

LEVERHULME
TRUST _____

The Leverhulme Trust Annual Lecture 2018

Dame Minouche Shafik: 'Why Are We So Miserable When Things
are Getting Better?'

Why Are We So Miserable When Things are Getting Better?

Minouche Shafik

Director

London School of Economics and Political Sciences¹

I have been very preoccupied with a paradox. Why are people in some of the richest and most successful countries in the world so miserable when so much of the economic, social and political data show that things are getting better? Where did all that anger and anxiety come from that is manifested in populism, terrorism, and worsening well-being and mental health? Are we, despite the massive gains in material progress in recent decades, living in an age of insecurity? And has that insecurity caused us to repudiate liberal democracy, liberal economies and a rules-based international system that have enabled this progress? And if that is the case, what can be done to restore a sense of security and well-being in our societies?

There are broadly two prevailing explanations for the current malaise – economic inequality and identity politics. While I agree with those explanations, I think the reason they caused such huge ruptures is that the mechanisms we have for dealing with them – our social contract – has failed to keep up with new pressures. By social contract I mean the rights and obligations of citizenship, the payment of taxes in exchange for public goods, and the way that society looks after the old and the young, the infirm and those who have fallen on hard times. Our social contract has frayed as a result of the pressures put on it by hyper-globalisation and the austerity that was imposed in the wake of the financial crisis. The answer is not to de-globalise and revert to our national silos, but to re-think our social contract to heal these tensions. We also need to prepare for an economic future in which ageing and automation will present new challenges.

Things Really have Got Better

I won't spend much time this evening on the easy part of the story. The evidence on the massive improvement in material progress is overwhelming and compelling. We are richer, healthier and safer than at any time in human history. As Yuval Harari has reminded us, "In the early twenty-first century, for the first time in history, more people die from eating too much than from eating too little...and more people commit suicide than are killed by war, crime and terrorism put together."² But the reams of data and volumes of publications that demonstrate this human progress have done little to shift public opinion which in many advanced economies is characterised by a "declinist" narrative.

The Age of Insecurity

My focus this evening will be on the advanced economies where I think the age of insecurity is most acute, although many of the symptoms can be seen in other parts of the world. In politics, the age of insecurity is manifested in the rise of populism. In economics, it is

¹ I have benefited enormously from helpful discussions and comments from Tim Besley, Julia Black, Mick Cox, Paul Dolan, Robert Falkner, Richard Layard, Eric Neumeier, Mike Savage, Nick Stern, Lucy Shackleton, Andres Velasco.

² Harari, Yuval (2016), "Does Trump's Rise Mean Liberalism's End?" The New Yorker, 7 October 2016.

associated with the view that advanced economies have stagnated with low productivity and poor prospects for future generations. And in social policy, there is evidence of declining subjective well-being and trust in many countries often accompanied by hostility to immigrants. Let's consider each in turn.

Populist Politics

There is no doubt that populist politics is on the rise across the world. The list is long and growing: the US, France, the Netherlands, Germany, Greece, Spain, Bolivia, Venezuela, the Philippines, Italy, Hungary, Poland, to name a few. All of these populist movements share common strategies – they are critical of elites, anti-pluralist, use identity politics, and claim to be the truly legitimate representatives of “the people.” Of course, populism has existed for decades – why the sudden increase around the world?

Confidence in elites took a huge blow with the financial crisis and great recession that followed. Elites lost credibility for their competence but also for the unjust burdens that “Main Street” had to endure (in the form of falling incomes, welfare cuts, collapsing housing markets) to save “Wall Street” (which seemed to get off scot free, with their bonuses). The crisis was a turning point that fuelled public anger that the system was rigged and enabled growing support for anti-elitist populist politicians especially in the epicentre of the crisis in the US and Europe. Arguably, elites saved themselves but sacrificed confidence in the system as a consequence.

Stagnant Economies

Turning to the economic causes of insecurity, there are very real fears that economic progress in advanced economies is slowing. The last decade has seen a sharp fall in productivity growth across OECD countries. Robert Gordon argues that the most important technological innovations occurred in the past and productivity growth will inevitably slow in future.³ Larry Summers has argued this means that the advanced economies are going through a period of “secular stagnation” which translates into low interest rates and low growth.⁴ This declinist narrative is also geopolitical as “The West,” which has dominated the world for the last 400 years, adjusts to the fact that the future will be dominated by “The East.”

Economic stagnation has been felt by many households, even if aggregate incomes have improved. McKinsey found that between 65-70% of households in 25 advanced economies (equivalent to 540-580 million people) experienced flat or falling incomes between 2005-2014. Young and less well-educated workers were the hardest hit. Survey data in the US, UK and France showed two out of five people felt their economic positions had deteriorated over that period. One third thought that their children would face the prospect of being poorer than their parents. Not surprisingly, those with stagnant incomes were more likely to have negative attitudes to immigration and to trade.⁵

³ Gordon, R.J. (2016) The Rise and Fall of American Growth: the U.S. Standard of Living Since the Civil War, Princeton: Princeton University Press.

