Globalization and the Race to the Bottom in Developing Countries

Who Really Gets Hurt?

NITA RUDRA

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The advance of economic globalization has led many academics, policy-makers, and activists to warn that it leads to a "race to the bottom." In a world increasingly free of restrictions on trade and capital flows, developing nations that cut public services are risking detrimental effects to the populace. Conventional wisdom suggests that it is the poorer members of these societies who stand to lose the most from these pressures on welfare protections, but this new study argues for a more complex conceptualization of the subject. Nita Rudra demonstrates how and why domestic institutions in developing nations have historically ignored the social needs of the poor; globalization neither takes away nor advances what never existed in the first place. It has been the lower- and upper-middle classes who have benefited the most from welfare systems and, consequently, it is they who are most vulnerable to globalization's race to the bottom.

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For my parents, Sujit and Lina Rudra

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Preface

My interest in politics and globalization emerged in my adolescence during frequent visits to India. Time after time I saw that the immense scale of poverty and destitution remained the same. Life at home in the United States, on the other hand, seemingly held the promise of endless choices and opportunities for advancement. I was particularly struck by the stark contrast between the health care and resources available to my grandfather, a village doctor in one of the most remote and poorest "gramas" (villages) in West Bengal, and my father, an FRCS (Fellow of the Royal College of Surgeons) surgeon practicing in Florida. I was astounded that two such diametrically opposed economies coexisted in the same world. From here, eventually, questions of distribution, international economics, politics, government choices, and policy design emerged. In my early years of graduate school I became particularly intrigued by the extent to which domestic policy choices seemed constrained by the global economy, and thus fascinated with issues in international political economy. It took some further study and field experience to begin to grasp the true complexity of the situation.

This book is my attempt to scratch the surface of how and why developing and developed countries face such different challenges in (and responses to) the current era of globalization. It is a product of my struggles with understanding the distributional consequences of globalization, and questions of if and how developing country governments can respond to it. The pages that follow illustrate just one view of the dynamic interactions between domestic politics and globalization in emerging nations, and their implications. With this primary purpose in mind, I set out to observe the interplay between economic openness, domestic politics, and social welfare policies in developing nations. I contend that, in emerging economies, it is, in fact, the middle class, rather than the poor, who are the ones most directly affected by changes in government welfare policies occurring as a result of economic globalization. This outcome is fundamentally not, as most people think, the product of contemporary globalization but, rather, of particular domestic institutions that have existed at least since the post-war era. Based on these findings, I surmise that the less well off in developing countries do not have the same opportunities to protect themselves from the risks associated with the expansion of global markets (or domestic markets, for that matter) as they do in the advanced industrialized countries, *but* that this is contingent upon particular domestic institutions that pre-date the current era of market expansion. We therefore need not worry about how potential reductions in welfare state policies in response to globalization hurt the poor, because the poor were never the main beneficiaries of such policies in the first place.

My interest in international political economy and the politics of developing countries has been influenced by several people. My greatest academic debts go to John Odell, James Robinson, Benjamin Cohen, and Renu Khator. John Odell has been my mentor since graduate school. His high standards of excellence, his deep intellectual curiosity, and his emphasis on good research design, together with the generous flow of his professional and intellectual advice, have had a profound influence on me. He has since given insightful comments and feedback on everything that I have written. This book might not have been completed without his influence and guidance through the years. I am deeply indebted to James Robinson. The book would never have begun without him; with boundless patience, over endless cups of coffee, he vetoed every book project I suggested – except this one. It was Jim who had the foresight to encourage me to pursue research on international economics and domestic politics with a focus on the developing world. Since then he has been a constant source of support and inspiration. He frequently challenges me to think about my argument more carefully, and little is more satisfying than his approval of my work. He has been a steady source of academic guidance and kind friendship over the years. I also sincerely thank Benjamin Cohen, who always provides such thoughtful comments and responses to my work, no matter how busy he might be. Particularly when I was struggling with the direction of the book project during its initial phases, I benefited immensely from his willingness to engage in random conversations related to this research project. Finally, I am grateful to Renu Khator, my mentor through my Masters, who is now the chancellor and president of the University of Houston. Renu encouraged and inspired me to continue with political science, despite my perceived limitations at the time.

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for helping me craft the title. Dan Thomas deserves very special thanks for helping me kick-start the book process. It was through conversations with him that I finally found a clear direction for the analysis. He was always willing to help in any way that he could – and he did, on many different levels. My good friend and colleague Sebastian Saiegh willingly read and discussed everything I asked of him. I appreciate his critical comments and suggestions of broader literatures to consult. I am also grateful to David Bearce, who has been a great colleague and read through my chapters, patiently responding to any and all IPE-related questions. Irfan Nooruddin has been particularly helpful by graciously volunteering to read my chapters and providing valuable feedback. Sarah Brooks was very generous with her time, providing me with pages of comments on my Brazil chapter and helping me discipline my thoughts. I do not know if I was able to address all her queries and concerns successfully, but I do feel that my work is better for attempting to do so. Very special thanks go to Joseph Wong, who helped tremendously with the South Korea chapter, and who provided such insightful and thoughtful points. Ashutosh Varshney provided careful and critical comments on the Indian case study. Stephen Haggard and Robert Kaufman continuously encouraged me to pursue this topic and emphasized the important contribution it could make to the wider literature. Amy Wakeland challenged me to ask the critical questions: why is it important, and who cares? She carefully read and discussed my argument and encouraged me to think more broadly about political science. I would also like to thank Hayward Alker, Barry Ames, Michael Goodhart, William Keech, Layna Mosley, Peter Rosendorff, Samira Salem, Martin Staniland, and James Vreeland, who helped on various parts of the book and/or gave me constructive comments and suggestions.

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Friends and family provided a rich source of support while I worked on the book. I was extremely fortunate to have Cassandra Thomas diligently read (and reread) and edit every single chapter in this book. Her keen sense of logic and her insightful comments were instrumental in pushing me to sharpen the primary arguments in the book. She listened patiently as I struggled with my ideas, then provided me with her impressively well-thought-out feedback. It was Cassandra who provided invaluable advice on how best to organize my case studies. Vikram Mangalmurti never hesitated to dialogue with me about the project and was absolutely instrumental in making certain that the book could appeal to a wide audience. Lisa Snead has always been a solid source of support and unfailingly reminded me not to give up. I could always count on Anna Ruth Worten-Fritz to offer good sisterly advice and, most of all, emphasize the importance of having a good attitude. Pierre Laporte has been good-naturedly demanding the completion of the manuscript for years and was extremely helpful during my fieldwork in Brazil. Both through example and good advice, Eric Garcetti, Carmen Sardinas, Isabel Garcia, Kaarina Roberto, and Nupur Dashottar constantly reminded me of the importance of keeping things in perspective. I must give my brother, Krish Sundaram, the deepest thanks for having the wherewithal to withstand my book stress. He has been utterly unfailing in his support through all the trials and tribulations, as well as the sweet moments of breakthrough. Finally, I would like to recognize the important contribution of my second dad, John Ford, who passed away during the final stages of this book project. Days before his passing, the news that I had finished the book was one of the few things that brought a smile to his face. His amazing courage and attitude towards life, along with his enthusiasm for my project, filled me with the spirit I needed to finally finish.

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whatever was needed to research this topic. He never tired from encouraging me and pushing me forward, and I was internally motivated not only by his faith in me but by his commitment to the project itself. Alongside his own work, he spent endless hours perfecting the numerous figures and tables in this book. But, most importantly, he has given me the stamina to pursue my goals without hesitation.

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1 Introduction

> The [Anganwadi] workers are paid only Rs. 1,000 [$21] a month and their helpers Rs. 500 [$11]. There is no dearness allowance,[1] no paid leave, and they also do not have social security.[2]

Such is the plight of India's Anganwadi workers, a low-caste disadvantaged group of workers that assists poor mothers and children with health and nutrition needs.[3] After working more than eight hours a day, total earned wages keep them well below the international poverty line of $1 per day. Their persistent demands for higher wages, job security, and social security have yet to be met by the Indian government. The key to obtaining these protections, the workers argue, is to be recognized as government employees instead of part-time workers.

India's Anganwadi are not alone. In the current era of globalization[4] disadvantaged groups of workers receive minimal or no protection against market risk. Examples from around the world attest to the near-universal tenuous position of marginal workers. The *Korea Herald* reports that approximately 70 percent of non-standard South Korean workers receive no social insurance, as compared to 1.7 percent for standard workers.[5] Brazilian legislation that provides social insurance and job dismissal protection exempts at least 40 million informal workers, including domestic workers, shoemakers, garment workers, and slum dwellers. These workers have begun clamoring for the same rights to unemployment insurance,

[1] Dearness allowance is a cash payment to employees that takes inflation into account and is part of the total wage cost.

[2] Protestors from the Joint Platform of Action, as quoted in "Recognize Us as Government Staff: Anganwadi Workers," *The Hindu* (Madras), July 26, 2006.

[3] More specifically, workers in "Anganwadi" centers are affiliated with the government's Integrated Child Development Services and play a crucial role in providing childcare to the poor. They tend to the health and pre-school education needs of children up to age six, as well as assisting pregnant women, nursing mothers, and adolescent girls with various aspects of health and nutrition.

[4] "Globalization" is defined in this book as the expanding international economic integration of markets in goods, services, and capital.

[5] "Bipolarization in Labor Market – How to Solve It?" *Korea Herald*, August 27, 2004.

maternity leave, paid holidays, and other benefits long afforded other working Brazilians.[6] Half a world away, thousands of Bangladeshi textile workers have taken to the streets with similar demands. Ugandan textile, leather, garment, and allied workers have recently filed grievances with the International Textile, Garment and Leather Workers Federation (ITGLWF) complaining that the Ugandan government ignores both internationally known workers' rights and the benefits required by Ugandan legislation.[7] In Thailand, the Kasikorn Research Center (KRC) expresses concern that workers in the agricultural sector and those with independent jobs, such as barbers and hawkers, will suffer as economic growth slows, since they have no access to social insurance or job security.[8]

Globalization skeptics react predictably to these scenarios; they respond with the following mantra: globalization hurts the poor. Their reasoning is fairly simple. Less developed countries (LDCs) participate in highly competitive global markets. Governments must cater to domestic and international capital interests by cutting wages and benefits. This could lead to a "race to the bottom" (RTB). According to this hypothesis, a world increasingly free of restrictions on trade and capital flows allows investors to scour the globe in pursuit of the highest rate of returns. Nations that harbor public policies that raise production costs or inhibit sound macroeconomic fundamentals risk lower profit margins and capital flight. Fearing such reprisals, governments are constrained from initiating (or maintaining) policies that guarantee a higher quality of life for their citizens, such as safety nets, environmental standards, and acceptable labor costs and protections. The anticipated result is that domestic politics loses its vigor and the forces of global commerce trump efforts to pursue all other things important to society.

China's growing presence in the global economy raises the stakes in this race to the bottom for developing nations. Greider (2001), a journalist, encapsulates these fears:

> Globalization is entering a fateful new stage, in which the competitive perils intensify for the low-wage developing countries … In the "race to the bottom," China is defining the new bottom. But the killer question asked by critics, myself included, is whether China can fulfill its vast ambitions without smashing the dreams of other striving nations … Too many producers, too few consumers in a global system where too many workers cannot afford to buy the things they make – that's the central contradiction. The destructive qualities and repeated crises are sure to continue, critics would argue, so long as the system advances by this roving

6 "Maids Fight for Wages, Security," *Gazette* (Montreal), April 24, 2000.
7 "Can Ugandans Finally Afford to Smile?" *The Monitor* (Africa News), April 4, 2006.
8 "Unemployment to Rise due to Economic Slowdown in Thailand," *Xinhua General News Service* (China), May 7, 2006.

exploitation of labor and prevents developing countries from pursuing more balanced, albeit more gradual, strategies.

According to this logic, the rapid race to the bottom is what hurts disadvantaged groups such as India's Anganwadi, South Korea's non-standard workers, Brazil's domestic laborers, Bangladeshi garment workers, and others. The race to the bottom hypothesis anticipates that international market pressures determine domestic social policy, and that the downward institutional convergence of policies and practices, which precludes adequate welfare protections for the poor, is inevitable.

In light of these concerns, it is surprising that the great bulk of existing scholarly research on the globalization–welfare nexus has focused on the advanced industrialized nations, not the developing world. After all, if the race to the bottom hypothesis is true, citizens of developing countries would be particularly vulnerable, given these countries' intense need for capital and, thereby, far greater susceptibility to global market pressures. And yet we have very little knowledge of if, how, and to what extent these pressures are really affecting poorer countries.[9]

This book provides the first comprehensive study of the interactions between globalization and the race to the bottom, domestic politics, and welfare strategies in the developing world. *The central focus of this book is on the observable implications of international market expansion on LDC welfare state policies*. To what extent are governments in developing countries vulnerable to RTB pressures on welfare state policies? If such pressures exist, what, if anything, can governments do about it? Is globalization simply making it impossible to protect the most disadvantaged citizens from the risks and uncertainties of globalization? Are domestic institutions and politics increasingly irrelevant in the LDCs as institutional convergence (purportedly) commences?

This book challenges the conventional wisdoms surrounding the race to the bottom hypothesis. I argue that, unlike in the advanced industrialized countries, globalization does indeed trigger a race to the bottom in developing countries. The broader implications of this defy traditional expectations, however. Previous analyses of globalization and its consequences have generally failed to examine the impact of the character and content of long-standing LDC domestic institutional arrangements. This book contends that it is not globalization per se that ultimately determines the plight of the poor but, rather, the interplay between globalization and a nation's domestic institutions. More precisely, fragmented

[9] Murillo (2000, 2002) and Brooks (2005) are important exceptions who explore the interaction between international market integration, domestic politics, and social policies in Latin America. They do not, however, focus on the effects of RTB per se.

labor movements, the government–labor relationship, and pre-existing national social policy configurations are structuring responses to the challenges of globalization. The central thesis in this book is that these domestic institutions have long deprived the poor of social protections *and* that these institutions continue to persist in twenty-first-century globalization. In other words, where social institutions have historically failed to protect the very poor in developing countries, the advent of globalization has not altered national institutional dynamics.

In fact, the statistical analyses and case studies presented in this book demonstrate that, though the poor may be most in need of services, the actual consumers of welfare state services in developing nations tend to be somewhat wealthier citizens. Hence, the key paradox is that the RTB pressures hurt mainly the middle classes in developing countries, not the poor.[10] The damage to the middle class is not colossal, however; members of the former fight vigorously to defend the status quo, thus preventing major institutional change and thwarting predictions of convergence towards the "neoliberal bottom."[11] To be absolutely precise, the nature of ongoing welfare retrenchment in LDCs does not represent the race to the actual *bottom*; rather, *the retrenchment reflects the general downward pressure from globalization on middle-class benefits*. Preventing the uniform freefall of social welfare benefits to the bottom are the distinct institutional configurations of each respective nation. These institutions generate systematically different reactions stemming from their prevailing ethos, development legacies, and political constituencies. In fact, defying the predictions of globalization skeptics, none of the existing distribution regimes show signs of advancing towards a welfare state based on neoliberalism *or*, for that matter, the principles of universalism.[12] Even when select welfare regimes adopt, for example, comprehensive social insurance coverage, the exclusion of marginalized groups persists on a de facto basis.

[10] Note that this book is not investigating whether the middle class in developing countries are overall winners or losers with globalization. The focus is on who gets hurt specifically by welfare retrenchment in the current era.

[11] Mishra (1999) presents the conventional view of the "neoliberal bottom." He argues that international organizations such as the World Bank and the International Monetary Fund (IMF) have been selling policies associated with the neoliberal bottom to developing countries by focusing on limiting government expenditures, deregulation, selective social services, and the private provision of welfare. Extensive reliance on means-tested welfare programs (i.e. strict eligibility criteria apply: property or wealth cannot exceed a certain amount) is also commonly associated with the neoliberal bottom.

[12] A welfare state based on the principles of universalism allows every citizen access to welfare services; social welfare schemes involve the entire population and are not limited to a particular income group.

As a result, the current predicament of India's poor Anganwadi workers and similar groups across the globe cannot be blamed simply on the race to the bottom. The distribution regimes in each of these nations never actually provided them with safeguards from market risks, either before or after economic openness policies were adopted. Also impeding any movement towards a universal welfare state is the absence of a cohesive labor movement and, in many LDCs, a government–labor relationship that is supported by clientelism. These domestic institutions or absence thereof collectively hinder substantive pro-poor welfare policies.

India's Anganwadi workers are fighting for recognition as government employees precisely because government employees are among the core of workers entitled to the most generous welfare protections. Anganwadi workers have been denied access to the much-coveted benefits ever since their positions were created in 1975. Their current demands are thus as valid today as they were several decades ago, before India's turn towards open markets. The quintessential problem now is that, as Keohane and Milner (1996: 256) put it, the "pressure of constraints and the lure of opportunities" associated with globalization make it that much more challenging for their demands to be fulfilled.

1.1 Globalization and the race to the bottom debate: the fundamental concern

A distinct and recent rise in poverty and inequality in many developing countries coincides with the adoption of economic liberalization policies and heightened anxieties about the race to the bottom. The United Nations (UN, 2005) estimates that over 58.7 percent of workers in the developing world still live on less than the $2 a day poverty threshold, and 23.3 percent live in absolute poverty, or less than $1 a day. What is worse is that the numbers of those living in absolute poverty rose during the 1990s in all regions, with the exception of select countries in the Middle East and north Africa, and east Asia (World Bank, 2000b). Studies have shown that income inequality has also increased since the early 1980s (see, for example, Cornia, Addison, and Kiiski, 2004). These statistics reveal a dismal reality for developing nations, a reality that engenders grave disappointment after scores of economists and policy-makers promised a world of boundless prosperity and consumer satisfaction as the result of globalization policies.[13] It is no surprise, then, that high-level international gatherings aimed at promoting global market expansion,

[13] See Guillen (2001) for a discussion on this perspective.

such as the biannual World Bank/IMF meetings, the World Trade Organization (WTO) ministerial meetings, Group of Eight summits, the World Economic Forum, and the Free Trade Area of the Americas (FTAA) summits, have drawn swarms of protestors in recent times. Demonstrators are commonly seen holding placards reflecting their alarm about the race to the bottom: "Globalization hurts the poor."

Some concerns about globalization are warranted. Many scholars have observed a positive correlation between globalization and worsening conditions for the lower strata of society, both in an absolute and a relative sense. Trade and foreign direct investment (FDI) have been found to exacerbate inequality by changing the skill composition of labor demand and thereby fueling the wage gap between skilled and less skilled workers (Hanson and Harrison, 1999; Wood, 1997). In a related point, developing countries that liberalized their capital accounts have been susceptible to financial crises and, in turn, have experienced increases in poverty and inequality (Baldacci, de Mello, and Inchauste, 2002). It is evident, even to the most ardent globalization enthusiasts, that international market integration can have negative consequences on distribution.

The current debates, however, are not about the successful functioning or necessity of markets per se. Scholars and policy-makers across the ideological spectrum have come to accept markets as the preferred mode of resource allocation, and, with this, a truism: markets create both winners and losers.[14] Certainly, developing countries that have steadfastly embraced open markets have seen improvements in economic growth (see Edwards, 1998, and Sachs and Warner, 1995).[15] Growth is not necessarily synonymous with improvements in equity, however. International economic theories, such as the Stolper–Samuelson theorem and the Ricardo–Viner model, help us predict which factors or sectors are likely to gain or lose with globalization. Tensions rise as various interests, such as marginalized groups, skilled and unskilled workers, tradable and non-tradable sectors, mobile and fixed asset holders, private foreign creditors and foreign financial intermediaries, benefit unevenly from international market policies. Globalization pessimists do not want to replace the market system; they simply want governments to do something about the negative consequences it can yield.

[14] A recent survey by international polling firm GlobeScan, analyzed in conjunction with the Program on International Policy Attitudes (PIPA) (2006) of the University of Maryland, revealed a strong global consensus for free enterprise systems and free market economies as "the best system." Citizens of both developed and developing nations were polled, and, on average, 61 percent agreed, while 28 percent disagreed.

[15] For a dissenting view, see Rodrik and Rodriguez (2000), who argue that the link between openness and growth is still an open question.

The goal of governments, then, has been to manage these distributional conflicts to ensure social stability and domestic peace. Polanyi (1944) long ago stressed that social stability depends on the coordination of redistribution with market exchange. A long line of scholars since then have noted the vital importance of maintaining welfare states alongside global market integration. The occasion for welfare state policies in LDCs is particularly acute in the present era. Early twenty-first-century globalization is unique in the way that market expansion has involved the developing world. As Garrett (2000: 942) indicates, "Large-scale portfolio lending to banks in developing countries for purposes other than raw material extraction, two-way manufacturing trade between the north and the south, and complex multinational production regimes were simply unheard of a century ago." The inference here is that, as LDCs have become more and more integrated in global markets, welfare state development has become the key means to a "fair" distribution of wealth and social stability. Take, for instance, Chilean President Michele Bachelet's statement during a recent visit to the United States:

> The logic of the market does not resolve all problems … as I see it, you need strong and powerful social policies by the state to resolve the problems of income and equality of opportunity.[16]

Herein lies the root of anxieties about current globalization. A sizable body of scholarship in the 1980s and 1990s maintained that governments could no longer manage distributional conflicts via social welfare policies. If international market expansion leads to a race to the bottom and erodes the welfare state, the implication is that government autonomy and domestic policies are being sacrificed at the altar of international markets and laissez-faire. Governments simply cannot act contrary to market forces and protect the poor as deemed necessary, given limited policy-making flexibility. The RTB model thus makes the teleological inference that competition to attract mobile factors of production leads governments to deregulate competitively until, eventually, welfare policies throughout the world would converge on the "lowest common denominator." In short, RTB scholars scrutinize the loss of state sovereignty concomitant with globalization. Ohmae's (1995: 11–12) oft-cited work summarizes it best:

> [N]ation-states have *already* lost their role as meaningful units of participation in the global economy of today's borderless world … Reflexive twinges of sovereignty make the desired economic success impossible, because the global economy

[16] Larry Rohter, "Visit to US Isn't a First for Chile's First Female President," *New York Times*, June 8, 2006, Section A, Late edition.

punishes twinging countries by diverting investment and information elsewhere … [A]s the downward ratcheting logic of electoral politics has placed a death grip on their economies, they become – first and foremost – remarkably inefficient engines of wealth distribution … the nation state is increasingly a nostalgic fiction.

Such doomsday scenarios and fast-growing anti-globalization movements drew more and more academics into the discussion. Turning to sophisticated methodological tools, positivist approaches, and systematic data collection and analysis, scholars began to dissect critically the links between global market expansion and the welfare state. If the evidence reveals that welfare states are withstanding the forces of globalization, then national governments are still the core actors and domestic politics remain vibrant. If the findings reveal otherwise, however, Ohmae's predictions ring true.

The majority of investigations to date have focused on the political economies of the advanced capitalist countries. Within the last few years a distinct and well-respected group of scholars in international political economy (IPE) and comparative political economy (CPE) have successfully challenged the race to the bottom hypothesis in the nations of the Organisation for Economic Co-operation and Development (OECD) (e.g. Bearce, 2007; Iversen, 2005; Basinger and Hallerberg, 2004; Mosley, 2003; Pierson, 2001, 1994; Huber and Stephens, 2001; Swank, 2001; Hall and Soskice, 2001; Garrett, 1998).[17] The common finding is that, in the OECD countries, a race to the bottom is not leading to cross-country harmonization of policies and practices at the lowest regulatory standard, or institutional *convergence*. Rather, domestic politics and institutions mediate the pressures of globalization, and national *divergence* prevails. Thus, by the new millennium, a new consensus has emerged among scholars in political science and economics that fears of a race to the bottom and waning welfare states have been overblown; national differences, particularly with respect to welfare (or distribution) regimes, remain more or less intact. The important message for the globalization pessimists is that the poor in OECD countries need not fear that social protections will decrease simply because of globalization.[18]

Despite these robust findings, anxieties about a race to the bottom persist among activists, journalists, and academics outside the political

[17] See chapter 2 for a discussion of the small number of scholars who challenge this hypothesis.

[18] Many argue that the critical pressures for change in OECD welfare states come from forces other than economic integration, such as demographics (Garrett, 1998), deindustrialization (Iversen and Cusack, 2001; Iverson, 2001), the post-industrial shift to low-productivity-improving jobs, and the welfare state's maturation (Pierson, 2001, 1996).

science field and North America.[19] The apparent disconnect between the select group of scholars who dismiss these fears and the rest of the world is striking. One important reason for this ongoing "dialogue of the deaf" is that existing empirical investigations of the globalization–welfare nexus have excluded the great majority of countries – i.e. the developing world. It is constructive to underscore that this (relatively) new consensus has been achieved absent parallel analyses in LDCs. We are, heretofore, left with little knowledge of how (and if) "domestic politics" still matters in developing nations and whether these states can similarly defy RTB pressures in welfare policies.

Less developed countries have not been entirely absent from the academic literature on globalization and the race to the bottom.[20] Studies exploring the race to the bottom in environmental standards (e.g. Chau and Kanbur, 2006; Porter, 1999), labor standards and protections (e.g. Mosley and Uno, 2007; Haouas and Yagoubi, 2004; Harrison and Hanson, 1999; Beyer, Rojas, and Vergara, 1999; Wood, 1997; Singh and Zammit, 2004; Chan and Ross, 2003; Mehmet and Tavakoli, 2003), total government spending (e.g. Rodrik, 1997a, 1998; Garrett, 2000), and, more recently, government welfare spending (e.g. Wibbels, 2006; Avelino, Brown, and Hunter, 2005; Kaufman and Segura-Ubiergo, 2001) include some developing countries. The problem is that these analyses have important limitations. First, many are largely based on conjecture and fail to present empirical data to increase confidence in their arguments. Second, studies that do conduct empirical tests are limited in the range of countries covered.[21] The tendency is to focus on single countries or regions, concentrating mostly on select countries in Latin America or east Asia. More recently, Haggard and Kaufman (forthcoming) have done a thorough analysis on welfare policies in these regions, and added the eastern European countries to the mix. The studies by Rodrik (1997a, 1998) and Garrett (2000) are also exceptions, but their measure of "total government spending" (or Rodrik's "total government consumption") is all-inclusive and does not capture the specific variables that protect

19 The majority of these assertions have not involved an empirical test of RTB propositions. Examples of well-known journalists advocating the RTB thesis are Friedman (2000) and Greider (1998). Examples of major international contributors to the anti-globalization movement from the perspective of RTB are Canadian journalist Klein (2002) and Indian activist Shiva (2005). For examples of prominent RTB scholars outside the United States, see the works of Sakamoto (1994) and Cox (1996). Parenthetically, in the United States and outside the discipline of political science, sociologists appear to be more divided about RTB than IPE or CPE: see, for example, Guillen (2001) versus Ross (2004).

20 Here I am referring to the literature in which globalization is taken as more or less exogenous, and the analysis focuses on RTB pressures on (fiscal) policy.

21 The study by Mosley and Uno (2007) is an exception.

citizens from the risks and uncertainties of globalization. Finally, all the studies would benefit from a more detailed explanation of causal mechanisms. The linkages between globalization and LDC social policies and the processes by which the race to the bottom impresses (or not) changes in social welfare strategies have yet to be unraveled.

It is important to emphasize that a focus on welfare schemes is only one vantage point from which to assess RTB dynamics. Other policy domains are relevant, but researching them is less feasible. Exploring the race to the bottom with respect to LDC environmental standards is problematic because, although legal constraints exist, enforcement is and was extremely ineffective, even long before globalization pressures hit.[22] Popular discussions about the race to the bottom in labor costs and standards are also commonplace. This variable is included in the second part of the book as a form of welfare policy; focusing specifically on this variable is impossible, however, because time-series cross-national data are extremely sparse.[23] Finally, tax competition has been a common way to assess (and reject) race to the bottom effects in OECD nations. According to RTB hypotheses, countries will abandon capital income taxation and rely on labor and consumption taxes (Zodrow, 2003; Rodrik, 1997a). Here again, little systematic data on tax incentive policies for capital is publicly available.[24] This book incorporates the effects of tax competition in an indirect way. Since spending is commonly a function of taxes, if globalization is associated with declining social outlays then the effects of increased tax competition can be implied.[25]

The overall paucity of empirical scholarship on globalization's effects in less developed countries is not entirely surprising. First, the race to the bottom is often thought to be more relevant for the advanced industrialized countries. This is because, from the perspective of citizens in the OECD countries, developing world standards represent the "bottom" that is luring corporations away. What is not so well recognized, however,

[22] See Porter (1999) for a more complete discussion on this issue.
[23] See Richards and Sacko (2001) for a recent analysis using existing empirical data. See also Mosley and Uno (2007).
[24] Common incentives are value added tax, social security tax, corporate income tax, property tax, licensing fees, import duties, and sales tax. See Li (2006) for the most recent analysis on this subject. In addition, although evasion is a problem in all countries, in LDCs there exists a plethora of non-transparent ways that taxes can be reduced (Alm, Bahl, and Murray 1991).
[25] As Rodrik (1997a: 6) argues, "The increasing mobility of capital has rendered an important segment of the tax base footloose, leaving governments with the unappetizing option of increasing tax rates disproportionately on labor income. Yet the need for social insurance for the vast majority of the population that remains internationally immobile has not diminished." See also Wibbels and Arce (2003).

is that developing countries are also competing with one another for export markets and mobile capital. These pressures have intensified with the entrance of large markets such as India and China on the global stage (see Wood, 1997). The second reason for the lack of analyses on developing countries is the inherent difficulty involved in conducting this type of investigation. Data in poor countries tend to be limited and, given the vast heterogeneity characterizing LDCs, making systematic cross-regional comparisons – particularly in the realm of domestic politics – is enormously complicated. Here again, however, the reasoning is short-sighted. With respect to the data, there exist ways, albeit time-consuming ones, to get around the problem.[26] Developing countries are also not impossible to compare across regions because they share some fundamental characteristics – i.e. late industrialization, underdeveloped markets, large informal sectors, struggling labor movements, high levels of poverty, and a somewhat stronger need for state intervention. In fact, this distinctiveness of LDCs as a group is the precise reason for an analysis such as this one, which seeks to parse out the differential impacts of globalization on the two sets of countries (developed and less developed) and, in the process, advance welfare theories beyond the Anglo-European context.

1.2 The focus and plan of the book

This book attempts to illuminate how governments in the developing world are responding to race to the bottom pressures by focusing specifically on how the interplay of globalization and domestic politics affects social welfare policies. The primary dependent variable of concern is welfare policy, broadly defined as the aspects of public policy designed to exercise government "responsibility for the injury and dependency of its citizens."[27] Analyzing LDC welfare strategies over time provides an important way to illuminate the complex and interdependent processes of globalization and RTB pressures, domestic politics, and (social) policy reactions. The few existing studies on globalization and welfare policy in

[26] LDC data are indeed sparse, and generally not as readily available as they are in the OECD countries. For example, much of the data used in this book were manually coded and standardized for comparisons across countries. I also used proxies to get at data that do not exist (e.g. labor's capacity to organize). Finally, I have supplemented the quantitative analysis with case studies. This can provide a second check on data measures.

[27] This definition of welfare builds on Lowi (1986). Typically, "dependency" suggests state policies that alleviate the extent of worker reliance on the market (see Esping-Andersen, 1990). I argue later, however, that "dependency" in the LDC context can also suggest state efforts to promote reliance (dependency) on the market.

developing countries are conceptually vague on two counts: what "race to the bottom" and "convergence" actually represent, and the processes through which each occurs. This problem can be addressed by systematically analyzing the domestic effects of globalization within and across nations and regions over time, making it easier to recognize the presence (or absence) of convergence, trace the causal paths, and more decisively evaluate the RTB hypothesis. I argue that three domestic institutional factors ultimately structure responses to the challenges of globalization: fragmented labor movements; institutional constraints arising from government–labor interactions; and national social policy configurations.

The book, in chapter 2, opens with the driving question: is there a race to the bottom in developing countries? I hypothesize that, in direct contrast to the developed nations, governments in the developing world are indeed succumbing to race to the bottom pressures. Building on Rudra (2002), I test this proposition by exploring the effects of trade and capital flows on three conventional mainstays of public welfare schemes: social security, education, and health spending. I focus on these particular sectors because they are fundamental for social well-being (see Dreze and Sen, 1989), and because they possess the most comprehensive set of cross-national welfare data available. My results indicate that, of these, it is social security programs that are the most sensitive to international market pressures. This finding is consistent with the RTB hypothesis that increased economic integration encourages governments towards market-friendly policies. Social security programs are often negatively targeted for acting contrary to market forces by pushing up labor costs and creating dampening effects on worker productivity. Accordingly, it is easy to see why these programs might be the first to be compromised in the face of RTB pressures.

Because we want to understand *why* race to the bottom outcomes in developing countries and OECD nations differ, identifying the causal mechanisms driving this outcome is critical. I find that, ultimately, it is the fragmented character of LDC labor market institutions that helps advance the race to the bottom in the social security sector. In contrast, economic and political conditions are more conducive for labor to overcome collective action problems in the OECD countries, making it easier to balance globalization pressures with sustained social outlays. This focus on labor's organizing capabilities is critical: in the first phase of the analysis, we want to know whether labor has the capacity to negotiate at par with capital and government negotiators. Existing research reveals that policy compromises between the three groups are particularly vital in the globalizing environment, ensuring that government interventionism (for labor, in this case) will be offset with positive macroeconomic consequences (Garrett, 1998). Indeed, it is unlikely that labor groups acting alone can successfully promote such policies; rather, they must form alliances with leftist parties, and even business groups (Swensen, 2002; Robertson, 2004; Remmer, 2002; Esping-Andersen, 1990). What is less emphasized is that a strong, encompassing labor movement is a fundamental prerequisite for this to occur (Garrett, 1998; Katzenstein, 1985).[28] I demonstrate that, since labor groups are less coordinated in LDCs, policy compromises that promote a win-win situation for capital *and* labor are unlikely, and governments are driven to cut back on select interventionist social policies that are purported to have harmful macroeconomic effects.

The conclusion in chapter 2 is that the effects of globalization are mediated by domestic institutions, especially labor market institutions, and, as a consequence, the same degree of resilience to race to the bottom pressures cannot be expected in the industrializing nations. This chapter thus confirms prevailing fears that RTB pressures are indeed leading governments to implement some form of welfare retrenchment in LDCs. As the subsequent chapters make increasingly clear, however, this observation by itself does not tell us who really gets hurt by these cutbacks and what "the bottom" of welfare policies actually entails in less developed countries.

Exactly who is being hurt by race to the bottom policy reactions? Chapter 3 takes a careful look at the nature of policy interactions between government and labor market institutions, and reveals a seeming paradox: contrary to popular wisdom, RTB pressures for cutbacks in social spending are *not* directly linked to worsening conditions for the poor in LDCs.[29] It is commonly the case that, in government attempts to build a political support base (particularly in the absence of sustained economic growth), social security, health, and education benefits have often been distributed to strengthen and manipulate interactions between government, business, and privileged labor groups in the organized economy.

Welfare schemes have thus been biased towards the protection of white-collar, salaried, and some blue-collar workers. Those large segments of the population with poor mobilization skills and sustained involvement in informal, non-wage work have long been excluded. The government–labor relationship gives rise to institutional constraints (i.e. privileged access to benefits, clientelism) that reinforce the divisions within LDC labor movements and buttress middle-class welfare policies.

[28] "Encompassing" is a term used by Olson (1971) in reference to labor unions. It refers to a centralized labor organization that includes a wide range of labor participants.

[29] This is certainly not to suggest that the poor do not get hurt from secondary effects as a result of this exclusion. For example, without social protections in the face of any economic crisis stemming from globalization, the poor will get poorer.

I argue that, while all three categories of social spending help improve income distribution in richer countries, the impact of social spending in the developing world is much less favorable. In effect, chapter 3 presents empirical support of the theoretical argument that LDC welfare policies generally focus on the non-poor.

The relationship between openness, government social expenditures (i.e. education, health, and social security and welfare), and income distribution is evaluated through a time-series cross-sectional panel data set for thirty-five less developed countries from 1972 to 1996. Significantly, only spending on education in LDCs encourages a more favorable distribution of income in the face of globalization. I argue that the pressures deriving from a more competitive global economy increase incentives for more equity-enhancing reforms in education, whereas publicly sponsored health programs and, particularly, social security and welfare programs confront greater political lobbying and clientelism. These insights, taken together with the findings in chapter 2, reveal that the race to the bottom in social security spending primarily affects the middle class and is not of immediate consequence to the absolute poor. Even more significantly, the findings present the important implication that LDC governments *can* do something in the face of RTB cutbacks: improve the efficiency of education spending by redirecting existing resources towards the poor.

Chapter 4 delves further into domestic institutional arrangements and reveals that the question of who wins or loses from globalization – or more specifically, the race to the bottom – is ultimately dependent upon national social policy configurations. The main contribution of this chapter is to broaden the analysis of convergence to evaluate the race to the bottom. I do this by moving away from the sole focus on expenditure cutbacks to a multifaceted examination of the institutional structures of LDC welfare schemes.[30] Esping-Andersen (1990: 19) has long emphasized that "[e]xpenditures are epiphenomenal to the theoretical substance of the welfare state." The identification and persistence of set constellations of distribution regimes in the developed world has more or less put to rest expectations of a race to the bottom in that sector of the world; but the question as it is applied to developing countries is still left wide open. As a consequence, it is left unresolved as to how or why less social spending in LDCs is necessarily associated with policy convergence, or a race to the bottom towards neoliberal welfare institutions. It is certainly possible that leaders might engage in low (or decreasing) social spending while promoting "illiberal" welfare measures, such as

[30] See Green-Pedersen (2004) for an excellent discussion of problems with existing theoretical conceptualizations of retrenchment, or, as referred to in this book, RTB.

public employment or labor market protections.[31] In other words, while developing countries may be universally affected by the race to the bottom, it does not mean that they are moving towards neoliberal policy convergence.

Chapter 4 sets out to identify the logic and existence of set patterns of distribution regimes in the developing world. The discovery of a distinct number of distribution regimes in the developing world well into the twentieth century, as presented in chapter 4, ultimately leads this book to predict that convergence towards the "neoliberal bottom" is not expected among developing countries. Using cluster analysis, I illustrate that welfare efforts in LDCs are either directed towards promoting market development (a *productive* welfare state), protecting individuals from the market (a *protective* welfare state), or both (a *dual* welfare state).[32] Placing the analysis of welfare states squarely within the context of their political economies makes it evident that these distribution regimes are part of complex historical configurations. I argue that initial development strategies are the basis of LDC welfare state divergence. Productive welfare states evolved in nations that pursued export-oriented development, while protective welfare states emerged in more closed economies.

The analysis of the logic and character of the different distribution regimes provides further insights on "who really gets hurt." Following Esping-Andersen (1990), I show that distribution regimes play an important role in aggregating interests and structuring access to the political arena. It was the middle classes who first benefited from these welfare schemes and, as a result, developed a vested interest in upholding the status quo. As they fight to preserve their benefits, regimes ultimately vary on the extent of welfare cutbacks, where they occur, and which programs are still vigorously protected from the forces of globalization. The reason why the race to the bottom is largely affecting the middle class and bypassing the poor becomes increasingly clear: *none of the classic LDC welfare regime types were originally geared towards helping "protect" the bottom strata of the population.*

To summarize, the government–labor relationship and the discovery of distinct patterns of welfare regimes in less developed countries expose the complex relationship between the pressures of early twenty-first-century globalization, domestic politics and social policies. As it turns out, the

[31] Note that reductions in public employment and labor market deregulation are basic components of the structural adjustment programs (i.e. neoliberal reforms) advocated by the IMF and World Bank.

[32] Indeed, this classification excludes personalistic dictatorships, although, arguably, they are more likely to implement welfare strategies that would protect select individuals or groups from the market.

race to the bottom story is far more involved than originally asserted by proponents of this hypothesis. Developing countries are indeed experiencing the effects of a race to the bottom. Two major caveats apply, however: first, what constitutes "the bottom" differs across the three welfare regimes; and, second, "the bottom" never included protections for the poor in the first place.

Chapters 5, 6, and 7 explore three case studies: India, Brazil, and South Korea. These cases illustrate the findings from the quantitative chapters and take a more in-depth look at the RTB relationship in developing nations. Qualitative analysis allows us to get a richer and more nuanced sense of how globalization affects institutional changes in welfare regimes, particularly since the 1997 financial crises, after which the availability of quantitative data is extremely limited.[33] India, South Korea, and Brazil have been selected as three regionally important countries that represent the protective, productive, and dual welfare state, respectively. The three case studies illustrate in great detail the primary findings of this book: despite evidence of the race to the bottom in developing countries, existing institutional arrangements resist convergence towards a neoliberal welfare state, and they ensure that the lower and middle classes are the ones most directly impacted (for better or for worse).

The pressures of globalization force some cutbacks in all three welfare regimes, but, alongside a few select signs of change, each retains important elements of institutional continuity. In the protective welfare states, globalization encourages a greater emphasis on commodification efforts,[34] although much of the remaining central welfare schemes remain more or less intact. Reform in the productive welfare states focuses more on cost containment and the implementation of some protective type policies (i.e. means-tested safety nets and social insurance programs). A concerted effort continues to be made, however, to preserve a considerable amount of state control. Finally, in the dual welfare state, the reform emphasis is on cost containment and improving access to primary education. Existing programs tend to clash most intensely with reform efforts in this particular welfare regime type. It is, therefore, the dual welfare state that is likely to experience the greatest degree of institutional change in LDCs. Significantly, however, the extent of institutional continuity indicates that pro-poor policies in all three welfare regimes remain relatively limited both before and after openness policies are adopted.

[33] World Bank and IMF data on LDC variables relevant to this book are sporadic after 1997.

[34] Commodification efforts, explained in more detail in chapter 4, refer to government attempts to encourage market participation on the part of workers, particularly through investment in human capital.

1.3 Contributions

The broader contributions of this book are threefold. First, the analysis directs its focus on the mediating effects of developing world domestic institutional arrangements in a large-N sample of regionally and economically diverse developing nations. Drawing from Weiss's (2003) depiction of "domestic institutions" as both normative orientations and organizational arrangements, this book exposes three institutional factors that play a primary role in explaining policy responses to globalization: the fragmented character of labor organizations (chapter 2); the nature of the policy interactions between government and labor (chapter 3); and distribution regimes that reflect "the organization of the political economy which aggregates interests and structures access to the political arena" (chapter 4) (see Weiss, 2003: 22).

Second, this book attempts to overcome vague assessments of the race to the bottom and policy convergence that make falsification difficult. I analyze RTB in terms of cutbacks *and* institutional changes.[35] More specifically, through a combination of quantitative and qualitative analysis, I assess cutbacks as reductions in welfare entitlements. This is operationalized by the lowering of benefit levels, stricter eligibility criteria for, and decreased durability of benefits (see Green-Pedersen, 2004: 7). In the second part of the book, I evaluate RTB as indicated by institutional change.[36] I rely primarily on Pierson (1996: 157) and determine if institutional changes comply with the following criteria: (1) significant increases in the reliance on means testing; (2) major transfers of responsibility to the private sector; and (3) dramatic changes in benefit and eligibility rules. Because Pierson focuses mainly on social-insurance-type policies, however, I add a fourth, and more general, criterion: the discontinuity of ("illiberal") institutional legacies. In essence, Esping-Andersen's liberal welfare state represents the lowest common denominator of existing welfare regimes, frequently referred to in this book as the "neoliberal bottom." The central tenets are limited public responsibilities for market failures, the encouragement of private welfare coverage as the norm (to help minimize public budgets and encourage work productivity),

[35] On this point, see Green-Pedersen (2004) for an excellent critique of the RTB literature.

