Ackerman, Frank. "Overview Essay: Responses to Inequality: The Welfare State," Part X, Frontier Issues in Economic Thought, Volume 5: The Political Economy of Inequality. Island Press: Washington, D.C. 2000. pp.327-339.

Social Science Library: Frontier Thinking in Sustainable Development and Human Well-being

"Responses to Inequality: The Welfare State" by Frank Ackerman

The degree of inequality that would be created by an unfettered market economy is unacceptable to almost everyone. In every developed country, and many developing countries as well, the government engages in large-scale intervention in the market to promote some aspects of equality. Among the most common forms of intervention are public pensions for retirees, free or subsidized medical care, unemployment benefits, and progressive taxation; in the most ambitious cases, these measures are joined by many more government programs and initiatives aimed at increasing equality.

Is this the solution to the problems of inequality? If we dislike the distribution of resources achieved by the market, can we simply vote to have the government change it? In a more optimistic and expansive era, such as the 1960s and 1970s, the affirmative answer to these questions might have been taken for granted. The last two decades of the twentieth century however, were a time of growing pessimism, cutbacks, and conservatism. The new conventional wisdom suggested that little could or should be done to modify the market allocation of resources. As a cynic said, referring to one of the celebrated liberal initiatives of the 1960s, "America fought a war on poverty, and poverty won."

In the short run, there was a partisan political explanation for the reversal. Poverty and inequality won the war, in the Anglo-American context, because the politicians of the Reagan and Thatcher administrations decided to surrender, if not switch sides, in the 1980s. Yet the retreat from government activism has outlasted those politicians, and has reached beyond the U.S. and the U.K. The critique of the welfare state is often presented, not as a political choice, but as an economic necessity. In a time of greater global competition and slower growth, it is claimed that even the richest countries can no longer afford the high levels of interference with the market that they have previously indulged in. Growth and employment are said to depend on efficiency, which requires minimization of costs and elimination of market distortions. Adherence to this doctrine compels endless efforts to cut back taxes and benefits, to make national economies lean and mean enough to endure.

This point of view is sure to cause discomfort among those who are concerned about equality. In fact, if our goal is greater equality, there is no comprehensive alternative to political action. Private bargaining between unequal parties in the marketplace will inevitably lead to

Reprinted with permission from Island Press, © 2000

unequal outcomes. Organization of unions or other grassroots initiatives to gain economic power, while essential, is a slow and difficult process – and if it succeeds, it will surely rely on the government to preserve and strengthen its gains. Thus if we care about equality, we need to recreate an economics that legitimizes government intervention and activism, and critiques the pessimism of the recent past. That is, we must explain what is wrong with the new economic orthodoxy of the late twentieth century, the prescription that movement toward laissez-faire is the best medicine for so many different diseases.

This essay begins with a look at the theoretical grounds for supporting government activism. It then presents a typology of different welfare state models, followed by a more detailed examination of the polar cases of Sweden and the U.S. The final section returns to the nature of the trade-offs involved in social welfare programs.

THEORIZING INTERVENTION

A good place to start in developing a theory of government intervention is the recent review article, "Does Egalitarianism Have a Future?" (Louis Putterman, John E. Roemer and Joaquim Silvestre 1998). Putterman et al. offer a critique of the way that economic theory treats the issue of equality, on many levels (only a few of which are mentioned here). The textbook notion that maximum efficiency is always desirable depends on the implausible assumption that distribution can be handled separately in a subsequent transaction: once the economy has reached its peak output, a hypothetical set of "lump-sum" transfers supposedly could achieve any preferred income distribution, without reducing efficiency. Since these hypothetical transfers never occur, and are in fact politically and organizationally impossible, economic theory cannot rely on them to solve (or dissolve) the question of distribution.

On a more practical level, Putterman et al. cite reviews of empirical research suggesting that the disincentive effects of welfare state benefits and taxes are relatively small. Nor is it obvious that removing all taxes and benefits would lead to a more ideal economy. There are, for example, large negative environmental externalities from many economic activities; taxing pollution and other undesirable environmental activities would lead to better, not worse, economic outcomes.