⁴ Summers, L. (2014), “U.S. Economic Prospects: Secular Stagnation, Hysteresis and the Zero Lower Bound,” Business Economics 49, pp. 65-73 (get better reference)

⁵ McKinsey(2016), Poorer than their Parents, McKinsey Global Institute

Well-being not doing so well

Turning to the social signs of insecurity, there is evidence of a broad-based decline in happiness in several major advanced economies -- starting with Italy, followed by the US, Denmark, Spain, France, Canada, the UK, Ireland, the Netherlands and Austria.⁶ It is interesting that, with the exception of Canada, all of those countries experienced serious dislocations during the financial crisis and have seen the rise of populist political forces.

The US has seen largest fall in happiness of any advanced economy except Italy and there has been considerable research to understand the causes of this. Blanchflower and Oswald show that Americans are becoming less happy over time and this trend is especially severe among those with less education.⁷ Real per capita incomes in the U.S. have more than tripled since the late 1950s, but the proportion of the population saying they are very happy has been flat and even slightly declined.

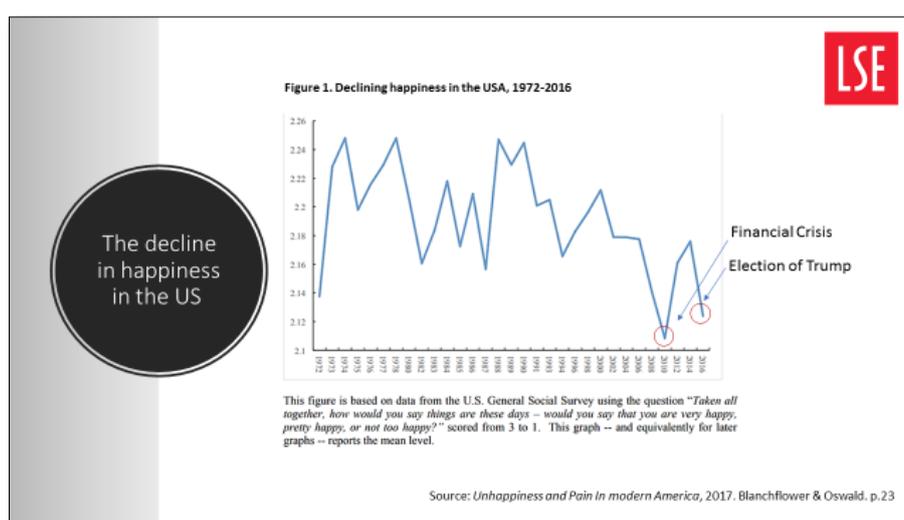


Figure 1: The decline of happiness in the US

Causes of the Age of Insecurity

The indicators above – the rise of populism, stagnant economies and deteriorating well-being – all point, to growing dissatisfaction in many countries. Some of this is driven by misperceptions often fuelled by misinformation from the media. But I believe there are also very real structural forces at play. Those structural forces include (1) inequality and who reaps the benefits of economic progress; (2) austerity and the fraying of safety nets that look after those who fall behind; (3) a reassertion of identity politics and questions of who belongs; and (4) fear about future prospects in light of massive technological changes ahead. Let me discuss each in turn.

Misperceptions and the Media

Let me start with misinformation driven by the media. There is no doubt that part of the perceived miserableness is because people get their local information through actual experience whereas national and global information is mediated through the media which has

⁶ Sachs, J.D., Layard, R. and Helliwell, J.F. (2018). *World Happiness Report 2018* (No. id: 12761).

⁷ Blanchflower, D and A. Oswald (2018), "Unhappiness and Pain in Modern America," forthcoming in *Journal of Economic Literature*.

become more negative. In the UK for example, most people believe crime is increasing, despite the fact that it has been declining steadily, and they attribute this perception to information they get from TV and the newspapers.⁸ As a result of this misperception, confidence in the government's ability to tackle crimes has fallen at the same time as actual crimes have declined sharply. Meanwhile, public spending on crime has risen steadily to respond to public perceptions based on anxiety fuelled by the media.

