

# Inequality in Western Europe

## Why the social-liberal model has failed

### Niels Charlier

Over the past few decades, the wealth gap in Western Europe has been widening. Several studies have shown this<sup>1</sup>. In other words, the rich are getting richer and the poor are getting poorer. This is very remarkable for a place in the world where democratic socialism has traditionally been the strongest and where government policies are aimed at the most optimal combination of capitalist efficiency and social justice. Many European states are on the edge of total bankruptcy and fear is growing that the welfare system as a whole is at stake. Although major protest is increasing against feared reductions in social rights, voting behaviour has been moving towards the conservative side.

Recovery of the Global Financial Crisis has been slower and more difficult in the European countries than it has been in other countries. Many governments are sinking away in to a major debt crisis. But some major economic challenges are older.

The globalisation of the economy has stirred up rock hard competition, particularly with Eastern Europe and the Far East where wages and taxes are much lower. As a consequence industry and business is moving away to these countries. On top of that, Western Europe is facing

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an ageing population which will very soon increase the cost of publicly funded pensions and health care and simultaneously decrease the number of working people paying for these services.

As an illustrative example we will consider Belgium, a small country in the heart of Western Europe with strong



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economic ties with Europe's two biggest economies: France and Germany. This country provides us an interesting mix of social-economic issues, huge debts and cultural conflict. The political economic model in Belgium, as in other continental countries, is often referred to as the 'Rhine model of capitalism', which has its roots in modern Germany and is often opposed to the 'Anglo-saxon model of capitalism' (in the English speaking world).

The major practicalities of the Rhine model include a strong social security net, the provision of education and health care by non-profit institutions rather than competing businesses and open negotiation between unions and employers on social contracts, including wages (rather than letting these be determined by the market). The Rhine model is often praised by politicians on both sides of the political spectrum. Even the most right-wing free-market parties in Belgium consider the provision of health care to be one of the fundamental tasks of government.

One of the frustrations of the more conservative side though is a certain dependency culture and mad bureaucracy that is often claimed to be institutionalised by the left-wing parties. There is definitely truth in this claim. For example, in Belgium and the Netherlands there is a phenomenon called the "pillarisation" of society. As a form of compromise between portions of society with different ideologies (called "pillars"), different institutions were organised for each of them: schools, trade unions, banks, scouting organisations and so on. For example, there is a socialist health fund, a liberal health fund and a Christian health fund, all of which are subsidised by the government.

<sup>1</sup> For example, the Paris-based Organization for Economic Cooperation and Development (OECD) released a report on income inequality in 2008, which covers developments spanning 20 years in 30 countries.

Traditionally, families would be loyal to their pillar across generations. This has been less and less the case over the last few decades, as voters become less predictable. However these different institutions still exist. Belgium is also divided along a cultural line, between northern Dutch-speaking Flanders and the southern French-speaking Wallonia. Wallonia, once a very prosperous region, has been struggling with mass unemployment for decades since its old coal mine industry declined. Socialists have been the main power in politics in the south ever since.

A great portion of the people live off unemployment incomes (often for several generations) or work for the government. Local governments are often corrupt in the way they hand out contracts and subsidies. The Flemish North has evolved in the meantime from a rural area to a rich economy based on technical knowledge and small businesses. The Flemish overtaxed middle class has become increasingly frustrated, as they feel they are supporting dependency creating governance that would gain no elective benefit from stimulating innovation.

Conservatives and liberals want to minimise bureaucracy and be stricter with those who are, as they say, taking advantage of welfare. The main goal would be to reduce debts and taxes and save the social security net for those who really need it. But this is not the only reason for the success of the right. Apart from enormous economic issues, there is also a “spiritual crisis” that causes unrest.

The decline of religion and traditions, globalisation, multiculturalism, and the rise of consumerism and increasing work pressure have left people with the feeling that something is “missing”, something intangible which they can rely on and binds people together. Conservatives promise to fill that gap through the ideals of family values, respect for authority and nationalism. (French president Sarkozy tried to open a debate on the French identity, which tragically turned in to a racist fest.) Conservative intellectuals like to blame the influence of the sixties generation, who questioned the existing fabric of society.

Conservatives do have a point to make on the rise of materialism and the lack of community spirit but they are wrong to blame the sixties. The spiritual crisis is the logical conclusion of a corrupt and immoral economic system that has been going on for centuries. The mistake that the generation of the sixties made was their dramatic failure to correctly identify the causes of what they were protesting. Instead they turned to ideologies with the wrong answers. And still today, the left fails to make the right connections.

