

FUTURE
OF EUROPEAN
WELFARE STATE

INFOGRAPHIC PAPER

→ by VÁCLAV BACOVSKÝ

INTRODUCTION

Europeans are proud of their high standard of living, social protection and generous provision of various public services. The global financial meltdown and the ensuing sovereign debt crisis in Europe triggered a debate about the sustainability of this model.

This briefing paper argues that welfare state needs to redefine its foundations in Europe because most of the states are not ready for new, upcoming challenges. Sovereign debt crisis, increasing global competition and ever-higher expectations of all citizens about the quality of services provided, changing social norms, growing migration, negative demographic trends: these are just some of the factors that put pressure on national governments to find working formulas for good welfare policies that do not overburden public budgets.

The debate on welfare policies tends to be very technical and drained in details. The aim of the paper

is to draw a bigger picture in this field – outlining both the recent and the current development and, in addition, focusing on some possible future trends. The text of this briefing paper is complemented by visualisations of interesting and relevant facts and figures. The focus lies on four major policy areas: education, labour market, healthcare, and pension system. These policies are crucial for the future well-being and stability of the European continent. Even more important is to raise public awareness of the challenges that stand ahead of us.

I would like to thank Leszek Balcerowicz, the former Polish Finance Minister, whose speech during the ELF event in Sopot in October 2015 was the immediate inspiration for this paper.

HISTORY – THE SPLENDED RISE OF WELFARE STATE

The origin of the modern welfare state is usually linked to the reforms of German Chancellor Otto von Bismarck during the period of 1883–1889 followed by similar reforms in France, Sweden, New Zealand and the UK before the WWI. In 1935 Roosevelt's US was the last developed country to introduce limited social security. The disaster of WWII accelerated the rise of welfare state to prevent democracy from falling victim to the perils of fascism and bolshevism. While the real boom of social spending followed during 1960s and 1970s, the global financial and economic crisis in 2008 could begin a new period of rationalized welfare.

A STORY OF SUCCESS?

Comparing the end of the 19th century and the beginning of the 21st century, one cannot overlook the unprecedented leap in the quality of life of all Europeans. Life expectancy in developed countries doubled from 40 to almost 80 years, literacy ratio reached nearly 100%, and child labour was completely eliminated. Human life improved in every aspect.

This progress overlaps with the rise of welfare state, leading to a conclusion that welfare state policies

and regulations stand at the heart of the progress. Such a conclusion is, however, rather premature as other factors may play an even more important role: the rise of capitalism and revolutionary progress in many sciences leading to many technological innovations.

While the positive contribution of welfare policies to the growing life quality is undeniable, real evaluation of welfare policies is difficult and highly normative (depending on the definition of such a term as social justice). Even if we accept the narrative of social democratic parties that the welfare state is a success story, we must stay critical and be aware of the fact that falling victim to one's own success is easy if we stick to one formula and stubbornly insist on it despite the changing environment. Success in the past is no guarantee for success in future. Adaptability is the key to long-term success also in welfare policies.

GROWING FOR EVER?

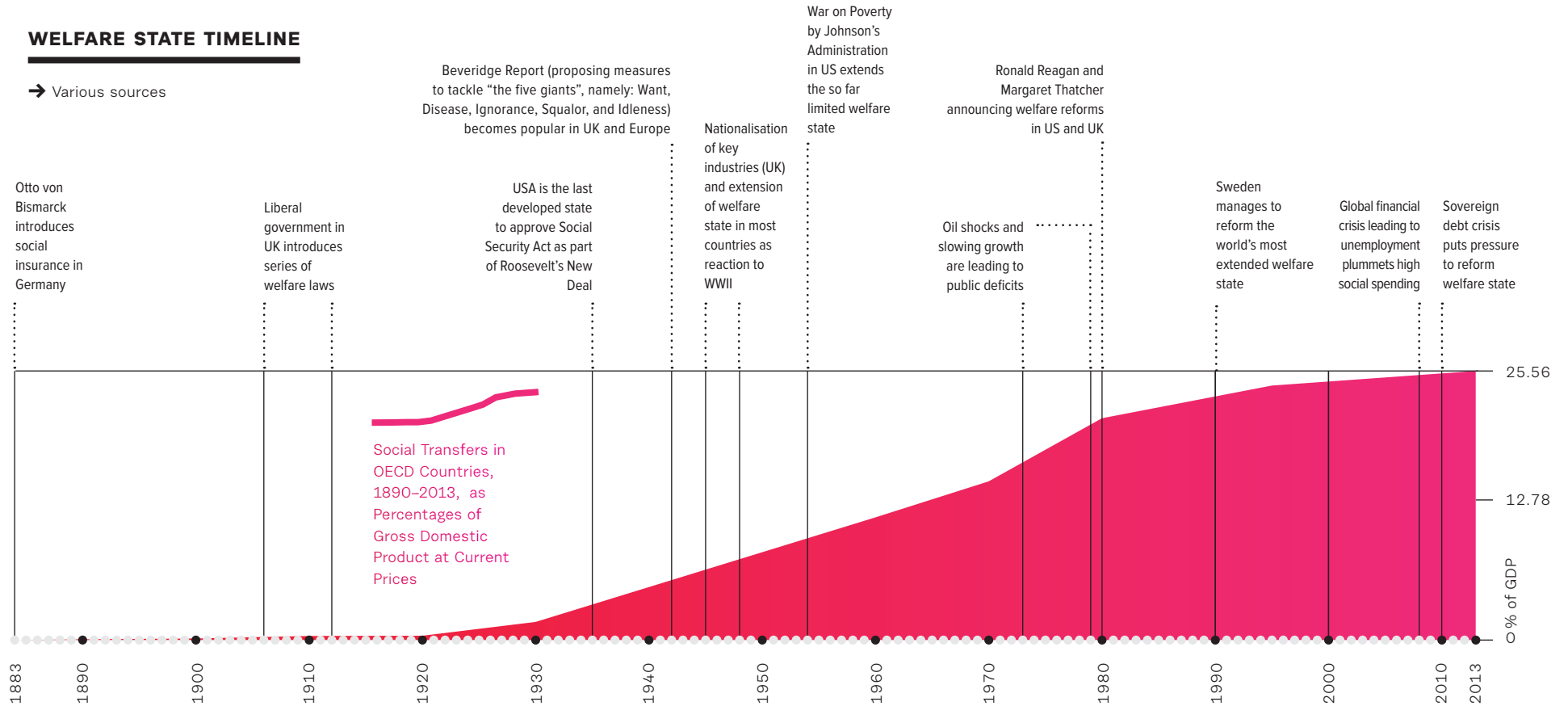
The timeline of welfare history and related social expenditures (see Timeline infographics) reveals a clear trend in steadily rising welfare costs, with some rare exceptions. The boom of the welfare state was made

possible thanks to the very good situation in the world economy in 1950–1975, the favourable demographic situation in European countries during this period and also to strong ideological pressures and the related political and interest groups.

Politically, there is certain inelasticity to scale back welfare. Political scientists point the finger at an unhealthy entanglement of welfare state policies in political competition and voter buying. Economists offer another aspect to be considered – Baumol Disease. The theorem by William Baumol says that productivity in labour-intensive industries increases more slowly than in other industries where machinery can be substituted for labour. As the prices for products go down due to higher productivity, the prices for services such as education and healthcare go relatively up. Since welfare policies are highly labour-intensive, it is probable that social spending will outpace the inflation.

WELFARE STATE TIMELINE

→ Various sources



Average person in 1883

- Women were not allowed to vote
- Men had to work for 10-18 hours per day, six days per week
- Child labour was still existent



Life Expectancy

years of life

Average person in 2013

- Women and men have equal social and political rights
- Average working week has 40 hours
- Child labour is non existent in Europe



BLESSING OR CURSE? VIRTUOUS AND VICIOUS CIRCLES OF WELFARE

Welfare state in Europe is often depicted both as the reason for the high living standard and as the root of the current malaise. The most prevalent labels and arguments are summarized in the virtuous- and vicious-circle diagrams.

MOVING BEYOND BLACK-AND-WHITE VISION

As will be argued in chapter on “Blocked reforms”, one of the major threats to successful welfare reforms is a polarized debate marked by black-and-white argumentation. This study attempts to move beyond the level of intentions, goals and principles and seeks to look at some facts, their context and policy implications.

.....
“What is ‘welfare’ for some groups may be ‘ilfare’ for others.”

Titmus, 1974: 27
.....

.....
“Institutions cannot be adequately characterized by their aims. The best aims in the world, if combined with bad incentives via the wrong institutions, can generate terrible outcomes.”

Daniel Shapiro, in Palmer 2012: 13
.....

