

# Structural change and the politics of dualization

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## 1. *Introduction: the missing link between structural change and increasing inequality*<sup>1</sup>

Poverty, inequality, and social exclusion are back on the political agenda in many rich democracies of Western Europe and North America, not only as a consequence of the Great Recession that has hit the global economy since 2008, but as a consequence of a long-term trend towards increased inequality that began some time ago, as demonstrated in the well-known 2008 OECD report «Growing Unequal?». Initially thought to be a development limited to the United States and the United Kingdom, wage inequality has also risen significantly in many western European countries as well as Korea and Japan; France and Belgium have so far for the most part resisted the trend. Although wage dispersion has increased in Scandinavia as well, it tends to be significantly lower than in the other OECD countries. Increasing wage inequality is largely said to be the result of the high-paid doing particularly well, not only relative to low earners, but also middle earners. Nevertheless, in many countries the incidence of low pay has increased significantly as well, not only in the UK and US but also especially in Denmark and Germany, where it has historically been much lower (OECD 2010, 295). For some observers the increasing levels of inequality in the UK and the US might not seem surprising given their market-liberal tradition. What seems surprising, however, is that

<sup>1</sup> This contribution summarizes the arguments and findings of the book *The Age of Dualization: The Changing Face of Inequality in Deindustrializing Societies* (edited by P. Emmenegger, S. Häusermann, B. Palier and M. Seeleib-Kaiser, Oxford University Press, 2012).

wage inequalities have also increased in social market economies of Continental Europe and Japan during the 1990s – a period characterized by many changes in labor market policies.

Our main argument is that tracing this increase in inequality back to mere structural factors would be a mistake: the missing link between structural change and increasing inequality is politics, notably the politics of dualization. If one wants to understand the dynamics of increasing inequality in the developed world, one needs to study the choices governments make in the light of the challenges that structural change has brought upon advanced capitalist democracies.

Three structural developments seem particularly relevant in this respect: deindustrialization, the feminization of the workforce, and globalization. Deindustrialization has led to a significant decline of relatively well-paid jobs in manufacturing, even in those countries that still heavily rely on the manufacturing sector to generate wealth such as Germany and the Scandinavian countries. Today, employment in the service sector outnumbers jobs in the industry in all OECD countries. Initially, deindustrialization has led to an expansion of welfare provision through early retirement schemes or similar programs in many countries, especially in (Continental) Europe (Iversen and Cusack 2000; Ebbinghaus 2006). At the same time Western democracies have witnessed job growth in the service sector, which is traditionally less regulated and unionized. Combined with low levels of productivity growth in the service sector and an increasing return on skill investments this is said to have accentuated wage pressure on low-skill employment (Iversen and Wren 1998; Baumol 1967). Moreover, it has been argued that Western democracies are witnessing a skill bifurcation between high and low general skills (Fleckenstein, Saunders and Seeleib-Kaiser 2011).

Closely associated with the process of deindustrialization is the feminization of employment. In recent years, women have increasingly entered the labor market. Female employment rates approach or even match male employment rates in many countries, especially in the English-speaking countries and Scandinavia (Oesch 2006). However, the feminization of the labor force has led to new challenges. Women suffer from discontinuous employment careers, because women are more likely to interrupt their working life in order to tend to family needs (Estevez-Abe 2005). Women work predominantly in the service sector and

often in nonstandard employment relationships (Oesch 2006). In parallel, the massive entry of women into paid labor has been accompanied by a destabilization of traditional family structures (Esping-Andersen 1999).

Finally, globalization is identified in the literature as a further structural force, restricting the autonomy of the nation state (cf. Held *et al.* 1999). Competition from low-wage countries has intensified the pressure to constantly increase productivity and shed low-skilled jobs in the manufacturing sector within the advanced economies of the North (cf. Wood 1994). The inflow of low-skilled migrants with weak labor market attachment has placed further pressure on labor markets. The internationalization of capital markets is said to have reduced governments' autonomy to tax capital (Scharpf 1991; Genschel 2002).

Even though these structural challenges are massive and real, they do not directly translate into growing inequality. Labor market policies, social policies, and wage-setting arrangements matter enormously for the form and extent to which structural challenges affect labor market patterns and the distribution of resources in a society. The ongoing variation between countries regarding the spread of unemployment, wage inequality, labor market (de-)regulation, and social policies testifies of the importance of politics.

