Book Review

Jonas Pontusson: Inequality and Prosperity: Social Europe vs. Liberal America.

Ithaca, NY: Cornell University Press, 2005. xiv+242 pp.

Inequality and Prosperity has two aims. One is to delineate the ways in which affluent countries differ in their economic institutions and their labour market and social policies. The other is to use macro-comparative analysis to shed some light on the question of whether the pursuit of low inequality is compatible with a healthy economy.

The book is highly successful in both respects. It will inform comparativists in political science, sociology, economics, and related fields as well as policy analysts and policy makers, and it will be an excellent choice for graduate and undergraduate courses in political economy and comparative politics.

Pontusson provides a very useful overview of the key features of Nordic and continental European 'social market economies' (SMEs) and Anglo-American 'liberal market economies' (LMEs). Particularly helpful are his discussions of labour market institutions (pp. 25–28 and ch. 6) and welfare state regimes (pp. 146–153). The book also includes a nuanced but readily comprehensible description of various indicators and measures of inequality, poverty, and macroeconomic performance.

The heart of the book is an empirical assessment of the degree to which low inequality does or does not impede growth of economic output and employment. The analyses are mainly bivariate, and Pontusson stresses throughout that the aim is largely to gain preliminary insight rather than present the final word on the matter. He also draws extensively on the findings of prior research. The conclusions he reaches include the following:

1. Levels of GDP per capita tend to be about equal across the two groups of countries (pp. 5–6).
2. Growth of GDP per capita tended to be higher in the SMEs in the 1960s and 1970s and similar across the two groups in the 1980s and 1990s (pp. 5, 7). It tended to be higher in countries with more generous welfare states in the 1960s and 1970s and no different in the 1980s and 1990s (pp. 167–168).
3. Unemployment rates have been similar across the two sets of countries. Four SME countries have experienced sustained high unemployment: France, Germany, Italy, and Spain (pp. 5, 9).
4. Since 1990, LMEs have tended to be more successful than SMEs at reducing unemployment (p. 71).
5. Long-term unemployment tends to be much more of a problem in continental SMEs than in the LMEs or the Nordic SMEs (pp. 71–73).
6. Employment rates tend to be highest in the Nordic SMEs, followed by the LMEs and then the continental SMEs (p. 77).
7. In the 1980s and especially in the 1990s, employment rates tended to grow more quickly in the LMEs than in the SMEs (pp. 81–82).
8. Low earnings inequality among employed individuals, high levels of employment protection, high social policy expenditures, and high payroll taxes are associated with slow employment growth (pp. 88–91, 124, 174–75, 178–80).

Pontusson also considers the question of whether the pursuit of low inequality is still feasible in the face of globalization and population ageing. Here, the principal findings are as follows:

1. Inequality of earnings among the full-time employed and of posttax-posttransfer income among households tends to be substantially lower in the SMEs than in the LMEs (pp. 5–6).
2. Inequality of pretax-pretransfer household income increased in nearly all countries in the 1980s and 1990s, and it did so to the greatest extent among the Nordic countries (pp. 30–40). This was partly a product of rising earnings inequality among individual workers, but mainly a product of declining employment (pp. 48–56).
3. In countries with rising market inequality, redistribution tended to increase. Thus, although posttax-posttransfer income inequality increased in many countries, it did so to a lesser extent than did pretax-pretransfer income inequality (pp. 195–197).

4. Countries with more generous social policy tend to have lower levels of income poverty (p. 158). Nations with more generous support for children and families tend to have lower levels of child poverty (p. 161).
5. The generosity of social policy has tended to decline in both SMEs and LMEs since the early 1990s. This is due mainly to pressures stemming from population ageing, globalization, and requirements for European Union monetary integration. Although relatively small, some of these changes are significant (ch. 8).

In my view, these inferences about the impact of low inequality on economic performance and about trends in inequality are compelling. Some are novel, while some buttress recent findings by other comparative analysts. Together, they suggest a need for rethinking of the still-common assumption of a steep equality-efficient trade-off and of the view that egalitarian pursuits are now hopeless in a global economy. The nuance, thoughtfulness, and clarity with which Pontusson approaches these issues make his analyses and interpretation a very welcome contribution.

What, then, is to be done? Pontusson offers some suggestions for social market economies and some for liberal market economies. For some of the social market economies, the principal challenge in coming years is to increase employment rates. Pontusson advises loosening of employment protection regulations and a shift from payroll taxes to income taxes (pp. 215–217). I have no quarrel with these suggestions. Pontusson does not advise these countries to allow wage inequality to increase (p. 215). Although I am somewhat sceptical about the ability of unions to prevent some decline in real wages at the low end of the distribution and unsure about the merits of doing so, this is a perfectly reasonable view.

Another recommendation for SMEs is continued high levels of wage coordination (ch. 5). Consistent with an extensive literature, Pontusson suggests that wage coordination is conducive to moderate growth of real unit labour costs (wages adjusted for inflation and productivity growth), that this permits less restrictive monetary policy, and that that in turn helps to increase employment and reduce unemployment. Here, I have some reservations. In an earlier analysis, I found no impact of wage coordination on real unit labour cost growth across countries in the 1990s (Kenworthy, 2002). Nor, in my view, is the evidence that SMEs in fact pursued tighter monetary policy in the 1990s sufficiently compelling. Also, the dependent variable for the analysis is levels of unemployment, whereas the more appropriate indicator would be *changes* in unemployment (or in employment).

Pontusson also argues that high public investment in primary and secondary education is helpful for reducing inequality in cognitive ability (measured by adult literacy), and therefore in earnings, and for improving competitiveness and growth (pp. 134–141). This could well be true. However, the cross-country association between public spending on K-12 education and inequality of cognitive skills is driven entirely by the Nordic countries. Those countries also invest heavily in early child care and preschool, and that, rather than K-12 schooling, could be the key to limiting cognitive inequality (Esping-Andersen, 2004). Also, Germany and the Netherlands have very little inequality of cognitive ability despite average educational expenditures. Furthermore, it is not clear what the relationship is between public investment in education and economic growth.

In liberal market economies, particularly the United States and United Kingdom, the principal challenge is to reduce inequality. Social market economies have largely succeeded in doing so, but many comparativists have become sceptical about the scope for institutional change in national economies. If institutions and policies cohere within each 'variety of capitalism', perhaps countries are largely stuck. Here, Pontusson offers the helpful suggestion that we distinguish between social democratic policies (such as public investment in education, active labour market policy, support for child care, universalism and generosity in social policy, and wage solidarity) and social market institutions (such as strong unions, coordinated wage setting, employer centralization, and concentrated ownership of firms). The latter may be quite difficult for liberal market economies to emulate, but the former are, to a considerable degree, a matter of policy choice.

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