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Erik Canton

A Social Contract for the New Growth Agenda: The Role of Trust

The new growth agenda in the EU places stronger emphasis on well-being, inclusiveness and sustainability. These are complex societal challenges that can only be addressed through a more active policy stance. Countries with strong social contracts are in the best position to do so. This article investigates the role of reciprocity to elicit cooperative behaviour and to gain popular support for a social contract between the state and its citizens. Social contracts require trustworthy public institutions. However, trust levels among citizens vary widely across EU countries. Citizens' trust in authorities can, *inter alia*, be eroded by a malfunctioning government. Low levels of trust make it more difficult to invoke reciprocity and progress on the new growth agenda.

Economic growth and beyond

While economic growth is still a central policy objective, the EU's new growth agenda also emphasises other crucial objectives to measure the performance of welfare states, such as inclusiveness, sustainability, resilience, open strategic autonomy and preparedness (see, for example, European Commission (2022a) and the May 2023 conference¹ organised by the European Parliament on beyond growth). Whereas there is a lively discussion on measurement issues as regards this new growth agenda (as witnessed by a proliferation of dashboards and scoreboards to monitor and compare performance according to the latest narrative), there is less attention paid to the fundamental question of whether welfare states are capable of organising the necessary collective action for achieving these broader objectives. Indeed, the adaptation of our welfare states in light of the expanding set of

policy objectives likely calls for more, rather than less, policy intervention (WEF, 2021; Ghosh, 2022), requiring a stronger political mandate. A series of rather drastic reforms of labour markets, tax, pension and social security systems, product markets, research and innovation systems, education and training systems, public administrations, and international trade systems would be needed to achieve these objectives.

Let us, for example, look at inclusiveness. There is an increased attention to income (and wealth) inequality, not only in national debates but also in international organisations. The European Commission's monitoring of structural reform progress in EU countries through the annual cycle of economic policy coordination (the European Semester) includes an analysis of inequality developments in the country reports, and the International Monetary Fund and the Organisation for Economic Co-operation and Development (OECD) are also intensifying their work on inequality. There can be various reasons for this renewed attention, e.g. the popular interest in the topic spurred by Thomas Piketty and Mariana Mazzucato, evidence that the benefits from economic growth are spread unevenly among the population, the rise of populism, trends such as skill-biased technological change and globalisation, and new empirical work on the relationship between income inequality and economic performance.²

Traditionally, welfare states are classified in terms of their position in the inequality-efficiency landscape. The common (somewhat caricatural) conjecture is that there exists an inequality-efficiency trade-off, where the US have opted for a combination of high efficiency and high inequality, whereas European welfare models feature lower efficiency and lower inequality.³ There is indeed evidence of a "transatlantic divide" in the sense that the US takes a

¹ For more information, see <https://www.beyond-growth-2023.eu/>.

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* The views expressed in this article are those of the author and not necessarily those of the European Commission.

² For example, Teichgraber and Van Reenen (2022) talk about the "lost Einsteins" and "lost Marie Curies" because of discriminatory barriers to talented people becoming inventors, which are detrimental to both equality and economic growth.

³ Several explanations for the relative generosity of European welfare states vis-à-vis the US have been proposed in the literature. Alesina et al. (2001) attribute the differences to the result of racial heterogeneity in the US. Redistribution to the poor, who are disproportionately black, is unappealing to many voters due to racial animosity. In European countries socialist parties have more political power. Bénabou and Tirole (2006) link it to beliefs in the long-run rewards of effort, where their model's "American" equilibrium is characterised by a high prevalence of just-world beliefs and a laissez-faire public policy, whereas the other, "European", equilibrium features more pessimism, a more extensive welfare state and lower income.

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different position in the equity-efficiency landscape than European countries. Such a trade-off may exist, for example, when the tax system to support income redistribution weakens the financial incentives for workers and entrepreneurs. However, in the policy debate it is often emphasised that there are complementarities between equity and efficiency, and that these complementarities are a key feature of European welfare states. This is expressed in the agenda of the European Commission, in particular in the priority “An economy that works for people; Ensuring social fairness and prosperity”. The narrative here is that individuals and businesses in the EU can only thrive if the economy works for them. This priority also mentions that the EU’s unique social market economy allows economies to grow and to reduce poverty and inequality, thus pointing at complementarities between the objectives of equity and efficiency.⁴

At the same time, European countries show large diversity in achieved equity-efficiency combinations (sometimes referred to as social diversity). The Nordic and Continental welfare model has relatively efficient public administrations, high equity, provision of high-quality public goods and services (such as education and health), high levels of trust to support the social contract, and high well-being. Mediterranean and Central and Eastern European welfare states are more likely to cope with less efficient public administrations, lower equity, weaker public service provision, lower levels of trust, and lower well-being.⁵ One thus cannot speak about *the* European social model. The more advanced welfare states all have an important role for the government, where citizens are generally supportive of the idea of a social contract, and public administrations are functioning relatively well.⁶

The aim of this contribution is to investigate a society’s capacity to build and maintain a social contract, with a dive into human behaviour and its interaction with the trust-enhancing or trust-reducing institutional environment.