[36] On the issue of assessing radical institutional change, I concur with Pierson (1996: footnote 39). He notes: "Establishing what constitutes 'radical' reform is no easy task. For instance, it is impossible to say definitively when a series of quantitative cutbacks amounts to a qualitative shift in the nature of programs. Roughly though, that point is reached when because of policy reform a program can no longer play its traditional role (e.g., when pension benefits designed to provide a rough continuation of the retiree's earlier standard of living are clearly unable to do so)."

and the targeting of welfare benefits and programs to only the demonstrably needy.[37]

Finally, this book reveals that protection (or the lack of it) for the absolute poor in less developed countries is an outcome of both international economic integration and domestic institutions. The disappointing but true reality is that, in the effort to "catch up" with the developed economies, the bottom strata have long been neglected by LDC governments. In no way does this analysis suggest that globalization affects only the middle class and is having *no* effects on the poor. It also leaves open the question of whether, overall, poverty and inequality are increasing in connection to market expansion. The bottom line is that, to the extent that globalization is impacting the poor, it is not through its effects on the welfare state (i.e. through a race to the bottom). Globalization might be making it harder to implement radical structural changes favoring the poor by constraining domestic fiscal policy resources, but the direction of change is being guided by domestic institutions and politics. Unfortunately, since institutions focusing on redistribution towards the poor did not exist before the rapid advancement of globalization, creating such institutions in the contemporary era is a formidable challenge. It is no wonder that studies have found poverty and inequality to be increasing with globalization. This book might not make it politically easier for national policy-makers to pursue strategies for the poor in this era of globalization. It is hoped, however, that this book will reveal the underlying sources of policy change and the causes for both institutional and political resistance to equity-enhancing redistribution policies.

[37] As Pierson (2000: 798) notes, "The liberal welfare states are associated with a host of social problems such as mounting poverty and inequality, and large gaps in the support of human capital development." Chapter 4 presents a more detailed description of Esping-Andersen's liberal welfare state.

2 The race to the bottom in developing countries

As pointed out in the introduction, scores of sophisticated analyses reveal that the race to the bottom is not a concern in developed countries. Does this imply that fears of a race to the bottom in the developing world are also misplaced? A full answer to this question must begin with an account of why globalization might affect rich and poor countries differently. That is, are there compelling reasons to expect a different outcome in developing countries from what has occurred in their more developed counterparts?

I argue that it is domestic institutional differences between developed and developing countries, especially those involving labor, that give rise to different policy reactions to international market expansion. In the current economic environment, the ability of labor market institutions in the developing nations to negotiate compromises effectively (or not) between government, labor, and business is the chief factor creating these differences. Unlike the advanced industrialized nations, where labor tends to be more organized and institutions more broad-based, the fragmented character of LDC labor organizations makes it near-impossible for them to negotiate with one voice, and the differing agendas give governments under pressure from international markets the leeway to reduce benefits. Thus, without mobilized and coordinated labor market institutions, RTB pressures prevail, and retrenchment in social spending will take place.

This chapter attempts to unravel how and why the effects of globalization in the developing world are mediated by domestic institutions linked to labor. It establishes both the causal mechanisms and empirical evidence in support of the race to the bottom in developing countries, and concludes that some anxieties about the domestic effects of globalization are indeed justified. Unlike in developed countries, LDC labor market institutions have been unable to facilitate collective action among the majority of workers, and, as a result, governments are able to follow through with reform in certain social sectors.[1]

[1] In this chapter, labor market institutions refer to collective bargaining arrangements for labor. This includes both normative orientations and formal rules and procedures on mobilization, as well as the extent of formal organizational arrangements involving government, labor, and business.

Section 2.1 initiates the analysis by reviewing the broader literature on globalization and welfare states, and identifies the conditions under which the race to the bottom is likely to occur. The principal insight of this section is that nations without labor market institutions that can adequately coordinate negotiations between government, labor, and business are likely to succumb to RTB pressures.

Section 2.2 builds on this theoretical foundation and presents an argument as to why labor market institutions in the developing world are insufficiently equipped for such coordination in the globalizing environment; labor is unlikely to overcome its collective action problems in LDCs to discourage governments successfully from reducing welfare spending. Drawing on Olson's (1971) *Logic of Collective Action*, I argue that mobilization problems are particularly acute in less developed countries because both low-skilled and surplus labor are abundant. The pressures of international market competition and the increasing demand for low-skilled labor during the process of globalization can aggravate these difficulties, making it even more challenging to form stable alliances.

Section 2.3 presents empirical evidence in support of this argument by first constructing a globalization–welfare model specific to developing countries, then testing it with unbalanced panel data and the fixed-effects method. I disaggregate globalization in terms of trade, portfolio investment, and foreign direct investment flows and assess their effect on the "welfare state," commonly operationalized in the literature as the extent of government spending on income transfer programs (e.g. public pensions), education, and health (see Kaufman and Segura-Ubiergo, 2001, and Avelino, Brown, and Hunter, 2005). As summarized in section 2.4, my findings substantiate the race to the bottom hypothesis in the sense that globalization does lead to cutbacks in social security spending. In contrast, however, education and health expenditures are not as sensitive to RTB pressures.

2.1 Existing literature on the globalization–welfare state nexus

Proponents of the race to the bottom hypothesis expect that expanding international markets and the prioritization of efficiency and competitiveness concerns will undermine welfare spending. Garrett and several other theorists have provided empirical evidence to refute such claims in the OECD countries, however (Garrett, 1998; Quinn, 1997; Huber and Stephens, 2001).[2]

[2] For exceptions, see the analyses of retrenchment in the OECD countries in Allan and Scruggs (2004), Hicks and Zorn (2005), and Korpi and Palme (2003). Burgoon (2001) discusses how different types of openness spur retrenchment in some types of welfare programs, but not in others.

The general consensus is that these nations have labor market institutions that can dampen the negative effects of globalization. Although some scholars have recently begun to investigate the ability of LDC governments to resist RTB pressures and maintain or increase existing levels of social spending in developing countries, the extant literature does not sufficiently explain why, in a globalizing economy, the politico-economic conditions affecting welfare spending might differ from developed countries and, as a result, render such nations more susceptible to RTB pressures.[3]

The race to the bottom hypothesis suggests that, due to the pressures of globalization, all states, regardless of their partisan compositions and national institutional differences, will embrace free market, laissez-faire policies in order to promote competitiveness (Mishra, 1999; Drunberg, 1998; Stryker, 1998; Strange, 1997; Gray, 1998; Greider, 1998; Cerny, 1995; Evans, 1997; Gill, 1995; Wibbels, 2006). Welfare spending is expected to be adversely affected for two reasons. First, social benefits are not regarded as efficient market-disciplining devices. Both the resulting upward pressures on labor costs and the possible negative effects on work incentives are claimed to depress export competitiveness. Second, governments are increasingly constrained from raising the revenues necessary to maintain social welfare programs. "Footloose capital," or the capacity to withdraw and shift productive and financial capital with greater ease, has made it increasingly difficult for governments to generate revenues through taxation (see Wibbels and Arce, 2003).[4] As international markets expand, governments reduce taxes on capital in order to compete with other states for foreign investment and prevent capital flight. Government borrowing becomes an unattractive option, since this can lead to higher debt and interest rates, and thereby deter investment. The last two decades have thus become witness to the reification of Lindblom's "markets as prisons" idea.[5] With increasing global competition, governments find it more difficult to protect citizens from the risks and uncertainties associated with market expansion.

By analyzing fourteen OECD countries, Garrett (1998) presents one of the most convincing challenges to the RTB hypothesis as applied to social welfare spending. Garrett's analysis extends the globalization–welfare

[3] See Wibbels (2006) for a discussion on particular economic conditions that encourage the race to the bottom in LDCs.
[4] For a critique of this idea, see Swank (1998).
[5] See Maxfield (1998) for reference to this idea.

debate initiated by Polanyi (1944), Katzenstein (1985), and Ruggie (1994).[6] Key to Garrett's analysis is the ability of labor market institutions to negotiate compromises effectively between government, labor, and business. He convincingly argues that, if the workforce is highly mobilized and coordinated (i.e. "encompassing"), the economic demands of globalization can be effectively balanced with redistribution policies. In other words, labor can strike policy compromises, such as keeping wage growth in accordance with productivity improvements, so that the highest possible level of disposable income (wages and work-related benefits) can be maintained (see Garrett, 1998: 9). Business and government are satisfied because interventionist social policies do not encumber macroeconomic performance. Garrett concludes that globalization has, in fact, strengthened left–labor movements and, consequently, cross-national partisan differences in the developed world have been sustained.

This position is not without its critics, however. Several theorists provide alternative institutional explanations for the resilience (or contraction) of social spending in developed countries. Iversen and Cusack (2001), for example, argue that deindustrialization, and not globalization, is responsible for the expansion of the welfare state. Pierson (1996) maintains that supportive interest groups and voters have resisted the dismantling of the contemporary welfare state.[7] He rebukes analysts of the RTB hypothesis for overlooking the crucial importance of the well-developed interest group environment in industrialized nations. Consumers of welfare benefits (e.g. the elderly and the disabled), he argues, have successfully mobilized to prevent a sharp deceleration of social spending (Pierson, 1996, 1994). Other studies show that well-organized labor groups acting alone cannot be the critical factor; they have to form alliances. In other words, to negotiate policies effectively, they must coordinate with other middle-class groups (e.g. Rueschemeyer, Stephens, and Stephens, 1992; Esping-Andersen, 1990), leftist, social democratic or Christian democratic parties (e.g. Robertson, 2004; Remmer, 2002; Huber and

[6] The theoretical basis for this debate was laid by the seminal work of Polanyi (1944), and advanced by Ruggie (1982) with his concept of "embedded liberalism." These authors separately conjecture that the state must make a broader commitment to social welfare in order to temper the "pernicious effects" of international markets. See also Cameron (1978), Rodrik (1997a, b, 1998), and Katzenstein (1985), who demonstrate the existence of a positive relationship between trade exposure and government social spending throughout much of the twentieth century.

[7] See Clayton and Pontusson (1998), who challenge some of the tenets of this thesis and move forward with a critique of Pierson (1996).

Stephens, 2001; Hicks, 1999; Western, 1999), or certain entrepreneurs (e.g. Mares, 2005).

This second set of research de-emphasizes the role that well-organized labor groups might currently play in preventing social spending cutbacks in mature welfare states.[8] Yet none of the aforementioned studies deny that labor groups were critical before welfare states reached this advanced stage, and that they can still be a primary pressure group behind policies intended to distribute societal resources more equitably (Boix, 2006; Korpi and Palme, 2003). What is most often overlooked is that the key to preventing retrenchment *in the global era* is labor market institutions encompassing enough to ensure that "economywide wage growth does not undermine the competitiveness of the exposed sector" (Garrett, 1998: 41).[9] Under such conditions, even business leaders will support social policies for the positive externalities they are likely to bring: social stability, a containment of labor militancy, skill investment, and, for some business groups, the socialization of risk (see Mares, 2003b). If labor groups are atomized, however, building alliances with other groups (business associations and political parties in particular) and forcing government to take current labor demands seriously will be extremely difficult. It is therefore imperative in the critical evaluation of the RTB hypothesis to get some sense of the organizing capacity of labor.

Unfortunately, recent explorations of RTB effects on social spending in developing countries have failed to take into account this key variable (Mares, 2005; Kaufman and Segura Ubiergo, 2001; Adsera and Boix, 2002; Wibbels, 2006). Mares (2005), for instance, predicts that workers in high-risk sectors will receive more generous welfare schemes than workers in lower-risk sectors. Yet a fundamental assumption in her analysis – that labor in less developed countries will or can be organized sufficiently to demand such compensations – remains untested.

Thus, the effect of globalization on social spending trends in developing countries, where labor remains an important pressure group, is in need of exploration. An LDC model that effectively captures the globalization–welfare nexus must account for the role of labor market institutions in the existence and maintenance of social welfare schemes.[10] The question of

[8] Although never precisely defined in the extant literature, the term "mature welfare state" generally pertains to two conditions: (1) government social budget allocations constitute a significant portion of gross domestic product (GDP); and (2) social welfare services and benefits extend to the majority of the population.

[9] This is arguably true of "coordinated market economies," which show institutional resilience in the global era (see Hall and Soskice, 2001, and Kitschelt *et al.*, 1999).

[10] Unless specified otherwise, "labor" refers to both low-skilled and skilled workers.

interest is how such institutions mediate the effects of globalization in developing countries, as compared to Garrett's sample of fourteen OECD countries.

2.2 Globalization, labor and the race to the bottom in developing countries

In a globalizing economy, RTB pressures in social spending are likely to be the most intense in nations highly endowed with low-skilled labor. Quite unlike many of the developed countries, labor groups in LDCs have limited institutional power. Their bargaining position is weak because the sizable population of low-skilled laborers is faced with collective action problems exacerbated by large pools of surplus labor. Labor market institutions in the developing world are characterized by decentralized labor groups that have only tenuous ties with each other, as well as with political parties and particular entrepreneurs. Therefore, globalization will lead to less, not more, social welfare spending.

Labor market institutions in developing countries are fragmented and weak, in large part because of collective action problems. The population of low-skilled laborers in LDCs is large, and scores of studies show that it is expanding with globalization. Not only are these workers difficult to mobilize, due to their low education levels and erratic work hours, but, according to Olson (1971), the higher the numbers in a group the greater the propensity for the free rider problem to occur and the less likely that the collective good (in this instance, welfare benefits) will be supplied.[11] The problem is intensified by the existence of a large surplus labor population in most LDCs.[12] This alters the cost–benefit ratio of organizing and reduces the incentives for low-skilled labor to mobilize for two reasons. First, in an era of heightened global competition, large enterprises profit from the existence of surplus labor pools because they help minimize labor costs, are unprotected, and increase flexibility. Unionization in this environment is improbable at best. Second, the presence of surplus labor makes it impossible to offer "selective incentives," as Olson (1971) suggests, to help overcome collective action problems. For example, competition from surplus laborers makes it extremely difficult for union organizers to offer secure employment for

[11] For more detailed hypotheses on why low-skilled labor groups in LDCs are difficult to organize, see Deyo (1989: chap. 6), Gereffi (1995), Lok (1993), and Ingerson (1984).

[12] The term "surplus labor" refers to the extent of "hidden" unemployment prevalent in the economy, and suggests that the supply of labor to industry is unlimited (see Rudra, 2005, for details).

union members.[13] Because so many low-skilled laborers are without work, they focus on employment and are unlikely to lobby for social welfare benefits.

Skilled labor groups in developing nations, in contrast, have greater capabilities to surmount collective action problems. These groups are generally smaller in size, less threatened by a surplus labor population, and more likely to lobby for welfare benefits.[14] In fact, the recruiting grounds for labor organizations in most LDCs have historically occurred in the skilled industries (e.g. heavy industries, white-collar companies). It is therefore no surprise that skilled labor groups tend to comprise the bulk of welfare beneficiaries in developing countries.[15]

Given this logic, the growth of skilled relative to low-skilled labor would help workers as a whole to overcome their collective action problems and advance their political interests, provided that the level of surplus labor is not too high. The higher the ratio of skilled to low-skilled labor and the lower the surplus in a country, the greater the likelihood that workers will form coalitions and be able to defend welfare spending.

The barrier to progress in this case is that globalization is likely to exacerbate existing collective action problems for workers in developing countries, even if their economic situation is improving. The importance of factor endowments in determining who gains and who loses with globalization stems from the Hecksher–Ohlin and the related Stolper–Samuelson theorems. These theorems suggest that low-skilled labor in LDCs should gain with increased exposure to international markets, while, in the more developed countries, the situation of high-skilled labor and capital will improve. It can be argued that this logic also applies to capital flows. Both productive and financial capital flows will increase in nations that are utilizing their most abundant factor more efficiently. Thus, in countries rich in low-skilled labor and poor in capital and high-skilled labor, globalization should improve the economic conditions (i.e. wages and/or employment) of low-skilled labor.

More powerful and encompassing labor institutions do not necessarily follow, however. According to Rogowski (1989), owners of locally abundant factors expand their political influence when openness occurs. His analysis suggests that low-skilled labor in LDCs will have a stronger bargaining position because of the greater wealth that accompanies

13 Note that, while LDCs with state-corporatist systems might offer some of these incentives, the objective is generally to control and weaken labor. Thus, the reference here is to independent unions.

14 On this point, see Manning (1998), Shafer (1994), and Deyo (1989, 1984).

15 For examples, see Mesa-Lago (1994, 1991), Midgley (1984), and Esping-Andersen (1996).

openness.[16] Conversely, capitalists and skilled laborers will be better able to influence government policies in the more developed countries. The implicit assumption in Rogowski's model, that the organizing potential of labor will be strong in an open economy, is inappropriate for developing nations, however. If globalization is encouraging the growth of low-skilled labor relative to skilled, as predicted by the Stolper–Samuelson theorem, and surplus pools remain large, mobilization problems will be even more difficult to overcome. Workers in LDCs, therefore, will find it difficult to advance their common political interests, despite any economic gains they may reap from globalization.

In sum, globalization leads to lower social welfare expenditures in labor-rich developing countries because fragmented, decentralized labor market institutions have limited political leverage. In developed countries, labor groups have the institutional clout to ensure that they do not lose political power with globalization, and can successfully demand compensation in the form of social welfare expenditures. The pattern of political bargaining power and interest of labor in LDCs is quite different, however. It is, in fact, the reverse of what has been predicted by existing political and economic theory.

2.3 The evidence

To evaluate this argument, I first provide comparative data on globalization and social spending trends. Then, to get a sense of the character of their labor market institutions, I compare data on "potential labor power" (PLP) in both developed and developing nations. Next, after presenting a developing world model of the globalization–welfare nexus, a more thorough empirical test of the RTB hypothesis is conducted by way of multivariate panel regressions. Lastly, the developing country model is compared to results from the OECD countries.

2.3.1 Contrasting trends in globalization and welfare: rich versus poor nations

The most sophisticated empirical works on globalization and welfare state expansionism tend to operationalize globalization by both capital and trade flows.[17] This analysis moves beyond existing studies, however, by

[16] Note that Rogowski does not make the distinction between skilled and low-skilled labor with respect to factor endowments.

[17] Garrett (1998). See Rodrik (1997a, 1998), for example, who argues that capital mobility and trade have differential effects on social policies.

investigating the differential effects that productive and financial capital, in addition to trade flows, can have on contemporary social policies.[18] The two can have quite distinct effects, particularly since they have different degrees of mobility.[19] Portfolio flows tend to be more volatile and thus pose a stronger "exit" threat, since they are based on speculation of stock yield differences and interest and exchange rate movements. In contrast, foreign direct investment is more stable and less sensitive to changes in other types of capital flows (e.g. short-term investment, long-term investment).[20] It is reasonable to expect, then, that, if RTB pressures are real, financial capital flows will have a stronger negative effect on welfare spending because of the (somewhat) greater risks and uncertainties associated with this type of market integration.

Trade is measured here as imports plus exports as a percentage of GDP, and capital mobility is represented by net portfolio flows and FDI as a percentage of GDP. The figures on social spending pertain to central government expenditures on education, health, and social security (SS) and welfare services (as a percentage of GDP).

Within the last two decades countries as diverse as India, South Korea, Mexico, Brazil, the Philippines, Ghana, and Kenya have begun liberalizing their economies. This turn towards openness began in the late 1970s and early 1980s. Countries in the developing world are slowly integrating into the global economy (see figure 2.1).[21]

Trends in government spending for social welfare have diverged during this period, however – expanding in the richer OECD countries and remaining relatively constant or declining slightly in the poorer developing countries (see appendix A for detailed social spending data). The total average government social budget allocations (social security, education, and health) in the developing economies have barely increased by 1 percent over the last three decades. This is striking given that social welfare programs are not a new phenomenon in LDCs. They were implemented as early as 1924, beginning with Chile, and have since spread to more than seventy other developing countries.

[18] Note that portfolio investment for the developing countries includes liabilities constituting foreign authorities' reserves, and covers transactions in equity securities and debt securities. This measure of portfolio flows has the largest number of observations for the developing world.

[19] Schwartz (1998) discusses the different implications of productive versus financial capital flows on welfare states.

[20] See Chuhan, Claessens, and Mamingi (1993) for empirical support for the notion that FDI is not "hot money."

[21] World Bank (1999); Yusuf (1999); Otsubo (1996); Little *et al.* (1993).

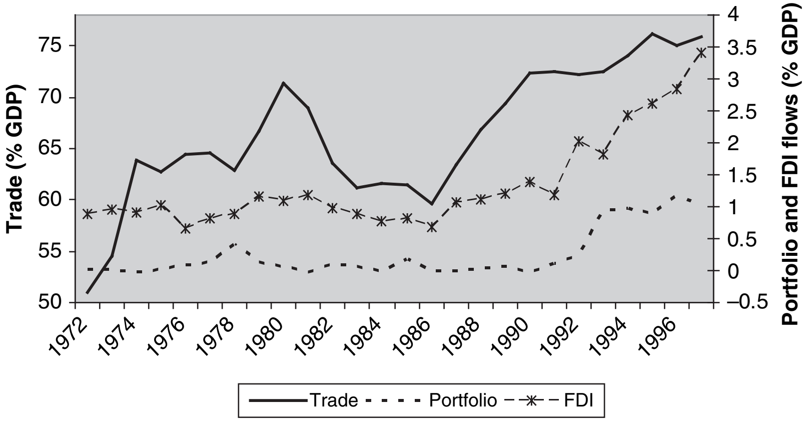

Figure 2.1 Globalization trends in developing countries, 1972–97

Note: Data for developing countries drawn from study sample of fifty-nine countries.
Sources: IMF, *Government Finance Statistics* (various years); IMF, *Balance of Payments Statistics* (various years); World Bank (2002b).

Developed countries expanded their combined social spending (SS and welfare, education, and health) from an average of 25 percent of their total GDP in the 1970s to 31 percent in the 1990s. Meanwhile, the lower-income countries spent an average of 6 percent in the 1970s and only 7 percent in the 1990s. The upper middle-income countries fared slightly better, with their total social budget expanding from 9 percent of GDP to 11 percent in the 1990s. It is notable that the social security and welfare sector experienced the most impressive increase in the OECD countries over the last few decades (3.8 percent), while SS and welfare spending in all LDCs combined improved by barely 1 percent. Tables 2.1–2.3 illustrate the striking contrast between the developing and developed countries.

The developing country sample and time frame used in this study include all those for which comparable data on welfare spending could be obtained.[22] The fifty-nine less developed countries are low-, middle- and high-income non-OECD counties.[23] This data set is regionally diverse,

[22] The time series stops at 1998 since standardized cross-country social spending data for most developing countries are scarce after this year. Furthermore, the expenditure data available post-2000 are not comparable with previous data because of a fundamental change in the IMF's accounting method (see IMF, 2001).

[23] Although Greece, Turkey, Mexico, and South Korea are currently OECD members, they are included in the LDC sample as upper middle-income countries because of the lower income levels that characterized them at the beginning of this study (the 1970s). To check

Table 2.1 *Low- and lower middle-income LDCs*

Social spending (% GDP)	1970s	1980s	1990s	Change 1970s–1990s
SS and welfare	1.47	1.58	2.07	0.47
Education	3.29	3.37	3.50	0.30
Health	1.32	1.46	1.62	0.39

Table 2.2 *Upper middle- and upper-income LDCs*

Social spending (% GDP)	1970s	1980s	1990s	Change 1970s–1990s
SS and welfare	3.86	4.27	5.40	0.49
Education	3.75	3.80	4.02	0.26
Health	1.59	1.81	2.00	0.45

Note: I include Singapore, South Korea, Greece, Cyprus, and Kuwait in the upper middle-income category since they were classified as middle-income countries throughout the 1970s and 1980s.

Table 2.3 *High-income OECD countries*

Social spending (% GDP)	1970s	1980s	1990s	Change 1970s–1990s
SS and welfare	11.68	13.69	14.23	3.4
Education	3.08	3.10	2.63	−0.19
Health	2.94	3.48	3.61	0.64
Decentralized SS and welfare	3.20	3.02	3.60	0. 40
Decentralized education	3.10	3.86	3.86	0.76
Decentralized health	1.90	2.95	3.14	1.2
Total SS and welfare	14.88	16.71	17.83	3.8
Total education	6.18	6.96	6.49	0.57
Total health	4.84	6.42	6.75	1.9

covering twenty Latin American and Caribbean countries, twelve African countries, eight Middle Eastern countries, ten Asian countries, and three European countries. Of these, the majority are low- and lower middle-income countries. This sample is biased, in the sense that it excludes eastern

if they are, in fact, outliers, regressions have been run with each country alternatively excluded individually, and then with them all excluded as a group. The estimates are not affected by their exclusion.

European countries[24] and several newly industrialized countries (NICs). For example, rapidly emerging international market participants such as China and Taiwan are among those excluded due to the lack of data.

One problem with the welfare data is that provincial and municipal expenditures are not captured and, thus, total social spending data for countries with decentralized disbursal have been underestimated.[25] This is particularly problematic for a small handful of high- and middle-income countries that have federal systems and high revenue-generating capacity at the local levels. The data used in this analysis should be viewed with this caution in mind. Nonetheless, it is reasonable to expect that trends in central government spending on social welfare reflect broader trends in developing country economies. For the OECD countries, fortunately, more decentralized data are available.[26]

2.3.2 LDC labor in a globalizing economy

Why might labor find it increasingly difficult to overcome collective action problems in a globalizing economy? The data presented in this section suggest that globalization indeed generates international demand for low-skilled labor in poor countries, and thereby encourages greater competition among countries with similar factor endowments. In several empirical studies, Wood shows how nations with high levels of low-skilled labor follow the principles of comparative advantage and place more emphasis on labor-intensive manufactured goods.[27] Table 2.4 clearly

[24] Eastern European countries are intentionally excluded from this data set, because their historical circumstances (particularly regarding state social spending) are distinct from the majority of non-OECD developing countries. These countries are not readily comparable to other LDCs, because they are undergoing a unique historical experience with respect to their market transitions, have comparatively different functions for the state and welfare, and, on average, maintain much higher levels of spending on welfare relative to GDP. (On the final account, the World Bank's third Policy Research Report (World Bank, 1994) places them in the same category as OECD countries.)

[25] The reason for this is that such cross-country data simply are not available. The IMF's *Government Financial Statistics* reports such figures sporadically, and it is difficult to know how much of state and local expenditures on social spending is drawn from federal subsidies, and thereby already accounted for in the data.

[26] Note that the spending data used for the OECD countries in this chapter still have some missing values for state and local government.

[27] Wood (1997, 1995, 1994) emphasizes the importance of this distinction between low-skilled and skilled labor. He claims that trade is based on the availability of skills, not capital. Wood defines skilled workers as those with more than a basic general education – e.g. professional and technical workers, managers, and craftsmen (Wood, 1994: 6). Thus, skilled workers are generally employed in high-skill intensive manufacturing. "Low-skilled labor" refers to workers who have limited or no education (referring to both Wood's BAS-EDs and NO-EDs, respectively).

Table 2.4 *The growth and share of labor-intensive manufacturing exports*

	Growth 1992–6	Share of exports 1996
Low-income countries		
Primary products	12.7	60.1
Natural-intensive manufacturing	12.6	13.4
Labor-intensive manufacturing	18.9	14.6
Technology-intensive manufacturing	13.2	3.6
Human-capital-intensive manufacturing	14.7	2.8
Lower middle-income countries		
Primary products	9.4	56.6
Natural-intensive manufacturing	7.6	4.6
Labor-intensive manufacturing	14.8	20.8
Technology-intensive manufacturing	21.2	11.3
Human-capital-intensive manufacturing	11.6	6.0
Upper middle-income countries		
Primary products	9.0	49.23
Natural-intensive manufacturing	18.8	7.23
Labor-intensive manufacturing	10.5	13.46
Technology-intensive manufacturing	13.3	15.54
Human-capital-intensive manufacturing	9.8	12.00
High-income OECD countries		
Primary products	8.07	23.86
Natural-intensive manufacturing	10.21	4.79
Labor-intensive manufacturing	8.57	9.07
Technology-intensive manufacturing	12.14	35.47
Human-capital-intensive manufacturing	9.50	23.43

Source: UN ITC Infobase, "National Trade Performances by Country 1999."

demonstrates, in line with the Stolper–Samuelson theorem, the growth of labor-intensive exports relative to other exports in countries known to have large pools of low-skilled labor.

The most important point confirmed by the data in table 2.4 is that the poorer the country the greater the likelihood that participation in international markets will be led by exports of low-skilled manufactured goods. The lowest-income countries have clearly experienced the highest growth rates in labor-intensive manufacturing. Increasing international demand for low-skilled workers might make it more difficult to overcome collective action problems. The high-income OECD countries, in contrast, have both the smallest rate of growth and the smallest share of labor-intensive exports. It is no surprise, then, that employment in high-skilled relative to low-skilled jobs shows minimal growth in low-income countries. Figure 2.2 illustrates the striking contrast between developed and developing countries in this regard.

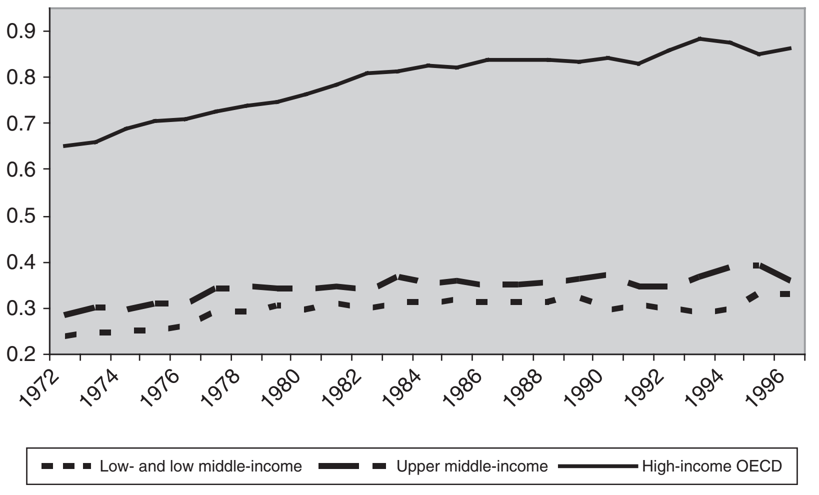

Figure 2.2 Ratio of high-skill employment relative to low-skill employment, 1972–97

According to the argument in this chapter, whether the accompanying increase in the number of low-skilled relative to skilled laborers employed in developing countries implies greater organizing capability for labor depends on the size of the surplus labor pool. Given the increasing trend in skilled labor in the middle-income countries, we can expect this capacity to increase *if* the surplus labor pool is shrinking. Figure 2.3 shows that there was indeed a slight decline in surplus labor in LDCs between 1972 and 1997, suggesting the possibility that labor power has improved. It cannot be overlooked, however, that, by the late 1990s, the level of surplus labor in LDCs was, on average, 24 percent of the working-age population, while in the OECD countries the average level was 7 percent of the working-age population. Moreover, the drop in less developed countries has only been an average of six percentage points. In sharp contrast, the level of surplus labor in Garrett's sample of OECD nations is less than a half what it was in the early 1970s. Several recent studies confirm that employment growth has failed to significantly reduce the vast amount of surplus labor that exists in the developing world (Schneider and Enste, 2002; Portes and Schauffler, 1993; UNIDO [United Nations Industrial Development Organization], 1992).

Given that the number of low-skilled laborers has been steadily increasing (since the mid-1980s) and that the developing world's surplus labor

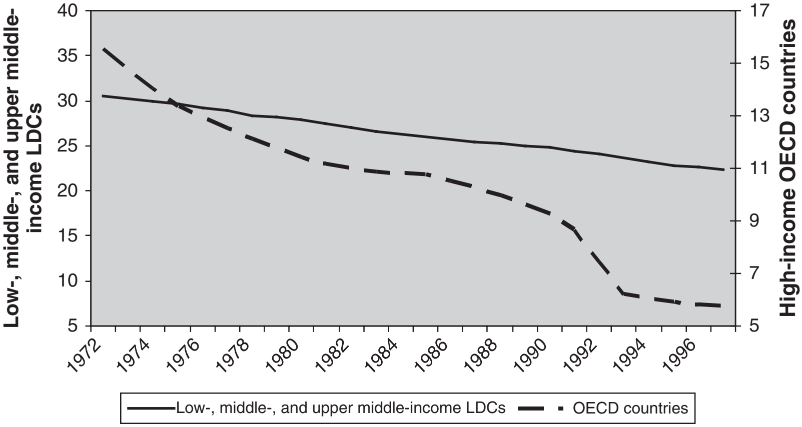

Figure 2.3 Surplus labor in LDCs and developed countries, 1972–97

Note: Surplus labor is calculated as [(working-age population – students enrolled in secondary education – students enrolled in tertiary education) – (labor force)]/working-age population.
Sources: World Bank, *World Development Indicators* (various years); ILO (2001).

population is still relatively high, the logic of Olson's theory suggests that labor market institutions will be unable to overcome their collective action problems in the current globalizing environment. To incorporate this idea, I have constructed an index of potential labor power. This is an indirect measure of labor power, used to capture the capacity of labor to form centralized, powerful labor organizations that are able, in turn, to form alliances with other interest groups, as well as more effectively negotiate with government and business representatives. The logic behind the index lies in the observation that the bargaining power of labor institutions is likely to improve with an increasing ratio of skilled to unskilled workers, given the greater capacity of the former for collective action, and decrease with the size of "surplus" labor, measured as the working-age population minus the economically active population and students in secondary and tertiary schools.[28]

In order to create the index, I divided each country's score by the highest value in the larger data sample (i.e. Sweden = 87) and multiplied by 100.

[28] This assessment of labor power is limited to the manufacturing sector, since data are not available for most countries outside this sector and, in any case, most labor organization takes place there.

Assuming that there is always some surplus labor and some low-skilled laborers, the PLP measure is:

$$PLP = \left[\frac{\left(\frac{\text{Number of skilled workers}}{\text{Number of low-skilled workers}} \right) \times \left(\frac{1}{\text{Surplus labor as percentage of working-age population}} \right)}{87} \right] \times 100$$

PLP falls as the number of low-skilled workers increases relative to skilled workers, and as surplus labor expands. To the extent that the surplus shrinks and labor markets become tighter, PLP increasingly depends on the ratio of skilled to low-skilled workers. Significantly, the logic of applying these direct measures of the structural conditions in labor markets as a way of assessing the extent of PLP is similar to Silver's (2003) "marketplace bargaining power" of labor. This type of bargaining power is the influence that "results directly from tight labor markets" (Silver, 2003). See appendix B for a more detailed explanation of the PLP variable.

Admittedly, PLP is an unconventional measure of labor's bargaining capacity. Garrett and other scholars capture the key features of OECD labor market institutions using existing measures of labor's negotiating and political power.[29] Unfortunately, such detailed data do not exist in the developing world. The most common method of assessing labor's potential political power in these countries is by unionization rates (Madrid, 2002; Devarajan, Ghanem, and Thierfelder, 1997; Galenson, 1994, 1962). A fundamental problem with this indicator, however, is that union density (the percentage of the working population that is unionized) is not comparable across countries in the developing world. Many LDC governments mandate compulsory membership in corporatist unions and impose constraints on labor's demand-making, leadership and internal governance (Collier and Collier, 1991). China, for example, has the highest union density in the developing world, yet labor has very little bargaining power (Chan and Senser, 1997). In general, unionization rates exaggerate labor's political strength in LDCs, and do not give any sense of the extent of "labor encompassment."[30] Moreover, no standardized cross-country time-series measures exist yet for a large number of developing countries. The next step is to employ an econometric test to

[29] Garrett (1998), for instance, captures labor market institutions in the OECD nations by operationalizing labor encompassment as union density and confederation share, and a political power measure that sums standardized scores for legislative and Cabinet-level government indicators. These two measures are aggregated to represent left–labor power.

[30] See, for example, Valenzuela (1989: 449) and Banuri and Amadeo (1991: 175). McGuire (1997) adds that unreliability in union data can result in huge discrepancies in existing cross-country compilations of union density estimates.

analyze more precisely labor's ability to mediate between the forces of globalization and pressures for welfare retrenchment.

2.3.3 Model specification

The argument that the character of labor market institutions moderates different (RTB) outcomes in poorer and richer countries is assessed in two stages. First, an LDC model examines the influence of both domestic- and international-level variables on government welfare expenditures to test the RTB hypothesis (see equation (1)). To check the robustness of the findings, each set of results is re-evaluated using an alternative measure of social spending. Second, equation (1) is reapplied to developed countries using Garrett's (1998) model to confirm whether or not the labor variable drives the differential welfare state outcomes in developing and developed countries.

I use both country and decade dummy variables to control for country-specific and time-specific fixed effects. Following Kaufman and Segura-Ubiergo (2001), I use decade rather than year dummies to account for the important differences in international conditions over the course of our time period. The years 1972 to 1979 cover the period prior to the debt crisis, while 1980 to 1989 were years generally marked by economic recession and painful structural adjustments. The final eight-year span (1990–7) covers the period of economic recovery that took place.

Based on econometric techniques advocated by Beck and Katz (1995), I correct for both panel heteroskedasticity and spatial contemporaneous autocorrelation. In addition, problems of potential serial autocorrelation within each panel are addressed by estimating and adjusting for a panel-specific AR(1) (first-order autoregressive) process. This model follows Achen's (2000) recommendation against applying the standard practice of simply using a lagged dependent to correct for serial autocorrelation. These results provide Prais–Winsten coefficients with panel-corrected standard errors (PSCEs).

2.3.3.1 The LDC model

$$\begin{aligned}(1)\ \Sigma \text{welf}_{it} = {} & b_1\text{PLP}_{it} + (b_2\text{trade}_{it-1} \times \text{PLP}_{it}) + (b_3\text{portfolio}_{it-1} \times \text{PLP}_{it}) + \\ & (b_4\text{fdi}_{it-1} \times \text{PLP}_{it}) + b_5\text{trade}_{it-1} + b_6\text{portfolio}_{it-1} + b_7\text{fdi}_{it-1} + \\ & \Sigma(b_j\text{X}_{jit-1}) + \Sigma(b_k\text{country}_{ki}) + \Sigma(b_l\text{decade}_{lt}) + \mu_{it}\end{aligned}$$

Three different dependent variables are included in "welf": public expenditures on social security and welfare; spending on education; and spending on health. The *b*s are parameter estimates in this equation, while the subscripts *i* and *t* represent the country and year of the observations, respectively; $\sum X$ represents the vector of control variables. The globalization variables ("trade," "portfolio" [portfolio flows], and "fdi") are lagged in order to take the period of "adjustments" into account.[31] Consistent with Garrett (1998), this model uses pooled cross-section and time-series data to estimate the results.[32] This estimation procedure has two benefits. First, the use of the fixed-effects model makes it possible to control for unobservable country-specific differences, eliminating much of the omitted variable bias of cross-section data.[33] Second, important changes that have occurred over time in the same country can be assessed. Using panel data ultimately combines the benefits of an increased number of observations with the ability to account for country-specific fixed effects.

The developing country model is estimated in three ways, and the results are reported in table 2.5 and appendix C. Model 1 reflects equation (1), using all three globalization indicators as causal variables. Model 2 drops FDI and re-estimates the model, since studies have shown that trade and FDI are correlated (Albuquerque, Loayza, and Servén, 2005; Aizenman and Noy, 2006). Finally, model 3 applies the two-stage least squares (2SLS) method to adjust for measurement error in the labor variable.

2.3.4 The variables

2.3.4.1 Dependent variable: social spending on education, health, and social security and welfare [WELF] The selection of social security and welfare, education, and health as the primary categories to assess welfare effort in developing countries follows the standard approach in the current literature (see, for example, Kaufman and Segura-Ubiergo, 2001, and Avelino, Brown, and Hunter, 2005). The social security and welfare variable captures traditional transfers and particularly pensions, and education and health represent spending on human capital investments. Each

[31] Theoretically, it is more sensible to anticipate a lagged effect, because international market occurrences take time to affect policy outcomes. See, for example, Rodrik (1997a), who uses lagged measures of openness.

[32] Note that, as emphasized earlier, this is an unbalanced data set for LDCs.

[33] For example, informal systems of old age support (i.e. extended families) are common methods of providing social security in many parts of Africa and Asia (see World Bank, 1994). Such variables are more significant in some countries than others. The fixed-effects model allows us to control for the influence of such idiosyncratic differences between countries without having to model them explicitly.

of these measures incorporates somewhat different welfare functions. The proportion of the budget devoted to social security and welfare captures what are sometimes called "uncompetitive" types of spending and transfers, a category that should be in greatest jeopardy given the "efficiency" pressures of globalization. Spending on education and health, by contrast, reflects the priority that governments give to human capital development, and could well be complementary to the demands of globalization. For example, increasing levels of FDI and trade might generate efforts to improve efficiency and, thereby, stimulate demand for better education and health systems. I examine each of these categories of spending as a share of GDP and on a per capita basis.

2.3.4.2 Primary causal variables: the interaction of economic globalization and labor power (PLP) in LDCs [TRADE × PLP, PORTFOLIO × PLP and FDI × PLP][34] At the heart of this study is the idea that globalization's effect on social spending depends on the character of labor market institutions in developing countries. The conventional measure of trade openness, exports plus imports relative to GDP, is incorporated in this model. The primary explanatory variables are the interactive effects of globalization and labor power. These interactive variables, by design, replicate Garrett's (1998) model of the globalization–spending relationship in the developed economies. Trade, net FDI flows, and portfolio flows as a percentage of GDP are combined with PLP in order to assess the extent to which existing labor market conditions can help moderate the globalization–welfare spending relationship. If the interactive effects of globalization and PLP are negative then it can be determined that the combined effects of low levels of PLP with increased exposure to higher levels of trade and capital flows result in lower government welfare commitments.

One particular caveat should be kept in mind: surplus labor may be over- or underestimated, depending on the actual age of the working population. The World Bank's metric of the "working-age population" is based on OECD standards. The value will be underestimated in countries where workers in the informal sector begin to engage in money-making activities well before the standard working age of fifteen

[34] Note that, following Braumoeller (2004), I run model 2.2 including triple interactions, since the inclusion of PLP in both interaction terms creates a "tacit interaction" between trade and the capital flows variable. The primary findings are not affected; the conditional coefficients are significant at the ninety-fifth percentile confidence level (see footnote 42 for details on calculation). For ease of presentation, the triple interaction results are not included here.