The key role of politics can be seen in three interrelated areas. The most visible labor market trend during the past decades was an increase in unemployment, and especially long-term unemployment, across the OECD. Many countries have experienced a step-wise increase in unemployment rates during the past three decades. Moreover, in many countries of Continental Europe, unemployment has become long-term (12 month or more) or even persistent for a substantial percentage of the unemployed. In most countries, the non-employment rate of people with low educational attainment is above 50 percent. Even though labor market divides were never fully abolished during the *Trente Glorieuses* of welfare capitalism, the increase in long-term unemployment has created a deeper divide between those having a job and those persistently lacking one. In most cases, the crisis has even increased unemployment, bringing it to numbers comparable to the unemployment crisis following the 1973 oil price shock (OECD 2010). The development of unemployment rates and patterns is however not uniform across

rich OECD countries. In contrast to much of Continental Europe, low levels of long-term unemployment can be observed in Scandinavian countries and in the United States. Although not at the comparatively low levels of Scandinavia or the US, long-term unemployment in the UK has also been below the EU-15 average since 1985. While it can be argued that the low levels of long-term unemployment in Scandinavia are at least partially the result of a strong commitment to active labor market policies, the relatively low levels of long-term unemployment in the UK and US seem not only to reflect the flexibility of the British and American labor markets, but also the limited support for unemployed workers, who drop out of unemployment support schemes (and statistics) sooner than in the other countries.

A second key change has been the de-regulation and flexibilization of employment contracts: the standard employment relationship, a core element of the post-WWII settlement in many European countries, is clearly on the retreat through the increase of atypical employment contracts, such as fixed-term contracts and (involuntary) part-time employment (Standing 2009). Despite the overall trend, stark differences between the countries can be discerned. According to the OECD employment database, part-time employment reaches levels of 20-30 percent in countries such as the UK, Australia, the Netherlands, and Switzerland, whereas it remains around 10 percent of the workforce in Greece, Portugal, Finland, and France. Moreover, part-time employment affects women much more than men: in a majority of OECD countries, female part-time employment exceeds 30 percent of female employment. Temporary employment, by contrast, is particularly widespread in the Southern European countries and – more generally – among young people. In Spain, France, Portugal, and Italy, over 45% of young labor market participants (15-24) are employed on temporary contracts (OECD 2010). Eichhorst and Marx (2012) provide further evidence on variation of atypical employment within Continental Europe, Kroos and Gottschall (2012) on atypical employment in the service sector in France and Germany, and Häusermann and Schwander (2012) on varying patterns of atypical employment across welfare regimes.

New inequalities, however, are not just a result of structural labor market changes, but they may also be a result of social policy developments. The 2008 OECD report itself highlights that although labor market developments have been a key driver

of increasing inequality, social policies have become less effective in reducing inequality and poverty during the past decade. As social inequalities and poverty have increased, a key question to be addressed is to what extent this has been the result of policy changes. Historically, market income inequalities and poverty have been attenuated by redistributive social policies. Contrary to arguments about «frozen welfare state landscapes» (Esping-Andersen 1996, 24) and the stability bias of path dependence (Pierson 2001), social policies have indeed been extensively reformed in many countries and may have subsequently lost some of their redistributive capacities (Gilbert 2002): a trend towards means testing, activation, and «privatization» of old-age security can be discerned in many countries. Moreover, while in a number of countries the social assistance reciprocity rate increased as a consequence of long-term unemployment and the subsequent *implicit disentanglement* of unemployed workers within earnings-related unemployment insurance, in a number of countries *explicit changes* in unemployment insurance programs have contributed to this development (Seeleib-Kaiser 1995). These reform trends are very likely to have contributed to the overall increase in inequality. Hence, differences in social policy designs partly explain differences in the extent to which inequalities and divides have expanded during the past decades. This is indeed one of the main findings of our research: social policy can either smoothen or amplify the divides resulting from labor market inequalities. For instance, Häusermann and Schwander (2012) show the differential effects of welfare regimes on insider-outsider divides: while Nordic and liberal welfare regimes reduce income gaps between insiders and outsiders, Continental and Southern welfare states even increase them. Tomlinson and Walker (2012) show how social policy structures recurrent poverty in the UK and Germany, and Emmenegger and Careja (2012) find that social and migration policy reforms strongly contribute to shaping the profile of insider-outsider divides. Hence, there is no direct link between structural changes and distributive outcomes. Both existing policies and policy reforms play a crucial role in shaping these outcomes.

In other words, we emphasize the importance of choice: structural pressures do not directly translate into policy change. Governments have to decide how to react to structural pressure, and they do so in the light of past policies, existing institutions,

power relations but also political goals and strategies. Liberalization might be considered one obvious political strategy for governments to pursue, especially if one takes into account the ideological dominance of economic liberalism during the past decades. Liberalization is generally understood as a strategy of pushing back the state in the domains of economic and labor market regulation as well as in social policy. In the context of the changes witnessed in the German political economy, Streeck (2009) has argued that a political strategy of *liberalization* has been pursued, and he identifies liberalization as a kind of a megatrend underlying all policy developments in advanced capitalism. We argue, however, that liberalization is not the only strategy governments have pursued. Rather, we have been witnesses of a political strategy which we call *dualization*.

