3
THE EGALITARIAN PARADISE?

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Introduction

The egalitarian structure of the Nordic countries is internationally renowned and often considered a salient feature of the so-called Nordic welfare model (Kautto *et al.* 1999). Although the basic characteristics of the Nordic welfare states are subject to ongoing discussion, international comparisons generally address the unique shape of the Nordic income distributions and how the Nordics have organized the welfare state (Bäckman 2009; Brandolini and Smeeding 2007; Esping-Andersen 1990; Fritzell and Ritakallio 2010; Kildal and Kuhnle 2005; Korpi and Palme 1998). The particular mix of low income inequality and effective redistribution programmes has historically been a prominent element in the Nordic welfare states and often considered a salient feature of the social-democratic regime as described by Esping-Andersen (1990) in his famous three-fold categorization of welfare capitalism.

For much of the post-war period, the Nordics have been at the top of the equality league, actually forming a family of their own in terms of (the lack of) income inequality and poverty (Fritzell *et al.* 2012). Similar to many other countries, however, the Nordics have experienced major challenges in recent decades, caused partly by increased fiscal constraints, the return of mass unemployment and demographic developments, such as ageing populations and immigration. In this period, income differences have widened in the Nordic countries and social policies have been scaled back. Whether or not the Nordic welfare states still offer their citizens an egalitarian paradise has not been sufficiently documented. The purpose of this chapter is to analyse the egalitarian structure of the Nordic countries and investigate how income distributions have changed along with the re-organization of the welfare state since the early 1990s. In this time, the Nordics, Finland and Sweden in particular, entered a deep financial crisis that appears to have marked an end to Nordic exceptionalism, both in terms of income inequalities (OECD 2008) and generous welfare benefits (Ferrarini *et al.* 2013).

We have structured the chapter as follows. First we describe the overall developments in the Nordic income distributions, focusing on inequality and poverty trends. We then use more recent empirical data and analyse income differences across particular risk groups. The development of the Nordic income distributions is then situated against the backdrop of changes introduced to major cash benefit programmes. The chapter concludes with the discussion of our findings.

Income distribution trends

Many affluent countries have become more unequal over the past two decades, including the Nordic countries. Although the Nordics remain characterized by comparatively compressed income distributions, it is striking to note that inequality has increased more in the Nordic countries than anywhere else since the 2000s (OECD 2011). This section takes a closer look at this increased income inequality, going beyond country averages and exploring both the similarities and differences between these countries. Since we are interested in long-term income distribution trends, we use data from the Cross-National Data Center in Luxembourg (LIS), which provides harmonized income survey data approximately for every fifth year since the early 1980s for many countries.

We use LIS data to cover the period 1990–2010 in the following. We are thus able to follow the development of income inequality in the Nordics from the fiscal crisis in the early 1990s until the first years of the great recession in 2008. Unfortunately, the Swedish data in LIS are only available through the 2005 wave. We have therefore imputed 2010 inequality data for Sweden based on income data from two waves (2005 and 2010) of the EU statistics on income and living conditions (EU-SILC). Iceland is not included in LIS and is therefore excluded in this analysis of long-term income distribution trends. Figure 3.1a–b shows the Gini coefficient and the EU at-risk-of-poverty rate in the Nordic countries.[1] We also show income inequality as an average for a larger group of European countries.[2]

The egalitarian structure of the Nordic income distributions is clearly apparent in Figure 3.1a, which describes the developments in the Gini coefficient for the period 1990–2010. Similar to previous observations, the dispersion of disposable income has widened in the Nordics. The most dramatic development occurred in Finland, where income inequality increased by about 25 per cent, from a Gini coefficient of 0.2 in 1990 to just above 0.25 in 2010. In Denmark and Sweden, the Gini coefficient declined during the financial crisis in the early 1990s, and here income inequality first increased in the second half of the 1990s. Despite increased inequality, however, plenty of leeway remains before the Nordic income distributions match those of