(to sixty-four) – i.e. child labor. Conversely, in developing countries where the retirement age is commonly under sixty-four, surplus labor may be overestimated. To address this measurement error, I apply the Lewbel (1997) method and re-estimate equation (1) using 2SLS (see model 2.3).[35]

2.3.4.3 Control variables: age dependency, youth population (population zero to fourteen years of age), elderly population (sixty-five and older), urbanization, debt, GDP per capita, growth, democracy, ethnic fragmentation and region dummies Several control variables help isolate this main relationship and check for other influences on welfare. Given that most nations in this sample are considerably underdeveloped, supplementary political and economic variables are included in order to tailor the model to these cases. Previous studies of developing country welfare spending have found that it increases with the number of young and aged dependents (World Bank, 1994; Esping-Andersen, 1990; Tang, 1996; Schmidt, 1995); the level of urbanization (Tang, 1996); both GDP per capita and growth (Brown and Hunter, 1999; Usui, 1994; Rodrik, 1997a, 1998; Tang, 1996); low debt (Schwartz, 1998); and democracy (Rudra and Haggard, 2005, Brown and Hunter, 1999; Atkinson and Hills, 1991; Eichengreen, 1996; Hicks and Swank, 1992). Unemployment figures, frequently linked to higher welfare expenditures in developed countries, are excluded because of the unreliability of such figures in developing nations (see Agenor and Montiel, 1996). I drop urbanization because of its high correlation with GDP. The percentage of the population aged over sixty-five (the elderly) is included in the model for human capital because care for the elderly is said to account for the greatest percentage of health expenditures. By the same logic, I control for the size of the youth population (ages zero to fourteen) in the education model.

[35] The conventional method for coping with this measurement error and mitigating the bias of the regression estimates is to use the instrumental variable approach. The difficulty, however, lies in finding outside data or instruments that are uncorrelated with the error of the equation but at the same time highly correlated with the explanatory variables. Therefore, as a solution to the insufficient instruments problem, Lewbel (1997) proposes using second and third moments of variables as instruments. For example, following Lewbel, if x_i is an element of the X matrix, then $q_i = (X_i - \text{mean}(X))^2$ is a legitimate instrument in addition to the x_i variables, and the instrumental variables estimator is consistent. Note that the Lewbel method has also recently been applied to solve problems of endogeneity (see Cheng *et al.*, 2006, and Ebbes, 2004; personal communication with Cheng Hsiao). The following variables also serve to construct the instrument: manufactured exports, service exports, portfolio flows, urbanization, debt, democracy, and economic growth.

Ethnic fragmentation and regional diversity could also play a role. Spending on public goods such as education tends to be low in countries where ethnic groups are polarized (Alesina, Baqir, and Easterly, 1999).[36] Since, technically, everyone has access to public goods, this research suggests that, in ethnically fragmented societies, one ethnic group will resist tax revenues that will provide public goods shared by other ethnic groups. Scholars such as Haggard and Kaufman (forthcoming) argue that regional factors (e.g. international political developments after World War II that weakened labor and the left in east Asia) can affect the level of spending.[37] To test the effects of ethnic fragmentation (which, according to the data, tends to be static), I first include it as a fixed effect. These results are difficult to interpret, however, since country fixed effects cannot be included at the same time.[38] I also test the impacts of regional dummies. In the end, however, after confirming that the exclusion of neither of these two variables drives the primary results, I opt to drop them from the final model and include only the country fixed effects; the latter absorb much of the explanatory power of ethnic fragmentation and region.

2.3.5 Results

Model 2.1 is re-estimated using different dependent variables to check for robustness: welfare as a percentage of GDP and per capita welfare spending. Equation (1) is estimated for fifty-nine developing countries, from the years 1972 through 1997, using the fixed-effects procedure (see table 2.5). Ultimately, in support of the race to the bottom hypothesis, social security and welfare is the variable that is the most sensitive to variations in international level variables, particularly trade openness. The combined effect of PLP and openness, as predicted, is negative and highly significant across the models for social security and welfare. The impact of the globalization

[36] Fragmentation (or *fractionalization*) is defined as “the probability that two individuals selected at random from a country will be from different ethnic groups” (Fearon, 2002: 21). ETHFRAC was compiled by Soviet ethnographers in 1964 and published in the *Atlas Narodov Mira*. The Soviets considered language to be the main way to distinguish ethnicities; accordingly, ETHFRAC captures ethnolinguistic fractionalization. Fearon (2002) codes EF with a slightly different coding scheme; he argues that different ethnic groups may speak the same language, but are ethnically very different. The two measures are highly correlated, but capture slightly different conceptualizations of fractionalization.

[37] Note that the inclusion of both country and regional dummies does not affect the results. In model 2.2, the east Asian dummy is negative and significant, and the Latin American dummy is positive and significant (compared with the Middle East, the omitted category).

[38] Linear dependency problems occur when both country fixed effects and ethnic fragmentation variables are included.

variables on education and health, in contrast, is not as robust. When all relevant domestic variables are controlled for, the results reveal that labor market institutions in the developing world are unable to prevent a race to the bottom in social security and welfare.

2.3.5.1 The LDC globalization–welfare model Table 2.5 illustrates how trade openness combined with PLP displays the strongest effect on social security and welfare spending. Interestingly, although PLP has a positive and independent effect on social spending (hypothetically, when trade equals zero), it is less effective when faced with international market pressures, particularly trade openness. The pattern of coefficients for the trade openness–PLP interactive variable is fairly consistent across the different models, suggesting that these findings are quite robust. In contrast, based on the conditional coefficients, neither of the FDI and portfolio interactive terms have consistent effects on SS and welfare spending. The portfolio–PLP coefficient is negative and significant, and the FDI–PLP coefficient is positive and significant in model 2.3 only, providing cautious support for the effects of these globalization variables.[39] Nevertheless, the negative coefficients of the trade openness interactive terms across the different models provide strong confidence in the finding that SS and welfare expenditures are indeed a function of high levels of exposure to global market activity and relatively weak labor power. These results cast doubt on previous analyses of welfare spending that have focused only upon domestic variables and downplayed the importance of international level variables in their analyses.[40]

In contrast, the effects of the globalization variables on health and education expenditures are ambiguous (see appendix C for the results tables on education and health spending in LDCs). The portfolio–PLP interaction variable appears to have a positive effect on education spending; we cannot be confident about this result, however, since it does not hold up to tests of robustness. The same holds true for the health spending models. None of the globalization variables had a consistent effect on government health expenditures as seen in the social security and welfare models. The trade–PLP coefficients flip signs within models 2.1, 2.2, and 2.3. These findings, taken together, suggest that international-level

[39] Testing significance levels (model 2.1) reveals that conditional coefficients on portfolio flows are insignificant when the levels of trade and FDI flows are high. Similarly, FDI is also insignificant when trade and portfolio flows are high.

[40] See, for example, Schmidt (1995), Tang (1996), Midgley (1984), Wahl (1994), and Atkinson and Hills (1991).

Table 2.5 *Social security and welfare spending in LDCs*

	Model 2.1		Model 2.2		Model 2.3	
	SS and welfare (% GDP)	SS and welfare per capita	SS and welfare (% GDP)	SS and welfare per capita	SS and welfare (% GDP)	SS and welfare per capita
PLP	0.20**	12.53***	0.19**	12.21***	0.48***	11.88***
	(0.09)	(3.97)	(0.08)	(3.85)	(0.12)	(3.99)
$Trade_{t-1} \times PLP$	−0.002*	−0.10***	−0.002*	−0.11***	−0.005***	−0.15***
	(0.001)	(0.04)	(0.001)	(0.04)	(0.002)	(0.04)
$Portfolio_{t-1} \times PLP$	−0.016	−0.28	−0.016	−0.22	−0.05***	−1.14*
	(0.016)	(0.74)	(0.015)	(0.70)	(0.02)	(0.60)
$FDI_{t-1} \times PLP$	0.005	−0.55***	–	–	0.17***	2.42***
	(0.004)	(0.21)			(0.04)	(0.94)
$Trade_{t-1}$	0.004	−0.10	0.004	−0.08	−0.001	−0.27**
	(0.004)	(0.12)	(0.005)	(0.12)	(0.005)	(0.12)
$Portfolio_{t-1}$	0.12	5.03	0.12	4.84	0.18**	6.65**
	(0.08)	(3.97)	(0.08)	(3.89)	(0.07)	(3.34)
FDI_{t-1}	0.002	1.24*	–	–	0.02	0.19
	(0.021)	(0.70)			(0.04)	(1.06)
GDP per capita	−0.73*	67.43***	−0.69*	65.02***	−1.26***	0.04***
	0.39	(12.05)	(0.39)	(11.75)	(0.43)	(0.01)
Growth	−0.007	−0.23	−0.008	−0.21	−0.004	−0.30
	(0.006)	(0.19)	(0.006)	(0.19)	(0.007)	(0.26)
Democracy	0.20	11.42	0.19	11.54	0.04	3.91
	(0.16)	(7.38)	(0.16)	(7.36)	(0.19)	(8.35)
Dependents	−1.52	9.44	−1.48	11.62	−0.45	68.07
	(1.06)	(39.35)	(1.04)	(39.94)	(1.25)	(42.62)
$Debt_{t-1}$	−0.005***	−0.14**	−0.006***	−0.15***	−0.004	−0.07
	(0.002)	(0.06)	(0.002)	(0.06)	(0.003)	(0.08)
R^2	0.71	0.69	0.70	0.68	0.74	0.78
N	750	750	754	754	591	591

Notes: *** = $p < 0.01$; ** = $p < 0.05$; * = $p < 0.10$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

variables have inconclusive effects on the level of public resources allocated towards health and education spending.[41]

It is intriguing that globalization leads to a race to the bottom in social security and welfare, but not education and health. Why might international economic factors have a more constraining effect on the former? Arguably, assessing SS and welfare spending alone in response to globalization is a more precise test of the RTB hypothesis. This type of expenditure has a direct impact on firms' bottom line, since this program is most often funded by payroll taxes, and, as stressed by many, it can have a negative effect on the productivity of workers (see World Bank, 1994). On the other hand, while supporting high levels of health and education expenditures can affect interest rates and tax rates and thereby encourage a race to the bottom, this type of spending has less impact on total wage costs. Disentangling the pressures of globalization on health is more complicated, however, since funding for health care can be provided by payroll taxes as well as by the government. Regardless, the findings suggest that the politics of social security and welfare differ markedly from the politics of health and education spending. This relationship is investigated in greater detail in chapter 3.

The best way to make sense of these results and understand the impact of PLP on welfare at various levels of globalization is to refer back to equation 1 and estimate the effects of the conditional coefficients.[42] Figure 2.4 graphs the effects of PLP on SS and welfare spending at different levels of openness.

The overall impact of labor power on social spending, contingent upon the level of globalization, exhibits diminishing returns. As revealed in figure 2.4, the ability of PLP to defend SS and welfare spending is mitigated as openness increases. In fact, calculating the effects of openness in another way – contingent upon levels of PLP – reveals that, overall, PLP levels in developing countries are too low to have an effect on welfare spending *as globalization occurs*.[43] The data thus support the existence of a relationship between globalization and cutbacks in welfare spending in developing economies.

41 When the health and education models are re-estimated without the globalization variables, the GDP per capita, demographic, and debt variables have more consistent effects.

42 Basing the estimations on model 2.1, the effect of increasing PLP on social security and welfare spending conditional on trade, portfolio, and FDI has the form: $\partial \text{welf}/\partial \text{PLP} = 0.20 - 0.002 \times \text{trade}_{\text{it}-1} - 0.016 \times \text{port}_{\text{it}-1} + 0.005 \times \text{FDI}_{\text{it}-1}$. Note that portfolio and FDI values are held constant at their means in order to estimate the impact of changes in trade.

43 As an example, again using model 2.1, the estimated effect of PLP on SS and welfare spending conditional on trade has the form: $\partial \text{welf}/\partial \text{trade} = 0.004 - 0.002 \times \text{PLP}_{it-1}$ and shows no significant effect.

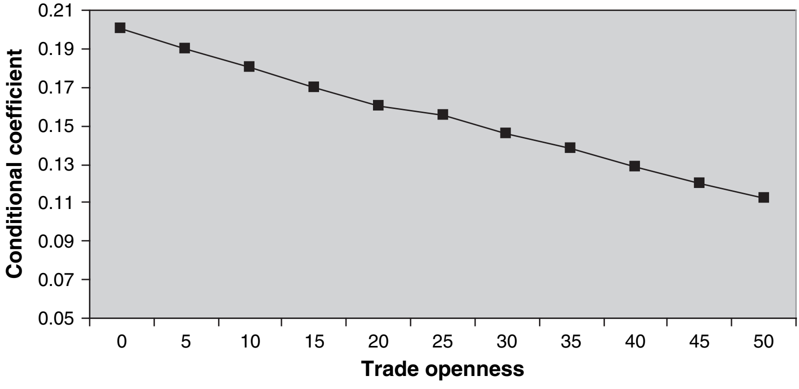

Figure 2.4 Conditional effect of PLP on social security contingent upon levels of openness

Notes: Portfolio flows and FDI are held constant at their means. The conditional coefficients are significant at the ninety-fifth percentile confidence level.

The findings with respect to the impact of some of the control variables, particularly the debt variable, reveal the importance of alternative political and economic influences on social spending, while controlling for international effects. It is surprising that democracy has no noticeable effect, particularly in light of recent analyses that emphasize its importance to social spending (Brown and Hunter, 1999; Rudra and Haggard, 2005). One difference is that the current model incorporates the insights of the welfare state literature and emphasizes the responsibility of labor market institutions in mediating the effects of globalization. Nonetheless, the extent of empirical evidence in support of the democracy–social spending relationship casts doubt on the conclusion that democracy has *no* effect on government social spending commitments. I return to this issue in the case studies in an attempt to make sense of these results.

In summary, the developing country data support the race to the bottom hypothesis with respect to social security and welfare. The weak power of labor market institutions in LDCs is unable to mitigate RTB pressures as globalization, particularly in terms of trade openness, advances. As predicted, their product terms are mostly negative and significant in developing economies. Is the character of labor market institutions in the developing world, represented here by PLP, the key mediating domestic variable that determines the different RTB outcomes in developing nations?

2.3.5.2 The comparison of RTB in LDCs and OECD countries Estimating a similar globalization–welfare model for developed countries emphasizes the importance of differences in the overall strength of labor market institutions. Findings in this section confirm that, unlike their counterparts in the developing world, institutions in the more developed countries are strong enough politically to encourage welfare state expansionism alongside globalization. This contrast between the two sets of countries is observed by adopting Garrett's (1998) globalization–welfare model for OECD nations and substituting the PLP variable for his labor variable, and then comparing the results with the developing countries. These final regressions have two important implications. First, since the results using the PLP variable in developed countries are similar to Garrett's results using his indicator of left–labor power (LLP), these regressions considerably increase confidence in the reliability of the PLP variable.[44] Second, a positive coefficient for the globalization–labor interactive variables corroborates the disparity in centralized bargaining power in the two sets of countries. These findings verify that the contrasting effects of globalization on welfare states in developed and developing countries are rooted in overall differences in labor market institutions.

The interactive globalization–PLP variable is expected to be positive in developed countries. Not only do richer nations face rather less severe collective action problems, but they also have institutions in place to help surmount them. Surplus labor problems are simply not as acute in the more developed countries. Labor markets in these countries tend to be much tighter. In addition, the pool of low-skilled laborers relative to the more skilled laborers in OECD countries has been steadily declining, suggesting that their collective action problems may be more easily overcome. It is no surprise that the average PLP in the advanced industrialized countries is eight times higher than the developing country average of PLP.[45] Finally, these are nations with long-standing liberal democratic traditions. Other welfare beneficiaries (e.g. the aged and the disabled) are also able to form strong interest groups and thus make it increasingly difficult for the government to roll back welfare spending.

Table 2.6 applies Garrett's welfare model to the high-income countries, but substitutes the PLP variable for his measure of LLP (for the corresponding education and health spending regression results, see appendix C). Additional control variables used in Garrett's (1998) analysis are GDP growth, the proportion of the population over sixty-five years

[44] See Campbell's (1988) tests for evaluating the validity of variables measuring a concept.
[45] Average PLP in the OECD countries is 9.8. The LDCs' average PLP is 1.2.

Table 2.6 *Social security and welfare spending in OECD countries*

	Model 2.4		Model 2.5	
	SS and welfare (% GDP)	Welfare per capita	SS and welfare (% GDP)	SS and welfare per capita
PLP	0.03	−0.81	0.008***	2.33***
	(0.02)	(5.09)	(0.002)	(0.67)
$Trade_{t-1}$ × PLP	−0.0003	0.05	–	–
		(0.08)		
$Portfolio_{t-1}$ × PLP	0.09*	33.62**	0.10*	31.36**
	(0.05)	(15.51)	(0.05)	(15.04)
FDI_{t-1} × PLP	0.007***	2.00***	0.007***	1.87***
	(0.002)	(0.65)	(0.002)	(0.62)
$Trade_{t-1}$	−0.05**	−20.57***	–	–
	(0.02)	(5.06)		
$Portfolio_{t-1}$	−6.07	−2339.20	−5.60	−2031.83
	(5.69)	(1579.51)	(5.61)	(1534.37)
FDI_{t-1}	−0.44**	−49.07	−0.55***	−62.31
	(0.21)	(62.58)	(0.20)	(58.18)
Growth	−0.08***	−1.87	−0.10***	−3.51
	(0.03)	(9.64)	(0.03)	(8.83)
Elderly population	0.74***	384.07***	0.78***	420.74***
	(0.19)	(63.91)	(0.21)	(74.17)
Unemployment	0.41***	62.95***	0.43***	66.74***
	(0.06)	(14.55)	(0.06)	(14.52)
R2	.93	.90	.88	.86
N	348	348	348	348

Notes: *** = p < 0.01; ** = p < 0.05; * = p < 0.10. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

old (POP65), and unemployment. Model 2.3 is not included here since PLP is subject to less measurement error in the developed countries.[46]

This final set of regressions closely replicates Garrett's results and appreciably strengthens the conclusions of this chapter. Comparing the results from the LDCs suggests that the developed countries have more effective labor market institutions and therefore the requisite political muscle to protect citizens from the adverse impacts of globalization. In nations exporting rather more skill-intensive goods, the product terms of the capital flow variables and PLP tend to be positive (see table 2.6 and

[46] The working-age population reported by the World Bank more or less corresponds to the working-age population in OECD countries.

tables C.1 and C.2).[47] In addition, in agreement with Pierson (1996), the significance of the aged population and unemployment variables indicate that labor is only one of several welfare beneficiaries that can successfully resist government penchants for welfare state retrenchment. Interestingly, in a manner similar to the results for the developing countries, globalization had less consistent effects on health and education spending (see tables C.3 and C.4).

The coefficient of trade interacted with PLP is anticipated to be insignificant in more developed nations. According to Schwartz (1998) and Huber and Stephens (1998), trade openness has a much weaker effect on social democracies than the internationalization of productive and financial capital. Increases in trade dependence have been modest in comparison to their rapid integration into financial markets over the last two decades. To account for the special characteristics of globalization in OECD countries, and because FDI and trade tend to be correlated, model 2.5 excludes trade instead of FDI. In direct contrast with developing countries, the social security and welfare model confirms expectations that RTB anxieties are not justified in the developed countries.

These findings more fully expose the explanatory power of the mediating variable, PLP. The appropriateness of applying this measure of the strength of labor market institutions to assess changes in government welfare expenditures in this era of globalization is confirmed. The results are consistent with Garrett's fully specified model, which demonstrates the positive effects of globalization in countries that do not enjoy a comparative advantage in labor. Thus, the statistical evidence presented in this chapter supports the argument that domestic institutional differences between rich and poor countries, especially those involving labor, drive contrasting race to the bottom outcomes in the current era of globalization.

2.4 Summary

This chapter demonstrates that, in direct contrast to the developed countries, developing nations are more vulnerable to race to the bottom pressures. Specifically, the investigation of fifty-nine developing countries from 1972 through 1997 indicates that social security and welfare spending is more responsive to openness than it is to increases in productive and financial capital flows. These findings challenge the emerging consensus

[47] Note that both the globalization variables (trade × left–labor power and capital mobility × left–labor power) are positive and significant in Garrett's central model of total government spending.

that fears of a race to the bottom are overblown. Rather, globalization affects welfare spending in the developed and developing nations differently because of the contrasting characteristics of their domestic institutions, most particularly labor market institutions. In the OECD countries, the organizing capacity of labor is relatively strong, and existing institutions can help workers overcome their collective action problems. In LDCs, however, the general trend has been a growing number of low-skilled workers relative to skilled workers. This factor, coupled with large surplus labor populations, exacerbates the collective action problems of labor, and makes it increasingly difficult for workers to mobilize systematically. Consequently, when confronted with the pressures of globalization, labor institutions in the developing world are less capable of defending their welfare benefits.

The findings in this chapter suggest that the difference in welfare state outcomes is due to a wide disparity in the encompassing nature of labor market institutions in developed and developing countries. Developing states appear to have some leeway in directing health and education expenditures, while the same cannot be said of social security and welfare. The exact reasons for this are not yet clear and warrant further investigation in the following chapters. Ultimately, in a globalizing economy, workers' prospective political gains from expanded trade and investment are outweighed by their inability to pressure the government collectively or cooperatively for social programs in their favor.

This chapter clearly demonstrates that LDCs lack encompassing labor organizations and, hence, their labor market institutions are unsuccessful at advancing policy compromises between government, business, and labor in the globalizing environment. One question remains unanswered, however: can select labor groups exert influence on particular social policies? If possible, how might particular pockets of labor groups exert such influence in developing countries? Leaders of decentralized labor groups clearly have fewer incentives and less institutional backing to care about the welfare of the whole labor force. Narrow groups of organized and skilled (and even low-skilled) workers in the formal sector can take advantage of their bargaining position and prevent the marginalized labor groups from obtaining any benefits. The ramifications of this insider–outsider problem receive closer attention in the following chapter.

3 Who really gets hurt?

Chapter 2 has established that the fragmented character of labor market institutions in developing countries makes it more likely that the governments of these nations will respond to race to the bottom pressures. Based on this evidence alone, globalization pessimists might claim that their fears are validated, and it is the end of domestic politics in the developing world; the zero-sum dichotomy between states and markets has been confirmed. But the analysis cannot stop here. What is really driving anxieties about globalization amongst academics, activists, and policy-makers is the concern that the race to the bottom hurts the poor. The fight in this case is not for (or against) domestic politics per se, but for the benefit of the less privileged.

This chapter goes a step beyond analyzing the capacity of labor to overcome collective action problems and negotiate policy compromises under globalizing conditions, and observes the effects of domestic institutional arrangements supporting government–labor relations. This approach reveals that the effects of international free-market competition are much more complex than is commonly assumed. While globalization is certainly increasing RTB pressure on less developed countries, the long-time policy interactions between government and *select* labor groups have engendered a set of social policies that were never designed to help the poor in the first place. Rather, the more privileged classes traditionally receive these benefits, and are therefore the immediate victims of any cutbacks. The findings in this chapter thus challenge the widespread perceptions that the poor are the primary targets of the unbridled race to the bottom in developing countries.

Simply observing whether the level of social spending is decreasing or increasing does not reveal the complete picture about who is being affected, either adversely or positively. Analysts who specialize in the comparative politics of developing countries provide important reasons to be skeptical of the effects of LDC welfare programs (Mesa-Lago, 1994; Weyland, 1995, 1996a, 1996b; Huber, 1996; McGuire, 1999). According to these scholars, such schemes disproportionately benefit economically and politically privileged labor groups in developing nations, such as higher-skilled blue-collar and salaried workers, and do not serve the goals of poverty alleviation. The maldistribution of benefits reinforces the divisions in the labor movement discussed in chapter 2. Nevertheless, it is still commonplace for scholars to extol the virtues of greater social spending. Resources devoted to this type of safety net purportedly protect citizens from the adverse effects of globalization, such as increasing economic uncertainty, poverty, and inequality.

There is clear reason to be cautious about the effectiveness of social spending, since a majority of relatively open developing countries continue to have high levels of inequality, in spite of the fact that most have attempted to implement some form of redistribution policies. This is particularly puzzling given that, over time, LDCs that have spent the highest amount on these welfare programs are the ones that, according to some measures, continue to be the most unequal (e.g. Brazil, Chile, Botswana).[1] The next step, then, is analyzing the distributional consequences of social spending to determine if government social commitments do in fact protect the disadvantaged from the risks and uncertainties associated with international market integration.[2]

In comparison, the efficacy of social spending in the countries of the OECD is a rather less contentious question. Esping-Andersen (1990) illustrates that, within the OECD nations, the social democratic welfare states in particular do quite well in balancing market-oriented, social welfare policies and a more equitable distribution of income. Social policies are strongly embedded in their domestic structure, institutions, and politics (Katzenstein, 1985; Pierson, 1996; Garrett, 1998).[3] The challenge ahead is to determine whether LDC social spending, which has typically favored more privileged labor groups, can be affected by the race to the bottom and yet still be reconstructed in ways that will improve the lives of all citizens. The objective of this chapter is thus twofold: (1) to resolve whether social spending helps improve conditions

[1] These countries have the highest Gini coefficients in the sample used in this analysis.

[2] By the "disadvantaged," I refer mostly to the poorest segments of the population, such as low-skilled and informal-sector workers. Since these groups have little economic security in LDCs (reliable employment, transferable skills, insurance mechanisms, assets, etc.), they are arguably the most affected by the risks imposed by globalization.

[3] The terms "embeddedness" and "disembeddedness" are derived primarily from Polanyi's (1944) *The Great Transformation*. In embedded economies, the market (and the institutions associated with it) is seen as integrated with all aspects of human life (political and social). In other words, developing *free* markets does not systematically dominate the policy agenda, and state-led social development (e.g. quality of life issues) assumes an equally important political priority. The policy agenda in a disembedded economy, on the other hand, tends consistently to favor either state intervention or the free market.

for the poor or is being directed towards the better off in developing countries; and (2) to determine if international market pressures push governments to engage in equity-enhancing reforms.

To address the issue of the redistributive nature of developing country social policies in this era of globalization, this chapter is divided into four sections. Section 3.1 establishes why evaluating the redistributive impact of social spending is essential to evaluate the merits and concerns of the RTB debate. Section 3.2 analyzes the relationship between globalization, welfare spending, and income distribution in the more developed economies, and then compares the results to developing countries. The primary questions are: (1) whether international market expansion has had a negative effect on income distribution in developing countries, as is so often proclaimed by globalization critics; and (2), if so, whether social spending is an effective tool to tackle it. This section reinforces an important theme from chapter 2: that citizens of developing nations face different prospects and challenges from those of richer countries as markets expand. In section 3.3, I question if any of the categories of social spending (education, health, and/or SS and welfare) are undergoing equity-enhancing reforms alongside globalization. To uncover answers to these questions, I employ two-stage least squares time-series cross-sectional estimations on thirty-five developing countries and eleven high-income OECD nations, covering data from 1972 to 1996.[4] To interpret the results in section 3.3, section 3.4 draws on the insights of the rational choice literature and illustrates how institutional constraints stemming from the historical government–labor relationship can help explain the effects of social spending on income distribution in a globalizing economy.

The findings in this chapter reveal several interesting patterns. To begin with, income distribution tends to be much more sensitive to trade flows in developing countries than it is in the more industrialized nations. The results indicate that increasing amounts of trade worsen income distribution in the developing world *if* the government does not engage in certain types of social spending to alleviate it. Capital flows, in contrast to trade flows, have a minimal effect on inequality in both sets of countries. Finally, while it is heartening that *all* three categories of social spending help improve income distribution in OECD countries, the effects of social

[4] Note that this is an unbalanced data set. Continuous inequality data for LDCs are sparse. I use yearly data in order to make use of every observation and to capture (when possible) the effects of annual changes that averages can miss. The LDC and OECD samples in this analysis both include all countries for which it is possible to obtain comparable data on income distribution and social spending.

spending are much less favorable in globalizing LDCs. Only spending on education encourages a more favorable distribution of income as the market expands, while health spending shows a weaker effect on improving equality in the globalizing environment, and SS and welfare expenditures in developing countries actually worsen income distribution. The results in this chapter are at odds with much of the World Bank literature, which argues that most types of government social spending are regressive or, at best, inefficient in developing countries.

Ultimately, this chapter emphasizes how the constraints and inducements of globalization affect the redistributive impact of certain types of social spending. Redistributive education policies are encouraged as economies open up, because their benefits are well known and are consistent with the normally divergent policy preferences of different social actors (e.g. capitalists, workers) striving to cope with the competitive pressures of globalization. Investments in programs that are typically financed through payroll costs, however, such as health and SS and welfare, are subject to greater political lobbying and clientelism. These latter benefits have typically been used by governments to manipulate and bolster their relationship with particular labor groups and thereby help reinforce the fragmented nature of labor market institutions in developing nations. Cross-class alliances are thus more likely to form in favor of education reform, over and above progressive changes in other social welfare programs.

3.1 Importance of the distributive effects of social spending in developing nations

The question of whether social spending helps improve the incomes of the poor in an era of rapidly expanding markets is vital for race to the bottom analyses. The RTB theory suggests that globalization severely constrains the ability of nations to pursue policies that protect the most disadvantaged groups. Chapter 2 clearly demonstrates that globalization curtails the expansion of some categories of social welfare. Is it also the case, however, that these welfare programs protect the poorer sectors of society as is commonly assumed? More specifically, do domestic institutions in developing countries support SS and welfare, education, and health programs that promote pro-poor redistribution?

Two important repercussions arise if social spending in developing countries is primarily directed towards more privileged groups rather than improving the lives of the poor. First, many of the anxieties about globalization and the race to the bottom have been misdirected towards only international-level variables; we have to take a much closer look at domestic politics and institutions to explain actual social welfare outcomes (e.g. worsening income inequality). Second, simply expanding the social budget will not help resolve distributional problems.

In the developed world, maintaining welfare states is both a preferred and viable strategy as these nations move towards greater market integration. Scholars argue that a race to the bottom must be avoided since social spending that protects the disadvantaged can be an asset to the economy (i.e. it provides greater social stability and political support for globalization policies) as openness occurs. Additionally, since research shows that the polities of the more advanced nations are relatively insulated from international political and economic pressures, the politics of social spending is less likely to be affected by globalization.

Welfare politics appears to be somewhat more vulnerable to international market conditions in the developing world, however. Scholars have argued not only that welfare spending in developing nations tends to be regressive (Malloy, 1979, 1993; Huber, 1996), but, as suggested in chapter 2, collective action problems inhibit the capacity of labor market institutions to demand more redistributive-type spending, particularly under conditions of globalization. It is therefore important, when analyzing the full extent and consequences of the race to the bottom, to investigate the possibility that LDC welfare programs actually protect the better off from the risks associated with an open economy. If this is the case, fears of declining social spending must be put into proper perspective. By the same logic, both globalization pessimists and optimists should be cautious about drawing the conclusion that countries with increasing levels of social spending are necessarily doing well for their poorest citizens.

3.1.1 Links between globalization, welfare spending, and inequality in OECD countries

For over two decades scholars have explored the dynamics behind the globalization–welfare relationship in more developed countries. Until recently the conventional wisdom has been that international market pressures would force the ultimate demise of the welfare state, because this type of government is costly and obstructs growth and efficiency efforts. Globalization scholars have now rejected this hypothesis in developed economies, however, and find that welfare spending can, in fact, *benefit* markets by increasing productivity and attracting capital.[5] For this

[5] Garrett (1998) shows that the macroeconomic consequences of redistribution policies in social democracies are not negative. He surmises that "these economic 'goods'

to hold true, however, globalization must be accompanied by a welfare state that is successfully redistributive and thereby promotes social stability.

Recent work has suggested that welfare spending in the developed economies not only protects the disadvantaged from the economic dislocations associated with globalization, but is increasingly part of the competitive formula (Scheve and Slaughter, 2006; Katzenstein, 1985; Garrett, 1998; Rieger and Leibfried, 1998). Welfare policies are an important outcome of the bargained consensus between business, government, and labor, particularly in the social democratic countries. As discussed in chapter 2, when labor market institutions are encompassing, labor can act collectively and negotiate certain trade-offs (e.g. lower wages for employment security) for two mutually beneficial outcomes: (1) social benefits not undermined by openness; and (2) flows of trade and capital undeterred by the level of social benefits. Welfare states in OECD nations have thus been constructed from both "bottom-up" and "top-down" pressures and, by design, protect market "losers."

All three types of spending explored in chapter 2 are expected to affect income distribution in OECD countries positively. As Marshall (1950) long ago argued, increases in social security spending can produce less inequality, particularly in Western countries that promote means-tested pensions,[6] although some disagreement persists on the precise type of social insurance scheme that most effectively helps the destitute.[7] Education spending can improve income distribution by providing the poor with the skills to earn higher incomes. Finally, health spending may help close inequality gaps by improving the health of the poor, reducing the incidence of illness, and thereby improving productivity and job security. These arguments assume, however, that social spending enables the poor to increase their incomes more rapidly than the rich.

If spending is indeed redistributive in developed countries then greater public expenditures on social programs and macroeconomic performance can be justified. The flow of neither trade nor capital will necessarily be disrupted when governments devote more resources to equity-enhancing

[predictable patterns of wage setting, in accordance with productivity and competitiveness, high-skilled and productive workers, low levels of social strife, etc.] are attractive even to mobile asset holders in the volatile global economy, offsetting the disincentives to investment generated by big government and high labor costs highlighted in neoliberal economics" (Garrett, 1998: 5). Also see Burgoon (2001).

6 Means testing or targeting suggests that individuals earning below a specified amount (of wealth or property) are entitled to the benefit, or will receive the benefit at a reduced rate.

7 Controversy persists as to whether means-tested social insurance programs or universalism contribute to inequality and if flat-rate systems or earnings-related benefit levels have the most redistributive effect. See Korpi and Palme (1998).

social programs. Mobile asset-holders can view government redistribution policies as productive, because redistributive welfare states can lead to lower social strife and encourage business–labor cooperation (Garrett, 1998). Put simply, one condition for maintaining high levels of social spending under conditions of globalization is that the welfare state has a positive effect on income distribution.

3.1.2 The link between globalization, welfare spending, and inequality in LDCs

As indicated in the introduction of the book, analyses of the globalization–welfare relationship in the developing world have begun only recently. Significantly, these attempts to assess LDCs' capacities to cope with the negative effects of globalization have overlooked one critical issue: many of the social welfare programs in these countries were not originally designed to protect marginalized groups. Several studies report that, from their inception, government social policies, particularly those pertaining to income transfers, have been implemented in a "top-down" fashion and used for purposes of political control and patronage instead of redistribution (Mesa-Lago, 1994; Huber, 1996; Weyland, 1996a, 1996b; McGuire, 1999).

If the findings in these studies are generalizable, we can expect that the rich are gaining relative to the poor from increases in government welfare spending. Social security might exacerbate inequality if richer groups enjoy more generous benefits packages (relative to contributions) than the poor. One consequence is that, in the face of ongoing market risks and uncertainties, wealthier beneficiaries maintain income stability as the unprotected poor experience greater economic hardships. Education spending can exacerbate income distribution if the poor have minimal opportunity to gain skills that will help them earn higher incomes. Finally, health spending may increase the gap between income groups if existing spending is directed mostly towards specialized care and providing health subsidies for the rich; without access to affordable health care, the poor will have little safeguard against illness and hence productivity, job security, and, ultimately, income will suffer.

In many developing countries, an urban formal-sector coalition that includes unions, civil servants, managers, and government officials has long benefited disproportionately from the social welfare system. Even in states where clientelism may be less pervasive, welfare provisions are limited to the formal sector, which is as low as 10 percent of the workforce in many developing countries (ILO [International Labour Organization], 2001). These conditions serve as a disincentive to forming more encompassing labor market institutions that could result in a redistribution of benefits from the richer labor groups to the poorer ones.

The implication of these studies is that, if social welfare systems do little to decrease the gap between the rich and poor, it will be particularly challenging for governments to maintain stability in the era of globalization. As argued in the previous chapter, a bargained consensus between labor, business, and capital is difficult to achieve in the developing world, and becomes even harder when confronted with international political and economic pressures. Since workers in LDCs do not have the same types of encompassing organizations as they do in many advanced economies, the growing duality between surplus and formal-sector workers creates a more competitive environment and makes it increasingly difficult for different subgroups of workers to forge coalitions and pursue equity-enhancing social policies.

Those engaging in the race to the bottom debate must take pause if indeed social spending in developing countries is not redistributive. The findings in chapter 2 would then demand further interpretation. If greater social spending is not reaching the poor then a race to the bottom is of immediate consequence to less vulnerable groups. Are decreases (or increases) in social security and welfare spending, in particular, directly affecting the income security of the poor? Ultimately, the distributional impact of social spending must be considered in order to determine whether encouraging states to spend more on existing welfare programs during globalization is in fact sound policy.

The critical question, then, is whether increasing welfare spending is to be greeted as progress. Existing studies in the comparative politics and globalization literatures have not empirically determined whether welfare spending, alongside international economic factors, affects income distribution positively or negatively. Even if, as some studies claim, privileged groups receive a disproportional amount of the benefits, government interventions may still improve the situation of the poor to some degree.[8] If welfare spending is regressive, however, increasing social spending could theoretically have the same destabilizing effects as lowering social spending in more progressive countries.[9] Do empirical data support the claim that governments of developing countries are

[8] For instance, although Brazil's corporatist state created the National Confederation of Workers in Agriculture (CONTAG) in 1963, the rural workers mobilized under this organization were eventually able to achieve some success in establishing progressive social policies in the 1990s (Weyland, 1996a, 1996b).

[9] According to Huber (1996), Costa Rica would be an example of a progressive LDC, because it has developed according to social democratic principles of universality and equity.

unlikely to redistribute resources *to the poor* in an era of globalization? Or does globalization provide certain incentives that encourage redistributive reform? Are certain types of social spending more redistributive than others? The model presented in the next section assesses whether the different types of social spending have a positive or negative impact on income distribution in globalizing economies.

3.2 The base model: the effects of globalization and social spending on income distribution

This model tests the determinants of income distribution in thirty-five developing countries and eleven high-income OECD nations. All cases for which data (on income distribution and social spending) are available are considered in this analysis. The sample represents fourteen low- and low middle-income non-OECD countries, eighteen upper middle- and high-income non-OECD countries, and eleven high-income OECD countries. The data form a time-series cross-section unbalanced panel covering annual information from 1972 to 1996. I apply the fixed-effects method using country and decadal dummies. This method controls for idiosyncratic differences across countries with regard to inequality.

Recall from chapter 2 that social spending is subject to measurement error due to decentralized spending in some developing countries. Fortunately, in this particular model, a new statistical procedure allows us to correct for this problem. In order to disentangle the links between globalization, social spending, and income distribution, the statistical analysis relies on the application of the 2SLS estimation procedure. The Lewbel (1997) procedure of using higher moments of the spending variables as instruments is applied in this model.[10]

The baseline equation is as follows:

$$\begin{aligned}\mathrm{Gini}_{it} = {} & \Sigma(\mathrm{welfare}^{\#}_{it-1}) + \Sigma(\mathrm{globalization}_{it-1}) + \Sigma(\mathrm{X}_{it-1}) \\ & + \Sigma(\mathrm{country}) + \Sigma(\mathrm{decade}) + \mu_{it}\end{aligned}$$

This equation tests the direct effects of openness and welfare spending on inequality. $Gini_{it}$ is the dependent variable, with larger Ginis suggesting greater income inequality. The Gini coefficient is a number between zero and 100, where zero means perfect equality (everyone has the same

[10] Refer to footnote 35 in chapter 2. The first stage includes higher moments of the welfare variable, the globalization variables, PLP, external debt, democracy, and the appropriate demographic controls.

income) and 100 means perfect inequality (one person has all the income, everyone else earns nothing). Higher Ginis thus represent higher levels of inequality in household- and individual-based distribution of incomes.[11] $Welfare^{\#}_{it-1}$ represents the same vector of welfare variables observed in chapter 2: education, health, and SS and welfare. It is the predicted value ($^{\#}$) estimated in the first stage. The subscripts i and t represent the country and decade of the observations, respectively.[12] *Globalization* represents the vector of international market variables: trade and capital flows. X_{it-1} is the vector of control variables: democracy, population, and GDP per capita.[13] Finally, decade dummies are included to account for the effects of regional and international conditions. All the variables are lagged to ensure that the direction of causality occurs from the exogenous variables to the dependent variable. See appendix D for detailed explanations of each of the variables.

One problem with pooled models is that countries with structural differences may exhibit identical coefficients. The determinants of inequality arguably differ in the OECD countries from the non-OECD countries. For example, democracy and urbanization can affect the distribution of government resources. The upper-income OECD nations were democratic, industrialized economies before the time frame of this study, however. Both these causal variables, particularly *democracy*, show little variation in the high-income industrialized countries and thus cannot be expected to have a major impact on current income distribution. Rather, *GDP growth* is more likely to have distributive effects in the OECD economies.[14] Regressions on the high-income OECDs and developing countries are therefore run separately.

3.2.1 *The dependent variable: income distribution*

Deninger and Squire's (1996) data on Gini coefficients are used to measure inequality in this analysis. This World Bank compilation of statistics on household income inequality is the most widely used in

[11] Deninger and Squire (1996: 580) state, "Given that the difference is not too large, we conclude that there is no reason to expect a large systematic bias in empirical work as a result of using both household-based and individual-based Gini coefficients."

[12] Decade dummies are particularly important to check the effects of the 1980s crisis on the model, particularly since social spending plummeted during that decade.

[13] Once again, as explained in chapter 2, country dummies are used to absorb much of the explanatory power of ethnic fragmentation and region.

[14] The logic of Kuznets' (1950) theory does not apply to this set of countries, since they are already "mature" economies.

current development research.[15] The benefit of using the Deninger and Squire data set derives from their painstaking efforts to satisfy particular standards of quality.[16] Ultimately, they accept only 682 out of their 2,600 observations as their "high-quality" set. See appendix E for technical details on the values used in this study.

The Gini coefficient is an appropriate dependent variable for this analysis, for two reasons: (1) gauging inequality is a commonly accepted method for determining whether the poor are gaining over time; and (2) large Ginis suggest the presence of instability (Alesina and Perotti, 1996), which many globalization analysts argue is also a possible outcome of globalization (Rodrik, 1997a).[17] Only data from the "high quality" sample are applied. Appendix F displays summary statistics for Gini coefficients in the developed and developing countries.

One possible objection to the use of this proxy is that worsening income inequality might not have an effect on poverty. To address this, I re-estimate the model using the concentration of income in the lowest quintile as the dependent variable. Significantly, measuring the dependent variable in these two ways affords a view of globalization and social spending effects on both relative and absolute poverty. These results are shown in appendix G.

15 See, for example, the influential works of Sala-i-Martin (2002), Forbes (2000), and Birdsall, Ross, and Sabot (1995). There are, of course, scholars who take issue with the sparse data coverage and its methodology (see Atkinson and Brandolini, 2001, and Galbraith and Kum, 2003).

16 These standards are: (1) data must be based on household surveys; (2) the population covered must be representative of the entire country; and (3) the measure of income (or expenditure) must be comprehensive, including income from self-employment, non-wage earnings, and non-monetary income.

