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Recalibrating Europe's semi-sovereign welfare states

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Recalibrating Europe's Semi-Sovereign Welfare States

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Abstract

Since the late 1970s, all the developed welfare states of the European Union (EU) have been recasting the basic policy mix on which their national systems of social protection were built after 1945. Intensified global competition, industrial restructuring, budgetary austerity, changing family relations and demographic ageing have thrown into question the once sovereign and stable welfare systems of the Golden Age'. Moreover, domestic issues of work and welfare have more recently become ever more intertwined with processes of European political and economic integration. In this respect, it is fair to say that in the EU we have entered an era of *semi-sovereign welfare states*. Together, these forces have produced a momentum of system change that goes far beyond the popular notion of welfare state 'retrenchment'. The 'new' welfare edifice suggests a departure from a 'politics against markets' social-protection perspective, towards more of a 'politics with markets', social-investment approach. This paper tries to capture the comprehensive character of the ongoing effort to recast the architecture of the post-war social contract in terms of the concept of welfare recalibration for both heuristic and prescriptive purposes. It also addresses the engagement of the EU in ongoing processes of recalibrating Europe's semi-sovereign welfare states. In the policy debate the term 'European social model' is often invoked. Yet such generalisations gloss over the immense differences in welfare state development, design and institutional make-up across the EU's 25 member states and, as a consequence, fail to capture the complexity of "contingently convergent" reform trajectories in the recent period.

Zusammenfassung

Seit den späten 70er Jahren stellen alle hochentwickelten Sozialstaaten der EU den Mix an Sozial-Politiken, wie er nach 1945 in den jeweiligen Staaten geschaffen wurde, auf den Prüfstand. Die intensivierte Globalisierung, der Umbau der industriellen Produktion, Budgetprobleme, sich verändernde Familienbeziehungen und eine alternde Bevölkerung führen zu immer mehr Zweifeln an dem lange Zeit bewährten und stabilen wohlfahrtsstaatlichen System des goldenen Zeitalters. Dazu kommt, dass in letzter Zeit bisher nationale Themen wie Arbeit und Wohlfahrtsstaat immer stärker in die Prozesse der europäischen Integration hineingezogen werden. In diesem Blickwinkel gesehen ist es angemessen zu sagen, dass in der EU die Ära der nur noch halbsouveränen Staaten begonnen hat. All dies zusammengenommen kann man sagen, dass sich eine Konstellation ergeben hat, in der sich ein Systemwechsel vollzieht, der weit über die populäre Wahrnehmung der Öffentlichkeit vom „Abbau des Sozialstaats" hinausgeht. Die Konstruktion der neuen Wohlfahrtspolitik bedeutet den Abschied von einer Politik des sozialen Beschützens „gegen die Märkte" hin zu einer Politik sozialer Investitionen „mit den Märkten". In diesem Papier wird versucht, die umfassende Bedeutung der fortdauernden Bemühungen zur Umgestaltung der Architektur des Sozialkontrakts aus der Nachkriegszeit zu erfassen - und zwar sowohl für heuristische Zwecke wie auch als

Handlungsanleitung. Die Analyse bezieht sich auch auf das Engagement der EU in den andauernden Prozessen, die halbsouveränen Wohlfahrtsstaaten Europas neu zu „justieren“. In politischen Diskussionen wird oft der Begriff vom „Europäischen Sozialmodell“ beschworen.

Aber solche Generalisierungen gehen über die wirklich großen Unterschiede in den wohlfahrtsstaatlichen Entwicklungen, in der Gestaltung und im institutionellem Aufbau der 25 EU-Mitgliedstaaten hinweg und verfehlen so als Konsequenz, die Komplexität der „kontingenten Konvergenz“ der Reformwege in den vergangenen Jahren richtig zu erfassen.

Content

1 The adaptive capacity of the semi-sovereign welfare state

The striking intensity and the comprehensive character of welfare reform across the majority of the Member States of the European Union (EU) since the 1990s are very much at odds with the prevalent image of a 'frozen welfare landscape' presented in the academic literature. Most importantly, the substantive extent of welfare reform across a large number of EU Member States adds up to a momentum of system change that goes far beyond the popular concepts of 'retrenchment', 'roll-back', 'retreat' and 'demise'. But to say that European welfare states are far from sclerotic is not to say that they are in good shape. With 20 million citizens out of work and 90 million people otherwise inactive, there certainly is no room for complacency.

Welfare reform is, of course, not a smooth process. Corrective measures are difficult, but in the face of protracted policy failures they are enacted and implemented through the competitive political process. While reform experiences over the past two decades have primarily been built on processes of domestic (crisis-induced) lesson-drawing, more recently, cross-national social learning has been taken up in the context of the EU. In short, welfare reform is a highly reflexive and knowledge-intensive political process. From this perspective, it follows that the welfare state is best understood as an 'evolutionary' system, whose goals, aims, functions and institutions change over time, however slowly and imperfectly.

Today, an increasing number of academic observers are advocating a new welfare repertoire based on consistent normative principles, coherent causal understanding, (re-)distributive concerns and institutional practices – a repertoire that is comparable in its generalities to that of the male-breadwinner Keynesian welfare state of the post-war decades. These observers concur in their diagnosis that the current imperative of recasting the welfare state is very much rooted in the incongruence between new 'post-industrial' social risks and diverse family and labour market needs, on the one hand, and the institutional resilience of male-breadwinner social policy provisions, on the other. In terms of policy solutions, these authors prioritise high levels of employment for both men and women as the key policy objective, accompanied by elements of flexibility and security that facilitate men and especially women in accommodating both work and family life, that are managed by new forms of governance and are based on subtle combinations of public, private and individual efforts and resources (Esping-Andersen et al., 2002; Esping-Andersen, 2005; Jenson/Saint-Martin, 2003; Taylor-Gooby, 2004). By adopting a life-course perspective, the advocates of the 'new' welfare architecture of the 21st century seek to identify the inter-connectedness of social risks and needs over the life course, on the basis of which they are able to draft a 'social investment' policy agenda. The Keynesian emphasis on 'effective demand' management is hereby shifted towards an emphasis on 'effective supply', with the implication of removing social barriers to labour market entry, discouraging early exit, making labour market transitions less precarious, and providing gender equality and equality of opportunity throughout the life cycle in response to the drastic changes in the worlds of work and welfare (Esping-Andersen et al., 2002; Ferrera/Hemerijck/Rhodes, 2000; Giddens, 1999, 2001; Kenworthy, 2004; NESC, 2005; OECD, 1999).