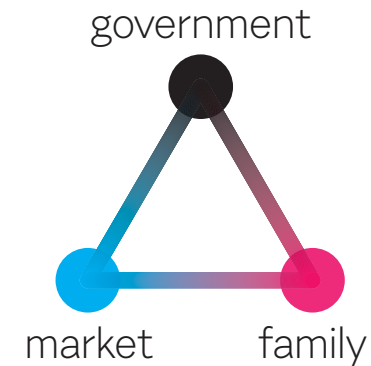


→ Source: Own

LEGITIMACY AND FUNCTIONALITY OF WELFARE STATE

MAIN WELFARE ACTORS

→ Source: Anderson, G. Esping, 2000



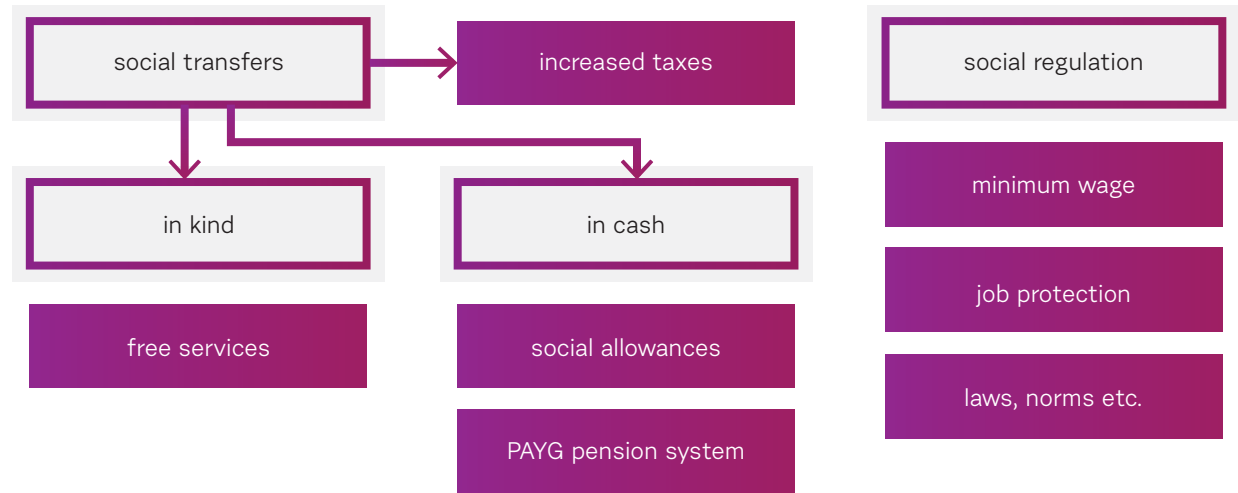
Over the years, welfare policies have grown in scope and depth, leading to different models of regulations, redistribution and provision of services. These are mutually entangled in a very sophisticated system. As a result, only a handful of experts understand the functionality and interrelatedness of particular policies.

The original basic principles of welfare state were providing security net for people unable to care for themselves. Over time, the governments in most developed countries embraced more ambitious goals of providing services that not only protect those in need, but aspire to provide some basic standard of living to large sections of citizens. Radical voices from the

left part of the ideological spectrum even suggest that governments should use welfare policies to even out the general standard of living for all. While such direction is regarded as radical and dismissed by pointing to the communist fiasco, it is still true that Europeans largely support the active role of governments in securing decent jobs and ensuring a reasonable standard of living. Underlying social norms, expectations and attitudes are highlighted by sociologists as crucial elements of any functional welfare state. Interesting differences between the attitudes of the Europeans and the Americans to poverty provide an explanation why both welfare states took different trajectories.

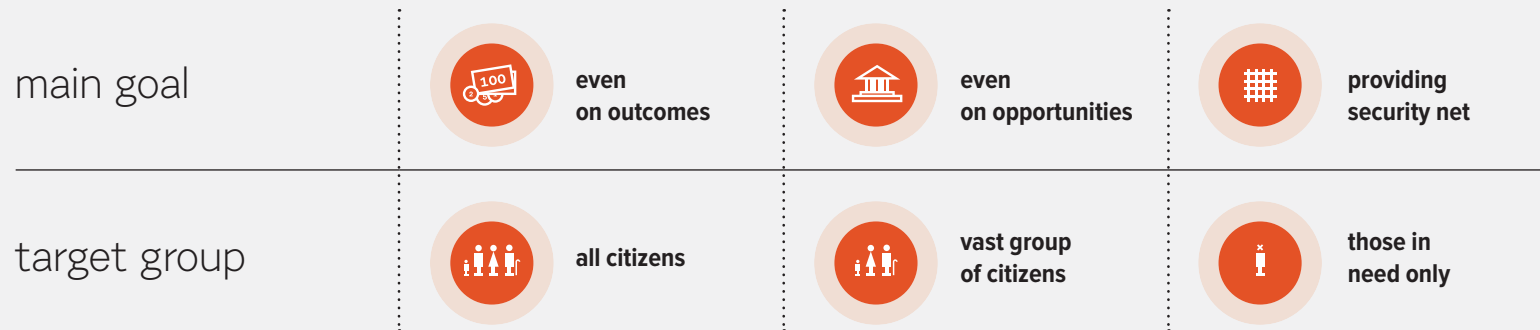
MAIN WELFARE TOOLS

→ Source: Balcerowicz, Leszek, 2014 — adjusted



WELFARE ASPIRATION AND TARGET GROUPS

→ Source: Bergström, Andreas, 2014 — adjusted



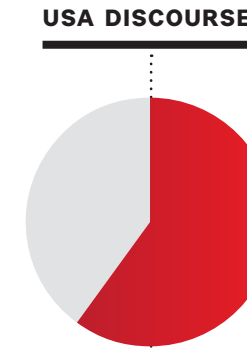
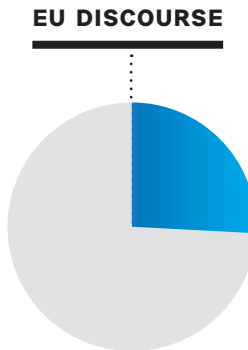
USA Discourse
Europe Discourse

**% OF EUROPEANS/AMERICANS AGREE
WITH FOLLOWING STATEMENT:**

→ Source: The World Value Survey

“the poor are lazy”

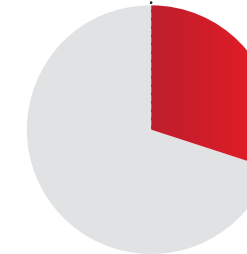
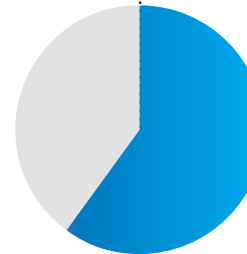
26%



60%

“the poor are trapped by the system”

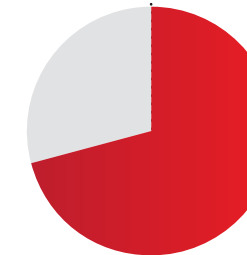
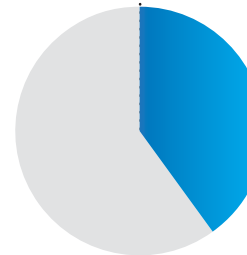
60%



30%

“the poor have a chance to escape from poverty”

40%



71%

Most Europeans expect governments to:

- ...ensure a job for everyone who wants one;
- ...ensure adequate health care for the sick;
- ...ensure a reasonable standard of living for the old;
- ...ensure a reasonable standard of living for the unemployed;
- ...ensure sufficient child care services for working parents; and
- ...provide paid leave from work for people who temporarily have to care for sick family members.

WELFARE STATE POLICIES AND THEIR COMPLEXITY

The agenda of the welfare state had grown in width and depth ever since WWII. Currently, the main tools of policies are based on redistribution of taxes and direct financial payments and on provision of various in-kind services. These apply according to certain criteria: testing the eligibility (universal vs. means-tested policies) and subsequently determining the amount of the benefit (income-related vs. flat-rate).

Universal benefits are often distributed to people who do not need them (thus being wasteful and inappropriate), but an undeniable advantage of such a universal approach is the simplicity which makes the system easy to administer and operate. This is one of the reasons why the new idea of granted basic income (universal and flat-rate) has recently become trendy in Europe. Universal income suggests cancelling the huge array of various benefits and allowances and introducing one universal payment. While the simplicity is elegant and promises substantial savings on administration, it remains unclear in what way it would shape the human behaviour. Would it rather support independence and give freedom or would it rather lead to a culture of entitlement and dependence?

Another trend of targeting and means-testing became recently famous thanks to the Brazilian program

Bolsa Familia, a successful conditional cash transfer that gives money to poor families providing they fulfil given conditions (such as sending children to school). Similar policies were partly introduced in Slovakia and Hungary, but met with criticism due to their clear bias toward the Roma minority.

All systems have their strengths and weaknesses; the major system challenge is how to avoid traps where benefits discourage personal activity and responsibility. Can we find a model that combines the simplicity of a universal model with the incentives behaviour and saves money of the conditional and targeted system?

COMPLEX AND BUREAUCRATIC

Proliferation of various rules and their complexity is one of the biggest challenges for the current welfare model. Although the intentions of lawmakers may be admirable, the problem is that as soon as various regulations enter the statute book they are usually almost impossible to remove. Regulation becomes very lengthy and complex as the law-makers try to define every possible situation to ensure predictability of proposed policies. Needless to say, the growing amount of interdependent regulations leads to unintended outcomes as it often runs counter the original intention.