17 A possible alternative dependent variable is instability. It would be useful to know if welfare spending is effective in maintaining social stability as globalization occurs. The problem, however, is that instability is an empirically and conceptually difficult variable to construct (Linehan, 1980). Aggregate statistics of instability, such as the degree of political violence, civil strife, and labor strikes, do not quite capture the link between openness, welfare spending, and its domestic consequences. Political violence is hard to disassociate from regime type, while numerical data on civil strife and labor strikes are not informative. As Murillo (2001) convincingly argues, the latter reflect institutional opportunities, cultural legacies, and political resources. Consequently, if we find through aggregate statistics that instability is rising alongside increased welfare spending, it is impossible to differentiate instability due to the effectiveness of redistribution policies (because governments have been required to take benefits away from the rich to make concessions to the poor) from that due to their ineffectiveness (because the poor are not receiving enough benefits). In addition, examining inequality is a more direct way of assessing whether the poor are gaining relative to the rich. As Alesina and Perotti (1996) indicate, increasing inequality leads to instability, and so the motivating factor in this analysis is to assess whether the preceding condition leading to social unrest is actually occurring with globalization.

3.2.2 *Independent variables*

3.2.2.1 Welfare spending For the purposes of this analysis, welfare in developing countries is best captured by per capita spending on health, education, and SS and welfare as reported in the IMF's *Government Finance Statistics* (GFS). This measure is used instead of welfare spending as a percentage of GDP, since per capita spending provides a more direct estimate of the *absolute* level of resources committed. As in chapter 2, "welfare" includes spending on social security and welfare, which captures primarily traditional transfers and pensions, as well as education and health. If welfare spending is redistributive then the coefficients of the three public expenditure variables will be negative and significant.

There are limitations with using the GFS data, however. Total social spending data do not reveal how expenditures for the different categories are disaggregated. For instance, data on education spending do not indicate if resources are distributed towards primary and secondary levels or university education, the former usually being associated with more redistributive-type spending. Similarly, it cannot be determined whether health expenditures are devoted to basic preventative care or costly curative programs. Since macroeconomic cross-country data do not provide this detailed information, we are forced to assess if *overall* spending is favorable for the poor. The results should be interpreted with this limitation in mind.

3.2.2.2 Globalization In order to incorporate the two primary international forces said to affect domestic politics, I once again measure the extent of globalization by both capital and trade flows. The conventional measure of openness, exports plus imports relative to GDP, is incorporated in this developing country model. I test the effect of capital flow by disaggregating it into portfolio and foreign direct investment flows. It is of interest to see whether various indicators of globalization have a direct impact on inequality, as suggested by the literature. If the globalization critics are correct then we can expect the openness coefficients to be positive and significant. Note that FDI tends to be statistically insignificant, and, since it is correlated with trade (and trade, not FDI, has the more significant impact in the race to the bottom model in chapter 2), it is dropped from the model.

3.2.2.3 Democracy Democratic nations should exhibit a more favorable distribution of income. Several studies argue that more authoritarian regimes cause income distribution to be skewed, because income will be concentrated in the hands of the few elites who hold political power

(Weede, 1982; Muller, 1988; Burkhart, 1997).[18] The Polity IV data set (2000), produced by the University of Maryland's Center for International Development and Conflict Management (CIDCM), is used here to derive this measure. Democracy is scored on a scale of zero to ten (ten being the highest), and rated by: (1) regulation, competitiveness, and openness of executive recruitment; (2) executive constraints; and (3) the regulation and competitiveness of political competition. Following Brown and Hunter (1999) and Kaufman and Segura-Ubiergo (2001), I also estimate the model using a dichotomous measure of democracy. Any country scoring at least seven is coded democratic, the rest as authoritarian. I use this approach since non-democracies should perform differently from democracies with respect to income distribution.

3.2.2.4 Economic development, urbanization, and population growth
Economic development, urbanization, and population growth are generally considered important determinants of inequality. According to Kuznets (1955), development has an inverse U-shaped relationship with inequality such that inequality increases in a nascent economy and then begins to decline as the country gets richer (Ahluwalia, 1976; Weede and Tiefenbach, 1981; Bollen and Jackman, 1985; Crenshaw, 1992; Burkhart, 1997). In the early stages of development, wealth is concentrated in the hands of the few who possess entrepreneurial and productive capabilities. A wealthier economy accelerates the urbanization process, dissipates rents by offering wider access to investment opportunities, and provides more revenue and infrastructure for redistribution. The per capita GDP variable is a quadratic estimation (GDP and GDP^2), and thus a negative and significant coefficient would confirm Kuznets' hypothesis.

Population growth is generally expected to have a negative impact on inequality. Rapid population growth can put stress on a country's resources and make it more difficult to improve labor productivity (Sheahan and Iglesias, 1998).[19] Population pressures automatically reduce the size of the share of personal incomes and lessen the probability that there will be an equaling out of income. Scholars argue that the effects of population growth on inequality are more directly measured through the age structure, however (Hargens and Felmlee, 1984; Sheehey, 1996). For

[18] Burkhart (1997) also argues that moderate levels of democracy have skewed income distribution, because economic benefits favor the urban middle class.

[19] Sheahan and Iglesias (1998) point out that population growth tends to increase the absolute size of the agricultural labor force, decreasing the ratio of land per laborer, and thus affecting labor productivity and incomes.

example, the POP65 variable should have a positive coefficient, because a larger elderly population suggests lower productivity, lower savings rates, and smaller intergenerational transfer of income (Deaton and Paxson, 1997). The POP65 percentage thus "unpacks" the effects of population growth.

Urbanization can also affect income distribution. The growth of the urban population contributes to a larger middle class, more employment, and a modern workforce (Boschi, 1987). As the labor force shifts from agriculture to the urban sector, low-paid rural jobs become less important and inequality is expected to decrease. Moreover, urban-based development sets the foundation for the expansion of a high-wage modern sector as well as better education and health facilities. Vanhanen (1997) predicts a negative relationship between urbanization and inequality, since the former leads to greater school enrollment and higher literacy rates. Because of the high correlation with GDP per capita, however, I drop urbanization and rerun each of the models as a check on the initial findings. The results do not change.

3.2.3 Results

The regression results reveal an interesting pattern. The developed nations fare much better than their less developed counterparts in utilizing social spending to maintain a favorable distribution of income, particularly under conditions of globalization. Portfolio flows have no effect on income distribution in either developed or developing countries, while trade flows exacerbate inequality problems only in the LDCs. As expected, the different components of social spending (education, health, and SS and welfare) help reduce the gap between rich and poor in developed countries. Perhaps more importantly, however, after all the relevant domestic variables are controlled for, most types of social spending in developing countries are not redistributive during globalization, *apart from* education spending.

The base model is first applied to the OECD countries to assess whether inequality models of richer nations need to consider the effects of international market integration. How valid are the concerns of globalization critics who warn that moving jobs offshore to low-wage economies worsens income distribution in the developed world (Nader, 1993; Greider, 1998; Atwood, 1993; Phillips, 1993; Gill, 1995; Daly, 1996; Scholte, 1997)? If their predictions are correct then the coefficients for both portfolio flows and the trade variable should be positive and significant. The results reported in table 3.1 challenge these claims and suggest that greater exposure to international markets has *no* effect on inequality.

Table 3.1 *Determinants of income distribution in OECD countries*

Variable	Model 3.1	Model 3.2	Model 3.3
Trade	0.01 (0.02)	−0.01 (0.02)	0.01 (0.02)
Portfolio flows	1.56 (6.24)	2.54 (6.13)	1.86 (6.26)
SS and welfare	−0.00102† (0.00064)		
Education		−0.013* (0.007)	
Health			−0.004 (0.004)
Growth	0.15** (0.07)	0.13* (0.07)	0.16** (0.07)
POP65	0.23 (0.36)	0.47 (0.44)	0.27 (0.50)
1970s	−0.34 (0.76)	−0.42 (0.76)	−0.15 (0.77)
1980s	−1.14* (0.61)	−0.95† (0.62)	−0.92† (0.63)
N	84	84	84
R^2	0.99	0.99	0.99

Notes: ** = $p < 0.05$; * = $p < 0.10$; † = $p < 0.15$. Fixed-effects regression estimates. Figures in parentheses are standard errors.

These results corroborate the findings of Mahler, Jesuit, and Roscoe (1999), who also discover few significant relationships between trade and capital flows and income distribution in developed countries.

What happens if the international economic variables are dropped from the model? Given that little empirical evidence exists here or elsewhere to show that globalization is a critical factor in explaining inequality trends in the industrialized world, I re-estimate the model without them. Although the results do not radically change in the absence of globalization variables, table 3.2 reveals stronger impacts from the social spending variables. The coefficients for both education and SS and welfare are now negative and significant, suggesting that these types of government social spending improve income inequality. Health spending appears to be the least effective social spending category. Inequality shows little sensitivity to the demographic variables. It is possible that the percentage of the population that is aged (POP65) does not have a direct effect on income distribution. Scholars have recently argued that the long-run stability and continuity of the welfare state in developed economies depends on well-entrenched interest groups (e.g. retirees, labor, the disabled) (Pierson, 1996). According to this logic, the impact of social spending would outweigh the effects of the demographic variables in countries that have reached advanced stages of political and economic development. Country-specific factors (dummy variables in the regression equation) also play a major role in determining levels of inequality (results not shown here). Altogether, these results suggest that the spending inequality profiles of the more

Table 3.2 *Determinants of income distribution in OECD countries – revised*

Variable	Model 3.4	Model 3.5	Model 3.6
SS and welfare	−0.0012* (0.00062)		
Education		−0.015** (0.007)	
Health			$-0.005^{\dagger}$ (0.003)
Growth	0.16** (0.07)	0.127* (0.067)	0.16** (0.07)
POP65	0.26 (0.34)	0.53 (0.45)	0.31 (0.45)
1970s	−0.31 (0.74)	−0.37 (0.75)	−0.11 (0.75)
1980s	−1.13* (0.62)	$-0.95^{\dagger}$ (0.63)	−0.84 (0.64)
N	84	84	84
R^2	0.99	0.99	0.99

Notes: ** = $p < 0.05$; * = $p < 0.10$; † = $p < 0.15$. Fixed-effects regression estimates. Figures in parentheses are standard errors.

globalized developed economies are more or less the same as the less globalized ones.

The next step is to compare how trade and capital flows affect income distribution in developing countries. Should openness have similar effects on inequality in developed and developing economies? Garrett (2000) and Rodrik (1998) combine their sample of rich and poor countries and thus do not consider structural differences between the two sets. Nevertheless, weak political and regulatory institutions, ineffective labor movements, histories of political repression and clientelism, and (relatively) late integration into the global economy are common characteristics for most LDCs, and give ample reason to suspect that openness might affect this set of countries differently. Table 3.3 reports the results for the less developed countries.

In direct contrast to the OECD countries, these results indicate that trade exacerbates inequality in poorer countries. The effects of trade are small, but significant. These findings give greater voice to globalization critics who focus on the developing world (Heredia, 1997; Cornia, 1999; Gopalkrishnan, 2001; Rao, 2001). It is also telling that each of the social spending variables is positive and significant. This finding, that government social expenditures exacerbate inequality in developing countries, supports recent World Bank reports that argue that the rich benefit relative to the poor under existing public education and health programs (World Bank, 2001b). The findings on SS and welfare also provide statistical support for studies of developing country social policies in the comparative politics literature discussed earlier.

Table 3.3 *The dependent variable: income distribution in non-OECD countries*

Variable	Model 3.7	Model 3.8	Model 3.9
Trade	0.06** (0.03)	0.05** (0.03)	0.05** (0.02)
Portfolio flows	−0.41 (0.80)	−0.10 (0.72)	−0.23 (0.77)
SS and welfare	0.11*** (0.04)		
Education		0.11** (0.05)	
Health			0.37*** (0.11)
Democracy	−4.07*** (1.47)	−2.96** (1.24)	−2.96** (1.20)
GDPcap	30.92** (12.57)	4.65 (13.97)	14.39 (12.89)
$GDPcap^2$	−2.62*** (0.91)	−0.78 (0.96)	−1.57* (0.91)
POP65	0.89 (1.51)	1.53 (1.61)	1.07 (1.66)
Urban	−0.37*** (0.13)	−0.27** (0.13)	−0.29** (0.13)
1970s	$-1.77^{\dagger}$ (1.14)	$-1.97^{\dagger}$ (1.23)	−1.83* (1.07)
1980s	−0.73 (1.00)	−0.66 (0.86)	−0.46 (0.87)
N	97	107	107
R^2	0.98	0.99	0.99

Notes: ***= $p < 0.01$; **= $p < 0.05$; *= $p < 0.10$; †= $p < 0.15$. Fixed-effects regression estimates. Figures in parentheses are standard errors.

It is interesting that the GDP variables are not significant in the presence of education and health spending. Much scholarly research has focused on the curvilinear relationship of wealth to inequality, establishing the Kuznets curve as both a stylized fact and economic law (Weede and Tiefenbach, 1981; Simpson, 1990; Crenshaw, 1992; Nielsen and Alderson, 1995). Since these studies do not control for social spending, however, it is possible that institutionalized welfare programs in the developing world offset the effects of the pressures described in Kuznets' theory. Recall that economic forces (i.e. investment opportunities) drive the logic of the Kuznets curve, while political variables (e.g. government intervention) are excluded from his model (Kuznets, 1955).

Capital flows, unsurprisingly, show no effect on inequality. None of the models in this analysis thus far have found capital flows to have a significant effect on social indicators. One possible explanation is that many developing countries have only recently begun to liberalize their capital accounts, and portfolio flows, on average, remain at a very low level relative to GDP (0.28 percent). Of course, some developing countries have experienced higher capital flows (e.g. Argentina, Brazil, South Korea, Mexico, Thailand, Indonesia), but these are clearly the exceptions. I therefore drop the capital flows variable in subsequent regressions. It should be emphasized, however, that including portfolio flows in any of the regressions does not affect the basic substantive findings of this chapter.

3.3 Globalization and prospects for equity-enhancing reform

If, as indicated in the results, openness exacerbates inequality, is it also possible that globalization provides incentives for social reform? As argued earlier, a redistributive welfare state helps maintain stability in the face of globalization, and it can spur competitiveness and discourage "exit." The question, then, is whether there are enough incentives to reform social spending so that it can mediate the adverse affects of globalization in LDCs. To test this possibility, the following model assesses the impact of government-directed social programs when states and domestic markets are subject to the pressures of foreign competition:

$$\begin{aligned}\text{Gini}_{it} = {} & \Sigma(\text{welfare}^{\#}_{it-1}) + \Sigma(\text{globalization}_{\,it-1}) \\ & + \Sigma(\text{globalization}_{\,it-1} \times \text{welfare}^{\#}_{it-1}) + \Sigma(\mathbf{X}_{\,it-1}) \\ & + \Sigma(\text{country}) + \Sigma(\text{decade}) + \mu_{it}\end{aligned}$$

In this equation, the coefficient for the interactive term between *globalization* and *welfare* indicates whether increases in different types of social spending help cushion the adverse effects of openness. If social spending is indeed more redistributive as markets expand then the coefficient on the interaction terms will be negative and significant.

Table 3.4 provides some empirical support for this speculation. It appears that the negative effects of openness on inequality are mitigated primarily by education spending. Public health spending has a significant but weaker effect on improving income distribution as trade expands. In the case of social security expenditures, however, increasing government budget allocations to this category clearly worsens income distribution. For a clearer illustration of these interaction effects, see appendix H.

These results for education are now at odds with emerging literature from the World Bank, which posits that public spending on education does not help the poor (see World Bank, 2002b, Hanushek, 1995, Nelson, 1999, and Mingat and Tan, 1992, 1998). Two possible reasons account for the discrepancy in results. Most importantly, the models differ by the inclusion of specific explanatory variables in this analysis (i.e. globalization), which are often excluded from the World Bank models. This is the first study to assess whether incentives for social reform increase in the face of globalization. Second, the World Bank analyses apply different dependent variables to assess the effects of education spending, such as

Table 3.4 *Determinants of income distribution in LDCs*

Variable	Model 3.10	Model 3.11	Model 3.12
Trade × SS and welfare	0.0008** (0.0004)		
Trade × education		−0.0009** (0.0004)	
Trade × health			−0.0019† (0.0012)
SS and welfare	0.06 (0.04)		
Education		0.15*** (0.05)	
Health			0.42*** (0.12)
Trade	0.02 (0.03)	0.10*** (0.03)	0.10*** (0.04)
Democracy	−3.72** (1.50)	−3.17** (1.24)	−2.88** (1.24)
GDPcap	36.73*** (12.02)	−4.64 (13.29)	3.85 (13.96)
$GDPcap^2$	−3.12*** (0.86)	−0.03 (0.96)	−0.78 (1.02)
POP65	−0.19 (1.38)	1.78 (1.47)	1.90 (1.51)
Urban	−0.26* (0.13)	−0.29*** (0.11)	−0.34*** (0.12)
1970s	−1.24 (1.25)	−1.92* (1.13)	−1.80* (0.98)
1980s	−0.16 (0.92)	−0.56 (0.65)	−0.33 (0.65)
N	97	107	107
R^2	0.99	0.99	0.99

Notes: ***= $p < 0.01$; **= $p < 0.05$; *= $p < 0.10$; † = $p < 0.15$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

enrollment and drop-out rates. The dependent variable in this study (inequality) is designed to capture more aggregate and long-term effects of spending.

The findings for health spending and its positive impact on income distribution (i.e. a negative coefficient) are not as strong as for education, but they still differ from the conclusions of Filmer and Pritchett (1999) and other World Bank studies that find government-directed health spending to be ineffective (Gwatkin and Guillot, 1999; Gwatkin, 2000; Musgrove, 1996). Again, these researchers are analyzing alternative dependent variables (e.g. infant mortality), and they do not necessarily consider the effects of globalization. Openness is thus an important variable to include in models for both health and education outcomes.

The results for SS and welfare spending are not comparable with other studies, however, since this is the first attempt to test their effects on inequality. The finding that SS and welfare spending exacerbates inequality in the face of rising trade flows is new, and supports many of the arguments posited, but not tested, by scholars mentioned earlier. These results imply that not only is this type of spending ineffective for the poor during globalization, it actually worsens the distribution of income.

The coefficients of the interacted variables are significant even when alternative explanatory variables are used as controls. As discussed earlier, the country dummies should account for much of the variance, given the large importance of country-specific effects such as history, cultural differences, etc. in explaining inequality. Tables 3.3 and 3.4 both reveal that urbanization, GDP per capita, democracy, and country dummies have strong effects on inequality in this model. Despite the strong effects of the control variables, however, government social spending still shows a negative impact on income distribution in developing countries, albeit small.

3.4 Robustness checks

To check the stability of these results, I re-estimate the model using the income share of the bottom quintile of the population as the dependent variable. Quintile data provide a second test of whether social spending benefits the poor during globalization. I also substitute the democracy dummy with the second-order polynomial function of democracy used in Burkhart (1997). These results are reported in appendix G. The primary (and secondary) findings are, significantly, not affected by these two changes and thus provide greater confidence in the validity of the statistical pattern revealed in table 3.4.

As a final check on the results, I rerun the models by using data averaged first by five years and then by decades to minimize potential problems relating to missing data.[20] I also run the models dropping those countries with the most missing data. The results are minimally affected.

In sum, globalization affects income distribution in developing economies more than it does in the developed countries. The negative and significant results for the various categories of OECD social spending lend support to the claim that the mature welfare states of Europe are redistributive and relatively immune to the effects of globalization. The findings for less developed countries, in contrast, reveal that, first, trade has an adverse effect on income distribution and, second, many of the existing welfare programs are not redistributive during globalization. The implication is that *the race to the bottom in social security and welfare is most directly hurting the middle class in developing countries*. Under conditions of globalization, only education spending encourages the reduction of income inequality. The significant coefficients on democracy, GDP per capita, and urbanization support the existing literature in its claims that domestic variables are also important determinants of developing country welfare spending.

[20] Note that I also interpolate missing data using Stata's *ipolate* command.

3.5 Interpretation of results: the role of government–labor relations, information, and interests

The statistical estimates in the last section reveal that education spending is more redistributive in the face of globalization than either health or social security and welfare. How can this pattern be explained? This finding is particularly interesting, given that development agencies such as the World Bank and the United Nations Development Programme (UNDP) often report that public spending in LDCs has been skewed towards the rich.[21] With deeper international market integration, however, education spending appears to have a positive effect on redistribution. A closer look at the government–labor relationship in an era of expanding markets sheds some light on these results. Drawing from the insights of the rational choice literature, I argue that the combination of institutions, information, and the preferences of politicians and interest groups affects social policy outcomes.[22]

Institutional constraints that evolved from government–labor interactions can contribute to the regressive nature of social security, education, and health programs. Under conditions of globalization, however, if there is a spread of information, and the interests of politicians and interest groups are affected, these institutional constraints can be overcome. The combination of institutional constraints, interests, and information thus offer a plausible explanation for the variations found in the equity-enhancing performance of education, health, and social security in the current era of globalization.

First, (formal-sector) labor's interactions with government and politics has contributed to the formal and informal constraints that discourage the poor and disadvantaged from mobilizing and demanding more equitable social reforms. The fragmented nature of labor organizations and, as Weyland (1995, 1996b) argues, the clientelist machinations and internal state fragmentation that can arise from government–labor relations underscore the basic difficulties in realizing social reform for the masses of poor people. Nonetheless, the spread of information can provide a means to overcome these institutional constraints (see Milner, 1997).[23] For example, increased scholarship, as well as political and media attention to the importance of education in a globalizing environment, can have a positive effect on the policy choices of various social groups. On the other hand, information asymmetry regarding the benefits of social investments, such as in social security, may create political disadvantages. Finally, the role of

[21] See, for example, the *World Development Report 2002* (World Bank, 2001b) and the *Human Development Report 2002* (UNDP, 2002).

[22] This emphasis on institutions, interests, and information draws on Milner's (1997) analysis.

[23] As Milner (1997: 18) summarizes, institutions are "socially accepted constraints or rules that shape human interactions."

preferences must also be considered (Milner, 1997). Redistributive reform will occur when the new policies improve politicians' ability to retain office, and when social actors enhance their net income. It is conceivable that, in a competitive global economy, progressive changes in education are increasingly consistent with the policy preferences of rival social actors (e.g. business and labor), while health and social security and welfare reform in developing countries are less so.

Elaborating on the first point, despite great variations within and between developing countries, some generalizations about government–labor relations can be applied. An emphasis upon rapid industrialization alongside the overall absence of transparent and accountable governance has created opportunities for a particularistic relationship between government and a relatively small portion of the larger workforce. Starting in the early twentieth century, LDC governments began reorganizing their economies towards manufacturing. In a world already industrialized and technologically advanced, the challenge was to do this as quickly as possible. Governments thus solicited cooperation from a small segment of workers in the key sectors at the neglect of the much larger workforce in the urban informal and agricultural sectors, with the primary aims of containing labor militancy and promoting industrial peace. Legislation and public policy that once included only civil servants, the military, and other professionals eventually expanded to incorporate salaried, skilled, and some low-skilled workers in key sectors. Generous welfare benefits commonly became a part of the package of "inducements and constraints" to control labor (Collier and Collier, 1979).

In the absence of a vibrant democratic environment with accountable administrative structures, however, welfare constituents demanded special favors and privileges, and politicians began to use these systems for patronage purposes. Education, health, and SS and welfare programs often served as vehicles of clientelism (Mesa-Lago, 1994; Weyland, 1995, 1996a, 1996b; Huber, 1996; Nelson, 1999). For example, in addition to distributing benefits to narrow groups of privileged workers, politicians appointed teachers, health personnel, and social workers in exchange for political support. Such practices served to contain labor militancy, reinforce divisions between labor groups (between insiders and outsiders), and promote political cooperation (amongst insiders). It is no surprise that these groups of privileged workers often lobby against social welfare reforms (Nelson, 1999). Weyland (1996b) further argues that patronage ties with different public agencies and officials can erode the central control of the state, making it even more difficult to reach consensus on redistributive reform. As a consequence, large numbers of rural poor and informal-sector workers continue to receive minimal social protections, even in countries that have been aiming for universal social coverage (Huber, 1996).

These institutional constraints (clientelism, state fragmentation) maintain the government–labor relationship that creates formidable obstacles to more equitable social welfare reform in the current era (see Kaufman and Nelson, 2004). Politicians who deliver social benefits continue to be influenced by narrow organized interests, regardless of the recent wave of democratization. Not only are the poor difficult to mobilize, their political difficulties are particularly severe unless their concerns overlap with the somewhat better off (Nelson, 1989). Several studies have shown, however, that disadvantaged groups face great difficulty finding allies to support their demands for fairer redistribution policies (Weyland, 1995, 1996a, 1996b; McGuire, 1999).

The results in this chapter, however, suggest that, as developing countries integrate into the global economy, these types of institutional constraints can be overcome in the area of government-sponsored education programs. How do the disadvantaged overcome such institutional obstacles, particularly to education reform, in an era of globalization? The interests of the poor and non-poor may converge *in the case of equity-enhancing education programs* for two primary reasons: (1) the increased distribution of information on education; and (2) the growing compatibility of policy preferences of rival social actors.[24] These conditions may well explain why the poor have been successful at obtaining a mass base of support for education reforms, while finding less in the health sector and none at all in social security and welfare.

Awareness of the benefits of greater education investment has increased dramatically. Intense media and scholarly attention is focused on this issue. Information is distributed through abundant scholarly research, the activities of international financial institutions (IFIs), and widespread publicity concerning the east Asian model. Neither health nor SS and welfare sectors have experienced the *same level* of endorsement from these three sources, particularly with respect to their importance in a globalizing economy.

More studies in economics and international political economy suggest that improving the skill base of the economy in developing countries mitigates the potentially harmful impact of globalization on inequality (Thompson, 1995; Davis, 1996; Feenstra and Hanson, 1996, 1997; Robbins, 1996; Wood, 1997; Bourguignon and Verdier, 2000; Chan

[24] See Mares (2003a, 2003b) for an excellent discussion of the role of cross-class alliances in the development of social policy in the OECD countries.

and Mok, 2001; Mazumdar and Quispe-Agnoli, 2002).[25] The adoption of skill-based technologies, transferred by transactions between developed and developing economies, increases the relative demand for skilled labor in both sets of countries (although the skill level of labor demanded in general in LDCs is still less than in the industrialized OECD nations). Easterly (2002: 82) argues that "the quality of education will be different in an economy with incentives to invest in the future." In contrast, studies pertaining to the economic effects of investments in health argue that overall productivity will increase, but do not necessarily show its direct relationship with international markets (Knowles and Owen, 1995; Rivera and Currais, 1999; Arora, 2001; Bloom, Canning, and Sevilla, 2001).

In addition to scholars, IFIs and developing nation policy-makers have underscored the merits of education in a global economy. Developing nations have been searching to draw lessons from the east Asian experience since the late 1980s and early 1990s. They focus specifically on building human capital vis-à-vis education (Nogami, 1999; Tilak, 2001). Moreover, although the World Bank emphasizes the importance of investing in *both* education and health in scores of its publications, working papers, reports, etc., it is the leading provider of finance for education projects in the developing world. In the fiscal year 2002, for example, a year of global economic slowdown, the bank's education lending went up by 26 percent to $1.4 billion, while loans to the health sector remained steady at $1.2 billion (World Bank, 2003a). Conceivably, other aspects of the social budget have not been subject to the same opportunities of information dissemination. As a result, social actors are, arguably, less exposed to complete information about the benefits of health and social security and welfare, relative to education.

Finally, the spread of information on education and its benefits can facilitate the formation of alliances between the poor and non-poor in a global economy. Compatible preferences of politicians and interest groups are the missing link explaining the statistical patterns that emerged in the previous section. Put simply, politicians and social actors from different classes are more likely to support education reform over health and social security reform. Policy-makers prefer more equitable education

[25] Note that several of these studies (e.g. Robbins, 1996; Feenstra and Hanson, 1997) argue that inequality will worsen if the demand for skilled labor is increasing relative to unskilled labor. This argument holds only in the short run, however. Governments must eventually carry out steps to improve the quality of nations' primary and secondary education if it is to be the foundation of successful tertiary education (see Chatterji, 1998). In addition, basic manufacturing jobs in LDCs require a minimal level of education (Wood, 1994). With the exception of countries with extraordinarily high levels of surplus labor, officials must take an interest in all levels of education to ensure long-term competitiveness.

spending, since it is known to help growth in a knowledge-based global economy (Bourguignon and Verdier, 2000). A more highly skilled labor force will increase returns to capital, draw in greater foreign investment, and court a more robust economy. Political support for the government in power will subsequently increase.[26]

Politically active interest groups (e.g. business and formal-sector workers) also favor education reform, because increasing the skill premium of the workforce ultimately promotes income maximization. Forward-looking business owners, in particular, are beginning to favor more equitable education systems (Nelson, 1999). Not only does improving the education system have substantial pay-offs as human capital investment but, more attractively, it is also a fixed cost incurred by the government and not capitalists concerned with the "bottom line." Globalization and growing demands for a more educated labor force ultimately mitigate business reluctance to support policies in favor of education reform (e.g. more progressive taxes, higher interest rates). Accordingly, both the poor and the non-poor have an incentive to overcome institutional constraints by forming broad coalitions in favor of redistributive education reforms.

Equity-enhancing policy reforms in health and SS and welfare, on the other hand, do not necessarily meet the policy preferences of *both* business and labor. Certainly, it would seem that government health spending would also count as a fixed cost that business should be happy to roll over to the government. In direct contrast to education, however, a large percentage of health costs (i.e. health insurance) are financed by payroll taxes. As such, health expenditures can make up a substantial component of the wage bill and have a direct impact on labor costs. Therefore, even if health reform may have pay-offs as human capital investments, it is less likely to be favored by business interests because of the direct effect on their income. Additionally, profit-maximizing firms have less incentive to support publicly funded health programs in developing countries where labor is abundant and easily substitutable, *ceteris paribus*.

Social security, or pensions, is generally the most regressive component of the social budget. Results from this study reveal that SS spending becomes even more regressive with globalization. It is easy to see why

[26] One possible objection is that, if the country is a democracy, then investment in education may not have immediate political pay-offs, and politicians will have less incentive to implement education reform. Although this may be true, the tenure of most popularly elected governments is, on average, three to five years, which is sufficient for at least some of the benefits of education to be realized. Second, because of the spread of information, making education an explicit government priority (e.g. President George W. Bush's policy on education in fiscal year 2002) has mass appeal.

obstacles to SS reform would mount, since both businesses and privileged labor groups have a vested interest in maintaining the existing system. Businesses are likely to be the first to resist reform in this sector because of the impact it would have on their competitiveness through higher wage costs. Formal-sector workers, the current beneficiaries of the existing welfare system, are also likely to resist demands for more redistributive pension funds because of the risks they face with globalization. Recall that chapter 2's results suggest that states can no longer provide these groups with the same level of protections that they once did under the long phases of import substitution industrialization (ISI). Increasingly, they are affected by economic uncertainties (i.e. unemployment, falling wages, etc.). Recent strikes and protests over such issues as job security, wages, benefits, etc. in countries as diverse as Bolivia, India, Brazil, Colombia, South Africa, and South Korea illustrate this point. In addition, governments may be particularly sensitive to the demands of these interest groups since they have the highest voter concentration.

To form cross-class alliances to overcome the institutional constraints against more universal social security coverage is more difficult than doing so for education. Information on its benefits is not as well known, and it is not as much in the interests of the non-poor already receiving benefits. Even reform-oriented governments may ultimately find it politically advantageous to maintain the existing regressive pension system and sustain their long-standing ties with privileged labor groups.

3.6 Summary

Is social spending redistributive in an era of globalization? Are existing discussions of the race to the bottom missing the mark, given that they operate under the assumption that social spending has a positive impact on the social welfare of the disadvantaged? It is clear from the findings in this chapter that social spending is redistributive in OECD countries irrespective of globalization, but this is not the case in developing countries. This analysis suggests that openness has a much more severe impact on inequality in developing nations. Only education spending helps mitigate these adverse effects, while health and social security and welfare spending do not. So, from this particular angle, the poor do gain something directly from globalization.

In an effort to make sense of these outcomes, I rely on rational choice theories and the importance of institutions, information, and interests. Institutional constraints come from a pervasive clientelism that has evolved from government tendencies to allocate benefits disproportionately to privileged labor groups in exchange for political support. Since the current beneficiaries have a vested interest in maintaining the existing system, it becomes difficult for the marginalized population to mobilize and form cross-class coalitions. I argue in this chapter, however, that globalization creates incentives for the creation of cross-class alliances in favor of reforms in education. Incentives increase because information about the benefits of improving the skill premium of (both low-skilled and high-skilled) labor in a technologically driven global economy is spreading, and businesses and labor both prefer that the government pay for this type of human capital investment. More equitable reforms in SS and welfare and health, on the other hand, would be costly for the middle and upper classes, and there are no (perceived) pay-offs in terms of improving their positions in a globalizing economy. In sum, influenced by a more competitive global environment, LDCs are finding it less challenging to implement equity-enhancing reforms in education, but more difficult to redirect existing social security and health programs towards the poor.

Having established that welfare retrenchment is most directly hurting the middle classes in developing countries, one unanswered question remains: does the race to the bottom hypothesis suggest that these nations are experiencing "convergence"? In the next chapter I assess if all LDCs are advancing towards the "neoliberal bottom." To do this, I move beyond a sole focus on the *levels* of social spending and look more closely at the content and structure of welfare states in developing countries. More details about why LDC social policies are geared towards the more privileged and not towards protecting the poor remain to be revealed.

4 LDC welfare states: convergence? What are the implications?

Chapters 2 and 3 have presented three important findings thus far. First, in direct contrast with the nations of the OECD, governments of developing countries are sensitive to globalization and race to the bottom pressures in social security and welfare. Nevertheless, the findings in chapter 2 suggest that, paradoxically, those that comprise the bottom quintile of income distribution are not the ones directly harmed by a race to the bottom; this is mostly because social security, education, and health spending in LDCs tends to be regressive, helping mostly the middle class. The third major finding is that, while levels of health and education may not be increasing in response to globalization, public education spending is becoming more equitable. These findings overall are instrumental in illustrating the complex relationship between states and markets in the current era of globalization; domestic institutions (i.e. labor market institutions, the government–labor relationship) mediate and influence policy outcomes in a decisive and meaningful way.

Are the broader implications of these findings that the race to the bottom is leading towards convergence in lower-income economies? In other words, are all developing nations advancing towards the adoption of the "lowest common denominator" – the "neoliberal bottom" – in welfare provisions for their citizens, emphasizing minimal social welfare protections and deregulation, and investing only in those social policies that complement markets (e.g. education)?[1] In fact, have all the key elements of welfare provision in developing countries been captured by just the three commonly emphasized programs in the broader welfare literature: social security, education, and health? Finally, is it fair to say that, as markets expand, the poor continue to be neglected in *all* developing countries?

Until this point, we have forced broad generalizations, perpetuating a common assumption in the literature that the political economies of

[1] See Mishra (1999) for further descriptions of the neoliberal welfare policies currently encouraged in developing countries.

developing countries are more or less homogeneous. This chapter seeks to evaluate this assumption critically and answer the above questions by initiating a more detailed analysis of developing countries' distribution regimes. It will do this through a multifaceted examination of the content or institutional structures of the LDC "welfare states," moving away from evaluating the race to the bottom solely in terms of expenditures and cutbacks. Identifying welfare states (which I also refer to as "distribution" or "welfare regimes") is important to highlight the range of social policies, schemes, and distribution-related institutions that are systematically linked to the state's larger role in "organizing and managing the economy" (Esping-Anderson, 1990: 2). Esping-Andersen argues that conceptualizing welfare states solely in terms of their expenditures can misrepresent their salient characteristics and how these fit into the broader workings of a country's political economy.

Surprisingly, existing scholarship overlooks the prospect of varieties of welfare regimes in the developing world. In direct contrast, over the last decade and a half the identification of set constellations of distribution regimes in the OECD countries has become key to the abandonment of the RTB hypothesis and concerns about convergence in favor of *systematic divergence* (Esping-Andersen, 1990; Huber and Stephens, 2001; Kitschelt *et al.*, 1999).[2] This same possibility – systematic divergence in distribution regimes – has never been explored in developing countries however. Whereas it is now commonplace in the OECD literature to refer to the theoretical and institutional content of welfare states rather than focusing on spending alone, the limited number of studies on LDC welfare schemes have focused mostly on the level of social spending, and have altogether neglected any consideration of nationally negotiated social pacts. Significantly, the persistence of systematic divergence (i.e. distinct distribution regimes) in less developed nations well into twenty-first-century globalization would suggest that the domestic structures and institutions of developing nations are not likely to erode easily in the near future, as is hinted by proponents of the race to the bottom hypothesis.

[2] As explained later, I derive three hypotheses from the existing literature. "Systematic divergence" suggests that differences between welfare states in the universe of cases are characterized by a particular order and logic, and not random. "Extreme divergence" implies that each country has a welfare state that responds only to local needs and shares little similarities with other nations. "Convergence" lies at the other extreme, describing a situation in which all welfare states are similar to one another. Recall that the RTB hypothesis predicts that welfare states will tend towards convergence, or institutional and policy changes akin to the (neo)liberal welfare model.

Building on Esping-Andersen (1990), this chapter identifies systematic divergence, or the existence of two ideal types of welfare states, in the developing world. Efforts are primarily directed either towards promoting the market dependence of citizens (a *productive* welfare state) or protecting select individuals from the market (a *protective* welfare state). Cluster analysis reveals a third group with elements of both: the weak dual welfare state. One of the most striking discoveries is that none of the classic LDC welfare regimes has been geared towards protecting the most vulnerable strata of the population, shedding greater light on the findings in chapter 3. Existing welfare states in the developing world tend to favor the middle class, or those who are capable of participating in markets (productive welfare state) and the relatively small percentage of the population employed in the formal sector (protective welfare state).

This chapter evaluates institutional convergence by using other developing countries as a comparative reference point. Data limitations prohibit the observation of convergence over time.[3] This task is left to the case studies. In the following chapters, case studies allow a more detailed investigation into the questions if and how distribution regimes are changing in response to globalization. The evidence thus far suggests, despite evidence of a race to the bottom in the developing country welfare regimes, that these nations are *not* moving towards the universal adoption of neoliberal welfare institutions, and the situation of welfare protections for the poor remains more or less as it was before globalization.

The structure of this chapter is as follows. In the next section, I discuss the shortcomings of the existing comparative political economy and international political economy literatures in recognizing the prospects for systematic divergence in developing countries. Section 4.2 lays out the logic supporting systematic variations in welfare regimes. Section 4.3 uses cluster analysis to provide a statistical test of the proposed typology of welfare regimes. Section 4.4 suggests a causal story behind the cluster results. The final section discusses the implications, caveats, and next steps.

4.1 Welfare states in developing countries? The existing literature

Discussions of the race to the bottom and its consequences are hollow if we do not know what social welfare arrangements have existed to protect

[3] Indeed, this is how studies questioning convergence and systematic divergence in the industrialized nations were initiated, and critical similarities and differences between developed countries unveiled (Brickman, Jasanoff, and Ilgen, 1985; Esping-Andersen, 1990; Hall and Soskice, 2001).

the most vulnerable in the first place. Surprisingly, scholars have paid very little attention to the question of the "LDC welfare state" and its institutional contents.[4] IPE scholars imply that a race to the bottom in a globalizing economy ensures significant similarities between the political economies of the many developing nations, and the existence of some sort of "LDC welfare state" is implicitly assumed (Avelino, Brown, and Hunter, 2005; Cerny, 1995; Rudra, 2002; Garrett, 2001; Wibbels, 2006). Since developing countries face similar economic challenges (e.g. demand for capital, large pools of surplus labor), they are expected to converge on neoliberal welfare policies for the purposes of attracting capital and promoting exports.

The negative correlation between expanding markets and social spending in less developed countries confirms this hypothesis (Wibbels, 2006; Rudra, 2002; Garrett, 2000). By focusing on social spending per se, however, IPE scholars presuppose the existence of the developing country welfare state without investigating its particulars. With little sense of the salient characteristics, it is unclear how or why less social spending is necessarily associated with an embrace of market-friendly neoliberal policies. Leaders may very well engage in low (or decreasing) social spending while promoting "illiberal" welfare measures, such as public employment or labor market protections.[5] The convergence question thus remains unresolved.

The gross lack of efforts to investigate institutional commonalities among the LDCs may, perhaps, have its roots in CPE convergence debates that for decades focused only on developed nations. Convergence is defined as "the tendency of societies to grow more alike, to develop similarities in structures, processes and performances" (Kerr, 1983: 3). From the 1960s until the early 1990s scholars believed that only post-industrial societies could experience convergence, since (successful) industrialization requires a particular arrangement of social and economic forces.[6] The inference was that developing countries were marked by "extreme divergence." In other words, developing nations had to be vastly

[4] The book by Gough *et al.* (2004) is one important exception in the discussion of LDC welfare regimes. They do not focus on locating their typology within the traditional political economy debates discussed in this analysis, however, and they introduce an impressive list of descriptive factors that are difficult to operationalize across all cases (e.g. insecurity). Additionally, Kurtz (2002) presents a very interesting analysis of welfare regimes in Chile and Mexico.

[5] Note that reductions in public employment and labor market deregulation are basic components of the structural adjustment programs (i.e. neoliberal reforms) advocated by the IMF and World Bank.

[6] These analyses follow from stagist or modernization theories of the 1960s.

different from one another because they were still in the early stages of economic development.[7]

Consequently, in contradistinction to the IPE literature, the early CPE discussions of convergence in OECD nations advanced two impressions of developing political economies: (1) the types are endless; and (2) welfare states are precluded because of low economic development. The leveling forces of industrialization are hypothesized to produce convergence in OECD social structures and policies – e.g. pluralistic decision-making, the ability of the state to extract resources, a preponderance of committed industrial workers, etc. (for examples, see Form and Bae, 1988, and Kerr *et al*., 1964). The logic implies that, if nations with high standards of living exist in a homogeneous world, then countries with low standards of living must live in a vastly heterogeneous one. The existence of welfare states is also seen as one of the by-products of industrialization. Only nations at high levels of economic development can form a welfare regime (Wilensky, 1975; Cutright, 1965). Plausible as these arguments may be, CPE scholars have not tested them as they apply to the developing world, and IPE scholars take an opposing position.

Ultimately, the problem in both camps is that the systematic divergence hypothesis has simply not been explored in developing countries. The discovery of distinct patterns of distribution regimes has more or less put to rest expectations of convergence in the developed nations but left open the question as applied to developing countries. Nonetheless, these advancements in the OECD literature hold important lessons for the developing world, as is often the case. First, studies indicating systematic divergence in the developed nations suggest that the level of development does not necessarily predetermine the configuration of national political economies. Both Esping-Andersen (1990) and Hall and Soskice (2001) reveal that national political economies are what determine economic performance and social well-being, and not the reverse. Second, the detection of either distinct patterns of distribution regimes *or* production regimes can confirm the systematic divergence hypothesis. Finally, as Esping-Andersen (1990) demonstrates, the theoretical substance of welfare states is of import to political economy, along with the level of expenditures.

[7] The literature on strong and developmental states serves as an exception to the assumption of extreme divergence among developing countries. The problem, however, is that this literature effectively depicts the political economies of a select few northeastern Asian countries; by default, the rest of the developing world falls into a single residual category defined by the absence of some basic characteristics essential for growth. In other words, in this literature, the majority of LDCs are identified on the basis of what political institutions they do *not* have rather than those they do have.