There are also institutional barriers to economic efficiency that result from extremely unequal distribution of resources, suggesting that some forms of government intervention can increase efficiency. To cite an example from more agrarian societies, land reform has frequently led to an increase in agricultural investment and output, due to the incentive effect of giving former tenant farmers an ownership stake in their farms. The same might be true for tenants in large-scale public or absentee-owned housing developments in major cities. More broadly speaking, public policies that guarantee an income floor or equalize access to credit may encourage low-income individuals to take more desirable economic initiatives – investing in their own education, or in new business ventures, for example.

The institutional and informational limitations that constrain the market are a major theme in the work of Joseph Stiglitz. In his interesting reflections on the failure of Soviet planning (Stiglitz 1994), he argues that the same limitations were even more problematical for

Reprinted with permission from Island Press, © 2000

socialism. Indeed, according to Stiglitz, if a perfectly competitive market economy were possible, then market socialism would also be possible, and might be preferable to private ownership. The private market succeeds, in his view, not because it is perfect or even perfectible, but because it deals with imperfections in a manner that is somewhat less bad than the alternatives.

However, in an economy characterized by limited information, institutional barriers, and unfortunate incentives, it is easy to see that the textbook theorems about general equilibrium fail, implying that market outcomes may be neither equitable nor efficient. Consequently, some forms of government intervention can lead to simultaneous improvement in both equity and efficiency (Stiglitz 1991). There is a vast literature on the unrealism and impossibility of general equilibrium (too vast for comprehensive citation; my own contribution is Ackerman 1999), all of which at least indirectly supports the idea that government activism could make market outcomes better rather than worse.

A similar theoretical perspective, more directly focused on the welfare state, is provided by Nicholas Barr (1992). The traditional economic justification for the welfare state, as explained by Barr, is that it arises in response to market failures in the areas of risk and insurance. The private market is incapable of providing affordable health insurance to all regardless of congenital defects or pre-existing illnesses; it cannot provide insurance against income loss due to cyclical unemployment, except for narrowly defined, low-risk groups; it cannot guarantee the real value of pension payments in the face of uncertain levels of inflation. Because people want these and other guarantees and services that the private sector cannot offer, they inevitably turn to the state. That is to say, some of the things that people want are universal guarantees of well-being, which are structurally so different from commodities that there is no possible private sector supplier.

Once the fabric of market optimality begins to unravel, there are many loose threads that can be pulled on. Consider the common belief that regulation of prices or quantities always makes market outcomes worse. A counterexample to this misleading bit of conventional wisdom is found in the analysis of minimum wage legislation by **David Card and Alan Krueger**. Economists are nearly unanimous in believing that minimum wage laws reduce unemployment, based largely on a priori reasoning from the simplest model of labor supply and demand. In their book, Card and Krueger describe extensive empirical evidence that is inconsistent with this conclusion, repeatedly finding either no change or a slight increase in employment due to increases in the minimum wage.

The chapter summarized here offers a theoretical explanation: to oversimplify slightly, the U.S. minimum wage is so low that it provides little incentive to work hard or remain on the job. So when fast food restaurants are forced to pay slightly more, they attract more and better motivated workers, and slow down their rapid rate of employee turnover. In an extended and somewhat critical review of Card and Krueger, John Kennan (1995) claims that their data is ambiguous and frequently mis-specified, rendering it difficult to draw any clear empirical conclusions. However, Kennan agrees that there is no large employment effect (and often no

Reprinted with permission from Island Press, © 2000

significant effect at all) of minimum wage changes, in essence supporting a modest version of Card and Krueger's key point.

THREE VARIETIES OF THE WELFARE STATE

Turning from theory to reality, it is clear that there is a widespread perception of crisis in the modern welfare state. Pressure for cutbacks has proved irresistible in one country after another. A major comparative study, directed by Gøsta Esping-Andersen, examines the problems and responses of welfare state policies in the 1990s in seven different regions of the world (Esping-Andersen 1996). As in his earlier work (e.g., Esping-Andersen 1990), Esping-Andersen emphasizes that there is nothing inevitable about the development of public policies for health, education, and welfare. Different countries at comparable levels of economic development have quite different levels and styles of services, growing out of their distinct political histories. As shown in Table 10.1, public social security and health expenditures in 1990 ranged from about one-seventh of gross domestic product (GDP) in the United States to one-third in Sweden. In many countries there was a moderate increase in these expenditures during the 1980s.