CORE POLICIES OF THE MODERN WELFARE STATE

→ Source: Own

The result is a sophisticated system in which the citizens often feel lost, not understanding their own rights and obligations.

Slashing red tape is a popular slogan of many political parties; in reality, however, it is more than difficult. The nature of welfare policies is bureaucratic. This not only bad. Bureaucracy makes all policies predictable and stable, equal and enforceable and, in case of good governance, also transparent and accountable (the latter, alas, is often not the case). The flip side of bureaucracies is rigidity, preference of formalistic (procedure- rather than outcome-oriented) approaches and a low level of innovation. If we want to reduce bureaucracy, a possible way is to empower other actors in welfare, such as private companies and civil society, through market principles.

One of the practical tools that can be used to prevent the ever-growing paperwork is the mandatory usage of “sunset clauses” – a measure in all legal norms that provides that the law shall cease to have effect after a specific date, unless further legislative action is taken to extend the law.



OLD AND NEW CHALLENGES

Many of the currently used principles of welfare policies were designed between the 1950s and 1970s. This period was marked by a high level of growth, enabling governments to pay for generous expenditures. The welfare state was backed also by well-functioning labour markets, strong families and a positive demographic curve.

The oil shocks in the 1970's and the following dip in economic growth revealed first cracks of the system. It is not a coincidence that the two most vocal critics of welfare – Margaret Thatcher and Ronald Reagan – came to power in that period. Both argued by reference to soaring costs, poor level of some public services and growth of state dependency among people. The public became more critical toward the effectiveness of welfare. The welfare state was accused of being often regressive rather than progressive, i.e. instead of helping the socially isolated and marginalized individuals,

policies often targeted the middle class. Effectiveness, efficiency and struggle for general support (legitimacy) were the traditional challenges in the 20th century.

The 21st century brings new challenges (reversed demographic trend, low growth) and old challenges in a new scope (globalisation, pressure for competitiveness and limited level of taxation, migration). Sociologists also point out the importance of transition to post-material values (higher esteem of leisure and free time) and shift in the family models (women emancipation, singles, childless couples etc.). The era of globalisation also brings new opportunities (such as easier communication, modern technologies leading to new quality of services). Perhaps the biggest game changer has come with the financial crisis and the ensuing sovereign debt crisis – public spending funded by state obligations is not a safe option any more.

OLD
CHALLENGES

Costs the welfare state is not sustainable in long term

Efficiency not delivering promised results for adequate price

Legitimacy is becoming unpopular as it favours middle class, and not those who are in need

Long-term change in social norms and family models

NEW
CHALLENGES

Lower economic growth

Demographic factors

Lobbying of interest groups

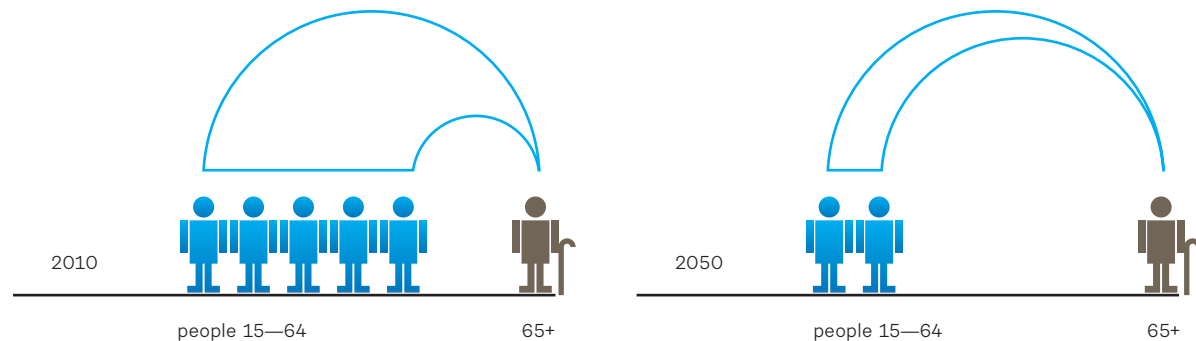
Migration pressures

Rising costs for high quality services

Limits of government debt

DEPENDENCY RATIO 65+ TO 15—64

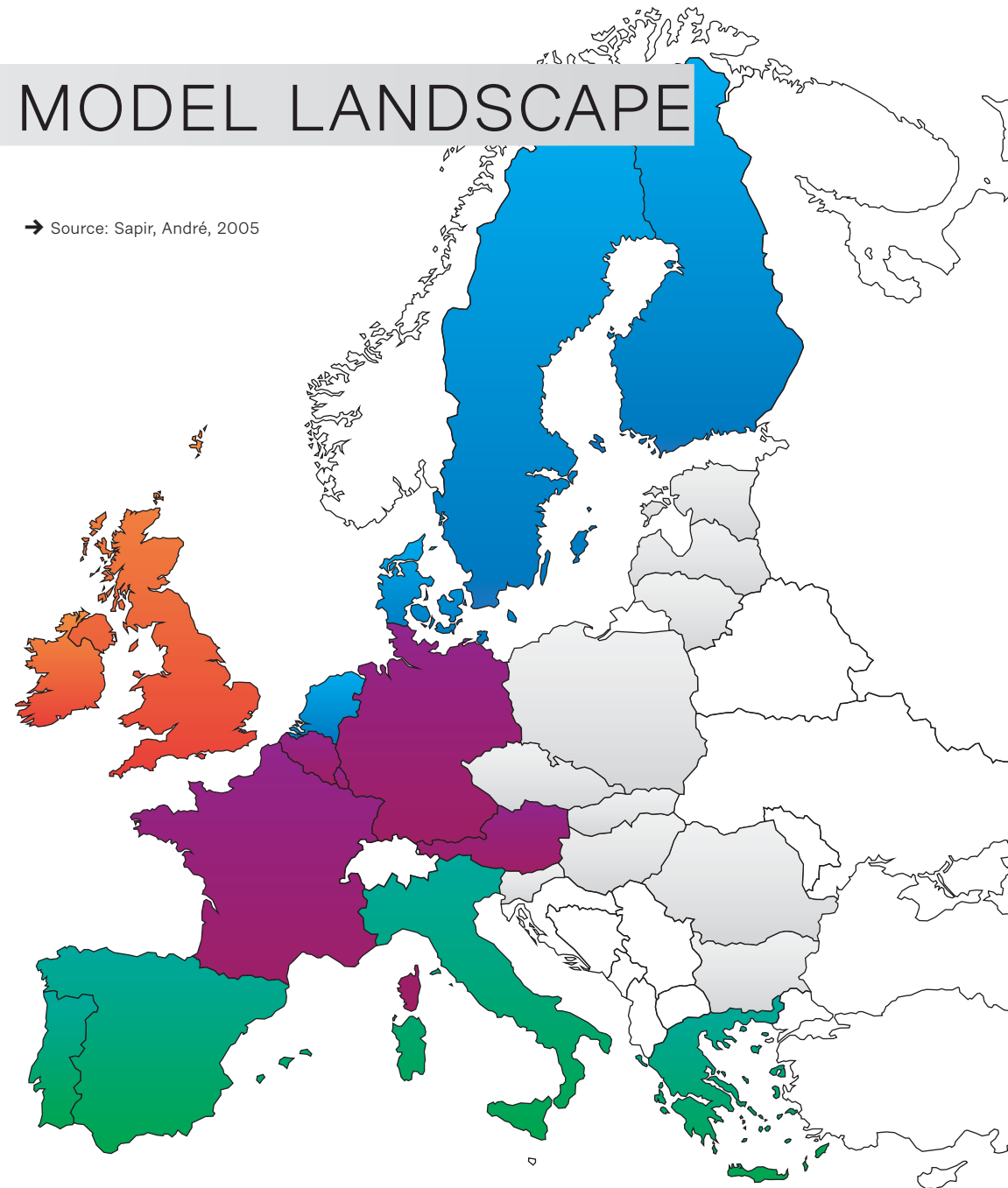
→ Source: Own



EUROPEAN WELFARE MODEL LANDSCAPE



→ Source: Sapir, André, 2005



The Post-socialistic countries (new EU-10) demonstrate much stronger emphasis on redistribution to prevent poverty. The model resembles a combination of the Anglo-Saxon and the Continental model. Welfare expenditures are, however, much smaller than those in the western half of the continent and generally. Moreover, the Post-socialistic countries within this group are highly internally differentiated.

TRAJECTORIES OF CHANGE CONTINENTAL COUNTRIES

Though the Continental model has proved to be less flexible, some countries were capable to introduce major reforms (such as Germany's labour market and pension system reform in the late 1990's and early 2000's). Other countries (such as France) remain firmly wedded to employment-based, contributory social insurance.

TRAJECTORIES OF CHANGE NORDIC COUNTRIES

The Nordic countries are marked by a high level of adaptation. Earlier, the welfare policies reacted to first challenges by shifting from cash transfers to family services, to policies that stressed activating employment and, above all, the integration of women into the labour market. Good examples of innovation can be found in Sweden and Denmark (e.g. voucher systems).