Resolving the convergence debate in developing countries has significant implications for policy and politics, particularly given trends in market integration. If early CPE views are indeed correct, and extreme divergence prevails, the policy decisions of developing world governments are without any (extraterritorial) bounds.[8] This would impose strong limitations on researchers and policy-makers committed to encouraging development in lower-income countries. Exemplars of history, the missions of IFIs, and generalized policy prescriptions lose persuasion in favor of "wait and see." The opposite occurs if IPE scholars are correct about RTB effects and convergence does exist, suggesting that domestic structures and processes are meaningless, and policy responds primarily to international economics. If systematic divergence characterizes the developing world, however, policy-makers are responsive to local needs and politics, as well as some transnational forces, such as survival in a global economy.

4.2 Contemplating systematic divergence in LDCs: patterns of welfare regimes

4.2.1 Questioning CPE convergence: why LDCs are likely to have welfare states

The analysis in this chapter challenges the contention of comparative political economy convergence scholars that welfare states are necessarily a post-industrial phenomenon. The historical experience of the OECD nations coupled with the specific challenges of contemporary globalization have made it impossible for governments in the developing world to ignore *embedded liberalism*, or calls to maintain social stability alongside market expansion (see Ruggie, 1982, 1994). The repercussions of nineteenth-century globalization, which focused on using state intervention to maintain "market-driven equilibria" instead of social protections, are well known: domestic unrest, economic breakdown, and inter-state rivalries, leading ultimately to World War I (Polanyi, 1944).[9] Largely in reaction to this experience, governments of OECD nations in

8 Recall that proponents of the convergence hypothesis in the CPE literature suggest that high levels of economic development provide the primary context to which policy-makers respond. This is "extraterritorial" in the sense that decision-making in the OECD countries is being driven by similar forces and thereby transcends national boundaries. By inference, then, low levels of economic development provide no specific context for policy-makers to respond to.

9 Examples of nineteenth-century state intervention are tariffs, access to capital, and encouragement of large-scale industries (Gerschenkron, 1962; Bairoch, 1993).

the period after World War II formalized their welfare regimes for the purposes of social welfare and stability (i.e. twentieth-century globalization).[10] It is therefore plausible, as Collier and Messick (1975) show, that the successful workings of welfare systems in advanced economies provide important precedents for modern developing countries.[11] In contrast, when today's advanced economies first embarked on the journey to industrialization, no real precedents for a welfare state existed.

Globalization since World War II has been accompanied by new challenges, particularly for late entrants to the international market, rendering the economic and political costs of ignoring embedded liberalism very high. First, the "magnitude, complexity, and speed" of today's global financial, commodity, and service market operations carry risks and uncertainties to citizens of *all* nations.[12] Compared to the advanced economies, LDCs are in a position of "maximum uncertainty," since only a few of them can actually influence the markets in which they trade and invest (Waterbury, 1999). Second, social reactions to the market are a common thread in both developed and developing countries. This is evidenced in developing countries by the large number of labor and capital strikes in response to the adoption of neoliberal policies. Third, although labor as a class is not strong and suffers from collective action problems, as the findings in chapter 2 indicate, pockets of labor groups can and do affect social policies. Fourth, the relatively recent spread of democracy and its link to embedded liberalism should not be underestimated. The expansion of the right to vote puts all those negatively affected by globalization in a better position to insist that international market expansion be moderated by the pursuit of other objectives.

To summarize, nineteenth-century-style state interventionism in the current era is just as unlikely in the developing world as it is in the developed nations. The contention that embedded liberalism is common practice among developing economies casts doubt on CPE predictions regarding (the lack of) LDC welfare states and extreme divergence. The first part of the IPE convergence argument seems plausible, however: challenges to growth in a global economy are likely to affect domestic social policy decisions. How convincing, though, is their reasoning that international

[10] Despite the growing mobility of capital and the collapse of the Bretton Woods arrangements in the early 1970s, which led to pressures on governments to revert to nineteenth-century-style state interventionism, embedded liberalism has been maintained. See Pitruzzello, 2004, for an interesting discussion of the differences between nineteenth- and twentieth-century globalization.

[11] I am grateful to Benjamin Cohen for emphasizing this point.

[12] See Keohane and Nye's (2000) discussion of what is (and is not) new about contemporary globalization.

market pressures ultimately force the universal acceptance of market-friendly social policies? While some combination of markets and domestic interventionism for social welfare has been common to all countries since World War II, the different historical, economic, and political realities of developing countries suggest not only that their national social systems will differ from the developed countries, but also that they will systematically vary from one another as well. This investigation rests on the premise that LDCs maintain some form of capitalist market economy. In all the countries in the sample, private enterprise exists, and the market remains the principal means of distribution.

4.2.2 *Questioning IPE convergence: twentieth-century globalization and different LDC welfare regimes*

4.2.2.1 Emphasis on commodification The capacity to "commodify" is likely to be the key factor differentiating developing country welfare states. This refers to the degree to which government-backed social policies ensure that the majority of people depend on wage labor, with wage levels largely determined by market forces (see Esping-Andersen, 1990). Commodification in this sense does *not* apply to the developed world, since the workforce is already "proletarianized."[13] Advanced welfare states in the post-war era have instead focused on counterbalancing proletarianization with "decommodification," or permitting people to make their living independent of pure market forces (Esping-Andersen, 1990).

Esping-Andersen (1990: 2) argues that the first step in conceptualizing the welfare state involves locating the primary source of tension that gave rise to its particular political economy, or to the "state's larger role in managing and organizing the economy." In the early European experience, proletarianization was the major source of conflict (Esping-Andersen, 1990; Koo, 1990). Concerns about the *absence* of proletarianization, however, particularly in the post-war era, have been the focus of LDC political economies (Koo, 1990).[14] This is chiefly because the progressive shift of the labor force from primary agricultural activities to secondary manufacture and tertiary commerce and services has not

[13] The difference between commodification and proletarianization is that the former refers to the process while the latter refers to the *successful* dependence of the majority of the workforce on (formal) wage labor for survival. OECD welfare states do not focus on commodification, since these economies have shifted emphasis from industrial production to services.

[14] As noted in the introduction, this assumption tends not to apply to personalistic dictatorships.

occurred as it did in Europe.[15] At issue, then, is not the elimination of *internal* "class, inequality, and privilege," as it has been in the OECD nations (Esping-Andersen, 1990), but, rather, minimizing *external* divisions between the rich and poor economies by expanding wage labor and "catching up" with the industrialized nations.

Significantly, business as well as labor is dependent upon welfare states that focus on commodification. Proletarianization in the current era arguably requires somewhat greater state intervention. The demand for skilled labor has increased, and a minimal level of education is often a prerequisite for entering today's markets (Blunch and Verner, 2000; Tendler, 2003). Wood (1994) and Wood and Ridao-Cano (1996), for example, find that, even in basic manufacturing sectors, workers in LDCs are generally low-skilled (not unskilled). This is in direct contrast to the experiences of early industrializers, where private entrepreneurs needed much less state intervention to begin production (Gerschenkron, 1962). In Europe, an actual "deskilling" of the workforce occurred during early industrialization, and literacy rates declined (Stone, 1969; Nicholas and Nicholas, 1992; Sanderson, 1972).[16] Households, churches, and Sunday schools, rather than the state, provided primary education (Nicholas and Nicholas, 1992).[17] According to the evidence presented by Goldin and Katz (1998), the complementarity between skill and technology did not begin until as late as the twentieth century.[18]

4.2.2.2 Point of divergence Despite the intense need for governments in the developing world to focus on expanding wage labor, some countries in the post-war era have placed substantially greater priority on decommodification *prior to* full-scale commodification efforts. First, the latter is politically much more difficult to achieve in some countries because of the mistrust that emerged towards international markets in the 1930s.

[15] See the data presented by Erickson and Peppe (1976), which confirm this trend in OECD countries. See Browning and Roberts (1990) for an alternative argument. In most LDCs, secondary-sector employment remains limited, while the tertiary sector, distinguished by large numbers of informal-sector workers, has been forced to absorb much of the rural surplus (Koo, 1990; Evans and Timberlake, 1980; Erickson and Peppe, 1976).

[16] The term "deskilling" refers to the replacement of skilled workers by a large class of unskilled, sub-literate factory operatives. See Nicholas and Nicholas (1992).

[17] Some argue that, because of the laissez-faire tradition, states hesitated to intervene in education. Initiatives to do so began in the late nineteenth century (Kiesling, 1983). To give one important example, the first real non-private school in England was introduced as late as 1944 with the 1944 Education Act. This permitted local authorities to establish and maintain both primary and secondary schools (Morrish, 1970: 83).

[18] Goldin and Katz (1998: 694) describe technology–skill complementarity as when "skilled or more educated labor is more complementary with new technology or physical capital than is unskilled or less educated labor."

Colonial interference and declining terms of trade for agricultural exports in that decade hampered the complementarity (real or perceived) between international market participation and the rapid expansion of formal wage labor, at least in the early stages. Second, recall that precedents set by the experiences of the OECD nations matter (Collier and Messick, 1975); pressures on all governments to provide some degree of decommodification intensified in the post-war period. Finally, LDC labor is more dependent on a "decommodifying" welfare state than its early European counterparts. The former relies on the state to represent its needs, because workers suffer from both persistent collective action problems (see Bellin, 2000) and the prolonged absence of a guaranteed minimum income.[19] Developing states are inclined to intervene to provide this minimum income (through public works projects, public employment, labor market protections, etc.), since the transformation of surplus labor into formal wage labor has been occurring through the market process at an extremely slow rate.[20]

In sum, it is feasible that some developing countries prioritize independence from the market even *before* full-scale proletarianization has been achieved (i.e. a protective welfare state). If this is the case, not all nations will have "productive welfare states" that direct welfare efforts primarily towards encouraging wage labor. The implication is that the relationship between commodification and decommodification in developing countries may not be linear, as it has been in the post-industrial economies (see figure 4.1).

4.2.3 Delineating different welfare regimes in developing countries

It is important to emphasize that a blueprint for a developing world welfare state that promotes either commodification or decommodification per se never existed. In the post-war era, referring back to the "primary tension that drives political economies," LDC welfare states took qualitatively different forms depending on *how* governments chose

[19] For many of the early industrializers, agriculture played a strong role in industrialization, while in the LDCs, as Bates (1981) argues, the popular strategy of rapid industrialization often came at a cost to the efficiency of the agricultural sector. The end result is a large surplus labor economy in which the absorption rate of labor is persistently low. This is not to deny that much of Europe had a large surplus (rural) population when welfare policies were first adopted. As Pandit and Casetti (1989) have shown, however, the level and rate of absorption of labor into the manufacturing sector was considerably slower in the developing world than in the now developed countries. This was further exacerbated by trends in the twentieth century towards greater mechanization, whereas the early industrialization experience was more labor-intensive (Baer and Herve, 1966).

[20] These government efforts are decommodifying in the sense that workers become less dependent on the market.

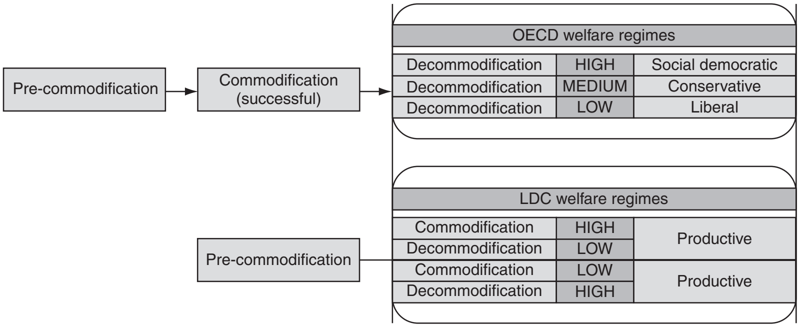

Figure 4.1 The era of embedded liberalism: welfare states in developed and developing countries

Source: The OECD decommodification rankings (low, medium, high) are from Esping-Andersen (1990: 52).

to address the lack of proletarianization and pursue their primary objective of creating a modern industrial order. Government intervention in the economy was guided by one of two goals: making firms internationally competitive, or insulating firms from international competition.[21] Why political leaders pursued one strategy over another is based on a whole host of factors, and is explored elsewhere (see Waterbury, 1999).[22] Central to this investigation is the fact that ruling elites pursued social benefits compatible with the chosen development strategy, and key to this compatibility was the co-optation of potentially powerful groups.[23] None of the elements of welfare state regimes were designed with poverty alleviation in mind.

[21] While state intervention could be directed towards both goals, historically LDCs have tended to advance in one area while retreating in the other. See statist literature for further arguments that government representatives are not simply a passive registrar of interests, implementing goals for what they perceive as the beneficial interests of society (e.g. Evans, Rusechemeyer, and Skocpol, 1985). It could be argued that governments had more policy-making autonomy during the initial stages of industrialization, given the disproportional reliance of capital and labor on the state.

[22] One possible objection is that the causal arrows could be reversed, and high levels of human capital (commodification) influenced LDCs to be more accepting of international market participation. While there might be some merit to this claim, a relatively highly educated workforce was no guarantee that LDCs would pursue outward-oriented strategy. Argentina and Uruguay, for example, had the highest rates of literacy (91 percent) in the developing world in the 1960s; they pursued the alternative strategy, however, and rejected an emphasis upon international market participation.

[23] This was feasible as the planned nature of industrialization meant that governments more or less knew who would be the winners. Even in the export-oriented countries (e.g. Taiwan, South Korea), governments "led" the markets and "picked" the winners (see, for example, Wade, 1990).

Protective welfare states have roots in a political economy that historically eschewed emphasis on international markets and ultimately focused government efforts on insulating domestic firms from international competition. This focus allowed politicians to exercise maximum discretion and control over the economy, particularly in the early stages. Absent the threat of international market competition and pressures of cost containment, rulers could provide allowances to workers *and* firms in the major industrializing sectors. Politicians had the flexibility to introduce direct and immediate benefits to workers that were contrary to employers' economic interests, mostly because the latter were compensated for through other means (e.g. tariffs, subsidies).

As a consequence, protective welfare states are a curious fusion of elements of socialism and conservatism. Like the OECD social democratic model, protective welfare states have a strong distrust of markets. Both regime types claim to detest the dehumanizing effects of unfettered capitalism. Commonalities with the statist variant of the conservative model also exist, particularly with its emphasis on the preservation of authority (see Huber, 1996). The conservative forces in protective welfare states fear that international markets can destroy their power and privilege.[24] Leaders thus prefer social rights that simultaneously promote loyalty to the state and create divisions among social groups (labor and business).[25] Full-scale commodification would certainly make it difficult for the state to be *the* most dominant factor in the expanding international economy.

At the same time, protective welfare states in developing countries are distinct from both the social democratic and conservative welfare models in that policies and strategies directed specifically towards reducing poverty are negligible. The pivotal factor is that emphasis on decommodification occurs prior to proletarianization and, consequently, social rights are directed towards a small clientele. Welfare policies may not be redistributive and beneficent, even though they are often thought of in this way. Titmuss (1965: 27) long ago stated that "when we use the term social policy we must not [...] automatically react by investing it with a halo of altruism, concern for others, concern about equality and so on." Before proletarianization occurs, making rights conditional upon labor market

[24] See, for example, Diamond's (1987) discussion on class formation in post-colonial states. See also Esping-Andersen's (1990: 41) discussion of statism and how it was feared that capitalism would destroy power and privileges.

[25] Schneider (2004: 37) argues that, in late-industrializing nations, state intervention in labor markets, wages, unions, and strikes actually hinders the development of lasting employer organizations. Rather than organizing to deal directly with labor, businesses focus more on influencing state policies concerning labor.

attachment, some work performance and actuarialism results in welfare benefits for only a small, privileged stratum.[26] This is a sharp departure from the OECD social democratic and conservative welfare states, in which emphasis on universalism and earnings-related contributions, respectively, has guaranteed the relatively poor access to government-supported social protections (see Korpi and Palme, 1998).[27]

Productive welfare states, in contrast to protective welfare states, prioritize commodification, and evolved initially from systems that actively encouraged participation in export markets. The goal of encouraging the international competitiveness of domestic firms creates an emphasis on cost containment and requires governments to surrender some control over the economy.[28] The range of social policies is then much more limited, as rulers are constrained from pursuing worker benefits that are independent of employer interests. In other words, the policies that prevail are those that can successfully serve the interests of workers and capital simultaneously.

In this respect, productive welfare states share certain elements with the liberal model. In contrast to its counterpart, this regime type embraces some of the nineteenth-century liberal enthusiasm for the market and self-reliance. The particular property of the liberal paradigm that ultimately comes to distinguish the productive welfare state is the emphasis upon strengthening the commodity status of labor in a globalizing economy. At the same time, the fundamental point of departure from the liberal model is that the state–market relationship is complementary rather than adversarial. Considerable public intervention aims to enhance international market participation. Social policies are circumscribed by this goal and promote worker loyalty without hindering business activity.

[26] See Esping-Andersen's (1990: 48) discussion on conditions for entitlements. "Actuarialism" refers to "the idea that the individual has a personal entitlement of a contractual nature."

[27] In an analysis of eighteen OECD countries, Korpi and Palme (1998) find that earnings-related benefits and "encompassing" social insurance institutions most effectively reduce inequality and poverty. Encompassing institutions constitute universal programs covering all citizens and are combined with earnings-related benefits for the economically active population. According to Korpi and Palme, the encompassing model is found primarily in the social democratic welfare states. These countries have the lowest poverty and inequality rates. The corporatist model ranks second (between social democratic welfare states and liberal welfare states) in the alleviation of poverty and inequality. Social programs in the corporatist model are directed towards the economically active population. Because these nations are successfully commodified, however, unlike the LDCs, most individuals with low incomes are part of the (formal) economically active population and, thereby, are eligible for benefits and protections.

[28] For example, even if governments intervene in the setting of prices and wages, their decisions will be constrained by considerations of international market performance.

In contrast, the OECD nations were never driven to be "productive welfare states" per se, because the commodification process was much more gradual, spanning over two centuries, and required rather less state intervention.[29]

The tension in this model lies in reconciling the push for dependence on wage labor with demands for emancipation from the market. As argued earlier, an excessive focus on commodification puts system survival at stake (Polanyi, 1944). Furthermore, although labor market dualism will be less prominent given government measures to provide capital with an abundance of productive workers, a clear class hierarchy still exists. Efforts to keep pace with an already industrialized international economy result in the rapid, simultaneous expansion of white-collar and blue-collar work (see Koo, 1990). The ongoing controversy then is the extent to which decommodification can be selectively employed to ensure system longevity. Governments of productive welfare states can attempt to address this problem through repression or by offering some minimum level of social benefits, usually for white-collar workers. While it is feasible that a protective welfare state could eventually evolve into a productive welfare state, *the reverse is unlikely to occur*.[30]

The productive welfare state shares one common element with the protective welfare state: policies that eschew the poor. Government efforts in productive welfare states are geared towards those who can participate in the market. As a consequence, non-participants, such as the chronically unemployed, disabled, or sick, receive somewhat fewer state resources. In a manner similar to that of the liberal welfare state, work ethic norms are encouraged rather than welfare, which is frequently stigmatized. The provision of welfare for the poor is even more inadequate in productive welfare states, since the targeted or means-tested programs that are the primary poverty alleviation strategies in liberal welfare states are much less available.[31] Targeting options in developing countries are expensive, because of the administration costs of identifying, reaching, and monitoring the target population (see Grosh, 1994).

[29] Recall that proletarianization was supported initially by private and non-governmental institutions. Much of the OECD welfare states literature takes commodificaton as a given, and focuses instead on government attention to developing a *highly* skilled workforce and training systems. See, for example, Hall and Soskice (2001).

[30] In other words, if productive welfare states are successful, they cannot become "protective," since the latter emphasize decommodification *before* commodification.

[31] Targeted or means-tested programs are aimed at recipients who fall below a nationally mandated income level or property limit. Korpi and Palme (1998) reveal that liberal welfare states that apply targeting as the means to reduce poverty are the least successful at reducing poverty. The social democratic and corporatist welfare states place less priority on means-tested programs.

4.2.4 *Cluster analysis: testing contrasting hypotheses*

Do developing countries display convergence or extreme divergence? Or, as this chapter posits, are they characterized by systematic divergence? Is it possible to discern a distinct statistical pattern that lends support to the idea that different welfare models in the developing world do exist and that they correspond to the protective/productive typology outlined above?

Cluster analysis is a quantitative method that can help discriminate between the above hypotheses. By facilitating the classification of objects into relatively homogeneous groups, this method can determine the number of LDC distribution regimes, if any. Each group identified by cluster analysis is as internally homogeneous as possible, but as distinct as possible from all other groups. The technique is applied to find similarities between units under classification, rather than interrelationships between variables (factor analysis). The objective is to group *n* units into *r* clusters, where *r* is much smaller than *n* (Lewis-Beck, Bryman, and Liao, 2004). Cluster analysis is one of the most popular means of constructing a typology.[32] Although it originated in psychology and anthropology, it has now become a valuable tool in biology, geography, political science, sociology, economics, and mathematics.[33]

To begin the search for natural groupings in the data, a clustering method must be selected. Partitioning, or non-hierarchical, methods do not apply here, since the number of clusters is not known a priori. Instead, I apply the hierarchical agglomerative linkage method, which considers each observation as a separate group. Next, the agglomerative algorithm considers N(N–1)/2 possible fusions of observations to find and combine the closest two groups. This process repeats itself until all observations belong to a single group, and a hierarchy of clusters is created. To begin this procedure, however, computation of a similarity or distance matrix between the entities is required. I apply the most common representation of distance, the Euclidean distance (Aldenderfer and Blashfield, 1984; Everitt, 1974) to calculate the distance between the units. To give a simple

[32] In addition to cluster analysis, the Q-sort technique is used by social scientists to develop classification schemes. This technique is unworkable, however, if the number of cases that need to be classified (thirty-two) exceeds the number of variables (ten) used for the analysis. Furthermore, the main purpose of Q-methodology is to provide the researcher quantitative means for examining *human subjectivity* (McKeown and Thomas, 1988). If accounting for self-reference is important to the researcher then the Q-method is best applied in place of cluster analysis (see Thomas and Watson, 2002).

[33] For example, cluster analysis has been used to refine diagnostic categories in psychiatry, detect similarities in artifacts by archaeologists, identify models of development in political science, and establish religiosity scales in sociology.

example, if two cases are identical, then the Euclidean distance between them will be zero. The final product is a tree-like representation of the data, or dendrogram, which illustrates the successful fusion of countries. It is completed only when all the countries are in one group.

Several agglomerative linkage methods exist in cluster analysis. The most common are single linkage, complete linkage, average linkage and Ward's method. These represent different mathematical procedures to calculate the distance between clusters. Following standard practice in the social sciences, and given the disadvantages of single and complete linkage (see Panel on Discriminant Analysis, Classification, and Clustering, 1989), Ward's method is used here and the weighted average linkage method is then applied as a robustness check.[34] Ward's method is designed to optimize the minimum variance within clusters, and works by joining groups that result in the lowest increase in the error sum of squares (Ward, 1963; Aldenderfer and Blashfield, 1984). At each stage, after the union of every possible pair of clusters is considered, the method fuses the two clusters whose increase in the total within-cluster error sum of squares is minimal. Several studies have observed that, in comparison to the above-mentioned alternatives, Ward's method ranks first in the recovery of true clusters (Blashfield, 1976; Tidmore and Turner, 1983).

Cluster analysis will confirm the systematic divergence hypothesis if it reveals a distinct number of welfare regimes corresponding to the productive/protective dichotomy. If early comparative political economy speculations of extreme divergence are correct, however, then cluster analysis will demonstrate no identifiable pattern. The number of clusters will be large, far outnumbering the two patterns predicted in this analysis. Finally, the third possibility, international political economy's predictions of convergence, will be confirmed if all developing nations fall into one cluster.

At this point, however, the IPE literature lends itself to significant ambiguity. Are less developed countries likely to converge upon productive or protective welfare states? Recall that the central process underlying convergence tendencies is the challenge of growth in a global economy. On the one hand, most IPE scholars implicitly assume that international market pressures will drive developing nations towards embracing social policies most similar to OECD liberal welfare states, which would result in LDC productive welfare states.[35] At the same time, however, as this

[34] I use the weighted average linkage method so that, if some of the clusters are small, the results will not be biased. This method gives equal weight to groups with small numbers of observations.

[35] Proponents of neoliberalism have long been encouraging LDCs to redirect public expenditure priorities towards fields offering high economic returns *and* the potential to improve income distribution, such as primary health care, and primary education.

analysis points out, since the 1930s many developing countries have found that insulating themselves from international markets has been the best way to respond to the challenges of growth in the post-war era. Consequently, it is feasible that many less developed countries may instead have evolved into protective welfare states.

4.2.4.1 Operationalizing concepts The primary goal is to assess welfare priorities in the developing world and see whether they follow the predicted pattern of privileging commodification or decommodificaton.[36] Simply applying the most common method – examining government budget priorities – is insufficient here, for three reasons. First, as Esping-Andersen (1990: 19) explains, "Expenditures are epiphenomenal to the theoretical substance of welfare states." Second, as the World Bank (1990) and the ILO (see Figueiredo and Shaheed, 1995) have pointed out, governments of developing countries often employ less resource-intensive means to protect their workers, such as labor market policies and public employment.[37] Third, it is impossible to know whether spending serves the desired goals or clientelistic needs (see Nelson, 1999; World Bank, 2003b). This issue is particularly salient in evaluating goals for commodification. If government spending is high, but the allocated resources are being misused and have little effect on improving the health and education of (potential) workers, then the country in question cannot be a productive welfare state.

The difficulty here is the dearth and questionable reliability of data that can capture such occurrences across the developing world. One solution, albeit imperfect, is to include a combination of policy, spending, and outcome variables.[38] The other alternative is to wait for more effective institutions to evolve or, relatedly, for more reliable data to become available. In such a case, the hazard is that policy-makers and citizens of LDCs are likely to face the consequences of a vicious cycle involving insufficient data, the neglect of important research, and the persistence of weak, ineffective institutions. Put simply, more effective welfare institutions may be dependent upon analyses such as this one, which attempt to make use of available data.

[36] Significantly, the concept of decommodification applied in this analysis is necessarily broader than Esping-Andersen's (1990) interpretation. For critiques of Esping-Andersen, see Lewis (1997), Gal (2004), and Room (2000).

[37] Arguably, while these policies command fewer government resources, they may ultimately be more expensive for the larger society in LDCs.

[38] How the inclusion of outcome variables helps the data problem is explained in more detail below.

Exercising the first option, I build on the insights of the most renowned experts of welfare in both developed and developing countries – Esping-Andersen (1990) and Dreze and Sen (1989), respectively – to determine the most appropriate indicators of developing world welfare states.[39] Spending and outcome variables are used to capture extensive public efforts aimed directly at expanding the basic capabilities of the population to suit wage labor markets. An emphasis on decommodification is detected by pervasive policies and government spending geared towards protecting individuals from the risks and uncertainties of the market. Protective welfare policies are then more commonly associated with (but not limited to) social-insurance-type variables. According to Esping-Andersen (1990: 22), decommodification ultimately "strengthens the worker and weakens the absolute authority of the employer." While it is reasonable to expect some overlap between "productive" and "protective" variables in practice, the division is driven by two very different logics and produces distinct socio-political outcomes (Dreze and Sen, 1989; Esping-Andersen, 1990).[40] See appendix I for more detailed explanations of the data sources and variables discussed below.

4.2.4.2 Variables representing productive welfare efforts Degrees of commodification are determined by the level of public investment in primary and secondary education, and basic health care, as well as literacy rates, rates of infant mortality, and the percentage of infants vaccinated against diphtheria, pertussis, and tetanus (DPT).[41] In the cluster analysis, I observe government expenditures on education and health as a proportion of the total public budget, since the aim here is to capture the extent of *government commitment* (see Rudra and Haggard, 2005). To put this in perspective, if education spending, for example, is measured instead as a percentage of GDP, countries such as South Korea and Singapore fall in the same percentile range as developing countries such as Mali, Malawi, and Liberia. All the same,

[39] The productive/protective dichotomy builds on Dreze and Sen's (1989: 16) distinction between "promotion" and "protection." In particular, Dreze and Sen's choice of promotion variables, or resources devoted to improving primary education and health, are used to determine "commodifying" or productive welfare states. The "decommodification" concept is drawn mainly from Esping-Andersen (1990). His argument that decommodification ultimately ensures that human fate is not directed by the laws of the market is central to the selection of "protective" variables in LDCs.

[40] For example, some scholars may argue that protective welfare benefits (e.g. pensions, labor protections) make workers more productive in the marketplace. The productive/protective dichotomy deals with ideal types and, in reality, we should expect some overlap, or modal tendencies of population distributions, between the polar alternatives.

[41] Note that immunization against measles is also included and does not affect the cluster groupings (not shown here).

measuring spending relative to the total budget more clearly reveals qualitative differences between LDC welfare states, and unveils a considerable variance between countries. As a compromise, I apply spending as a percentage of GDP and per capita spending as robustness checks.

The outcome variables (literacy, mortality, and immunization rates) help the analysis for two reasons. First, outcome variables reflect past policies. Nations with a legacy of responsiveness to international markets are likely to have pursued market-promoting social policies at an early date. In other words, if developing countries have high "outcomes," it suggests that previous leaders have emphasized commodification. This is particularly relevant since, as previously explained, once an economy has successfully achieved commodification the country cannot thereafter become a protective welfare state. Second, outcome variables can help see beyond the numbers. Public officials might be engaging in high levels of clientelism, using resources for patronage purposes rather than effecting positive outcomes. From this perspective, high levels of spending alongside low outcomes are telling, indicating weak government commitment towards a productive welfare state. Nevertheless, since other factors might determine outcomes in addition to government spending (efforts of non-governmental institutions and organizations, GDP, etc.), I drop all the outcome variables and run the model again as a check. The cluster groupings are almost identical, although, as predicted, the differences between clusters are less obvious *but still statistically significant* (see appendix J).

4.2.4.3 Variables representing protective welfare efforts Five variables capture the extent to which developing country governments aim to decommodify, or protect workers from market risks and uncertainties: the extent of public employment, spending on social security and welfare (pensions, family allowances, unemployment, old age, sickness and disability), housing subsidies, labor market protections, and investment in tertiary education. As a final point, while means-tested poor relief should also be included as a protective welfare mechanism, cross-country comparable data are virtually non-existent.

Public employment is one of the most pervasive methods of market protection in the developing world (see Rodrik, 1997c). In some cases, it provides short-term security in earnings, such as hiring for public work projects, but in the larger number of instances the public sector provides "secure" jobs (Rodrik, 1997c; Gelb, Knight, and Sabot, 1991). As Robinson states:

> The permanent status that many, in some cases the majority of, civil service employees enjoy means that apart from dismissal for grave disciplinary reasons they are assured of employment until retirement, providing a degree of protection

and privilege not found in the private sector. (Robinson, as quoted in Rodrik, 1997c)

Given that cross-country comparable data on public employment are extremely sparse, the percentage of the government budget that is spent on employee wages and salaries is used to estimate this variable.

Analyzing spending on social security and housing as a means to guard against income risks is common in the broader welfare literature. In developing countries, pensions tend to be the largest component of this spending. They ensure a steady flow of income over a lifetime, regardless of market shocks and uncertainties. Unemployment, family allowances, and sickness protections, though less common in developing countries, provide security in the face of short-term absence from the market. Housing subsidies also help stabilize incomes (Chapman and Austin, 2002; Renaud, 1984). Higher-skilled workers, and especially civil servants, often receive housing as part of their wage package.

Labor market protections are common welfare measures in the developing world that help "guarantee" incomes by placing institutionalized restrictions on firms' hiring and firing decisions (Betcherman, Luinstra, and Ogawa, 2001). Data for such protections, however, are beset with problems (Rama and Artecona, 2002). One reliable, albeit crude, indicator is the ratification of ILO conventions by nations. Enforcement standards are effectively nil, and ratifications do not necessarily translate into policy innovations. Recent research has shown that ratification has a significant effect on labor costs (Rodrik, 1996), however, and can reflect internal political factors such as government preferences or the power of left-wing parties (Brookmann, 2001). It is fair to assume, then, that labor market protections will be relatively low in countries that have ratified a very low number of ILO conventions (e.g. the United States, South Korea, Singapore).[42]

Lastly, the provision of free or heavily subsidized tertiary education when primary- or secondary-level education access is less than universal awards a strong promise of future income security to those who have access to the former (see World Bank, 2002b).[43] Particularly

[42] As a robustness check, I also run "labor regulation data" constructed by Botero *et al.* (2004). The drawback in using this data set is that it focuses on one year, and data are missing for three LDCs from the sample. Excluding the major outliers, the correlation between the ILO data in the sample and Botero *et al.* is 0.65. The final results differ in that Panama, Paraguay, Greece, Colombia and Thailand fall from cluster 1 (productive) to cluster 2 (dual).

[43] Demographics play an important role in determining levels of public spending on education and social security. Note that, in addition to assessing the different levels of education spending (primary, tertiary) as a percentage of total government expenditures, they are also measured as a percentage of GDP, and spending per student relative to GDP per capita. Although the final cluster results are minimally affected by the alternative

Table 4.1 *Determining the number of clusters by the Duda and Hart (1973) procedure*

	Duda/Hart	
Number of clusters	Je(2)/Je(1)	pseudo-T-squared
1	0.6329	17.4
2	0.5907	12.47
3	0.6622	5.1
4	0.5848	9.94
5	0.4350	7.79
6	0.4675	2.28
7	0.3835	3.21
8	0.6985	3.45
9	0.5853	4.25
10	0.3488	5.6

since high-skilled labor is in relatively high demand yet scarce supply in the majority of developing countries, such workers can secure great advantages in the bargaining process.

4.3 Analysis results

The results of the cluster analysis are shown in tables 4.1–4.3. Because cluster analysis has a low tolerance for missing data, the final sample size is thirty-two countries. This sample is still marked by regional and economic diversity, and thus remains fairly representative of the developing world. Each variable represents data averages for 1990 through 1997 (the latest date for which cross-national data are available for a large number of

specifications, the latter is emphasized since it is the only measure that takes demographics into account. Several countries in Africa and south Asia, for instance, show average levels of spending on primary education. Because these LDCs have the highest growth rates of school-age population, however, the number of children actually benefiting from state assistance is quite small, and the lack of funds is creating an education crisis. Evaluating LDCs on the basis of spending per student provides a more accurate assessment of commitment to primary education. Zambia, Bangladesh, and Malawi are excellent examples. This measure also effectively captures disproportionate spending on small populations of students enrolled in tertiary education. For SS and welfare, however, controlling for number of beneficiaries is more complex, since the data do not tell us the number of aged persons receiving these benefits. In addition, this category is not limited to pensions. Nonetheless, to get a general sense of the impact of elderly demographics, a variable is created by dividing the social security and welfare data by the proportion of persons aged over sixty-five. The results are very similar, with only Panama dropping from cluster 1 to cluster 2.

Table 4.2 *Cluster groupings*

Country	Cluster
Chile	1
Colombia	1
Costa Rica	1
Cyprus	1
Greece	1
Israel	1
Kuwait	1
Malaysia	1
Mauritius	1
Panama	1
Paraguay	1
Singapore	1
South Korea	1
Sri Lanka	1
Thailand	1
Trinidad and Tobago	1
Argentina	2
Brazil	2
Mexico	2
Uruguay	2
Bolivia	3
Dominican Republic	3
Egypt	3
El Salvador	3
India	3
Iran	3
Lesotho	3
Morocco	3
Tunisia	3
Turkey	3
Zambia	3
Zimbabwe	3

Notes: South Korea is included because it did not become a member of the OECD until 1996. Turkey is included because, although a member of the OECD since 1961, it is not a high-income country. Greece is included because it has only recently been classified as a high-income country by the World Bank.

developing countries). Results are analyzed in the following three steps: (1) assessing how many cluster groups exist; (2) determining which countries fall into each cluster; and (3) evaluating the characteristics of each cluster and its member countries to assess whether or not they confirm systematic divergence.

Table 4.3 *Cluster analysis*

		Commodification						Decommodification					
	Country	Immunization	Infant mortality	Literacy	Primary and secondary education spending	Health spending	*Country average*	Housing spending	ILO conventions	Wages and salaries spending	SS and welfare spending	Tertiary education spending	*Country average*
Cluster 1 (productive)	Chile	9	8	8	2	10	*7*	7	7	3	10	2	*6*
	Colombia	2	6	6	7	9	*6*	5	8	2	4	3	*4*
	Costa Rica	7	8	8	5	10	*8*	1	7	10	8	5	*6*
	Cyprus	10	9	9	9	5	*8*	6	7	6	9	1	*6*
	Greece	4	9	9	3	7	*6*	3	9	4	8	2	*5*
	Israel	10	10	7	9	6	*8*	8	6	1	9	4	*6*
	Kuwait	7	9	3	8	3	*6*	6	3	4	5	9	*5*
	Malaysia	8	8	5	8	4	*7*	9	3	5	3	8	*6*
	Mauritius	6	7	5	7	8	*7*	7	4	7	7	9	*7*
	Panama	5	6	7	4	10	*6*	6	9	9	9	4	*7*
	Paraguay	1	5	7	2	4	*4*	5	5	9	6	7	*6*
	Singapore	8	10	6	5	5	*7*	9	3	6	1	5	*5*
	South Korea	5	10	10	6	1	*6*	4	1	1	5	1	*2*
	Sri Lanka	7	7	6	7	3	*6*	3	4	3	7	8	*5*
	Thailand	8	5	8	6	8	*7*	6	2	7	1	3	*4*
	Trinidad and Tobago	6	7	10	3	8	*7*	10	2	9	7	7	*7*
	Cluster average	*6*	*8*	*7*	*6*	*6*	*7*	*6*	*5*	*5*	*6*	*5*	*5*
Cluster 2 (dual)	Argentina	3	6	9	6	1	*5*	3	9	4	10	2	*6*
	Brazil	2	4	5	2	5	*4*	1	10	1	9	5	*5*
	Mexico	5	5	6	1	2	*4*	4	10	4	8	3	*6*
	Uruguay	9	7	10	4	4	*7*	1	10	2	10	3	*5*
	Cluster average	*5*	*6*	*8*	*3*	*3*	*5*	*2*	*10*	*3*	*9*	*3*	*5*
Cluster 3 (protective)	Bolivia	1	1	4	1	3	*2*	2	6	7	8	6	*6*
	Dominican Republic	1	3	4	1	9	*4*	10	4	5	2	1	*4*
	Egypt	4	2	1	8	2	*3*	8	8	4	4	6	*6*
	El Salvador	3	4	2	1	9	*4*	5	1	10	3	1	*4*
	India	1	2	1	4	1	*2*	8	5	1	2	8	*5*
	Iran	10	4	2	3	7	*5*	9	1	10	5	7	*6*
	Lesotho	3	1	3	10	9	*5*	5	1	7	1	10	*5*
	Morocco	6	2	1	10	2	*4*	2	6	8	4	8	*6*
	Tunisia	9	5	1	9	6	*6*	7	8	7	6	9	*7*
	Turkey	2	3	4	5	3	*3*	3	5	9	2	5	*5*
	Zambia	4	1	2	2	6	*3*	2	6	2	1	10	*4*
	Zimbabwe	6	3	5	10	6	*6*	10	1	8	5	10	*7*
	Cluster average	*4*	*3*	*3*	*5*	*5*	*4*	*6*	*4*	*7*	*4*	*7*	*6*

Notes: The cluster analysis results have been calculated using *wardslinkage* command in Intercooled Stata 8. The stopping rule is Duda and Hart (1973). Averages are rounded to the nearest integer to facilitate comparability. Housing, health, and social security and welfare are ranked according to percentage of total government spending. Education variables are ranked as spending per student (refer to footnote 43). Note that, as explained later in the text, the membership of Panama, Paraguay, and Greece in cluster 1 is not robust.

The first critical step is to determine the number of clusters present in the data. The appropriate number is a question of particular interest, since it can provide support for the ideas of either comparative or international political economy, or for systematic divergence. If, as implied by CPE scholars, no cluster structure is shown then efforts to identify a few broad categories of welfare states among developing countries are meaningless. The distinctions between countries are greater than the similarities between them. At the other extreme, a single cluster would imply that developing countries as a whole are a relatively homogeneous group. The IPE view then prevails, and state intervention to "create a modern industrial order" has had more or less the same welfare consequences in all developing countries.

Over thirty "stopping rules" (procedures to determine the number of clusters in a data set) are applicable in cluster analysis. Fortunately, Milligan and Cooper (1985) have conducted a well-known study to distinguish between them and assess which criteria provide the most valid test for the existence of a cluster. Their experiment suggests that the Duda and Hart (1973) procedure is one of the best stopping rules. The ratio criterion for this procedure is Je(2), which is the sum of squared errors within a cluster when the data are broken into two clusters. Je(1) provides the squared errors when one cluster exists. The three-group solution is most distinct here, since the sum of squared errors (Je(1)) increases substantially in the four-group solution. Duda and Hart Je(2)/Je(1) estimates are presented in table 4.1. The conventional rule for deciding the number of groups is to determine the largest Je(2)/Je(1) value (0.6622) that corresponds to a low pseudo-T-squared value (5.1) that has a higher T-squared value above and below it. The results from this method, surprisingly, indicate that a *three*-group solution is most distinct in this hierarchical cluster analysis, contrary to the expected two ideal regime types.

The next step is to determine which countries are in each cluster. Table 4.2 presents the country members of the three clusters. This pattern reveals that, although region plays a role, it is not a predominant factor in the welfare groupings. While only Latin American countries comprise cluster 2, the members of clusters 1 and 3 represent Africa, the Middle East, east Asia,[44] Latin America, and south Asia. Income effects appear to play a somewhat larger role, although, again, not a decisive one. Cluster 3 contains only low-income and lower middle-income countries. Cluster 1 reveals a more economically diverse set of countries, however, ranging from lower middle-income to high-income LDCs. This finding shows that poorer

[44] Indonesia, originally included in cluster 3, has to be dropped from the analysis because the data necessary for robustness checks are missing.

nations can also successfully promote commodification. Similarly, cluster 2 contains both low middle- and high middle-income countries.

The existence of three clusters fundamentally challenges both the extreme divergence and convergence hypotheses. The next logical question is whether the statistical analysis supports systematic divergence. To assess this, the clusters are ranked according to their levels of welfare efforts towards protection and production. Decile data are computed for each welfare variable, and then each cluster (and country) is ranked from one to ten. For example, the first decile is the point with 10 percent of the data below it and 90 percent above it. It is given the lowest score of one. The ninth decile is the point with 90 percent of the data below it, while the score given to values within the top 10 percent is ten. Table 4.3 displays these values. The greatest weight is placed on the cluster averages, since the statistical procedure uses algorithms to differentiate the most homogeneous *groups*. It is noteworthy that differences between deciles tend be quite significant.[45] The average for each country within the cluster is important, but each welfare category contains information that should not be overlooked. See appendix K for a graphical representation of the results (dendrogram).

Focusing on the cluster averages, several patterns emerge. Clusters 1 and 3 appear to favor the productive and protective components of welfare, respectively. Cluster 2, in contrast, favors neither welfare state category. This discovery reveals that some LDC welfare states take dual roles in the post-war economy, raising questions about whether dual welfare state status is transitory. A detailed breakdown of the clusters is given below.