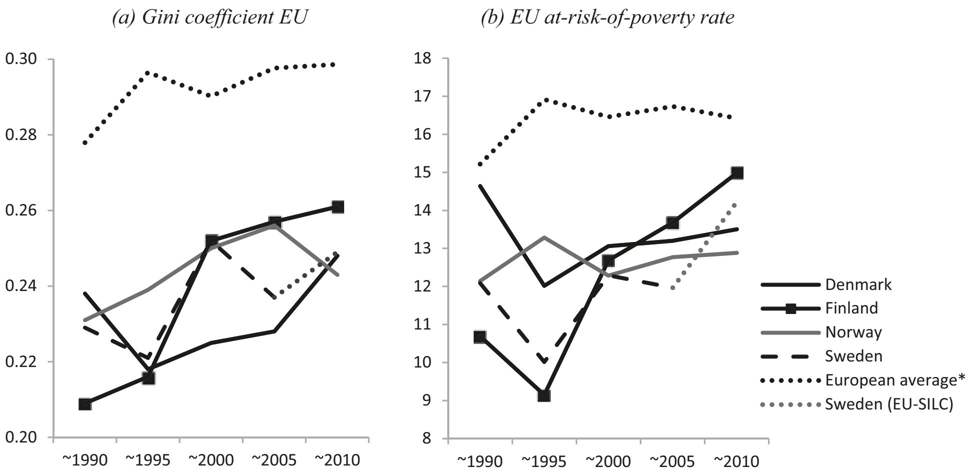

Figure 3.1 The Gini coefficient and the EU at-risk-of-poverty rate in the Nordic countries and other European countries, approx. 1990–2010

Note: * excludes the Nordic countries.

Source: LIS and EU-SILC (own estimates).

many other European countries. The income inequality in our larger group of European countries evidently exceeds that of the Nordic countries. From this perspective, we may very well conclude that the Nordics continue to perform like an egalitarian paradise. Averages conceal individual differences, however, and it is possible to find European countries that are at least as egalitarian as the Nordic countries. Belgium and the Netherlands are two examples of countries where income inequality is close to the Nordics.

Increases in Gini coefficients over the last two decades are often explained by the rapid growth of top incomes and capital gains (Atkinson and Piketty 2007). By excluding the incomes at the very top of the distribution, we have reduced these effects somewhat, although we cannot completely rule out the possibility that much of the increased income inequality is due to capital gains and developments in high-end incomes. In order to reach a more complete understanding of the egalitarian structure of the Nordic countries, it is therefore necessary to focus more explicitly on the changes in the lower part of the income distribution and analyse the developments in the EU at-risk-of-poverty rate. Relative poverty measurements are less sensitive to changes in top incomes than the Gini coefficient and overall measurements of income inequality.

Similar to the Gini coefficient, the results in Figure 3.1b show how relative income poverty has increased in the Nordic countries, at least since the mid-1990s. Despite differences between the individual countries, the Nordics are also more egalitarian than many other European countries in this regard. They are evidently getting closer to the European average, however, where the relative income poverty in many countries has been rather stable since the mid-1990s. The reduction in relative income poverty in Denmark, Finland and Sweden in the early 1990s has mostly resulted from substantial declines in median incomes following the financial crisis (Fritzell *et al.* 2012). This rather paradoxical result highlights the importance of complementary approaches when analysing poverty developments in periods of deep economic crisis (Kangas and Ritakallio 1998). Alongside reductions in relative income poverty in both Finland and Sweden in the early 1990s, consumption-based poverty estimates did in fact increase (Kautto 2000; Palme *et al.* 2002). It is interesting to note that increases to the Gini coefficient in Norway are not mirrored in poverty statistics, which is most likely due to developments in capital gains and top incomes. Aaberge and Atkinson (2010), for example, reveal a dramatic increase in top income shares following the major Norwegian tax reform in 1992.

