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Poles Apart? Alternative Welfare Trajectories under Finance-Dominated Capitalism

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ABSTRACT

By connecting the post-Keynesian view of financialization with Comparative Political Economy, we suggest some elements for an updated interpretation of the existing models of welfare. As a main element of novelty, we consider how high-income countries are reacting to the pressures of finance-dominated capitalism, namely by extending, keeping, or retrenching their welfare systems. The contribution of the article is three-fold. First, we elaborate on the nexus between welfare and financialization. Second, we introduce a multidimensional index aimed at assessing the degree of welfare of 32 OECD countries for the period 1990–2015. Third, we compare our index with the socio-economic models identified in the literature and with the patterns of financialization. Two trajectories emerge from our exploration: on the one side, Scandinavian and Continental European countries moved toward relatively higher levels of welfare; on the other side, lower levels of welfare feature Anglo-Saxon, Asian, Mediterranean, and Central and Eastern European countries. Besides such divergence, we find that the process of financialization was more intense in countries with stronger welfare, which likely opted for a compensation strategy. Our work highlights the relevance of policies and institutions in shaping different welfare systems and coping with the challenges of the current phase of capitalism.

KEYWORDS

Comparative political economy; financialization; globalization; institutions; welfare

JEL CLASSIFICATIONS

I38; P51; E60

Introduction and Background

In a recent contribution, Colin Hay raised a thought-provoking question: *Does capitalism (still) come in varieties?* There is no easy answer to this question, but the author argues that, *even if it is accepted that capitalisms vary, it does not necessarily follow that capitalism comes in varieties* (Hay 2020, 302). This statement opens the door to further interrogation: although capitalism does not really come in varieties, how should we assess the different ways in which policymakers deal with the threats in the current age of capitalism? The 2007–09 financial and economic crisis and the subsequent decade of stagnation represented a test for many advanced economies to determine whether their socio-economic model was able to cope with the challenges of contemporary capitalism – following Hein (2019), we shall refer to that as ‘finance-dominated capitalism’. Indeed, it is widely agreed that the welfare state experienced a profound transformation in the phase of intensified globalization that occurred from the mid-1970s/early-1980s (Bonoli 1997; Sapir 2006; Kim and Zurlo 2009): grounded on the seminal intuition by Katzenstein (1985), the

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research literature testified to different reactions against trade liberalization in terms of welfare provision depending on different socio-economic models (see among others Onaran and Boesch 2014; Yay and Aksoy 2018). More recently, however, some scholars sought to argue that also the ascendancy of finance and financial motives might have contributed to shaping heterogeneous welfare systems (Kohler, Guschanski, and Stockhammer 2019; Hein, Paternesi Meloni, and Tridico 2021). The present work is situated within this discussion. Our exploration is inspired by the emerging approach to Comparative Political Economy (CPE) built on post-Keynesian (PK) grounds (Stockhammer 2021). Following this line of inquiry, we move somewhat away from the traditional *Varieties of Capitalism* method (Soskice and Hall 2001): while recognizing the worldwide establishment of finance-dominated capitalism, we will argue that its challenges can be faced and managed through different policies and institutions that, in turn, generate and outline differentiated models of welfare.

Specifically, we contribute to this literature by offering some elements for a revised interpretation of the existing taxonomies of socio-economic models. We shall suggest that a sort of dualization emerges when different strategies to deal with the pressures of nowadays capitalism are considered, a dichotomy that is not independent of the role of policies and institutions. We identify two trajectories: on the one side, the ‘reactive trajectory’, followed by countries adopting or defending a more generous welfare system to protect those who are damaged by increasing financialization; on the other side, the ‘compliant trajectory’, followed by countries accommodating the needs of financial capitalism by retrenching welfare provision to promote competitiveness and a business-friendly environment.

We are aware that the welfare sphere involves different domains. This is the reason why we consider it a multi-faceted matter, which includes policies, institutions and, not marginally, their outcomes. In particular, we assess the level of welfare of each economy based on the three broad pillars, namely the direct provision of social expenditure by the government, the institutions operating in the labor market and the distribution of income. In so doing, we set forth an empirical investigation on 32 OECD countries (from 1990 to 2015) aimed, first, at quantifying the magnitude of the welfare state and, second, at checking how socio-economic models deal with financialization. In detail, we condense five socio-economic indicators representative of the just-mentioned three pillars into a synthetic index, termed ‘Welfare Index’, which aims at assessing the degree of welfare of each country at different points in time. Once the index is computed, we verify how it relates to the welfare models previously identified in the literature, and if the patterns of financialization are significantly different depending on the welfare trajectory.

The article proceeds as follows. In the second section, we overview the existing organizations of welfare and socio-economic models. The third section reviews and discusses financialization and the features of finance-dominated capitalism. In the fourth section, we elaborate on the connection between our dimensions of welfare and financialization by providing some descriptive evidence for each socio-economic model. The fifth section is devoted to the empirics: we first present our index of welfare, and then we juxtapose it with the existing welfare models and different measures of financialization. The concluding section suggests some elements for an updated interpretation of the prevailing welfare taxonomies.

A Bird’s Eye View of the Literature on Welfare and Socio-Economic Models

In the early 1990s, CPE emerged as a promising field of research devoted mainly to comparisons among economic systems. It deals with several matters, such as different institutional settings, modes of production, labor, banking and financial systems, and so forth. Studies on CPE often rely on heuristic frameworks and get involved with the creation of taxonomies of socio-economic models. The preeminent one was proposed by Esping-Andersen (1990), who considered the Liberal or market-oriented model (including Anglo-Saxon or ‘English-speaking’ countries), where

the State has a residual role in the economy; the Conservative/Corporative, family-oriented model (comprising Continental European countries), where both the State and employers play a supporting role; and the Social-Democratic, state-oriented model (principally representing Scandinavian/Nordic countries), with universal protection and services. While methodologically still relevant, this grouping was based on the evidence before 1990, an element that casts doubt on its robustness over time. Moreover, the recent decades are characterized by a generalized shift toward a market-oriented paradigm of economic policy, grounded on the ideology of neoliberalism, that threatened the effectiveness of the welfare state (Palley 2020). In this regard, even the Scandinavian model, largely considered the most generous, has undergone profound transformations (Greve 1996; Kvist and Greve 2011) that have somewhat limited the universality of welfare, making it more constrained and conditional (Jensen and van Kersbergen 2017; Taylor-Gooby, Leruth, and Chung 2017).¹ One of the explanations for the retrenchment of the welfare state has been the concern for its sustainability, threatened by globalization – especially by the process of financialization and technical progress leading to increased unemployment of unskilled workers – and by an aging population (Meier and Werding 2010). Both would have led to increased spending on unemployment benefits and pensions, respectively, and reduced the fiscal revenue due to a lower share of people who are employed.

These changes, combined with the economic, political, and institutional transformations of the new century, have stimulated some recent updates to the taxonomy. One of the most well-known came from Hay and Wincott (2012), who added the Mediterranean group (Ferrera 1996) and the Central and East European (CEE) countries: the former tends to concentrate social spending on older people (i.e., they have a sizeable pension system) and to protect the employment status of workers as a priority over providing unemployment insurance for people who lose their job (Sapir 2006); the latter is marked by a poorer welfare sphere compared to Continental or Western Europe, with most CEE countries (except Hungary) emphasizing social insurance more than social assistance (Nelson 2010).²

Further attempts aimed at classifying countries have been made by Amoroso (1998), Jessop (2002), and Amable (2003). Recently, Tridico and Paternesi Meloni (2018) have summarized the existing classifications by combining public social spending along with many features that have been considered by the flourishing approaches to CPE, such as intensified globalization in terms of trade openness and financial flows, growing inequality and increasing labor market flexibility. Accordingly, they clustered countries into six groups, namely the Anglo-Saxon model, the Continental European model, the Mediterranean model, the Scandinavian model, the CEE model, and the Asian model (see Table 1).³

Notably, this cross-fertilization of categorization emerged in parallel with the ‘*Varieties of Capitalism*’ literature developed from the seminal work by Soskice and Hall (2001), who distinguishes between coordinated market economies (CMEs) and liberal market economies (LMEs). Conversely, Tridico and Paternesi Meloni (2018), who present a new classification based on the Amable’s taxonomy (2003) with the addition of the CEE model suggested by Fenger (2007), moves along the lines traced by Hay and Wincott (2012): this perspective differentiates countries based on the size of the welfare sphere, intended as direct welfare support, institutions and policies operating in the socio-economic environment, the functioning of the labor market, and – not subordinate – how income is distributed among social blocks and citizens. Accordingly, this

¹The neoliberal reforms in Denmark – under the paradigm of *flexicurity* (see Pariboni and Tridico 2019) – make it the most obvious case of how the universality of welfare has slowly been transformed into conditionality (Trenz and Grasso 2018), yet something similar has also happened in Sweden since 1990 (Blomqvist and Palme 2020).

²Of course, some specific cases hold. For instance, it has been argued that the Czech Republic and Slovenia show a quite generous welfare state (Feldmann 2006), while Slovakia and Estonia took a clear neoliberal turn. The interested reader may refer to Šikulová and Frank (2013) and Thorhallsson and Kattel (2013).

³The exploration also involved Chile, Israel, Mexico and Turkey, that nevertheless could not be clustered due to their specific features. In this work, we will follow the same convention.

