

The Real Threat to Liberal Market Economies

Higher Inequality and Lower Mobility

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THE WELFARE STATE IN LIBERAL MARKET ECONOMIES

In 1985, the Ford Foundation assembled a group of distinguished social scientists to consider the future of the American welfare state in the context of “Reaganomics” and the rise of neo-liberal policies. Ralf Dahrendorf, one of the members of the group, delivered what fellow member Albert Hirschman called “a magisterial opening statement,” in which he recalled T. H. Marshall’s theory of citizenship. According to Marshall, over the last three centuries, the notion of citizenship had broadened from civil to political and – in the 20th century – social rights, thus building the foundations of a liberal market economy.

In his introductory remarks, Dahrendorf wondered what, if any, the next evolutionary step might be in the continued development of citizenship and democracy, and he did so in the context of what at the time was perceived to be a profound crisis for the welfare state. While the assembled experts and the final Ford Foundation report addressed many of the issues involved – from welfare dependency to the new urban underclass – they paid little attention to the potential combination of two developments: greater economic inequality and lower social mobility. Even today, few are fully aware of this trend and fewer still grasp its implications.

This is particularly surprising given that a pattern of increasing economic inequality and decreasing social mobility, already noticeable in the 1980s, has gained greater momentum over the last 30 years. This pattern amounts to nothing less than the ‘social arrest’ of a growing number of people in more and more OECD countries. People belonging to this group are trapped in low-paying jobs with little prospect of advancement for themselves and their families, often earning too much to receive government support but too little to make ends meet. They gain little respect from their fellow citizens, and are economically and socially cut off, as well as geographically and culturally isolated.

KEY INSIGHTS

THE COMBINATION OF RISING INEQUALITY AND DECLINING SOCIAL MOBILITY CONSTITUTES A CRISIS OF “SOCIAL ARREST” IN MANY OECD COUNTRIES.

THE PROBLEM OF GROWING REGIONAL INEQUALITIES IN COUNTRIES LIKE GERMANY, THE US A, AND THE UK IS COMPOUNDING THE ISSUE OF DECREASING SOCIAL MOBILITY.

TO ‘RECOUPLE’ THE SOCIAL AND THE ECONOMIC, A COMPREHENSIVE PROGRAMME—INCLUDING PROGRESSIVE TAXATION, BETTER SKILLS TRAINING AND A STRENGTHENED CIVIL SOCIETY—IS NEEDED.

ECONOMIC INEQUALITY

Albert Hirschman was among the few who anticipated the growing social divide when he wrote in 1991: "In these days of universal celebration of the democratic model, it may seem churlish to dwell on deficiencies in the functioning of Western democracies. But it is precisely the spectacular and exhilarating crumbling of certain walls that calls attention to those that remain intact or to rifts that deepen. Among them there is one that can frequently be found in the more advanced democracies: the systematic lack of communications between groups of citizens..."

The lack of communication is social, cultural and political. Large segments of the population in today's divided societies have grown increasingly disconnected from politics. As analysis by former Dahrendorf Forum researcher Alexandru Filip shows that, from 2002 to 2014, the share of the 'disconnected' has risen by 40 per cent in Western European countries. The disconnected are those without a job, with no qualifications, and no membership of civic associations; these numbers would rise further were we to include those employed in low-wage jobs with little prospect of advancement. A new kind of 'precariat' has emerged, characterized by socio-economic anxiety, isolation from wider society, and resentment

towards elites. Not surprisingly, this development is likely to be connected to the recent surge in left- and right-wing populism, neo-nationalism and authoritarian tendencies.

INEQUALITY HAS A GEOGRAPHICAL COMPONENT, WITH ENTIRE REGIONS AT RISK OF FALLING BEHIND

While the trend is most pronounced in the US and UK, it holds true across many developed market economies, according to researchers from the Centre for Economic Policy Research. Sadly, more and more parents can no longer assume, or even hope, that their children will be better off than they are. Indeed, as a 2018 OECD report finds, "it would take around four to five generations for children from the bottom earnings decile to attain the level

of mean earnings" in the average OECD country. The problem is more severe in countries with high inequality, such as the US and UK. In these countries, "earnings mobility prospects tend to be usually weaker in countries where income inequality is high, and stronger in countries where inequality is low". For individuals, 60% of those in the bottom earnings quintile remain there four years later, while 70% of those in the top quintile stay there over the same time period. This results in what the OECD calls 'sticky floors' and 'sticky ceilings', both of which have become more pronounced since 1990.

More and more, inequality shows a geographical component, with entire regions at risk of falling behind – the new kinds of 'walls' Hirschman alluded to. The Brookings Institution finds that US cities with a population of over 1 million have contributed 72 percent of total employment growth since the financial crisis, while those between 50,000 and 250,000 have only contributed 6 percent. Since 1970, the wages in the top 2 percent of US metro areas have risen by nearly 70 percent, while earnings in the rest are only 45 percent higher.