Old and new poverty

The Nordic welfare states were largely developed over a period when full employment was a realizable element of macroeconomic policy and most citizens qualified for earnings-related compensation in major social insurance schemes. This was largely still the case in 1990, when Esping-Andersen's seminal book was first published. However, the 1990s crisis that was soon to come altered these conditions substantially. The Nordic labour markets have thus changed considerably since the heyday of welfare state development in the decades immediately following the Second World War. The smooth transition into work for new entrants into the labour market, which was an implicit, built-in assumption in the Nordic welfare model, now seems to be an historical artefact. As in many other countries, low-skilled peripheral occupations in the Nordic labour markets are now characterized by increased job insecurity and restricted access to social security, similar to what Standing (2011) described as the 'precariat'. While the Nordics have traditionally been successful in combating the 'old' risks emanating from temporary interruption or retirement from paid work, concerns are sometimes raised in connection with 'new' social risks that have emerged alongside post-industrialization (Taylor-Gooby 2004). While

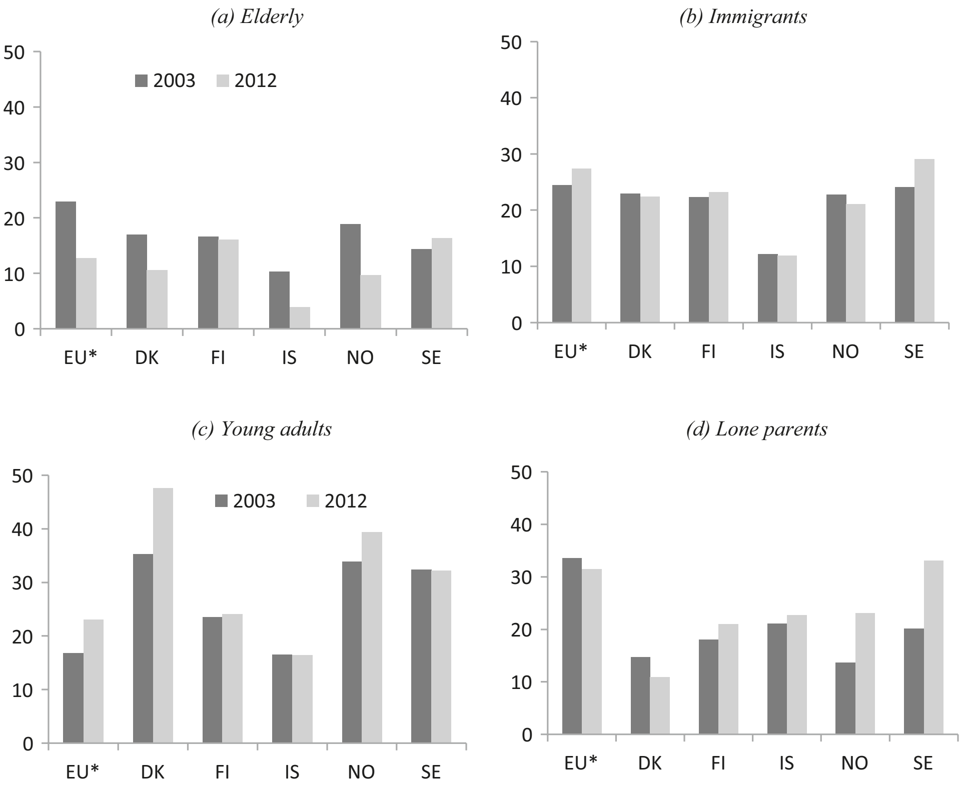

Figure 3.2 The EU at-risk-of-poverty rate among the elderly, immigrants, young adults and lone parents in the Nordic countries and other European countries, 2003 and 2012

Note: * average excluding the Nordic countries.

Source: EU-SILC (own estimates).

Timonen (2004) argues that the Nordic welfare model is well equipped to address new social risks, Fritzell *et al.* (2012) show that, in reality, poverty risks for immigrants and young adults are either on par with or higher than those of many other European countries.