## 2. *What is dualization?*

Various related concepts – such as dualism, dual labor markets, insider-outsider divides or dual welfare systems – have been developed in the literature, so that we feel a few sentences on these concepts might be helpful to situate the terminology we propose thereafter. The notion of *dualism* was initially developed in micro-sociological analyses investigating firms' behavior and labor market developments (Doeringer and Piore 1971; Stinchcombe 1979; Berger and Piore 1980). The work on *dual labor market theory* emphasized the distinction between primary and secondary labor markets. In this approach, the primary labor market is characterized by good working conditions, high wages, secure jobs, and promotion prospects, while jobs in the secondary labor market are poorly paid, unstable, and characterized by bad working conditions. According to Piore (1980, 24), dualism within the labor market arises when portions of the labor force tend to be insulated from uncertainty and variability in demand (primary labor market), while others have to weather the fluctuations in demand (secondary labor market). In this sense, the notion of dualism refers to the outcome level of labor market divides.

Beyond the field of labor market theory, critical welfare state analyzes have focused on the concept of a «*dual welfare system*» (Tussing 1975) in the United States for some time.

According to this line of research, different social protection policies are geared to the poor and the non-poor (cf. Weir, Orloff and Skocpol 1988). In this sense, the notion of dualism refers to an institutional difference, rather than a structural one. Very much in line with this argument, Leibfried and Tennstedt (1985) have argued that historically the German welfare state has systematically differentiated between *Armenpolitik* (policy for the poor) and *Arbeiterpolitik* (policy for workers). More recently, the work by Hacker (2002) has emphasized the divided nature of the American welfare state. In a similar vein, Seeleib-Kaiser, Saunders and Naczyk (2012) show that while post-war welfare systems were aimed at harmonizing and unifying social protection, either through a unique encompassing model or through the multiplication of similar social insurance schemes, dualist strategies in welfare reform have re-surfaced mainly through strategies of privatization.

A final related strand of research originated in the work of labor market economists, emphasizing the micro-level and highlighting the rationale of firms, employers, and unions. The work on *insider-outsider politics* and strategic bargaining emphasized differences between the employed and the unemployed (Blanchard and Summers 1986; Lindbeck and Snower 1988; Saint-Paul 1996; 2002). Most importantly, these authors have stressed that labor market insiders face incentives to seek higher wages at the cost of jobs for outsiders. Recent work by political economists and political scientists has focused on such insider-outsider politics from a more macro-political perspective, trying to understand the mechanisms and processes leading to the creation of outsiders, understood more broadly as both the unemployed and workers in non-standard employment relationships (cf. Rueda 2005; Seeleib-Kaiser, van Dyk and Roggenkamp 2008; Emmenegger 2009; Schwander and Häusermann, forthcoming). The focus of this research goes beyond the mere labor market to also include the analysis of party politics, elections, and various policies (including labor market and welfare state reforms).

Given these related but distinct roots of the concept of dualist developments in labor markets and policies, there is a risk of conceptual confusion with the term dualization, as it might refer to structural patterns, policies, politics, or even outcomes. Hence, we suggest a terminology which delimits the term «*dualization*» to denoting a *process by which policies increasingly differentiate*

rights, benefits, and services provided to different categories of recipients. Thereby, the position of insiders may remain more or less constant, while only the position of outsiders deteriorates. Alternatively, policies may lead to the creation of new categories of outsiders that were previously treated according to the same rules as insiders. Thus, dualization is a process that is characterized by the differential treatment of insiders and outsiders and that can take the form of newly created institutional dualisms or the deepening of existing institutional dualisms (*policy output*). At the *outcome* level, the process of dualization is very likely to lead to greater social *divides*, but this is not necessarily the case, as we can witness dualization at the policy output level without increasing divides at the individual outcome level, if, for instance, outsider policies are relatively generous. Hence, conceptually we differentiate between process (dualization), output (institutional dualism), and outcome (divide). Figure 1 displays our conceptual framework graphically.

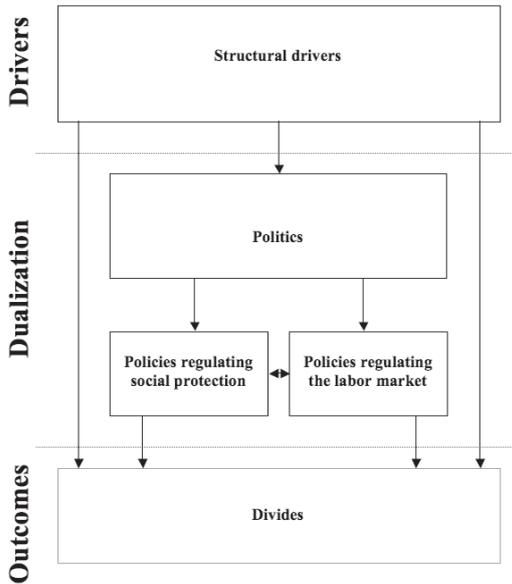


FIG. 1. Dualization as a political process: concepts and analytical framework.

Source: Emmenegger et al. (2012, 11).

