Law, Society & Organisations
Volume V, Issue 9 (2 / 2020)

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ASSESSING WELFARE STATES – RISK AND CAPABILITY OF TRUST

Keywords

Welfare state;
Risk;
Trust;

Abstract

Is the welfare state efficient? Is it a resolution for problems associated with risk? While looking at high-level generalization, the opposite polarity can be seen on this topic: supporters and critiques. Nevertheless, both sides still need much more accurate empirical pieces of evidence. Moreover, using specific theoretical perspectives can help to obtain an accurate assessment of patterns for institutional analysis. In this paper, risk phenomenon will be assessed within welfare states and it will be analyzed how risk can be related to welfare policies and "trust". The analysis cannot be limited solely to one field; economic, political, and social aspects also ought to be taken into consideration for further investigations. Nevertheless, in this paper, the concepts will only be analyzed in terms of economic factors.

RISK AND UNCERTAINTY

The Welfare States are tools for dealing with risks. Risks can be various, but the most essential ones, in this case, are the risks citizens face on a daily basis. All societies require a need-based system of relief; otherwise, arguably, they would not be societies. The central problem of the modern welfare state was (and still is) how to maintain the work-based system as primary or, put another way, how to prevent large-scale migration into the need-based system. The resolution to this dilemma was to erect a system of categorical welfare. Traditional categories are childhood, old age, sickness, disability, and widowhood (Stone, 1989).

It turns out that introducing welfare stigma reduces the socially optimal self-insurance and raises the socially optimal social insurance. It may be efficient for the society to operate at a point on its opportunity frontier where an increase in risk-taking decreases mean post-tax income and welfare stigma. In the presence of moral hazard self-insurance efforts are invariant with respect to welfare stigma, whereas social insurance increases upon introducing welfare stigma. To sum up, introducing welfare stigma decreases self-insurance and increases social insurance (Eichner & Weinreich, 2014).

Institutions can vary on this topic, as the insurance system can be governmental, private, and composition of both; consequently, welfare states can vary based on categorization. Social insurance (for unemployment, disability, sickness, healthcare) is based on the actuarial notion of calculable risks. As such, markets can produce social insurance. However, these markets are plagued by problems of adverse selection relating to the exclusion of high-risk categories (for example the elderly or the sick) from social insurance, and by free-rider problems that limit the comprehensiveness of social insurance (Veen, Yerkes, & Achterberg, 2012).

It is shown that lower trade frictions may increase the marginal costs of public funds, which gives an argument for reducing (steady-state) public consumption. However, tighter integration of product markets unambiguously leads to more variability in private consumption, and this gives a case for expanding the social insurance provided via state-contingent public sector activities (Andersen, 2002).

Two contrary opinions can be noted; first, reducing tax can help with heterogeneousness of risks' allocation, and can decrease demand for social insurance; second, reduction of international integration percentage can help to deal with the requirement for social provision.

Esping-Andersen (1990) categorized welfare states by the scale of dealing with risks:

· Liberal;
· Conservative;
· Social Democratic.

The welfare state is based on a notion of social solidarity that bridges social divisions between classes, solidarity that binds the fates of the lower and the middle classes, the poor and the rich, the young and the old and the sick and the healthy together in welfare programs based on risk-sharing between high- and low-risk categories. Economic and social processes of globalization and individualization are thought to weaken these bonds of solidarity between different social groups and to undermine the willingness of people to support each other in times of bad luck (Veen et al., 2012).

In this case, Globalization and Individualism can be seen as a threat to the welfare state; a more collectivist mindset can lead to risk-sharing, and it will compensate for the gap between the poor and the rich. One of the factors affecting risk-sharing in society is trust. In other words, if citizens can rely on the government for the future, paying high taxes, reducing the risks of the less advantageous groups can lead to the expanded welfare states.

In the case of moral hazard, Eichner and Weinreich (2014) noted that welfare stigma does not affect the choice of individual risk-taking. However, the level of social insurance is again increasing in the preference intensity of the social norm. Comparing self-insurance and social insurance in the social optimum and under moral hazard, it is shown that individual risk-taking at moral hazard is inefficiently high (low) if individuals exhibit a weak (strong) preference for the social norm (Eichner & Weinreich, 2014).