Table X.1. Public Social Security and Health Expenditures

	Public social security and health expenditure as a percentage of gross domestic product	
	1980	1990
Canada (1982 and 1990)	17.3	18.8
Denmark	26.0	27.8
France	23.9	26.5
Germany	25.4	23.5
Netherlands	27.2	28.8
Norway	21.4	28.7
Sweden	32.4	33.1
United Kingdom	14.1	14.6

Source: Excerpted from Table 1.1, page 11 (based on OECD data), in Gøsta Esping-Anderson, ed., *Welfare States in Transition: National Adaptations in Global Economies*. London: SAGE Publications, 1996.

There are some common roots (as well as divergent branches) to the budgetary crises facing the social welfare programs of many countries in the 1990s or earlier. Slower economic growth has reduced tax revenues and increased the need for income supports. The aging of the population throughout the developed world – which is most acute in Japan and in southern Europe – increases the cost of pensions and medical care. Growing numbers of single mothers and other nontraditional household structures create a demand for new services and programs. Yet none of this has led to wholesale abandonment of past approaches. When faced with a budgetary crisis, most countries make only marginal adjustments in the type of social welfare they provide for their citizens. Drastic changes in political philosophy are largely confined to the cases of abrupt overthrow of a regime, as in the end of the Soviet era, or earlier in Chile.

Reprinted with permission from Island Press, © 2000

Esping-Andersen's widely cited typology of the varieties of welfare states divides most developed countries into three groups:

- the Anglo-Saxon countries (Britain, U.S., Canada, Australia, New Zealand), where "neo-liberal" or "residual" programs rely largely on limited, means-tested benefits and modest social insurance plans;
- continental Europe (Germany, France, Italy, and others), where "corporativist" programs provide a high level of job security and social insurance, but do little to find jobs for the unemployed, or to provide family-oriented benefits such as child care; and
- Scandinavia, where the "universal" approach to social welfare combines a high level of income maintenance and wage equality with active labor market policies, social service expansion, and gender equalization.

The three varieties of welfare states have measurably different effects in reducing poverty. Table 10.2 contrasts the extent of poverty both before and after government intervention in 15 developed countries. The data for this and many other international comparisons comes from the Luxembourg Income Study, a massive compilation of comparable economic and demographic data for different countries. In Table 10.2, the columns labeled "Pre" show the extent of poverty based on pre-tax, pre-transfer incomes – that is, poverty that would have occurred based on market incomes alone. The columns labeled "Post" present the corresponding poverty rates based on post-tax, post-transfer incomes – that is, actual poverty based on household incomes after government intervention. The "Change" columns are the difference between Pre and Post, or the percentage reduction in poverty rates achieved by taxes and transfers.

Reprinted with permission from Island Press, © 2000

Table X.2. Impact of Taxes and Transfers on Poverty Rates

	All persons				Children		
	Year	Pre*	Post*	Change (%)	Pre*	Post*	Change (%)
United States	1994	26.7	19.1	–28.5%	28.7%	24.9%	–13.2%
Australia	1989	23.2	12.9	–44.4	20.5	15.4	–24.9
Canada	1991	23.4	11.7	–50.0	22.7	15.3	–32.6
United Kingdom	1991	29.2	14.6	–50.0	28.7	18.5	–35.5
Finland	1991	15.6	6.2	–60.3	11.6	2.7	–76.7
Spain	1990	28.2	10.4	–63.1	20.7	12.8	–38.2
Ireland	1987	30.3	11.1	–63.4	30.3	13.8	–54.5
Italy	1991	18.4	6.5	–64.7	11.0	10.5	–4.5
France	1984	21.6	7.5	–65.3	27.4	7.4	–73.0
Germany (W.)	1989	22.0	7.6	–65.5	11.7	8.6	–26.5
Norway	1991	21.8	6.6	–69.6	12.7	4.9	–61.4
Netherlands	1991	22.8	6.7	–70.6	15.2	8.3	–45.4
Denmark	1992	26.9	7.5	–72.1	17.1	5.1	–70.2
Sweden	1992	34.1	6.7	–80.4	18.4	3.0	–83.7
Belgium	1992	28.4	5.5	–80.6	17.2	4.4	–74.4

*"Pre" means poverty rate based on pre-tax, pre-transfer income; "post" means poverty rate based on post-tax, post-transfer income. In both cases, poverty is defined as 50% of each country's median income, adjusted for household size.