My argument is built up as follows. First, Section 2 qualifies the underspecified use of the concept known as the 'European social model' in the face of the three-pronged challenge of economic internationalisation, post-industrial differentiation and permanent austerity. Next, Section 3 provides an inventory of a number of substantive changes in the make-up of Europe's mature welfare states over the final quarter of the 20th century. Section 4 presents the current effort to recast the architecture of the post-war social contract in terms of the concept of welfare recalibration for heuristic and prescriptive purposes. Next, Section 5 highlights the constraints and opportunities for EU engagement in ongoing processes of recalibrating Europe's welfare states. Since the mid-1980s, domestic issues of work and welfare have become increasingly intertwined with processes of European political and economic integration. In this respect, it is fair to say that in the EU we have entered an era of semi-sovereign welfare states (Leibfried/Pierson, 2000). In conclusion, Section 6 addresses the political imperative for a 'social-investment-centred' welfare agenda in the early 21st century. It is my contention that with a little more policy creativity, we should be able to turn the current tide of inward-looking pessimism regarding the sustainability of the 'European social model' into a renewed political effort represented by forward- and outward-looking 'social pragmatism'.

2 Caveats and challenges to the 'European Social Model'

In the heated debate over the future of the EU, the concept of a distinctly European social model is increasingly being used in policy discussions and political debate. Although European welfare states share a number of features that set them apart from other geopolitical regions like North America and Southeast Asia, it is important at the outset to make a number of qualifying reservations with regard to the underspecified use of the notion of 'European social model'. My most important caveat is that the notion of a European social 'model' is inherently static. While the architects of the post-war welfare state, John Maynard Keynes and William Beveridge, could assume that the future would be made up of stable male-breadwinner families and expanding industrial labour markets, this picture of economy and society no longer holds. Since the late 1970s, consecutive changes in the world economy, labour markets and family structures have disturbed the once sovereign and stable welfare 'equilibria' of employment-friendly macroeconomic policy, collective wage bargaining, progressive taxation, broad social security coverage and protective labour market regulation. As a consequence, all the developed welfare states of the EU have been recasting the basic policy mix upon which their national systems of social protection were built after 1945 (Hemerijck/Schludi, 2000). Moreover, couching policy discussions in terms of competing 'models' easily triggers ideological strife — a battle between warring alternatives represented by antagonistic advocacy coalitions. A casual glance at the recent French referendum campaign over the Constitutional Treaty clearly reveals the clash between two polarised positions. The French version of the European social model was pitted against a false stereotype of the 'Anglo-Saxon' model of capitalism, allegedly a 'free market without a safety net'. In addition, the notion of a distinctly European social model suggests a large degree of uniformity transcending national boundaries, which surely cannot be sustained empirically in an EU of 25 Member States. There are immense differences in development, policy design, eligibility criteria, modes of financing and institutional make-up across Europe (Esping-Andersen, 1990; 1999; Ferrera/Hemerijck/Rhodes, 2000). Finally, the notion of a distinctly European social model suggests a lot of virtu on the part of rational policy-makers, which also gives the impression that best practices can easily be transported from one Member State to another. Many social reform initiatives taken in recent years in the areas in question were expedient responses to impending economic crisis and political conditions. Also, the incubation periods of reforms before they start to pay off in terms of growth and jobs are extremely lengthy. Usually, it is incoming governments that reap the benefits of painful reforms enacted by their predecessors. In short: there are no models of eternal bliss to copy.

Despite the significant progress already made in different countries, there are still three sets of challenges urging contemporary policy-makers to persist in their efforts to reform the welfare state, redesign institutions and elaborate new principles of social justice. First, from without, international competition is challenging the redistributive scope and decommodifying power of the national welfare state. Many academic observers believe that the increase in cross-border competition in the markets for money, goods and services has substantially reduced the room for manoeuvre of national welfare states (Scharpf, 2000). Economic internationalisation demands countercyclical macroeconomic management, while increased openness exposes generous welfare states to trade competition and permits capital to move to the lowest-cost producer countries. Finally, there is the danger that tax competition will result in an underprovision of public goods. Second, from within, ageing populations, declining birth rates, changing gender roles in households as a result of the mass entry of women to the labour market, the shift from an industrial to the service economy, and new technologies in the organisation of work, are engendering suboptimal employment levels, new inequalities and skill-biased patterns of social exclusion. According to Gøsta Esping-Andersen (Esping-Andersen et al., 2002), the main reason why the existing systems of social care have become overstretched stems from the weakening of labour markets and family households as traditional providers of welfare. In addition, new sources of immigration and segregation, also in the housing market in metropolitan areas, pose a challenge to social cohesion. And, finally, while policy-makers must find new ways to manage the adverse consequences of economic internationalisation and post-industrial differentiation, their endeavours to recast the welfare state are severely constrained by long-standing social policy commitments in the areas of unemployment and pensions, which have ushered in a period of permanent austerity (Pierson, 2001). The maturation of welfare commitments — policies put in place to cater for the social risks associated with the post-war industrial era — now seem to be crowding out and overloading the available policy space for effective policy responses, especially in public services under conditions of low economic growth. This spectre of permanent austerity is likely to intensify in the face of population ageing. As an intervening variable in the process, European (economic) integration is fundamentally recasting the boundaries of national systems of social protection — constraining the autonomy of domestic policy options but also opening up opportunities for EU-led multilevel open policy coordination (Ferrera, 2005; Zeitlin/Pochet, 2005).

3 A series of profound reforms

The welfare state, in the shape and form in which it developed in Western Europe in the second half of the 20th century, represents a unique historical achievement. Never before in history, as Fritz Scharpf puts it, 'has democratic politics been so effectively used to promote civil liberty, economic growth, social solidarity and public well-being' (Scharpf, 2003). Towards the late 1970s, the celebration of the welfare state gave way to doubts. The oil crises of the 1970s, together with the changing character of international competition, deindustrialisation and the eroding effectiveness of domestic Keynesian demand management, led to a massive surge in unemployment not seen since the 1930s. In the 1980s, the 'prospects for survival' of the welfare state were recognised as poor. Economists singled out the accumulation of perverse labour-market rigidities produced by the welfare state as the obstacle that was impeding flexible adjustment, blocking technological innovation and hampering employment and economic growth in an integrating world economy (OECD, 1994). But despite the obvious 'irresistible forces' urging for reform, the European welfare state proved to be, as one leading scholar put it, an 'unmovable object' (Pierson, 1998).

A finer-grained comparative analysis of long-term developments, however, shows that the empirical foundations of welfare state inertia are fairly shaky. On the contrary, over the final quarter of the 20th century, developed EU welfare states have been recasting the basic social contract upon which their national welfare states were built after 1945. If we interpret the welfare state more broadly than only social protection as it is narrowly understood, it is possible to paint an extensive, cumulatively transformative process of policy change across a number of intimately related policy areas.