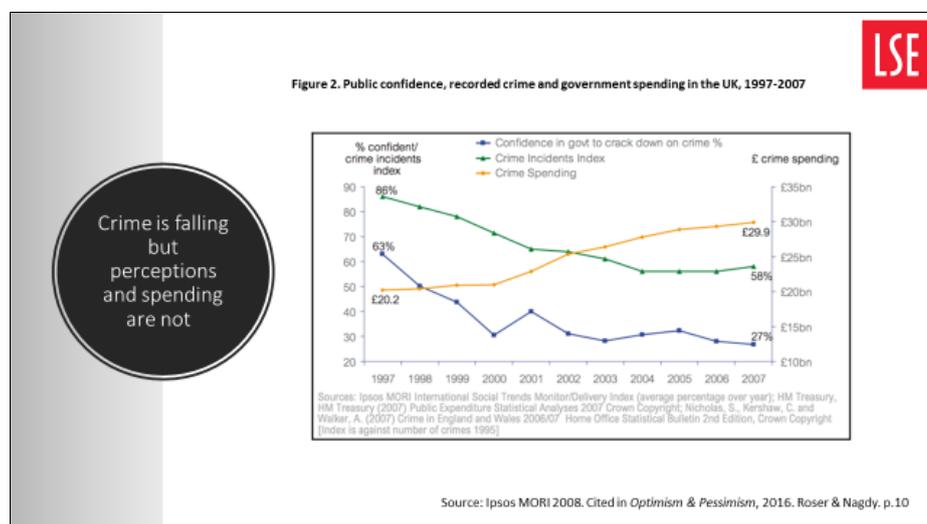


Figure 2: Crime is falling but perceptions and spending are not

There is also no doubt that media coverage has become more negative over time as competition in journalism has become more fierce. Consider data analysed using a technique called “sentiment mining” by Kalev Leetaru drawing on every article published in the New York Times between 1945 and 2005 as well as an archive of translated articles from 130 countries between 1979-2010. Sentiment mining evaluates the emotional tone of articles by counting how frequently positive words (like good or nice) are used relative to negative words (like horrific or terrible). It shows clearly that the “tone” of the news has become more negative over time. Social media, with its competition for “clicks” – has only accelerated this trend.

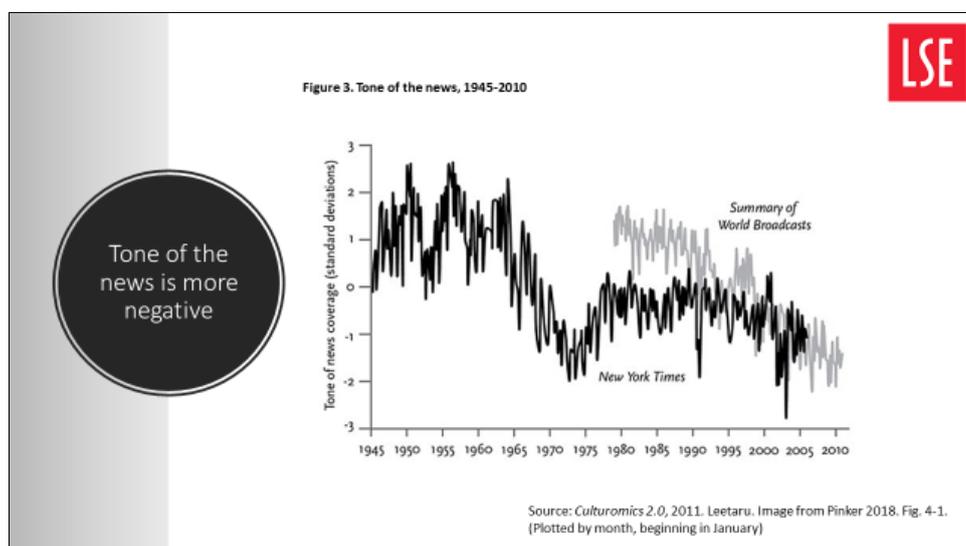


Figure 3: Tone of the news is more negative

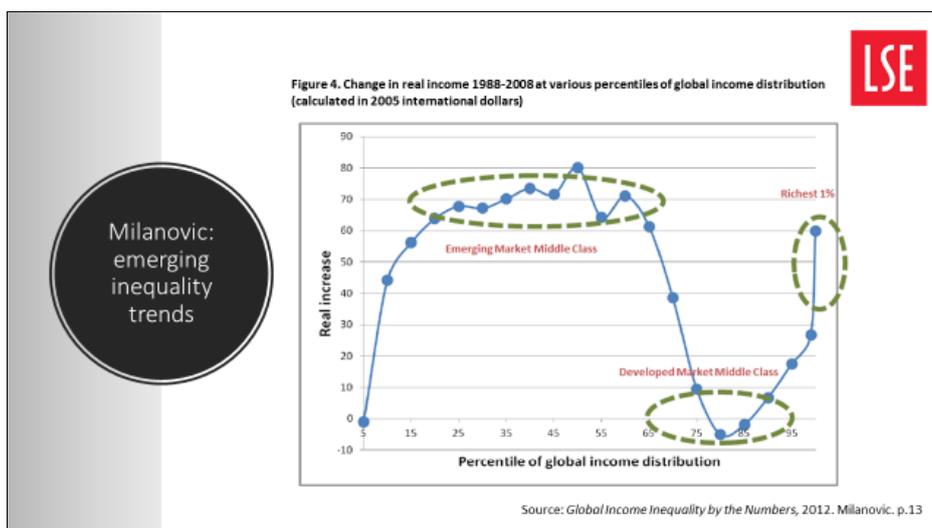


Figure 4: Milanovic, emerging inequality trends

Inequality

Let me turn to the structural forces. Globalisation is often blamed for rising inequality within countries alongside convergence between countries. The middle class in emerging markets and the richest 1% have benefited enormously while the middle class in the advanced economies have suffered. Through a combination of technological change and competition, globalisation has driven down wages of lower skill workers in advanced economies.

Inequality also makes people less generous and tolerant. More unequal societies seem to have lower social cohesion with less willingness to help others, lower levels of trust and lower civic engagement. Some of that spills over into anti-immigrant sentiment. Even though immigration expands the economic pie, it can be socially divisive if native populations do relatively less well. Debates about when immigrants should be eligible for welfare benefits are symptomatic – native populations are sharing their “citizenship premium” with others and want to have a say as to who should be eligible and after what length of time.