Cluster 1 clearly privileges commodification over decommodification. As would be expected, several of the east Asian economies, as well as some Latin American countries noted for their emphasis on education (e.g. Costa Rica), fall into this category. The average scores for commodification are higher than the average scores for decommodification in most of the member countries. Panama and Paraguay appear to be anomalies, since their scores do not appear to reflect the prioritizing of productive welfare activities. This turns out not to be too surprising, however, for, as we shall see, further robustness checks reveal that these two countries (along with Greece) appear to be sensitive to model specification and fluctuate between clusters 1 and 2.

In cluster 3, empirical evidence for the developing world welfare paradox is highly suggestive: poorer countries, which arguably need

[45] For example, LDCs falling in the sixth decile for primary education spend almost 30 percent more per student per capita than do those in the fifth decile.

productive welfare states the most, appear to be expending the least effort towards this goal. Attention to housing and tertiary education seems to feature most prominently in the protective welfare states. The outcome variables are telling. For several developing countries (e.g. Egypt, Lesotho, Morocco), despite their high spending on primary education, literacy rates remain low. This suggests that funds either are being used for clientelistic purposes or are simply incommensurate with the level of need. Health spending also appears to be regressive in relation to outcome variables. On the other hand, several LDCs in this category rank in the top percentiles for protective categories such as wages and salaries and tertiary education.

The smallest group, cluster 2, appears to place emphasis on productive and protective activities, yet average scores for both welfare categories are moderate (i.e. five). This cluster is more appropriately labeled a *weak* dual welfare state, since these countries place more emphasis on the proletarianization process than the protective welfare states, but significantly less than the productive welfare states. In terms of commodification, the difference between cluster 2 and cluster 1 is that health and education are *both* stressed in the latter.[46] Uruguay is an exception; its level of health spending is low relative to cluster 1, however. Brazil's profile is also distinct, in that, although education spending is low and outcome variables are not as high as other members of cluster 2, its literacy rates outrank similar middle-income countries in cluster 3. Most striking is that, on the protective side, cluster 2 ranks in the highest percentile for labor protections (ILOCNV) and social security and welfare. On the other hand, average scores for housing, wages and salaries, and tertiary education spending are considerably lower than in clusters 1 and 3.

The existence of cluster 2 is an important revelation. Based on the theoretical discussion, we can assume that governments of weak dual welfare states in the early post-war period were not completely hostile to international markets. It is certainly possible to be primarily inward-oriented but, at the same time, encourage some export competitiveness. Cluster 2, then, represents a combination of the two ideal regime types: social policies that respond to the demands of capital *and* the needs of labor groups. Consequently, relative to the other two clusters, we might expect heightened political competition for scarce public resources. Partisan politics, for example, may be vibrant in these countries. One optimistic scenario, if partisan politics can successfully steer greater productive welfare efforts, is that they can then offset the tendency towards

[46] Notice that, in cluster 1, the spending or outcome variables (or both) in health and education are high.

Table 4.4 *Effects of current welfare regimes on poverty (percent undernourished)*

Independent variable	Coefficient estimates
LDC welfare regime	0.57
(commodification/decommodification)	(0.87)
Democracy	0.18
	(0.70)
GDP per capita	−8.33***
	(2.88)

Notes: *** = $p < 0.01$. $N = 28$, $R^2 = 0.37$. Robust standard errors in parentheses. Data for "percent undernourished" from the UNDP's *Human Development Reports*: http://hdr.undp.org/statistics/data, accessed May 3, 2006. Note that "welfare regime" remains insignificant when "GDP per capita" (and "democracy") is dropped from the model because of potential multicollinearity issues (with "welfare regime").

elitism engendered by early decommodification policies. This raises questions about the transitory nature of this cluster; weak dual welfare states could get mired in partisan politics that ultimately perpetuate the status quo (if capital and/or protected labor wins), or they could move incrementally towards productive welfare status (if structurally unemployed labor groups win).

Confirmation of the protective/productive welfare typology supports the contention that welfare regimes in developing countries have been geared towards privileging higher-income groups. Put another way, very low-income individuals excluded from the market receive the lowest priority for social protections in all three regime types. The primary beneficiaries in protective welfare states are a small group of formal-sector workers, while, in the productive welfare state, only income-earners (actual and potential) enjoy some guarantee of a steady stream of income through education opportunities. The poverty tables in appendix L suggest that regime types are uncorrelated with levels of poverty; countries in all three categories maintain extremely high poverty rates. This does not, however, rule out the possibility that certain developing world welfare models might have *indirect* effects on poverty, simply through encouraging greater economic growth.

Table 4.4 takes a more systematic look at whether developing country welfare regimes focus on protecting the poor. The multiple regression technique assesses whether developing country welfare regimes have any *direct* effect on poverty alleviation. To operationalize regime types, I subtract each country's decommodification score from its commodification score in table 4.3; higher values are thus associated with productive welfare states.[47] A negative and significant coefficient would suggest that, as the score increases (regimes are more productive), poverty is reduced, and, when the score decreases (regimes are more protective), poverty increases. Conversely, a positive coefficient means that, as the measure is increased (regimes are more productive), poverty is increased, and, when the measure is decreased (regimes are more protective), poverty is decreased. The percentage of the population that is undernourished is used as a proxy for poverty, since alternative poverty data are sporadic at best for these countries.[48] As expected, the coefficient for welfare regime type is insignificant, suggesting that LDC welfare regimes are *not* directed towards protecting the poor. Since small sample size can be a problem, I also re-estimate the results using a bootstrapping technique.[49] The findings are unaffected.

4.3.1 Robustness checks

Do the cluster results hold up to changes in the conditioning information? The results for the cluster groupings and member countries are highly robust to three important changes. First, I run the analysis using an alternative to Ward's method. One common problem associated with Ward is that it tends to be heavily influenced by outliers (Ketchen and Shook, 1996). To check this, I use instead the weighted average method, which gives groups equal weighting in determining the combined group, regardless of the number of observations in each group. Given that differing clustering methods most often produce different results, Lorr (1983) suggests that similar results from two distinct methods provide great confidence that the underlying structure is being recovered. As second and third robustness checks, I substitute the welfare variables measured relative to GDP and GDP per capita in place of those measured as a proportion of total public expenditures. With the exceptions of Greece, Paraguay, and Panama, which fall into cluster 2 (instead of cluster 1), the results are identical in both models.

[47] I also estimate the model substituting the cluster variables (1= productive, 2 = dual, 3 = protective) with commodification/decommodification scores, and the results are the same.

[48] Data on numbers of undernourished people are still unavailable for four countries, however: Cyprus, Greece, Israel, and Singapore.

[49] Small sample size can influence the ratio of the coefficient to standard error upon which the statistical inferences are based. The bootstrapping technique uses the small sample as a good approximation of the unobserved population, and then draws samples with replacement over a given number of replications, in this case 1,000. The large number of replications increases confidence in the sampling distribution.

4.4 Initial interpretation of the results

The cluster results suggest that developing countries tend to favor either productive or protective welfare states. Scholars from a variety of disciplines have long recognized the intrinsic and instrumental values of *both* productive and protective types of social legislation (see, in particular, Dreze and Sen, 1989). So why, then, the ultimate trade-off between commmodification or decommodification efforts in LDCs? Close attention to how historical legacies of managing state–international market tensions have affected welfare states sheds some insights on these results. Building on the neoclassical political economy (NPE) and historical institutionalist literatures, it can be understood that the initial choice of development strategy and complementary welfare policies create distributional coalitions, which thereafter have a vested interest in maintaining existing institutions and reinforcing them.[50] This analysis therefore presents the possibility that institutional continuity is linked to the role of positive feedback effects from the original distribution regimes.

The NPE literature maintains that state intervention encourages the formation of narrow interest groups that engage in rent-seeking behavior.[51] Government intervention in protective welfare states initially creates social policies that cater to the groups empowered (directly or indirectly) by minimal international market exposure (i.e. workers in the civil services, the military, urban formal-sector and salaried workers). These distributional coalitions make it increasingly difficult for the government to engage in the significant amount of redistribution required to promote commodification. Productive welfare states, on the other hand, introduce benefits acceptable to employers struggling to compete in the international economy. Demands for greater labor benefits are subsequently met with stiff political resistance. Leaders are ultimately loath to pursue policies that alienate their traditional support groups and increase social instability. As a consequence, this self-reinforcing process suggests that, once welfare regimes are institutionalized, actors and interests may undergird their existence.[52]

Testing the precise causal relationship linking industrialization strategies, welfare regime types, distributional coalitions, and path

[50] This proposition derives from arguments that state intervention creates distributional coalitions (see Colander, 1984, and Srinivisan, 1985), and also builds on the institutionalist theories of path dependence (see Thelen, 1999, 2004).

[51] The term "rent-seeking" refers to lobbying activities triggered by different licensing practices of governments. The increased income gains of the beneficiary occur at a loss to the greater society. For examples, see Srinivisan (1985) and Collander (1984).

[52] This path dependence can be disrupted by significant events such as repressive dictatorships or economic crises. See, for example, Collier and Collier (1991).

dependence is beyond the reach of this analysis on account of the data problems involved.[53] Nonetheless, one way to assess if there is some link between countries' initial decisions regarding the extent of their participation in international markets and the welfare regimes that evolve (and persist) is to compare early development strategies with the recent (1990s) cluster groupings. Signs of such a connection can be taken as a preliminary indication that social actors who benefit from the original welfare arrangements make reversals increasingly unlikely.

To get some sense of initial post-war development strategies, I examine the level of manufactured exports (as a percentage of GDP) in each country at the earliest dates available and compare this to their 1990s commodification/decommodification scores.[54] After crises erupted in many developing countries following their initial experimentation with import substitution, most had settled upon their distinct industrialization strategies by the late 1960s and early 1970s. Unfortunately, the earliest available export data for most developing countries date from the 1970s. Economies that focused on orienting firms towards international markets are expected to reflect high levels of manufactured exports. Figure 4.2 lends support to the assertion that more inward-oriented LDCs (low manufactured exports) in the earlier decades tend towards protective welfare regimes (low commodification scores) in the present. These data thus provide the first indications of a connection between early development strategies, the implementation of (initially) compatible social policies, and the distributional coalitions that evolve to defend it.[55]

To evaluate the relationship between initial development strategies and developing country welfare regimes further, I perform a multiple regression test on the thirty-two cases using robust standard errors to correct for heteroskedasticity. I control for two common variables said to affect government investment in commodification: GDP per capita and democracy (for examples, see Brown and Hunter, 1999, and Kaufman and Segura-Ubiergo, 2001). The regression results, summarized in table 4.5, suggest that the initial development strategy has a significant effect on current welfare regimes and thus provides greater support for "lock-in."

[53] Operationalizing distributional coalitions across countries, for example, is extremely difficult in this type of analysis.

[54] I focus on manufactured export ratios instead of trade ratios in order to obtain a more precise indicator of industrialization strategy. For instance, LDCs that export abundant primary products but were focused on inward-oriented industrialization strategies have high trade ratios that would make them appear outward-oriented. The commodification/decommodification scores are calculated by subtracting each country's decommodification score from its commodification score in table 4.3.

[55] Note that, as the previous section details, the categorization of Paraguay and Panama in cluster 1 is not robust.

Table 4.5 *Effects of early development strategies on current welfare regimes*

Independent variable	Coefficient estimates
Manufactured exports (1970s)	0.70**
	(0.34)
Democracy	0.14*
	(0.076)
GDP per capita	0.77**
	(0.29)

Notes: ** = $p < 0.05$; * = $p < 0.10$. N = 32, $R^2 = 0.41$. Robust standard errors in parentheses.

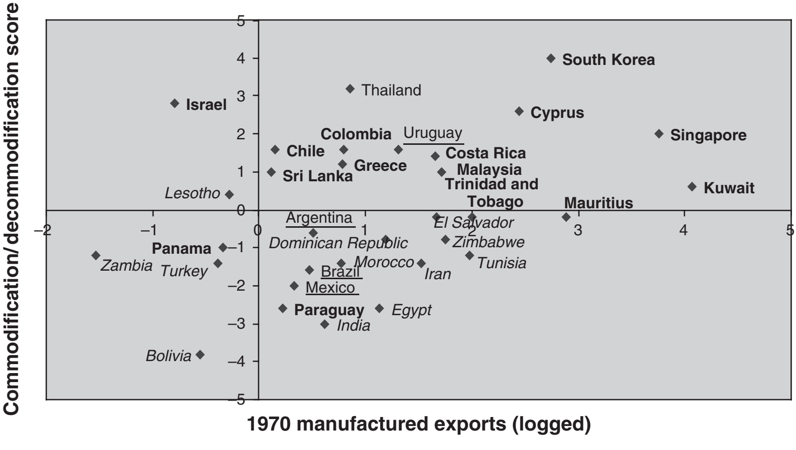

Figure 4.2 Welfare regimes and early development strategies

Notes: Productive welfare states are represented in bold, dual welfare states are underlined, and protective welfare states are italicized.

"Manufactured exports" is intended to represent a political variable, since it serves as a proxy for enduring distributional coalitions formed in the early stage of development.

The sample size is admittedly small and, as stated earlier, can be problematic. To increase confidence in the results, I apply the bootstrap technique once more, and again get similar results.[56] The persistent

[56] I also run ordered probit models using the 1990 cluster category (1 = productive welfare, 2 = (weak) dual welfare state, 3 = protective) as the dependent variable and find similar results. I do not present these results because reporting the coefficients of an ordered probit model is quite involved, and the consequence of small sample size in probit models is greater than it is for least squares estimation (Hart and Clark, 1999).

effects of early development strategies should still be viewed with caution, however, since country-specific variables (e.g. initial factor endowments, history, culture) and data for important political controls (e.g. partisanship) are unavailable. These results nonetheless bolster the argument for a relationship between early development strategies and current developing world welfare regimes.

This exposition does not allow any analysis of institutional change. Clearly, some countries have experienced changes in their welfare regimes such that they no longer correspond to their early development strategies. For example, nations such as Colombia and Costa Rica pursued mostly inward-oriented development strategies in the early post-war era, and yet they are productive welfare states.[57] Already steps ahead, research on OECD distribution regimes has convincingly shown how endogenous political dynamics can alter supporting coalitions and their functional roles to produce very different institutional arrangements (see Pierson, 2004, and Thelen, 2004). The role of distributional coalitions in creating "lock-in" has only been implied here. In the case study chapters, although a more rigorous theoretical analysis and testing of *both* institutional reproduction and transformation are beyond the scope of this project, I undertake a preliminary analysis of institutional change.

4.5 Implications

This study challenges prevailing comparative and international political economy conceptions of developing countries by illustrating systematic divergence in their welfare states. Contrary to CPE expectations, welfare states are not necessarily by-products of post-industrial development, and they cluster into three distinct welfare regime types. Most importantly for this analysis, the findings from this chapter question IPE convergence predictions by examining the institutional content of the developing world welfare state and demonstrating that these nations maintain qualitatively different kinds of distribution regimes in the current era of globalization. As suggested by IPE analysts, the pressures of international market competition impose important constraints on policy-makers in terms of the choices made as to how best to strengthen their position in the global economy. At the same time, however, the persistent variation among the types of welfare states implies that local needs and politics continue to serve as important sources of diversity. The LDC welfare state thus

[57] Significantly, these countries contrast with LDCs that remained protective welfare states in the 1990s, even after switching to outward orientation strategies as early as the 1980s (e.g. Turkey, Morocco, India).

remains a key institution to manage the tensions and dilemmas that emerge from exposure to the international economy. The important paradox, however, one that is critical to the race to the bottom debate, is that none of these distribution regimes were originally designed to address issues of poverty. The existence of three clusters of welfare regimes well into the twentieth century intimates that developing countries, similarly to developed nations, demonstrate a sustained capacity to formulate systematically different social policies that aim to align economy and society.

Before stressing the broader implications, however, it is important to be clear about the theoretical and empirical limitations of the analysis applied in this chapter. The proposed causal explanation linking LDC policy-makers, development strategies, distributional coalitions and welfare regime type is tentative and begs further exploration. Empirically, the findings from this study can only be suggestive. The unavailability of data impresses strong limitations on the number of observations included and, consequently, the kinds of econometric tests employed. Future research would greatly benefit from more extensive and reliable time-series data.

Nonetheless, this first attempt to uncover "varieties of welfare capitalism" in the developing world based on existing data is provocative. To the extent that the analysis hits upon key differences in welfare regimes, important policy and research implications emerge. This chapter suggests the importance of going beyond simply analyzing the level of government expenditures in globalizing countries. Rather, recognizing the different domestic arrangements related to welfare in LDCs underscores the concentration of institutional protections for the middle class rather than the poor, and it provides a more precise way to assess whether the historic choices of these nations (productive, protective, dual) will endure in the face of rising international market competition. As such, a race to the bottom neither mandates convergence nor means that the poor are worse off as a consequence.

The cross-sectional nature of this analysis provides important insights on developing political economies, but it prohibits a more complete test of IPE convergence theories. One of the fundamental questions ahead, then, is whether or not developing countries are maintaining their welfare institutions *into the twenty-first century*, particularly as international market pressures intensify with the entrance into the market of such potential powerhouse countries as China and India. I now turn to the case studies to answer this question, and to explore in more detail the main findings in the quantitative analyses.

5 Globalization and the protective welfare state: case study of India

The following three chapters illustrate the findings from the previous portion of the book by selecting one representative from each cluster: a protective welfare state (India); a productive welfare state (South Korea); and a weak dual welfare state (Brazil). These case studies are intended as heuristic devices, rather than another hard test of the hypotheses in this book. The purpose of the case illustrations is to provide a more nuanced and detailed look at the primary research finding: as international market demands systematically affect government policy decisions in developing countries, distinct institutional arrangements governing the distribution of welfare persist and, as a consequence, middle-class labor groups are the ones most directly hurt by race to the bottom pressures. The country overviews essentially provide greater in-depth analysis of how national social policy configurations are structuring responses to globalization. The addition of the case study analysis allows a more applied understanding of the consequences of globalization in terms of cutbacks (RTB) *and* institutional changes. In addition, they permit consideration of the role of other factors not emphasized in the quantitative analysis, such as democracy.

One caveat should be kept in mind as the case studies unfold in the following chapters. Because the causal linkages have been empirically verified in the earlier chapters, I take on the broad panorama of each country's political economy and related social welfare strategies in a swift, bold, and unrestrained manner. In other words, the quantitative analysis serves as the primary guide to this schematic interpretation of the seemingly unrelated, chaotic, and complex events related to a race to the bottom. I dare say that, if these chapters were to be viewed in isolation from the previous discussion, some readers would find the interpretation of events capricious, and it would certainly not win the plaudits of experts and practitioners specializing in specific areas of welfare reform in these countries. My primary goal, however, is to provide a broad, contextual understanding of the relationship between the race to the bottom, domestic politics, and welfare policies in developing countries.

Beginning with the case of India, this chapter confirms that RTB pressures are quite real. Total government expenditures have decreased by almost 6 percent since India adopted liberalization policies in 1991.[1] Even more alarmingly, government social security, health, *and* education expenditures have concomitantly declined since 1991, suggesting that the resources devoted to this particular sector are being targeted as efforts to impose fiscal discipline and prepare for international competition intensify.[2] Manmohan Singh, the minister of finance from 1991 to 1996 and the current prime minister, made a telling statement in 1992 about how globalization and race to the bottom pressures in social welfare funding were constraining the Indian government's room to maneuver:

> Some people have criticized the stabilization program as being anti-poor. I admit that in an economy which has been living beyond its means, stabilization does hurt… It is true that the fiscal compulsions have forced us to restrain the growth of all expenditure, including social expenditure. But considering that interest payments are a fixed contractual obligation, that defense expenditure cannot be cut beyond a certain point because of the security environment confronting us, that expenditure on government cannot be drastically reduced without a wage and DA[3] freeze or a sharp reduction in employment, that various subsidies cannot be removed overnight, we had very little option but to do what I did. *Those who criticize the cuts in social spending should tell us what other expenditure could be cut to make room for increased spending on social sectors.* (Singh as quoted in Mooij and Dev, 2004: 112; emphasis added)

The globalization–welfare state nexus in developing countries is far more complex than is anticipated by the race to the bottom debate, however, and India proves no exception. In spite of cutbacks in several social policy areas, India maintains a protective welfare regime. India's key modes of welfare protection – generous labor market protections and high levels of public employment – have experienced minimal changes, and commodification strategies still lag far behind nationally set goals and international standards. Furthermore, it is not just social spending that tends to serve the better off in India, as India's distribution regime more generally has historically concentrated protections on the non-poor. It thus becomes apparent why, in the final analysis, the current race to the bottom is more directly hurting the middle class and not India's poor; the

1 This estimate is calculated as a percentage of GDP from the IMF's *Government Finance Statistics*, for various years from 1972 to 2003. Note that, prior to globalization, India's total government spending increased at an annual average of 3 percent. A declining trend, at an annual average of 0.04 percent, began after globalization.

2 These sectors show a decline in spending when measured both as a percentage of GDP and as a proportion of total government expenditures.

3 DA represents "dearness allowance," or cash payments to employees that take inflation into account and are part of the total wage cost.

fate of the latter continues to be determined by pre-existing domestic institutional arrangements that never protected them in the first place.

This chapter is divided into six sections. Section 5.1 describes the key features of India's protective welfare state. This section takes its cue from chapter 4, staying away from the sole focus on social spending, and undertakes a multifaceted examination of the content or institutional structure of India's welfare regime. The following section (5.2) exposes the effects of globalization on India's protective welfare state. More specifically, I illustrate the extent of the race to the bottom, exploring the Indian case in connection to the findings of chapter 2.

Section 5.3 is divided into two parts. The first puts the extent of welfare cutbacks into broader perspective. I reveal the high degree of institutional continuity in India's welfare regime despite the retrenchment of some social sectors. This section goes beyond the findings of the cluster analysis in chapter 4 to reveal the ways in which globalization does or does not affect *institutional changes* in welfare schemes. This reconceptualization reveals that the race to the bottom does not necessarily lead to institutional convergence towards the minimal neoliberal welfare state, and, aside from some noted education reforms, India's protective welfare state still concentrates on middle-class benefits.

The second part of section 5.3 makes clear *why* institutional continuity persists in India, by focusing on the mediating effects of domestic institutions. I illustrate, in turn, how the three institutional factors outlined in the previous chapters determine policy responses to globalization in India: the organization of the political economy, which aggregates interests and structures access to the political arena (chapter 4); the nature of the policy interactions between government and labor (chapter 3); and the fragmented character of labor organizations (chapter 2). I should emphasize here that, in all the case studies, I discuss more generally the expression of fragmented labor movements (or PLP) rather than focus on the structural characteristics of the labor market.[4] Section 5.4 asks the key question: who really gets hurt? This section delves into how a race to the bottom in India's social sectors hurts the middle class as a consequence of its historically protectionist welfare regime. Section 5.5 examines other factors not considered in the quantitative analysis. Finally, section 5.6

[4] In exploring the character of LDC national labor market institutions in the following chapters, low PLP (or the structural constraints of the labor market – large numbers of low-skilled labor, surplus labor – that inhibit labor mobilization in LDCs) is already assumed. More detailed data on PLP for India, Brazil, and South Korea are available in chapter 2. The focus here is more generally on the implications of fragmented labor movements.

draws some general conclusions about protective welfare states in the current era of globalization.

5.1 India's protective welfare state

As revealed in the previous chapter, India's distribution regime is classified as protective. The Indian government has long focused on decommodification efforts in two particular ways: labor market protections, and employment creation in the public sector. Not only does India rank among the highest in the developing world in terms of the percentage of workers employed in the public sector, it also maintains some of the most labor-friendly rules and norms governing working conditions and industrial relations. These two pillars represent the core of India's protective welfare state.

At the same time as these protective measures became enshrined in the constitution, Jawarhalal Nehru, the independence leader and India's first prime minister, envisioned a strategy of promoting national security by building a relatively autarkic economy (Nayar, 2001). He adopted an economic model that was guided by Mahatma Gandhi's emphasis on *swadeshi*, or self-reliance.[5] Import substitution industrialization policies were soon implemented in an effort to eschew international market influences and thereby promote India's strategic independence. India's development approach was characterized as "export pessimism," and, eventually, the sluggish growth of exports was linked to India's dawdling "Hindu rate of growth." By successfully "delinking" its economy, India essentially participated in world markets far less than any other large developing country in the first few decades after independence (Rudolph and Rudolph, 1987).

As a consequence, the extensive tax and tariff structures, as well as stiff regulations in connection with trade and foreign investment, succeeded in cutting India off from the global economy, and thereby simultaneously reduced government and employer resistance to costly welfare measures. Not having to compete in international markets, less efficient public-sector firms began to dominate the organized economy, and the size of the public bureaucracy (including the government's key administrative service, the Indian Administrative Services [IAS]) expanded (Rudolph and Rudolph, 1987). Employment in state enterprises and the number of civil servants rapidly increased. By the same logic, both public and private employers could pass on the costs of high labor market protections by raising domestic prices and offering often substandard goods and services.

[5] The first *Swadeshi* movement, from 1905 to 1908, called for a total boycott of foreign goods, particularly imports (Encarnation, 1989).

Taking a closer look at India's decommodification bias, recall from chapter 4 that labor market protections are restrictions on the ability of economic agents to enter or exit contractual, formal employment relationships (Gitterman, 2002). This includes not only the formal ILO core codes, such as freedom of association and collective bargaining, but also legislation that promotes labor market rigidities (e.g. costly layoffs, inflexible wages). India's strong pro-labor bias is reflected in several constitutional enactments upon independence in 1947 and more than 200 labor laws guaranteeing labor some of the most generous freedoms in the developing world. Of these, the most important are the Trade Unions Act, Industrial Disputes Act (IDA), and Contract Labor Act (CLA), which govern labor's freedom to organize, the terms and conditions of employment, and prohibitions against hiring contract labor, respectively. For example, since India's independence, firms with more than 100 workers have had to apply for formal government permission to lay off workers, and this permission is rarely forthcoming (Sen Gupta and Sett, 2000; Basu, Fields, and Debgupta, 1996). It is no surprise that India ranks in the top percentile of developing countries in several indices of labor market regulations (i.e. mandatory severance pay, statutory duration of maternity leave, number of strikes and lock-outs per year), as documented by Rama and Artecona (2002).

Paradoxically, however, by making it more difficult for firms to dismiss and hire workers, India's extensive labor laws are a direct affront to its second decommodification strategy of employment creation. The emphasis upon employment provision as a tool to address poverty has its roots in Kautilya's *Arthastra* Sanskrit writings on politics and statecraft in the fourth century BC (Dev, 1995).[6] Since independence this policy priority has taken two tracks. The first is the continuation of pre-independence strategies that provided public relief work, particularly during famines. The Employment Guarantee Scheme (EGS) in the state of Maharashtra and, nationally, the Jawahar Rojgar Yojna (JRY), for example, guarantee unskilled manual work for those willing to work at very low wages. In general, however, no more than five days per family per month are offered by JRY, and at its highest level of enrollment no more than 1.2 percent of the workforce is employed (Subbarao, 1997).[7] While the EGS has

[6] Note that an emphasis on the merits of education also has its roots in ancient Indian texts (see Scharfe, 2002). What is interesting for this analysis is that, even though emphasis on both protective and productive welfare strategies can be traced back to ancient India, it is only a commitment to the former that is maintained at present.

[7] This percentage was calculated by dividing Subbarao's (1997) statistic that approximately 55 million people gained employment during the agricultural off-peak season by the size of the labor force listed in the World Bank's *World Development Indicators* for 1997.

provided an important source of relief (and empowerment) for the rural poor, it has also been widely critiqued for corruption and the more affluent gaining a larger share of EGS earnings (Gaiha, 1996; Echeverri-Gent, 1994; Ravallion, 1991). The second and more far-reaching track guarantees secure employment in the public sector, benefiting mostly the middle class (civil servants, employees of state-owned enterprises). India ranks fourth highest in the developing world after Benin, Zambia, and Ghana, with public-sector employees comprising 72 percent of total employment in the organized sector (Heller and Tait, 1984; ILO's LABORSTA database).

Alternative welfare strategies, as discussed in chapter 4, have not received the same resources or policy attention in India. According to data from the IMF's *Government Finance Statistics*, total central spending in education, health, *and* social security reaches just 1 percent of GDP, which is far below the developing world average of 7 percent.[8] Consistent with India's emphasis on protective welfare policies, however, total government spending on social security has been higher than its investment in education. Spending on housing is also, on average, less than 1 percent of GDP, and has received extremely low priority on India's public policy agenda (Sivam and Karuppannan, 2002).

With the bulk of the benefits and privileges associated with India's welfare policies directed towards labor market protections and public employment, the resources allocated to means-tested, or targeted, anti-poverty schemes are comparatively meager.[9] The lack of investment in poverty programs is actually quite surprising, given India's history of socialism and extensive public commitments to help the poor, particularly after independence. Analyses of some of India's major pro-poor schemes, such as rural public works (RPW) and the Integrated Rural Development Programme (IRDP), reveal that the outlays have been misdirected, either failing to attract the poor or enabling "leakages" to the (relatively) well off (Gaiha, 2000). The Public Distributions System (PDS) is the earliest publicly funded safety net and, according to Radhakrishna and Subbarao's (1997) World Bank study, India's most "far reaching in terms

[8] It is difficult to find consistent data on social spending in India. Recent data from the government of India suggest that total central government spending on education, health, and social security averages approximately 5 percent of GDP (see appendix M).

[9] For a broader overview of existing poverty alleviation schemes in India, see Ministry of Finance (2005: chap. 10). It is difficult to obtain data on the total amount spent on means-tested poverty alleviation programs in India. One estimate suggests that, on average, 0.3 percent of GDP is spent on programs focused on lower-caste members (see Mooij and Dev, 2002, 2004). These tend to be the largest of India's targeted programs, but others do exist.

of coverage as well as public expenditure (on subsidy)."[10] Yet Radhakrishna and Subbarao's (1997) findings reveal that overall PDS welfare gains in terms of income and nutritional status have been "very meager."

India has also maintained a "reservation policy" under which specific quotas are reserved for the scheduled caste and scheduled tribe (i.e. members at the bottom of India's caste hierarchy, formerly known as the untouchables) in government jobs, education institutions, public housing, and several political institutions, such as parliament, state assemblies, and panchayats (village councils). Consistent with the institutional norms of India's protective welfare state, employment (i.e. quotas or "reservations") in the public sector has been a primary means for assisting the lowest caste. While this program has had some success, scholars argue that the majority continue to remain in a situation of poverty (see Deshpande, 2005).

To summarize, India's distribution regime maintains an imbalance between select protective welfare policies and an extremely low commitment towards human capital investment. The next section introduces the globalization question: what is the effect of international market integration on India's protective welfare state?

5.2 Race to the bottom?

India's embrace of globalization began in the mid-1980s with Rajiv Gandhi's trade and industry reforms, but did not gain momentum until after the balance of payments crisis of the early 1990s.[11] Gandhi's halting efforts were India's second major attempt at liberalization, and illustrate the difficulties in transitioning from such a tightly controlled domestic economy to an internationally oriented market economy. Both scholars and policy-makers generally agree, however, that India's long-lived inward-oriented socialist regime, inspired by Nehru, finally experienced a decisive break in 1991 when the then prime minister, Narasimha Rao, eliminated import licensing for most goods, cut import duty rates, actively promoted foreign direct investment, allowed the exchange rate to depreciate, and made attempts to deregulate financial markets.

[10] PDS provides selected food commodities, such as rice, wheat, sugar, and kerosene oil, at subsidized prices.

[11] Rising inflation, the Bofors scandal, and the defeat of Rajiv Gandhi's Congress (I) party in 1989 by the leftist National Front coalition significantly deterred the liberalization process (Denoon, 1998). India's first attempts at liberalization (1966–8) during the premiership of Indira Gandhi drew strong labor and business opposition, and hence were short-lived.

Figure 5.1 Social security and welfare, 1972–97

Notes: Social spending as a percentage of total government expenditures shows a similar trend, with spending levels tapering off in the mid-1980s. Per capita social security spending peaked in 1990 (graphs not shown here).

State and local spending data should be viewed with caution, since states' total expenditures include central government transfers.

Source: IMF, *Government Finance Statistics* (various years).

Policy reactions to globalization pressures are most evident in India's social security, education, and health sectors. In contrast, as will be seen in the next section, the race to the bottom has made less of an imprint on the core of India's welfare strategies (labor market protections and public employment). Cutbacks in education, health, and social security expenditures began shortly after Gandhi's attempts at liberalization and have not since been restored. Figures 5.1–5.3 illustrate these trends. These findings for education and health expenditures are not completely consistent with the predictions in chapter 2 that only social security would be sensitive to the impact of RTB pressures. See appendix M for more recent data on these trends collected from national sources.

In all three sectors, spending peaks around the mid-1980s and declines steadily after 1991, alongside increases in trade and capital flows. Important post-liberalization national policy rulings on India's social security and health sectors provide additional evidence of the race to the bottom. The reductions in education spending, however, are the most surprising, given India's publicly declared intentions in 1986 and 1991 to invest more heavily in education. The Planning Commission's

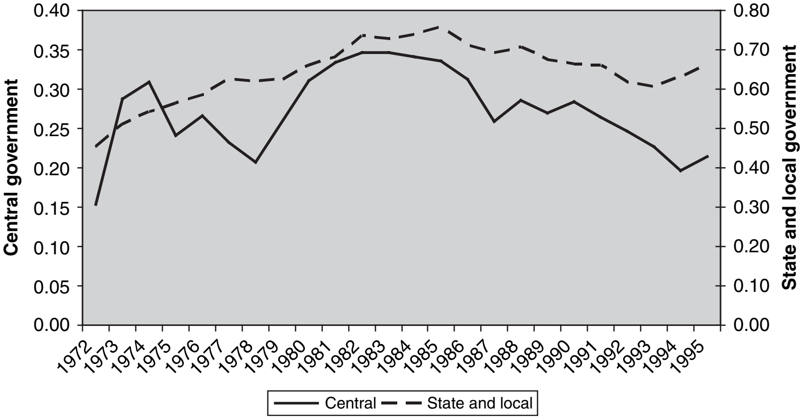

Figure 5.2 Health spending, 1972–97

Note: Health spending as a percentage of total government expenditures shows a clearer peak, and then declines after 1983. Health spending per capita begins to level off and shows only a slight decline starting in 1985 (graphs not shown here).

State and local spending data should be viewed with caution, since states' total expenditures include central government transfers.
Source: IMF, *Government Finance Statistics* (various years).

subsequent reduction of budgetary resources directed towards this sector suggest that the pressures of globalization are indeed very real.[12]

5.2.1 *Social security*

While there is much heterogeneity among Indian states in terms of their social sector spending and achievements, this analysis focuses on the budget and priorities at the central level. The latter has strong influence and direct control over the direction of social spending in the states (Rao and Singh, 2005), and India's constitution reveals a clear predisposition towards the central government in the distribution of fiscal powers. Even though such items as social planning and services, the welfare of labor, social security, and unemployment are included on the Concurrent List, the actual delegation of responsibilities reveals an inherent "centripetal" bias (Rao and Singh, 2005: 136).[13] The almost parallel trends between the

12 India's Planning Commission is the government institution responsible for formulating five-year plans that determine the priorities and effective allocation of India's resources.
13 The Concurrent List refers to those categories in which the state and central governments have joint jurisdiction.

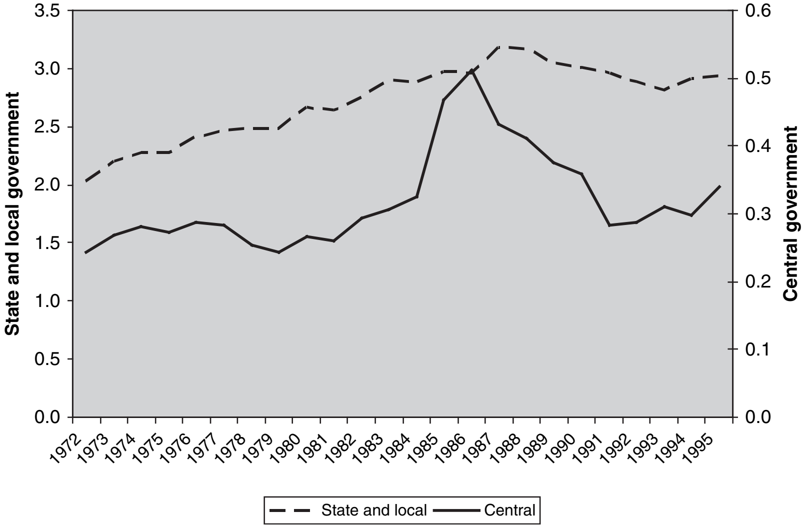

Figure 5.3 Education spending, 1972–97

Notes: Education spending as a percentage of total government expenditures and education spending per capita show similar trends, with spending levels peaking in the late 1980s (graphs not shown here).

State and local spending data should be viewed with caution, since states' total expenditures include central government transfers.

Source: IMF, *Government Finance Statistics* (various years).

central and state and local governments in social spending suggest that this is indeed so, although it should be noted that substantial heterogeneity among states' social performance does exist. Nonetheless, inter-state variations in both social commitment and performance – Kerala, for example, does exceptionally well – should be kept in mind.

As figure 5.1 indicates, since India's turn towards globalization the country has had to pull back the reins on its rising social security expenditures. Two major policy initiatives suggest that this trend will continue in the long run. In 1998 India imposed stricter eligibility criteria by raising the retirement age from fifty-eight to sixty. This change was one of the less politically controversial moves towards social security reform, raising only minor protests by youth associations.[14] As a result, India's dependency ratio (the proportion of dependents to working-age population) immediately decreased. This was a significant attempt to reduce the state social security budget, particularly since the

[14] "Youth Front against Raising Retirement Age," *The Hindu* (Madras), October 6, 2001, Southern States section.

implementation of the pay-as-you-go Employee Pension Scheme (EPS) for private-sector workers in 1995 called for a continued 1.6 percent contribution from the state.[15]

A second and much more controversial policy reform that reflects the race to the bottom is pension privatization for state employees. The New Pension Scheme (NPS), passed in 2004, is a market-based guarantee mechanism that requires contributions from union, state, and local employees to be placed in individual pension accounts, ostensibly lowering the extent of publicly guaranteed benefit levels. The reform unleashed major protests and outrage from leftist parties and trade unions, and has since been called back to parliament for review. Nonetheless, first-time institutional developments, such as the formation of a statutory regulatory body, the Pension Fund Regulatory and Development Authority, to undertake revisions in the pension sector, and the first ever comprehensive examination of policy questions connected with the OASIS program underscore the government's commitment to reform.[16] Significantly, the majority of the OASIS recommendations towards reducing government pension commitments have since been placed on the policy agenda. The recent advancements, overall, have given Indian social security experts confidence that the reform process is inevitable.

5.2.2 Health care and education

Evidence of a race to the bottom in India's public health sector is revealed in the National Health Policy, passed in 2002. First, not only does the proposal (to raise total health expenditure from a mere 0.9 percent of GDP to 2.0 percent) fall far below the 5 percent recommended by the World Health Organization, but expenditures have since declined (Ministry of Finance,

[15] Note that the state was already making a similar contribution to the Family Pension Scheme, which was replaced by the more comprehensive EPS in 1995 (Goswami, 2002). Initially, private sector workers were only covered by the Employee Provident Fund (EPF). This is a fully funded program that provides a lump sum benefit at retirement. Reformers have long been concerned that EPF does not adequately provide protection from longevity and inflation. The implementation of EPS did not satisfy reformers, however, as workers' contribution rates increased by two percentage points, and factors such as ceilings on pensions and the lack of indexation suggest that returns from EPS will be lower and will further disadvantage the private sector (Goswami, 2002: 104). This is disconcerting, since private-sector workers have long received low levels of old age protection under India's social security system, and India's worker contribution rates were already "amongst the highest in the world" (Ministry of Social Justice and Empowerment, 1999). Note that the Old Age and Social Income Security (OASIS) report on social security calls for (and parliament is considering) the withdrawal of the 1.6 percent state contribution to EPS.

[16] India is one of the few countries to have set up an independent regulatory agency for its social security system.

2005: table 210). Second, the plan drew national criticism for encouraging a greater role for private care, and shirking government responsibilities at the primary level.[17] Generally, 83 percent of all health care expenditure is borne "out of pocket," making India one of the most privatized systems in the world (Ministry of Health and Family Welfare, 2002: 10). This is a concern, since government has failed to increase its regulation of the private sector to ensure that there are common standards of performance.[18] The impact of globalization has also been felt in the reduction of central grants to the states for public health and disease control programs (Purohit, 2001).

Finally, after several concerted and very public efforts to prioritize education after liberalization efforts had begun in 1985, the first official government document to declare that globalization was still putting pressure on education resources made headlines.[19] Recent government documents declare that economic liberalization and the accompanying structural adjustment policies constitute one of the biggest challenges in funding education.[20] Declining education expenditures, in the absence of any specific policy initiatives designed to curb education spending, suggest that budgetary allocations to this sector are among those targeted in the globalizing environment.

5.2.3 Summary

Since the adoption of economic liberalization policies in India, reduced public spending and select policy changes indicate retrenchment in social security schemes and health care. More specifically, raising the retirement age and establishing the NPS were policies aimed at reducing overall non-wage costs linked to social security. Retrenchment pressures in the health sector are revealed by cutbacks in central grants to the states for public health and disease control programs, a decline in overall spending, and a continued role for private care and deregulation despite the fledgling nature of India's health care system. The most unexpected finding is

[17] See "National Health Policy is Slammed," *Times of India* (Delhi), November 5, 2001.

[18] "Health for All: A Goal Too Far?" *Financial Express* (Mumbai), May 31, 2003.

[19] See "Social Reforms to Boost Productivity," *The Hindu* (Madras), August 24, 2000. For example, the National Policy of Education in 1986 first introduced the idea that education is a fundamental right for all children up to age fourteen. The United Front government presented this Bill in 1997. Finally, the United Progressive Alliance (UPA) made universal access to quality basic education a fundamental pillar of its Common Minimum Programme in 2004 – a continuation of the United Front's Basic Minimum Services program initiated in the late 1990s.

[20] For the details, see Ministry of Human Resource Development (2000: Part II – Analytic Section, cont. 3), prepared by the ministry in conjunction with the National Institute of Educational Planning and Administration.

that public spending on education has been decreasing since liberalization in spite of the fact that education has been declared a national policy priority by the last two administrations.

5.3 Institutional change

In light of the race to the bottom cutbacks discussed above, is globalization causing regime change? Is India's protective welfare state headed towards the neoliberal bottom? Or is India transitioning to a productive welfare state? With the onset of globalization, the minimal changes in official labor policies and public employment rates reveal that a paradigm shift in India's welfare philosophy has not yet occurred. Nonetheless, India has implemented some *incremental* changes, guided by the institutional norms and organizations of its protective welfare state. The first subsection below discusses the degree of persistence of India's welfare state, and the next presents a brief illustration of how and why domestic institutional arrangements in India have prevented radical regime change.

5.3.1 Welfare regime change?

Overall, India's current state of affairs suggests that regime change has been minimal. In the details to follow, I illustrate this on the basis of four criteria discussed in the introduction: significant increases in the reliance on means testing; major transfers of responsibility to the private sector; dramatic changes in benefit and eligibility rules; and the discontinuity of "illiberal" institutional legacies.