Distribution and redistribution of the resources and how governments can deal with it were popular debate topics for decades. Korpi (2006) noted that regarding welfare state expansion, employers have often been antagonists, under specific conditions – consenters, but very rarely protagonists. Well-developed welfare states and coordinated market economies have emerged in countries with strong left parties in long-term cabinet participation, or in countries with state corporatist institutional traditions and confessional parties in intensive competition with left parties. Economically well-endowed categories with relatively low risks are likely to prefer to situate distributive processes within a market-property nexus; those with higher risks and lesser economic resources are likely to support an extension of social citizenship which counteracts the effects of differences in resources and risks. Such class-related micro-foundations are however not iron laws producing identical outcomes over time and among countries; instead, they are likely to increase the probability for some outcomes while decreasing probabilities for others (Korpi, 2006).

When there is a risk of losing money, economic agents will start to save money, instead of spending, and doing investments. One of the main questions of the investigations by Keynesian and Post-Keynesian scholars is whether under which conditions economic agents behave rationally when it comes to the money. However, it is related more to uncertainty, than risk. Risk is a situation in which a decision must be made concerning a certain event and the probability distribution of this event is known. Uncertainty, on the other hand, characterizes a situation in which the probability distribution of the event does not exist (Ferrari Filho & Camargo Conceicao, 2003). Moreover, in this situation, institutions are crucial, to build and reshape the preferences of economic agents. As institutionalism scholars noted, money is one of the most essential (if not the most important) institution in the capitalist economy, because economies operate in historical rather than logical time, economic agents take decisions under conditions of genuine uncertainty and, as a result, the outcome of the decisions they make cannot be predicted.

As Veen & Yerkes (2012) noted, social risks as risks that do not result from individual choice but as risks that are (also) produced by the social system of production, and the risk of occupational disability in an industrial economy as an example of social risk. Based on their findings, people experience job insecurity, this spurs support for unemployment insurance. The opposite is also true: work secure people, that is, people who expect to find employment easily when in need of a job, show less support for unemployment insurance. However, the author finds no evidence for the hypothesis that flexibilization weakens the social bond between workers, which consequently undermines their willingness to share risks. The changing nature of work shapes workers' perceptions of risks, fostering a growing need for risk reduction through social insurance. This conclusion confirms the hypothesis that individualization – in this case in the labor market – can strengthen welfare state support and thus the willingness to share risks because (in this case) labor market flexibilization makes people more aware of their vulnerability (Veen & Yerkes, 2012).

From a risk management perspective, one economic agent's risk will be another agent's reward or vice versa. It can be assessed by the Prisoner's Dilemma; the government can prevent it by involving, and decommodification is a crucial tool in this case. There is no "right" regulation of risks, and it is different from country to country, situation, or industry.

However, the behavior of economic agents' uncertainty has been misleading in numerous investigations. The idea that "the rational expectations hypothesis is nothing else than an extension of the rationality hypothesis to expectations" has been a misleading but (unfortunately) extremely popular argument for the REH (The Rational expectation hypothesis). To put it in a game-theoretical vocabulary, the rational expectations equilibrium is "Nash equilibrium", not "a dominant strategy" equilibrium. In addition, policy changes affect the quality of expectational coordination, change the perspective. It suggests that the evaluation of the change of quality of expectational coordination associated with a policy change is an unavoidable and potentially major dimension of any policy change (Guesnerie, 2013).

As Hey (2002) mentioned, Economics has a well-organized story of decision making under risk and uncertainty. It adopts a two-way classification, which he summarized as the following:

1. Static decision making under risk
2. Static decision making under uncertainty
3. Dynamic decision making under risk
4. Dynamic decision making under uncertainty

There are no clear pieces of evidence, what is the acceptable level of risk or risk aversion. But, it is clear that a risk-free environment is also not achievable. If the government cannot manage earlier to diminish the level of risks citizens face and deal with on daily basis, it is supposed to intervene when the rate is too high to be managed.