TRAJECTORIES OF CHANGE MEDITERRANEAN COUNTRIES

The Mediterranean countries: reforms were recently introduced as austerity measures (in Spain, Italy, Portugal and Greece) partly dictated by IMF and the EU, hence becoming highly unpopular and potentially undermining the legitimacy of democracy of the national states and the EU.

TRAJECTORIES OF CHANGE ANGLO-SAXON COUNTRIES

The Anglo-Saxon model has also proved capable of adaptation: in contrast to Nordic countries, Britain gradually moved toward a greater emphasis on targeted services and income-testing, assigning greater responsibility for welfare to the market (converging with the US regime).

TRAJECTORIES OF CHANGE POST-SOCIALISTIC COUNTRIES

The Post-socialistic countries – displaying various trajectories (Slovenia, Hungary, Czech Republic) – have increased public spending to catch up with the continental models, but have reacted to the new economic situation by new measures. Baltic state social spending remains very low. Overall, these states are more flexible in introducing reforms.

KEY WELFARE POLICIES: EDUCATION

The European landscape of educational policies is very diverse both in structure and outcome. We can find here some remarkable success stories in secondary level education performance: Finland as a long-term leader and Poland as a successful reformer. Most EU countries, however, are doing below the OECD average in the international comparison called PISA (Programme for International Student Assessment). At the university level, the picture is even more worrying: there are only two Universities in TOP10 and only 13 in TOP50 according to the Shanghai Academic Ranking of World Universities.

While this study deals mostly with economic aspects of education, it is important that the imperative for the best possible education is not driven by economic arguments only. Well educated people enjoy a greater level of personal freedom, a broader scope of opportunities and well-being.

The economic benefits of successful reforms are huge. According to a recent study (Hanushek, Woessmann, 2012), an increase of 25 PISA points can lead to long-term additional growth of between 2.5% to 4.6% of GDP. To reap such benefits, some difficult reforms are needed though. Finding funds to pour more money into the system is actually not the hardest challenge.

Given the high complexity of any educational reform, the biggest challenge for political reform seems to be the question how to overcome political myopia. Educational reforms are costly in terms of resources as well as political capital and gains only come in distant future (after students have left school and become a significant proportion of the workforce). The interest to improve education does not correspond with the electoral cycle of most politicians.

THE CONTROVERSY ABOUT SWEDISH VOUCHER REFORM

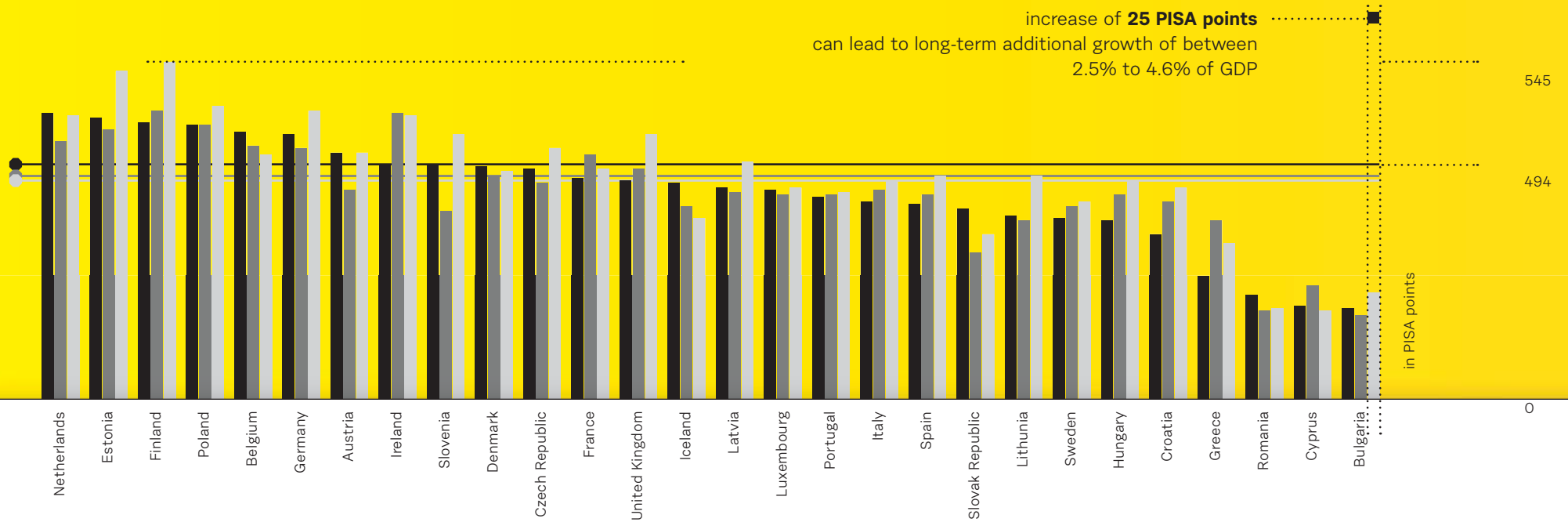
One of the most disputed topics in education is voucher system. Proponents (as famous and diverse as Milton Friedman and Steve Jobs) argue that vouchers give parents an opportunity to choose between private and state schools, create competition and hence lead to an increase of quality. Sweden introduced this system in 1992 and has served as an interesting case study ever since.

Sweden has done relatively poorly in the international comparison PISA (2000–2012) which served as the main argument of voucher system critics. In spite of this, recent studies suggest that the culprit for the drop in the PISA performance are the curricula changes introduced in the early 1990s together with the voucher reform. Unlike Finland, Sweden focused on individualized learning and underestimated the role of “disciplinary climate” in schools. Overall, authors of a recent study (Edmark, Frölich, Wondratschek, 2014) find that school choice has had a rather positive impact, particularly for minority and low-income students. Undoubtedly, the Swedish model has led to a stronger role of private schools (in 2008, 10% of pupils were enrolled in private schools and the number is still growing).

PISA 2012 — EU IN COMPARISON

→ Source: OECD

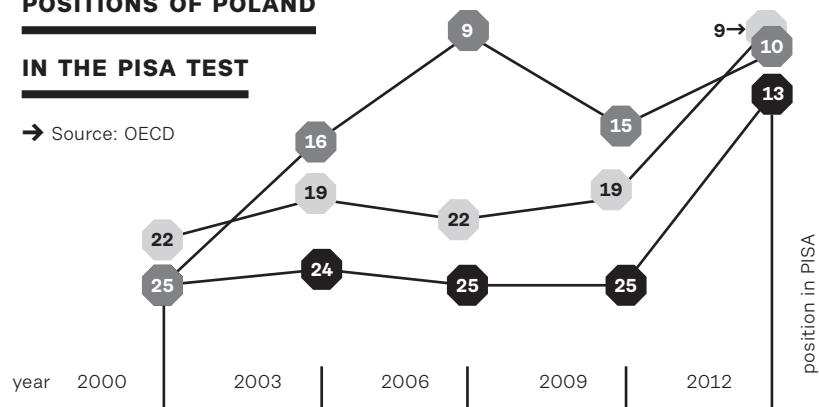
math
 reading
 science



POSITIONS OF POLAND

IN THE PISA TEST

→ Source: OECD



SUCCESS STORY: POLAND

Poland's education reforms introduced continuously after 1999 have produced a large overall improvement in educational performance in the PISA test. Increased hours of instruction and delayed tracking of students into the vocational education stream were the most important factors in the improvement of test scores. Poland now ranks 9th among all countries in overall reading scores on PISA, the only transition country to go from being below the OECD average on PISA to above average.

KEY WELFARE POLICIES: LABOUR MARKET

Despite the fundamental freedom of Europeans to move and work across the whole EU, low worker mobility and some informal barriers are still fragmenting the EU job pool into many national markets with specific legislative conditions. Deep recession in the EU exacerbated the negative trends and exposed the north-south divide in the job market.

The high unemployment problem is well known, peaking in 2012 at 10.5% and surpassing the record high of 10.4% from 1994. Moreover, unemployment in the EU is becoming increasingly 'structural', so that higher joblessness rates do not correspond to a more intense competition for vacancies. While particularly the youth unemployment is very worrying, the need for reforms is backed also by further statistics.