In macroeconomic policy, up to the late 1970s Keynesian macroeconomic policy priorities geared towards full employment as a principal goal of economic management prevailed. In the face of stagflation — i.e., the combination of high inflation and rising unemployment — the Keynesian order gave way to a stricter macroeconomic policy framework centred on economic stability, hard currencies, low inflation, sound budgets and debt reduction. Persistently high public deficits and inflation rates are undesirable in themselves and incompatible with global financial markets. The current framework of

European Monetary Union (EMU) and the Stability and Growth Pact (SGP), however, does not provide for an adequate macroeconomic regime. The key problem today is that EMU and the SGP do not do justice to the differences in economic circumstances across the Member States. The European Central Bank (ECB) sets interest rates in accordance with European-wide averages and the development of the trade cycle rather than with nation-specific shocks. Although fiscal discipline is in the self-interest of Member States, once a recession hits it is already too late to tinker with employment regulation and social protection. Moreover, inconsiderate and bold reforms of labour market regulation and social protection during a downturn stifle the market and are likely to generate economic stagnation and social unrest. Macroeconomic stability is a must, but a little more flexibility is called for.

In the 1980s, the responsibility for employment shifted away from macroeconomic policy towards adjacent areas of social and economic regulation. In the field of wage policy, a reorientation took place from the 1980s onwards in favour of market-based wage restraint in the face of intensified economic internationalisation. Since the early 1980s, wage restraint has resumed importance as a requirement for successful adjustment by facilitating competitiveness, profitability and — as a second-order effect — employment. Strategies of wage moderation have been pursued in many European countries through a new generation of social pacts linked with wider packages of negotiated reform, including labour market regulation and social protection. The rediscovery of a jobs-intensive growth path by way of social pacts in the Netherlands, Ireland and Denmark has also allowed sectoral bargainers to strike decentralised deals on productivity, training and job opportunities for less productive workers. In the 1990s, the EMU entrance examination played a critical role in the resurgence of national social pacts for hard-currency latecomers like Italy, Portugal and Greece, stimulating policy-makers and the social partners to rekindle cooperative, positive-sum solutions to the predicament of economic adjustment, for example by making taxation and social protection more 'employment friendly' (Fajertag/Pochet, 2000).

In the area of labour market policy, in the 1990s the new objective became maximising employment rather than inducing labour market exit, and this implied new links between employment policy and social security. The greater the number of people participating full time and part time in the labour market, the greater the contribution they make towards maintaining the affordability of adequate levels of social protection. This is also the key message of the Jobs, Jobs, Jobs Report of the Employment Taskforce, established by the European Commission and chaired by the former Dutch prime minister Wim Kok (Kok et al., 2003). In the process, public employment services (PES) in many countries have lost their placement monopoly. And although private placement agencies have still not gained a substantial share of the market, they have at least compelled the PES to modernise their service delivery. With respect to labour market regulation, understood in the more narrow sense, empirical evidence from Denmark and the Netherlands suggests that the acceptance of flexible labour markets is enhanced if it is matched by strong social guarantees. While systems combining restrictive dismissal protection with meagre unemployment benefits essentially cater to the interests of insiders, 'flexicure' systems based on minimal job protection but offering decent standards of social protection for the unemployed are best able to bridge the gap between insiders and outsiders.

Within the sphere of social security, the changes in macroeconomic management and wage policy have resulted in a shift from passive policy priorities aimed at income maintenance towards a greater emphasis on the activation and reintegration of vulnerable groups. In the process, the function of social security has changed from the passive compensation of social risks to a corrective attempt to change the behavioural incentives of claimants and employers, together with an emphasis on preventative social investments. This is also evidenced by the shift from out-of-work benefits to in-work benefits. Different strategies are appropriate to different welfare states. In the United Kingdom, where income guarantees and unemployment benefits are modest, individual tax credits to support low-wage workers and their families are very popular. In continental Europe, the main problem is that hefty social contributions price less productive workers out of the market. In the face of the relative weakening of traditional male-breadwinner social insurance programmes, policy-makers in these countries have turned towards strengthening the minimum income protection functions of the welfare state, coupling this approach with strong activation and reintegration measures. Many European welfare states seem to be evolving towards a dual social protection model, combining both Bismarckian social insurance and Beveridgian minimum income protection tiers. In this respect, the French and Belgian welfare states have increased social assistance protection for the neediest, using targeted benefits instead of universal benefits financed through taxation and general revenues. In 2005, through the so-called Hartz IV reforms, Germany followed suit while at the same time stepping up job-search requirements for the non-employed.

In the area of old-age pensions, the most important trend is the growth of (compulsory) occupational and private pensions. Most welfare states are engaged in developing multipillar systems, combining pay-as-you-go and fully funded methods with a tight (actuarial) link between pension benefits and contributions. Fiscal incentives have been introduced to encourage people to take out private pension insurance. In the 1990s, a number of countries, notably the Netherlands, France, Portugal, Ireland and Belgium, started to build up reserve funds in order to maintain adequate pension provision when the baby-boom generation retires. Changes in indexation rules have also helped to reduce pension liabilities. In Spain restrictions have gone hand in hand with an attempt to upgrade minimum pension benefits. Measures to combine work and retirement involving tax allowances and partial pension benefits have been introduced in Denmark and Belgium. Finland has developed policy approaches for improving the occupational health, working capacity and well-being of ageing workers in order to keep older workers in the workforce for as long as possible (Clark/Whiteside, 2003).

Social services have experienced something of a comeback lately. Spending on childcare, education, health and care for the elderly, as well as training and employment services, has increased practically everywhere in Western Europe over the past decade (Taylor-Gooby, 2004). Ageing and longevity, especially, generate a need for care that working families cannot or are no longer willing to provide. In Scandinavia the expansion of services to families began in the 1970s in tandem with the rise in female labour supply. It was in large part this policy of 'de-familialisation' of caring responsibilities that catalysed the dual-earner norm. In most other European countries, female employment growth came much later (Daly, 2000). In southern Europe it is only during the past decade that we have seen a sharp rise. Throughout the EU, leave arrangements have also been expanded — in terms of both the time and the scope of coverage — to include care for the frail elderly and sick children. Social service delivery organisations have also been given more autonomy in deciding how to use resources in the pursuit of agreed outcomes and more incentives to innovate in the search for improvements, while also structuring their accountability to service users and central government in new ways.