4 For more information, see https://commission.europa.eu/strategy-and-policy/priorities-2019-2024/economy-works-people_en.

5 See, for example, Marozzi (2015), who reports that citizens in Denmark, Norway and Finland have the highest trust in public institutions, whereas in former communist, Iberian and Mediterranean countries the population is much less trustful.

6 Evaluation of the performance of welfare states could be based, for example, on subjective welfare measurement, such as the well-being of EU citizens coming from the EU-SILC data collections. The average life satisfaction was consistently at the higher end of the scale in Austria, Finland, the Netherlands, Sweden, Denmark, Luxembourg and Ireland. For Bulgaria, Hungary, Latvia, Cyprus, Croatia, Greece, Portugal and Lithuania, the results were consistently at the other end of the scale.

Social contracts

A social contract is an implicit agreement among the members of a society to cooperate for social benefits, for example by sacrificing some individual freedom for state protection. Such a social contract is based on the notion of fairness, and assumes some form of reciprocity in the population to get a political mandate; for example, Fong et al. (2006) make a case that people support the welfare state because it conforms to norms of reciprocity and they reject the widely accepted median voter model to study redistribution.

A considerable part of the population shows reciprocal behaviour. From the behavioural economics literature, going back to e.g. Akerlof (1982) and Frank (1987), we know that people tend to cooperate voluntarily. Reciprocity is a response to friendly actions even if no material compensation is offered, and it differs from cooperative behaviour in repeated interactions induced by the prospect of future benefits (Fehr and Gächter, 2000) and intrinsic motivation (Canton, 2005). Reciprocity is closely linked to fairness.⁷ According to Fehr and Gächter (2000, 159-160), “reciprocity means that in response to friendly actions, people are frequently much nicer and much more cooperative than predicted by the self-interest model” and “the power to enhance collective actions ... is probably one of the most important consequences of reciprocity.”

Reciprocity is essential to generate democratic support for the welfare state, based on a social contract. Reciprocity is, however, a *conditional* kindness, and this article explores mechanisms through which voluntary cooperation is put at risk. Indeed, the conditionality attached to reciprocal behaviour underlines the importance of studying its interaction with the economic environment and institutional framework.

Trust and the importance of trustworthy public institutions

The thought experiment developed in this article is that in a high-trust environment, social contracts based on reciprocity can emerge, welfare states can thrive, and reciprocal behaviour enhances voluntary cooperation. In a low-trust environment, it is unlikely that the social contract will receive popular support.

In their impressive work on measuring preferences, Falk et al. (2015) find a grouping of positively correlated traits

7 Expressions with similar meaning include “quid pro quo”, “a favour for a favour”, “tit for tat”, and “you scratch my back, and I’ll scratch yours”.

Table 1
Pairwise correlations between preferences at the country level, global evidence

	Positive reciprocity	Negative reciprocity	Altruism	Trust
Positive reciprocity	1			
Negative reciprocity	-0.154	1		
Altruism	0.711***	-0.132	1	
Trust	0.363***	0.160	0.272**	1

Notes: Reported coefficients are pairwise Pearson correlations between average preferences. * $p < 0.10$, ** $p < 0.05$, *** $p < 0.01$.

Source: Falk et al. (2015).

involving pro-sociality, namely positive reciprocity, altruism and trust. Table 1 reports the pairwise correlations.

According to Falk et al. (2015, 15), “it is hard to imagine stable and high levels of trust in environments absent positive reciprocity, i.e. trust rewarding behaviors.” The role of trust links naturally with reciprocity, as expressed, for example, during general elections. Recalling that reciprocity is a form of conditional cooperative behaviour, such support will depend on citizens’ trust in the capacity of the government to implement and maintain the social contract.