Countires are listed in order of the change in poverty of all persons.

Source: *State of Working America*. Excerpted from Table 8.15, page 377 in Gøsta Esping-Anderson, ed., *Welfare States in Transition: National Adaptations in Global Economies*. London: SAGE Publications, 1996.

In addition to documenting the dismal U.S. performance, the table illuminates two aspects of Esping-Andersen's typology. First, the Anglo-Saxon countries accomplished the least in overall poverty reduction; and second, the Scandinavian countries did far better than some (not all) other European countries in reducing child poverty.

Specifically, the welfare state achieved a mere 28% reduction in overall poverty in the U.S., by far the worst performance in any of the 15 countries. The other Anglo-Saxon countries, Australia, Canada, and the United Kingdom, reduced overall poverty by 44-50%, more than in the U.S. but less than in any of the other European nations, where 60-80% of poverty was eliminated by government intervention. Sweden would have had the highest rate of overall poverty in the absence of the welfare state, but it also had one of the highest rates of poverty reduction.

In terms of reduction in child poverty, the picture is somewhat different. The U.S. lifted only 13% of pre-tax-and-transfer poor children across the poverty line. Italy did worse in percentage terms, though it had the lowest level of pre-tax-and-transfer child poverty. In all the other countries, taxes and transfers reduced child poverty by at least one-fourth. However, Germany (and Italy) did no better than the other Anglo-Saxon countries, while the four Scandinavian countries, France, and Belgium each eliminated more than 60% of child poverty.

Reprinted with permission from Island Press, © 2000

Among Esping-Andersen's three models, the continental European one is perhaps the least successful, particularly in its more rigid, southern European variants. The numerous job-related provisions keep the cost of labor quite high; indeed, the trend has been toward declining employment rates due to earlier retirement, high youth unemployment, and other factors. Yet little is done to create new employment opportunities. Social programs, influenced by strong religious traditions in several countries, assume the existence of a traditional family. Unpaid, usually female labor is still frequently required for care of children and the elderly in the home. While most European countries have achieved relatively equal distribution of income across broad population groups, they have not done so in a way that sustains employment growth, nor in a way that supports gender equality and autonomy within the household.

The other two models attract more attention, as plausible, rival responses to the economic problems of the end of the twentieth century. The Anglo-Saxon approach helps to maintain labor market flexibility, lowering the price of unskilled labor by limiting the cost of social supports. The result has been high and rising inequality, far beyond the continental European or Scandinavian levels – but also low unemployment, in Britain and particularly in the U.S., in the 1990s. In contrast, the Scandinavian model offers numerous egalitarian benefits, many of them tied to employment, along with active training, information, and other programs designed to move as many people as possible into paid work. Family-oriented social programs such as extensive public child care increase both the supply of, and the demand for, paid female labor. The result is far greater equality than in the Anglo-Saxon model, but also greater public sector costs, and, it seems, higher unemployment.

We will turn, therefore, to an examination of the polar cases: Sweden, the best-known and in some ways most complete example of the Scandinavian model; and the U.S., the most extreme case of the Anglo-Saxon approach. The overarching question is, can Sweden's expansive egalitarianism be sustained, and even imitated elsewhere – or is it necessary to cut back to the minimal American levels of social welfare in order to recreate the foundations for growth? There is an obvious parallel with the discussion of the "high road" and "low road" management strategies in earlier parts of this book.

THE SCANDINAVIAN ROUTE

Much has been written about the Scandinavian welfare state in general, and about Sweden in particular (see, for example, John Stephens 1996). The article by **Anders Bjorklund and Richard Freeman**, summarized here, analyzes the economic basis for Swedish egalitarianism. According to Bjorklund and Freeman, Swedish workers are much more equal than American in hours of work per year, as well as in hourly wages. Wages are compressed both on the supply side, by the labor movement's long-term efforts to achieve wage equalization, and on the demand side, by government policies designed to pay many low-productivity workers more than their marginal product. This form of subsidy brings many handicapped and low-skilled people into the labor force, where they enjoy the same benefits that are available to all Swedish workers, rather than creating isolated, separate programs for them.