The United Kingdom and France have seen a particularly pronounced divergence between their wealthy capital cities and the provinces. A study by the UK2070 Commission finds that, compared to a 1971 baseline, by 2013, the north of England had fallen by 17 points, while London has risen by 12. Similarly, a report on regional inequality in France finds that, by 2010, Lorraine's GDP per capita was only 76% of France's as a whole, down from 95% in 1975. The Île-de-France region (containing Paris), however, had risen from 148 to 165 % of the French average. Regional inequality in Germany is also pronounced. The poorest federal state, Mecklenburg-Vorpommern, trails behind the rest of Germany substantially, with a 2016 per capita GDP of \$29,133, compared to a national average of \$43,110. By contrast, the city-state of Hamburg has a per capita GDP of \$69,719.

WHAT CAUSED THIS DEVELOPMENT?

Informed by neoliberal ideology and most famously associated with the reform packages introduced by Ronald Reagan and Margaret Thatcher, most western economies underwent structural reforms aimed at increasing competitiveness, curbing the power of entrenched interests and coping with the loss of manufacturing – thus paving the way for service-based economies. While those reforms were in some ways justified (considering the ‘stagflation’ following the 1970s oil shock), they were not accompanied by adequate measures to address their wider social consequences. This led to what economist Dennis Snower identified as the ‘decoupling’ of economic and social trajectories: despite economic growth, the real wages and advancement prospects of large parts of the population have stagnated or worsened. For example, from 1973 to 2017, net productivity in the United States rose 77%, while real hourly wages increased only 12 %, according to the Economic Policy Institute. The number of ‘working poor’ (those who work but fall below 200% of the poverty line) has also risen to 14% of the US population, over half of whom are people of colour.

The extent of countries’ efforts to balance domestic considerations with the effects of advancing globalization differs: for example, Sweden and Germany were much more active in protecting labour relations than the UK or USA. And while social arrest is a pervasive problem, its magnitude is country-specific. The OECD finds that in many Nordic countries the intergenerational income elasticity of males (the degree to which a son’s average income correlates to that of his father) is around .2 (low correlation with father’s earnings), while in the UK, USA, and Italy is roughly .5 (high correlation with father’s earnings). These differences suggest that policy responses matter for the question of social arrest and thus that they should be investigated.

What can be done about the ‘social arrest’ of growing populations and the inherent dangers of divided societies? Already in 1995, at the height of globalization, Dahrendorf argued in a paper commissioned by the United Nations that global

economic integration requires ‘perverse choices’ for liberal democracies: global competitiveness requires either adopting measures detrimental to the cohesion of civil society, or restricting civil liberties and political participation. Accordingly, the quandary for OECD countries in the 21st century “is to square the circle between growth, social cohesion and political freedom”. Most OECD countries did not even attempt such squaring exercises. Instead, informed by neoliberal thought, they focused solely on economic growth.

In Dahrendorf’s formulation, the economic drivers of globalisation, decoupled and operating in transnational space, undermine the nation state (sovereignty), which in turn loses legitimacy (democracy). Protectionist economic policies could potentially strengthen the nation state but at the cost of economic growth. Moreover, mixed with identity politics, they can constitute powerful enablers for left or right populism, or as Dahrendorf put it, the growing authoritarian temptations of divided societies.

WHAT CAN BE DONE ABOUT THE “SOCIAL ARREST” OF GROWING POPULATIONS AND THE INHERENT DANGERS OF DIVIDED SOCIETIES?

Dahrendorf (1995) offered – in his words – “six modest proposals.” Slightly reformulated, they include: anticipating changes in the workplace and preparing affected population groups for them; undercutting the supply route for the precariat; strengthening local communities and regions in danger of being cut off; creating a stakeholder economy; adjusting government responsibilities and budgetary priorities to what’s possible; and changing public discourse to encourage a broad public debate to counteract the non-communication Hirschman warned about.

Yet nearly thirty-five years after the Ford Foundation assembled its group of experts to assess the future of the United States, and a quarter century after Dahrendorf’s report to the UN, the modest proposals no longer seem potent enough to

reverse the pattern of higher inequality and lower social mobility. Nothing short of a 'recoupling' of the social and the economic will do, in order to begin tearing down the dividing walls Hirschman feared.

CONCLUSION

For addressing social arrest, tax reforms and social mobility programs are needed to realign levels of social inequality with the range of opportunities available for different socio-economic groups. To accomplish this, tax reforms to reduce income inequality and wealth disparities - and to incentivize economic mobilization in terms of entrepreneurship and employment - must be implemented. This should be accompanied by social mobility programmes designed to function as "social conveyor belts." These would include massive investments in education and skills training to boost employability, and measures to create more equal opportunities for younger generations.

Safety nets, regional policy and migration management are required to undercut the

formation of a precariat and to stave off inter-generational downward social mobility. Safety nets must be put in place to protect those populations most exposed to the negative effects of globalisation and technological change. Furthermore, policies to compensate for regional disparities - including managed migration at domestic and international levels - need to be developed in order to reverse the troubling trend toward stark regional economic divergence.

Measures should also be taken towards strengthening civil society, with the goal of improving self-organization, encouraging social participation and counteracting exclusion. An enabling environment for civil society contributes to conflict management and reduces authoritarian tendencies.

Finally, sustained debates among disconnected publics must be encouraged in order to enhance social cohesion. Reinvigorated public debate can help heal current divides, prevent new ones from emerging and serve as the basis to restore faith in social mobility and equality.

FURTHER READING

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