Low (or even non-existent) productivity growth rate and lower employment rate – all these statistics used to explain the EU/US gap in economic dynamism actually point to rigidities in labour markets and their unfair dual character. In many markets 'insiders' on full-time contracts are privileged with high levels of job protection and generous pension provisions, while 'outsiders' (usually the young) struggle to get any job or have to get by on a succession of shorter contracts with no benefits. Unlike the 'insiders', the short-term nature of their contracts means that they are the first to be laid off

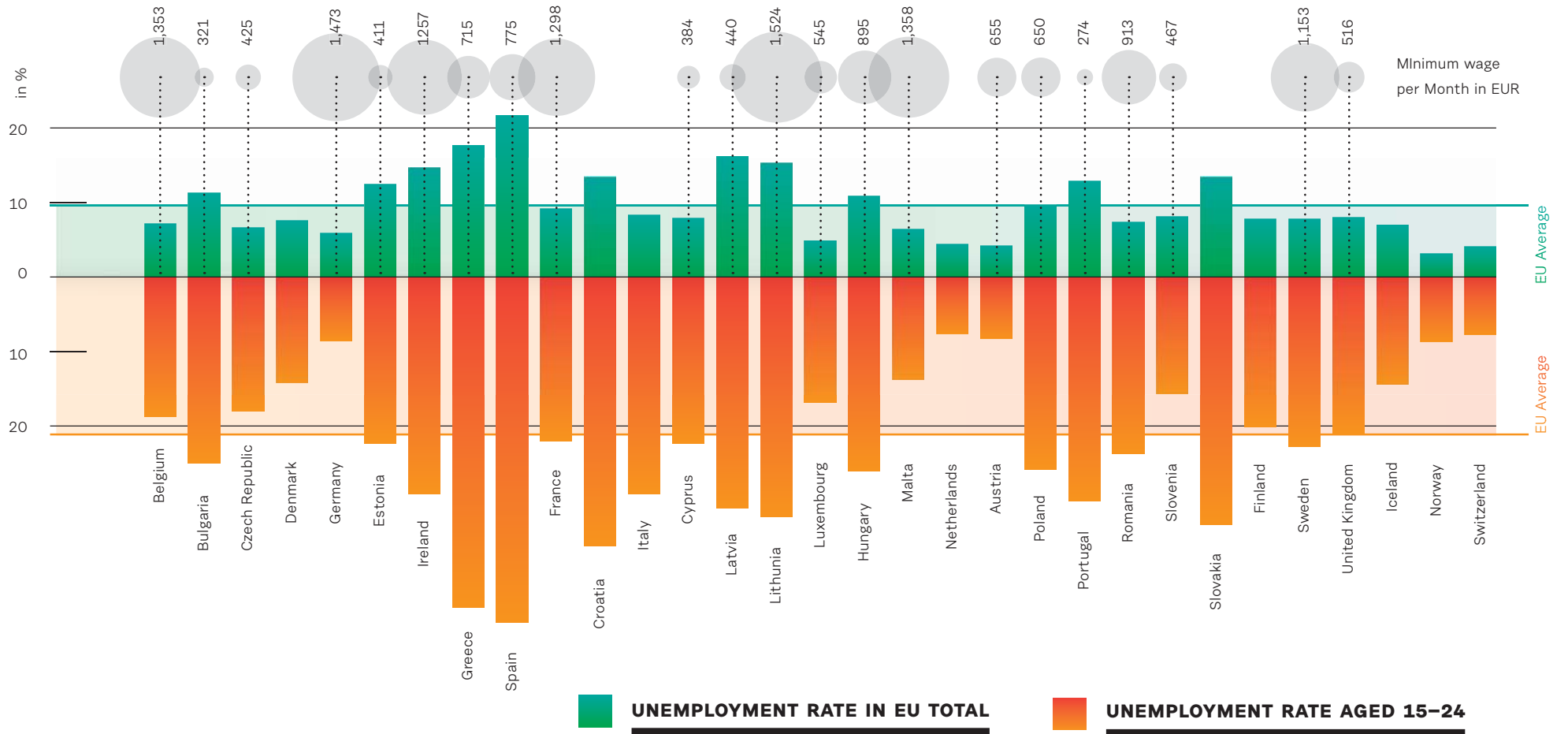
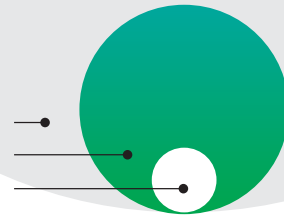
YOUTH UNEMPLOYMENT

Since 1945 the youth unemployment has been consistently higher than that of the older population. Nevertheless, ever since 2008 it has been increasing at a particularly alarming rate. Almost 1 in 4 young people in the EU are out of work and in some regions of Europe the youth unemployment rate is well in excess of 50%.

The effects of youth unemployment are well described: protracted unemployment at the early stage leads to lower social and cultural capital. This further deteriorates the employability and leads to poorer well-being. The vicious circle is rounded by increased participation in crime and alcohol and drug addiction. Even if these people ultimately find a job, bad experience at the beginning of their career results in reduced wages over a long period of time (between 13 and 21 percent by the age of 42).

It is much more difficult, however, to find the real causes and the right policy measures. The immediate trigger of soaring youth unemployment is the depth of the current recession. When we look beyond this, we see that many countries plagued with high unemployment continue to be saddled with rigid labour markets or under-performing education systems (or both, as is the case of the Mediterranean countries).

507.7 millions EU citizens
26.654 million of unemployed in the EU
6.6 million of new unemployed after crisis outbreak



UNEMPLOYMENT RATE IN EU TOTAL

UNEMPLOYMENT RATE AGED 15-24

→ Source: Eurostat

→ Source: Eurostat

MINIMUM WAGE

Minimum wage is a highly contested concept that can serve as an example of the difference between noble intentions and often clashing realities. While the aim of minimum wage is to help workers, economic research shows that it usually ends up harming workers and the broader economy. Minimum wages particularly stifle job opportunities for low-skill workers, the youth and unemployed, which are the groups that policymakers are often trying to help with these policies.

A review of more than 100 minimum wage studies (Neumark, Wascher, 2006) found that about two-thirds have negative employment effects. EU countries with minimum wage laws suffer higher rates of unemployment than those that do not mandate minimum wages. This point is even more pronounced when we look at rates of unemployment among the EU's youth: in EU countries with minimum wage laws more than 1 in 3 young adults (27.7%) is unemployed. This is considerably higher than the youth unemployment rate in the seven EU countries without minimum wage laws (19.5%).

There is no “free lunch” with government mandating a minimum wage. If the government requires the employers to pay certain workers higher wages, they will make adjustments to pay for the added costs, such as reducing hiring, reducing benefits, cutting employee work hours, and charging higher prices. Some policymakers falsely believe that employers can and will absorb the costs of minimum wage increases through reduced profits.

KEY WELFARE POLICIES: HEALTHCARE

Good healthcare treatment has many benefits: it prolongs life expectancy while preserving its quality. That has also substantial economic consequences. Although the quality and length of life are hard to express in numbers, Marc Pomp, a Dutch economist, estimates that over a lifetime health care costs € 280.000 but yields no less than € 450.000 (Pomp, M. in: Canoy, M. 2010: 7).

All developed countries in the world face the same trilemma of affordability, quality and access to health care. In other words: how to provide high quality health and long-term care services to an ageing population in a cost-efficient manner.

The rising pressure on health care comes from two major factors. The first is demographic: we do not just live longer, but the ageing population is more prone to chronic diseases and, at the same time, more demanding on the quality of the provided services. Second, the prices for the state of the art technologies, treatments and materials are rocketing high. A recent study says that the costs for researching and developing new

medicaments increased almost ten-times between 1975 and 2006 in the US, with a similar increase to be expected in Europe as well.

Without proper adjustments of health care policies, public expenditures are likely to soar. The current in-kind nature of provided services and low levels of private contribution lead to low public awareness of the real costs of health care. As Europeans largely support the model of universal coverage, there will be ever higher pressure for reforms in order to put the costs under control in the near future.

Although complete reliance on market principles is hardly possible due to inherent limitations (informational asymmetry, potential prohibitively high costs for some individuals, equality of treatment issues), some reforms suggest that well-designed managed competition in health care has a higher probability of spending tax money in a prudent way. The Netherlands and Switzerland are pioneering reforms that focus more on incentives and competition as central elements in the medical system.

HEALTH CARE REFORM IN THE NETHERLANDS

The Netherlands' reforms in the health care sector launched in 2006 have aimed at introducing more competition among private health insurance companies (eliminating the difference between public and private insurance). All patients can choose freely between insurers and can switch once a year. The overall assessment of the new system is that whilst there are numerous problems, on balance the system yields more benefits than costs.

A recent evaluation mentions the following positive outcomes of the reform: a more competitive insurance market with freedom of choice; increased transparency; increased activity by insurers to negotiate with health suppliers; more attention given to the quality of health care than before. Politicians and bureaucrats seem farther removed from operative health care decisions in the Netherlands than in almost any other European country. The biggest challenge seems to be the control of costs and management of mergers among big insurance companies and the weak role of prevention (lacking incentives for both patients and insurance companies). In 2012, reforms expanded the role of the market in the hospital sector and reinforced budget controls.

USER-CENTRED DESIGN IN HEALTH CARE

While in terms of the outcomes the level of health care services is generally rising, in many countries the encounter with hospitals and other health care facilities remains a very stressful experience. This is not only due to the very nature of suffering from physical problems, but also due to the quality of services provided that often do not match the growing expectations. Patients are used to responsive and customer-centred services provided by private sector corporations and expect to be treated as active, interested and informed participants also by physicians.

Several pilot projects based on human-centred design in health care facilities were undertaken to find out how to make the services more user-friendly, how to innovate, incorporate modern technologies and social media. The method of user-centred design involves teams of service users, service providers and designers in a collaborative process of identifying problems with the existing service, envisioning new solutions and implementing them.

