Introduction

The 1990s have been a decade of big changes for welfare states. The adaptation process which in the United States and in Britain started in the 1980s has become part of policy-making also in continental European countries. The main objective of reform is to restore the compatibility of social policies with the changing economic and demographic contexts. In most cases, this objective is pursued by retrenching existing social programmes. Welfare retrenchment, thus, is not any longer an Anglo-Saxon idiosyncrasy. Countries such as Sweden, France and Germany, in which social policies are widely praised and contribute to the structure of national identities, have all curtailed their welfare states in the last few years.

In both waves of retrenchment, pension schemes have been a privileged target of governments' attempts to reduce spending on welfare. Pensions generally constitute the largest single item of social expenditure, so that successful cost containment in this area of policy is particularly beneficial to governments' budgets. In addition, pensions are directly exposed to the twin pressures of economic and demographic change. Economic changes, like globalisation, are reducing governments' ability to generate revenues. On the other hand, population ageing is resulting in increased pension expenditure. This is a powerful incentive for governments to take action. It explains why pension reform has been high on the agenda in most advanced industrial countries over the last decade.

In general, however, continental European welfare states are proving to be less vulnerable to cuts than their Anglo-Saxon counterparts. One way to explain this is with reference to their higher degree of middle-class integration. The United States, and to a lesser extent Britain, were retrenching residual welfare states. In the United States, the losers of welfare reforms had little potential for political mobilisation, and were de facto unable to influence policy-making. In Britain, although the inclusiveness of welfare arrangements before the Thatcher decade was significantly stronger, a political system which concentrates power in the Cabinet helped to neutralise the effects of external opposition to cuts in welfare programmes.

Welfare retrenchment in continental Europe seems to be different. The higher levels of coverage and generosity of social programmes there make social policies meaningful to larger sections of the population, including politically influential middle-income voters. Either through informal mobilisation or threats of electoral punishment, pro-welfare interest groups have managed to maintain strong pressure on governments, and to moderate their retrenchment initiatives. In addition, few political systems in western Europe offer the same level of power concentration of the Westminster model. Instead, most of them provide veto points, which can be used by external groups to prevent the adoption of unwanted legislation. This is perhaps most clearly the case in Switzerland.

This book, in fact, originated from a comparison of welfare retrenchment in Britain and in Switzerland. In the early 1990s, Switzerland went through its worst economic downturn since 1945, and the neo-liberal ideas that had inspired the Thatcher reforms of the 1980s gradually gained ground among Swiss elites. Employers, the powerful banks and the political right wing were increasingly arguing in favour of a more radical approach in economic and social policy, based on lower social expenditure, a more flexible labour market, lower taxes and so forth. The conditions were ripe for a shift in public policy like the one experienced by Britain in the 1980s. Nevertheless, Swiss policy-makers had to operate in a substantively different political system with different political institutions.

In Switzerland, policy decisions are generally the result of compromises that are indirectly supported by some 80 per cent of the electorate. As political scientists have pointed out, this is not due to a particular listening attitude of Swiss policy-makers. Rather, it is the Swiss constitutional structure which makes provision for power-sharing and offers veto points, such as referendums, to unsatisfied minorities. The result is that Swiss governments have tended to incorporate potential dissent, in order to reduce the risk of being unable to get legislation accepted. For this reason, the legislative process in Switzerland is among the most lengthy in Europe, and innovative policies are rather unlikely. Typically, viable compromises can be achieved only via incremental change.

As policy-makers started embarking on a rethinking of the welfare state, it became clear that Swiss political institutions were going to constitute a formidable obstacle to the neo-liberal ambitions of economic and political elites. The sort of reforms they were advocating were unlikely to generate the level of consensus that is usually needed to legislate in that country. Reforms were likely to be unpopular with large sections of the electorate, and were thus at a high risk of defeat in referendums. A 'Thatcherite revolution' was probably impossible in the Swiss institutional context, but could policy change be achieved at all?

To try to answer this question was the initial stimulus for this study, which, in general, is more concerned with the impact of constitutional structures and political institutions on the process of welfare state adaptation. I chose to concentrate on the particular area of pensions because that is where such institutional effects are more likely to be visible. In most industrial countries, public pension schemes are widely supported by the population and have an impact on the lives of large sections of the electorate. As a result, pension reforms are likely to generate strong opposition. Those who oppose reform will tend to exploit institutional veto points where available. Arguably, this will make the institutional obstacle to retrenchment more visible. For it is not institutions *per se* that impede retrenchment. They can provide an opportunity to influence policy, but there needs to be a social group prepared to take up this opportunity; otherwise the potential impact of institutions on policy remains unnoticed.