In terms of the first criterion for institutional change, increases in means testing, there has been minimal change. India's targeted poverty policies have not seen much improvement in recent decades, and, as such, are consistent with previous practices. Expenditures on means-tested anti-poverty programs that aim to help the disadvantaged directly have actually fallen since 1990. For example, 1990–2001 government data estimates presented by Mooij and Dev (2002, 2004) show a significant decline in welfare programs devoted to the scheduled tribes and castes, and targeted programs such as the Drought Prone Areas Programme, Integrated Rural Development Programme, and rural wage employment programs. This certainly does not bode well for the poor, given that these programs have long registered far less than 1 percent of GDP (see figure 5.4). While the current administration's recent launch of the ambitious National Rural Employment Guarantee Programme (NREGP), which guarantees rural households 100 days of employment per year, may turn out to

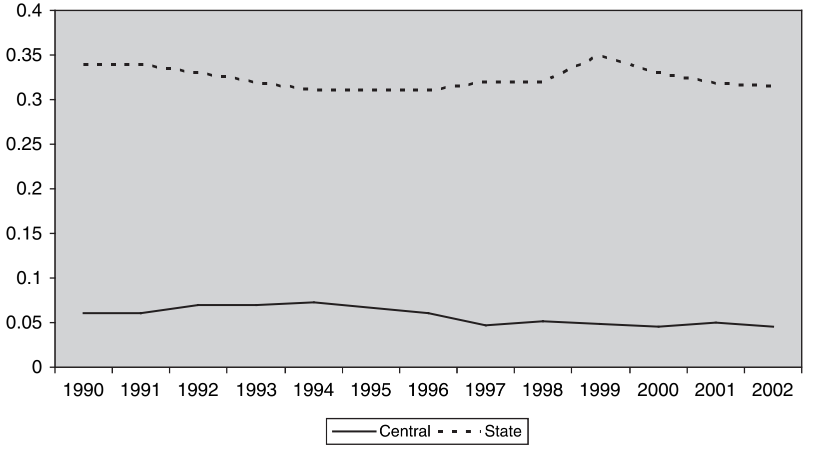

Figure 5.4 Expenditure on scheduled castes, scheduled tribes, and backward castes, 1990–2002

Source: Ministry of Finance (2003, 2004).

be an exception, it has been widely criticized.[21] The overall trend in means-tested programs remains one of minimal change.

The second criterion, dramatic changes in benefit and eligibility rules, has also shown little evidence of being met. While some incremental changes have been made to social security, such as an increase in the retirement age and a contribution by civil servants of 10 percent of their salaries, when placed in an international context these changes can be seen to be relatively minor. India's mandated retirement age is still below the international average of sixty-two, and the dualism between social insurance benefits for the private and public sectors remains.[22] In addition, civil service pension spending has risen rapidly since the early 1990s, and remained relatively stable from 2000 to 2004 (Palacios and Whitehouse,

[21] Launched in February 2006, the first phase of the program will take place in 200 of India's most impoverished districts. It is scheduled to be expanded nationwide. The prime minister, Manmohan Singh, has described the initiative as "historic" (Amelia Gentleman, "India's War on Poverty: Easy Victory Unlikely," *International Herald Tribune*, February 28, 2006). Nonetheless, based on India's past experience with employment guarantee programs, both activists and scholars remain extremely skeptical about the viability of the current plan. They question the government's (under)estimations of the cost of the program, the extent of its long-term commitment, and the spread of corruption (see Sharad Joshi, "National Employment Guarantee Scheme – Well-intentioned, but Poorly Designed," *Hindu Business Line*, August 24, 2005, and Amelia Gentleman, February 28, 2006).

[22] See the retirement age data reported by Bonturi (2002).

2006). Since the total number of civil servants has not simultaneously increased over the same period, this trend suggests that benefits per person have not significantly diminished. A recent newspaper report put it well: "Pension reform in India is moving at a painfully slow pace."[23]

The third condition, a major transfer of responsibility to the private sector (in the provision of social services), has also not been met. While it is true that there is some discussion of privatization in the social security, health, and education sectors, advances towards this end have been minimal. In education, for example, government officials have reported recently that they will not accede to WTO demands to open up education services.[24] The privatization of social security is still in the discussion phase, and the final outcome is yet to be determined. Privatization has increased in India's health sector, but this is a trend that began long before globalization. The level of public health spending is extremely low (0.6 percent of GDP and 1 percent of total government spending), and was so long before India's turn to global markets.[25]

The final mode of assessment of regime change is whether major policy or funding changes have been directed towards the mainstays of India's welfare state. In other words, we need to look at the extent of institutional continuity. The continuation of labor market protections and state responsibility for securing employment are the most convincing signs of institutional continuity, and deflect concerns of convergence towards the liberal welfare state. In terms of India's extensive labor market protections, there have been surprisingly few official policy changes. Amendments to the IDA and CLA that allow more flexibility for employees to hire and fire, as well as permit the hiring of contract labor, face stiff resistance from unions.[26] Intense pressure for reform began during Rao's administration in the early 1990s. A tripartite body of business, government, and labor, the second National Commission on Labor (NCL), was formed, and the most wide-ranging reforms were proposed *for the first time* in the 2000–2 budget (Roychowdhury, 2003). These reforms are still being debated in parliament, however, and, even more significantly, the current administration has shown a greater reluctance to pursue any

23 "Reform Pensions," *Financial Express* (Mumbai), August 8, 2006.

24 "India May Remove Education from WTO Wishlist," *Indian Express* (Delhi), February 3, 2006.

25 Systematic data on private health expenditures are not available for the early years after independence.

26 Currently, the IDA requires firms employing more than 100 workers to seek prior government permission for layoffs and any changes in job specifications, while the CLA prohibits contract workers in certain situations at the discretion of the government.

drastic changes, announcing in May 2004 that it would "refrain from uncritical endorsement of the hire and fire approach."[27]

Nevertheless, it cannot be said that RTB pressures are completely absent in terms of labor market reform. As several Indian labor scholars, and even the media, document, labor reforms still occur informally and – as Jenkins (2004) puts it well – "by stealth." First, to bypass laws against retrenchment, employers have stopped paying salaries or simply abandoned operations (Kaur and Maheshwari, 2005; Sen Gupta and Sett, 2000).[28] Second, while the federal laws might still be intact, some individual states have adopted more liberal labor policies (e.g. amendments to the CLA in Andhra Pradesh), creating less resistance to reform among neighboring states (Jenkins, 2004).[29]

Public employment has been more resistant to change, however, both de jure and de facto, particularly in terms of India's overstaffed bureaucracy. In fact, from the mid-1970s to the mid-1990s, most of the increase in "organized" employment has been absorbed by the public sector. Raw public-sector employment figures from 1985 to 2003 reveal an increase of over 1 million persons. Pressure for restructuring has occurred mostly in public-sector manufacturing enterprises rather than the public sector as a whole (Roychowdhury, 2003). One of the few policies designed to reduce the public sector workforce, the Voluntary Retirement Scheme (VRS), has not been that successful. This policy has eliminated fewer than 2 percent of "potentially redundant employees," according to recent estimates (Agarwala and Khan, 2002).[30] The fundamental problem is that the thousands of officially declared "sick" industries, or those enterprises (particularly public) that operate at chronic losses, are notoriously difficult to shut down. Figure 5.5 illustrates the "stickiness" of jobs in the public sector. Total numbers employed in the public sector have steadily increased, but, as a percentage of the total, public employment has remained relatively constant since economic liberalization policies began to be adopted in the mid-1980s.

In sum, the legacy of India's protective welfare state appears to be conditioning the direction of social welfare change in the current era of

[27] Andy Mukhergee, "India's Harsh Labour Laws May Change, Quietly," *International Herald Tribune*, February 2, 2005.

[28] Of course, while employers have long attempted to bypass these laws, the pressures of globalization and the growing informalization of the workforce, as well as the increasing number of "sick" industries, have accelerated this practice (Sinha, 2004; Jenkins, 2004).

[29] See also Andy Mukherjee, "India's Harsh Labour Laws May Change, Quietly," *International Herald Tribune*, February 2, 2005.

[30] Datta (2001) reports data from the Ministry of Heavy Industries and Public Enterprise to the effect that, from 1991 to 2002, a total of 138,472 workers (or approximately 0.7 percent of the total employed in the public sector) accepted VRS.

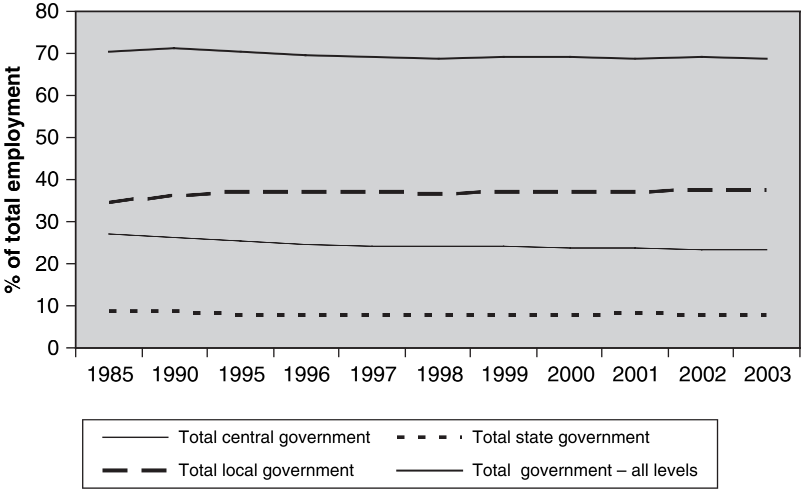

Figure 5.5 Total public employment in India, 1985–2003

Note: "Total public employment" covers all employment of the general government sector plus employment by publicly owned enterprises.
Source: ILO's LABORSTA database (accessed September 2005).

globalization. Relatively marginal changes to the core elements of its protective welfare state signal a particular pattern of policy responses. In contrast to public employment, the most visible effects of RTB pressures occur in the traditionally neglected welfare sectors – health and education, and even social security. Relative to India's key protective welfare schemes that have been encouraged since independence, social security programs are relatively new. Recall that the EPS was introduced as late as 1995. Social reforms in India thus appear to vary according to both the pressures of globalization *and* the prevailing normative orientations and organizational structures of India's distribution regime.

5.3.2 *Mediating role of domestic institutions*

This section draws on the Indian case to demonstrate the causal mechanisms that underlie institutional continuity, as discussed in chapters 2, 3, and 4. First, I investigate how India's protective welfare state aggregates interests and structures access to the political arena. Next, I look at how India's government–labor relationship enables only select labor groups to have privileged access to politicians and welfare benefits. This ultimately reduces the incentives for workers to overcome their collective action problems, over and above the existing structural constraints discussed in chapter 2. Finally, I describe India's fragmented labor movements in detail to illustrate how non-encompassing labor groups are able neither to encourage a transition to a more universalistic welfare state nor to block race to the bottom reforms.

How is it that decommodification policies continue to prevail over commodification policies at the expense of the majority of the population? India's early industrial strategy helped provide three groups in particular privileged access to politicians and the policy agenda: the industrial capitalist class, the landed elite, and the professionals (civilian and military), including white-collar workers in the public sector (Bardhan, 1984).[31] Some sections of unionized workers eventually became part of this dominant coalition (Bardhan, 1984: 67). This is not to suggest that these groups act cohesively in the form of strong business associations or labor unions. Rather, they remain individually strong, but collectively weak. Welfare policies that were implemented in tandem with this industrial strategy had, at a minimum, the tacit consent of one of these broader groups.

While India's constitution recognized the importance of both productive and protective welfare policies, it was the protective welfare policies favored by the dominant coalition that received political commitment and material support from governing elites. Organized labor and white-collar professionals, particularly in the public sector, were the primary pressure groups. Domestic industrialists and the landed elite, while initially opposed to many of the protective benefits, were too divided to offer resistance. In the insulated economic environment, however, the IAS, Members of Parliament, and members of India's Legislative Assembly found alternative ways of compensating them with licenses, subsidies, cheap credit, and protectionism.

In the meantime, it was not the case that the importance of commodification-type policies, particularly education, went unrecognized by the political elite. Political rhetoric in support of universal primary education in India has always been strong. For at least the first five decades after independence, however, the Indian government grossly failed to meet its education targets and progressively allocated fewer and fewer budgetary resources to this sector (Tilak, 1999). The fundamental problem is that elites have consistently managed to direct education investment away from the poor and promote what best supports their interest: tertiary education.

[31] As Weiner (1986) explains, the government's ISI policies, industrial licensing system, policy of taking over sick firms, and restrictions on foreign investment all benefited the industrialists. The subsidized credit, governmental price support program, and subsidized inputs (water, power, fertilizers, diesel fuel) benefited rich farmers. Finally, the bureaucrats gained power and income through their control over the elaborate system of patronage, particularly in the distribution of state subsidies.

India's early industrial strategy gave priority to industries producing capital goods, which translated into a high demand for skilled labor. Members of India's privileged groups put pressure on the state to invest in tertiary education in order to have continued access to these coveted jobs.

The lack of investment in mass education also helps the elite groups maintain their position and reinforce their assets (Tilak, 1990; Weiner, 1991). In private interviews with this author, one of India's highest governing officials in the previous government, led by the Bharatiya Janata Party (BJP), was glib, saying: "Politicians do not want the poor to be educated." Reform advocates have been repeatedly frustrated with the lack of a clear motivation to make education a budgetary priority (see Shariff and Ghosh, 2000: 1405).[32] This is not surprising, as, for decades, none of the members of the dominant coalition demonstrated an interest in promoting education, and those who would benefit directly from the expansion of primary and secondary education have not had the same privileged access to politicians.

Similar dynamics underlie the fate of primary health care in India. On the eve of independence the Indian government's Bhore Committee initiated a program for the national provision of medical and health services to citizens. It was one of the "most rational and far-sighted documents of its kind" (Deodhar, 1982: 78). The plan included guidelines for effective rural health services, integrated preventative, promotive, and curative services with the full participation of the population, and health care provision to the neediest. Again, however, India's efforts at promoting universal health care never won the support of any of the members of India's dominant coalition. The Bhore Committee's plan ultimately gave way to super-speciality and diagnostic care, serving the interests of domestic and foreign investors such as those associated with the high-tech, medical, and electronic equipment industries (Purohit, 2001).

Essentially, the core elements of India's protective welfare state have persisted because the system put in place by early state elites is now sustained by the bureaucracy, sections of the governing party, and portions of the labor community. Any radical attempts at reform that require significant redistribution and create more universalistic welfare policies

[32] In the early years after independence it was strikingly apparent that political debates lacked a clear motivation for making education a priority (Weiner, 1991). A review of the activities of the Central Advisory Board of Education (CABE), which is the principal forum for formulating and reviewing national education policy, highlights the lack of direction underlying India's educational policies. It is not until the late 1960s, two decades after independence, that any link between education and national economic development was emphasized. Various rationales for the importance of primary education have been given, such as nationalism, religious and cultural development, and "educational progress." CABE documents are referenced from Biswas and Agrawal (1986).

have been met with weak political support. As a consequence, despite the current economic reforms and growing disenchantment with the state, it has proved difficult to dismantle institutionalized welfare policies. In fact, many observers comment that globalization and local beliefs in its negative consequences have incited greater protests amongst existing welfare beneficiaries in India and made them even more determined to hold on to their benefits as far as possible.

The government–labor relationship and how it evolved presents a second reason why it is difficult to dismantle India's protective welfare state. Rudolph and Rudolph (1987) characterize this relationship as one of state dominance. They observe, "It serves the interests of the state to keep labor fragmented and prevent it from concentrating its force along oligopolistic lines, hence weakening its voice in policymaking and minimizing its political role" (269). Labor leaders in India are far more focused on promoting their own political interests and the concerns of their affiliated groups than on welfare policies that serve the interests of the entire labor force.

Institutional constraints in the form of clientelism and patronage have arisen to support this relationship. India's "steel frame of administration" is led by a single dominating elite civil service, the Indian Administrative Services (formerly the Indian Civil Service). The IAS is the principal "face" of the government to the public and is responsible for implementing government programs. It is, in theory, at the helm of ensuring a sound business environment, curbing corruption, and providing public services (World Bank, 2000a). Instead, India's administrative system has become highly permeable to the appropriation of public resources for private ends (Jain, 2001; Bardhan, 1984). Civil servants and ministers are known to use the social policy agenda for patronage; welfare benefits and appointments encourage the cooperation of formal labor, "buy" political support, and reward friends. For example, governing elites have long distributed subsidies towards higher education to gain political favors from public servants, teachers, and high-income elite groups (Tilak, 1999). The Indian government's cooperation with the General Insurance Corporation to insure those segments of the population with the greatest ability to pay serves as another example. This has led to the unregulated growth of the private health sector, which excludes more than 90 percent of the Indian population (Ellis, Alam, and Gupta, 2000).

Ultimately, unless governing elites and political parties sever their close ties with formal labor, welfare benefits in India will continue to be protective towards a very small (privileged) segment of the population.[33] The

[33] Each political party in India sponsors its own labor union. As a result, each enterprise hosts multiple unions affiliated to various political parties (Lansing and Kuruvilla, 1987).

government–labor relationship has consequently provided various unions political influence that is grossly disproportionate to their membership. The power of such unions has, furthermore, allowed excess employment in the public sector to continue (see Kuruvilla, 1996: 650).

India's highly fragmented labor movement suggests a third reason why institutional continuity persists, and it explains in particular how and why this can occur at the same time that the government succumbs to (some) RTB pressures. Based on the success of European labor movements (discussed in chapter 2), it can be surmised that, if India's labor movement overcomes its collective action problems and develops more encompassing organizations, two related scenarios preventing a race to the bottom and, possibly, institutional change are feasible: (1) it could prevent RTB cutbacks by backing policies that balance efficiency and compensation concerns; and/or (2) India could advance towards a more universalistic welfare state. Instead, India's labor movement is unable to foster a transition to a welfare state that serves a broader clientele or to encourage increases in spending that would benefit more labor groups. The fragmented structure and composition of India's formal labor organizations undermines the political power of labor as a group.[34] Labor unions in India, in consequence, do not represent the collective interests of workers. Rudolph and Rudolph (1987: 268) summarize it best:

> Disproportionate organization and mobilization of white-collar professional and skilled labor reveals that organized labor has elected to follow the path of least resistance, to work with the conscious and accessible rather than with vulnerable and dependent unskilled laborers in industry and agriculture.

At best, labor in India can help push for the status quo.

Rules and norms governing collective action and industrial relations exacerbate the extent of fragmentation. For example, the Trade Union Act (1926) requires only seven persons to form a union, and it permits an unlimited number of unions in each factory. Unions tend to view this Act as an indication of their freedoms, particularly their right to organize. Analysts argue, however, that the multiplicity of unions in India has exacerbated inter-union rivalries and created a conflict-ridden industrial relations climate (Lansing and Kuruvilla, 1987; Mathur, 1996; Papola, 1994; Ratnam, 1996; Sinha, 1994). In just one decade, from 1980 to 1990, the number of unions doubled from 4,435 to 8,828, whereas union density increased only slightly over one percentage

[34] Unlike many developing countries, union membership has always been voluntary in India.

Table 5.1 *Employment in unionized and non-unionized sectors (millions), selected years 1972-99*

	Unionized	Non-unionized	Total	% unionized
1972	18.8	217.5	236.3	8.0
1978	21.2	249.5	270.7	7.8
1983	24.0	278.7	302.7	7.9
1988	25.7	296.3	322.0	8.0
1991	26.7	342.1	368.8	7.2
1994	27.4	365.4	392.7	7.0
1996	29.9	381.6	409.5	7.3
1999	28.1	408.0	436.1	6.4

Sources: 1972–88: Sinha (2004); 1991–9: Tata Services (2002).

point.[35] India has about ten major confederations that have more than 500,000 members.

The prospects for improving fragmented labor movements in the globalizing environment are not encouraging. First and foremost, unions are losing standing. The pervasive belief is that unions nowadays do not have the scope to negotiate on behalf of labor relative to the past. Every union member and leader interviewed for this study vocalized the opinion that international market pressures for low wages and the growing demand for informal labor have transferred greater bargaining power to employers. Second, studies show that inter-union rivalries have intensified and left–labor party ties have weakened with globalization (Roychowdhury, 2003). Neither is labor receiving much party support, as parties traditionally sympathetic to labor issues have taken "pro-market" positions since reform began in earnest in 1991 (Sarangi, 2005). It is no surprise, then, that the percentage of trade union membership has been declining, although it is critical to emphasize that this change has not been dramatic (see table 5.1). Labor groups in India are not likely to form a unified front anytime soon, and will, by default, continue to support policies that favor the middle class.

Without effective resistance from India's fragmented labor movement, the government instituted some RTB-type social reforms – albeit incremental ones – in response to the pressures of globalization. These did not

[35] Union density represents union membership as a percentage of total paid (formal) employees (and not the larger workforce). Union density increased from 25.5 percent in 1980 to 27 percent in 1990. Contrast these numbers with Sweden, for instance, where there are only sixty-four unions, and union density is 84 percent.

occur completely without opposition from labor groups, however. For instance, the great majority of India's major trade unions have been opposed to social security reforms that facilitate the transition to the defined-contribution plan. Similarly, union demands regarding pension funds, including resisting foreign investment, maintaining current state deposit rates, continuing access to the Provident Fund, and increasing the rate of return for the country's largest state-run pension fund scheme, have all gone unheeded. Interestingly, active union support for the "social security for the unorganized sector" Bill has been subdued in comparison.

In terms of protesting cuts in the health and education budgets, labor has yet to provide unified support. Some central labor union representatives have participated in select "education for all" campaigns. Various teachers' unions staged several protests over reforms in higher education (e.g. state and central budget cuts, increases in working hours, attempts to emphasize meritocracy in recruitment and promotions), but these reactions were reportedly "too late."[36] The privatization of the health sector marches onward despite occasional protests, and, as analysts observe, the private health care industry in India is "quietly facilitating a revolution."[37]

Despite some incremental changes in spending and welfare policies, India's welfare state remains largely consistent. There have been no significant increases in means-tested programs, no major transfer of responsibility to the private sector, no dramatic changes in benefit and eligibility rules, nor any discontinuity of "illiberal" institutional legacies. According to these criteria for regime change, therefore, it has not taken place. This institutional continuity is a result of several factors, including the following: the interests and privileged access to political power of certain groups; a government–labor relationship that grants only select groups access to benefits; and a fragmented labor movement that is unable to unify for the sake of protecting its wider interests or prevent some welfare retrenchment (in middle-class benefits).

5.4 Who really gets hurt?

Who is impacted most by the race to the bottom in India? Does it hurt the poor, as proponents of the race to the bottom hypothesis assert, or has this type of spending missed the poor from the start? Against this backdrop, is globalization providing any incentives for reforms that would benefit subordinate groups? In all cases, the majority of India's protective welfare

36 A. Jayaram, "Teachers' Stir: A Fight that Came Late," *The Hindu* (Madras), February 19, 2001.

37 "India Questions UNESCO Report," *The Hindu* (Madras), November 10, 2005.

schemes have been directed towards the relatively better-off urban, formal sector, which constitutes only 10 percent of India's working population. Cutbacks in existing social schemes then suggest that the middle and lower-middle classes feel the immediate effects of welfare reform, rather than the bulk of India's poor: small farmers and agricultural laborers, artisans and self-employed in household enterprises, petty traders, and casual non-agricultural workers (Bardhan, 1984). These sectors constitute the underprivileged "casual laborforce" in India.[38] The Indian case study reveals that, overall, the situation for the disadvantaged is not significantly improving (*in terms of welfare benefits*), and the pre-globalization tradition of neglecting the poor is being maintained. The one exception is that some resources in the education sector are being redirected towards promoting universal education. This finding is consistent with the predictions in chapter 3. In this section, I focus on the impacts of social security, education, and health reforms, since this is where race to the bottom effects in India have been the greatest.

5.4.1 *Social security*

Social security programs in India are the most regressive in comparison to the other sectors. This is primarily because less than 10 percent of the working population is covered by formal provisions for old-age income security (Ministry of Social Justice and Empowerment, 1999), and, furthermore, civil servants, followed by public enterprise employees, maintain the highest level of pension provisions. In other words, some estimates indicate that almost one-third of the pension budget is directed towards civil servants, and up to 70 percent is spent on all subcategories of public-sector employees,[39] who for decades did not have to make any pension contributions during the tenure of their employment.[40]

The extent of social insurance coverage for the elite white-collar workers (senior public-sector officials and the managerial class) is striking. Agarwala and Khan (2002) estimate that labor elites account for approximately 1 percent of the workforce, or 3 million workers. Their compensation packages, which include top medical care, housing, old-age

[38] This term is commonly used in India to refer to those working outside the formal sector, or informal labor force.

[39] This percentage is derived from official estimates of the proportion of workers in the public sector relative to total employment (see Tata Services, 2002).

[40] In addition to their pension benefits, public employees also have access to the General Provident Fund (GPF), to which workers may contribute a minimum of 6 percent of their monthly salary (Goswami, 2002). This is in contrast to the private sector, where employees must contribute 12 percent to their provident funds.

benefits, survivor benefits, and employment injury and benefits, parallel the highest international standards. As Guhan (1992: 285; emphasis added) puts it:

> The fundamental problem is that coverage tends to be highly skewed towards the public services and workers in the organized factory to the almost complete neglect of the self-employed, workers in the urban informal sector, and, most important, the large mass of rural laborers. Typically, the categories which are covered benefit directly from budgetary funds (as in the case of public employees) or through social insurance, to which there is a sizable contribution from the exchequer, while the element of social assistance available for workers in the unorganized sector is relatively insignificant. Consequently, *the social security system taken as a whole is highly regressive*.

The direct impact of the current SS reforms thus falls primarily upon public employees. Of course, while some types of government employees are more privileged than others, the latter's wages and benefits are still substantially higher than their counterparts in the unorganized economy.[41] It is no wonder that public employees have shown stiff resistance to the new pension scheme, in which the state no longer guarantees their high benefits. For instance, one of the most contentious issues of reform is that government employees will no longer be guaranteed a fixed pension, and they will now have to contribute to their own pension benefits, at a rate of 10 percent of their salary every month.

The race to the bottom in social security thus primarily hurts the middle class. It neither hurts nor helps the poor directly. The latest attempts to provide coverage for the informal sector have yet to be successful. Most recently, Atal Vajpayee, the former prime minister, launched a proposal, the Social Security Scheme for Unorganized Workers, in 2004 as part of the Common Minimum Programme (CMP).[42] The scheme would provide unorganized workers with old-age pensions, and accident and medical insurance. At the time of writing, however, the Bill still awaits parliamentary clearance, and has been criticized for its vague definitions of "unorganized workers," for inadequate penal provisions for violators, for demanding unreasonable enrollment fees and stable employment,

[41] Public-sector employees have traditionally enjoyed higher wages and salaries than their counterparts in the private sector (Rudolph and Rudolph, 1987: 263–5).

[42] Also referred to as basic minimum services, the United Front government in 1997 passed the CMP, which presented specific guidelines aimed at empowering the disadvantaged. The CMP was subsequently extended by the current UPA coalition government. One of its basic principles is "[t]o enhance the welfare and well-being of farmers, farm labor and workers, particularly those in the unorganised sector, and assure a secure future for their families in every respect" (Common Minimum Programme, as quoted in "UPA Government to Adhere to Six Basic Principles of Governance," *The Hindu* [Madras], June 28, 2004).

and for having minimal legislative backing.[43] At present, the majority of Indian workers engaged in unorganized and informal work do have access to a few voluntary pension schemes, but these are not well publicized (Ministry of Social Justice and Empowerment, 1999).[44] It is, therefore, the middle classes who are most greatly affected by the post-liberalization retrenchment in social security benefits.

5.4.2 Health care

In the arena of health reforms the effects of globalization do have some direct impact on the poor, but, again, the group most hurt by changes is the middle class. Recent studies have found that public health subsidies in India disproportionately favor the richer groups. First, only one-third of government health expenditure is on preventive and curative care, and, of this, nearly 75 percent is spent on secondary- (specialized care) and tertiary-sector hospitals (specialized, capital-intensive care) (Sankar and Kathuria, 2003). Rural areas are often overlooked, as only 33 percent of government health expenditures are distributed to such areas even though they account for 73 percent of the population (Garg, 1998). Second, upper-income groups go to private hospitals for superior treatment, *and* they are the largest consumers of public health facilities. Contrary to common practice in OECD countries, access to public facilities is not universal in many developing nations, and India is an exemplar case. The poor can ill afford even basic public health services. Although treatment in public hospitals is subsidized, richer groups receive privileged access to public subsidies.[45] Finally, only 26 percent of the miniscule portion that the government spends on public health is allocated to preventative care (e.g. disease prevention, maternity, and child health), which tends to give higher benefits to the poor (Garg, 1998). Furthermore, chronic

[43] The legislation has been criticized harshly by the left. See, for example, W. R. Varada Rajan, "Expose This Cruel Fraud on Unorganised Workers," *People's Democracy*, March 7, 2004, and M. K. Pandhe, "Mobilise Workers to Modify Unorganised Workers Bill," *People's Democracy*, January 20, 2008. In addition, Chandrasekhar and Ghosh (2006) conclude that "the amount of coverage is so low that it would still leave most families with need to look elsewhere to finance the total costs of these contingencies."

[44] The most well known is the Public Provident Fund (PPF), which, according to some official estimates, still provides coverage for less than 1 percent of the working population more than three decades after its implementation (Gillingham and Kanda, 2001). Under PPF, individuals receive rates of return that are administratively determined. Benefits are normally paid out in lump sum upon retirement, although early withdrawals are permitted after five years.

[45] See discussion by Mahal (2003). Significantly, Mahal finds that, even if private health care increases in India (as the government is attempting to accomplish), the redistributive effect will be small when richer groups have privileged access to public facilities.

medicine shortages in public health facilities require households to bear a substantial share of the costs (Ramesh and Nishant, 2004).

Unlike reductions in the social security sector and government health spending since liberalization, however, the growing participation of private industry and multinationals in the health care sector is of immediate consequence to the poor. Purohit (2001) argues cogently that allowing greater private-sector participation detracts from the Indian government's commitment to basic health facilities. Private companies focus on high profit margins, super-speciality, and diagnostic care, making it increasingly unlikely that the basic needs of the majority who are part of the unorganized economy will be met.

Nonetheless, the point to be emphasized in this analysis is that the conditions exacerbating India's health performance and care for the poor existed long before globalization. The World Bank's Operations and Evaluation Department has confirmed that, in the 1970s and 1980s, the tenuous quality of public health assistance in India was affected by the limited resources devoted to health care (which did not in any case effectively target the most vulnerable groups), inadequate management and personnel policies, poor maintenance and equipment, and inter-district disparities in fertility, health, and cultural and institutional characteristics (World Bank, 1999a). The World Bank has invested more in India's health sector than in any other country, but still reports that, "over the *past three decades*, progress, particularly for the poor, has been slow and uneven" (World Bank, 1999a: 1; emphasis added). Globalization might exacerbate this situation of deteriorating public health services for the poor but, clearly, India has long been struggling with providing high-quality health care for the majority of its population.

5.4.3 Education

Education spending in India is also widely critiqued for its bias towards the privileged. A comprehensive review in 1985 by the Ministry of Education reported that expenditure on elementary education had fallen by 35 percent since the First Five-year Plan (in the mid-1950s), while the share for university education had risen by 78 percent. Not surprisingly, then, enrollment in higher education grew five times as rapidly as it did in primary education during this same period (Tilak, 1990). One of India's experts on education, Jandhyala Tilak (1990, 1999) has repeatedly labeled the country's lack of educational achievement its "most conspicuous failure." In light of India's constitutional mandate (article 46) that "the State shall promote with special care the educational and economic interest of the weaker sections of the people," rhetoric has far surpassed reality.

A comparison of the percentage of children reaching grade five in 2000/1 (59 percent) with similar countries is telling: Cameroon (85 percent); China (99 percent); Zambia (77 percent); Indonesia (89 percent) (UNDP, 2004).

In striking contrast to the social security and health sectors, however, declining total education expenditures since globalization have occurred alongside a redistribution of existing resources towards education programs that benefit the poor. Within the last decade, and for the first time since independence, there have been unmistakable signs that India is slowly shifting its priorities towards elementary education. India's accomplishments have won the plaudits of external agencies such as the IMF, which recently declared India's recent achievements in universal elementary education a "quiet revolution" (Wu, Kaul, and Sankar, 2005).

Three important legislative changes indicate this commitment. First, efforts to address the elitist bias in India's educational system began immediately after liberalization's tentative beginnings in 1986 with the second National Policy on Education.[46] The policy aimed to achieve universal enrollment and the retention of children in school up to age fourteen by 1995. Two relatively successful and expanding schemes that came out of this policy focus on improving basic amenities in village schools and universalizing primary education by emphasizing decentralized management, participatory processes, and capacity-building at all levels of government.

Second, after decades of effort, the ninety-third constitutional amendment was passed in 2001, recognizing elementary education as a fundamental right and making it compulsory. This is quite an accomplishment, given that Weiner's (1991) historical analysis observes in detail how India has repeatedly failed to make education compulsory since independence.[47] The national program that came out of the recent amendment, *Sarva Shiksha Abhiyan*, stipulates that all children will have completed primary school by 2007 and upper primary education by 2010. *Sarva Shiksha Abhiyan* focuses on increasing participation (particularly of the traditionally disadvantaged, such as the handicapped, girls, and those

[46] Tilak (1990) laments the fact that India has taken an average of eighteen years to formulate new education policies. The first National Policy on Education was adopted eighteen years after independence, and next, eighteen years later, the second (1986) policy was developed.

[47] Weiner (1991) argues that the central government's shortfall has been that India's laws permit but do not require central and local governments to make education compulsory. It is important to emphasize here, however, that Weiner's analysis ends in the early 1990s, just as globalization policies were being adopted on a large scale.

living in less populated rural areas), transparency, and public accountability. It also takes measures to ensure states' commitment.

Finally, in 2004 the government imposed an education tax of 2 percent on all central direct and indirect taxes. These revenues have been earmarked specifically for primary education. Indeed, the Tenth Five-year Plan (2002–7) directly reveals that revenues for the primary sectors will come at the cost of subsidies to university education, as opposed to raising total spending altogether.

How, then, has India managed to overcome political resistance to redistributive reforms in education, but not other social sectors? Increasing awareness of the importance of education in a globalizing economy has helped mobilize an informal coalition of policy-makers, domestic business, and the poor. As predicted in chapter 2, the spread of information on the benefits of education has contributed to a cross-class interest convergence. India's governing elites are playing a leading role in spreading information about the benefits of education in an increasingly competitive international market environment.

At the same time, the poor *and* business groups in India have displayed unprecedented support for universal education. On November 28, 2001, almost 50,000 people from poor villages and towns had mobilized during the deliberation of the Education for All (93rd Amendment) Bill in parliament. Sadgopal called it a "historical event":

> It was probably the first time in the history of independent India that people had gathered to demand the right to education. These peasants, landless laborers and slum dwellers, both men and women, demolished the myth promoted by the state and the educated civil society that the poor are interested only in roti, kapda and makaan (food, clothing and shelter) and not in educating their children. They understood that … today, without a Class 12 certificate, a young person stands little chance of obtaining either employment or admission to professional courses. For the Scheduled Caste and Scheduled Tribes, too, the benefits of reservation become available only after Class 10 or 12 as the case may be. Hence the demand for right to education for all children up to 18 years.[48]

Business support for primary education is even more striking, given that there has been a long history of apprehension among India's corporate sector to take upon itself "social responsibilities" such as education. At a recent convention on "Corporate Sector Participation in Elementary Education" organized by the Confederation of Indian Industry (CII), the minister for human resource development, Arjun Singh, appealed to

[48] Anil Sadgopal, "A Convenient Consensus," *Frontline* (Madras), December 22, 2001. Note that this group was concerned that the Bill applied "Education for All" to the age group of six to fourteen, rather than all children from birth to eighteen years.

industry "to look at supporting elementary education not as an act of charity but a decision, which would lead to reform in education, and economic upliftment thereafter."[49] Most tellingly, despite contention within the industry, CII, India's largest and strongest business association, has come out in support of the 2 percent tax earmarked for primary education.[50]

The high levels of spending on tertiary education per student confirm the long history of bias towards this sector. The data also confirm, however, that the 1990s trend in primary education spending shows some improvement, while tertiary-level spending is on the decline. Although inter-state variances still exist, these trends nonetheless suggest that India is gradually redirecting its priorities.[51] The 7 percent growth in literacy rates (for adults above fifteen years of age) in 2000–1 (from 57 to 61 percent), the highest ever annual increase in India, is a good indication that India's growing commitment to universal education is taking effect (*World Bank*, 2005b; see also Dev and Mooij, 2002).

Nevertheless, these developments in education, while positive, must be kept in broader perspective. India's recent achievements have thus far failed to have a major impact. The recent UNESCO (2005) *EFA Global Monitoring Report* did not include India on its list of countries that stood a chance of attaining the goal of universal primary education by 2015. Instead, India ranked among the thirty countries least likely to meet literacy targets because their "very low literacy rates are not increasing fast enough" (UNESCO, 2005: 70). This report was received with great disappointment among India's governing officials.[52]

5.4.4 Summary

It appears that education is one social sector that is experiencing equity-enhancing reform as globalization advances. The trends shown in figure 5.6 suggest that, while the education budget as a whole may be declining, India is redistributing resources away from tertiary and towards primary education. Although the decline in expenditures on tertiary

[49] "Arjun Singh Calls upon Industry to Support Elementary Education," CII Online, August 26, 2004. Available at www.ciionline.org/news/newsMaina4ce.html?news_id=826200423418PM (accessed July 9, 2007).

[50] CII Online, August 26, 2004.

[51] In no way has India made a dramatic shift away from higher education. Note that Dev and Mooij (2002) argue that university and higher education recorded a record rise in the late 1990s (in terms of central expenditures). Rather, the emphasis here is that there were some earnest and effective attempts at redistribution by the Indian government in the 1990s.

[52] "India Questions UNESCO Report," *The Hindu* (Madras), November 10, 2005.

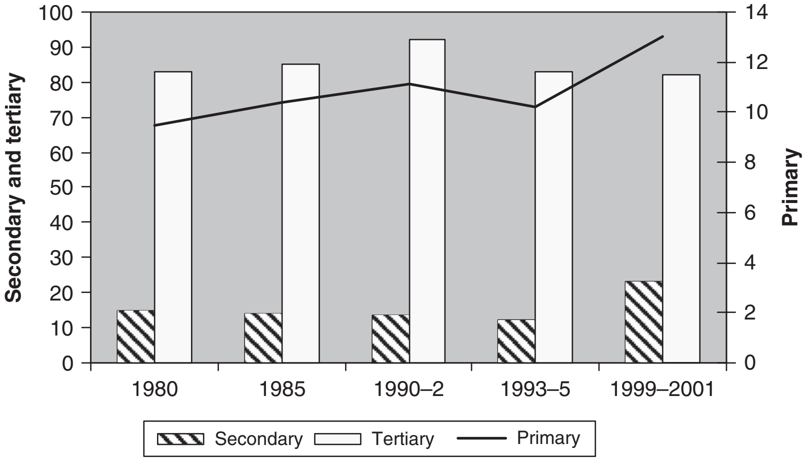

Figure 5.6 Spending on primary, secondary, and tertiary education, selected years 1980–2001

Notes: Years chosen are based on data availability.
Data represent spending at all levels of government.
Source: UN's: Global Educational database.

education is undeniably small, it is particularly striking that resources devoted to this sector began to shift soon after India's financial crisis in 1991. While the changes may not be fast enough or sufficient to solve the existing problems, it is nonetheless encouraging that reforms are being implemented in such a way as to include the least privileged groups.

The health and social security sectors in India have long neglected the disadvantaged, and so the recent cutbacks have the greatest impact on the non-poor and show little evidence of (successful) equity-enhancing improvements. The education sector is unique in its efforts to include the least advantaged segments of the population. Most social programs remain biased in favor of the privileged, however, and the overall impact of globalization on social spending seems to result in harm to the middle classes, with minimal direct effects on the poor.

5.5 Other factors: democracy, ethnic fragmentation, and culture

Given India's long-standing democracy, it is virtually impossible to ignore the prospective role of political freedoms in influencing some changes to India's distribution regime. This warrants a full investigation elsewhere, but, to get a sense, it is worthwhile to consider the following puzzles: why did education reforms become a campaign priority in 2004, although efforts to mobilize the poor began more than a decade earlier, in 1988? Why was the ambitious NREGP (National Rural Employment Guarantee Programme) launched only recently when rural poverty has been a perennial issue? Even more strikingly, the Social Security for Unorganised Workers Bill, which aims to provide benefits for India's 400 million informal-sector workers, has recently been drafted. Exploring these issues may provide some evidence that democracy can affect institutional changes.

There has been a widespread perception that the surprise defeat of the BJP-led National Democratic Alliance in the 2004 general election was a signal that democracies must respond to the poor under conditions of globalization. The former deputy prime minister, L. K. Advani, later admitted that the "India Shining" and "Feel Good" catchphrases widely used by the BJP in its campaign in reference to India's economic accomplishments since liberalization failed to impress the poor.[53] Analysts argue that the urban and rural poor found this particularly offensive. The poverty-stricken residents of one entire village (Harkishan Pura) decided to boycott the elections in response to the increasingly difficult economic conditions they had faced since liberalization. One villager commented: "India may be shining for them [politicians] but our life is without any sheen and shine."[54] It is telling, then, that the newly elected leadership (United Progressive Alliance) immediately presented education as its highest priority, after years of struggling in parliament, as part of its wider campaign to reach out to the poor.[55] Analysts skeptical about the NREGP's long-term prospects attribute its recent adoption to the fact that "the government needed to pass this legislation to fulfill its election promise," but anticipate that "it would soon die a natural death."[56]

Why, then, did the econometric tests in chapter 2 fail to produce consistent results on democracy? The electoral connection, while important, may also be evident in some authoritarian and semi-democratic systems (see Kaufman and Nelson, 2004: 484). Another possibility is that democracy matters, but the time lag for institutions related to democracy to impact on social welfare strategies is difficult to determine except on a case-by-case basis. In the case of the Education for All legislation, the poor began mobilizing and pressuring government officials in the late 1980s, but the Bill did not come into effect until more than one decade later. It may also be

53 Vinay Kumar, "Advani Admits 'India Shining' Campaign Failed to Click," *The Hindu* (Madras), May 28, 2004.
54 "Village Decides to Boycott Elections," *Times of India* (Delhi), March 8, 2004.
55 Access to primary education was a central theme of the Common Minimum Programme.
56 Amelia Gentleman, "India's War on Poverty: Easy Victory Unlikely," *International Herald Tribune*, February 28, 2006.

the case that democracies do not spend more (i.e. increase the *level* of spending) with globalization, as was observed in chapter 2, but encourage more efficient distribution of different welfare resources (see Rudra and Haggard, 2005).