Dualization can take three different forms: It might result in a deepening of existing institutional dualisms, i.e. the differential treatment of insiders and outsiders becomes significantly more pronounced; a widening of existing institutional dualisms, i.e. groups that have been previously treated like insiders are increasingly treated like outsiders; or finally be the product of new institutional dualisms, which did not exist during the post-war era of economic growth.

What distinguishes dualization from other concepts, such as polarization, segmentation, and marginalization? Most importantly, these other concepts largely focus on the *outcome* level and do not necessarily address the *politics* of change. For example, the concept of polarization is generally used in the literature to describe a pattern of employment growth that is characterized by the simultaneous creation of high-paid professional and managerial jobs and of low-paid personal service jobs, while no mid-skilled manual and clerical jobs are created (Wright and Dwyer 2003; Goos and Manning 2007; Autor, Katz and Kearney 2008). Segmentation refers to the division of labor markets into subgroups with very little or no mobility between these subgroups (Stinchcombe 1979; Berger and Piore 1980). Finally, marginalization describes the process of individuals being relegated to the margins of society (Mullaly 2006). Thus, all these concepts focus on the level of individuals. Political processes play a secondary role.

In contrast, dualization stresses political change and the politics of change. Dualization describes the widening, deepening or the creation of new institutional dualisms (output). Whether political change leads to new inequalities (outcome) is an empirical question, to which various studies give nuanced answers. Clegg (2012), for instance, referring to unemployment benefit reforms in France and Belgium, shows that these reforms led to very different distributive outcomes, universalistic in Belgium and inegalitarian in France. Similarly, Peng (2012) argues that governments in South Korea and Japan to some extent smoothened the consequences of dualization on the labor market by introducing social benefits for outsiders. We argue that the translation of structural pressures into policies and outcomes has to be understood as a political process, in which politically and economically stronger groups are using their power resources to insulate themselves from the negative effects of these structural

pressures, and in which governments make deliberate choices in favor or against outsiders. Thereby, changes in the labor market are translated into the social policy realm, where new distinctions arise or old institutional distinctions are re-activated. Feedback effects and vicious circles are likely to strengthen this effect because weak labor attachment and social exclusion are associated with weaker political representation.

### 3. *Mapping dualization: variation across countries, sectors, and social groups*

Mapping dualization implies that we define insiders and outsiders, as dualization is a process that is characterized by the differential treatment of insiders and outsiders. In line with the political science literature on insider-outsider divides (Rueda 2005; King and Rueda 2008; Emmenegger 2009; Schwander and Häusermann, forthcoming), we (Emmenegger *et al.* 2012) have defined insiders and outsiders on the basis of their labor market position. While insiders typically benefit from standard employment relations, outsiders are often either unemployed or in employment relationships characterized by low levels of pay, social benefits, and employment protection.

Some societal groups are overrepresented among outsiders in all countries studied: women, young labor market participants, low-skilled workers, especially in the service sector, immigrants, and workers of migrant origin. These groups are more likely to be unemployed or atypically employed, and they are more likely to be poor and to suffer from insufficient social rights. The available evidence suggests that their inferior status is persistent over time. Tomlinson and Walker (2012) show that those prone to poverty in the present are much more likely to experience or remain in poverty in future periods. The lasting structural disadvantages of outsiders imply that policies dealing with insiders and outsiders must be adapted. Either they need to target these groups specifically or they need to develop a new universalism able to cover both types of labor market situation.

However, even though similar societal groups are affected by the risk of being outsiders, we observe important variations along at least three dimensions. First, the composition of insiders and outsiders differs across welfare regimes: in the Nordic and

Continental countries, gender is the most important dimension, while in Southern Europe outsidership concerns mostly young labor market participants and in the Anglo-Saxon countries, outsiders are predominantly found among the low-skilled (Häusermann and Schwander 2012). Only immigrants seem to be an important source of cheap labor in all countries (Emmenegger and Careja 2012).

Second, some countries are more affected by processes of dualization than others. Liberal welfare regimes account for the highest share of outsiders among their workforce (Häusermann and Schwander 2012)<sup>2</sup>. In addition, some welfare systems, in particular France, Germany, and Spain, not only reproduce, but even exacerbate insider-outsider divides: while France and Sweden, e.g., have very similar average income differences between insiders and outsiders before taxes and transfers, the French welfare system contributes to an increase of these differences by 7.9 percentage points (up to 40.4 percent), while the Swedish welfare system diminishes these differences by 7.1 percentage points (down to 24.9 percent) (Häusermann and Schwander 2012). This shows how tremendously important policies are in shaping insider-outsider divides. However, it does not imply that outsiders are worst off in absolute terms in those countries that exacerbate these divides. E.g., whilst the German welfare system accentuates income-differences between insiders and outsiders, it is nonetheless more successful in preventing the onset of poverty than the British welfare system (Tomlinson and Walker 2012). This can be explained by the fact that despite its conservative-corporatist character the German welfare system has a considerably higher social wage than the British welfare system.