Since the UK and Switzerland are two rather extreme versions of majoritarian and consensus democracy respectively, I decided to include in the analysis a third country, France. This is a country that is generally ranked close to Britain with regard to its government's ability to impose policy change. However, in the area of pension policy, the involvement of the trade unions in the management of social security and the strong level of public support enjoyed by the welfare state have contributed to reduce the extent of governmental control over policy-making. In addition, a division within the executive in the 1993–5 period further diminished the level of power concentration. The result was that, in that period, the French government was forced to accept compromises to a more substantial extent than is normally the case.

This book also aims to explain why given paths to pension reform are adopted in some countries but not in others. It argues that the political limits to welfare retrenchment are country-specific and that, as far as pensions are concerned, they depend on the interaction between political institutions and the design of pension schemes. The former provide opportunities to affect policy, the latter structure patterns of interests in relation to pension policy. Political institutions can generate veto points and opportunities to influence policy-making for external interests. Pension scheme design, in turn, affects the perception of actor's self-interests, and may or may not create opportunities for politically feasible reforms. The way in which these two institutional effects interact is likely to have a powerful influence on the direction of reform.

The first conclusion of this study is that governments committed to reform pensions, and operating in political systems which offer substantial veto points, are likely to pursue their retrenchment initiatives in combination with concessions targeted on key potential opponents, and that such strategies can work. In Switzerland, the inclusion of measures which had been demanded by the left and by the labour movement in a pension reform package managed to strengthen its electoral appeal. The reform was eventually accepted in a referendum. In France, a government weakened by a division within the executive and worried about an upcoming presidential election managed in 1993 to obtain the acquiescence of the most radical sections of the labour movement by including some carefully designed *quid pro quos*, which responded to long-standing demands of the trade unions.

The significance of this finding relates to the initial questions from which this study grew, i.e. whether fragmented political systems, such as Switzerland's, had the capacity to adopt politically difficult reforms in the areas of pension and social policy. In the case studies reviewed here, fragmented political systems did manage to secure the adoption of unpopular cuts in pensions, when these were combined with *quid pro quos* for key external actors. This suggests that welfare state adaptation is politically feasible in systems characterised by numerous veto points, but will be less unilateral and will tend to include retrenchment as well as improvements in provision.

This is not to claim that a focus on political institutions alone can produce predictions with regard to policy outcomes. By looking at these rules we can get a hint of how the positions of the various actors will be aggregated, but we can say little on the final outcome unless we know what each actor wants. Actors' preferences in pension policy, however, are structured to some extent by the institutional design of the relevant programme, so that a combined focus on political and pension institutions can improve the predictive capacity of this model.

This brings me to the second finding of this study, which refers to the existence of a common pattern of *quid pro quos* in pension reforms adopted in countries which have pension schemes of Bismarckian inspiration. In France, but also in Germany and in Italy, the recent pension reforms and the proposals for future policy change have tended to combine cuts in the generosity of the schemes with a restoration of the original character of pension policy. In particular, the non-contributory elements which were integrated in these schemes to achieve general social policy aims are being removed and taken on (including financially) by governments. In all three countries the separation of non-contributory and insurance-based benefits is a key demand of the trade unions, which typically regard social security as an insurance plan covering the entire working population, as opposed to an area of state policy. The inclusion of such measures in reform packages that are mainly concerned with reducing expenditure can secure trade union support, or at least acquiescence.

These institutional effects are likely to become more important in future, as the main political cleavage in social policy-making seems to be shifting from the left–right axis to an opposition between governments, to a large extent regardless of their political orientation, and a pro-welfare coalition of interest groups, which is often led by the labour movement. This has long been the case in France where the Socialist governments of the 1980s clashed with the unions on a number of occasions. As new left-of-centre governments have been voted into power in Europe, this shift in the dominant cleavage in the politics of social policy has become more evident. In Germany, Italy and, to a lesser extent, Britain, the left-of-centre governments of the late 1990s are committed to continue reforming their welfare states, and the main confrontation is between themselves and the labour movement. Economic conditions allow very narrow room for manoeuvre and as a result the left, even when in power, has little choice but to adopt retrenchment policies in the area of welfare.

If, as I argue, the main cleavage in social policy reform is shifting from the left–right axis to an opposition between governments and a pro-welfare coalition, then the institutional explanation of policy outcomes will acquire additional relevance and possibly replace the ‘politics matter’ thesis as one of the key approaches to social policy analysis. The degree of influence that pro-welfare interest groups have on policy depends to a large extent on the opportunities provided by the political institutions. Absence of veto points means that governments will be able to go much further in the restructuring of their welfare state. In contrast, political systems that offer veto points will find it more difficult to adapt their welfare states and pension systems to a changing economic and demographic environment. As a result, they will need to develop more sophisticated strategies to secure the adaptation of their welfare arrangements.

