the service economy, the pluralization of employment forms such as increasing rates of temporary and part-time work, the increasing flexibilization of labour markets, the increase of atypical and female employment, family instability as well as ageing.

In addition, fiscal constraints on the welfare state force governments to continuously adjust welfare programmes. The transition of the employment system from male and manufacturing based, to predominantly female and service sector based leads to a simultaneous process of declining resources and concomitant increasing financial needs. Therefore many countries have over the last two decades witnessed a process that aims to balance old with new social

risks. The process combines a simultaneous call for welfare state retrenchment with an expansion of welfare in response to the needs of new employment groups (Häusermann 2010:2; Pierson 2000).

The translation of economic and social changes into policy outputs is far from straightforward and is shaped by the interplay between structure institutions and actor's preferences and strategies. A number of factors shape this process: the level of multidimensionality of the policy issue, the degree of fragmentation of interest groups and political parties and the potential of conflicts. More fragmentation implies more flexibility and a greater degree of coalition formation and therefore implies change (Häusermann 2010). Governments formed by proportional representations, have managed to include more specific interests and enhancing welfare state politics based on a cross-class compromise (Cusack et al. 2010). Regarding employment two main reform patterns have emerged over the last two decades: activation and dualization.

Activation

Over the course of the post-war period, labour market participation changed radically. While the participation of women steadily raised, the employment rate of elderly workers, low skilled workers and men dropped. Particularly the recession following the 1970s oil shock led to a further fall in activity rates. In that context, most governments during the 1990s pursued a policy of activation i.e. increasing the rate of participation in the labour force (Bonoli 2010). In Anglo-Saxon liberal countries, activation strategies were based on incentivizing the unemployed into finding work by cutting welfare entitlements. In the rest of Western Europe, governments pursued mixed approaches which combined lower welfare payments, with positive incentives, sanctions but also training and

education measures. Those groups of unemployed who had dropped out of the labour market completely were the focus of activation measures.

As the pressure to find employment was tightened, the distinction between insurance based social protection and poverty relief measures was often blurred. In the past, unemployment benefit entitlements from social insurance aimed at securing a good standard of living for a certain period of time. These benefits were often seen as detrimental to incentivizing the unemployed to find work. Instead, flat rate and means tested benefits were introduced which were tightly coupled with the obligation of the individual to look for work. Welfare restructuring for the long-term unemployed and activation strategies were pioneered by the Clinton Administration in the USA, and then followed by the British Labour government, as well as the Netherlands, Germany and Denmark (Hassel and Schiller 2010).

Similarly, existing programmes on early retirement had led to declining employment rates among the elderly. These programmes were step by step dismantled during the last two decades and employment rates for the elderly as well as pension age generally increased. Moreover, pension entitlements from state pensions were generally cut (Ebbinghaus 2011a).

Dualization

Dualization denotes the process in which policies differentiate between rights, entitlements as well as services among different groups or categories of entitled citizens. The main distinction is between labour market insiders and outsiders. Labour market insiders are in a secure employment position, while those without

or insecure employment are labour market outsiders.⁹ In the process of restructuring the welfare state, both groups were treated differently.

There are three different forms of dualization: an increase of prevalent institutional dualisms through an acceleration of the differential treatment of insiders and outsiders, an expansion of the prior institutional dualisms by shifting parts of the insiders to the group of outsiders, and finally the development of new institutional dualisms (Emmenegger et al. 2012:10).

‘New’ and non-traditional groups entering the labour market such as women, young employees or migrants are particularly at risk of being clustered to the outsider group as their probability of entering stable and skilled standard employment relationships is by trend smaller than for older men (Mcdowell et al. 2012; Barbieri and Scherer 2009). This directly links to the increased visibility of dualization processes in society. Whereas until the 1970s, the precarious situation of women was not visible on the political level, as family and marriage policies provided protection, the last decades have increasingly politicized this problem. The same also counts for the outsider group of immigrant workers (Emmenegger and Careja 2012) who are considered the overrepresented group in non-standard, precarious working conditions (ibid. 2012:128; Kalleberg 2009).

Increasing institutional dualization can also be explained by looking at the median voter. As employed insiders shape the preferences of the median voter, the support for insider – oriented dualization- maintaining policies also increases. If as a consequence insiders perceive that political parties enhance outsider-oriented welfare policies, they risk being dropped (Lindvall and Rueda 2012:279). Dualization is not a completely new phenomenon and has certainly featured in labour market policies before. However, the number of people

⁹ Definitions of insiders and outsiders vary. See Häusermann and Schwander (2012) and Rueda (2006).

affected, the composition of either groups, in particular of outsiders, as well as the visibility of the divide and the political sources of dualization are considered different in recent decades (Emmenegger et al. 2012a:306).