This section goes beyond an analysis of the overall trends and focuses more closely on the poverty risks in different groups characterized by old and new risks. Figure 3.2a–d shows the EU at-risk-of-poverty rate among elderly people, immigrants, young adults and 'lone parents' in the Nordic countries and as an average of our larger group of European countries. The analysis is based on EU-SILC income data and restricted to the years 2003 and 2012. Here, we are also able to include Iceland. We will start by discussing the relative income poverty among the elderly, as shown in Figure 3.2a.

Old age is conventionally regarded as an old risk that has been highly prevalent throughout the entire post-war period. In 2003, poverty among the elderly was clearly lower in the Nordics than in many other European countries. By 2012, the egalitarian structure in these countries had become less pronounced. In both Finland and Sweden, relative income poverty in old age now exceeds the European average, which dropped substantially over the ten-year period analysed here. Moreover, Sweden is the only Nordic country with an increase in old-age poverty over this period. It is worth noting that among the non-Nordic countries, only Belgium and the UK have higher old-age poverty rates than Sweden (not shown). Contrary to the developments in Sweden, relative income poverty among the elderly declined substantially in Denmark, Iceland and Norway, whereas old-age poverty rates in Finland almost show a standstill. The old-age poverty rates in Iceland are particularly low.

Ageing populations pose considerable financial pressure on the Nordic economies. Another topical challenge is the growing influx of refugee immigration. Figure 3.2b illustrates the poverty rates among immigrants. Here, we have restricted the analysis to people of working age (27–54 years).[3] It should be noted that poverty estimates are too crude for an overall analysis of how successful countries are at integrating immigrants into society. For example, country of origin, residential time and the reason for immigration are all factors that seriously influence poverty risks. Both the number and composition of new people moving into the country are also closely related to immigration policy, which nowadays differs significantly between the Nordic countries as well as across Europe as a whole. Among the Nordics, Denmark and Finland are often considered to have more restrictive immigration policies than Norway and Sweden; at least with respect to asylum seekers.[4] Until the autumn of 2015, Swedish immigration policies were among the most liberal in Europe.[5] Except for Sweden, all of the Nordics for which we have data have relative income poverty rates among immigrants that are lower than our European average.[6] It should be noted, however, that several of the non-Nordic countries have immigrant poverty rates that are lower than in Denmark, Finland and Norway. Included in this category are Germany, Ireland, Portugal, the Netherlands and the UK.

The financial situation of young adults is evidently problematic in many of the Nordic countries, particularly in Denmark and Norway, where relative income poverty among young adults (20–24 years) increased between 2003 and 2012. In comparison, relative income poverty among young adults has been fairly stable in Finland and Sweden. Relative income poverty is more widespread among young adults in the Nordic countries than in many other European countries, although Finland and Iceland are on par or even below our European benchmark. Here again, some words of caution are motivated when poverty estimates are interpreted cross-nationally. The Nordics are renowned for how their youth leave the parental home at early ages (Buchmann and Kriesi 2011). The Nordic youth thus tend to form their own households at an earlier age than in many other European countries, where children tend to continue living in the parental household and share their income for much longer periods. Another issue concerns the treatment of students and apprentices in poverty analyses. Although we analyse people aged 20–24, there may still be many students and apprentices in this age group. A low income among those who are pursuing an education or receiving training may obviously be problematic, although schooling in this age group is voluntary and can be regarded as an investment in future income. When those in education are excluded from the analysis, relative income poverty among young adults in the Nordic countries is reduced substantially and much closer to our European average (not shown).

Lone parents have comparatively low poverty risks in the Nordic countries. In our analyses, the overall pattern suggests that Nordic poverty rates are well below those of many other European countries. Despite this positive testimonial regarding the Nordic welfare states, the overall trend is more disappointing. Except for Denmark, relative income poverty among lone parents has increased in recent years. In both Norway and Sweden, the increase in relative income poverty has been quite substantial. In 2013, the poverty rate among lone parents in Sweden actually exceeded the European average. It should be noted, however, that poverty estimates among lone parents in Sweden are very sensitive to the income threshold used in poverty measurement. At lower poverty thresholds, the Swedish lone-parent poverty rate is below the European average (not shown).