Three stages of risk evaluation, which might be used by the government to develop an effective risk management strategy include: absolute risk assessment, relative risk assessment, and reducible risk assessment.

Absolute risk assessment is concerned with the number of deaths, injuries, or illnesses from hazardous products and activities.

The second stage relative risk assessment is concerned with risk comparisons. The risks or risk-benefit ratios from different products and activities are compared

The third stage focuses on the net benefits to society if action is taken. It includes comparative risk assessment, which examines the net change in risk due to manufacturer/consumer response to a regulation, and cost-effectiveness/cost-benefit analysis, which compares the costs and benefits from various risk reduction strategies. This stage of risk evaluation is important in selecting the optimal regulatory mix, including informational and non-informational regulations (Dardis, 1988).

One more issue related to risk can be asymmetric information problems. Moselle, Degeorge & Zeckhauser (2007) summarized that, when risk choice is observable, agents with private information on their quality face strong incentives - regardless of their quality - to pick performance lotteries with low risk. When risk choice is conspicuous, conservatism helps good types separate themselves. Bad types will not like equilibrium. Nevertheless, they will choose conservatism because that is better than maximizing their expected outcome but admitting their type (Moselle et al., 2007).

A welfare state that focuses on investment in human capital and the enhancement of individual opportunities is often called a social investment state (Veen et al., 2012).

At the same time, welfare states are a product of industrial society. Changes through decades from Materialist to Post-Materialist values have been followed up with the changes toward the service economy. As Inglehart (2007) mentioned, it is the shift from survival to self-expression. In his investigation, Rodrik (1998) noted that more open economies have bigger governments, but at the same time, public sector activities are supposed to be more expanded.

CAPABILITY OF TRUST

Citizens have various opinions about welfare states; therefore, trust in welfare states may vary from country to country. But, generally, it depends on the government's ability to handle the situation, for that reason, the capability of institutions can affect citizens' opinions.

There are two cases: when citizens feel the support by the government, the procedures are transparent, and decommodification is at a high level, then citizens' feedback will be positive and because of the high rate of trust, one of the main characteristics of welfare states – high taxes, can give the fruits. However, if citizens think there is a case of corruption, discrimination of groups, and incapability of dealing with the issues, the feedback would be negative, consequently, the level of trust would be lower. National surveys from Sweden and Norway indicate that political trust is strongly linked to more concrete aspects of welfare policy: taxation, welfare financing forms, welfare services delivery, tax evasion, and abuse of welfare benefits (Edlund, 2006).

Bjørnskov & Svendsen (2012) found out that, trust determines the size of welfare states as well as three crucial features: high levels of political confidence, strong legal institutions protecting private property rights, and low level of bureaucratic corruption. Trust is an important mechanism for redistribution. While talking about trust, two types can be mentioned: social trust and particular trust. Social trust differs fundamentally from a particular trust by being extended to people on whom the trusting part has no direct information other than a shared nationality, particular trust is the type of trust formed in repeated transactions or other situations in which actions and reputations are built on either a history of transactions or other observable and relevant information (Bjørnskov & Svendsen, 2012).

In his investigations from 2006, Edlund answered the following question in the case of Sweden: Is distrust in institutional capability an important prerequisite for general welfare state support withdrawal? And he found out, there is little evidence that distrust in the institutional capability of the welfare state has translated into widespread anti-welfare state sentiments. For many citizens, distrust in the capability of the welfare state is an issue of insufficient resources and they are willing to increase social spending in order to improve social services and benefits. For other citizens, distrust is closely connected with anti-welfare state sentiments. These very different preferences for the welfare state largely follow the left-right dimension in Swedish politics. Workers, women, and public sector employees are over-represented among those who want to restore the welfare state, whereas the self-employed, those in service class I, men, and employees in the private sector tend to prefer a less ambitious welfare state. In the short run, institutional distrust may not be a problem for the legitimacy of the welfare state (Edlund, 2006).