Third, the actual forms of atypical employment that characterize the country-specific insider-outsider divide differ. Eichhorst and Marx (2012) argue that there are five different paths taken by Continental European countries: defection from permanent contracts plays a particular role in labor market dualization in France and the Netherlands; defection from full-time jobs is particularly pronounced in the Netherlands, but also Austria and Germany; defection from dependent employment in the

<sup>2</sup> Outsidership is also widespread in South Korea. According to Peng, between 42 and 53 percent of all salaried employees in South Korea are employed on a temporary contract.

form of precarious self-employment is widespread in Belgium and France; increasing levels of wage dispersion to integrate low-skilled workers into the labor market are used in Austria and Germany; and large government-sponsored labor cheapening schemes have been developed in Belgium and France. In a similar vein, Kroos and Gottschall (2012) document the changing employment structures in the public social services in France and Germany. They contrast the «high road» of social service provision and employment in France with the more semi-professional «low road» in Germany. Given these different paths towards labor cost reduction, the «typical» outsider actually looks quite different, depending on the importance of fixed- and part-time work, precarious self-employment, and low-wage work in a particular country. This heterogeneity of the composition of insiders and outsiders accounts for the fact that both inequalities and possible policy strategies against insider-outsider divides are largely country-specific. Nevertheless, the different manifestations of the insider-outsider divide are part of the same dualization trend, because the social and political disadvantages outsiders encounter are similar across countries.

Existing evidence indicates that, generally, the crisis seems to have reinforced the existing divides and dualisms in the labor market and in the welfare states, but under the specific circumstances of the crises, the risk of «outsiderness» has started to affect the core workforce more strongly, too. It is of course too early to decide what the long-term impact of the 2008 financial crisis will be, but we can try to draw some insights from the various countries' reaction to the crisis so far.

The rise of unemployment has been very uneven, being particularly high in the US, Spain, and Ireland, and comparatively limited in the Netherlands and Japan. Moreover, «job losses have been disproportionately large for certain workforce groups and industries (e.g. employment losses have been far above average for construction, temporary and low skilled workers, and youth)» (OECD 2010, 17). Here we see that part of those who are typical outsiders have been particularly hit by the crisis, especially the young, the low-skilled, and the atypically employed. Moreover, the OECD report (2010) underlines that public Short Time Work schemes have played an important role in preserving jobs during the crisis in certain countries. For instance, these schemes allowed to save as many as 200 000 jobs in Germany by 2009 and 400

000 in Japan. This is a typical pro-insider policy, since short-term work allows keeping in employment those who are qualified and productive enough in the threatened industrial sector (thanks to public subsidies). Meanwhile, those who have an atypical work contract are sacked or not hired anymore.

What has been unusual is that «employment has fallen significantly more for men than for women, probably due to the sectoral profile of the recession (*i.e.* especially large employment losses in mining, manufacturing, and construction)» (OECD 2010, 18). This indicates that the economic crisis following the financial crisis has pushed deindustrialization further, thereby affecting men more strongly than women, even though women pre-crisis had a much higher risk of being outsiders than men. Similarly, some of the reactions of governments to the crisis in terms of cutbacks and austerity policies have started to deteriorate the position of public servants, who previously seemed to be the typical, shielded labor market insiders (IRES 2010; Laulom *et al.* 2012). Public expenditures in this field are expected to decrease due to lower salaries of civil servants (Romania, Baltics, Ireland, Spain, Greece, Portugal, Hungary) or wage freezes (Italy, France) and fewer employees. Finally, several countries have also taken measures to increase the flexibility of the labor market, especially for workers in permanent contracts (Spain, Portugal, Denmark; on Italy see below).

#### 4. *The politics of dualization*

What are the drivers of dualization? Why are there new and increasing insider-outsider divides in most countries? And why are these divides deeper in some countries than in others? Employers and trade unions have been crucial in shaping the specific dualization trajectories (Emmenegger *et al.* 2012).

Employers as protagonists for cost containment, labor market flexibilization, and limiting social protection have been politically crucial for dualization processes (cf. Seeleib-Kaiser *et al.* 2012; Eichhorst and Marx 2012). Whether or not and in what ways employers are successful with their demands for labor market flexibilization largely depends on prior institutional arrangements, governance structures, and power resources as well as the specific economic circumstances. However, their preference

for flexibilization turned out as being more or less a constant throughout all countries.

The role of trade unions is more complex. The expansion of private service sector employment as well as atypical employment has had an overall negative effect on union density, as it has contributed to the erosion of the traditional base of unions in the manufacturing sector, putting unions in a largely defensive position. In a number of countries, labor unions have agreed to various labor market and social policy reforms negatively affecting outsiders through concession bargaining, while maintaining the level of protection for insiders (either through the defense of preexisting social insurance arrangements or through the introduction of new (semi-)private insurance complements). In other words, unions, especially traditional unions in the manufacturing sector have acted as consenters, facilitating dualization (Palier and Thelen 2012; Peng 2012). These cross-class alliances, primarily within the manufacturing sector and with the support of the state, have in various countries contributed to «saving» the manufacturing base of the economy at the expense of outsiders, primarily employed in the service sectors.