Developments in social protection

The analysis of income distributions above revealed how the Nordic countries remain highly egalitarian, also by European standards. However, this special trademark of the Nordic welfare model has become less distinctive along with substantial increases in both income inequality and relative income poverty. Although parts of this widening of the Nordic income distribution are due to developments in top incomes, there are also significant changes in the lower tail of the distribution. For low-end income groups, changes to welfare state provisions are crucial determinants of material well-being. In order to provide a more comprehensive account of the current state of the Nordic welfare model, we will here situate the analysis of income distributions against the changes introduced to social policy.

The Nordic countries are renowned for their comprehensive welfare states, which provide almost universal access to high quality benefits and services. As already mentioned, however, beginning in the early 1990s, the Nordics have moved away from the signifying features of the social democratic regime described by Esping-Andersen (1990). Nearly all of the areas of the Nordic welfare states have been subject to re-organization, albeit with substantial cross-national differences. The changes introduced to cash benefits are perhaps most relevant in this regard. Figure 3.3a–e shows the net replacement rates in major cash benefit schemes in the Nordic countries and as averages of our larger group of European countries for the period 1990–2015. The data emanate from the Social Policy Indicators Database (SPIN) and show the net benefit as the percentage of the net wage for stylized households.[7]

The development of cash benefits in the Nordic countries over the period 1990–2015 is generally characterized by stability and decline, at least when programmes are evaluated in terms of their generosity. A few success stories are observed, particularly in the area of paid parental leave, where benefits in Denmark and Norway have substantially improved. Here, the Nordics evidently perform better than many other European countries.

Despite a nearly constant erosion of social assistance since 1990, the Nordic countries also score higher than our European average when it comes to minimum income benefits. In the other programmes, however, the distinctiveness of the generous Nordic welfare model is less clear. In unemployment insurance, the Nordics even underperform in relation to the European average, whereas in the remaining programmes the Nordic countries are scattered around our European benchmark in a seemingly random fashion.

The Swedish development is noteworthy and provides numerous examples of substantial cutbacks to income replacement. Income replacements in unemployment insurance, old-age pensions and social assistance net replacement are down by one-third. Cutbacks to paid parental leave are also substantive, but here Sweden is still comparatively generous, surpassed only by Norway. It is not possible to provide a detailed explanation here of the developments in individual countries. It is worth noting, however, that Sweden already cut formal levels of income replacement in social insurance during the financial crisis of the early 1990s, after which time income ceilings for benefit purposes lagged behind wage increases. In unemployment insurance, this hollowing out of income replacement continued well into the 2000s, not least as part of the policy packages for increasing the work incentives adopted by the centre-right government between 2006 and 2014 (Ferrarini *et al.* 2012). The sharp decline in old-age pension net replacement rates in the mid-1990s coincides with the introduction of a new Swedish pension system with notionally defined contributions as a principal component (Lundberg 2003). The downward trend in social assistance is mainly due to a combination of price indexing and changes introduced to reference budgets (Kuivalainen and Nelson 2012). It is notoriously difficult to link policy changes to developments in income distributions. Nonetheless, it is evident