In terms of the financial architecture of the welfare state, finally, we can observe an increase in user financing in the areas of childcare, care for the elderly and medical care. At the same time, fiscal incentives have been introduced to encourage people to take out private services and insurance, especially in the areas of health and pensions. Management audit systems have been introduced to control and monitor the volume of public expenditure; this has taken the form of limited annual budgets and delegation of financial responsibility and autonomy to schools and hospital in countries like Sweden, Germany and the Netherlands. With respect to taxation, as a result of intensified competition across the EU, many Member States have started to pursue a combination strategy of lower statutory tax rates and a broadening of the tax base. This implies a shift away from the focus on vertical redistribution between rich and poor citizens, but, as consequence of base broadening, not per se at the expense of prevailing welfare commitments.

Over the past two decades, as the above inventory of reform shows, many European welfare states have — with varying degrees of success, but in some cases also failure — taken measures in order to change the direction of economic restructuring by pushing through adjustments in macroeconomic policy, industrial relations, taxation, social security, labour market policy, employment protection legislation, pensions and social services, and welfare financing. Many reforms have been unpopular, but several have been implemented with the consent of opposition parties, trade unions and employer organisations. In the process, we have seen the rise and fall, respectively, of the 1970s Swedish model of macroeconomic management, the 1980s German 'Rhineland' model of diversified quality production and the 1990s Dutch employment miracle. While today the Celtic Tiger, the Danish Lego model, the Finnish knowledge economy and revamped New Britain under Tony Blair figure as model countries to emulate, nothing can guarantee that their welfare systems will prove effective in responding to the next phase of social and economic turmoil. The welfare reform momentum of the 1980s and 1990s was triggered largely by intensified international competition within the context of the internal market in the enlarged EU. Thus far the endogenous dynamics of the transformation of work, gender, family and demography have remained secondary in the reform agenda, in part due to opposition from the remaining vestiges of male-breadwinner welfare provision. There is a real need to take policy issues related to post-industrial social change on board in the next wave of reform.

4 Understanding welfare recalibration

Welfare reform crucially builds on processes of domestic lesson-drawing, but increasingly, especially in the context of the EU, on cross-national social learning. As such, social policy reform processes cannot simply be reduced to political explanations of changes in the balance of power and interests. None of the policy actors participating in lengthy processes of welfare reform over the past two decades could rely on well-informed conceptions of what kind of social policy paradigm would ultimately result from their efforts of experiential domestic and cross-national exploratory policy learning. Active reformers were equally unable to judge with much precision how the sequence of policy shifts across a large number of interdependent policy areas would affect their own political and economic interests over time.

In an attempt to capture this more encompassing endeavour to rewrite the post-war social contract, especially since the 1990s, Maurizio Ferrera, Martin Rhodes and I have in recent years turned to the multidimensional concept of welfare recalibration for both heuristic and prescriptive purposes (Ferrera/Hemerijck, 2003; Ferrera/Hemerijck/Rhodes, 2000).[1] The notion of welfare recalibration is meant to suggest an extensive form of remodelling by way of providing a new cast for the welfare state as we know it along four key dimensions: functional, distributive, normative and institutional recalibration. The guiding question of welfare recalibration is: What sort 'new welfare architecture' is compatible with international competitiveness, the transformation of working life, the demise of traditional family structures, demographic ageing and fiscal austerity? Hereby welfare recalibration is a highly reflexive and knowledge-intensive, interconnected and multipurpose reform process. Reform decisions pass through and are based upon cognitive, normative, distributive and institutional judgements as to how to improve policy performance under conditions of structural and environmental change. Each of the four dimensions of welfare recalibration requires elaboration.

Functional recalibration has to do with the social risks against which the welfare state aspires to protect. The need for functional recalibration is often described in terms of the shift from 'old' to 'new' social risks facing people as a result of the transition from a male-breadwinner industrial to a dual-earner post-industrial society. Skill-biased technological change, the feminisation of the labour market and demographic ageing (as a result of rising life expectancy and rapidly falling birth rates) are the most important drivers of the new post-industrial risk profile. While the boundaries between being 'in' and 'out' of work have been blurred by increases in atypical work, low wages,

1 The term 'recalibration' was suggested to us by Jonathan Zeitlin.

subsidised jobs and training programs, one job is no longer enough to keep low-income families out of poverty. In the face of demographic ageing and in the light of a declining workforce, nobody can be left inactive for long. European welfare states are all in the process of moving away from the breadwinner/caregiver model, under which mothers are expected to stay at home with their children, to a model of 'employment for all', under which mothers are expected to enter the labour force. This transition, which Ann Orloff discusses in terms of the 'farewell to maternalism', is not merely the product of changing gender values (normative recalibration), it is also part of a more deliberate strategy of policy-makers in the face of population ageing to attract mothers into the workforce through activation programs, tax subsidies, part-time employment regulation, and the expansion of family services (Orloff, 2005). As new social risks concern both the labour market and family life, they extend the demand for functional recalibration from unemployment, sickness, disability and old-age insurance to family-friendly services to encourage labour market opportunities for women and raise birth rates.

The challenge is to reconcile women's new career preferences with the continued desire to form families. Failure to do so will produce either fertility rates below the renewal level or suboptimal levels of employment and income. Female employment is the key to resolving child poverty, which is on the rise in most European countries. Child poverty rates decline by a factor of three or four when mothers work. Labour market participation rates in southern Europe, especially for the younger female cohorts, are rapidly catching up to northern European averages. Among older women (aged 55−64), the employment gap is still considerable, at levels of only 16% in Italy and 23% in the Netherlands, compared to 65% in Sweden. Exit from the labour force at age 50, as Esping-Andersen forcefully argues, implies major foregone lifetime income and probably inferior pension entitlements for women, and for the public economy foregone government (tax) revenue. The standard family-friendly policy package includes a neutral, individual taxation regime, maternity-cum-parental leave with job security, and subsidised childcare (Esping-Andersen, 2005).

Since life chances are so strongly determined by what happens in childhood, a comprehensive child investment strategy with a strong emphasis on early childhood development is imperative. Access to affordable, quality childcare is sine qua non for any workable future equilibrium. Esping-Andersen maintains that childcare demand cannot be adequately met via commercial care markets. In a purely commercial regime, low-income parents will probably not be able to afford quality care. They may respond by placing children in cheap, low-quality care or by withdrawing from the labour market altogether. Inaccessible childcare will provoke low fertility; moreover, low-quality care is harmful to children and low female employment increases child poverty (Esping-Andersen, 2005). It should be emphasised that highlighting early childhood development goes beyond the idea that childcare is necessary to allow mothers and fathers to reconcile work and family life. A 'child-centred social investment strategy' is needed to ensure that children will be lifelong learners and strong contributors to their societies. More children, educated to perform in a knowledge economy, are needed to keep the economy going for a retiring baby-boom generation with high care needs.