However, Obinger *et al.* (2012) demonstrate that it would certainly be wrong to simply characterize trade unions as «dualizers». Left corporatism, i.e. a corporate arrangement between a left government with strong and encompassing interest organizations, can also mitigate processes of dualization. Particularly encompassing labor unions can partly overcome the core organizational dilemma faced by many unions, whereby membership interests of more narrow unions in the short term cannot be reconciled with their long-term organizational interests. Hence, encompassing unions may also represent the interests of outsiders. As Clegg clearly demonstrate (2012) in his comparison of Belgian and French unemployment protection, the participation of unions in unemployment benefit administration acts as a «recruiting sergeant» for Belgian trade unions. This clearly differs from the role played by French unions, only representing about ten percent of the workforce, in the administration of unemployment compensation. As a consequence, Belgian unions have advocated more «solidaristic» reforms of unemployment policies than the French unions.

Finally, political parties are in a particularly difficult situation, since they need to reconcile interest representation with

electoral appeals to broad sections of the society. Lindvall and Rueda (2012) suggest that when mainstream left parties chose to focus on issues that are primarily relevant to insiders, as the Swedish Social Democrats did in the election of 1998, they are punished by outsiders; however, a strategy reconciling the interests of insiders and outsiders is not necessarily sufficient to gain power as it may lead to the defection of labor market insiders to center-right parties. In this sense, the authors concur with previous studies on this topic (Rueda 2005; Häusermann 2010): Social Democratic parties face a new electoral dilemma when dealing with dualization.

### *5. A few thoughts on political choice and the reform of the Italian labor market<sup>3</sup>*

How can we interpret the most recent developments in Italian labor market policy in the light of the arguments developed above? Processes of labor market dualization have long characterized Italy. Today, Italy has one of the most dualized labor markets in the Western hemisphere. For instance, despite an unemployment rate that is below the EU27 average (8.4 versus 9.7 percent), Italy is characterized by one of the highest youth unemployment rates in Europe (29.1 versus 21.4 percent)<sup>4</sup>. In contrast, among workers aged 25 to 74 years, the Italian unemployment rate is significantly below the EU27 average (6.9 versus 8.3 percent). In a similar vein, while employment among men is only slightly below the EU27 average (67.5 versus 70.1 percent), Italian women are considerably less likely to work than their European sisters (46.5 versus 58.5 percent). What is more, unemployment among Italian women (9.6 percent) is considerably higher than among men (7.6 percent). Moreover, Italy has an exceptionally high employment concentration in very small firms (almost half of the workforce being employed in firms with less than 10 employees) and one of the highest rates of self-employment in Europe (Pedersini and Colletto 2010). This employment pattern underlines the dualism

<sup>3</sup> We are grateful to Georg Picot and Federico Pancaldi for helpful comments on this section. All errors remain ours.

<sup>4</sup> Data are from Eurostat and refer to 2011 unless otherwise indicated (accessed 15 March 2013).

in the Italian labor market, as both workers in small firms and the self-employed have not had equal access to social policy benefits and employment security. Finally, the Italian economy is characterized by one of the largest informal sectors in Europe (cf. Schneider 2005), which to a considerable extent relies on undocumented migrant labor (Reyneri 2003).

Certainly, Italy's economic decline with below average economic growth since the 1990s is not solely the result of labor market dualization. There are also other important factors such as the lack of competitiveness (rank 43 out of 142 countries, World Economic Forum 2011, 15), corruption (rank 72 out of 176 countries<sup>5</sup>), an overly regulated economy (rank 73 out of 185 countries, World Bank 2013, 3), and rapidly increasing unit labor costs (11.4 percent between 2005 and 2010 compared to an OECD average of 8.3 percent<sup>6</sup>). However, the skewed distributional consequences of this underwhelming economic performance point to the *importance of the institutional design of the welfare system* (Jessoula and Alti 2010) as well as of *politics* in explaining the labor market divides that can be observed between the young and the old, men and women, formal and informal workers, as well as migrants and natives.

The dualization of the Italian labor market is rooted in long-standing institutional divides both in labor market and social policy arrangements, such as the limited scope of unemployment compensation schemes, strong employment protection regulations, and the huge informal sector. Some of the recent developments, especially in the realm of social policy even seem to reinforce these dualisms (Jessoula and Alti 2010). That said, we would like to focus this discussion solely on the recent labor market reforms of the Monti cabinet and to spell out the political choices that were made and their interpretation in terms of dualization.