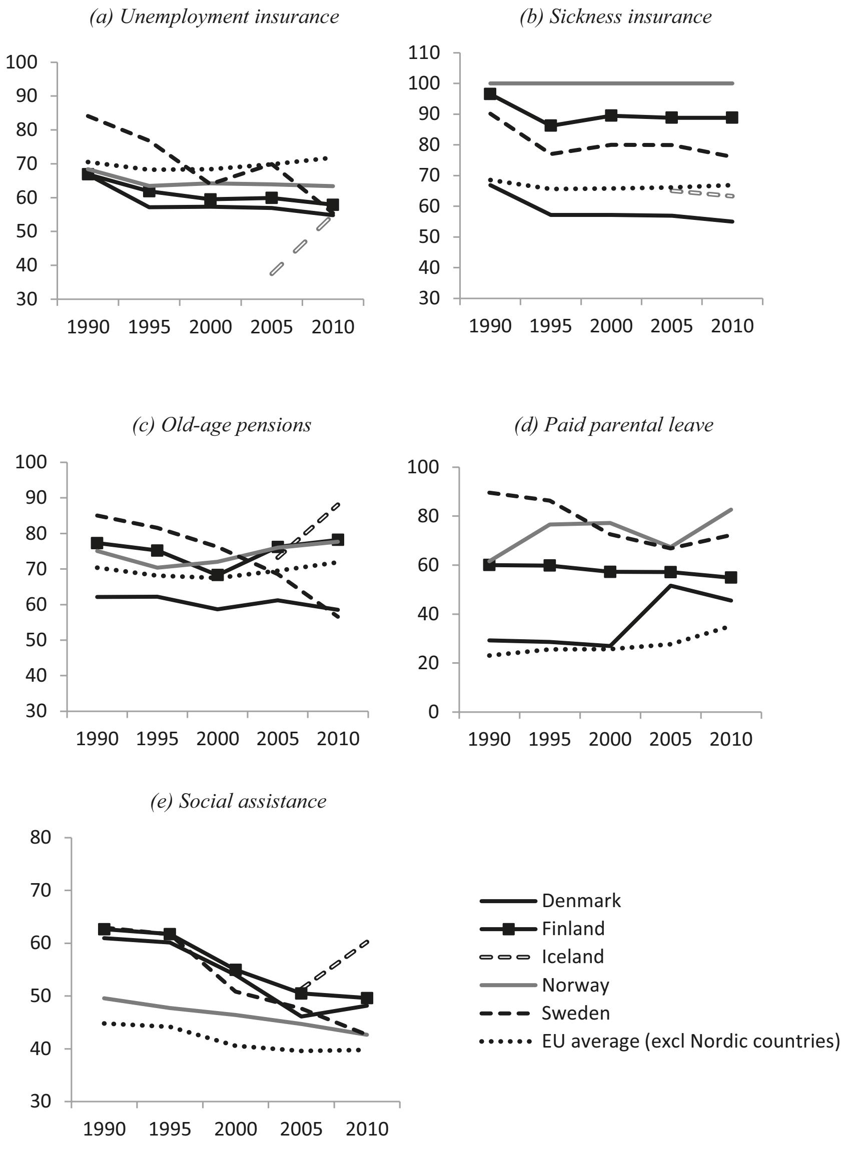

Figure 3.3 Net replacement rates in major cash benefit schemes in the Nordic countries and other European countries, 1990–2015
Source: SPIN.

that the overall increase in income inequality and relative income poverty in Sweden coincided with major cutbacks in cash benefits. One example is, of course, the increase in relative income poverty among elderly people and the simultaneous trend of deteriorated old-age pensions in Sweden.

Cutbacks to income replacement in the other Nordic countries have been less severe than in Sweden, mostly in the range of 5–15 per cent of pre-1990 crisis levels. We only find a few instances of clear improvements in income replacement. The development of paid parental leave in Denmark and Norway are two examples, another one being the Norwegian old-age pension scheme. Norway appears to have the most generous contemporary welfare model, ranking highest not only among the Nordic countries but also in a European context in terms of income replacement in unemployment and sickness insurance, as well as in paid parental leave. In old-age pensions, income replacement in Norway is also fairly generous and on par with the newly reformed pension scheme in Finland. The gradual increase in Norwegian old-age pensions seems to be mirrored in income statistics in so far as the old-age poverty rate in Norway declined substantially between 2003 and 2012. Compared to social insurance and paid parental leave, it should be noted that Norwegian social assistance benefits are fairly low. This result should be interpreted cautiously, however, as Norwegian social assistance is calculated on the basis of national guidelines rates, which may differ from the actual local rates. Nonetheless, our data quite clearly support previous observations that the Norwegian welfare state nowadays is quite special, not least since revenues from the oil and gas sector eased the financial pressures for major institutional change (Kuhnle 2007).