Table 1. Country classification (and codes) by welfare model.

Anglo-Saxon	Continental European	Mediterranean	
Australia (AU)	Austria (AT)	Greece (GR)	
Canada (CA)	Belgium (BE)	Italy (IT)	
Ireland (IE)	France (FR)	Portugal (PT)	
New Zealand (NZ)	Germany (DE)	Spain (ES)	
United Kingdom (UK)	Luxembourg (LU)		
United States (US)	Netherlands (NL)		
	Switzerland (CH)		
Scandinavian	Central and Eastern European (CEEC)	Asian	Extra
Denmark (DK)	Czech Rep. (CZ)	Japan (JP)	Mexico (MX)
Finland (FI)	Estonia (EE)	South Korea (KR)	Turkey (TR)
Iceland (IS)	Hungary (HU)		Chile* (CL)
Norway (NO)	Poland (PL)		Israel* (IL)
Sweden (SW)	Slovak Rep. (SK)		
	Slovenia (SI)		

Note: *Due to data availability, Chile and Israel are not considered.

Source: Tridico and Paternesi Meloni (2018).

approach offers an appropriate background for our purposes as it takes into consideration both the socio-economic outcome and the institutions and policies involved in generating that outcome.

Financialization and Finance-Dominated Capitalism: An Overview

Before turning to the nexus with welfare, let us frame the concept of financialization. It is hard to find an all-encompassing definition for that, as pointed out by Sawyer (2014), Palley (2013, 2016) and van der Zwan (2014). The related literature generally identifies this term with the increase in the size and importance of a country's financial sector relative to its overall economy (Hein 2019; Pariboni and Tridico 2019). Financialization has been defined also as 'the deregulation of the financial sector and the rise of shadow banking, rising gross indebtedness of the private sector, the ascendance of shareholder dominance at the firm level, the financialization of everyday life and the emergence of several macroeconomic regimes under the dominance of finance' (Hein 2019, 976). There are many alternative and complementary definitions for this phenomenon,⁴ and it is even harder to provide a clear picture as financialization develops continuously in terms of evolving and involved instruments, markets, agents, and actors (Pariboni and Tridico 2019). Epstein (2005, 3) refers to financialization as 'the increasing role of financial motives, markets, players and institutions in the operation of domestic and international economies.' Krippner (2005) provides a definition of financialization conceptualized in the broader domain of social and political sciences, describing it as the growing dominance of capital financial systems over bank-based financial systems. Similarly, Tomaskovic-Devey, Lin, and Meyers (2015, 525) use the term financialization to identify 'the post 1980 expansion of both the financial service sector and increased investment in financial instruments by the non-financial sector.' Recently, the topic has been critically (re)considered by Michell and Toporowski (2013), who offered some observations on financialization and the financial process; similarly, Palley (2021) provided a revisit of the concept of financialization, which partially overlaps with political economy, highlighting the existence of 'a politics of financialization that goes hand-in-hand with the economics' (Palley 2021, 461).

⁴Analogous to Hein (2017), Sawyer (2014) used the term 'financialised capitalism' to describe the ascendance of shareholder supremacy and the emergence of growth regimes under the dominance of finance. Wray and Papadimitriou (1999), Engelen and Konings (2010) and Tridico (2017a) refer to 'financial capitalism'. Flaherty (2015) used the term 'finance-driven' capitalism.

For our purposes, we find Hein's (2019) description of 'finance-dominated capitalism' (henceforth, FC) particularly apt to capture the cross-cutting nature of the current age of capitalism, and for this reason, we shall refer plenty to this term. Financialization is intimately consistent with a stage of capitalism that is quite different from the one that characterized advanced market economies between the post-WWII period and the early 1970s. In FC, global and financial markets are considered as the main drivers of growth and, therefore, both policies and institutions should allow for their establishment (Tridico 2017a).

As far as the peculiarities of FC are concerned, Hein, Paternesi Meloni, and Tridico (2021) indicate some broad aspects. First, the age of FC is characterized by a decreasing share of income accruing to workers and by increasing inequality among wage earners.⁵ Second, FC favored shareholder power vis-à-vis workers, and that contributed to reducing productive investment through the imposition of short-term strategies – following the 'downsize and distribute' principle (Lazonick and O'Sullivan 2000; Lazonick 2014), as well as by draining internal resources available for real investment purposes (van Treeck 2009; Onaran, Stockhammer, and Grafl 2011; Tomaskovic-Devey, Lin, and Meyers 2015; Stockhammer 2015; Tori and Onaran 2020). Third, FC has boosted the role of debt-financed consumption (Barba and Pivetti 2009; Cynamon and Fazzari 2008), and in so doing created the potential to, at least partially and briefly, compensate for the depressing demand effects that have been imposed on consumption and investment by redistribution and shareholder value orientation (van Treeck and Sturn 2012; van Treeck 2015).

The multi-pronged nature of financialization makes it difficult to translate such a complex process into a single measure capable of describing its rise. Moreover, it may assume heterogeneous shapes and dimension across countries and time (cf. Karwowski, Shabani, and Stockhammer 2020). For this reason, we shall refer to alternative indicators of financialization, each of them capable of depicting a specific aspect of this complex phenomenon.

As capital markets are one of the major sources of business finance in most advanced economies, a natural proxy for financialization is the market capitalization of listed domestic companies (MKT). Plenty of empirical evidence testifies the appropriateness of this metric in capturing the process of financialization (Engelen and Konings 2010; Godechot 2016; Tridico 2017a; Özdemir 2019) in the sense of rising financial claims and incomes about the real economy (Pariboni and Tridico 2019).

We will also refer to the amount of domestic credit provided by the financial sector (CRED), expressed as a percentage of GDP. Regarding households, it has been argued that in a situation of stagnating incomes credit represented, at least in the short-to-medium term, an effective tool for alleviating stagnation tendencies (Barba and Pivetti 2009; Cynamon and Fazzari 2015). For this reason, it can be considered as a proxy for financialization intended as higher indebtedness (Pariboni and Tridico 2019; Pariboni, Paternesi Meloni, and Tridico 2020).

Moreover, we shall refer to the amount of distributed income of non-financial corporations (DIV), intended as the sum of dividends and withdrawals (as a percentage of GDP). Indeed, shareholder value orientation can be considered the counterpart of financialization at the firm level, in terms of governance principles and as an indicator of short-termism. That metric is widely used in the literature on the relation between financialization, on the one hand, and investment and economic performances, on the other hand (Stockhammer 2004; Pariboni, Paternesi Meloni, and Tridico 2020; Tori and Onaran 2020).

Finally, financialization is not independent of the whole process of globalization of the economies (Baud and Durand 2012). Both aspects should not be seen as disconnected from progressive deregulation and neoliberalism, and it is not by chance that FC emerged alongside increased openness, an element that fostered capital mobility and allowed foreign investors to pursue

⁵In this regard, the paramount example in literature is the skyrocketing remuneration of executives, top managers and more generally the so-called 'top 1' percent's share of income (Bivens and Mishel 2013).

cheaper labor costs and higher returns. Concerning the reaction of different socio-economic models to globalization, Tridico and Paternesi Meloni (2018) asserted that Scandinavian and Continental European countries followed the ‘compensation thesis’ by regulating increasing globalization through the expansion of the welfare state (Rodrik 1998; Lindert 2003). By contrast, Anglo-Saxon/Liberal, Mediterranean and the CEE countries converged in reducing public social expenditures during the last decades, thereby endorsing the ‘efficiency thesis’, according to which the process of globalization needs to be accompanied by the contraction of welfare states to promote external competitiveness (Alesina and Perotti 1994; Blackmon 2006). In light of this debate, the metrics of financialization introduced so far could not be capable of representing the processes at the intersection of financialization and globalization comprehensively, as they do not capture direct capital flows that involve foreign actors. For this reason, we will also refer to foreign direct investment (FDI) as a fourth proxy for financialization (Iamsiraroj and Ulubaşoğlu 2015; Zélicity 2022).

Welfare Dimensions and Financialization through the Lens of the PK Approach to CPE

Several reasons, which involve both theoretical and empirical matters, lead us to consider that welfare trajectories and increasing financialization may relate to each other. Remarkably, finance is explicitly considered in the literature on *Varieties of Capitalism*, where we see a dichotomy between bank-based financial systems in CMEs (which allow long-term finance and strategies) and market-based financial systems in LMEs (with shorter time horizons and financial instruments). Nonetheless, financialization has not been deeply considered yet in the welfare model approach. This obliges us to elaborate on the potential connections between the process of financialization and the welfare sphere. At the theoretical level, we do that by drawing from the literature at the intersection of CPE and PK economics (among others, Baccaro and Pontusson 2016; Behringer and van Treeck 2017; Stockhammer 2018, 2021; Stockhammer and Ali 2018; Kohler and Stockhammer 2021; Hein, Paternesi Meloni, and Tridico 2021).⁶ At the methodological level, we shall refer to our dimensions of welfare by following the clusters of countries identified by Tridico and Paternesi Meloni (2018). In the remainder of this section, we shall explore the likely nexus between welfare and financialization with respect to the following domains of welfare (on which our multidimensional analysis will rely), namely: (i) public social spending, (ii) labor market institutions, and (iii) income distribution.