In fact, attempts at smoothening the effects of labor market dualism for outsiders have been made repeatedly already before the appointment of the Monti cabinet. For instance, reforms marginally widened the scope of the *cassa integrazione* to further companies and introduced some unemployment benefits

<sup>5</sup> Source: Transparency International, URL: <http://cpi.transparency.org/cpi2012/results/> (accessed 15 March 2013)

<sup>6</sup> Source: OECD, URL: [http://stats.oecd.org/Index.aspx?DatasetCode=ULC\\_ANN](http://stats.oecd.org/Index.aspx?DatasetCode=ULC_ANN) (accessed 15 March 2013).

to young unemployed with insufficient contributions. However, benefits remained low and tight eligibility conditions restricted access (Picot 2012). When Monti announced his reform agenda for the labor market, it read as an agenda to «de-dualize» the Italian labor market: the so-called Monti-Fornero reform set out to reduce dismissal protection for insiders, extend unemployment benefit coverage to outsiders with weak contribution records, and introduce active labor market policies. In the political decision-making process, however, the reform was considerably watered down. Nevertheless, it somewhat restricted the recourse to fixed-term contracts, semi-dependent work, and «false» self-employment, while the protection against dismissal in case of open-ended contracts has been slightly decreased. In particular, if judges find a dismissal for economic reasons to be unlawful, the employer does not automatically have to reinstate the dismissed worker. Instead, the employer has to pay only compensation. However, judges still have the freedom to demand reinstatement if the economic reasons for the dismissal are found to be «manifestly groundless». In a similar vein, the Monti-Fornero reform reorganizes the system of unemployment benefits, thereby widening its coverage, while shortening benefit duration. Active labor market policies, by contrast, remain largely ineffective. While the reform aimed at a development of this notoriously underdeveloped field in Italian labor market policy (Berton, Richiardi and Sacchi 2012), the necessary decrees to enact this development are still lacking.

An appreciation of the distributive choices that the Monti government made with this reform is complex, not least because the content of the reform has been diluted in the course of the political process. Several prominent economists as well as business representatives have criticized the reform for not going far enough. The government's initial goal was to significantly reduce dismissal protection, but under pressure from trade unions, the draft law was considerably watered down, leading Confindustria, Italy's main employers' organization, to voice the concern that the reform might make the labor market even more rigid («Financial Times», 5 April 2012). Italian employers seem to be particularly worried about the new fee to discourage the use of fixed-term contracts and the extension of waiting periods between two fixed-term contracts, although there are still plenty of other forms of nonstandard employment relationships

that employers can fall back on. In contrast, they consider the reform of dismissal protection to be too timid because judges still can demand the reinstatement of dismissed workers, while legal fights over redundancies might continue to lead to long trials and high legal costs.

Hence, the Monti-Fornero reform illustrates both the importance as well as the difficulty of political choices. What proved decisive for reform outputs were not structural pressures, but domestic politics. The 2013 election has clearly shown that Italians are dissatisfied with the current state of politics. Although in desperate need of decisive but also democratic leadership, Italy faces a politically uncertain future at least until the next election. Hence, Italy continues to be «trapped» in a situation characterized by low social trust, the absence of broader coordinated solutions in labor market policy, and, as a result, largely inefficient outcomes (Bonoli and Emmenegger 2010).

## 6. *Conclusions*

In this article, we have strived to adopt a «multidimensional» perspective, meaning that we argue that we need to study the developments in the realms of labor market, social policy, and related policy fields jointly. This allows us to overcome the limits of analyses that adopt a more narrow focus. Focusing solely on income distribution (as the OECD «growing unequal» study (2008) does for instance) an increase in inequalities can be ascertained. Analyzing labor market developments (as Goos, Manning and Salomons (2009) do), one may come to the conclusion of polarizing labor markets. Scrutinizing social rights and social policies, observers often identify a general «crisis» of the welfare state (Huber and Stephens 2001), retrenchment, and potentially a recalibration of social policies (Pierson 2001) without sufficiently acknowledging the interactions of social policies with labor market developments. In other words, social policies can echo and reinforce developments on the labor market or on the contrary counterbalance the consequences of deteriorating labor market conditions.

Second, we stress the role of politics and political choice. Indeed, a striking characteristic of recent accounts of increased inequalities or social divides is that they are often perceived as