The research by Edlund & Lindh (2013), in the case of Sweden, created an analytical framework covering trust in public institutions (TPI) and market institutions (TMI). The results of the empirical analysis showed that public support for state-organized welfare is clearly not only affected by citizens' conceptions of what the state can do but also by citizens' conceptions of what other institutional constructs - in this case, market institutions - cannot do. And the main findings were the following:

- TMI has a robust negative effect on WSS (Welfare State Support);
- The expected relationship between TPI and WSS is strengthened controlling for TMI;
- TMI mediates the relationships between socio-economic variables and WSS. These findings underline the importance of bringing in other institutional configurations that are seen as conceivable alternatives to the state for administrating social welfare, not the least in studies primarily interested in the link between TPI and support for state-organized welfare.

In other words, a basic idea in class-based welfare state theory was supported: welfare policy preferences are strongly dependent on the type and quantity of risks and resources that social groups bring to the market (Edlund & Lindh, 2013).

Social trust can be measured by surveys, with the only question, whether people think others are generally trustworthy. While generalizing quantitative analyses on this topic, it can be observed that for Scandinavian countries the percentage is generally higher, than other OECD countries. But, does it mean that in these countries the welfare state size is also can be bigger? Some scholars noted that the relationship between social trust and redistributive actions by governments can determine the size of welfare states. Moreover, the most important finding is that the missing link explaining the long-run sustainability of large welfare states could be the existing stock of social trust predating their very existence; history matters (Bjørnskov & Svendsen, 2012).

Veen & Yerkes (2012), while investigating the Dutch welfare state, noted the following findings:

Welfare state support is still high in the Netherlands and that support for the welfare state in transition is based on an increasingly shared normative ideal of obligatory reciprocity as well as on perceptions of deservingness

Individualization is expected to undermine welfare state support. However, processes of structural individualisation undermine welfare state support, but cultural individualization does not.

People with low levels of social integration are less supportive of the welfare state – irrespective of their economic interests, whereas people who cherish individuality – cultural individualists – support the welfare state. Their support, however, is related to their economic interests: it increases when their own socio-economic position weakens.

Individualization not only strengthens the normative ideals of freedom and self-actualization, it also makes people more aware of their vulnerability. It is this awareness that feeds welfare state support.

In short, social solidarity does not conflict with individualization, rather, it facilitates it. The increased insecurity in other spheres of social life, resulting from individualization, is compensated by creating a collectively organized safety net through social security. To some extent, this confirms Luhmann's thesis that the awareness of risks will increase in a risk society (Veen & Yerkes, 2012).

Despite neo-liberal and communitarian arguments that welfare retrenchment might not necessarily be excessively harmful, as informal social networks will take over the interventionist of the welfare state, the analysis does show ambiguous outcomes in that respect. First of all, the success of informal social networks in preventing deprivation is less compared to the success of the welfare state, refuting the criticism of state intervention. Second, it nonetheless needs to be underscored that the functional quality of informal social ties differs across welfare states (Reeskens & Van Oorschot, 2013).

There are numerous researches on happiness and welfare states. As mentioned above, there is a link between trust and the welfare state. Consequently, is it can be summarized that, if citizens do trust in the institutions and the capability, it can lead to the expansion of welfare states, and if this expansion can lead to more happy and satisfied lives of citizens of the least advantaged?

Gainer (2012), while assessing happiness within welfare states, mentioned the following:

Self-reported life satisfaction of the least advantaged does not improve from an increase in the size of the welfare state more than the self-reported life satisfaction of the average citizen. In short, the welfare state does not benefit the worst-off in a society in terms of happiness more than the average member does. Although there is a statistically significant and positive coefficient for the size of Welfare State and Rawlsian satisfaction—the magnitude of these estimations is relatively small. Even if the smallest Welfare State became the largest, the average happiness of the least advantaged would not increase by more than 12 %. Regardless of the measure of the size of the Welfare State, a one standard deviation increase in the size of the Welfare state impacts average happiness, inequality-adjusted happiness, and Rawlsian satisfaction identically. There is not a statistically significant difference between the effects on each. (Rawls' difference principle in the broader egalitarian and utilitarian literature: Rawls' difference principle can be viewed as a limited trade-off between egalitarianism and utilitarianism, with several significant differences. One such difference is that Rawls discusses 'primary social goods' instead of 'utility') (Gainer, 2012).