Public Social Spending

The PK approach argues that the process of financialization tends to sow the seeds for stagnation tendencies in advanced economies to the extent that it threatens aggregate demand and increases inequality (Hein 2013, 2016, 2019; Tridico and Pariboni 2017; Hein, Paternesi Meloni, and Tridico 2021; Stockhammer 2021).⁷ In this context, the retrenchment of welfare states that has occurred in the past two decades may have exacerbated the slow recovery, particularly in European countries afflicted by austerity policies. Notably, the combined effect of stagnating income and welfare retrenchment might have fed a vicious circle of increasing private indebtedness and debt-led recovery, with the ensuing dangers in terms of financial instability and unstable

⁶Notably, most of these works focus on the relationships between differentiated welfare or socio-economic systems, on the one side, and growth models, on the other side; while the present work emphasizes the link between the welfare sphere and financialization.

⁷In principle, ‘finance-led growth’ had been viewed as a viable alternative to Fordism or the paradigm of economic policy adopted during the Golden Age (Boyer 2000).

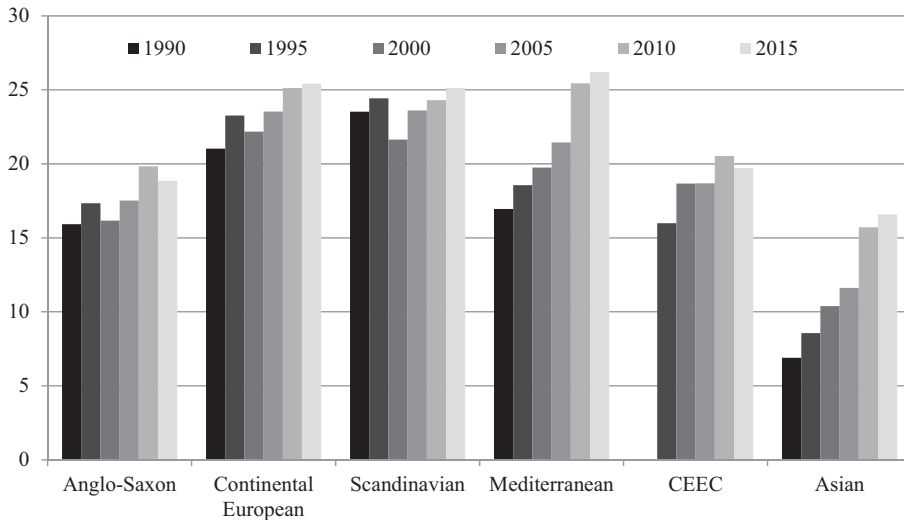


Figure 1. Public social spending by welfare model. Public social spending clustered by welfare model, based on simple average value of public social spending (as % of GDP) for each group, calculated annually. The group of CEE countries (CEEC in the figure) starts from 1993. *Source:* our elaboration on OECD data (see [Appendix A](#)).

aggregate demand (Barba and Pivetti 2009; Hein and van Treeck 2010; Galbraith 2012; Kim 2013; Setterfield and Kim 2017; Stockhammer 2017). Contrary to what had effectively happened (i.e., a process of welfare retrenchment), the PK approach posits that public social spending is the most natural tool to face the threats of FC (Stockhammer 2017; Palley 2020), as, through direct welfare support, governments may compensate increasing income disparities. A variety of welfare can be therefore traced by observing different responses in terms of social expenditures across socio-economic systems. In this respect, [Figure 1](#) depicts the average value of public social spending (in percent of GDP) grouped by welfare models. Generally, Continental European and Scandinavian countries exhibit higher public welfare spending, while Anglo-Saxon countries are lower. This pattern seems to be quite stable over time, confirming a greater welfare effort from countries belonging to the Corporative tradition and, to the contrary, a lower welfare provision in countries endorsing a more Liberal model. There are, however, some exceptions, as it is the case of the recent upward trend in Mediterranean and Asian countries. Nevertheless, the first is motivated by the fact that Mediterranean countries did not experience a sustained recovery after the 2007–09 turmoil, and they also faced the 2010–11 sovereign debt crisis and the subsequent policies of fiscal austerity; these episodes contributed to both reduced GDP and increased automatic stabilizers. The second mainly depends on the extremely low levels of public social spending by South Korea in the ‘90s, which was approximately 3% of GDP compared to the current 10%.⁸

Labor Market Institutions

A rising body of PK literature has been critical of the features of FC since they imply that wage compensation may be merely considered as a cost to be compressed, rather than a source of aggregate demand (Hein 2015, 2018; Pariboni and Tridico 2019; Pariboni, Paternesi Meloni, and Tridico 2020). As wage growth is essentially viewed as an obstacle to be removed to fit with the

⁸There are, of course, different patterns across countries regarding the type of social spending. In this regard, the interested reader may refer to the ‘Social Expenditure database’ (OECD) by social program, where nine types of spending are identified (namely old age, survivors, incapacity, health, family, active labor market programs, unemployment, housing and other policy areas).

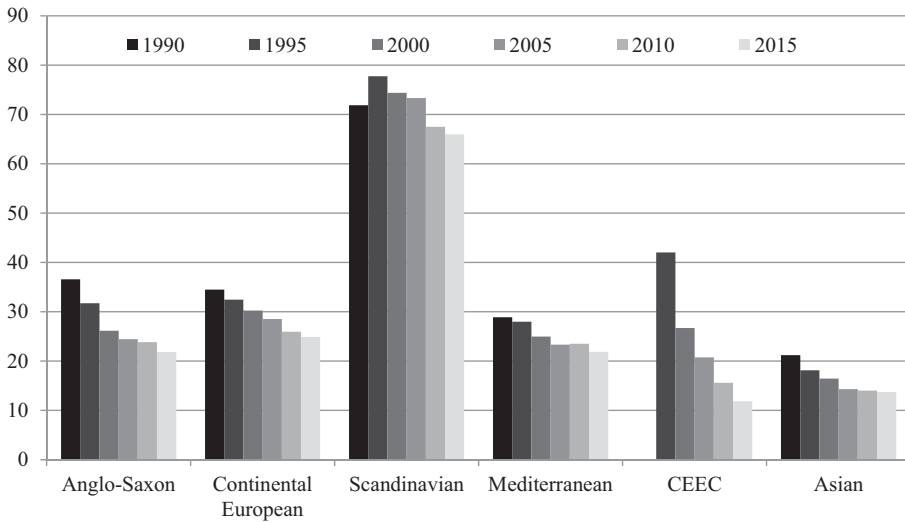


Figure 2. Trade union density by welfare model. Unionization rates clustered by welfare model, based on simple average value of unionization rate for each group, calculated annually. The group of CEE countries (CEEC in the figure) starts from 1993. *Source:* our elaboration on OECD data (see [Appendix A](#)).

needs of businesses and investors on a global scale, in the context of FC trade unions are driven to lose power, while labor flexibility dramatically increases (Tridico 2012). Consistently, the main policies and institutions that have been the hallmark of advanced economies in the last two to three decades are those regarding labor market flexibility. Putting it differently, trade unions need to be weakened to eliminate frictions and rigidities in the labor market, and their actions need to be confined because, as argued by Acemoglu and Robinson (2015), strong unions may counterbalance the political influence of FC.⁹ The general decline in unionization has worsened the bargaining power of workers, leading wages to stagnate (Paternesi Meloni and Stirati 2022) and contributing to the problems of low pay, in-work poverty and income inequality (Coats 2013). In this respect, [Figure 2](#) depicts the patterns of unionization rates across different socio-economic models.¹⁰ Trade union density exhibits a constant decline in all models, particularly in Anglo-Saxon and CEE countries. However, unionization rates are still much higher in the Scandinavian model than in the other models in which they are approximately at the same level (except for Asian countries that present lower unionization).

In addition to the declining political power of unions, the normative aspect must be considered when assessing the strength of labor market institutions. Most recent literature regards the new apparatus of economic policy that was built in the last two decades as stemming from the new ‘Washington consensus’ and as linked to the processes of globalization and financialization (Galbraith 2012; Arestis, Charles, and Fontana 2013; Stockhammer 2015; Palley 2020). Such consensus has called for the implementation of new institutional forms that are based on labor market flexibility, intended as the increased freedom of employers to hire and fire workers (Tridico 2012). Flexibility has remarkably increased in recent times as policy makers have facilitated the rapid adjustment by firms of their production systems to FC. In this regard, [Figure 3](#) shows the

⁹The role of trade unions has also been stressed outside the PK community by Borjas and Ramey (1995) and Gordon (2012).

¹⁰As an alternative, the collective bargaining coverage could be used to represent labor market institutions. Notably, some countries present diverging tendencies: for instance, France shows low union density (8% in 2015) but high collective bargaining coverage (98%). However, as indicated by Iversen, Soskice, and Hope (2016), ‘in nearly all advanced economies, union membership is in structural decline (...) but the coverage of union wage agreements has not fallen in line with membership’ (176). This element suggest that union density should be considered as a better candidate to capture the process of labor movement’s power erosion.