an «unavoidable» mechanism. The OECD's (2008) report on increasing inequalities does not aim to explain why inequalities have grown over the past decades. Goos *et al.*'s (2009) hypotheses for explaining job polarization are based on mere market mechanisms (routinization, offshoring, or growing income inequalities). They eventually understand job polarization as a correlate to technological progress (Goos *et al.* 2009, 58). Even prominent political economy scholars seem to have lost confidence in the impact and effectiveness of policies. Many of those who have pointed to increased insider-outsider divides as a likely feature of socioeconomic development in Continental Europe have done so not necessarily by referring to market mechanisms, but to institutional path dependency. Esping-Andersen (1996) as well as Iversen and Wren (1998) assume that insider-outsider divides will increase in Continental welfare systems in face of deindustrialization mainly because of their traditional institutional settings. Their prediction that labor would continue to be shed because of the logic of the conservative welfare model has, however, proven to be wrong. What we show is that, starting in the early 1990s (and in some countries even sooner), new employment policies, accompanied by important welfare reforms (especially in unemployment and old age insurance), have diverted the Continental European (as well as East Asian) models from their traditional routes (Emmenegger *et al.* 2012). Corporatist conservative systems were able to overcome the «welfare without work» problem of the 1990s by creating many nonstandard jobs and new types of social beneficiaries. As Eichhorst and Marx (2012, 81) note, «we can speak of a common trend in Continental Europe to redefine labor market outsiders: while they were typically kept outside the labor market in the 1990s (as expressed in high shares of long-term unemployment and inactivity), they now increasingly participate in the labor market, but in inferior jobs that deviate from the rule of the standard employment relationship.» The social partners and the political actors have played an important role in this process.

Common to all policies that have facilitated and reinforced dualization processes is that they have been inspired by a «neoliberal» agenda, which was only partially implemented, i.e. only for some parts of the workforce, but not for others. And these distributive choices are political choices. This is probably where we differ from a view that identifies recent developments as a

general trend towards liberalization (such as in Streeck's (2009) account of the transformation of German capitalism). Whereas these accounts identify a general transformation of capitalism, eventually eroding security and benefits for all members of the workforce, we argue that liberalization was partial, as it has been primarily applied to «new» jobs in the tertiary sector, while an ever-shrinking core of insiders continues to enjoy relatively generous employment and social protection.

It remains of course an open question whether this type of dualistic structure of labor market and social protection policies will be sustained in the future. In the longer run, and in the light of the developments triggered by the crisis and described above, one may ask if dualization is only a transitory stage towards liberalization. Streeck relevantly asks «why the fringe should not continue to eat into the core until nothing much remains of it?» (Streeck 2010, 512). In other words: why should the extension and marginalization of outsiders not continue until no insiders are left? If that was happening, dualization would merely be a transitory phenomenon in a much more general trend towards liberalization. Even if we cannot directly answer this question on the future of developed capitalist economies, we can ponder arguments for and against the stability of dualized policies and labor markets.

Politically, two arguments suggest that dualization and insider-outsider divides may last: a clear segmentation of insiders and outsiders in the labor market and institutional feedback effects. First, one may argue that the fringe is not really eating the core, since the outsiders are not competing directly with the insiders for jobs, income, and social rights: outsiders do not have the same occupations, usually do not work in the same economic sectors (male blue-collar workers, e.g., are not outsiders in Continental Europe), they do not have the same skills, and they sometimes lack citizenship. Because of this rather clear occupational segmentation of the labor force into insiders and outsiders, outsiders do not directly increase the cost of the insider workforce. Put differently, outsiders do not work in the same jobs for less money, they work in different jobs. Hence, two different «labor market regimes» may co-exist alongside each other, one for the insiders and one for the outsiders. The second mechanism that may stabilize dualistic patterns is institutional. As we argue, liberalization and flexibilization have been targeted at

atypical workers, while the shrinking core has remained largely protected. In addition, outsiders are clearly less active politically, which can be seen as an institutional feedback effect. Labor market segmentation translates into clear differences in terms of power resources. One can then hypothesize a self-reinforcement effect again related to power asymmetries between insiders and outsiders: the worse the conditions of outsiders, the less they will mobilize and organize. The greater the difference in social and political resources between insiders and outsiders, the more able the insiders will be to secure political power and to secure their status.

Undeniably though, some of the current dualization policies are undermining the privileged status of insiders in the future. In many European countries, future pensions will be much lower for most of the pensioners. Also, in many cases such as Germany, France, Sweden, Japan, or South Korea, new entrants in the labor market, even in core sector industries, are – upon entering the labor market – usually offered much less protected conditions than the older generations in the same occupations. In the long run, once the older insiders will have left the labor market, the new ones will experience new, more flexible, and more precarious employment systems. In that sense, part of the insiders will disappear through generational transformations, thereby possibly lowering the dualistic structure of current labor markets. But it will take another 30 years or so to see this demographic transition unfold.

Finally, we emphasize that dualization – whether temporary or stable – is not a functional necessity. Governments have room for political maneuver. Even within the most corporatist conservative systems, we showed that some countries have been able to implement policies designed to smoothen the effects of dualization. France is still less dualized than Germany, but more dualized compared to Belgium in the realm of unemployment protection. However, the most interesting cases of «smoothened dualization» in Europe are probably Austria, the Netherlands, and Switzerland, providing effective minimum social standards for outsiders. Unfortunately, Italy was not a prominent case in the dualization project – mostly for the lack of comparative data – but we think that the political challenges we outline speak strongly to the difficult choices Italian political leaders face.

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