To what extent dualization is pursued as a clear political strategy is disputed. Rueda argues that in particular centre-left governments in OECD countries have tended to promote less egalitarian policies in favour of insiders (Rueda 2006:405). Social-democratic parties are more committed to labour market insiders compared to the centre-right and have therefore been willing to sacrifice the interests of labour market outsiders. Similarly, trade unions, even more than Socio-democratic governments are tempted to defend the interests of their members, the insiders as unemployed or persons working in precarious employment relations are generally not unionized (Esping-Andersen 1999).

FUTURE CHALLENGES OF GLOBALIZATION AND SERVICE ECONOMY

In contrast to the golden years of democratic capitalism which lasted from the end of WWII to the early 1970s, no new economic model combining employment and welfare has been found. Rather national political economies have entered a phase of ongoing restructuring in which business, employment and social policy have to be readjusted on a continuous basis. The main drivers for the process are changing division of labour of the global economy, in which emerging economies take on parts of the manufacturing sector that have previously dominated the economy of the industrialized world. We can therefore identify three main processes of change: globalization, deindustrialization and technological change.

Globalization

The global economy has now become a dominant feature for many jobs, not just in the export industries. However, to what extent globalization is undercutting terms and conditions and forces governments to cut social spending is disputed. Initially the balance of economic openness for modern economies was positive. Katzenstein long ago identified that small open economies tended to have large welfare states, because governments aimed to compensate the losers of structural change and smoothen the effects of economic fluctuation (Katzenstein 1985). There is also little evidence that globalization has led to a race to the bottom. Taxation and public spending has remained high in many countries. Public investment in education and infrastructure remains an important component for productivity. Countries have long held on to different taxation rules without investors avoiding high tax countries (Garrett 1998: 823).

Others however, such as Dani Rodrik, have argued that the effects of globalization will lead to more tensions between winners and losers. International trade will undermine social norms in many countries and increase the pressure to maintain competitiveness. Governments will find it difficult to safeguard social protection (Rodrik 1997:4-5). Economic opening has certainly contributed to the stagnation of average wages in many advanced economies. Off-shoring might have kept some industries competitive, but has led to the loss of employment in these sectors. Unskilled workers in developed economies have experienced declining wages and job insecurity.¹⁰

Proponents of an increase of trade openness argue that a high degree of international trade integration can lead to long-term welfare benefits. First, foreign direct investors, mainly from industrialized countries, can import some of the basic labour standards from their home countries (Mosley 2006:1). A similar argument contends that both exporting firms and foreign-owned plants

¹⁰ For a good summary of the arguments see Freeman (1995).

have comparatively better working conditions than domestic employers (Moran 2002; Harrison and Scorse 2004). Second, globalization may even increase politics' room to manoeuvre due to better access to capital: governments "wishing to expand the public economy for political reasons may do so (including increasing taxes on capital to pay for new spending)" (Garrett 1998: 823). FDIs are said to improve local living situations, thus also labour standards (Flanagan 2006:188). However, as Sengenberger (2005:66) emphasizes, these findings are hardly surprising, given that "both the source and the destination of recent FDI flows were the most developed countries with comparatively high labour standards".

This critical approach is backed by others, who claim that globalization will decrease the stability of employment relations (Rodrik 1997) or, at worst, lead to competition along the lowest common denominator (Deacon 2000). In contrast to the compensation thesis, which predicts an increase of welfare due to global trade, the competition thesis argues that global trade leads to a decrease of social spending (for an overview see Genschel 2004). It has, however, proven difficult to make robust empirical claims. While several authors have found a positive correlation between the relationship of foreign economic penetration and government respect for civil liberties in developing countries (Richards and Gelleny 2003; Meyer 1998), other authors report mixed influences (Mosley and Uno 2007) or evidence for a negative correlation (Cingranelli and Tsai 2003). Then again, several studies find little or no evidence that variations in collective labour rights are due to discrepancies in FDI (Busse 2002; Neumayer and de Soysa 2006).

The increase of precarious working conditions is a phenomenon often attached to the process of globalization, capital mobility and the continuous pursuit of low cost production in less developed countries (Kalleberg 2009). In the political discourse it is used as a term to symbolize the changing employment

relation in western economies. This process takes place in all countries irrespective of the welfare regime.