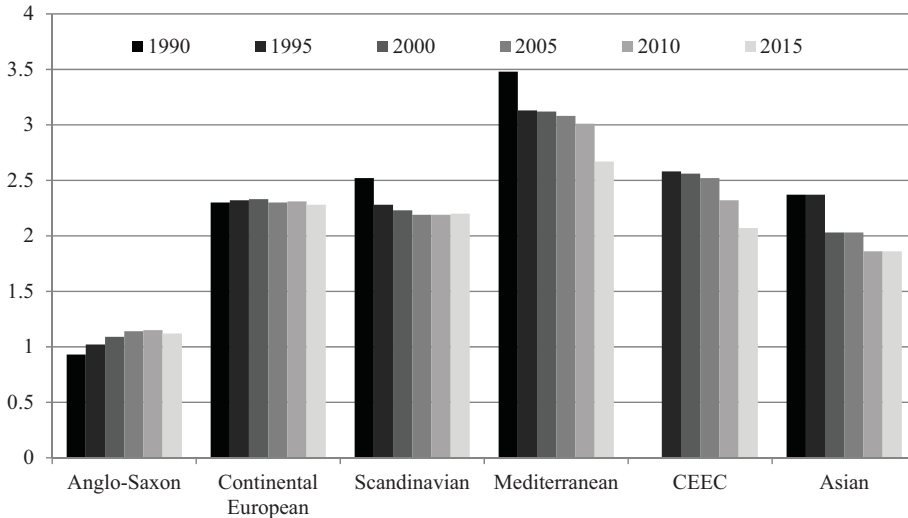


Figure 3. Employment protection by welfare model. Employment protection clustered by welfare model. Based on simple average value of the index of employment protection legislation for each group, calculated annually. The group of CEE countries (CEEC in the figure) starts from 1993. *Source:* our elaboration on OECD data (see [Appendix A](#)).

patterns of the employment protection index, an indicator based on the strictness of job legislation that reflects the degree to which employers are free to manage workers at will. Mediterranean countries show the highest employment protection, but with the strongest decline; Anglo-Saxon countries display the highest labor flexibility; countries belonging to the other models are on a similar, intermediate level.

Income Distribution

Many empirical works belonging to the PK approach elaborated on the relationships between financialization and income distribution, with the latter considered at both the functional and the personal level. The cornerstone of these works is the idea that financialization has fostered the implementation of the ‘downsize and distribute’ principle, whereby the only objective is to maximize dividends to shareholders at the cost of squeezing wages and downsizing firm dimensions (van Treeck 2015; Palley 2016; Hein 2019). Plenty of literature has testified that short-term strategies and shareholder value maximization have contributed to reducing both the wage share (Stockhammer 2013; Dünhaupt 2017; Pariboni and Tridico 2019) and investment in the non-financial sector (van Treeck 2009; Tori and Onaran 2020) decreased. That can be one of the reasons why increasing income inequality at the functional level not only involved emerging economies but also advanced ones, where the wage share in national income declined dramatically during 1980–1990 and later stagnated. In this regard, [Figure 4](#) reports the average wage share by country group. Asian countries show the highest wage shares, despite huge downward trends in the last decades; while wage shares remain higher in Scandinavian and Continental European countries than in Anglo-Saxon, Mediterranean, and CEE countries. Notably, after the 2007–09 financial and economic crisis, wage shares in Scandinavian and Continental European countries stabilized and even started to rise again.¹¹

¹¹This has recently been highlighted by Hein et al. (2018), Hein (2019) for Sweden and Germany, as two representatives of these groups.

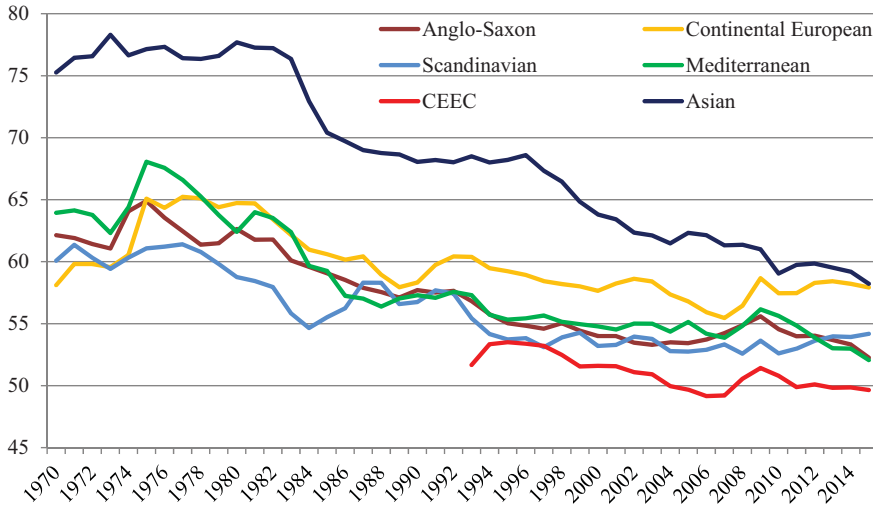


Figure 4. Wage shares by welfare model. Wage shares clustered by welfare model, based on simple average value of labor income share (adjusted wage share) for each group, calculated annually. The group of CEE countries (CEEC in the figure) starts from 1993. *Source:* our elaboration on Ameco database (see Appendix A).

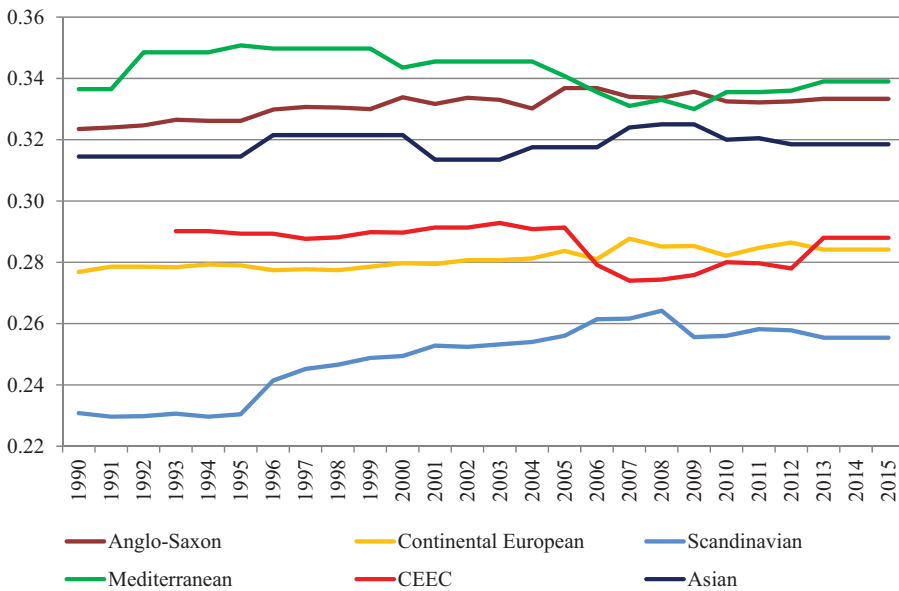


Figure 5. Income inequality by welfare model. *Note:* income inequality clustered by welfare model, based on simple annual average value of Gini coefficient for each group, calculated annually. The group of CEE countries (CEEC in the figure) starts from 1993. *Source:* our elaboration on OECD data (see Appendix A).

The increasing disparity is also found in the last decades when assessing income distribution at the personal level, as documented also outside the PK literature (see among others Atkinson 1999; Milanovic 2002; Piketty 2014). Recently, Antonelli, Calia, and Guidetti (2019) and Ranaldi and Milanović (2021) have shown that different socio-economic models present significantly different magnitudes of income inequality at the personal or household level. From the PK point of view, FC can contribute to income polarization through the redistribution of income from workers to top managers and from low-income households to the rich (Lin and Tomaskovic-Devey

2013; Hein 2018). In this respect, numerous works showed that, during the last twenty years, financialization is significantly correlated with higher inequality in personal incomes (Kus 2013; Flaherty 2015; Tridico 2017b). Figure 5 reports the average Gini coefficient, one of the most widespread measures of income polarization, regarding different socio-economic models, indicating greater levels of inequality in Mediterranean and Anglo-Saxon countries than in Scandinavian ones. Nevertheless, evidence confirms a quite general upward trend when changes are investigated instead of levels, confirming the increase of income disparities in the context of FC.

The three dimensions and the underlying indicators presented in this section will be the building blocks for our empirical exploration, which is aimed at quantitatively assessing the magnitude of the welfare systems of each country and at relating it with both the existing groupings and different measures of financialization.

The 'Welfare Index': Relationships with Welfare Models and the Patterns of Financialization

Our empirics draw on the already reported elaborations concerning the relationships between welfare and financialization. We wonder if countries belonging to different socio-economic models would be facing the challenges of FC in two opposite ways, namely: by opting for a relatively more generous welfare state, and hence exhibiting a 'reactive trajectory' (henceforth, RT), or by retrenching their welfare dimensions, and hence showing a 'compliant trajectory' (henceforth, CT). To test this hypothesis, we proceed by following a three-step strategy. First, we calculate our index of welfare by condensing the five variables examined in the previous section into a single metric. Second, we juxtapose it with the six models recently suggested by Tridico and Paternesi Meloni (2018): this test is intended to detect potential similarities and diversities and, more importantly, to discuss if a polarization of welfare trajectories would be confirmed by the evidence. Third, we verify if countries with higher/lower levels of welfare provision – and similarly if countries belonging to the RT or the CT grouping – are associated with different levels of financialization.