If Europe wishes to be competitive in the new, knowledge-based society, there is an urgent need to invest in human capital throughout the life course. The activity rate of those with higher education exceeds 80% practically everywhere in Europe, whereas the corresponding figure in the case of people with only primary education is less than 40%. Considering the looming demographic imbalances we face, we surely cannot afford large skill deficits. High school-dropout rates provide a good indicator of the welfare deficit we face (above 30% in Spain, almost 25% in the Netherlands and less than 15% in Denmark and Sweden). While inequalities are widening in the knowledge economy, this also implies that parents' ability to invest in their children's fortunes is becoming more unequal. Everyone's favourite solution is, of course, education. The revitalisation of both the Irish and the Finnish economies is in part based on increased investments in education, preventing early departure from formal education and training, and facilitating the transition from school to work, in particular that of school-leavers with low qualifications. Social and employment policies aimed at developing the quality of human resources for the knowledge economy assume the role of social investments.

Distributive recalibration concerns the rebalancing of social protection provisions across policy clienteles, stakeholder interests, and public and private resources. Many of the so-called 'new social risks', like family formation, divorce, the elderly becoming dependent on care, declining fertility and accelerating population ageing are primarily borne by young people and young families, signifying a shift in social risks from the elderly to the young. However, the new risk-bearers lack critical social and political influence. Their ability to exert electoral and extra-parliamentary pressure is limited by the fact that, for most people, exposure to new social risks is a transitory phase of the family life course, concerned with child-rearing, care for the elderly, or labour market entry and exit (Taylor-Gooby, 2004).

The interaction between economic performance and the welfare state is largely mediated through the labour market. The majority of Europe's mature welfare states are confronted with a syndrome of labour market segmentation between 'insiders' and 'outsiders'. As family and gender issues remained secondary in the reform momentum of the 1980s and 1990s, post-industrial social and economic change seems to perversely reinforce an over-accumulation of insurance benefits on the side of 'guaranteed' breadwinner workers with quasi-tenured jobs, alongside inadequate protection for those employed in the weaker sectors of the labour market, particularly young people, women, immigrants and older low-skilled workers. Most likely, labour markets will become ever more flexible. While the boundaries between being 'in' and 'out' of work have been blurred by increases in atypical work, low-wages, subsidised jobs and training programs, one job is no longer enough to keep low-income families out of poverty. Post-industrial job growth is highly biased in favour of high-skilled jobs. However, increased labour market flexibility, together with the continuing rise in female employment will, in addition, also encourage the growth of a sizeable amount of low-skilled and semi-skilled jobs in the social sector and in personal services. The policy challenge is how to mitigate the emergence of new forms of labour market segmentation through what could be called 'preventive employability', combining increases in the flexibility of labour relations by way of relaxing dismissal protection while generating a higher level of security for employees in flexible jobs. Flexible working conditions are often part and parcel of family-friendly employment policy provisions. There is a clear relation between the ratio of part-time jobs and female employment growth. But the ability of part-time employment to harmonise careers with family depends very much on employment regulation, that is, whether part-time work is recognised as a regular job with basic social insurance participation, and on whether it offers possibilities for career mobility.

Special attention should also be given to the labour market problems of migrants and non-EU nationals, whose rate of unemployment averages twice that of EU nationals. Skills, cultural and language barriers, and discrimination together call for a real improvement in integration policies, including access to social citizenship. In our ethnically and culturally diversified societies, the welfare state faces the major challenge of ensuring that immigrants and their children do not fall behind. The recent outbreak of violence in the banlieus of the metropolitan cities of France reveals how economic exclusion and physical concentration reinforce educational underperformance, excessive segregation and self-destructive spirals of marginalisation. The overriding policy lesson is that in the face of demographic ageing and in the light of a declining workforce, nobody can be left inactive (for long)!

The combination of late entry into the labour market by young people, early exit by older workers and higher life expectancy translates into a looming financing deficit for the welfare state. Most European pension regimes are both inequitable and ineffective, and are also replete with early exit measures defended by labour market insiders. Ageing is a challenge but also a blessing, since people live longer in good health. Two trends justify adjustment of retirement regimes: a) the health status of each elderly cohort is better than that of the last; at present a man aged 65 can look forward to another ten healthy years; and b) the skill gap between the elderly and the young is rapidly narrowing. Older people in the future will be much better educationally prepared than now to adapt to the knowledge economy with the aid of retraining and lifelong learning. Beyond the development of multipillar systems, including both PAYGO (pay-as-you-go) and funded schemes, in the area of pension policy, the challenge lies in how to allocate the additional expenditure that inevitably accompanies population ageing (Myles, 2002). Of crucial importance in terms of equity remain first-tier pension guarantees financed from general revenue and indexed to prices for when the next generation of flexible labour market cohorts start to retire. The provision of sustainable pensions requires that we raise the employment rates of older workers and increase retirement age to 67. Later retirement is both effective and equitable. It is efficient because it creates both more revenue intake and less spending at the same time. It is intergenerationally equitable because both retirees and workers contribute in equal proportions. Flexible retirement and the introduction of incentives to postpone retirement could also greatly alleviate the pension burden. Although there has been a slight increase of part-time work among the elderly and it has been shown that part-time work and participation rates among older people are positively related, there is still little systematic and comprehensive policy activity to enhance the variable opportunity set for older workers. If older workers remain employed for ten years longer than is now the norm in early-exit welfare regimes, household incomes will increase substantially, which implies less poverty, less spending on social assistance and greater government revenue.

Normative recalibration concerns the norms and values implicated in the dilemmas emerging from the search for functionally effective and distributively fair policy proposals. Protecting the vulnerable and preventing the disadvantaged from becoming vulnerable lay at the heart of the normative underpinning of the post-war welfare state. Politically, the more reform proposals alter the distributive balance between groups and vested interests, the more important it is, of course, to put forward and elaborate new normative frameworks and discourses capable of advocating the reform agenda as a 'win-win' project, i.e. of justifying reform in terms of underlying 'moral foundations' (Vandenbroucke, 2002). The normative philosophy behind recent labour market reforms is one of reciprocal obligations. Welfare recipients must be obliged to accept employment or training in order to receive benefits, while the state has the obligation to enhance the employability of benefit claimants. Raising female participation in the labour market is also an issue of gender equality and social justice.