With 56,000 cases per year of violence and aggression of patients attending Accident and Emergency Departments in the UK hospitals, the NHS decided to implement user-centred design method to alleviate the problem. While the project is still running, minor changes

in communication of staff with patients and installing information screens in waiting rooms has already led to positive results in the patients' behaviour. Similar projects were run in US hospitals to mediate conflicts among hospital staff. Sitra, the Finnish Innovation Fund, experimented with health kiosks in shopping centres which are staffed by nurses, provide routine care and stay open late and on weekends. Such out-of-box solutions rarely come from public administration.

User-centred design should be implemented in broader range as a whole new world of innovation is promised by incorporation of smart devices and social media in prevention and other areas of health care.

CAN SMART MOBILE DEVICES REVOLUTIONIZE HEALTH CARE?

High availability of smart mobile devices in our population may revolutionize health care: small, inexpensive sensors (capable of blood pressure gauging or of snapping medical-quality images) and analytic software make it possible for patients and doctors to capture all kinds of data to improve care. Patients can play a more active role in their own health. Voice over IP can be used so that doctors and nurses can make house calls without ever leaving the office. All major technological giants (including Apple and Microsoft) are creating mobile health products

and investing in start-ups. In addition, older technologies, such as WI-FI connectivity or cloud computing, should be put to more efficient use in the current health care system.

HOW DO WE DEAL WITH COLLECTION, TRANSPARENCY AND PROTECTION OF EXPONENTIALLY GROWING HEALTH DATA?

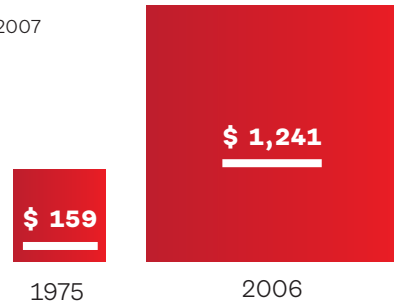
A potential revolution caused by mobile devices will only highlight the current challenge of collecting, storing and using health data. Data is everywhere and the challenge is to use that data to make meaningful decisions and provide better care.

IBM estimates that 80% of medical data is unstructured, hidden and fragmented. It is spread among researchers, health insurers, state and local governments, primary care providers and hospitals, where it is further isolated in multiple places (EMRs, labs, physicians' notes etc.).

Getting access to this valuable data and factoring it into clinical and advanced analytics is critical to improving care and outcomes, incentivizing the right behaviour and driving efficiencies. Proper big data analysis could help our ability to anticipate and treat illnesses. Furthermore, the use of big data could better identify waste in the health care system.

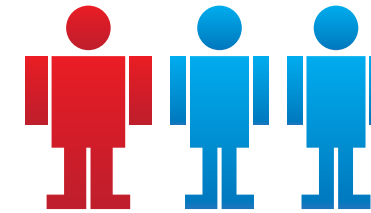
**FULL COST OF BRINGING A NEW CHEMICAL
OR BIOLOGICAL ENTITY TO MARKET**

→ Source: J.A. DiMasi and H.G. Grabowski 2007



OBESITY

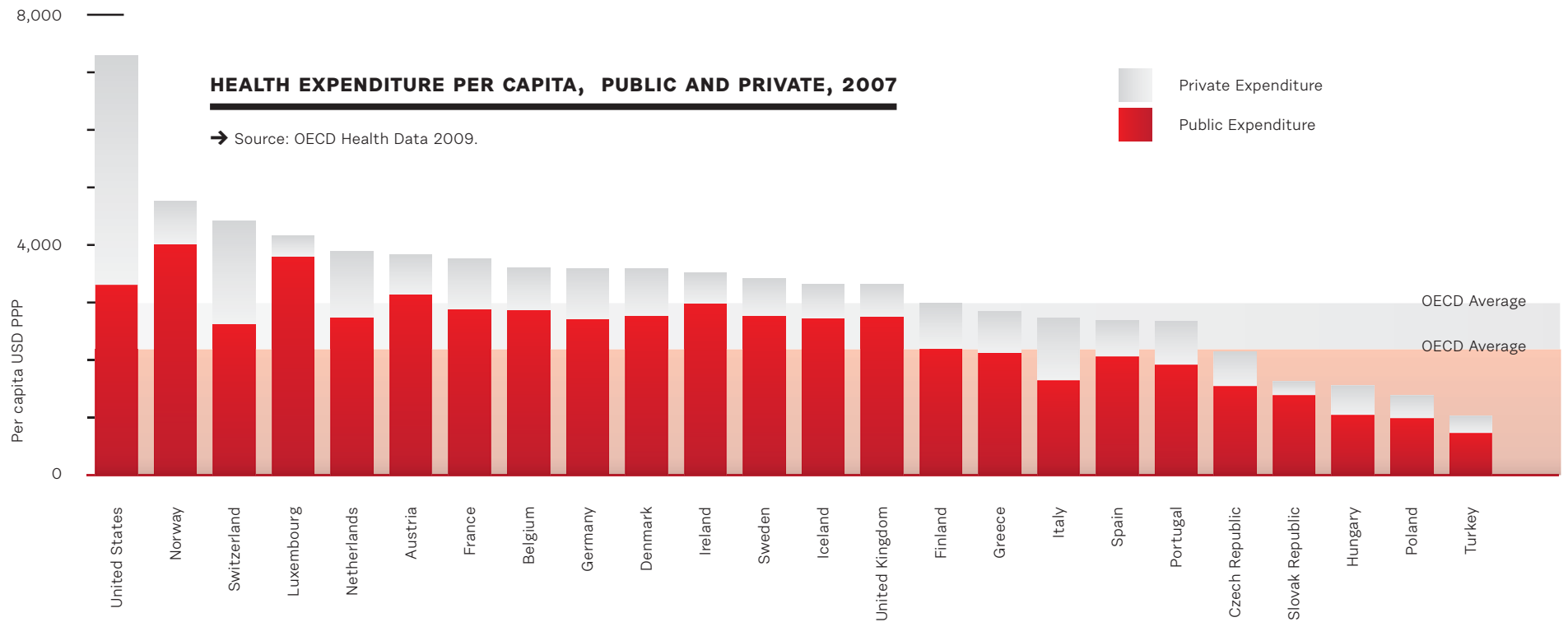
→ Source: WHO Europe



1 in 3 11-year-olds is overweight or obese in Europe

HEALTH EXPENDITURE PER CAPITA, PUBLIC AND PRIVATE, 2007

→ Source: OECD Health Data 2009.



KEY WELFARE POLICIES: PENSION SYSTEM

71.8%



think that future generations of retirees will be worse off than those currently in retirement

Average for France, Sweden, Germany, UK, Poland, Hungary, the Netherlands, Spain.

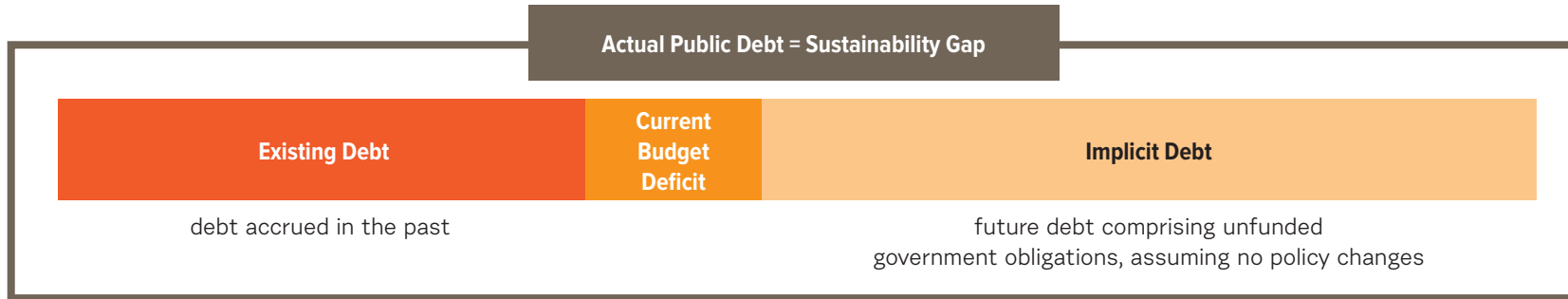
→ Source: Aegon Retirement Readiness Survey

The population of Europe is ageing. This demographic pressure comes from two basic factors: while back at the beginning of 20th century the average life expectancy was around 40 years of age, in 2014 in many European countries life expectancy goes already beyond the age of 80. At the same time, fertility rates continue to fall. This means that working population will be shrinking in the coming decades. The infographics No. x depicts the dependency rate. This rate tells us how many people in active working age there are for one pensioner. Currently, this rate is roughly 1:4 or 25% (four working people for one pensioner), whereas in 2050 this rate will be 1:2 or 50%.