Data and Methodology

The main reference for our empirical exploration is the work by Hein, Paternesi Meloni, and Tridico (2021), who focused on the period straddling the 2007–09 financial and economic crisis. We extend their work in three directions. First, to adopt a longer-term perspective for the analysis of welfare trajectories, we expand the timespan going backward to 1990. Second, we explicitly consider indicators that represent income distribution: as discussed in the third and fourth sections, FC is likely to increase inequality at both personal and functional levels, and hence a more generous welfare sphere may also imply a more equitable income distribution.¹² Third, when comparing our metric of welfare to the existing taxonomies, we make use of the six groups identified by Tridico and Paternesi Meloni (2018) instead of the five groups by Hay and Wincott (2012): this allows us to isolate the Asian model from Corporative/Continental Europe, as both public social spending and the wage share are significantly different.

We make use of five indicators representative of the three pillars of welfare. Specifically:

¹²Some warnings have to be mentioned when dealing with indicators of income distribution, and in particular the wage share. On the one side, they can be not completely independent of 'direct' welfare provision through public social spending, as government action through taxes and transfers can alter income distribution. On the other side, even countries with strong welfare states, high union density and low inequality at the personal level can have a low wage share if coordinated policies of wage moderation are pursued.

- i. Public social spending (PSS) is proxied by the social expenditure made by the government (in % of gross domestic product);
- ii. Labor market institutions are represented by the unionization rate (TU) and the index of employment protection (EP);
- iii. Income distribution is analyzed at both the functional and the personal levels by making use of the wage share (WS) and the Gini coefficient (GINI), respectively.

Further details about data and sources are reported in [Appendix A](#). We define a system as more generous in terms of welfare when it presents higher public social spending, stronger labor market institutions and equitable distribution of income, the latter being represented by a *higher* wage share and a *lower* income inequality. As higher values of the GINI represent higher income concentration (with 0 = perfect equality and 1 = perfect inequality), we use its complement to the unity (1-GINI) to represent income equality. In this way, higher values of all our indicators are representative of a more generous system in terms of welfare.

We calculate the Welfare Index as a weighted combination by using a Principal Component Analysis (PCA), as in Hein, Paternesi Meloni, and Tridico (2021). Being the degree of welfare not directly observed, we consider it as a latent variable (LV), and we sought to infer it mathematically from five manifest variables (MVs). Technically, by seeking a linear combination of MVs such that the maximum variance is extracted from them, the PCA condenses a large set of variables to a single indicator that still contains most of the information provided by the larger set. The principal components are defined as a linear combination of the original variables, and these coefficients are then stored in a 'loading matrix', which can be interpreted as a rotation matrix since it rotates data such that the projection with the greatest variance goes along the first axis (*varimax*). Two further technical aspects have to be noted. First, we use z-standardized values for each variable; this allows us to use a covariance-based model (instead of a correlation-based one), even if our original MVs are not expressed in the same unit. Second, we do not consider a hierarchical construct within our empirics to avoid the imposition of a rigid structure on the data.

The main advantage of this methodology is that PCA simplifies the complexity of high-dimensional data while retaining trends and patterns, and, in the case of our Welfare Index, it does this by transforming the data into a *single* dimension which acts as a summary of socio-economic features. More details on the empirical procedure are available in [Appendix B](#).

We set forth the PCA analysis by computing the Welfare Index for the whole set of 32 countries at different time horizons (namely, 1990, 1995, 2000, 2005, 2010 and 2015). The choice of countries reflects the work of Tridico and Paternesi Meloni (2018), although we cannot include Chile and Israel because of a lack of data (cf. [Table 1](#)). Moreover, 23 out of 32 countries are considered in 1990 (in addition to CEE countries and Germany, data are not available for Iceland and Ireland for that year). All of this leads us to consider 183 observations, meaning an observation for each country-year combination; this strategy allows us to homogeneously compare the degree of welfare both across years and among countries.

Findings

[Figure 6](#) depicts the ranking of countries-years based on the scores of the Welfare Index, reported in detail in [Appendix C](#). At first sight, our empirics confirm the hypothesis of polarization: what emerges from our synthetic indicator of welfare is a kind of dichotomy of trajectories undertaken by the six socio-economic models, with positive values of the index typically achieved in Scandinavian and Continental European countries, while Anglo-Saxon and Asian countries exhibit a lower performance. In the middle of the scatter, we find Mediterranean and CEE countries, with the latter more oriented to lower welfare (the right tail of the distribution). Lastly, we

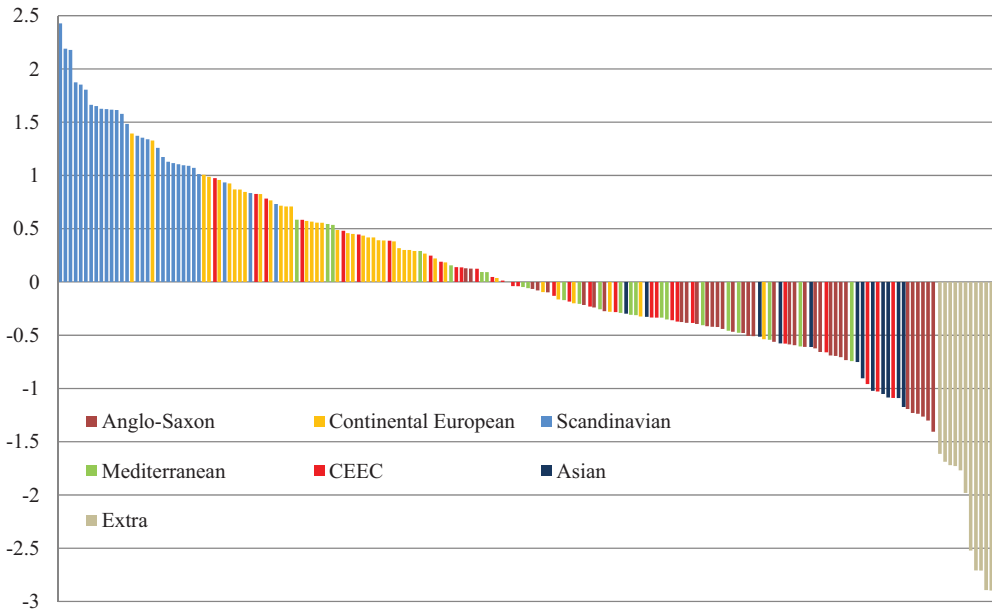


Figure 6. The Welfare Index. The graph depicts different values of the 'Welfare Index' calculated with respect to the whole set of 32 countries at different time horizons (namely, 1990, 1995, 2000, 2005, 2010 and 2015). Each bar represents a country-year observation (e.g., Sweden 1995 on the far-left, and Mexico 2000 on the far-right, as indicated in the detailed ranking reported in Appendix C). *Source:* our elaboration.

have a look at Mexico and Turkey: these countries performed the worst in terms of welfare generosity, validating the intuition nested in Tridico and Paternesi Meloni (2018).

Of course, some specific cases emerge at the national level and, therefore, merit discussion. On the left tail of the distribution, we systematically find Sweden, Finland and Denmark – Norway, particularly in the first decade of the 2000s, has fallen further behind. This is not surprising since PSS in Scandinavian countries is, on average, about 24% of GDP, as compared to 19% in the other observations. Conversely, at the bottom of the ranking, and immediately before Mexico and Turkey (not grouped), preceded by the United States that exhibits the worst welfare performance among Anglo-Saxon countries, mainly due to high income inequality at the personal level (the average Gini is 7 p.p. higher than in the rest of the sample) and very poor labor market institutions (notably, the EP is, on average, 0.25, as compared to 2.23 in the remaining countries). In the bottom positions, we observe two other withing-group heterogeneities. Both South Korea and Estonia seem to move away from the Asian and the CEE cluster, respectively: while the poor welfare scores of the former are mainly driven by low PSS (only 10.11% of GDP in 2015, the second-last value after Mexico), the low welfare generosity of the latter can be associated with its recent phase of transition toward a more liberal paradigm of economic policy (Thorhallsson and Kattel 2013), which might suggest that it should no longer be included in the CEE grouping (its average PSS is about 15% GDP, compared to 20% in the rest of the sample). The opposite reasoning can be advanced for Slovenia (where the average PSS is approximately 19%), which appears to meet the features of Continental European countries in terms of welfare (Tomšič, Kristan, and Adam 2008). In the middle, we find countries that combine some traditional traits of the Corporative model with elements of the Liberal model. The most emblematic cases are Italy and Japan: Italy exhibits positive, although very low, values of the Welfare Index throughout the entire timespan, and it is the most generous Mediterranean country in terms of welfare; Japan shows a moderately higher (albeit still negative) value of the Welfare Index, combining high wage share

Table 2. Socio-economic dimensions, the Welfare Index and welfare macro-models.