More generally, this book argues that, despite the emphasis in current research on public policy on institutional resistance to change, governments in different political systems have been able to devise specific strategies which managed to bring about substantial policy change. Carefully designed reform packages stand a good chance of being adopted even in fragmented political systems, but then lead to qualitatively different adaptation processes. Veto points can be neutralised by integrating potential opponents in policy-making, or by targeting some key concessions on them. After all, the landscape of social policy in Europe is perhaps not as frozen as it might seem. The new problems that have emerged in the 1990s have demanded a quick response, which most governments were unable to deliver. However, as learning processes begin to produce results, we might see an acceleration in the restructuring of the European welfare states.

The book begins by looking at the socio-economic pressures on pension schemes, in particular those related to demographic change. It provides a picture of the factual background against which current pension policy-making takes place (ch. 1). Next the focus moves to theory. The questions and the hypotheses which have been briefly presented in this introduction are spelt out in a more detailed manner, and they are related to some of the most influential views on social policy-making (ch. 2). There I put forward a model for the analysis of pension reform which focuses on political institutions as an independent variable of pension policy. Chapters 3 to 5 are accounts of the political processes that led to the adoption of pension reforms in Britain, Switzerland and France. As far as possible, I have tried to follow a similar structure in the presentation of the case studies. First, I look at the institutional and political context in which reforms have been adopted; second, I provide a description of the country's pension system; third, I concentrate on the pension policy-making process; and, finally, I focus on the link between what has been observed and the theoretical framework presented in chapter 2. Finally, chapter 6 highlights the key elements that emerge from the comparison of the case studies, and links them to the theoretical discussion of chapter 2.

1 Dimensions of the pension problem: institutions, economics and politics

The long-term sustainability of current pension arrangements is one of the major issues with which advanced industrial societies will have to deal over the next few decades. The projected increase in the size of the older population, combined with a reduction in the number of workers, constitutes a significant challenge to the viability of existing pension systems, which, according to many commentators, need to be substantially reformed. While these general views are widely accepted, there is little agreement as to what the actual size of the pension problem is now and will be in future. Those who have analysed the phenomenon have reached conclusions that range from apocalyptic scenarios in which, if nothing is done, the elderly will appropriate increasing large shares of national income with massive detrimental consequences for the welfare of younger generations (World Bank 1994a; Thurow 1996), to less pessimistic ones, in which the occurrence of an increase in pension expenditure is accepted as a likely development, but it is felt that this will not constitute a major economic problem (Johnson and Falkingham 1992; European Commission 1995).

The evidence reviewed in this chapter suggests that gloomy predictions of a 'demographic time bomb' have little credibility. However, it seems clear that, when the baby-boomers born after World War II reach retirement age, pension expenditure will increase quite dramatically over a relatively short period of time. Most likely, this will result in a financing problem.

What is more, concern for pension scheme finances has been heightened by recent economic and political developments. First, the ongoing process of economic internationalisation is putting pressure on governments to reduce, or not to increase, rates of taxation. To do otherwise would put the competitiveness of their national economies at risk, with potentially serious consequences for their countries' prosperity (Gough 1996; Rhodes 1996). Second, countries willing to participate in EMU need to respect a number of economic criteria. In particular, a government budget deficit higher than 3 per cent of GDP is not considered as acceptable. As a result, countries committed to joining and remaining in the European single currency (such as France, Germany or Italy) have been forced to take steps to reduce public expenditure. Pensions, generally the largest single item of social expenditure, are an obvious target for saving measures. These elements, combined with the threat of a substantial change in the demographic structure of the population, constitute a powerful pressure on governments to take action. In this study, the term 'pension problem' refers precisely to this series of pressures on pension policy.

This chapter discusses some of the aspects that contribute to defining the pension problem. Above all, it aims to establish what are the conditions in which the pension problem emerges and in which debates on the future of pensions take place, or, in other words, the factual background against which political actors operate. In this respect, it constitutes the basis on which to build an analysis of the politics of pension reform.

First, it provides an overview of provision for retirement in industrial countries. It looks at the differences between pension systems and at their origins. Starting points can be important for the course of reform, because, as is increasingly being recognised, they tend to channel developments and debates in some given directions. Second, it focuses on the socio-economic pressures that are likely to affect pension policy over the next few years. The discussion covers demographic and expenditure projections as well as the variation in the living standards of the retired population. This review of empirical evidence concludes that there are real pressures on governments to take action in the area of pension policy, in order to continue providing income security in old age. Third, the chapter looks at the main options for reform available to policy-makers. These are analysed mainly in relation to their economic effects, although it is clear that they have different implications in so far as politics is concerned. That is why the chapter concludes by making the case for an analysis of the politics of pension reform. Pension systems are highly sensitive distributional mechanisms. They transfer huge sums of money across generations, time, occupational groups, income groups, genders and so forth. Their distributional equilibrium reflects the power relationship between the different political actors who designed them. The result is that, once a settlement is reached, departures from it are likely to be extremely delicate exercises. In particular, when the objective of reform is to achieve savings, policy change is likely to create winners and losers. That is why pension policy in general and especially the recent pension reforms have been characterised by an impressive level of political controversy.