Austerity

Social safety nets are intended to cushion shocks over one’s lifetime and as the economy evolves. The effectiveness of tax and transfer policies in shielding citizens from the shock of the Great Recession varied greatly between countries and over time.⁹ Safety nets worked particularly well in the United States turning a 4% drop in market incomes into a 1% rise in disposable incomes. This 5% gain was achieved as a result of the Obama administration’s stimulus plan that transferred more than \$350 billion to households in the form of tax relief and assistance to workers affected by the downturn, including raising unemployment benefits and extending their duration. In France, the safety net raised median disposable income by three percentage points above median market income. In the United Kingdom, transfers fully offset the decline in market incomes as a result of the redistributive policies of the then Labour government.

⁹ McKinsey (2016), *Poorer than their Parents? Flat or Falling Incomes in Advanced Economies*, McKinsey Global Institute.

Of course, the cost of these redistributive policies (and the wider costs of bailing out the financial system) was a massive accumulation of debt in the post crisis period. Countries like the US, the UK, and Italy saw debt levels rise to around 100% of GDP. The need to bring debt down to sustainable levels resulted in austerity policies that had significant political and social consequences. While welfare states did their job initially, they were thinned out by austerity and many households fell through the safety net. Fetzer argues that in the UK, welfare cuts fell most on those parts of the country that ended up voting for the populist UK Independence Party and for Brexit.¹⁰ His econometric analysis of multiple elections leads him to the conclusion that austerity caused Brexit.¹¹

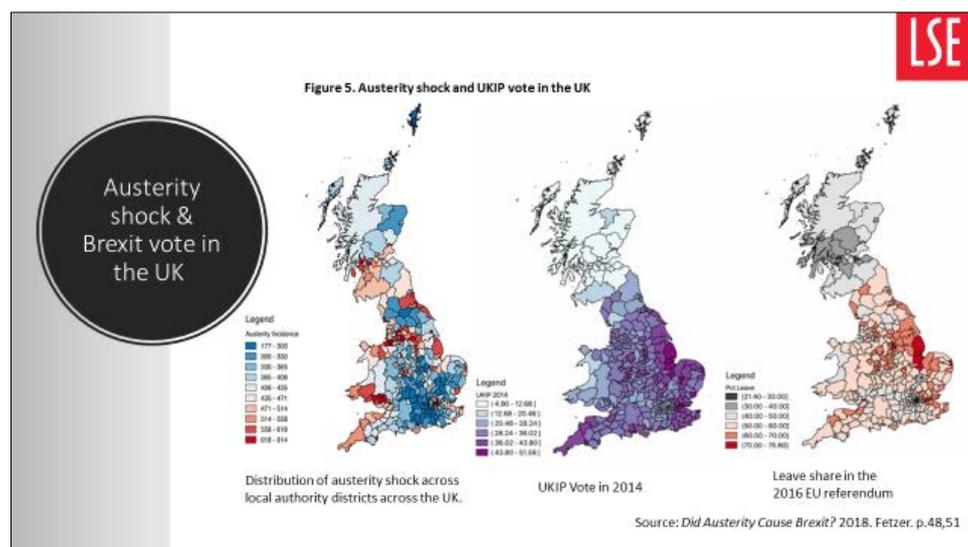


Figure 5: Austerity shock and Brexit vote in the UK

Identity Politics, Nationalism and Failing Democracies

Another manifestation of insecurity is the rise of identity politics, a reassertion of localism, national sovereignty and disaffection with democracy. Images of boats crossing the Mediterranean full of refugees and people illegally crossing the land border between the US and Mexico caused panic among many voters. That panic was rooted in the very large increase in immigration over the last decade in several countries. Despite the economic benefits of immigration which have been well documented,¹² the political and social impact was underestimated. This spilled over into support for populist and sometimes fascist parties across Europe and the US and an increase in racist incidents in many countries. Support for right wing populist parties increased in areas experiencing high levels of low skill immigration in countries like the US, Italy, Denmark and Austria.¹³

¹⁰ Fetzer (2018), "Did Austerity Cause Brexit?" Working Paper no. 381, Warwick University.

¹¹ A similar argument has been used to explain the rise of Nazism in Germany, although the historical circumstances are obviously very different. See Gaolfre-Vila, G., C.M. Meissner, M.McKee and D. Stuckler (2017) "Austerity and the Rise of the Nazi Party," NBER Working Paper No. 24106.

¹² See Goldin, Ian, Geoffrey Cameron and Meera Balarajan (2016) Exceptional people: How migration shaped our world and will define our future, Princeton: Princeton University Press.

¹³ Fetzer, T. (2018). *Did Austerity Cause Brexit?* (No. 7159). CESifo Working Paper, Warwick University.