(A) <i>T</i> -test mean comparison based on the score of the Welfare Index							
Differences (WI > 0) – (WI < 0)	1990	1995	2000	2005	2010	2015	All
Public social spending (PSS)	10.93*** (1.77)	7.14*** (2.10)	6.92*** (1.56)	6.91*** (1.55)	6.32*** (1.59)	7.00*** (1.60)	7.34*** (0.73)
Trade union density (TU)	22.40*** (6.91)	24.56*** (6.06)	23.24*** (6.17)	25.25*** (6.21)	22.73*** (5.82)	23.07*** (5.99)	23.68*** (2.55)
Employment protection (EP)	0.27 (0.41)	0.47* (0.28)	0.47* (0.27)	0.46* (0.26)	0.66*** (0.22)	0.69*** (0.19)	0.52*** (0.11)
Wage share (WS)	–3.76 (2.86)	–2.02 (2.41)	–1.75 (2.29)	1.17 (2.29)	1.71 (2.05)	3.22 (2.28)	–0.01 (0.98)
Income equality (1-GINI)	0.10*** (0.02)	0.09*** (0.02)	0.08*** (0.01)	0.07*** (0.01)	0.06*** (0.01)	0.06*** (0.02)	0.07*** (0.01)
Observations	23	32	32	32	32	32	183
(B) <i>T</i> -test mean comparison based on reactive trajectory (RT) vs. compliant trajectory (CT).							
Differences (RT) – (CT)	1990	1995	2000	2005	2010	2015	All
Public social spending (PSS)	8.95*** (2.26)	8.69*** (2.00)	5.88*** (1.77)	6.39*** (1.68)	5.05*** (1.81)	5.78*** (1.83)	6.61*** (0.80)
Trade union density (TU)	18.05*** (7.56)	18.77*** (6.99)	23.82*** (6.39)	25.43*** (6.42)	24.07*** (5.93)	25.09*** (5.99)	22.89*** (2.69)
Employment protection (EP)	0.24 (0.42)	0.14 (0.29)	0.13 (0.29)	0.11 (0.27)	0.20 (0.26)	0.35* (0.22)	0.20* (0.12)
Wage share (WS)	–1.48 (2.98)	1.50 (2.50)	1.85 (2.37)	2.72 (2.31)	2.65 (2.08)	5.40** (2.22)	2.39** (0.99)
Income equality (1-GINI)	0.09*** (0.02)	0.07*** (0.02)	0.07*** (0.02)	0.06*** (0.02)	0.06*** (0.02)	0.06*** (0.01)	0.07*** (0.01)
Observations	23	32	32	32	32	32	183

Coefficients indicate the ‘difference of averages’ in observations (country-year). The outcome of our *t*-tests is the acceptance or the rejection of the null hypothesis which states that differences are purely due to random and not systematic errors, while the alternative hypothesis states the opposite. In Table 2(A) we consider the sign of the Welfare Index (WI) as a discriminant, and therefore we compare observations with positive and negative values of the index. In Table 2(B) we discriminate countries on the basis of showing a RT (namely, Scandinavian and Continental European groups) or a CT (all other groupings). Standard errors in round brackets; number of observations in square brackets; ****p* < 0.01, ***p* < 0.05, **p* < 0.1.

with low unionization (about 20% against an average of 33% in other countries) and EP (1.59 against an average of 2.18 in the remaining countries in the sample).

All in all, our index is supportive of the idea that, except for some cases, the degree of welfare is higher in Scandinavian and Continental European countries than in Anglo-Saxon, Asian, Mediterranean and CEE groupings. According to our findings, the first two models pursued a RT, while the remaining countries a CT.

Some empirical diagnostics are needed to verify if our index effectively reflects the indicators that it aims to condense. To this purpose, in Table 2 we verify whether the average values of each socio-economic indicator are significantly different from observations belonging to alternative clusters. We consider two alternative criteria: we first confront countries based on positive and negative values of our Welfare Index; second, we identify the two clusters according to our idea of model polarization – that is, by referring alternatively to the two macro-models labeled as RT (comprising Scandinavian and Continental European countries) and CT (all remaining countries). What emerges from the first criterion is that four out of five welfare dimensions show statistically different averages (about 7% GDP in PSS, 0.5 in EP, more than 20 p.p. in TU, and 7 p.p. in the Gini), with the only exception being the wage share (Table 2(A)). When we make use of the second criterion (Table 2(B)), our idea of dualization is entirely confirmed since all welfare indicators showed statistically different means (with also a 2% gap in the average values of the wage share).

Table 3. Financialization, the Welfare Index and welfare macro-models.

(A) T-test mean comparison based on the score of the Welfare Index							
Differences (WI > 0) – (WI < 0)	1990	1995	2000	2005	2010	2015	All
Market capitalization (MKT)	-13.31 (10.24) [23]	-17.06 (12.73) [32]	-6.17 (23.89) [32]	3.44 (18.14) [32]	-15.80 (18.52) [32]	-12.35 (17.07) [32]	-10.41 (7.49) [183]
Credit by financial sector (CRED)	-36.95 (43.52) [12]	-50.15 (44.87) [14]	-11.91 (48.02) [14]	-7.10 (22.45) [31]	20.70 (24.44) [31]	1.41 (23.83) [30]	7.19 (12.12) [132]
Dividends of non-financial corporations (DIV)	-0.21 (0.69) [19]	1.68* (0.85) [21]	2.01 (1.46) [21]	3.86** (1.54) [21]	3.23** (1.59) [21]	5.27* (2.80) [21]	2.79*** (0.75) [124]
Foreign direct investment (FDI)	1.61 (0.99) [21]	0.55 (1.01) [30]	5.13 (4.15) [30]	13.16* (6.64) [32]	11.91 (8.21) [32]	-0.26 (10.96) [32]	6.01** (2.82) [177]
(B) T-test mean comparison based on reactive trajectory (RT) vs. compliant trajectory (CT).							
Differences (RT) – (CT)	1990	1995	2000	2005	2010	2015	All
Market capitalization (MKT)	-2.02 (10.71) [23]	13.12 (13.32) [32]	57.85*** (22.33) [32]	42.02** (16.95) [32]	29.47* (18.59) [32]	31.09*** (16.82) [32]	29.06*** (7.44) [183]
Credit by financial sector (CRED)	-0.96 (45.06) [12]	-16.22 (42.56) [14]	6.75 (43.69) [14]	20.09 (22.67) [31]	27.06 (24.88) [31]	24.01 (23.89) [30]	20.83* (12.33) [132]
Dividends of non-financial corporations (DIV)	-0.18 (0.62) [19]	1.93** (0.82) [21]	3.45*** (1.31) [21]	4.82*** (1.39) [21]	4.54*** (1.34) [21]	7.33*** (2.51) [21]	3.65*** (0.71) [124]
Foreign direct investment (FDI)	0.85 (0.93) [21]	0.68 (1.04) [30]	13.75*** (3.86) [30]	17.50** (6.49) [32]	14.36* (8.15) [32]	8.75 (10.53) [32]	9.91*** (2.87) [177]

Coefficients indicate the 'difference of averages' in observations (country-year). The outcome of our t-tests is the acceptance or the rejection of the null hypothesis which states that differences are purely due to random and not systematic errors, while the alternative hypothesis states the opposite. In Table 3(A) we consider the sign of the Welfare Index (WI) as a discriminant, and therefore we compare observations with positive and negative values of the index. In Table 3(B) we discriminate countries on the basis of showing a RT (namely, Scandinavian and Continental European groups) or a CT (all other groupings). Standard errors in round brackets; number of observations in square brackets; *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.

The Patterns of Welfare and Financialization

We now relate welfare trajectories to the trends of financialization. To this purpose, we verify if countries belonging to different models behave differently in terms of some indices of financialization. We investigate it by performing the just-mentioned tests for the comparison of averages to the four metrics of financialization introduced in the third section, namely: market capitalization (MKT), domestic credit provided by the financial sector (CRED), distributed dividends of non-financial corporations (DIV), and foreign direct investments (FDI). In doing that, we discriminate countries by using the same criteria introduced in the fifth section above: specifically, the first criterion allows us to confront countries based on the scores of our Welfare Index (Table 3(A)), while the second criterion identified the two trajectories termed RT and CT (Table 3(B)).

Some interesting results emerge by juxtaposing the process of financialization with different models. On panel average, market capitalization (MKT) was about 41% of GDP in 1995, it peaked at 74% before the financial crisis (2005) and then settled at approximately 63% (2015). Notwithstanding this trend, and contrary to what emerges for the welfare domains, no evidence of polarization is traced concerning MKT when discriminating based on the values of the Welfare Index. Indeed, in 2015 the average MKT of countries with a positive value of our index of welfare was about 56% GDP, while 69% in the rest of the sample, with no statistically

significant differences between the two averages. Nevertheless, when we apply the dichotomy between RT and CT, we find that Scandinavian and Continental European countries present higher market capitalization than countries belonging to the CT. This finding is consistent with the idea that, in countries belonging to the RT, higher welfare generosity may have partially compensated for the harmful effects of financialization. An additional element emerging from our analyses is that the financialization process remarkably involved all the countries under investigation: Asian, CEE, Mediterranean and Scandinavian countries almost doubled their average market capitalization as compared to 1995, while Anglo-Saxon countries did not experience such a relative increase due only to their early process of intense marketization (already started in the 1980s).

We reach a similar conclusion when investigating the patterns of financialization by making use of the credit provision (CRED). When distinguishing countries based on the sign of the Welfare Index, in 2015 we find a virtually zero difference in the amount of credit (144.7% GDP in countries exhibiting positive values in the index, and 143.3% in the rest of the sample). This element indicates a significant degree of convergence toward very high levels of financialization. However, the picture is partially different when clustering countries in the two trajectories of RT and CT: in 2015, the difference reaches 24 p.p. of GDP (approximately 134% in CT and 158% in RT), despite non-statistically significant. When the whole timespan is considered, we find a significantly higher level of credit provision in RT than in CT (about 21% GDP), while the difference is not significant when using the sign of the Welfare Index as a discriminant. However, it is worth highlighting that both trajectories converged to higher levels of financialization in terms of credit: while in 1990 the credit by the financial sector settled, on average, at 95% GDP, in 2015 it reached 144% GDP (after having peaked at 156% GDP in 2010).