1.1 The institutional level: an overview of pension systems

As in other areas of social policy, there are substantial cross-country variations in pension systems,[1] even if the analysis is restricted to a fairly homogeneous geo-political area, like western Europe. Similarity exists in the sense that virtually all countries have legislated old age pension programmes. Beyond that, it becomes more difficult to find consistency between different pension systems (Palme 1990: 147).

Several attempts to make sense of these variations have been made, some of which are reviewed below. In particular, researchers have tried to identify ideal-types of pension provision, which can be found in a more or less pure form in a number of countries. To a large extent, this exercise overlaps with the more general effort aimed at classifying welfare states, as pensions typically constitute the largest social programme and are often seen as the backbone of a welfare state.

The classification of welfare states in recent years has tended to revolve around three types, or regimes (Esping-Andersen 1990), or four depending on whether or not one considers southern European welfare states to constitute a distinctive category. This approach focuses mainly on the outcomes of social programmes, in terms of decommodification[2] and social stratification. A socialist or social democratic regime is found in Nordic countries. In this model, welfare arrangements (including pensions) cover the whole population and perform a fair amount of vertical redistribution, and access to benefits is less dependent on labour market participation than is the case in other countries. A second model, referred to as corporatist or conservative, is found in continental European countries. The key social programmes cover the working population only and grant earnings-related benefits which guarantee the maintenance of status differentials at times of inactivity. Those who do not participate in the labour market have to rely on often stigmatising social assistance schemes. Finally, a liberal regime is found in English-speaking countries. Its most distinctive characteristic is the preference for programmes targeted on the poorest sections of the population. It reinforces social divisions because

[1] Throughout this study the notion of 'pension system' is used to designate the totality of transfers to the older population which are either compulsory, provided by the state or encouraged by legislation (e.g. through tax concessions). This excludes other sources of income for the elderly such as earnings, private savings, social assistance and intra-family transfers. A pension scheme, by contrast, is understood here as a single arrangement which has the aim of providing income to older people. In virtually all industrial countries pension systems consist of various pension schemes.

[2] Decommodification is defined as 'the degree to which individuals or families can uphold a socially acceptable standard of living independently of market participation' (Esping-Andersen 1990: 37).

the affluent have no stake in these programmes. In addition, since benefits are often very low, it does not constitute an alternative to individual provision. The existence of a fourth regime of southern European welfare states has been postulated (Leibfried 1992; Ferrera 1996b). Its key features are a highly fragmented income maintenance system with a strong emphasis on old age pensions, the persistence of clientelism and a stronger reliance on the family as an alternative to labour market participation.

While works aiming at classifying welfare states like Esping-Andersen's have tended to focus on outcomes, studies dealing only with old age pensions have typically concentrated on the institutional design of the various systems and on their evolution in a historical perspective. Reference is often made to two distinct models of pension provision which were introduced at the end of the nineteenth century in Germany, Denmark and New Zealand. In 1889, Germany instituted a pension scheme for industrial workers. The scheme was meant to guarantee retirees a level of income related to their earnings while in work. Denmark (1891) and New Zealand (1898), in contrast, introduced means-tested pension schemes targeted on the poor (Myles and Quadagno 1997; Overbye 1996a).

These two models of pension policy had two very different underlying objectives. In the German case, the scheme introduced by Bismarck was part of a political project aimed at containing the rise of the labour movement. The adoption of a pension scheme, as well as of other social programmes introduced more or less simultaneously, was meant to buy the allegiance of the rapidly emerging working class. As a matter of fact, Bismarckian social legislation was accompanied by laws which banned the political organisation of workers (Alber 1986: 5; Baldwin 1990: 59–65). Understandably, the schemes were confined to industrial workers, as other groups did not constitute a threat to social stability, and Bismarck had no immediate interest in improving their conditions. The Danish scheme, in contrast, did not have such an overt political aim. Its introduction constituted mainly a modernisation of the existing system of poor laws. Its objective was to alleviate poverty across the whole population (Baldwin 1990: 65–76). Given their different goals, the two original approaches to pension policy used different means as well. The German scheme was financed by contributions shared equally by employers and employees (with a state subsidy); it granted earnings-related benefits; and entitlement to a pension was based on having paid contributions. Its overall result was status maintenance in retirement. In Denmark, by contrast, the 1891 pension scheme was tax-financed and means-tested, and granted flat-rate benefits. As such, it continued in an ameliorated form the tradition of poor relief enshrined in the previous system of poor laws.

In subsequent years, other countries followed the example set by