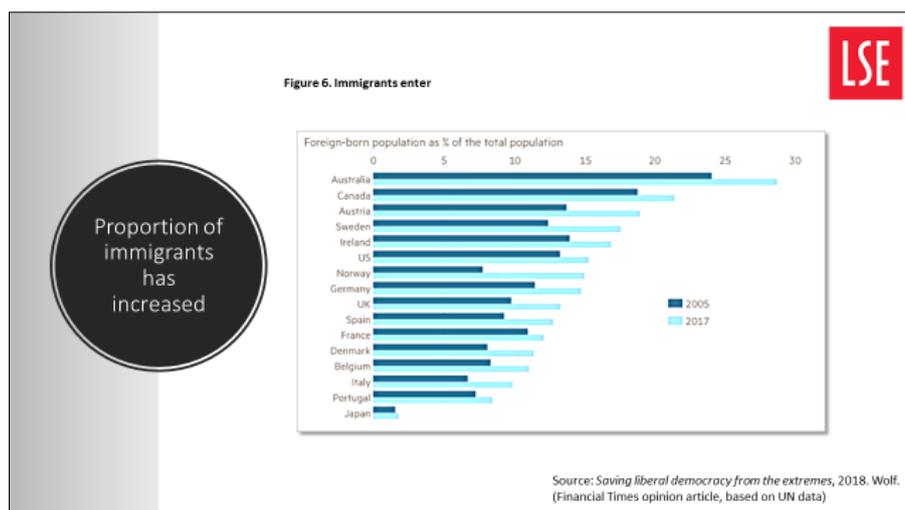


Figure 6: Proportion of immigrants has increased

The concerns about population growth are also rooted in very real challenges. While most countries in the Americas, Europe and Asia are facing the demographic challenge of ageing, most of Africa and parts of the Middle East will experience significant increases in population in the years ahead. Sub-Saharan Africa’s population of about 1 billion today will double by 2050 and could experience another doubling to 4 billion by 2100 according to the UN. That has been driven by major gains in reducing infant and child mortality with little reduction in birth rates – the average African woman still has 5 children on average. Promoting female education and access to contraception to accelerate the demographic transition is vital.

Concerns about loss of sovereignty and disaffection with democracy have grown as politics in many countries have become a combination of oligarchy and technocracy. The rich, powerful and those with special interests have disproportionate power over political outcomes. Voter turnout is falling in many countries and politicians are among the least trusted groups in most countries. Democracies have also been hollowed out by the rise of the technocracy (central banks, regulatory agencies, international treaties) and by growth in lobbying. All of these have reduced the impact of citizens on policy making.¹⁴

When I first came to the LSE and tried to understand management in universities, I asked “Where does the power lie?” And I was told “where you are not.” Citizens in democracies today often feel that way. People sense that power is elsewhere – in global markets, in distant institutions known by acronyms (many of which I have worked in), in political process dominated by vested interests, in technocracies. Citizens have lost the sense that they can shape their own destinies.

Fear of Future Prospects

When people fear the future, they find little comfort in the fact that they are doing better than their ancestors did in the past. Those fears are grounded not just in current experience of low wages and precarious work, but also in the impact that technology will have on future jobs.

¹⁴ Mounk, Yascha (2018), *The People vs. Democracy: Why Our Freedom is in Danger and How to Save It*, Harvard: Harvard University Press, p. 92.

We know that about half of jobs that are routine and repetitive are likely to be automated.¹⁵ McKinsey estimate that around 15% of the global workforce (about 400 million workers) could be displaced between 2016-2030. Fear of automation is, however, already having political consequences.¹⁶ Delsman finds 21 of the 22 states most prone to automation voted for Trump while 15 out of 15 states least prone to automation voted for Hilary Clinton.¹⁷ There is also a risk of further bifurcation of labour markets with automation. The US Bureau of Labour Statistics predicts that for every new highly paid job in software development, there will be 6 new low paid jobs in the care sector.¹⁸

Compounding the anxiety about automation is the rise of precarious work at low wages with no or minimal benefits. While some find great advantages in these more flexible work arrangements, others experience serious economic insecurity. Many young people on such temporary contracts face a period of “prolonged adolescence” in which they are unable to accumulate the wealth required to own a home or secure a pension. Precarious employment reduces both physical and mental health as individuals lose a sense of agency over their own lives.¹⁹ So even though we live in a world of unprecedented peace and prosperity, many people look to the future with trepidation and fear.

A New Social Contract

There are many aspects to why we are so miserable – misperceptions fuelled by the media, inequality, austerity, identity politics, disillusionment with democracy, and fears about the future because of structural changes in demography and technology. The response, I would argue, is that we need to provide citizens with a greater sense of security and better future prospects which is embodied in the social contract. Any new contract that is struck will vary across societies since this is fundamentally values driven. In every society there is a division of responsibilities between families, the voluntary sector, the market and the state. It is that sharing of responsibilities we need to renegotiate in light of new economic realities. In this final section of my talk I would like to highlight some of the possible policies we could consider.

A Fairer Economy

A key element of a new social contract is a fairer economy. There is much talk about the problem of inequality and very little action. In the medium term, what are often called “pre-distribution policies” are key – education and skills, social mobility, infrastructure investments in poorer regions, spreading productivity improvements to the frontier.