This is a huge challenge for public budgets where old-age pensions are the biggest spending. Many countries still largely rely on “pay-as-you-go” systems. This is a non-funded scheme, i.e. the current working population is paying the pension benefits to pensioned people. This system was working perfectly when the working population and wages were growing. Currently, however, the demography puts an enormous pressure on this scheme, since the pensions are increasingly funded by government loans. Recent opinion polls reveal that the public is worried about the future level of pension benefits. The majority of the interviewed sample believes that future generations will be worse-off compared to current situation.

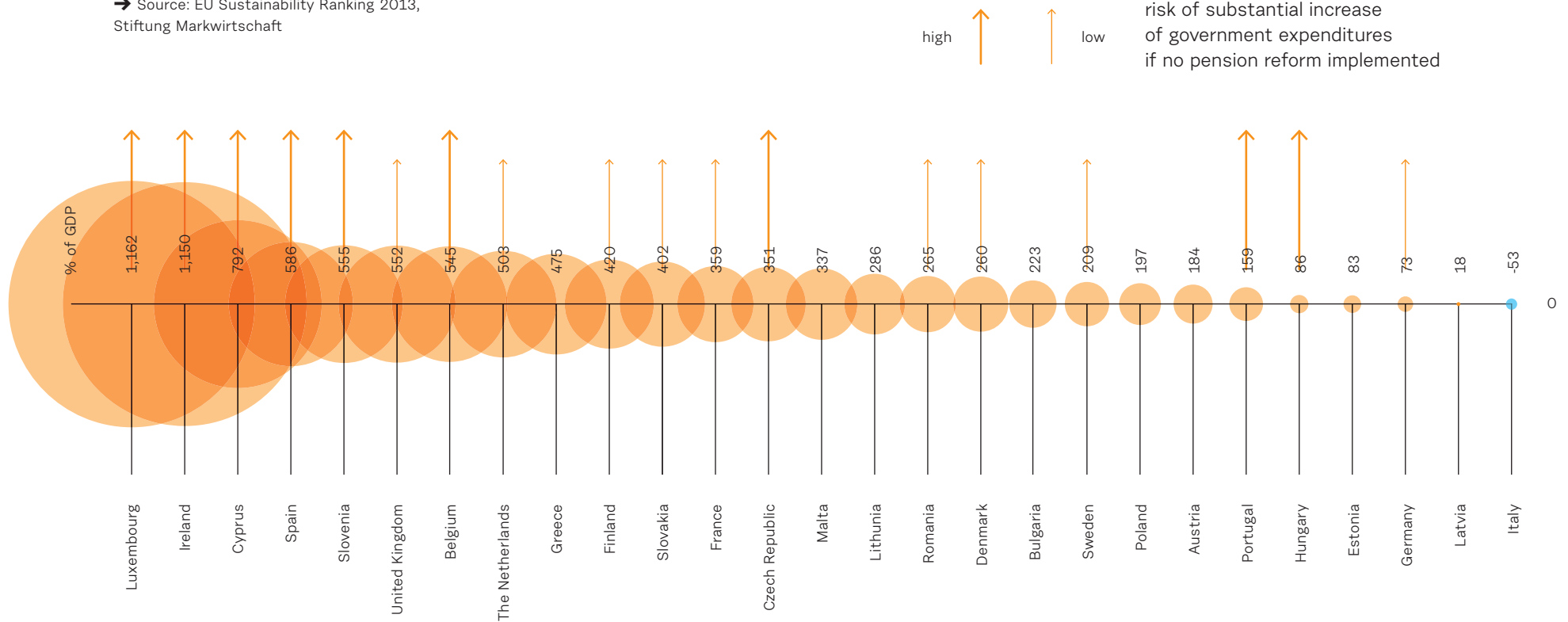
IMPLICIT PENSION DEBT

The implicit pension debt (i.e. unfunded pension liabilities) consists in the present value of pension promises, net of future pension contributions that are implicit in the current legislation (future mandatory expenditures). This topic became important not only due to the Maastricht criteria in the EU and the sovereign debt crisis. Introduction of pension reform may be very costly in the initial phase, and deterioration of public finances can be only properly evaluated if implicit debt of unreformed pension schemes is calculated. Rating agencies are calculating pension and health care liabilities when rating national bonds. Currently, EU has launched a binding methodology manual for the member states to include implicit pension debt in official national accounts as of 2015.



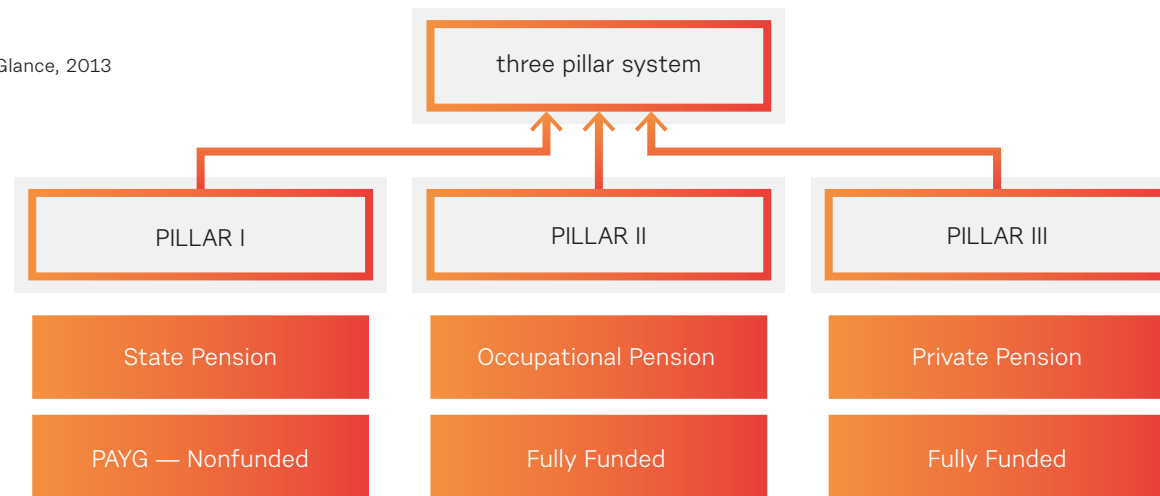
ACTUAL PUBLIC DEBT (INCLUDING IMPLICIT PENSION DEBT)

→ Source: EU Sustainability Ranking 2013, Stiftung Marktwirtschaft



THREE PILLAR SYSTEM

→ Source: OECD Pensions at a Glance, 2013



RECENT REFORMS

Increasing the normal pension age has been the most common reform during the past five years. As a consequence, the majority of OECD countries will have a retirement age of at least 67 years by the middle of this century. A few countries are going beyond this age by linking increases of the pension age directly to the evolution of life expectancy. Large structural reforms leading to a complete overhaul of the pension system have been rare in recent years. Several countries, however, have introduced, or have decided to introduce, a defined-contribution pension scheme (for example, the Czech Republic, Israel and the United Kingdom).

→ Source: OECD Pensions at a Glance, 2013

OVERHAULED REFORMS:

Worrying trends are to be observed in Central Europe. Hungary has gradually dismantled the mandatory second pillar since the end of 2010 and transferred accounts to the first pillar. In Poland, contributions to private schemes are to be progressively reduced from 7.3% to 3.5% to allow an increase in contributions to the country's new pay-as-you-go public financing pillar. The Slovak Republic allowed workers to move back to the state-run scheme from private DC plans in June 2009 and made occupational pensions voluntary for new labour market entrants. However, the move was short-lived: in 2012, private pensions were again made compulsory. These changes lead to very low trust in the government efforts to modernize pension scheme. The introduction of the second pillar in the Czech Republic raised little interest, to be revoked just two years later.

→ Source: OECD Pensions at a Glance, 2013

BLOCKED REFORMS

.....
 “The biggest threat to social justice in Europe is not radical institutional change, but the ‘frozen’ welfare state landscapes where resistance to change is institutionalised, and major interest groups are able to define how welfare systems operate.”

.....
 Patrick Diamond and Guy Lodge, 2013

As the welfare policies grew in scope and range, the welfare state became one of the most contested issues in politics. Welfare policies are directly linked to socio-economic status, attitudes towards welfare correspond to major ideological (left–right) cleavages in party systems. Taxation and welfare policies are the issues that make people go voting. This has several consequences for the development of the welfare state.

The real problem is the asymmetry in welfare scaling: politicians need significantly less of political capital to increase and enlarge welfare benefits, while cutting or reforming them is highly unpopular and often leads to political defeats in elections. The propensity of politicians to buy voters and not to be responsible for the mid- and long-term consequences is amplified by the short political cycle.

The positive side of the high voter salience of welfare policies is their relatively wide media coverage; the flip side, however, is that the discourse is prone to populism. Discussion about welfare may easily become highly ideological. While welfare policies should be backed by values reflecting the general attitudes of population, in reality authentic problems are obscured by artificial quarrels. While analyses of policies confirm

different trade-offs in the design of policies (one cannot have universally available generous public services and low taxation at the same time), the public discourse tends to be full of artificial dichotomies used plainly for labelling the political opponents (greed versus solidarity, government versus markets etc.).