Reprinted with permission from Island Press, © 2000

The Scandinavian model grew out of a political and economic theory that is relatively little known outside its home region. The political philosophy of the Swedish Social Democratic Party (the long-dominant political party and architect of the welfare state) is explained in Timothy Tilton (1990)[*]. The core principles of Swedish social democracy include a belief that democracy should include full participation in economic and social as well as political life; a view of society and the state as "the people's home," characterized by solidarity and equality; and a preference for a socially controlled economy, in which proper expansion of the public sector can extend, not threaten, freedom of choice. Social democracy seeks to restrict the scope of the market, not necessarily through public ownership, but through "decommodification" of human needs – that is, by making essential services available as the rights of all citizens, independent of their status in the marketplace.

The economic theory of social democracy, and the reasons for its success in its heyday, are explored in the article by **Karl Ove Moene and Michael Wallerstein**. The political basis for social democracy is the strength of the labor movement. Yet contrary to widespread fears, a strong labor movement does not always mean that industry is weak. In fact, centralized nationwide wage bargaining, with a powerful union federation that pushed for equalization of wages, turned out to be surprisingly efficient for Scandinavian industry. Newer plants and higher-productivity industries gained an advantage from the compressed wage schedule, while older plants were forced to retire, and labor and capital were driven out of lower-productivity industries. The union federations recognized that their jobs depended on Scandinavian exports remaining competitive in world markets, and, while working for wage compression, restrained the growth of average wages. Industry, for its part, maintained relatively high and steady employment – which, as Moene and Wallerstein demonstrate, may be the profit-maximizing strategy if labor market institutions make it difficult to hire and fire workers, and the business cycle swings rapidly up and down.

The Scandinavian economic model is widely seen as being in decline, or at least in retreat. (Assar Lindbeck 1997 provides a relatively critical evaluation and literature review.) Sweden's centralized wage bargaining broke down in the 1980s, and there has been a recent trend toward less equal wages -- though by comparison with any standard except Sweden's past accomplishments, the wage structure remains remarkably compressed. The breakdown occurred initially because employers faced shortages of skilled labor, and wanted to offer higher pay to attract qualified employees; it has now spread to a somewhat more general differentiation in wage rates.

By the end of the 1980s Scandinavia, like the rest of Europe, faced an economic downturn, high unemployment rates, and budget deficits. Cutbacks in benefits and programs adopted at that time were often interpreted as signaling the failure of the Scandinavian model. Yet the death notices were premature; the Scandinavian economies recovered after the recession, just as other countries did.

The occasional cutbacks seemed, in some cases, justifiable by any reasonable standards. Sweden's sick pay policy, which previously guaranteed every worker 90% of usual earnings starting on the first day of an illness, may indeed have encouraged excessive absenteeism;

Reprinted with permission from Island Press, © 2000

Swedish workers took many more sick days than their counterparts in other countries. Cutting back to a guarantee of only 75% of earnings starting on the third day of an illness does not seem merciless, and apparently is leading to rates of reported illness more in line with experience elsewhere. Similarly, Sweden's active labor market policy, combined with wage compression, may have overshot the mark, making it too easy to get a job without advanced training. Despite generous educational funding, Sweden now has a less educated workforce than many developed countries. Slightly greater incentives to stay in school and acquire advanced education and skills might well be desirable.

BACK IN THE U.S.

Americans do not, except in the most rhetorical flights of conservative imagination, experience the problem of excessively egalitarian social welfare programs. Many comparisons make it clear that among the developed countries, the U.S. is the least equal, and the least enjoyable place to live for those near the bottom of the income distribution. For example, in an analysis of Luxembourg Income Study data for the mid-1980s, Lee Rainwater (1995) finds that the percentage of families with children that fell below the poverty line (half of the country's median income, adjusted for family size) ranged from 3.5% in Sweden to 20.3% in the U.S.; all the European countries in the study were below 10%. The U.S. was also in the lead among the eight countries Rainwater examined for the poverty rate among two-parent families (11%). For the poverty rate among single mothers, the shocking U.S. rate of 58% was more than matched by Australia's 61%; in Sweden, only 6.5% of single mothers were poor.