A number of policy analysts today advocate 'dynamising' Rawls' theory of social justice (Esping-Andersen et al., 2002; Ferrera/Hemerijck/Rhodes, 2000). They suggest a tentative shift in emphasis in the normative debate away from a static notion of distributive justice, focused on here-and-now redistribution, and towards a dynamic social-liberal notion of restoring equality of opportunity across the life course. This implies a reorientation in social citizenship, away from freedom from want towards freedom to act, while continuing to guarantee a rich social minimum. Redistribution, for example through progressive taxation, remains important. These authors also advocate modern social policy as a societal investment, mobilising the developmental capabilities of citizens to achieve self-reliance under post-industrial conditions, rather than as income-replacing compensation for industrial market failures. Esping-Andersen seeks inspiration in John Rawls' 'difference principle', which stipulates that substantial changes in the social status of citizens must be to the greatest advantage of the worst off (Rawls, 1971). Rawlsian ideas of social justice are primarily pertinent with respect to market inequalities. John Myles has argued that the elaboration of a new normative framework of distributive fairness, touching on norms of intergenerational equity and intragenerational justice, is particularly urgent in the field of old-age policy. Intergenerational equity, he maintains, implies that the transition costs associated with population ageing be proportionately shared by both young and old. In agreement with Rawls' difference principle, pension reform should thus be to the advantage (or to the least possible disadvantage) of the worst off within both the working and the retired population (Myles, 2002). Ronald Dworkin has forcefully argued that considerations of distributive fairness should take account both of the social circumstances that produce inequalities in living conditions and of the family and individual choices that affect life chances (Dworkin, 2000). To the extent to which the emergent new social risk profiles cut across the boundaries between the public and private spheres, they raise pressing normative questions about individual, family, social and public responsibilities (Schmidt, 2005). The normative position of Amartya Sen is rooted in his concept of capabilities (Sen, 1985; 2001). For Sen, material equality is at best a necessary but not a sufficient condition for a fair distribution of life chances. What is decisive is the ability of citizens to convert the resources available to them into living conditions they themselves aspire to. Sen's normative view corresponds with a more flexible endowment of resources, which may be unevenly distributed but nevertheless enable individual citizens to realise their own life plans. From the perspective of social capabilities, active participation in employment is of crucial importance because participation in social life through employment relations is vital for gaining respect from others as well as self-respect in post-industrial societies (Salais, 2003). Following the logic of Sen's capability approach, Günther Schmid advocates labour market policy interventions to empower citizens to act as autonomous agents and, especially, to allow for choice between different employment statuses according to shifting preferences and circumstances during the life course (Schmid, 2005; Schmid/Gazier, 2002). Having the opportunity to change these plans and to make transitions between various kinds of employment, for instance between part-time and full-time work, or dependent work and self-employment or a combination of both, without repeated disruptions, is important in the face of economic internationalisation and post-industrial differentiation. The normative focus of social policy hereby shifts from ex post redistribution towards preventive or ex ante employability. Wolfgang Streeck views the new 'asset-based' discourse of social justice in terms of 'supply-side egalitarianism' given that it hinges on the deployment of resources to improve and equalise citizens' individual abilities to compete in the knowledge economy (Streeck, 1999). Greater flexibility and widespread low-wage employment is likely to increase relative poverty and overall economic insecurity for sizeable groups in the population. An unchecked rise in income inequality will worsen citizens' life chances and opportunities. As a consequence, it is impossible to avoid some form of (passive) minimum income support. Temporary inequalities, low wages and poor jobs are less problematic than long-term poverty and inactivity traps. They become problematic when they negatively affect opportunities for future life chances on a structural basis. It is therefore necessary to have an even more tightly woven net below the welfare net for the truly needy to meet minimum standards of self-reliance.

Institutional recalibration concerns reforms in the design of institutions, levels of decision-making, and social and economic policy governance, including the separate and joint responsibilities of individuals, states, markets and families. One of the most distinctive institutional features of the European welfare state has been its public legalistic nature: the responsibility of ensuring social solidarity and cohesion has ultimately relied on national (i.e., central) government in terms of policy formation, funding, administration and implementation. Various developments have been challenging this state-centric edifice of the welfare state in recent years — a challenge often summarised in the emergence of new forms of 'governance' beyond the traditional territorial nation-state. The ongoing redefinition of the role of the state with respect to welfare provision is apparent in three ways (Supiot, 2001). The inevitable failure to deliver diversified public goods and decentralised services in turn triggers popular discontent with the public sector; hence the need for policy change and innovation and experimentation with new forms of public and private service provision in childcare, education and training, and professional care for the elderly. As a consequence, national governments no longer hierarchically monopolise welfare provision. Diversified demand in the face of tight budgets makes it increasingly difficult for governments to apply uniform rules and procedures to welfare servicing. Customisation of welfare provision to meet individual needs with transfers and services goes together with institutional devolution, decentralisation, liberalisation and privatisation. Many countries (especially the larger ones) have been experimenting with decentralisation of competencies to subnational (regional and local) governments. Markets and families have gained greater responsibility and community-based 'third sector' associations have been called on to deliver new services. From a horizontal perspective, there is an increasing recognition that effective social policy formation and implementation today requires 'joined up' governance across government departments, public agencies, private-sector organisations and community associations, together with more effective forms of policy coordination across various functionally differentiated policy areas of activation, social protection, family services and housing. Last but not least, the EU has in recent years emerged as an autonomous supranational body of social regulation and to some extent redistribution (through the structural funds), creating additional layers of multilevel governance, to which I now turn.

5 Beyond the 'double bind' of social Europe

The negative outcomes in France and the Netherlands of the 2005 referenda on the Constitutional Treaty are indicative of the 'growing pains' of the shift from an elite-driven diplomatic to a broader political EU. The rejection of the Constitutional Treaty by French and Dutch voters evidenced discontent about globalisation, unease over immigration and resistance to the prospect of Turkey joining the EU in the near future — this against the background of a stagnating euro-zone economy (Wallace, 2005). The Single Market, EMU and the SGP, which started out as a path-breaking structural policy reform of enhanced European economic cooperation, potentially putting long-term growth and stability structurally on a higher plane, are increasingly seen as a set of constraints that undermine domestic room for manoeuvre. To be sure, the countries that stayed out of the first round of EMU — the United Kingdom, Sweden and Denmark — are faring much better. However, the current legitimacy crisis of the EU is not merely a problem of economic performance; it is a crisis of political leadership and policy engagement. Domestic political elites from Left to Right have been all too happy since the adoption of the Single Market to scapegoat the EU for painful reforms. Hereby they fed popular discontent against the new Constitution which they themselves eventually supported. Now that the public genie is out of the bottle, it is impossible to go back to the status quo ex ante of elite-driven technocratic European integration with the Commission in the driver's seat, supported only haphazardly by Member States governments. In order to counter the tendencies of Europe's national political economies to become inward-looking, protectionist and xenophobic, nostalgically glorifying the past successes of their sovereign national welfare state, EU political leaders are required to develop a policy vision on social progress that European citizens can support. Without a social agenda, the EU will not get the support for much-needed reforms at the level of the national state over pension and services at the level of the EU. The EU affects domestic welfare policy repertoires essentially through four avenues of intervention:

- 'Community method' legislation within the framework of the internal market, such as health and safety and equal opportunities legislation;
- Macroeconomic constraints for the euro zone agreed to in the context of EMU and the SGP;
- Jurisprudence of the European Court of Justice based on case law, largely derived from market compatibility requirements;
- Agenda-setting policy coordination through the articulation of common challenges, the joint diagnosis of new social risks and the identification of potentially effective domestic policy solutions to emerging European social problems.