Although welfare state policies were largely progressive originally (attempting to redistribute income from the wealthy to the poor, leaving middle class intact), currently it is the middle class that is the direct beneficiary of social security entitlements. Welfare for the wealthy in many member-states makes reforms of the system extremely challenging.

THE POWER OF INTEREST GROUPS

Mancur Olson argued in his famous book “The Logic of Collective Action” (1965) that small organized groups have advantage in democracies. Defending group interests requires some level of organisation, which is time-, energy- and money-consuming. Hence, narrow groups pursuing their particular interests that matter deeply to them are much more likely to get organized rather than broad constituencies pursuing general goals. In the 20th century, large interest groups

such as labour unions were important actors (using the political influence to block reforms). Lobbying by powerful corporations (especially in health care) has become more prevalent in the 21st century. The most un-organized, un-represented and un-defended is the young generation. No wonder that young people are fuming about their prospect of inheriting debts from the past and suffering from new austerity measures imposed by those who caused the current problems.

LACKING REFORMS IN THE EU

While the first trigger of the sovereign debt crisis was the meltdown of the financial system, the economic crisis was worsened by the missing, blocked or unimplemented reforms in welfare policies, notably in labour market and education. Low adaptability of

.....
 “Outdated labour market and social policies simply do not allow the Single Market, [...] to unleash their full potential in meeting the challenges of globalisation and technological change.”

Sapir, 2005: 373

EU member states marked the period of 2000–2010 . The Lisbon Agenda of the EU prescribed member states reforms (without any sticks to make them do so) which were related to welfare policies. Poor overall performance has had a serious impact on the single market in the EU, the real engine of economic growth. Andreas Sapir predicted already in his report of 2005 that lacking reform will leave Europeans unprepared for global competition. As a consequence, he argued, Europeans will perceive not only globalisation as a threat, but also the EU Single Market as such.

DEMONIZED MARKETS

Market principles can be used in limited scope for allocation of public goods, such as education or health care. Nevertheless, they are always present in all types of welfare models as one of the main actors. We should not overlook there is nothing like a unified actor called market without further attributes. In the mixed economy of the welfare state, markets differ substantially not just across different states but also across particular policy fields within one state. It is also misleading to think that the right wing advocate markets while the left oppose them. In reality, both left and right wing parties use market reforms, though the goals and rhetoric may differ. Right wing parties often strengthen market principles to limit the size of welfare, to cut public provision through more private financing. Left wing parties usually pursue a different agenda: through markets they try to enhance welfare state legitimacy and efficiency. Despite this fact, the discourse about markets in welfare has a strong normative tone: the market is either the saviour of all problems of modern governance or its death knell.

FALSE DICHOTOMIES IN IDEOLOGICAL RHETORIC

.....

INDIVIDUALISM versus COMMUNITY
 MARKETS versus GOVERNMENT
 CONSUMERISM versus CITIZENSHIP
 GREED versus SOLIDARITY
 EFFICIENCY versus EQUITY

CORRUPTION AND LOW TRUST IN GOVERNMENT

Low level of trust in government is a major drawback for many EU member states, limiting their capacity to adjust to current challenges. In particular, the public trust is hampered by kleptocracy of the ruling class and a wide spread of corruption in some countries. In Central Europe, some reforms got under pressure after governments were accused of pursuing a hidden agenda: the newly introduced conditionality of unemployment benefits in Czech Republic and Hungary was accompanied by doubtful public procurements favouring service providers close to government parties. The same mistrust accompanies pension reforms that were partly overhauled in Poland, Hungary and the Czech Republic. Distrust is a significant factor in the Mediterranean countries as well: notorious has become the Greek case of government lying about the real state of public finances for a long time. It is not surprising, therefore, that current reforms are massively opposed.

WELFARE MODEL 2.0

In the previous chapters, we tried to summarize the recent and current situation in Europe. Let us call the current average welfare model “Welfare Model 1.0”. It can be also defined as “Welfare State 1.0”, since it is based on domination of government. Although some states showed the ability to react and adjust their policies (such as the Nordic countries), the overwhelming attitude was a mere cutting and trimming at the edges of the system (however painful they were), without asking the significant questions about the real aims and appropriate tools of the Welfare model for the 21st century. We cannot do the same and just try to lower the costs. We need a different approach. What is needed is a Welfare Model 2.0, a model that would take advantage of the opportunities for improvement offered by new information technologies in areas such as health, education, and e-government.

Some argue that the current situation is not as bad as to ring the alarming bell. While this can be argued only case by case for each country, one general observation applies throughout Europe: if we want to have a better standard of living (and hardly anybody can oppose

this) in the coming decades, the welfare system must be adjusted as soon as possible. The reason for this is the long curve of the change trajectories in areas such as education or pension systems.

It is not only the level of our well-being, but also the sustainability of our democracies that is at stake here. Decreased standards of living and, above all, the distrust in a better future can put dangerous populist and authoritarian parties into saddle. If people do not trust in future, they want security now and at all costs. That, however, locks the current welfare state in a rigid modus preventing experimentation and proper adjustment.

IS A WELFARE MODEL 2.0 POSSIBLE?

While sovereign debt crisis has already drawn public attention to the lack of financial sustainability of the current welfare state model, a real change in thinking will be needed. Europeans still largely expect the governments to take care of their well-being. The problem is, however, that governments alone may not

stand up to new challenges in a radically changing environment. The European welfare landscape has already offered some good practices to learn from. Although there is no one-size-fit-all formula for all the countries, some patterns of successful reforms are visible. Some cross-fertilization with good practices from other areas (private sector, civil society) is needed as well.

Innovation as the leading principle

Bureaucratic structures of public administration prefer predictability to innovations. That is good if the model is working well. But as we are struggling to find a sustainable way of financing our welfare policies, more innovation is needed. Public officers working at the interface with the public should be empowered to come with new solutions. We need less process-oriented, but more outcome-oriented approach in public administration. We must support innovation coming also from outside the public administration – from private companies, civic organizations, citizens and users in general. We need more courage to experiment, we

need to think in terms of completely new services, and come with bold applications of modern technologies. Smart governments and municipalities should support creation of new innovative centres and run pilot projects (as the Nordic countries have already done).

Big and small changes

While in some areas (e.g. pension system) only big government reforms can bring sustainable adjustment, in other policies change can also be more incremental and initiated from bottom-up. Making the visit of a job centre, school or hospital a more user-friendly experience does not necessarily need new legislation at all times. Since the internet and modern technologies are revolutionizing many areas of human life, we should seek completely new approaches to the design of public services. Small details in the design of policies can sometimes lead to significant benefits. User-centred design is one of possible methods to be applied: if businesses have used it to develop innovative solutions, why not apply the same approach to overcome challenges in the welfare policies?

Reliable analysis and evidence-based policies

The origin of current welfare policies dates back to an age when information was scarce. But information is abundant and growing exponentially. Huge amounts of data are being gathered by public administration on every day basis. Unfortunately, it happens only too often that the data is fragmented and unused. Most states lack clear principles and policies for open and transparent data processing. Gathering and analysing

Big-data is a trend in current business. Governments must follow and allow public and private companies to use aggregated data in open databases (without sensitive personal details). A significant advantage of this approach is a higher role of evidence-based decisions in everyday politics. Some governments (e.g. Estonia, UK) have already blazed the trail in this area.

Technology and internet

Introduction of modern technologies is no magic formula to change the welfare state automatically for the better. Paradoxically, we could recently witness many failed attempts to introduce complex IT systems (such as Obamacare). Looking back, computers had been introduced to public administration many decades ago now but they had never really led to any major productivity leap. Technologies bring social revolution only after they get technologically boring. In other words, we should neither overestimate the short-term impact nor underestimate the long-term one. The combination of a high penetration of the public with internet connection and with smart mobile devices can be the game changer in many policies. More importantly, technology will soon or later lead to changes in the paradigm of public administration, finally putting citizens at the centre of the public-sector universe. New trends have been sketched out in the chapter on health care but these technologies may even more revolutionize the education. Although the quality of teachers will arguably remain the crucial factor, with online courses, anybody can attend the best available courses today. Online services in the area offer huge potential for savings while they are also simpler, faster, and more convenient.

Markets in the welfare

Competitiveness and more choice for citizens is possible even in welfare policies. Although market principles will have limited role in allocation of public goods, examples from the education and health care sector prove that their application has been underestimated. Abundance of information available both to the government, markets and the citizen (lowering the information asymmetry) can lead to redefinitions of markets in many fields. We need to analyse what forms of markets we need and focus on their design (the regulation, oversight, and enforcement) rather than on everlasting debates concerning the competition between state and market.

Responsible and accountable governance

Only governments enjoying sufficient trust can introduce long-lasting reforms. Governments often know what kind of reform is needed but lack of trust and personal courage prevent any change. While political inactivity is very dangerous, we also need to avoid reforms implemented by force (as we saw in the Mediterranean countries): such reforms spurn public protests and may be overhauled by the next government, which makes any future reforms attempts less trustworthy. Pragmatism and less ideology is needed to ensure broad consensus. Well informed citizens are also an indispensable factor to create pressure on governments to act responsibly.

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