But in the near term, it is essential that we do more to address inequality through some degree of redistribution. Tax reforms in OECD countries in the 1980s and 1990s have lowered top personal income tax rates and corporate tax rates while raising VAT – all of which have reduced the progressivity of our tax systems. This is especially problematic given that labour markets were already generating greater inequality in market incomes. Given that wealth

¹⁵ McKinsey(2017), “A future that works: Automation employment and productivity”, McKinsey Global Institute, January

¹⁶ Mounk; Kolko study on “Trump was stronger where economy was weaker”. The People vs. Democracy: Why Our Freedom is in Danger and How to Save It, Harvard: Harvard University Press. p 158

¹⁷ Delsman, Ben, “Automation and Populist Vote Share,” forthcoming cited in Mounk (2018) p. 158.

¹⁸ Turner, Adair (2018), “Capitalism in the Age of Robots: Work, Income and Wealth in the 21st Century,” lecture at the School of Advanced Studies, Johns Hopkins University, April, exhibit 4 and 13.

¹⁹ Sverke, Magnus, Johnny Hellgren, and Katharina Naswall (2002), “No Security: A Meta-Analysis and Review of Job Insecurity and Its Consequences,” Journal of Occupational Health Psychology, volume 7, no. 3.

inequality has grown even more unequal than income, it seems inevitable that we need to explore taxing wealth such as inheritance, land and real estate. Recent research from the IMF shows that greater equality is good for economic growth, so such reforms may also help restore sluggish growth rates in many countries.²⁰

We also need to find ways to put a floor on people's incomes to make sure all can enjoy a reasonable standard of living even if they earn low market wages. I am not a proponent of universal basic income except in poor countries who lack the capacity to manage a welfare state or where it is substituting for an even worse policy, like energy subsidies. Universal basic income is expensive (about 6% of GDP for most advanced economies) and inferior to a properly functioning welfare state.²¹ It risks undermining the social contract that those who are able to work should contribute and does not take adequate account of the importance of meaningful work to well-being. Instead, wage subsidies, earned income tax credits, or higher minimum wages are better solutions combined with access to public services such as education, health, and other public goods.

We also need to find a way to redress the massive shift in global income in favour of capital and away from labour. For example, labour is taxed heavily (such as through payroll taxes) while capital is often taxed at a lower rate or subsidised through various incentives. There are issues of international tax competition that make this complicated. But we have made some progress in reducing tax base erosion and profit shifting by multinationals under the OECD's auspices²². It would be worth investing more effort to make sure that taxation of capital occurs where the economic activity actually takes place rather than in havens and through various "tax efficient" structures. Such changes would go a long way in restoring a sense of fairness in the world economy.

In response to automation, we should think more creatively about work hours. Since the 19th century, hours worked have declined steadily from about 70 hours per week to the current convention of 40 hours. As countries get richer, they tend to work fewer hours. This trend seems likely to continue as parts of jobs are automated. It will be important to use the productivity gains to eliminate aspects of jobs that are routine and repetitive (and bad for well-being) and substitute them for more meaningful work and leisure.²³ Making benefits portable and adjusting them pro-rata to hours will help people in work keep a sense of security in an era of automation.

²⁰ Ostry, M. J. D., Berg, M. A., & Tsangarides, M. C. G. (2014). "Redistribution, inequality, and growth," International Monetary Fund, discussion paper, February.

²¹ International Monetary Fund. (2017). Tackling Inequality. *IMF Fiscal Monitor*, Washington D.C. October.

²² Kudrle, R. T. (2014). "The OECD and the international tax regime: Persistence pays off," *Journal of Comparative Policy Analysis: Research and Practice*, 16(3), 201-215.

²³ The danger is that the time liberated is used for what Adair Turner calls "zero sum activities" or what David Graeber calls "bullshit jobs." See Turner (2018) and Graeber (2018).

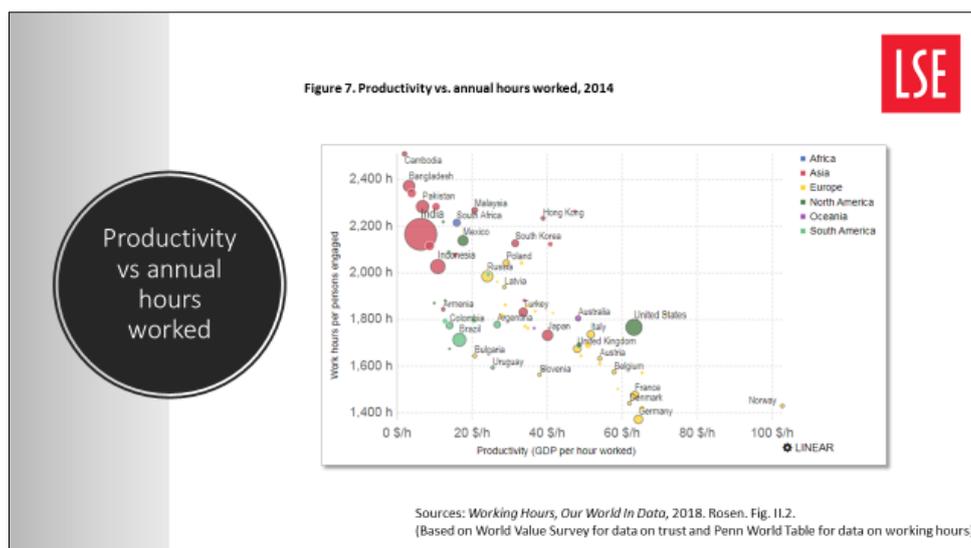


Figure 7: Productivity vs. annual hours worked

Rethinking our safety nets

Welfare states exist to pool risks and offset to some extent the impact of luck on life chances. None of us know what family we will be born into, what accidents or genetic surprises may affect our health, what misfortune may befall our children. To create a just society that deals fairly with such surprises and the fact that our needs and incomes vary enormously over the lifecycle, we create insurance mechanisms to share these risks. This also serves to insure the equal standing of all citizens so that they can participate fully in public life.