For Iceland, we only have preliminary data for 2005 and 2010, and we totally lack data on income replacement in paid parental leave. Regarding developments in cash benefits, Iceland has historically been lagging behind the other Nordics but has been catching up in recent years (Olafsdottir and Olafsson 2014). Our data support this observation. Income replacement in unemployment insurance, old-age pensions and social assistance in Iceland was substantially strengthened between 2005 and 2010. Unemployment insurance net replacement rates in Iceland are now on par with those of Denmark and Sweden. In terms of the generosity of old-age pensions and social assistance, Iceland holds the top position in the Nordic welfare league. While these observations should be interpreted cautiously due to the preliminary nature of Icelandic data in SPIN, we would like to recapitulate that Iceland outperformed the other Nordics quite substantially in terms of relative income poverty among elderly and young adults. Since young people generally have more difficulty qualifying for earnings-related social insurance benefits, it is reasonable to assume that social assistance is particularly important in this age group.[8]

Conclusions: egalitarian paradise lost?

The Nordic countries are often described as small, open economies that are vulnerable to external pressure caused by globalization, technological change and international business cycles. From this perspective, the increase in income inequality and relative income poverty in the Nordics comes as no surprise. Industries have been closing down in all of the Nordic countries coupled with an increased outsourcing of unskilled jobs and an increasing wage gap between skilled and unskilled labour; all factors expected to exacerbate inequality (Atkinson 2015). Meanwhile, unemployment remains stubbornly high, particularly in Finland and Sweden. The Nordic countries are not unique in this context. In Europe, we find several countries with small, open economies that should also be heavily exposed to major structural shifts. Many of these economies have not witnessed a corresponding increase in income inequality, something that brings interest to the link between the egalitarian structure of the Nordic income distributions and social policy developments; or simply the changing nature of the Nordic welfare model.

In this chapter, we have analysed the Nordic income distributions against the backdrop of changes introduced to major redistribution programmes. Much of the empirical analysis concerned changes in the lower part of the income distributions, where the role of social policies becomes particularly important. In the Nordics, poverty among people in the prime of life has less to do with inadequate wages and more with a lack of earnings, either due to unemployment or underemployment (Halleröd *et al.* 2015). For these impoverished persons, redistribution programmes will obviously add substantially to disposable income.

The Nordic welfare model is re-organizing: major cash benefits are being scaled back and income inequalities are on the rise. Moving beyond such broad characterizations of the Nordic welfare states, however, it is actually possible to find examples of both good and poor outcomes. At aggregate level, the Nordics continue to perform better than many other European countries. From a European perspective, the Nordic countries still have lower levels of overall income inequality, regardless of whether focusing on Gini coefficients or on EU at-risk-of-poverty rates. However, cracks in the facade appear when the focus shifts to changes over time or when poverty rates are disaggregated by risk groups. Here, the egalitarian structure of the Nordic welfare model becomes less distinct. We observe this tendency most clearly in the development of relative income poverty, where substantial increases in the Nordics are narrowing the distance to other European welfare states.

While it is tempting to lump all of the Nordic countries into a single category, it is important to emphasize the substantial intra-Nordic variation, both in terms of inequality outcomes and the generosity of social policy. Finland and Sweden in particular were hit hard by the deep financial crisis in the 1990s, with severe economic consequences for groups who already had a weak position in the labour market, such as immigrants, youths and 'lone parents' (Palme *et al.* 2002). In the 2000s, it is more difficult to identify particularly bad performers among the Nordics, although relative income poverty continued to increase, primarily in Finland and Sweden.