EU social and economic policy coordination can be broadly characterised along two dimensions. First, there is the relevance of cross-border risk-pooling through binding legislation against unruly competition through the well-known 'Community method'. Second, in their central role as agenda-setters, EU institutions can help diagnose the nature and magnitude of the fundamental challenges and identify potentially effective policy solutions to these challenges. Although the relationship between these two dimensions of EU policy coordination goes beyond mere overlap and coexistence, in the academic debate over the future of 'social Europe', these two forms of policy coordination are more often than not seen as *alternatives* rather than *complements*.

Leading scholars, most notably Wolfgang Streeck (1995) and Fritz Scharpf (1999), have argued that the Single Market and the introduction of EMU, in the wake of successive rounds of enlargement, are exemplary for the overall tendency of 'uneven growth' between the EU's economic and social policies. The latter, market-correcting 'positive integration' has been unable to keep up with the market-expanding logic of 'negative integration': 'the removal of tariffs, quantitative restrictions, and other barriers to trade or obstacles to free and undistorted competition' (Scharpf, 1999: 50−52). On this pessimistic reading, European welfare states face the predicament of a 'double bind'. On the one hand, Member States are unlikely to shed their welfare-state obligations as this would jeopardise the political base of their legitimacy. On the other hand, EU Member States have, since the mid-1980s, become irreversibly committed to a pervasive program of European economic integration. In the face of this 'double bind', national policy-makers cannot want to shed their welfare-state functions without jeopardising the territorial bases of their political legitimacy, while at the same time they cannot want to reverse the process of economic integration, which increasingly exposes their now semi-sovereign welfare states to regulatory competition. The double bind presents national and EU-level policy-makers with a thorny dilemma: common European solutions are desirable, but neither feasible nor effective on account of national interests, political sensitivities and the huge diversity of social security systems in an EU of 25 members (Scharpf, 2002).

The logic of the 'double bind', arguing from a more voluntarist standpoint, can however be turned into a 'double engagement'. This arises out of a corollary to Europeanisation. Domestic adjustment problems resulting from economic integration can trigger political spillovers that drive consecutive rounds of EU policy initiatives — pressed for by domestic policy-makers — to deal with the unintended consequences of the first round of liberalisation. Such spillovers create the political space for 'uploading' social policy considerations to the level of the EU. The spectre of competitive welfare retrenchment due to the predominance of 'negative integration' can thus serve as a critical trigger (and hence intellectual resource) for progressive EU and domestic policy-makers, encouraging them to engage in 'positive coordination' to constructively recalibrate national welfare regimes and the European social policy agenda. The remarkable resurgence — alluded to earlier — of 'social pacts' across the EU in the 1990s is exemplary of the logic of 'double engagement' at the domestic level. Following this line of reasoning, Maurizio Ferrera and Elisabetta Gualmini (2000) go so far as to claim that EMU in effect saved the Italian welfare state from complete ungovernability. At the level of the EU, the introduction of a separate employment chapter in the Treaty of Amsterdam provided for a new European political space for 'double engagement'. The European Employment Strategy, later dubbed the 'Luxembourg process', was accepted on condition that no national authority would be transferred to Brussels, there would be no extra cost, and EMU rules would be fully respected. Likewise, in committing the EU to become the 'most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth and more and better jobs and greater social cohesion', the Lisbon summit in March 2000 put forward an integrated agenda of economic, employment and social objectives, helping EU economies to perform better, while contributing to social cohesion and political stability. In terms of institutional innovation, the European Council at Lisbon formally recognised the Open Method of Coordination (OMC) as a new form of European governance, based on common guidelines to be translated into national policy, combined with periodic monitoring, evaluation and peer review organised as learning processes and accompanied by indicators as a means of comparing best practices. Since the introduction of the employment strategy in Luxembourg, OMC has quickly spread to other social policy areas, such as social inclusion (2000), pensions (2001) and health care (since 2004). In terms of substance, open coordination processes strongly focus on 'new' rather than 'old' social risk categories, most notably active ageing or avoiding early retirement, part-time work, lifelong learning, parental leave, gender mainstreaming, flexicurity (balancing flexibility with security), reconciling work and family life, and social exclusion (Zeitlin, 2005).

Open coordination, if given more EU political clout and national commitment, can play a key role in ongoing processes of welfare recalibration. OMC provides for an institutional space for mutual learning and deliberative problem-solving, generating new cognitive, normative and practical input for defining an overlapping consensus on EU objectives and ambitions concerning social and economic performance, but not specific national programs and institutions. The tie that binds the open method is not so much values, policies or institutional structures, but rather a common identity defined in terms of problems. OMC is flexible and incremental and recognises national differences, which makes it easier to achieve agreement on policy redirection; it allows for change and in fact anticipates change by encouraging feedback, policy learning and lesson-drawing (Maher, 2004). Through OMC persistent heterogeneity may be exploited for purposes of experimentation and innovation. By diagnosing common European challenges and identifying promising policy approaches through information pooling, OMC induces Member States to re-assess, re-evaluate, and re-examine policy performance and established policy approaches in comparison with other countries under the political pressure 'to get something done' on urgent social questions in the face of increasing economic interdependencies (Zeitlin, 2005). OMC is extremely useful for creating a climate where policy change is possible without triggering social or political unrest. In its respect for national political traditions and policy legacies, OMC could enhance the legitimacy of the EU as a social union. It serves both substantive EU objectives for work and welfare and more ambitious national reform strategies. But the real beauty of OMC is that it helps us to focus on reform beyond the formalism of the traditional Community method, which so often only serves to obfuscate reform. OMC is about a 'doubly engaging' policy process par excellence in that it seeks to interlink domestic policy-making and EU coordination, combining common action and national autonomy beyond the traditional and inflexible Community method and the rather formal and defensive deployment of the subsidiarity and proportionality principles in EU policy-making. In effect, OMC signals a shift towards a richer and more constructive notion of subsidiarity.