When extending the inquiry to the distributed dividends of non-financial corporations (DIV), the two criteria qualitatively show the same result: countries with higher scores on the Welfare Index, as well as countries belonging to the RT grouping, present higher levels of financialization. Specifically, this difference peaked in 2015, with a gap of 5.2 p.p. for the first criterion and 7.3 p.p. for the second. The pattern is confirmed when considering all the period. The process of financialization of non-financial corporations, measured as distributed dividends (in percent of GDP), is, therefore, more intense in countries belonging to the Scandinavian and Continental European model (on average, 6% GDP) than in the rest of the sample (2.4%). Partially, this may depend on the progressive transition toward a market-based financial system (instead of the traditional bank-based one) of some European countries: particularly, from 1995 to 2015 dividends nearly tripled in Scandinavian countries and doubled in Continental Europe.

The same test has been applied to the fourth metric of financialization, namely foreign direct investment (FDI), inflows plus outflows in percent of GDP. As discussed above, this metric can capture some features of financialization that are associated with the financial aspects of globalization. According to the empirical evidence, financialization also intensified in terms of FDI in recent times: in this regard, the average FDI of our panel of countries was approximately 3% of GDP before 2000, it reached 15% before the global financial and economic crisis (in 2005) and then stabilized (about 13% in 2015). When considering this indicator and comparing it to different levels of welfare provision, we find a picture that is quite consistent with the analysis of dividends. FDI is higher in countries exhibiting higher welfare states, that is, in those countries identified as presenting positive values of the Welfare Index or belonging to the RT, alternatively. Nonetheless, such dissimilarity emerges in the last years exclusively, confirming what is postulated by the compensation argument: according to the evidence, Scandinavian and Continental European countries willingly regulated both increased financialization and globalization through an intensification of their welfare states, following the strategy of compensation, while countries falling into the CT group have opted for models in line with the efficiency argument.¹³

Two main outcomes emerge from this exploration. On the one hand, we find evidence of a general intensification of the process of financialization in all its dimensions, supporting the idea of a wide-reaching tendency toward the traits of FC. On the other hand, countries have chosen to deal with it in opposite ways. In those that have preferred to be compliant with this process, direct welfare provision and institutions have been progressively reduced. This is particularly evident in the Anglo-Saxon world, which opted for a retrenchment after a period characterized by relatively generous welfare systems (from the post-World War II until the 1970s). In contrast, countries that at the beginning of the 1990s still presented stronger welfare systems, such as those belonging to the Continental and Scandinavian models, institutions and public social spending represented a reaction against the negative aspects of financialization.

Of course, the timing of the policy responses to increasing financialization, if any, may vary across countries or even across countries belonging to the same model. Similarly, the way welfare is provided (e.g., social insurance vs. services, coverage rates, eligibility criteria, and the structure of benefits) can differ across States (cf. Esping-Andersen 1990). Despite these caveats, our findings are in principle consistent with the perception of Hay (2020) that kicked off our paper: FC seems to be the ultimate frontier of capitalism all over mature economies, which, however, may handle it by opting for a more generous welfare state, as in the case of a RT, or for a retrenchment of the welfare sphere, as in countries presenting a CT.

Concluding Remarks

The post-Great Recession phase of stagnation posed important challenges to high-income countries in several domains of the economy and represented a test case to determine whether their welfare states could deal with the threats of capitalism in its most recent version. In this article, we elaborated on the nexus between welfare and financialization by following the emerging, PK approach to CPE.

After having discussed the current taxonomies of socio-economic models, we scrutinized our hypothesis of alternative welfare trajectories under financialization. In so doing, we built a comprehensive metric of welfare that condenses different dimensions (a ‘Welfare Index’ for 32 OECD countries from 1990 to 2015). The index offers some interesting food for thought when compared with the welfare models already identified in the literature and the patterns of financialization. While recognizing a general, worldwide tendency toward the features of finance-dominated capitalism, the index supports the idea that countries are facing the current phase of capitalism in two distinct ways. That allows us to advise some elements for an update to the existing groupings by suggesting a dualization between countries willing to increase and/or maintain higher levels of welfare (here identified as belonging to the ‘reactive trajectory’), and countries that opt for a retrenchment of welfare provision (the ‘compliant trajectory’). When juxtaposing our index with the current classifications, we find two distinct tendencies: on the one side, Scandinavian and Continental European countries are likely to belong (albeit with a few exceptions) to the RT group, sharing higher welfare provision and stronger labor market institutions, combined with a more equal distribution of income; on the other side, Anglo-Saxon, Asian, Mediterranean, and CEE countries appear to be increasingly characterized by the traits of the CT, that is, poorer levels of public welfare support, lower labor market institutions and higher income inequality.

¹³Partially beyond the scope of this work, we verified how our index of welfare relates with globalization by juxtaposing it to three standard measures of trade openness, as well as to a composite index of globalization (the KOF Index). Results are reported in Appendix D. All metrics indicate that globalization is more intense in countries and models with a more generous welfare state: countries with a positive Welfare Index present higher trade openness (+30% GDP), export (+17% GDP), import (+12% GDP), and the KOF (+6 p.p.). The picture is completely confirmed when discriminating based on the RT/CT dichotomy. This side-exploration confirms the hypothesis of a compensation strategy.

While all countries are converging to higher financialization, this process is even more intense in the Scandinavian and Continental European model, that is in countries featuring higher welfare. This element has a relevant policy implication: socio-economic measures and institutions can be strong enough to the point that countries with a higher level of welfare generosity have been able to counteract the negative effect of the current era of capitalism by achieving lower disparity, although in the presence of deeper financialization.

That leads us to take seriously the last debates casting doubt on the existence of differentiated capitalisms: while all countries are converging to higher levels of finance, the socio-economic consequences of this process can still be faced, managed and mitigated through different policies and institutions – that is, through different welfare systems. In other words, the ‘compensation argument’ already emerged in the literature concerning globalization seems to be valid also for the process of financialization of the economy.

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Appendix A. Data and sources

Public social spending (PSS)	Public social spending (as % GDP). Source: OECD.Stat, Social Expenditure Database (SOEX).
Trade union density (TU)	Trade union density (administrative data, survey data when administrative data are not available). Source: OECD.Stat, Income Distribution and Poverty.
Employment protection (EP)	Strictness of employment protection – individual and collective dismissals (regular contracts). Source: OECD.Stat, Labor.
Wage share (WS)	Adjusted wage share (% of GDP). Source: Ameco database. Series have been integrated with the ILO database (labor income share).
Inequality index (GINI)	Gini coefficient post taxes and transfers (disposable income). Due to data availability, note that for 2015 we use data of 2013. Source: OECD.Stat, Income Distribution and Poverty.
Market capitalization (MKT)	Market capitalization of listed domestic companies (% of GDP). Source: World Bank database.
Credit by financial sector (CRED)	Domestic credit provided by the financial sector (% of GDP). Source: World Bank database.
Dividends of non-financial corporations (DIV)	Distributed income of non-financial corporations, dividends plus withdrawals (% of GDP). Source: Eurostat.
Foreign direct investments (FDI)	Foreign direct investment, inflows plus outflows (% of GDP). Source: our elaboration on World Bank database.
Export (EXP)	Export of goods and services (% of GDP). Source: World Bank database.
Import (IMP)	Import of goods and services (% of GDP). Source: World Bank database.
Trade openness (OPEN)	Export plus import of goods and services (% of GDP). Source: World Bank database.
KOF Globalization Index	The KOF Globalization Index measures the economic, social and political dimensions of globalization. Source: ETH Zurich, KOF Swiss Economic Institute (https://kof.ethz.ch/).

Appendix B. Statistical annex

Welfare Index: descriptive analyses and correlation matrix of MVs.

Variable	Observations	Min	Max	Mean	Std. dev.
PSS	183	2.682	31.685	19.494	6.146
TU	183	4.500	95.200	32.759	20.842
EP	183	0.257	4.833	2.169	0.764
WS	183	36.873	75.280	54.771	6.635
1-GINI	183	0.488	0.791	0.692	0.057

Variables	PSS	TU	EP	WS	1-GINI
PSS	1.000	–	–	–	–
TU	0.283	1.000	–	–	–
EP	0.136	0.035	1.000	–	–
WS	–0.014	0.017	–0.058	1.000	–
1-GINI	0.590	0.513	0.091	0.166	1.000

Principal components/correlation

Number of obs. = 183.

Number of comp. = 5.

Trace = 5.

Rotation: varimax

Rho = 1.0000.

Component	Eigenvalue	Difference	Proportion	Cumulative
Comp1	1.96968	0.889755	0.3939	0.3939
Comp2	1.07992	0.153999	0.2160	0.6099
Comp3	0.92592	0.221147	0.1852	0.7951
Comp4	0.70477	0.385066	0.1410	0.9361
Comp5	0.31970	–	0.0639	1.0000

Principal components (eigenvectors).