Who do we feel obligations to take care of and share risks with? How wide can that circle be drawn? These questions have become more complicated in less homogenous and globalised societies. How much do obligations go beyond families to communities or other regions? What about poor people in other parts of the world? What responsibilities sit alongside those obligations? Are we obliged to leave future generations at least an equivalent endowment of physical, social and natural capital as we were given?

Since we can anticipate dislocation in labour markets with automation, we should make it easy for firms to hire and fire workers as the economy changes but then provide workers with generous unemployment benefits, training and job placements so they are better supported and can adjust. “Flexicurity,” as it is called in Denmark, is just such a system but relies on firms being willing to pay higher taxes and to engage with social partners on skill needs in exchange for more flexible employment rules.

We also need to reverse the decline in social mobility we have seen in many countries. Research at LSE shows that countries with higher social mobility grow faster because they more effectively match people to the right jobs, generating higher productivity.²⁴ Research for the US shows that the best thing you could do to raise innovation and productivity is to provide opportunity to the “Lost Einsteins” who are disadvantaged by circumstances of their

²⁴ Western countries with higher social mobility grew on average 2.43% annually as against 1.77% for low mobility countries. Hassler and Rodriguez-Mora, “IQ, Social mobility and growth,” CEPR Discussion Paper Series No. 1827, March 1998.

birth.²⁵ Greater investment in equalising education opportunities and outcomes would have a high payoff and enhance citizen's confidence in the fairness of the system.

We also need to address issues of intergenerational fairness.²⁶ For example, the UK already spends more on the old than the young. Old people vote and are very effective at protecting their interests – young people should do the same. But older people need to care, not just about our own children and grandchildren (who they can support with bequests), but about others' too since they will inhabit the same society. One mechanism for redressing this intergenerational issue is to give every young person an entitlement which they can use to invest in their skills over the course of their lifetime.²⁷ This would provide a mechanism for a new social contract between generations that invests in young people which would be paid back in higher taxes in future that will contribute for caring for the elderly.

We may also need to reinstate the reciprocity and insurance element in welfare provision as part of a renewal of the social contract. There is a toxic perception that there are “hard working people” and “welfare scroungers” when in fact, as John Hills at LSE has shown, the vast majority take out (in the form of education, health care and pensions) broadly as much as they put in (in taxation when they are working) over the course of their lifetimes. The rich pay more tax, but tend to live longer so get more in pensions and health care in old age. Means-testing of benefits has exacerbated these misperceptions.

Perhaps we need to revisit the political and social advantages of universal benefits which are better for getting political buy-in and ensuring quality. The founder of the welfare state, William Beveridge (my predecessor as Director of LSE) intended the welfare state to be based on the concept of universal social insurance. That link was lost as it increasingly was funded through general taxation and some citizens opted out through private provision. Titmuss, once said that “Separate discriminatory services for poor people have always tended to be poor quality services.” Keeping the middle class engaged with public services sustains a sense of mutual obligation and keeps pressure to maintain service standards

Positive patriotism, renewed democracies

Questions of who is a citizen and what nationalism means merit a wider discussion. Nationalism has been taken over by populist and reactionary forces crowding out more inclusive interpretations. Yet nationalism is the foundation of self-determination and the social solidarity necessary to build a welfare state. The historian of nationalism Ernest Gellner once said that nationalism is like an “inverted refrigerator.”²⁸ Conventional refrigerators generate cold on the inside and emit heat on the outside; with nationalism, in order to create warmth within it is necessary to generate some cold without.

We need to find ways to foster a more inclusive nationalism that is based, not on race or religion, but on shared identities. Nations are “imagined communities” and those feelings have to be fostered and nourished.²⁹ There are many positive examples – the World Cup, the recent Royal Wedding, the London Olympic opening ceremony with its quirky celebration of the NHS. One of my favourite examples is the Great British Bake Off which brings together

²⁵ Van Rensselaer, John (2018), “Lost Einsteins: Who Becomes an Inventor in America?,” Centre for Economic Performance, London School of Economics, 2018.

²⁶ Climate change is a huge intergenerational equity issue but I will not address it here given my scope is already large.

²⁷ Shafiq, N (2018), “Universities alone can't fix the UK's skills deficit,” *Financial Times*, 5th September 2018.

²⁸ Gellner, E. (2008). *Nations and Nationalism*, Ithaca: Cornell University Press.

²⁹ Anderson, B. (1983). *Imagined communities: Reflections on the Growth and Spread of Nationalism*. New York and London: Verso.

participants from hugely diverse backgrounds united by the desire to bake the best Victoria sponge. And while these are positive examples, they are distinctive and have just enough “coldness” in them to unify (Victoria sponge is not mille feuille!).