In March 2010, Belgian newspapers reported that the wealth gap (calculated by the ‘Gini-coefficient’) had increased during the past few decades<sup>2</sup>. This is ironic considering socialists have been part of coalition governments for over forty years. A report two months later stated that in the past two years the cost of a home had increased twice as fast as wages<sup>3</sup>. Can it be so hard to link these two things together? Could it be that the rising cost of land is an important factor in making the poor poorer and the rich richer?

There are a few things that are widely accepted by politicians and economists along the political spectrum. In the near future, we will all have to work harder, work longer and accept a decrease in wealth. Each of us (read: everyone except for some) will have to pay their share of the cost.

There is no alternative for being able to pay back the debts and to afford future pensions. But doesn't this go against common sense and intuition? Isn't it the case that productivity has multiplied over and over again the past few centuries because of the gifts of technology? Should that not mean that life becomes increasingly easy and more comfortable?

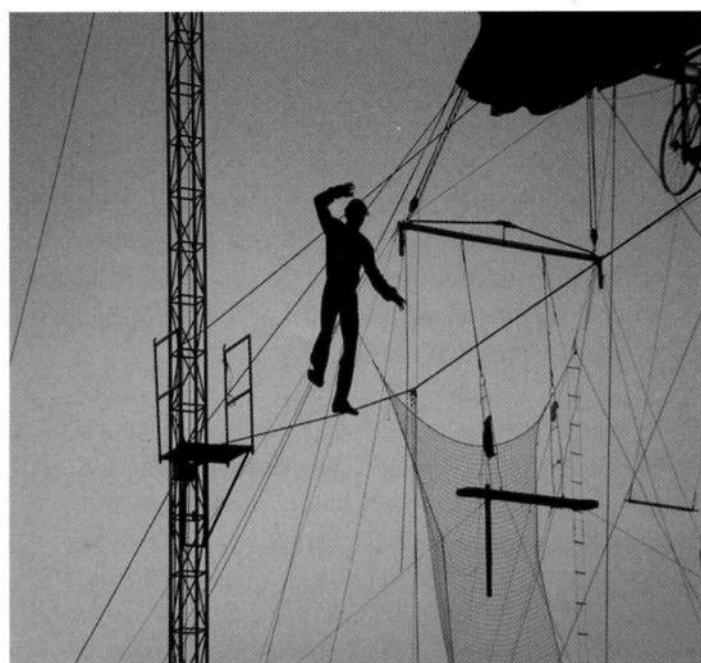
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The fruits of this increased productivity must be benefiting someone. (It is quite remarkable that conservatives care more about those on the social bottom who take ‘advantage’ of unemployment benefits than those on the social top who are getting richer as they sleep, though they are both funded by others’ work.) The financial crisis is usually treated as if it were an external, unavoidable force or natural disaster that needs to be cleaned up. Some on the left grumbled that “bad guys” did it, but no structural explanations were offered.

In Belgium however, there are other conflicts that dominate politics. Brussels, the capital of Belgium and de-facto capital of the EU was originally a Flemish city, but has evolved since the formation of Belgium in 1830 to a mainly French enclave within Flanders.

<sup>2</sup> A study done by the Directorate-general Statistics and Economic information of the Belgian federal government in March 2010 showed the Gini coefficient had increased from 0.238 in 1990 to 0.376 present.

<sup>3</sup> Based on a study done by consulting firm McKinsey in May 2010.



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The Flemish are still half traumatised by their history. Being treated as second-class citizens by a French upper class, they fought a long political and social battle. This explains why they are terrified of the so-called 'Frenchification' in the area. The Flemish country side around the city is being pushed away due to the urban sprawl of Brussels.

Many Flemish politicians have already stated the situation is mainly a social problem: wealthy people wanting to escape the city are attracted by the near-by rural side, which makes land prices unaffordable for the children of the original inhabitants. This problem in fact occurs around all cities, though in this specific case it is given a cultural dimension: the original population feels overpowered and disrespected by the newcomers who, unwilling to speak Dutch, expect the neighbourhood to adapt to them rather than the other way around. In the end, Frenchification really is gentrification. In Belgium, disputes about land might not lead to violence like it does in many other places of the world, but it does lead to recurring political quarrels and instability.

Migration is easily blamed for the urban sprawl. The truth is that, like in all cities, a high number of unused buildings or land proves that space has not run out in the inner city. Dilapidated neighbourhoods are everywhere. There is clearly a problem of land speculation and bad governance. New migrants, hoping to find the Promised Land in the heart of Europe, soon get disappointed as they remain excluded from the community, and turn criminal and violent.

A great part of the solution would be to charge a Land Value Tax as public revenue to provide public services, as Georgists have been advocating for over a century. This would end speculation on land and reduce its cost. It would stimulate an efficient use of land, and clean up the bad neighbourhoods.