For the latter part of the period 1990–2010, we were able to analyse poverty trends by population risk groups (elderly, immigrants, young adults, lone parents). Almost no Nordic country succeeds at protecting all of these risk groups from poverty. With the exception of Iceland, it is possible to find at least one risk group where the poverty rate is on par or even exceeds that of many other European countries. In terms of poverty trends, the developments among young adults and lone parents are particularly worrying, where several Nordic countries display substantial increases in economic hardships. Here, the Nordics seem to perform worse than elsewhere in Europe. However, there is little to indicate that the Nordic countries are particularly bad performers in meeting the challenges of immigration. In Sweden, a country with a particularly massive influx of refugees, the at-risk-of-poverty rate exceeds that of many other European countries, but only marginally. The more restrictive immigration policies in Denmark – and to some extent also in Finland – may have reduced this particular poverty problem slightly. However, developments in Norway indicate that a greater influx of immigrants does not necessarily translate into higher poverty rates. In Norway, the risk of poverty among immigrants actually declined slightly from 2003 to 2012 despite having more liberal immigration policies than both Denmark and Finland.

Parallel to the increases in income inequality and relative income poverty, the Nordic welfare states provide several examples of major institutional change, often in the downward direction. The development of cash benefits in Sweden is striking in this regard, where income replacement in major redistribution programmes has deteriorated substantially. In an international perspective, it is difficult to find retrenchment patterns in income replacement resembling those of Sweden. Even if we leave Sweden aside, however, the Nordic exceptionalism with regard to benefit generosity is clearly overstated. Here, the contemporary Nordic countries stand out only in the areas of paid parental leave and social assistance. For other major social benefit programmes, the status of the Nordic welfare model is less superior to those of many other European countries. Ironically, Sweden is the country that acted as the archetypical Nordic welfare state for several years but now seems furthest away from Esping-Andersen's (1990) social democratic regime type, whereas Iceland, which was not even included in Esping-Andersen's categorization, is closest to these configurations.

The development of the Nordic income distributions and the social policy cuts obviously raise questions about the persistence of the egalitarian structures of the Nordic countries. Clearly, the Nordic welfare states are changing in directions that appear to be drifting away from an 'egalitarian paradise'. Several of the distinguishing features of the Nordic welfare model remain, however, and it would therefore be inaccurate to frame developments in terms of an 'egalitarian paradise lost'. It seems more appropriate to conclude that, in terms of egalitarian structures, the Nordics remain different, although the unique characteristics of the Nordic welfare model have become less apparent.

Notes

1 The Gini coefficient is an often-used measure of income inequality with values ranging from 0–1. Values close to 0 indicate that all individuals have almost exactly the same income, whereas values close to 1 show that income concentrates among a few individuals. The EU at-risk-of-poverty rate is a relative poverty measure, as the income threshold is set to 60 per cent of the national median household disposable income. In all of the analyses of income distributions, we have adjusted disposable income for economies of scale within households. Here, disposable income is divided by a weight where the first adult receives a value of 1, each additional person aged 14 and over receives a value of 0.5, and each child younger than age 14 receives a value of 0.3. Following the recommended LIS procedures, we have excluded the top 1 per cent and the bottom 1 per cent incomes.

2 Here, we have included all of the so-called old EU member states for which LIS provides data, including Austria, Belgium, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Spain and the UK. The Nordic countries are of course excluded from this European reference.

3 Here, immigration is defined in terms of birth country. We do not distinguish between immigration into Europe and immigration between countries within Europe. In order to exclude, as far as possible, students and people in early retirement, we have defined the working age group as those aged 27–54 years.

4 Both Iceland and Norway are part of the European Economic Area (EEA) and thereby bound by the same free movement of labour as the EU member states.

5 The Swedish government made temporary adjustments to its immigration policy in 2015 following the major refugee crisis in Europe.

6 In EU-SILC, data on immigrants are missing for Iceland.

7 Details about measurement and data are available online (www.sofi.su.se/spin) and in Ferrarini *et al.* (2013).

8 In all of the Nordic countries, eligibility for earnings-related social insurance benefits are based on contributions paid into the scheme in one way or the other, either by the insured individuals themselves or by their employers.

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