Sheldon Danziger, **Sandra Danziger**, **and Jonathan Stern**, examines the paradox of America's child poverty amidst affluence. A number of factors have led to deterioration in the economic position of poor children. In the 1970s and 1980s, an increasing percentage of men did not earn enough to keep a family above the poverty line; and an increasing percentage of children were raised by single parents, usually mothers. Government transfers targeted to children were steadily cut back. In particular, the program of last resort, Aid to Families with Dependent Children (AFDC), was squeezed ever tighter until its final abolition in the 1990s. Moreover, taxes on poor families increased in the 1980s, further reducing the net transfer they received from the government. These trends were only partially offset by the increase in women's earnings and the decrease in average family size. Danziger et al. emphasize the scandalous health and other consequences of America's child poverty, and suggest several straightforward public policy initiatives that could raise the incomes of poor families.

It is sometimes suggested that the U.S. offers more opportunities than other countries for mobility out of poverty, potentially offsetting the effects of greater inequality at any point in time. While a greater percentage of people are poor in America, they might, on average, spend less time being poor. Unfortunately for this theory, an empirical study suggests just the opposite. In Figure 10.1, the horizontal axis shows poverty rates for families with children in selected countries. The vertical axis represents the transition rate, or the probability of a poor family escaping poverty (defined as going from below 50% to above 60% of median income in one year). The negative slope of the graph shows that in the countries with the lowest poverty rates, a poor family was most likely to escape from poverty. There are proportionally far fewer Dutch

Reprinted with permission from Island Press, © 2000

and Swedish poor people, *and* they are much more likely than poor Americans to get out of poverty in any one year.

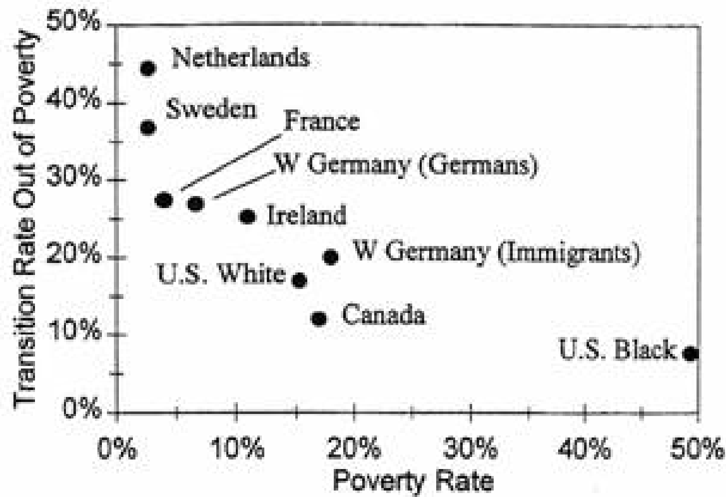

Figure X.1. Poverty Rates and Transitions: Families with Children, Mid-1980s. Poverty rate is percent of families below 50% of country's median income. Transition rate is percent of families who were poor one year who had more than 60% of median income in the next year.

Source: Excerpted from Table 8.16 and Figure 8E, pages 378–379 in Gøsta Esping-Anderson, ed., *Welfare States in Transition: National Adaptations in Global Economies.* London: SAGE Publications, 1996.

The study examines ethnic Germans and immigrants separately within Germany, and whites and blacks separately in the U.S. Figure 10.1 shows that in both countries the majority fares better than the minority. Note that the gap between the two is much smaller in Germany, and that white Americans are roughly comparable to immigrants in Germany in terms of poverty rates and transition rates. Black Americans are virtually off the chart of developed country data, with by far the highest poverty rate and the lowest likelihood of escaping from poverty.

The Anglo-Saxon version of the welfare state, although far less generous and expensive than the Scandinavian model, nonetheless provokes more controversy and resistance from taxpayers. The narrow, means-tested programs of the "residual" welfare state evidently generate less popular support than more expensive but universal programs. Middle-class Scandinavians do grumble about their tax burden, which is far greater than anything Americans would accept. Yet the Scandinavians, realizing that taxes pay for their parents' pension, their children's college education, their grandchildren's day care, and the whole family's health insurance, may not devote themselves to demanding tax cuts with the same fervor as their American counterparts.