Renewing democracies such that citizens feel they have a real say necessitates disempowering others who currently dominate the process disproportionately. That requires reducing the influence of money on politics and giving fewer opportunities for vested interests to shape policy. Much has been said about the problem of professionalization of politics but one consequence is that when the public do not identify with politicians, they will turn elsewhere. We also need to better align “technocracy” and democracy by introducing more accountability and perhaps rethinking which decisions are best suited to expert versus political decision making.³⁰

Restoring confidence in the future – work and well-being

In order to have a successful transition to automated and digital economies, governments and businesses must facilitate the mobility of workers to new jobs. But for this to be successful, workers need to be guaranteed a fair share of the benefits from this transition. Mechanisms to give workers more bargaining power, the use of profit sharing and more cooperative production structures are ways to accelerate the transition – otherwise those being left behind will keep voting for policies such as restrictions on trade or labour mobility that thwart modernisation of the economy.³¹

We know we have a major transition ahead in labour markets and it is necessary to prepare. Unfortunately, spending on worker education and training has been declining across OECD countries. Firms have fewer incentives to invest in workers who turn over more often. Public spending on facilitating worker transition and dislocation assistance is also shrinking as share of GDP across the OECD. Denmark, which is characterised by low unemployment and ranks top of the happiness scale, is the only country I am aware of that spends significant sums (1.7% of GDP) on “workfare” that focuses on empowering and reskilling their workforce considering.

Ageing means everyone who is fit will have to work longer and re-tool several times in their careers. Abolishing retirement ages and removing age limits for student loans (as has happened in the US and UK) are a good start. Linking eligibility for pensions to life expectancy as has been done in the Netherlands is an even better step. Giving part-time and temporary workers (who tend to be lower skilled and paid) more rights to pensions, paid leave and training as has been a positive reform in countries like Denmark, Germany and the Netherlands. Extending benefits to contract or short-term workers is also part of the solution.³²

Concluding Thoughts

Why are so many people feeling insecure? Because not everyone has shared in the material gains of recent decades, we are worried about the future and we have underinvested in the

³⁰ Tucker, Paul. (2018). Unelected Power: The Quest for Legitimacy in Central Banking and the Regulatory State, Princeton University Press.

³¹ For an interesting theoretical model that explains these dynamics, see Estache, A. and R. Foucart (2018), “On the Political Economy of Industrial, Labor and Social Reforms as Complements,” ECARES working paper 2018-13, Université Libre de Bruxelles.

³² Matthew Taylor (2017), “Good work: the Taylor review of modern working practices”, Department of Business, Energy and Industrial Strategy, UK Government.

mechanisms that help people adjust to new realities. We have also lost a sense connection in our democracies and in our nations. Behavioural psychology tells us that humans give greater weight to losses than to gains of equivalent size.³³ Even though we are better off materially in the aggregate, is what we have lost worth more to us? Is the loss of community and social cohesion worth more than gains in economic growth?

This is where I think economists need a bit of humility. Too often we worship at the altar of efficiency. In some areas of policy, it may be best to tolerate a bit of inefficiency for the sake of political and social cohesion. This “inefficiency” can take many forms – a more gradual pace of trade liberalization, phasing in immigration to allow absorption capacity to be built, investing in declining regions even when the returns might be higher in mega-cities, subsidizing unproductive workers because employment per se has wider social benefits. And while economists can quantify these trade-offs, it is the job of politics to make these choices.

We know that populists do not have the answers to the big questions we face – going back to the past is never possible. We need new ideas and we need them soon. I have argued that the new ideas fit under the banner of a new social contract. The social contract is around how we pool our resources to get public goods we agree together – and defining who is a citizen and how much responsibility we have for each other as citizens. We also need to find ways to do this internationally since many of the challenges we face – such as climate change, pandemics, cybersecurity – will require a new global social contract to solve.

Although daunting, I am also encouraged by the role universities can play in fostering this new social contract. Research shows that education is the answer to many of these challenges – in addition to providing skills for the future to support economic growth, education is good for health, social cohesion, democracy, and trust. I draw some hope from the fact that the latest Edelman trust barometer reports that there has been a resurgence of trust in experts and academics who are now the most trusted institutions in the world.

At LSE, we are busy doing our part to shape the social contract. Tim Besley is leading some thinking about the social contract under the banner of “Beveridge 2.0.” Our new Health Policy Department is leading a Commission with the Lancet on the future of the NHS. Our Media Department has launched a Commission on Truth, Trust and Technology. The Centre for Economic Performance has an active research programme on the future of work. Our Centre for the Analysis of Social Exclusion is working with the IMF to rethink welfare states around the world. What a great time to be a social scientist and what a wonderful time for Leverhulme to be in a position to support such important work.

A new social contract that we build together, can be the basis for this being the best of all possible worlds and for everyone to feel that we have the best of all possible futures ahead of us.

³³ Novemsky, N., & Kahneman, D. (2005). “The boundaries of loss aversion”. *Journal of Marketing Research*, 42(2), 119-128.