Economic and Social Security and Substandard Working Conditions

Growing Public: Social Spending and Economic Growth Since the Eighteenth Century. By Peter H. Lindert. Cambridge, U.K.: Cambridge University Press, 2004. Volume 1: *The Story.* xvii, 377 pp. ISBN 0-521-82174-6, $65.00 (cloth); 0-521-52916-6, $24.99 (paper). Volume 2: *Further Evidence.* x, 230 pp. ISBN 0-521-82175-4, $70.00 (cloth).

For nearly four decades economists have been telling us that there are no free lunches; in other words, every silver lining has a cloud. One of the favorite applications of the "no free lunch" principle is to the issue of welfare/social spending. Economists contend that the safety net resulting from tax-funded government spending on welfare, old-age pensions, health insurance, and the like comes at the high price of slower economic growth. The notion that welfare spending is harmful to the economy is quite old. David Ricardo maintained that "the clear and direct tendency of the [English] poor laws . . . is not, as the legislature benevolently intended, to amend the condition of the poor, but to deteriorate the condition of both poor and rich" (*Principles of Political Economy and Taxation,* 1817). One of the major conclusions reached by Peter Lindert, in his important and timely two-volume study of the evolution of social spending over the past two centuries, is that economists have greatly overstated the costs of the welfare state. Indeed, the empirical evidence suggests that "the net national costs of social transfers, and of the taxes that finance them, are essentially zero" (p. 29). It would appear that free lunches do exist, for reasons that I will discuss below.

Lindert's discussion of the costs and benefits of the welfare state is only one part, albeit the most eye-catching part, of this wide-ranging work in comparative economic history. Volume 1, written for non-specialists, presents "The Story"; it is tailor-made for upper-level undergraduate courses in economic and social history, public policy, and welfare economics. Volume 2 presents "Further Evidence," including the regression results that underlie the findings presented in the first volume, and eighty pages of appendices. Graduate students and scholars studying the welfare state will want to read this volume in conjunction with Volume 1. For those who want to probe even deeper, most of the underlying data are available on Lindert's home website at the University of California, Davis.

After two introductory chapters laying out "patterns and puzzles" and major findings, Volume 1 is divided into three parts, covering "the rise of social spending" (Chapters 3–7), "prospects for social transfers" (Chapters 8–9), and the effects of social spending on economic growth (Chapters 10–12). Chapters 3 and 4 examine the role played by poor relief in Europe and America before 1880. Lindert shows that publicly financed poor relief (welfare) was quite small in all countries before the late nineteenth century. The reason is simple—political voice was concentrated in the hands of the elite, who had little interest in taxing themselves to help others. Moreover, there was not a simple linear relationship between the share eligible to vote and social spending. The extension of the

franchise to the lower-middle class, as occurred in England in 1832, often led to a reduction in welfare spending, because small capitalists, shopkeepers, and yeoman farmers were even less willing to pay poor rates than was the labor-hiring elite. Widespread support for welfare spending did not come about until the vote was extended to the working class.

Chapters 5 and 6 (and Chapter 15 in Volume 2) examine public schooling in the nineteenth and twentieth centuries. The three major determinants of the rise of mass public schooling in the nineteenth century were "elite self-interest, democracy, and decentralization" (p. 87). Germany and the United States, which "left primary schooling finance to decentralized local control," were the early leaders in public elementary education, while Britain, which did not, lagged far behind. Chapter 6 offers explanations for the decline in U.S. leadership in public education in the second half of the twentieth century.