Trust in hierarchy more generally is contested when bureaucracies malfunction. To recall, reciprocity is about conditional kindness. Societies in which individuals attach normative properties to the collectively enforced social arrangements manage to introduce and sustain a social contract (see, for example, D’Agostino et al., 2011). This social contract thus enables the development of a welfare state reminiscent of the ones in the Netherlands, Denmark and Sweden. According to Falk et al. (2015), individuals in northwestern Europe are more social. This social attitude can be connected with the normative property of collective action. When collective action has normative properties, individuals are more inclined to support this collective action and are more likely to report a social attitude. A consequence of this claim is that governments are themselves responsible for pro-social attitudes in society. When these normative properties become the subject of debate, popular support for the social contract may diminish and public action becomes more difficult to organise.

An implication would be that governments must be careful to invoke the principles of reciprocity and mutual obligations in the design of the welfare state, for example by attaching conditionality to be eligible for social security

such as the search effort to find another job (van der Ploeg, 2004). Flaws in the design of the collective arrangements are costly to society (moral hazard) and undermine reciprocity-induced popular support for the social contract.

Another example of costly bureaucracy would be related to the incidence of corruption.⁸ Corruptive practices such as government officials accepting bribes in return for granting certain benefits to citizens are not only costly in terms of the waste of public resources, but also corrode the above-mentioned normative properties of collective action and trust in public institutions. Indeed, social arrangements may never be introduced when a country suffers from the presence of extractive political institutions (in the terminology of Acemoglu and Robinson, 2012). As Rothstein (2010, 20) puts it: “countries tend to cluster so that countries with large and mostly universal welfare state programs also have low levels of corruption, a high degree of social trust, and high levels of happiness and social well-being. And vice versa, why countries with smaller welfare systems tend to be higher on corruption, have lower levels of social trust, and lower levels of social well-being.”

An environment suffering from corruptive practices is clearly short of the necessary checks and balances to make institutions trustworthy. Hardin (2002) defines trust in terms of “encapsulated interest”: person A trusts person B because person A knows that person B has the interest of person A at heart to some extent. Therefore, according to Hardin, trust must be cognitive (it requires knowledge about other persons’ trustworthiness) and relational (it refers to trust in a specific person). Trustworthiness is thereby not an inherent personal property, as person A could trust person B, while person C may not trust person B. The interpersonal aspect implies that one cannot have trust in institutions, since we cannot possibly know all the people in these institutions. Hardin refers in this context to quasi-trust, i.e. when there are checks and balances that either mimic or substitute for trust (such as a critical and independent press, an effective and efficient justice system, professional societies, an active Ombudsman). People finding out about each other’s trustworthiness create a network, ultimately generating social capital.

Vertical and horizontal trust

The literature distinguishes between vertical and horizontal trust. Vertical trust refers to trust of citizens in the hier-

⁸ Corruption is defined as the misuse of public office for private gain (Becker and Stigler, 1974). There is also a literature on corruption, trust and economic growth (see for example Serritzlew et al. (2014) for a review).

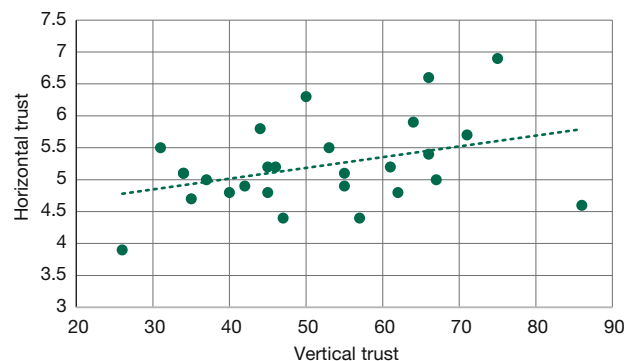
archy (e.g. their employer, public and political institutions), while horizontal trust is about trust in fellow citizens. Popular support for the social contract breaks down when vertical or horizontal trust is diminished. This could be the case when public officials or politicians engage in corruptive practices (reducing vertical trust). Popular support for the social contract can also be at risk, for example, when social security provisions are (widely) abused (reducing horizontal trust). Horizontal trust can only emerge in the presence of vertical trust (Rothstein and Eek, 2006).

This empirical finding of a causal relationship from vertical to horizontal trust, but not vice versa, places special emphasis on the importance of trustworthy public institutions. Reciprocity-driven popular support for a social contract becomes more difficult when trust in these institutions is fading away.