In practice, however, OMC processes are far from perfect. Especially, the method's degree of 'openness' in terms of political exposure and commitment, together with the lack of substantive focus, should be criticised. OMC practices are particularly poorly integrated in domestic policy processes; public awareness, media coverage and parliamentary overview remain poorly developed. The role of the European Parliament so far has been only considered in strictly advisory terms, while, more seriously, national parliaments have let themselves be marginalised in the process. Open coordination is dominated by a new class of higher civil servants and EU officials. These problems of political accountability have not been compensated (enough) by other mechanisms of civil society articulation and representation. To be sure, without substantive consensus or common concerns and a sense of urgency for cross-national problem-solving, there is the danger that OMC will end up as a ritual of 'dressing up' existing policy legacies. Taking heed of the Sapir report on economic growth (Sapir et al., 2003) and the Kok reports on employment (Kok et al., 2003) and the Lisbon strategy (Kok et al., 2004), there is a clear need to refocus the Lisbon agenda, urging national governments to act together and go beyond defending the vested interests of their now semi-sovereign welfare states. A greater focus on growth, employment and social cohesion in a three-year sequence may be sufficient to render processes of open coordination less opaque and to facilitate better coordination across policy sectors both at EU and national levels.

6 The imperative social pragmatism

Welfare state futures are not preordained. Neither the doomsday scenario of the demise of the European welfare state, predicted by economists in the 1980s, nor the prevalent image of a 'frozen welfare status quo', pictured by comparative scholarship in the 1990s, can be corroborated by the European welfare reform experience since the late 1970s. In the 1980s, welfare provisions became more austere. Since the mid-1990s, we can observe an incipient process of 'contingent convergence' of employment and social policy objectives and the adoption of increasingly similar policy initiatives (encouraged also by the deepening of the EU social agenda), signalling a transition from a corrective and passive welfare state to a more proactive social investment strategy, with much greater attention being paid to prevention, activation and social servicing. In hindsight, it seems that in their efforts to repair the increasingly dysfunctional policy repertoires of the golden age, domestic and EU policy-makers, pressed by intensified economic internationalisation and post-industrial differentiation, under conditions of permanent austerity have turned to combining elements from different welfare regimes. In their different attempts to achieve greater efficiency and equity, we can observe a trend of welfare hybridisation, based on domestic policy experimentation and processes of cross-national social learning. The EU, as an institution that spans national boundaries, herein provides a vital additional exploratory space for cross-national agenda-setting, benchmarking of policy performances and sharing of domestic policy reform experiences. European welfare states are no longer closed systems; they are increasingly open, evolutionary systems that are inhabited by agents who learn and constantly apply the lessons of domestic experience and EU social and economic policy coordination. Over the past decade, EU social policy-makers have reluctantly given up their first-order preference for the administrative 'one-size-fits-all" routines of the Community method, directed towards binding social and labour standards, and, as a consequence, have been rather slow to endorse what are in their view second-best, voluntarist processes of open coordination and social dialogue, involving both domestic and EU policy-makers in monitoring progress, diffusing best practices, and redefining common concerns and shared social and economic objectives. And given that community legislation will inevitably become more difficult in a more heterogeneous EU of 25 Member States, social progress will have to rely more on horizontal EU social dialogue and the 'soft law' processes of the open method of coordination so as to balance common concerns and legitimate diversity. To be sure, the image of 'doubly engaging' welfare recalibration has been placed in jeopardy by the loss in commitment to the Lisbon momentum, and also in the light of the French and Dutch referendum outcomes. Processes of open coordination have to become more overtly political by introducing robust democratic parameters. In the highly charged political context of today, 'one-size-fits-all' directives from Brussels, for example on weekly working hours, are surely not the way forward. The EU should stimulate more daring forays into two-way political engagement over an ambitious policy agenda endorsed by the European Council and the Member States. Social progress in the EU has to be built on the politics of 'double engagement".

Despite the imperative of 'double engagement', social policy reform essentially remains a domestic enterprise: reforms have to be endorsed by elected governments and national political parties (preferably supported by key organised interests) and implemented through domestic administrative structures. By the same token, processes of welfare recalibration certainly do not require a search for a 'blank-slate' new model, a radically novel blueprint to replace the social and economic policy repertoires that exist at national level. We live in a world of path-dependent solutions. Reform, even radical policy change, does take place, but it is 'institutionally bounded' change. Any attempt to measure social and economic performance is critically dependent on identifying the particular institutional conditions under which it is possible to formulate and implement effective and equitable policies. The interaction between economic performance and welfare policy is far too complex and dynamic to allow for simple remedies and quick fixes. The analysis of social policy as an investment resource thus relies heavily on sophisticated understandings of the modus operandi of the welfare state, which are more complex than those supported by neoliberal orthodoxy; the latter, at best, views social policy as necessary side-payments to groups adversely affected by economic restructuring. But in contrast to the possible adverse effects of social policy on economic performance, the reasoning behind the idea of social policy as an investment occupies a difficult intellectual and political position. Although comprehensive welfare states are surely not economically dysfunctional, there are social policies that do have a negative impact on economic processes, like excessively generous social benefits not backed by activating labour market policies. We always need to consider the 'fine' structures of the welfare state in conjunction with inside and outside policy pressures. This also makes the political nature of policy prescriptions eminently conditional.

Welfare reform is a political process that involves the strategic framing of policy problems and solutions by political actors and interests. Reforms are the products of lengthy processes of (re-)negotiation between political parties, governments and often also the social partners. In order to gain political legitimacy for promising new policy formulas, political entrepreneurs wishing to put novel policy alternatives on the political agenda are pressed to elaborate new normative priorities (or to redefine old ones) and to communicate their (novel) cognitive insights regarding the challenges ahead in a publicly compelling manner so as to convert current anxieties over economic internationalisation, post-industrial differentiation and conditions of permanent austerity into a more mobilising pursuit of policy priorities and political ambitions. Following the logic of Sen's capability approach, the policy priorities listed above concern policy interventions to empower citizens to act as autonomous agents, and, especially, to allow for choice between different employment statuses according to shifting preferences and circumstances during the life course (Schmid, 2005; Sen, 2001).

Necessary investments in family services, education and training, subsidised employment, labour market integration for immigrants, decent basic pensions and adequate minimum income protection do come with a price ticket. However, in the medium term, the gains are very likely to outweigh the initial costs of the social investment strategy. Moreover, investments in (public and private) social services also provide job opportunities, especially for women, older workers, young people and immigrants. And in increasing the volume and improving the quality of the workforce, high-return investments support economic growth. This, in turn, generates additional government revenue, which ultimately contributes to the long-term sustainability of the European welfare state.

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