Chapter 7 (together with Chapters 16 and 17 in Volume 2) offers explanations for the rise of social transfers (welfare, unemployment insurance, pensions, health care, and housing subsidies) after 1880. The countries whose social spending increased the fastest from 1880 to 1930 tended to have high and rapidly growing per capita income, political voice for the working class, and a relatively large share of the population over age 65. The most important reason for the increase in social spending was the extension of the franchise to low-income workers, who were strongly in favor of redistributive transfer programs. Lindert explains the finding that "a greater share of elderly in the population raised all kinds of social transfers," not just spending on pensions, as follows: "An older population tipped social sentiment and the political balance of power in favor of granting security of income and wealth" (p. 184). In 1880 and 1890, the leaders in social spending as a share of GDP were the Scandinavian countries and the United Kingdom. By 1930, Weimar Germany had taken the lead in social spending, followed by Ireland, Scandinavia, the United Kingdom, and New Zealand. The period from 1930 to 1960 witnessed huge increases in social spending in all the OECD countries for which Lindert has data. This "social transfer revolution" was caused not only by continued income growth, democratization, and population aging, but also by the effects of the Great Depression, World War II, and the spread of communism, which led middle-class voters to feel more of an affinity with those in the working class. In particular, the Great Depression "gave middle-income voters new reasons to believe that they and their families might sink economically and might need a safety net." Middle-class feelings of social affinity were stronger in countries where the population was ethnically homogeneous and where "the middle and bottom income ranks were more intermobile" (p. 189).

Chapter 8 examines the forthcoming "public pension crisis" that will result from the continued aging of the population. OECD countries are faced with "three unattractive choices": raise the tax rate on those currently working; cut non-pension transfers; or reduce pension generosity. Lindert predicts that, while total spending on pensions will continue to increase, pension benefits per elderly person will decline as a share of average income in those countries with 15% or more of the population aged 65 and over. So long as the aged bear most of the cost, "the public pension crisis will not become a general crisis for the welfare state" (p. 204). In Chapter 9 Lindert argues that countries in the second and third world face serious welfare/pension crises. These crises are as much a result of "larger political and budget breakdowns" as they are of population aging (p. 221).

Chapters 10 through 12 (and Chapters 18 and 19 in Volume 2) address the free-lunch puzzle. Why is it that welfare states like the Scandinavian countries do not have slower economic growth than low-spending countries like the United States, Japan, and Switzerland? Lindert offers several reasons. First, welfare states typically have pro-growth tax policies—they fund social spending with taxes on consumption and labor income, rather than capital. The tax mix is regressive, but avoids the huge disincentives that economists are always warning us about. Thus, workers are not only the major beneficiaries of social transfers, they also largely pay for them. Second, government subsidies to early retirement and generous unemployment compensation have little effect on GDP, because welfare states use these policies "as a way to get the least productive workers out of their jobs" (p. 252). Third, some social transfer policies, in particular child care support and public health care, raise GDP per capita. Finally, welfare states have reduced the distorting effects of social programs and lowered administrative costs by adopting the principle of "universalism": "The most efficient tax-transfer world is one in which everybody is entitled to similar basic income support and basic services, while facing the same tax rate on all consumption" (p. 302).

This is an outstanding work in comparative economic history, which I look forward to assigning to my students. Lindert asks big questions, and painstakingly collects the data needed to empirically answer these questions. The data sets he constructed for this work represent a major contribution to our understanding of the historical welfare state, and the fact that he has made them available on his website is an added bonus. If readers question any of Lindert's conclusions (some of which are surprising and provocative), they can go to the website, download the data, and judge for themselves.

My only quibbles are with the organization of the two volumes. Chapter 6, on the late twentieth century decline in U.S. leadership in public education, seems out of place in Volume 1, while some version of Chapter 13 (Volume 2), which provides "a minimal theory of social transfers," should appear early in the first volume. Finally, in preparing Volume 1 for non-specialist readers, Lindert has sometimes left out much of the supporting information—some chapters would have benefited from additional evidence that has been relegated to the second volume. For example, Chapter 7, on the rise of social transfers since 1880, which in my opinion is the most important chapter in Volume 1, is too short (at 20 pages, it is one-half the length of Chapter 6). I would have split Chapter 7 in two, one part covering 1880–1930 and the second covering 1940–1995, and beefed up both chapters with material from Chapters 16–17 in Volume 2.

However, these are minor issues. Any reader who wants more information than is presented in Volume 1 can turn to the second volume, to Lindert's previously published journal articles, and to the data sets located on his website. Those readers who dig deeply in these volumes will be richly rewarded. *Growing Public* greatly increases our understanding of the rise and the effects of social spending, and is a welcome empirically based response to the ever-growing economic literature arguing that the costs of the welfare state are unacceptably high.

George R. Boyer
Professor of Labor Economics
School of Industrial and Labor Relations
Cornell University