Deindustrialization

Some authors have argued that the globalization has been accompanied by an ever more drastic challenge at the national level that has led to the need of increased welfare state restructuring and expansion even more than globalization: deindustrialization (Iversen and Cusack 2000:316). Deindustrialization defines the process in which the employment structure in a country moves from employment in the first (agricultural) and second (manufacturing) sector towards a dominating employment in the third (service) sector. The structural changes away from manufacturing and towards the service economy began in the 1960s. The reasons for this shift are manifold: the saturated demand of the domestic and wealthy international economies for traditional manufactured products, shifting patterns of demand, increased female employment and technological progress as well as the increasing demand for service-based activities (Häusermann 2010; Iversen and Cusack 2000).

One of the challenges of deindustrialization leading to an increased need for welfare state expansion has been the non-transferability of skills between manufacturing and service based occupations (Iversen and Cusack 2000:327). Depending on the original focus and importance of skills within the national employment structure, the process of deindustrialization leads to an increased level of welfare state expansion to cope with this phenomenon. This argument contradicts the perspective outlined by Esping-Andersen that strong and egalitarian welfare states are linked to strong and participatory industrial working classes. Despite varying forms of deindustrialization across OECD countries, all governments have reacted to the problems posed by deindustrialization, underlining its importance (ibid.:346). Moreover, Iversen and Cusack claim that in fact deindustrialization has a stronger explanatory

power for explaining welfare state expansion and reform in the last decades than globalization or partisanship. They argue that an increased level of welfare state expansion was necessary in order to protect the workers in the first and second sector if their employment position was threatened by technological change or the acquired skills or social benefits were not transferable to the service sector (2000:325).

However, Manow et al. are critical about the consolidation of both first and second sector shift towards the third as ‘deindustrialization’ and propose a finer distinction between ‘de-agrarization’ and ‘deindustrialization’ in order to explain the shifts in employment as well as the concomitant shifts in welfare expansion in the post-war period (Manow et al. 2013). They claims that in contrast to the transition from second to third sector, labour transition from agriculture to manufacturing with regard to skills was less problematic as the majority of manufacturing jobs required only a modest level of qualification in that period (ibid). The deindustrialization theory of Iversen and Cusack denotes therefore only the period since the 1980s when involuntary shifts from second to third sectors results due to a decrease in demand for manufacturing due to technological innovation.

The flip side of deindustrialization is the rise of the service economy which inhers both potential and risks for employment relationships (Schelkle 2011). The increase in employment possibilities for women and younger generations benefits the economy and society as it increases the overall workforce. At the same time, trade unions are barely represented in this sector. Second, trade unions have failed to keep up their image with the changing forms of employment. Recent studies indicate that trade union representation is perceived to be beneficiary only for long-term stable employment relationships, because this still is the main principal interest group for unions. By protecting these insiders from the risks of atypical and insecure employment relations, these

outsiders are automatically also kept away (Johnson et al. 2011). The increase of atypical employment forms has a negative impact on the interest in labour representation. The probability of individuals to join a union is on average 4.5 percent smaller if the latter has either a part-time contract or a non-permanent contract (Ebbinghaus 2011b:115-118).

CONCLUSION

Employment relations and the welfare state are closely related. They shape each other in various ways. Changes in the welfare state have repercussions on employment relations and vice versa. The dynamic relationship between the two can be systematically assessed by comparative research since both vary considerably between countries.

However, both, employment relations and the welfare state, have developed over the last century in tandem under very specific economic circumstances. Both are a product of the rise of mass production in advanced industrialized countries, in which a majority of the population was either directly or indirectly employed through manufacturing firms. Mass production implied stable jobs and clear division of labour and responsibility between, employers, workers and the state.

This situation has now changed. In the last quarter of the 20th century, advanced industrialized countries have seen a rapid and deep transformation of their economies. Manufacturing employment has been moved offshore, the service economy expanded and policy-makers have moved away from protective and Keynesian policies towards supply side reforms and ‘commodification’ in the words of Esping-Andersen. The majority of workers on national labour markets are now women workers and atypical work – part-time, fixed-term and precarious work – is on the rise.

The new labour market requests a new welfare state. Politics and policy-makers are busy adjusting welfare provisions and institutions. Political coalitions are shifting and former clear political alliances such as the one between trade unions and center-left parties are strained. The process of adjustment and transformation has not come to a new equilibrium but is currently ongoing. It remains to be seen whether, when and how a new stable arrangement can be found.

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