A recent Special Eurobarometer reports that trust in people (horizontal trust) varies across member states and is especially high in Denmark and Ireland (European Commission, 2023). A high level of trust in national public administrations (vertical trust) is observed for example in Luxembourg, Denmark and Finland (European Commission, 2022b). The Nordic countries are often mentioned as countries with high levels of trust, and the reasons for this have been extensively studied in the literature. For example, OECD (2021) reports that the high quality of public services in Finland is expected to contribute to high institutional trust, as these services are a tangible aspect of what people get in return for their tax payments.⁹ The police in Finland is the most trusted institution, which could be explained by high-quality education and continuous training for police officers, the perception of high ethical standards, and almost non-existent incidents of corruption involving police personnel. Denmark and Finland are the best-performing countries according to the Corruption Perception Index 2022 of Transparency International. On the other hand, countries where citizens have lower levels of trust in public institutions tend to be countries with more frequent incidences of corruption and weaker checks and balances. This can manifest itself in the form of political interference against independent media. Whereas trust levels in the Netherlands are generally high, vertical trust in the Netherlands has plummeted by 14 percentage points in the survey conducted in summer 2022 since the previous measurement in

⁹ This would illustrate the principle of reciprocity as a conditional kindness.

Figure 1
Correlation between horizontal and vertical trust in the EU



Notes: Each dot represents an EU country. Horizontal trust is measured by asking respondents to what extent they agree with the statement “You assume that people have only the best intentions” (on a scale from 0 to 10, where 0 means “does not describe you at all” and 10 means “describes you perfectly”). Vertical trust is measured by asking respondents how much trust they have in their public administration (% tend to trust).

Sources: European Commission (2022b) for vertical trust; European Commission (2023) for horizontal trust.

winter 2021-2022.¹⁰ This serves as a reminder that trust cannot be taken for granted and needs to be cherished and carefully maintained. Figure 1 shows the dispersion of these trust levels across EU countries, and the positive correlation between vertical and horizontal trust.

Policy implications

This article makes the point that progress on the new growth agenda in the EU can only be achieved if national governments manage to organise the mandate to do so, and this requires that their institutions be trustworthy. It has investigated the role of reciprocal behaviour in the

¹⁰ The Eurobarometer survey does not contain questions about the reasons behind the change in trust levels. Nonetheless, this reduction in vertical trust in the Netherlands is possibly related to the turmoil triggered by a number of political scandals, in particular the childcare benefits scandal (“toeslagenaffaire”) and the Groningen gas crisis. The childcare benefits scandal revealed false allegations of fraud made by the Tax and Customs Administration (with the use of discriminatory artificial intelligence algorithms), while attempting to regulate the distribution of childcare benefits. Many citizens encountered severe financial damage, and there were substantial delays in the provision of compensation. The Groningen gas crisis was related to problems in the implementation of compensation schemes for citizens who suffered from earthquakes and tremors linked to gas extraction in Groningen, causing substantial damage to buildings. The causality between the gas extraction and these earthquakes and tremors, as well as the causality between the earthquakes and tremors and the damage to the buildings has often been contested, which has led to delays in the phasing out of the extraction activities and in the roll-out of the support schemes. Interestingly, trust levels in the EU remained fairly stable in the Netherlands in the same period (a two percentage point drop in “tend to trust” from winter 2021-2022 to summer 2022).

organisation of collective action. The property of conditionality implies that reciprocal behaviour cannot be taken for granted, and positive reciprocity can turn into negative reciprocity (such as retaliation) when circumstances change. The somewhat inconvenient example would be dysfunctional bureaucracies and in particular the involvement of public officials in corruptive practices. This would put the trustworthiness of public institutions at stake and is likely to erode reciprocity-induced popular support of the social contract.

A more general conclusion that can be drawn is about reform sequencing. The existence of trustworthy public institutions is an essential condition for a country to advance the welfare state. Trustworthy public institutions help to foster popular acceptance of the social contract. Genuine efforts to restore or strengthen trust should therefore be on top of the reform agenda in countries where citizens have low levels of trust. Some of these reforms are relatively straightforward and not very costly. Others may take substantial time to bear fruit and be politically difficult to implement, because it is hard to give up vested interests and there are strong path dependencies in institutional settings.

For example, trustworthy institutions have systems of checks and balances in place, such as networks of experts providing independent advice (e.g. National Productivity Boards and advisory bodies on climate change for evidence-informed policymaking), an Ombudsman, protection of whistle-blowers, citizen engagement practices, and an open policy towards the press and the media. These checks and balances can be organised relatively quickly, though capacity and reputation building to act more effectively can take longer. Strong checks and balances help to discipline the public administration and can improve the quality of the political choices and implementation processes, thereby contributing to public institutions' trustworthiness.

More generally, trustworthiness is related to the quality of the institutional framework. Substantial work has been done on the quality of public administration and public governance (see, for example, European Commission, 2017; World Bank, 2022). This work identifies the conditions to be fulfilled for being a modern, democratic state, such as accountability, political stability and the absence of violence, government effectiveness, regulatory quality, rule of law, and the control of corruption.

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