It would create jobs and provide a fund to give proper shelter to the homeless. It would seriously reduce urban sprawl allowing rural land to remain rural land and, by extension, allow Flemish land to remain Flemish land. Land Value Taxation would solve cultural conflicts by reducing the need for communities to compete for land, and making regions and cities self-reliant. But the benefits go much further.

The message of the Georgists is that governments should be using the most natural forms of revenue: returns to common resources and natural monopolies like land and money creation. This would resolve the enormous financial difficulties European countries are facing. It would release the enormous community value that is locked up in land, and stop it from flowing towards those who control the financial system. It would provide the funds for the ageing population. By reducing taxes on work, savings and trade, the local economy could be made competitive again. It would end the frustration of the overtaxed working middle class. So what is stopping Western Europe from taking these measures?

Liberals suggest a tax shift from labour to consumption. The left suggest a tax shift from labour to capital. Though both suggestions deliver no good solution, this shows just how desperate the need for a better revenue system is. Many are trapped in a 'Robin Hood' philosophy: take from the rich to give to the poor. But the real effects of these sort of taxes is that the rich always find a way to avoid them, the working middle-class is overtaxed and the poor get trapped in poverty and dependency. Moreover, this way of thinking completely ignores the most fundamental question: how did the rich get so incredibly rich?

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The European ideologists simply miss the intellectual tools to draw the right conclusions. They are trapped in an artificial one-dimensional reality. The Rhine model tries to create social justice through negotiations between employers and employees. This traditional division between employers and employees – labour and capital - completely ignores the special role that the land and financial markets play in the distribution of wealth.

Most modern economists do not make a distinction between capital and land. Neither do they make a distinction between real capital and money, which is only a tool for exchange. When missing these so fundamental concepts, there is no way to draw the line between what is rightfully public and what

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is rightfully private. In fact, the debate isn't even there. There is not even a minority that advocates Land Value Tax, as exists in the UK. There is no continental Fred Harrison. The responsibility of social scientists is overwhelming. Promoting a European version of Georgism would require a slightly different approach to the Anglo-saxon, libertarian Georgism. Libertarian thought – which is very focused at small government – is part of American culture, but this is not the case in Europe.

George himself was not a libertarian. He promoted publicly funded education, health care, research, social care, museums, transportation, and more<sup>4</sup>. In fact, he saw the growth of government as a natural evolution. George didn't want government to be small, per se. He wanted it to be efficient, to avoid corruption and unnecessary bureaucracy in order to use the common funds only for the common good.

Land Value Taxation makes governments financially as well as democratically accountable. When governments waste their revenue on bureaucracy or ineffective measures, their revenue shrinks; however, if they invest their funds in a clever way, they create room for their own growth.

Governments can therefore only grow organically and in an efficient manner. European ideologists easily reject the idea of paying tax for received benefits. It seems contradictory with one of their basic principles: that the strongest should carry the heaviest weights. This however, is only seemingly so.

The value of land, as the classical economists taught us, is created by the community as a whole. The productivity in an area, due to cooperation and knowledge, is what makes land valuable. Naturally, the strongest and smartest will contribute to this value more than those which are weaker even though, unlike in the case of labour and capital, one cannot determine who contributed what. I will explain this by an allegory.

Imagine a group of people living on a deserted island. They need to collect wood for burning. They agree that everyone can use their own collected sticks for personal use. Some will be able to carry more than others. At some point however, they find a fallen tree. They decide that if they all work together, they can lift it up and carry it to the camp. Once the task is done, they decide to give everyone an equal share of the wood. While the strongest clearly carried more of the tree's weight than others, the result is still indivisible, as it was the joint effort and cooperation of the group that made it possible to carry the whole tree. In the economy, the value of land is like the tree, while the value of labour and capital are like the sticks.

Most georgists pay little attention to welfare. They usually point out that by creating much more opportunity the need for welfare is reduced. While this is true, welfare still has a role to play in the georgist system. Community-created wealth can be used to help those who are physically less able, or simply have more difficulties to find their place in society.

These public services do benefit the whole community, as they provide security and safety for all. It would also stimulate self-reliance and innovation and does not make anyone feel that they are being penalised for their effort. A georgist revenue shift could prevent the feared collapse of Europe's social system and market economy. But that would require a revolution of thought, from redistribution and robin-hoodism towards predistribution<sup>5</sup> of the common resources. This would create 'real' Social-liberalism, as Georgism is the most social and most liberal system possible.

<sup>5</sup> Term borrowed from Joseph Huber, German economist.



<sup>4</sup> "All social advance necessarily contributes to the increase of this common fund. (...) Here is a fund belonging to society as a whole from which without the degradation of alms, private or public, provision can be made for the weak, the helpless, the aged; from which provision can be made for the common wants of all as a matter of common right to each..." – Henry George, Social Problems, Chapter XIX: The first great reform