The complex question of who pays for the welfare state is addressed in the article by **Ardeshir Sepehri and Robert Chernomas**. They divide society into capitalists, workers, and welfare recipients, and make a number of reasonable estimates about which taxes are paid and which government benefits are received by each group. Their awkwardly named "welfare-

Reprinted with permission from Island Press, © 2000

adjusted transfer ratio" is the ratio of taxes paid to benefits received for workers and welfare recipients combined. When the ratio is below one, then there is a net transfer from capitalists to the other groups; when the ratio is above one, then capitalists are net recipients of benefits funded by workers' taxes.

In both Canada and the U.S., Sepehri and Chernomas find that the ratio declined from 1955 to 1975, falling below one in the early 1970s. In the U.S. the ratio began to rise steadily after 1975, shifting the financial burden of government away from capital and onto labor. (This corresponds closely to the discussion of the corporate offensive that began in the 1970s, discussed in earlier parts of this book.) In Canada, with a different political history, the ratio remained below one until 1983, but then began a steady rise resembling the U.S. pattern.

TARGETS AND TRADE-OFFS

While the universalism of the Scandinavian model is an appealing answer to inequality, it does not appear to be on the immediate agenda in most countries. In a world of limited resources and contentious policy debates, it will continue to be important to examine the trade-offs between the different objectives of the welfare state. In another comparative study using the Luxembourg Income Study data for the 1980s, Deborah Mitchell (1995) asks whether there is a trade-off between the *effectiveness* of income transfers in reducing poverty and income inequality, and the *efficiency* of those transfers, in directing their expenditures to the target groups.

A positive finding that there is a trade-off might mean, for instance, that the efficiently targeted programs are small and mean, whereas effectiveness in reducing poverty or inequality requires offering generous universal benefits that "inefficiently" spill over into the middle class. Mitchell concludes that there is a clear trade-off in relation to reducing inequality – for instance, Sweden achieves the greatest reduction in inequality through its government transfers, but with the greatest spill-over. However, her findings are less clear in relation to reducing poverty. The U.S., Canada, and Switzerland appear to be both less efficient and less effective at reducing poverty than the other seven countries in the study.

The last article summarized here, by **Anthony Atkinson**, offers a critical look at the practice of targeting benefits to narrowly defined, usually need-based, groups of recipients. While not rejecting targeted programs out of hand, Atkinson suggests several reasons to question the assumption that more precise targeting of expenditures is always an improvement. Some programs have objectives other than reaching the most needy, such as the promotion of social solidarity. Some forms of targeting involve significant administrative cost and potential for error. The nuisance and stigma attached to applying to a welfare bureaucracy may discourage a large part of the eligible population from claiming the benefits they are entitled to.

Perhaps most significant is the work incentive problem. Benefits that automatically fall as wages rise amount to a hidden tax on earnings, potentially discouraging work effort and creating a "poverty trap." This can be avoided either by universal benefits, or by programs that, like many European child allowances, are constant up to a high income, well above the median, and then reduced or eliminated for upper-income groups.

Reprinted with permission from Island Press, © 2000

In conclusion, the economic crunch and budget problems that affected welfare states in the 1980s and 1990s have forced cutbacks and readjustments around the world. But these are marginal adjustments, which have not refuted the underlying arguments that support government intervention to promote equality and provide basic human welfare. Comparative analysis of the wide range of international experience underscores the effectiveness of political activism in altering distributional outcomes.

There is no reason to endorse the highly unequal distribution of resources that would be achieved by the market on its own. As we have seen, there are fundamental flaws in the argument that this process is uniquely efficient. There is no single mode of social welfare that inevitably emerges at a certain level of development: the possible outcomes range from America's relatively unequal distribution of income, to Sweden's remarkably more equal pattern. While it may not be possible to jump abruptly from one end of this spectrum to the other, it is certainly possible for societies to debate and change their distribution of resources.

Reprinted with permission from Island Press, © 2000