Standardized variable	Comp1	Comp2	Comp3	Comp4	Comp5	Unexplained
PSS	0.5543	–0.1520	–0.0381	–0.6342	0.5157	0
TU	0.5055	0.0667	–0.2872	0.7301	0.3528	0
EP	0.1499	–0.6404	0.7147	0.2380	–0.0043	0
WS	0.1005	0.7413	0.6366	0.0232	0.1860	0
1-GINI	0.6361	0.1132	–0.0075	–0.0873	–0.7582	0

Latent variable	Manifest Variables	Correlation (LV/MV)	Communality	Average communality
Welfare Index	PSS	0.778	0.605	0.394
	TU	0.709	0.503	
	EP	0.210	0.044	
	WS	0.141	0.020	
	1-GINI	0.893	0.797	

Appendix C. The Welfare Index: scores and ranking

Rank	Code	WI	Rank	Code	WI	Rank	Code	WI
1	SW 1995	2.428	62	FR 2015	0.418	123	UK 2015	-0.383
2	SW 1990	2.191	63	FR 2010	0.391	124	PL 2015	-0.384
3	FI 1995	2.179	64	LU 2015	0.390	125	AU 2000	-0.394
4	DK 1995	1.874	65	HU 1995	0.388	126	ES 2000	-0.405
5	FI 1990	1.854	66	FR 2005	0.381	127	UK 2005	-0.416
6	SW 2000	1.805	67	NL 1995	0.318	128	CA 2015	-0.421
7	DK 2010	1.663	68	DE 2015	0.301	129	CA 2010	-0.422
8	FI 2015	1.652	69	NL 2015	0.301	130	IE 2015	-0.441
9	SW 2005	1.626	70	FR 2000	0.291	131	PT 2000	-0.458
10	DK 2005	1.623	71	IT 2005	0.291	132	UK 1995	-0.468
11	DK 2000	1.618	72	NL 2010	0.267	133	GR 1990	-0.477
12	DK 2015	1.615	73	CZ 2000	0.247	134	CA 2000	-0.480
13	DK 1990	1.578	74	FR 1990	0.221	135	CA 2005	-0.506
14	FI 2010	1.484	75	CZ 2010	0.190	136	NZ 2015	-0.508
15	BE 2015	1.394	76	NL 2005	0.184	137	JP 2005	-0.514
16	SW 2010	1.372	77	IT 2000	0.156	138	CH 1990	-0.538
17	FI 2000	1.355	78	SK 2000	0.139	139	PT 1995	-0.544
18	SW 2015	1.340	79	CZ 2005	0.138	140	AU 2015	-0.563
19	BE 2010	1.329	80	IE 2010	0.128	141	JP 1995	-0.576
20	FI 2005	1.258	81	NZ 1990	0.125	142	EE 1995	-0.579
21	IS 2005	1.173	82	SI 1995	0.124	143	NZ 2005	-0.587
22	NO 1995	1.129	83	PT 2010	0.093	144	NZ 1995	-0.594
23	IS 2015	1.116	84	IT 1995	0.092	145	GR 1995	-0.605
24	NO 1990	1.105	85	CZ 2015	0.047	146	IE 2005	-0.609
25	IS 2000	1.096	86	NL 2000	0.037	147	JP 2000	-0.611
26	IS 2010	1.090	87	HU 2000	0.012	148	UK 2000	-0.623
27	NO 2015	1.071	88	GR 2015	0.001	149	UK 1990	-0.658
28	IS 1995	1.013	89	HU 2005	-0.039	150	EE 2010	-0.660
29	AT 1995	1.006	90	HU 2010	-0.040	151	IE 2000	-0.691
30	BE 2005	0.988	91	ES 2010	-0.048	152	NZ 2000	-0.695
31	SI 2000	0.976	92	GR 2010	-0.058	153	AU 2005	-0.706
32	BE 1995	0.959	93	CA 1995	-0.066	154	AU 2010	-0.734
33	NO 2010	0.934	94	CA 1990	-0.080	155	PT 1990	-0.743
34	AT 1990	0.925	95	CH 2015	-0.096	156	JP 1990	-0.752
35	BE 1990	0.869	96	IE 1995	-0.098	157	KR 2015	-0.905
36	AT 2000	0.868	97	SK 2010	-0.130	158	EE 2000	-0.958
37	BE 2000	0.845	98	CH 2010	-0.165	159	KR 1990	-1.022
38	NO 2005	0.835	99	PT 2015	-0.170	160	EE 2005	-1.028
39	SI 2005	0.827	100	PL 1995	-0.184	161	KR 2010	-1.053
40	AT 2005	0.826	101	CH 2005	-0.201	162	KR 1995	-1.085
41	SI 2010	0.783	102	PT 2005	-0.205	163	EE 2015	-1.090
42	DE 1995	0.766	103	UK 2010	-0.216	164	KR 2005	-1.090
43	NO 2000	0.732	104	SK 2015	-0.231	165	KR 2000	-1.174
44	AT 2015	0.716	105	AU 1990	-0.240	166	US 2010	-1.193
45	DE 2000	0.709	106	ES 2015	-0.257	167	US 1990	-1.230
46	AT 2010	0.709	107	AU 1995	-0.275	168	US 1995	-1.238
47	IT 2015	0.584	108	CH 1995	-0.280	169	US 2000	-1.263
48	SK 1995	0.583	109	PL 2010	-0.283	170	US 2015	-1.301
49	LU 1995	0.573	110	ES 1990	-0.291	171	US 2005	-1.406
50	LU 1990	0.567	111	JP 2015	-0.298	172	TR 2005	-1.614
51	LU 2005	0.557	112	ES 1995	-0.309	173	TR 1995	-1.688
52	LU 2010	0.556	113	GR 2005	-0.312	174	TR 2015	-1.720
53	IT 2010	0.545	114	CH 2000	-0.324	175	TR 2000	-1.729
54	IT 1990	0.535	115	JP 2010	-0.328	176	TR 2010	-1.769
55	NL 1990	0.488	116	PL 2000	-0.334	177	TR 1990	-1.981
56	SI 2015	0.480	117	HU 2015	-0.335	178	MX 2010	-2.523
57	LU 2000	0.459	118	ES 2005	-0.335	179	MX 2015	-2.709
58	FR 1995	0.450	119	GR 2000	-0.352	180	MX 2005	-2.710
59	CZ 1995	0.446	120	PL 2005	-0.359	181	MX 1995	-2.893
60	DE 2010	0.435	121	SK 2005	-0.371	182	MX 1990	-2.898
61	DE 2005	0.418	122	NZ 2010	-0.376	183	MX 2000	-2.951

Appendix D. Globalization, the Welfare Index and Welfare Macro-Models

(A) *T*-test mean comparison based on the score of the Welfare Index.

<i>Differences</i> ($WI > 0$) – ($WI < 0$)	1990	1995	2000	2005	2010	2015	All
Export (EXP)	20.22** (7.44) [23]	13.84* (6.69) [32]	18.80** (8.92) [32]	17.80* (9.41) [32]	20.28* (10.34) [32]	14.50 (12.64) [32]	17.27*** (4.00) [183]
Import (IMP)	15.01** (6.59) [23]	9.98 (5.92) [32]	14.39* (7.62) [32]	11.68 (8.19) [32]	14.57* (8.46) [32]	11.73 (10.34) [32]	12.63*** (3.37) [183]
Openness (OPEN)	35.24** (13.98) [23]	23.83* (12.51) [32]	33.20* (16.41) [32]	29.48 (17.49) [32]	34.86* (18.74) [32]	26.24 (22.93) [32]	29.91*** (7.34) [183]
Globalization Index (KOF)	11.78** (3.51) [23]	5.55* (3.16) [32]	5.58** (2.62) [32]	5.91** (2.22) [32]	5.61*** (1.87) [32]	3.78** (1.83) [32]	5.98*** (1.29) [183]

(B) *T*-test mean comparison based on reactive trajectory (RT) vs. compliant trajectory (CT).

<i>Differences</i> (RT) – (CT)	1990	1995	2000	2005	2010	2015	All
Export (EXP)	25.15*** (6.77) [23]	12.12* (7.04) [32]	17.39* (9.35) [32]	18.14* (9.64) [32]	17.79 (10.80) [32]	16.08 (12.99) [32]	17.01*** (4.13) [183]
Import (IMP)	20.00*** (6.04) [23]	6.33 (6.29) [32]	9.86 (8.133) [32]	10.70 (8.456) [32]	10.11 (8.97) [32]	11.85 (10.67) [32]	10.73*** (3.51) [183]
Openness (OPEN)	45.16*** (12.70) [23]	18.45 (13.26) [32]	27.25 (17.37) [32]	28.84 (18.00) [32]	27.91 (19.79) [32]	27.94 (23.60) [32]	27.74*** (7.61) [183]
Globalization Index (KOF)	14.36*** (3.07) [23]	11.89*** (2.66) [32]	10.04*** (2.25) [32]	7.97*** (2.06) [32]	6.91*** (1.81) [32]	5.56*** (1.74) [32]	8.92*** (1.24) [183]

Coefficients indicate the 'difference of averages' in observations (country-year). The outcome of our *t*-tests is the acceptance or the rejection of the null hypothesis which states that differences are purely due to random and not systematic errors, while the alternative hypothesis states the opposite. In Appendix D(A) we consider the sign of the Welfare Index (WI) as a discriminant, and therefore we compare observations with positive and negative values of the index. In Appendix D(B) we discriminate countries on the basis of showing a RT (namely, Scandinavian and Continental European groups) or a CT (all other groupings). Standard errors in round brackets; number of observations in square brackets; *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$.