World Happiness Report (2020):

"This new evidence of the power of an environment to raise average life quality and to reduce inequality can explain the reason for the higher happiness of the Nordic countries largely in terms of the high quality, often hard-won, of their local and national social environments. The author compares the distribution of happiness among 375,000 individual Europeans in 35 countries with what it would be if all countries had the same average levels of social trust, trust in institutions, and social connections as are found in the Nordic countries. The new distribution does not change anyone's health, income, employment, family status, or neighborhood safety, all of which are more favorable, on average, in the Nordic countries than in the rest of Europe.

The current European distribution of happiness would shift significantly, with a higher mean and with much less inequality if the trust and social connection levels of the Nordic countries existed across all of Europe. Close social connections are very important; they are only modestly more prevalent in Nordic countries than elsewhere in Europe. It is the higher levels of social and institutional trust that are especially important in raising happy and reducing inequality."

CONCLUSIONS

The Welfare States are tools for dealing with risks. Risks can be various, but the most essential ones, in this case, are the risks citizens face on daily basis. It turns out that introducing welfare stigma reduces the socially optimal self-insurance and raises the socially optimal social insurance. It may be efficient for the society to operate at a point on its opportunity frontier where an increase in risk-taking decreases mean post-tax income and welfare stigma. Institutions can vary on this topic, as the insurance system can be governmental, private, and composition of both; consequently, welfare states can vary based on categorization. Social insurance (for unemployment, disability, sickness, healthcare) is based on the actuarial notion of calculable risks. As such, markets can produce social insurance.

At the same time, welfare states are a product of industrial society. Changes through decades from Materialist to Post-Materialist values have been followed up with the changes toward the service economy. Globalization and Individualism can be seen as a threat to the welfare state; a more collectivist mindset can lead to risk-sharing, and it will compensate for the gap between the poor and the rich. One of the factors affecting risk-sharing in society is trust. In other words, if citizens can rely on the government for the future, paying high taxes, reducing the risks of the less advantageous groups can be led to the expanded welfare states.

It was mentioned that, social risks as risks that do not result from individual choice but as risks that are (also) produced by the social system of production, and the risk of occupational disability in an industrial economy as an example of social risk. From a risk management perspective, one economic agent's risk will be another agent's reward or vice versa. It can be assessed by the Prisoner's Dilemma; the government can prevent it by involving, and decommodification is a crucial tool in this case. There is no "right" regulation of risks, and it is different from country to country, situation, or industry.

There are no clear shreds of evidence, what is the acceptable level of risk or risk aversion. But, it is clear that a risk-free environment is also not achievable. If the government cannot manage earlier to diminish the level of risks citizens face and deal with on daily basis, it is supposed to intervene when the rate is too high to be managed.

Citizens have various opinions about welfare states; therefore, trust in welfare states may vary from country to country. But, generally, it depends on the government's ability to handle the situation, for that reason, the capability of institutions can affect citizens' opinions. There are several types of research showing that trust determines the size of welfare states as well as three crucial features: high levels of political confidence, strong legal institutions protecting private property rights, and low level of bureaucratic corruption. Trust is an important mechanism for redistribution. Social trust can be measured by surveys, with the only question, whether people think others are generally trustworthy. While generalizing quantitative analyses on this topic, it can be observed that for Scandinavian countries the percentage is generally higher, than for other OECD countries.

"Self-reported life satisfaction of the least advantaged does not improve from an increase in the size of the welfare state more than the self-reported life satisfaction of the average citizen. In short, the welfare state does not benefit the worst-off in a society in terms of happiness more than the average member does."

To summarize, the questions related to risk, happiness, and trust still need much more investigations, but the most important point should be mentioned; countries with stronger welfare programs are dealing with everyday risks more efficiently, citizens have more trust in their governments and the distribution of happiness is significantly much more equal and high than in other countries.

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