Other socio-political factors, such as ethnic divisions and culture, arguably contribute to the continuity and change (i.e. RTB pressures in certain non-core sectors) of India's protective welfare state. Ethnic diversity helps explain why establishing encompassing labor organizations in India might be exceptionally challenging. As Varshney (2002) has argued, many of the divisions in India's civil society and related political rivalry occur along pre-existing ethnic rather than class lines. Indeed, social divisions in India are extremely complex (religion, linguistic, caste, class, regional) (Manor, 1996), making it all the more challenging for workers to establish common interests in the globalizing environment; sensitivity to race to the bottom pressures and the continuity in particularistic welfare policies are underscored. Finally, the hierarchical caste system and value of group status deeply embedded in India's culture cannot be completely ignored in analyzing its patterns of public good provision. Weiner (1991) links the culture factor to the persistent adoption of elitist social policies, such as the long-time neglect of mass education. Neither culture, democracy, nor ethnic fragmentation can fully explain the post-liberalization changes in India's welfare state, however, since these are relatively stable variables; the recent equity-enhancing reforms in education are an example.

5.6 Implications

Ultimately, the details of the Indian case study reveal that, even in the face of some RTB cutbacks, overall many of the protective welfare schemes remain more or less intact. Signs of institutional continuity are threefold. First, the key elements of India's protective welfare state – labor market protections and public employment – have been relatively resistant to globalization pressures. Second, although India has experienced one important equity-enhancing change that does benefit the poor (i.e. a greater commitment to universal education), government support of protective measures still strongly prevails over productive measures. For instance, health outcomes in India remain extremely dismal and political elites are doing little to change this. Finally, the poor have long been neglected by India's protective welfare state, and this continues to be the case as India expands its reach in international markets. Existing welfare schemes continue India's historical tradition of disproportionately protecting a very small portion of India's larger workforce.

This chapter has also demonstrated how and why protective welfare states such as India have not experienced radical regime change in the current globalizing environment. The pressures of globalization moderated by well-entrenched interest groups, the government–labor relationship, and fragmented labor organizations in India produced two repercussions: (1) they inhibited a coordinated response to globalization that could avoid the trade-off between efficiency and welfare; and (2) they reinforced a welfare state that protects the better off. Greater information about the benefits of education and cross-class interest convergence contributed to the one exception in pro-poor reform: slight improvements in primary education. In addition, India's democratic environment is also one of the intervening variables that contributed to pro-poor reform. Democracy may not have emerged as significant in the quantitative chapters (see particularly chapter 2), because the effects of democracy are more complex than is commonly understood.

At the same time, these findings raise several questions. What are the long-term implications? Will the incremental changes towards labor market flexibility (de facto) and improvements in education lead to a paradigmatic shift to a productive welfare state? For now, it is too early to tell, but the resilience of welfare policies (e.g. public employment) that continue to buttress powerful interest groups does not bode well for this transition. Nevertheless, although India's education reform efforts have not been groundbreaking, particularly given the much larger changes required to improve the living conditions of the majority of the population, they are a promising development in light of the country's history of poverty and its neglect of elementary education. Another question worth investigating in future analysis is why some protective welfare states emphasize some decommodification policies (e.g. public employment) over others (e.g. social security). This case study suggests that country-specific historical circumstances may be the culprit.

6 Globalization and the productive welfare state: case study of South Korea

What are the effects of globalization on productive welfare states? In contrast to protective welfare states, such as India's, are they advancing towards the neoliberal bottom?[1] Who gets hurt from changes in welfare policies as markets expand in productive welfare states? Using details from the case of South Korea, this chapter seeks to answer these questions by illustrating how the interplay of international markets and domestic institutions shapes social policies in a productive welfare state. Just as in protective welfare states (e.g. India), globalization pressures are real and have prompted cutbacks in several of South Korea's welfare programs. At the same time, the South Korean government has also explored ways to make the productive welfare state more "protective." The introduction of universal pensions and health insurance constitutes two examples. This is very distinct from India, a protective welfare state, where the (relatively) major path-breaking reforms have been in the "productive" welfare category (e.g. education). Despite succumbing to some race to the bottom pressures, however, the main features of South Korea's productive welfare state remain intact: promoting citizens' market reliance through extensive state intervention and a concentration of public resources on commodification, particularly education. As a result, the situation of better-off groups in society is similar for both regime types: long-standing domestic institutions essentially guarantee that the more privileged sectors will have access to protections from the risks and uncertainties associated with the globalizing environment. This chapter reveals how international market pressures have led to some welfare retrenchment, yet institutional continuity characterizes South Korea's productive welfare state in the current era of globalization.

[1] For productive welfare states, which, by definition, invest disproportionately more than other LDCs on human capital and less on protective welfare schemes, signs of neoliberal changes might include less state involvement (spending and regulation) in the provision of social safety nets for its citizens (except perhaps means-tested programs) and more private provisioning of productive welfare schemes.

The first section describes the key elements of South Korea's distribution regime, outlining how and why it is a productive welfare state. Section 6.2 demonstrates the effects of RTB pressures on South Korea's welfare state. Next, by illuminating the interplay between globalization and domestic institutions, section 6.3 reveals the extent of institutional continuity in South Korea's productive welfare regime and how and why these long-lived institutions tend to guide policy choices even in the current era. Section 6.4 looks into who is most hurt by the race to the bottom in South Korea, and section 6.5 considers the effects of "other factors" affecting the degree of regime persistence. Section 6.6, in conclusion, reflects on the overall implications for productive welfare states in an expanding global economy.

6.1 South Korea's productive welfare state

South Korea's welfare state has applied extensive state intervention to encourage citizens to be dependent on the market.[2] Particularly since the administration of President Park Chung Hee (1961–79) adopted an export-oriented development strategy in the early 1960s, welfare policy has centered on the promotion of wage labor by simultaneously increasing public support for education services and minimizing protectivist welfare policies that increase reliance on the state. This is not to suggest that South Korea's early approach to industrialization is the primary reason why investment in education is so high and protectionist policies so low. History, culture, factor endowments, and security concerns, as well as the American and, particularly, the Japanese occupations, are also linked to the South Korean prioritization of education. The relevant point is that the government's emphasis on the linear advancement of education (from first concentrating resources on primary-level education and then moving on to secondary-level education) is also associated with the 1960s development strategy and the consequent emphasis on linking benefits to the expansion of wage labor.

Efforts towards an expanding secondary education started in the 1960s *after* primary education had been universalized and the export-oriented growth strategy adopted. Education development and economic planning were not systematically coordinated before the 1960s. Despite

[2] See Holliday (2000) for a related discussion of South Korea's "productive welfare state." Holliday defines the east Asian productive welfare state as one that places social policies as secondary to economic policies, but he does not empirically distinguish between the two. The analysis in this book, however, is unique in its attempts to differentiate social policies in the developing world.

President Syngman Rhee's (1948–60) attempts, the administration lacked "a well thought out economic development plan that could guide educational need" (Seth, 2002: 116). It was not until after President Park Chung Hee's administration adopted the export-oriented strategy that the Five-year Plan for Educational Reconstruction was linked to the first Five-year Economic Development Plan (Lee, 1974). One of Park's primary objectives was to increase the primary enrollment figure to 100 percent and gradually shift education planning and development towards the secondary level (Seth, 2002). This linear expansion of investment in education stands in contrast to the policy adopted in many developing countries, such as India, which began investing heavily in tertiary education *before* primary or secondary education even approached universal coverage. It is no coincidence that policy-makers in South Korea began to view education development on a par with economic planning, while India, for decades, subordinated education goals to the needs associated with its chosen development strategy.

Cultivating a workforce commensurate with the needs of its early industrialization strategy has been a priority of successive South Korean governments since the 1950s. In the 1960s, even though a primary-level education was mostly sufficient since South Korea was focused on low-skill, labor-intensive exports, the president organized the first Council for Long-range Comprehensive Educational Planning. Policy-makers quickly came to recognize the importance of "the human factor" in achieving the mission of export-oriented economic growth (Lee, 1974: 16–17).[3] During his inaugural address, Park Chung Hee noted:

> Self-reliant economy and self-defense are the basis of national independency, peace and prosperity. We will make greater efforts to educate for brains, who are needed to build a highly industrialized society based on heavy-chemical industries and to upgrade our science and technology to the world class.[4]

Education has been the centerpiece of South Korea's productive welfare state, rather than "protective measures" such as social security, labor market protections, public employment, and housing. South Korea's welfare state has emphasized individual responsibility and encouraging citizens to become more dependent on the market. Take, for example, the

[3] As Amsden (1989) puts it, however, it is important not to deify South Korea's education system. South Korea's long-term education planning was not always completely successful, although it did consistently maintain some important features.

[4] President Park Chung-Hee's Inauguration Address, December 27, 1978 (in Korean). The Korean text can be downloaded from the website of the National Archives and Records Service: www.archives.go.kr/president/index.html.

revolutionary words of President Park after a widely supported military coup had brought him to power:

> You, a young girl sitting in the second class compartment, your white hand holding a book of French poetry. Your white hands I abhor. We must work. One cannot survive with clean hands. Clean hands have been responsible for our present misery… I believe the slogans of "Economy comes first," "Priority goes to construction" and "Labor's supreme." (Park, 1963: 177, 179)

Public officials clearly embraced the view that providing all citizens with a formal education complies with the "Economy comes first" philosophy and is key to promoting individual self-reliance. Park emphasized in the early 1960s:

> Reorganization of the school system and rationalization of its management, reform of education taxes providing for free and compulsory education…and an administrative posture giving priority to field education should be established… *I stress the indispensable importance of education for training in the productive capabilities vitally essential to industrial modernization and economic reconstruction*. (Park, 1962: 232–3; emphasis added.)

Ever since then the South Korean government has played a central role in education, both through provision and intervention. Successive governments have spent, as a proportion of the total budget, much larger sums on education than on other social sectors. On average, South Korea spends almost three times more on education than on health and social security combined. The extent of education spending as a percentage of total government spending (i.e. 24 percent) at the dawn of the twenty-first century is an indication of the government's commitment to education relative to other social welfare services. South Korea falls in the top quintile of the full sample for its expenditures as a proportion of total government spending.[5] In stark contrast to India, the great majority of this spending is devoted to primary and secondary education, and most of the elementary schools and two-thirds of the secondary schools are public (Kim and Lee, 2002).

Compared to the size of its economy, however, the South Korean government spends an average amount on education relative to other LDCs.[6] This is still consistent with the institutional norms of South Korea's productive welfare state, as, without necessarily increasing the *level* of expenditures, the government is heavily involved in regulating

[5] This calculation is based on the sample of developed and developing countries used in this analysis.

[6] This has been the case from the early 1980s until the present. During the 1970s South Korea spent slightly less than the LDC average on education.

education and ensuring that the expansion of lower education has occurred in an orderly (and equitable) fashion, and it has made concerted efforts to improve the efficiency of spending (see McGinn *et al.*, 1980). For example, the government has ensured universal access to primary and secondary education by centralizing control in the Ministry of Education (MOE), controlling tuition rates, regulating the entry process to primary, secondary, and tertiary education, and randomly assigning students by computer to attend both private and public schools (Lee, 2002; Kim, 2001; Seth, 2002).

In contrast, the South Korean government has played a minor role in both the provision and regulation of health care. Similarly to India, the government has invested little in health delivery, and since the 1960s it has taken a laissez-faire approach to the supply side of health services by the private sector. In 1966 only 7 percent of total health care services were provided by public institutions (see McGuire, 2006: 11), and currently, four decades later, it has risen slightly, by three percentage points, to 10 percent (Lee, 2003). Public outlays on disease prevention and health promotion continue to be extremely low (OECD, 2004). Unlike India, however, the poor quality of public-sector provision of services (qualifications, service at public health care facilities, updated equipment) has not been the fundamental issue and is at par with international standards (Jo and Choi, 2002; OECD, 2004). How, then, has South Korea achieved such dramatic improvements in life expectancy and infant mortality rates over the last few decades? McGuire (2006) argues convincingly that it is South Korea's rapid income growth that is responsible for this achievement, not public intervention.

At the same time as it has been promoting productive policies such as education, the South Korean government has long prevented the expansion of protective welfare schemes such as social security, housing, public employment, labor market protections, and direct poverty alleviation programs. In terms of social insurance protections, both coverage and the level of benefits have been very low. Despite President Park's public promise to introduce a National Pension Scheme in 1972, and the formation of several task committees to introduce the program, he postponed the program just four days after it was officially launched (Kim, 2006). Only civil servants, military personnel, private school teachers, and workers in large establishments enjoyed some pension coverage.[7] It is remarkable that, even today, government expenditures on social security

[7] For example, large South Korean firms maintained a severance pay system that granted employees a lump-sum amount paid on retirement or separation from the firm (Yang, 2001a).

barely exceed 1 percent of GDP, despite the recent reforms in the NPS designed to support universal social security coverage (discussed in more detail later). This is far below even the most liberal welfare states, such as the United States, which spends 21 percent of its GDP on SS and welfare.[8]

Housing needs have been largely ignored by the South Korean government (Park, B.-G., 1998; World Bank, 1979), even in the face of a chronic housing shortage. It was not until the 1980s that President Roh Tae-woo's (1988–1993) regime pursued the "Two Million Housing Units Construction Plan" to address the housing shortage (Doling, 1999). These houses were to be built in four years, and the role of the public sector in housing provision was to increase. President Kim Young Sam (1993–7) stopped supporting the construction of public housing rental units soon afterwards however, in 1994. Park (1998) reports that, after 1993, government expenditure on housing decreased by over 10 percent annually.[9]

In stark contrast to India and many other developing countries, South Korea has also avoided public employment as an effective or desirable social welfare protection strategy. Even when public enterprises accounted for a proportionately high percentage of total investment in the early 1970s, public enterprise contribution to jobs created was extremely modest (Jones, 1975). Jones (123) argues that South Korea's public enterprises were "a most inefficient means of employment creation." Civil servant employment similarly constitutes a low percentage of total employment relative to other developing countries, and has been steadily decreasing since the turn of the century. Data indicate that South Korea's total public employment (as a percentage of the labor force) places the country in the bottom quintile of developing nations. Its ratio of public employment to total employment is twenty percentage points less than the global average in developing economies.[10] South Korea's public works programs did not start until the late 1980s and, even then, employed a very small percentage of the poor. Indeed, South Korea's low unemployment levels even during times of economic crisis have contributed to the overall lack of demand for public employment as a welfare strategy.

[8] These values are based on data from the IMF's *Government Financial Statistics*, various years.

[9] Note that the proportion of government expenditure on housing decreased from 2.3 percent in 1989 to 0.6 percent in 1995.

[10] Data from the ILO report total public employment, including those employed in state-owned enterprises. Estimating a sample of non-OECD countries that include east European nations reveals a public employment average of 31 percent. Data from South Korea reveal that total average public employment has been 9.7 percent since the late 1970s, placing the country in the bottom quintile of the data set.

Similarly, for most of South Korea's modern history, governments have played a minimal role in providing labor market protections. Some legislative protections against dismissals did exist; because of the implicit practice of lifetime employment, however, governments did not face great pressures to enforce them. The issue was that lifetime employment contracts were limited to a very small percentage of workers affiliated with chaebols.[11] These large industries could manage the costs of doing so because of the many years of sustained economic expansion. At the same time, until the late 1980s labor repression was standard practice, as were heavy restrictions on organizing and protesting.[12] The absence of such labor market protections has long ensured that employers maintained a clear advantage in the bargaining process.

Finally, South Korea's productive welfare state has been averse to providing monetary assistance to working individuals who live at or below the poverty level. South Korea maintained a Poor Law tradition for over thirty-five years after independence in 1945. Although article 19 of the first constitution in 1948 stipulated that "those individuals incapable of working due to the old age, illness, or other reasons shall be protected under law by the state," no institutional support was put into place until the 1960s (Kim, J.-S., 2004). Korea's primary poverty alleviation strategy, the Livelihood Protection System (LPS), was implemented in 1961 and involved six kinds of aid: livelihood, medical, educational, maternity, funeral, and self-support. The problem was that these protections had very low coverage because of extremely stringent conditions for eligibility. By 1974 only one out of four persons in absolute poverty was receiving benefits (Kim, J.-S., 2004). Cash benefits were estimated to reach fewer than a half of those under the official poverty line (Kwon, 2002). The fundamental philosophy, as indicated by article 3 of the 1963 Social Security Act, was "not to hamper the spirit of self-support of the people" and cash assistance was to be issued "gradually as provided for by law in light of the economic circumstances of the state" (Kim, J.-S., 2004: 150). The means test provision thus applied only to non-able-bodied persons, disqualifying the large number of working poor between the ages of eighteen and sixty-five. Even today, South Korea's means-tested programs, though expanded, are still described as "strict" by policy experts and cover only 3 percent of the population (see Kwon and Holliday, 2007).

[11] Chaebols are large business conglomerates in South Korea, most often family-owned and usually clustered around one parent company.

[12] In particular, labor repression was practiced using three mechanisms: restrictions on union organization, controls on the incidence and manner of strikes, and limits on wage increases in private firms.

In sum, in direct contrast to India, the South Korean government has long placed proportionately greater weight on human-capital-type welfare programs, specifically education, than on more protective social schemes that increase dependence on the state as opposed to the market. The contrasting characteristics of the two regime types reinforce the findings in chapter 4 that most LDCs face a trade-off between human capital investment and protective welfare policies. The next section explores the pressures of globalization and the extent of cutbacks in South Korea's welfare state.

6.2 Race to the bottom

Advances towards more open markets in South Korea began in the early 1980s. In 1980 South Korea implemented the first major programs for liberalizing import protections, followed by a five-year tariff reduction plan beginning in 1984. After significant pressure from the United States, capital account liberalization was also initiated in the early 1990s (Lukauskas and Minushkin, 2000; Crotty and Lee, 2002). The 1997–8 financial crisis and subsequent IMF-mandated policy changes resulted in even more substantial trade reforms and the further dismantling of controls on international capital flows (e.g. additional reductions in tariff barriers, the elimination of quantitative restrictions and a number of subsidy programs, lower barriers to FDI, the complete opening of the bond market to non-residents, and the removal of all restrictions on foreign borrowing by South Korean firms). The pressures of globalization thus began to intensify in the early 1980s, followed by more extensive reforms after the financial crisis of 1997–8 (Yang and Hwang, 2001; Choi, 2002; Kim, 1994). The following sections focus on the effect of globalization on South Korea's welfare regime beginning in the early 1980s, with particular focus on the aftermath of the crisis.

Did these advances towards globalization lead to a race to the bottom? In a manner similar to what happened in India, the major welfare cutbacks linked to globalization pressures have occurred in the sectors that are not key features of South Korea's welfare regime: social security and labor market protections. The trend in both sectors was an initial improvement in benefits after globalization policies were first adopted in 1980, followed gradually by retrenchment, most predominantly after the financial crisis. The cutbacks in South Korea's social security sector are particularly startling, given that, in both domestic and external academic and policy-making circles, South Korea is commonly referred to as a "welfare laggard." This label has been earned primarily because of the consistently low levels of public spending allocated to social-insurance-type functions.

Indeed, as discussed earlier, the level of social security spending (relative to both GDP and total government expenditures) is exceptionally low in comparison to other countries, both in its own and in contiguous income brackets.[13] South Korea has been similarly criticized for labor management relations that have grossly favored the latter. Deyo's (1989) analysis has made a lasting impression by attributing South Korea's phenomenal economic growth to a "dark underside": the extreme political subordination and exclusion of workers. Signs of a race to the bottom emerge in both social security and labor protections, however, despite the already existing low commitments relative to international standards.

6.2.1 Social security

Cutbacks in the social security sector subsequent to economic liberalization are consistent with the predictions of chapter 2. Before the crisis, however, and not long after the initiation of globalization policies in the early 1980s, the government adopted two important reforms in the social insurance sector that suggested resistance to race to the bottom pressures. Both these reforms involved higher costs for the government and employers, accounting for some of the rise in SS expenditures after the late 1980s (see figure 6.1). First, South Korea implemented a partially funded National Pension Service (NPS) in 1988.[14] Second, unemployment insurance was instituted in 1992 for firms with thirty or more employees, and later expanded to firms with five or more employees after the financial crisis resulted in high numbers of unemployed workers.[15]

Of the two reforms, South Korea's newly implemented NPS calls for greater focus, since unemployment benefits have been extremely modest overall and cover only a small fraction of the unemployed. This is not to underplay the significance of the adoption of an unemployment scheme in South Korea, since very few developing countries have done so. Analysts are skeptical that the new program is part of a "genuine insurance scheme creating entitlement to benefits," however. As Bidet (2004: 11) pointedly

[13] Argentina and Greece, for example, spend an average of 5.3 and 7.6 percent on social security (as a percentage of GDP), respectively, while South Korea allocates only 1.2 percent on average. These averages are calculated from the IMF's *Government Finance Statistics* over the 1972–97 time period.

[14] The NPS is labeled as "partially funded" because it has elements of both a fully funded and a pay-as-you-go scheme. As a fully funded system, it has a substantial amount of reserved funds, and plan sponsors must contribute to equal actuarial liabilities. It also has elements of pay-as-you-go, since payment of annuities is not guaranteed by the reserves and contribution rates are not based on actuarial estimates (see Yang, 2000).

[15] "Will the Unemployed's Right to Live Be Secured?" *Hankyorhe* (Seoul), February 3, 1998, 23.

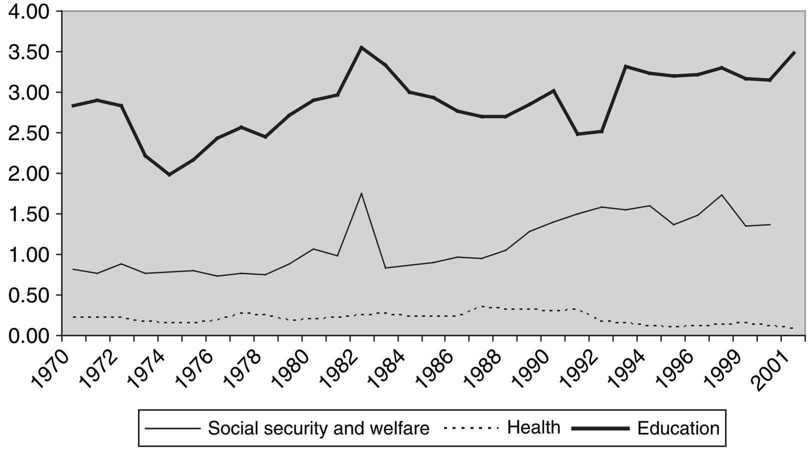

Figure 6.1 Government social expenditures as a percentage of GDP, 1970–2001

Source: IMF, *Government Finance Statistics* (various years).

summarizes the situation, "The new and radical possibility of joining a genuine unemployment insurance scheme may now exist on the statute book, but it has so far made little impression on popular thinking. The idea of registering as a jobseeker and being paid an allowance remains alien to many Koreans…" He further documents that the employment budget was cut by 60 percent between 1999 and 2000.

The National Pension Service, on the other hand, appears to be a marked departure from South Korea's past. For decades after independence, the majority of industrial laborers and the self-employed did not have pensions (Yang, 2000). From 1960 to 1988 only civil servants, military personnel, private school teachers, and workers in large establishments enjoyed coverage. In 1988 pensions became mandatory in workplaces with ten or more employees, and then in establishments with five or more employees in 1992. President Kim Young Sam made the expansion of pension coverage one of his main electoral pledges the following year. Honoring his commitment, in 1995 coverage was extended to include the rural self-employed and fishermen, and four years later the urban self-employed were included as well. The NPS is funded by employers and employees only.

Soon after the financial crisis, however, and in the face of mounting criticism from business representatives (e.g. the Korea Chamber of Commerce and Industry), the government began revising the pension law. Concerns about the sustainability of South Korea's social programs were particularly intense after the financial crisis of the late 1990s. The primary issue was that, in the current environment, the level of benefits was considered too generous relative to the low level of mandated contributions.[16] These contentious reform Bills were adopted even before the NPS had started to pay out full pensions.[17] Labor's reaction to these reforms is well represented by the following statement from an official of one of South Korea's leading labor confederations: "The government's estimates [of the expected draining of funds] have been made by blowing the financial crisis totally out of proportion."[18]

Three major reforms initiated in 1998 suggest welfare retrenchment. First, the average income replacement rate was reduced from 70 percent to 60 percent.[19] A current reform Bill, proposed in 2003, focuses on even more substantial curtailment of the benefit level. The Ministry of Health and Welfare explained that contributors will ultimately "pay more but get less."[20] Second, the eligible age was to be raised from sixty to sixty-five. And, third, it was agreed that the contribution rate would be re-evaluated every five years starting in 2013.[21]

While South Korea's aging population and government mismanagement have certainly contributed to the urgent push for reform, signs of globalization pressures are also evident. From the RTB perspective, it is revealing that the South Korean government has had to avoid two fiscal tools for stabilizing the fund: increasing taxes and introducing higher government contribution rates. Applying general revenues to maintain pension benefits is off the bargaining table because of the effect it would have on tax rates.[22] Social insurance schemes are based solely on employer and employee contributions. Labor union officials have argued, rather futilely, that the government should consider supporting low-income subscribers "with state funds like in advanced countries,

16 In 2000 the World Bank reported that the NPS will incur deficits by 2037 and the fund will be completely depleted by 2049 ("World Bank Recommends Systemic Reform of Korea's Pension Scheme," *Korea Herald* (Seoul), January 17, 2000).

17 There are recipients, however, of survivor pensions, invalidity pensions, and lump-sum benefits (Kwon, 1999). The payment of full pensions is scheduled for 2008.

18 "Pay More, Get Less under New Pension Plan," *Korea Times* (Seoul), August 22, 2003.

19 South Korea's replacement rate is the monthly pension at retirement age (on average sixty-one), divided by the wage of the last month at work.

20 "Pay More, Get Less," August 22, 2003.

21 "KDI Proposes Pension Reform to Cope with Aging Population," *Korea Times* (Seoul), May 28, 2002.

22 As one official from South Korea's Employer Federation commented regarding pressures for a retrenchment of pension benefits, not only are they against the government increasing taxes to raise the requisite resources, it is known that the government simply will not agree to it.

instead of trying to increase the burden on citizens."[23] A 2004 proposal requesting a basic pension plan financed by general taxes has been adamantly opposed by the government (Kim, 2006). Palley (1992: 801) concludes that currently "the political-economic drive of low income taxes and low taxes on equity transactions…leaves few resources available for necessary services for the disabled and the elderly."

South Korea's contribution rate is very low by international standards, and advocates of the race to the bottom hypothesis could feasibly argue it currently represents the "lowest common denominator" in government spending on social insurance benefits.[24] Increasing the contribution rate above the current 9 percent is hotly contested by the business community, primarily because of the effect this would have on payroll costs.[25] While the government has agreed to consider recalculating the benefit every five years, a gradual increase in the contribution rate was not legislated (Phang and Shin, 2002), and analysts of pension reform express great skepticism (Yang, 2001a; Moon, 2002). What has been agreed is that the maximum limit of the contribution rate will stay intact until 2009.

To summarize, the implementation of unemployment insurance and, in particular, the National Pension Service suggests resistance to RTB pressures. Major reforms have been made to these programs, however, including a reduction in the average income replacement rate, an increase in the eligible age of recipients, and a regular re-evaluation of the contribution rate starting in 2013. These changes impact South Korea's existing social insurance scheme and suggest that welfare retrenchment eventually occurs after economic openness policies have been adopted.

6.2.2 Labor market protections

Race to the bottom effects also emerge in South Korea's system of labor market protections. As in social security, these cutbacks came after an initial period of expansion following the economic liberalization. Not long after

[23] "Pay More, Get Less," August 22, 2003.

[24] For example, (employer and employee) contribution rates in the United States are 12.4 percent, 13 percent in Japan, up to 28 percent in Brazil, and 9.5 percent in India – a low-income country that requires no pension contribution from the wage-earners (*Social Security Programs throughout the World*, available at www.ssa.gov/policy/docs/progdesc/ssptw). Note that, for many nations with low contribution rates by wage-earners, the contribution rates of either the government or the employer, or both, are high (e.g. Sweden, Australia, Brazil). The South Korean government does not make any financial contributions to the social insurance scheme aside from administration costs and a small portion of the pensions for those on low income.

[25] Moon (2002); "Firms, Labor Question Pension Plan," *Korea Times* (Seoul), August 8, 2004.

economic liberalization was initiated, in 1988, labor gained important political freedoms, such as the right to organize, union pluralism at the national and industrial level, and pledges of limited government interference in dispute resolution and arbitration. Since these gains, however, labor has faced a difficult battle. Primary issues included official recognition of the Korean Confederation of Trade Unions (KCTU), which was delayed until as late as 2001; the recognition of teachers' unions, which, after a long and protracted fight, was accepted in 1999; and the recognition of multiple unions at the enterprise level, which has been postponed three times and is now set to be implemented in 2009. The slow pace of these reforms post-globalization suggests that RTB pressures contribute to the government's reluctance to provide labor with the full set of basic standards adjudicated by the ILO. Since the financial crisis, labor's situation seems only to have worsened. The ILO has consistently ruled that the South Korean government continues to violate freedom of association principles (US Department of Labor, 2003; Cho, 2002; Jang, 2004; Buchanan and Nicholls, 2003). Concerns include the arrest and detention of trade unionists, the government's refusal to register new labor unions, and the adoption of labor legislation contrary to freedom of association.

Race to the bottom pressures also appear to have affected legislation related to employment protections. These reforms, on balance, favor employers. The first major indication of RTB effects is the formal dismantling of the system of lifetime employment. This is an arrangement whereby an employer guarantees lifetime employment to workers, who, in turn, remain committed to that firm (Lindauer, 1984). A Supreme Court ruling on the Labor Standards Act (LSA) in 1989 marked the end of this regime by codifying South Korea's labor laws and legislating limitations on worker dismissals (Kitt, 2003). While employers view the LSA as a concession to labor since "urgent managerial need" now has to be established before lay-offs are permitted, workers view any regulations permitting lay-offs as a direct affront to their rights. The fundamental problem is that the LSA conditions for dismissal are sufficiently vague to render management and labor alike unsure of their rights (Kitt, 2003). In practice, however, employers have gained the advantage; Kim Soh-Young (2004: 545) observes that, by 1991, the Supreme Court had legally expanded the scope of employers' managerial need and clearly gave more consideration to the employers' interests than the concerns of employees. In addition, the 1998 amendments to the LSA were an attempt to make lay-offs easier for employers by eliminating the need for court orders to effect dismissals.

Changes in the laws were not the only way for employers to gain advantages over employees. Employers who still found the requirement for "managerial urgency" too onerous resorted to other means to forgo the rigors of dismissal. First, they avoided the LSA by the use of "honorable retirement." In 1998 35 percent of firms utilized honorable retirement to encourage the "voluntary" dismissal of workers (Kitt, 2003). Second, and with more profound effect, employers increasingly began to recruit temporary, or "non-standard," workers, who are not statutorily protected from "unjust" dismissals (Lee and Lee, 2003; Kim and Cheon, 2004; Kitt, 2003).

6.2.3 Summary

In sum, after the turn towards globalization and the 1997 financial crisis, labor market protections have declined because of frequent violations of freedom of association, the dismantling of the lifetime employment regime, the legalization of redundancy dismissals, recommended early retirements, and the increased hiring of non-standard workers. This, in addition to the retrenchments in social insurance policies, suggests the effects of a race to the bottom on South Korea's welfare state.

6.3 Institutional change

Despite the cutbacks just discussed, the South Korean welfare state is characterized by institutional continuity. Recall that Pierson (1996) uses three criteria to determine institutional change versus continuity: (1) significant increases in the reliance on means testing; (2) dramatic reductions in benefit and eligibility rules; and (3) major transfers of responsibility to the private sector. I add a fourth: the persistence of institutional legacies. The fact that South Korea has not experienced the first three, while long-standing institutions persist, suggests that, despite some retrenchment, the country is not racing to the neoliberal bottom. It is evident that the institutional norms associated with South Korea's productive welfare state continue to guide the direction and character of reforms under the conditions of globalization. All the new protectionist schemes introduced after economic liberalization are employment-based and thereby encourage market dependency, including the revised poverty alleviation schemes. Furthermore, the sustained emphasis on equity in (lower) education ensures that a strong, interventionist role for the government will persist well into the twenty-first century. South Korea also maintains government investment in education to a much greater extent than protective welfare schemes.

The first part of this section therefore focuses on the ways in which institutional continuity manifests itself in South Korea's welfare state, despite the effects of RTB pressures. The second subsection deals with the question of *why* paradigmatic welfare regime change has been difficult in South Korea.

6.3.1 Welfare regime change?

This section explores the four criteria for institutional change in turn. The incremental changes to South Korea's protective welfare schemes are worth noting. Important elements of its productive welfare state remain intact, however.

First, despite some changes, South Korea has not moved towards a major expansion of means testing. The National Basic Livelihood Security (NBLS) system was adopted in 2000 to replace the 1961 Livelihood Protection System. The key difference in the two programs is that the program now includes working persons who fall below the poverty line. While this appears to be a promising development, the OECD (2000: 138) reports that the eligibility criteria are still very stringent and, ultimately, not much better than NBLS (see also Kwon and Holliday, 2007). Interestingly, consistent with the institutional norms of South Korea's welfare state that encourage market dependence, cash benefits are conditional upon voluntary participation in cooperatives or vocational training. Benefits are denied to those who are able to work and refuse to comply with benefit rules, such as a refusal to accept training placements offered by authorities (OECD, 2000). Jung (2005: 18) concludes:

> The Korean government…has hardly had experience in their implementation for social assistance recipients. Accordingly, whether the NBLS system would turn out to be an epoch-making social assistance program, elevating the level of the Korean social welfare remains to be seen.

Second, there have been no radical changes in benefits. The cutbacks in social security discussed in the previous section can hardly be considered dramatic. It is difficult to represent the increase in the retirement age by five years or the reduction of the replacement rate by ten percentage points (from 70 to 60 percent) as a paradigm shift to a liberal welfare state. The average replacement rate in a liberal welfare state such as the United States is 46 percent, which is substantially lower than it is in South Korea (Congress of the United States, 2005).[26] In addition, South Korea's mandated retirement age for receiving benefits is now about

[26] The difference in the rates should be regarded as a rough evaluation. Replacement rates in various countries are not always directly comparable and must be viewed with caution.

average. It is the same as in most liberal welfare states and even some social democratic welfare states.

In terms of eligibility, both health insurance and pension coverage have become universal, but only de jure: 40 percent of South Korean wage-earners still remain without any coverage (see Kang, 2005). From this perspective, then, benefits in the aggregate have not experienced much increase.

The third condition, of "major transfer of responsibilities to the private sector," does not hold in the South Korean case. Private-sector participation has increased only in those social sectors that have always been market-oriented. In social security, the government resisted World Bank pressures to integrate retirement allowance in a funded and privately managed defined-contribution plan (Yang, 2004). In education, the bulk of post-secondary institutions were private long before globalization policies were implemented, and this continues to be the case. Recent efforts to increase the number of independent private schools at the secondary level have met with significant resistance.[27] A similar situation exists for South Korea's health sector, although the private sector has long dominated health care at all levels (primary, secondary, and tertiary). As noted earlier, the government has always played a minor role in South Korea's health delivery system. The private-sector, fee-for-service system prevailed even before the 1988 introduction of insurance plans, and has expanded since then. For example, 34.5 percent of all hospitals were public in 1975, and this share had dropped to 4.9 percent by 1994 (Yang, 2001b). While this is a large percentage change, in terms of absolute numbers the extent of public involvement has always been minimal. In 1975 approximately sixty-three hospitals were public, and this number had fallen to thirty-two by 1994. Moreover, the government continues to maintain minimal regulations regarding location, quality, and the type of service the private sector provides, as well as the level and nature of competition between them (Ramesh, 2004). The long-standing trend of private-sector dominance in the health sector thus continues into the twenty-first century.

Finally, continued state intervention in education services ensures that "market dependency" is consistent with past institutional norms. The South Korean government still intervenes heavily in education and maintains strong centralized control over this process, despite the rising concerns of reform advocates that excessive state intervention has compromised the quality of education and poses an obstacle for continued economic development in the globalizing era.

[27] "Roh Opposes Elite Private Schools," *Korea Herald* (Seoul), March 24, 2006.

Recent governments have been keenly aware of the need to improve the quality of South Korean education in the current era of globalization. A speech made by the minister of education soon after education reform was first initiated in 1995 (i.e. the Commission for Education Reform) encapsulates this sentiment:

> We are about to step into a new era of unprecedented changes as national boundaries disappear and globalization proceeds. A new paradigm of economy is formulated as intellectual capital such as knowledge, technology and information replaces tangible and physical assets. In the light of rapid changes, we are all confronted with new challenges, and we must prepare ourselves to survive through the new era. The future jobs will require more diverse vocational abilities and knowledge, calling for educational reform and a guaranteed system of lifelong education for all.[28]

Demands for greater school autonomy and less state regulation by all sectors of society (teachers, labor groups, civil society groups, business) have met with only limited success, however. The education system has remained highly centralized and uniform in standard, content, and method, with the exception of only some minor reforms (Seth, 2002; Kim, 2005). Specifically, the main areas of concern about centralized command and its compromising of educational quality – the system of student quotas, the tendency towards uniformity of curriculum and a state entrance exam – remain more or less intact. The Presidential Commission for Education Reform, appointed in the early 1990s, resulted in minimal reforms and actually reinforced the status quo, leaving "structural problems unaddressed" (Kim, 2005; Seth, 2002). The South Korean Assembly has passed a Bill that is a modified version of the current system without many of the elements of reform (Park, 2000). As Kim (2005: 13, 14; emphasis added) puts it:

> In spite of such a favorable environment, however, the reform measures which the civilian governments employed did not bring significant changes to the existing educational system… [I]nternal conditions shifted the themes of education reform debate from liberalization, decentralization, and so on, to a reform that would enhance educational performances – in particular, "quality, excellence and the nation's competitiveness" – within the existing arrangement but *with enhanced state intervention* and financial commitment.

The Private Schools Law, aiming for both deregulation and decentralization, represents the latest contentious political battle. This law will encourage more private high schools to become "self-reliant" and attract

[28] "Educational Reform Must Cope with Social Diversification," *Korea Times* (Seoul), April 30, 1999.

top-quality students. In response, the conservative Grand National Party boycotted parliamentary sessions and caused a legislative impasse.[29] Plans to implement more autonomy and transparency in state universities by increasing stakeholder participation are also stalled.[30]

This is not to suggest that absolute institutional stasis characterizes the South Korean productive welfare regime. The codification of labor market protections and the attempt at universal coverage of both social and health insurance that started in the late 1980s (discussed in greater detail in section 6.4) are indeed significant developments, given the virtual absence of formal protectionist policies since independence. These reforms do not constitute paradigmatic institutional change, however, for three specific reasons. First, these schemes are employment-based, and thereby reinforce the productive welfare state's emphasis on market reliance. Second, the South Korean government's attention to education still far surpasses its investment in protective policies. For example, in 2001 public spending on education exceeded social security by a ratio of two to one. Finally, as was the case in India, the working poor continue to have limited access to protections from market risks (as is explained in greater detail in section 6.4).

In sum, since the current reforms are being guided by the South Korean principle of market reliance, it is more accurate to interpret recent welfare reforms in the country as following a "productive" path. These findings are consistent with Kwon and Holliday (2007: 242; emphasis added). They argue:

> The extent of the reforms undertaken since [the 1997–8 Asian financial crisis] has been exaggerated by many observers and analysts. In fact, when the reality of Korean social policy is separated from the rhetoric that surrounded it…, the extensions that took place in the late 1990s turn out to have been rather modest. *Crucially, they did not alter the fundamental character of the Korean welfare state in this era of globalization.*

6.3.2 Mediating role of domestic institutions

In this section I explore the mediating role of institutions in response to globalization pressures and investigate why key elements of the productive state have remained intact in spite of some retrenchment. First, the strategy of export-oriented development and the prioritization of

[29] "Schooling the Brightest," *Yonhap* (Seoul), December 29, 2005.

[30] "Education Marked by Disputes over Reform," *Korea Times* (Seoul), December 29, 2005. According to the plan, universities would be governed by a board consisting of a president, regional community members, and alumni representatives. The goal is to allow ordinary workers to have influence on the university governance committee.

commodification policies have structured access to the political arena for particular distributional coalitions (i.e. the chaebols). These groups support the key features of South Korea's productive welfare state. Second, given that labor is not among the privileged interest groups, the government–labor relationship does not depend on protective welfare benefits to maintain labor's political support and social peace. Instead, the government–labor relationship evolved on a basis of open conflict and confrontation. This antagonistic relationship makes it exceptionally difficult for government and labor to reach mutually beneficial agreements that could be advantageous for all categories of South Korean workers in the globalizing environment. Adding to this, labor groups are fragmented. Ideological divisions abound, making it virtually impossible to for them to lobby *with one voice* against race to the bottom pressures or ensure unified support for pro-poor social policies.

Elaborating on the first point, in the attempt to pursue a successful export-oriented development strategy, a symbiotic relationship between government and big business evolved (Kim, 1997; Evans, 1998). From the early 1960s onward President Park preferred to deal with a small number of entrepreneurs, and persuaded them by expanding their licenses in industries and protecting them from foreign inputs. The critical differentiating factor from the Indian approach was that this support was contingent upon firms' increasing their exports and outward foreign investment.

Government prioritization of commodification was beneficial to the chaebols, guaranteeing a readily available, trained, and productive workforce even in the initial phases of development. As Amsden (1989: 235) notes, education was one of the primary reasons the chaebols "reoriented their activities away from rent seeking and toward profit maximizing." She continues:

> Once the entrepreneurs saw the managers were capable of managing, that the engineers were capable of producing products that worked, capital investment became a viable option.

This economic weight that the chaebols have generated has provided them with privileged access to the policy-making environment, *relative to other interest groups* (see, for example, Park, 1987). By the late 1970s, for instance, it was common practice for large firms to demand favorable treatment in exchange for financial contributions to the ruling party (Haggard and Moon, 1990; Nam, 1995).[31] South Korean governments

[31] Note that, while government manipulation does not guarantee that business associations will always be effective, entrepreneurs may still exploit their personal linkages to gain benefits (Park, 1987). The relevant point is that other interest groups in South Korea cannot resort to either of these options.

are therefore sensitive to political counter-attacks by the large business representatives, such as the Federation of Korean Industries (FKI) (see Haggard and Moon, 1990, for examples). Given these structural constraints, the government has been far from immune to the chaebols' resistance to the implementation of more protective welfare measures.

South Korea's major business leaders concur that such protective welfare policies and programs would interfere with the "economy first" approach and reduce worker productivity. Big business leaders have actively protested against the current slate of protective reforms (e.g. labor market reform, pensions, NBLS), and are concerned that they will exacerbate labor–management relations by emboldening labor. At a relatively recent meeting with the government, one of the heads of the nation's five largest economic organizations was quoted as saying, "Accommodating such demands basically goes against the basic principle of 'no work, no pay' and can have dangerous implications. Such demands simply cannot be met."[32] Another participant argued, "It is our hope that the government consult with businesses before implementing these changes since they can have a strong impact on their financial conditions."[33] Although chaebol resistance is not always successful, reformers face an uphill battle in confronting the largest interest group in the country.

The nature of the government–labor relationship has also contributed to the institutional bias towards education and against the protective welfare benefits that South Koreans generally view as promoting state dependency. In contrast to India, South Korea's government–labor relationship has evolved on the basis of repression and confrontation. Until recently, successive governments unabashedly pursued a pro-business stance and overtly excluded labor. No attempt was made to harmonize the interests of labor and capital in South Korea, other than the emphasis on education. Rather than attempting to incorporate the labor movement and mobilize workers as a base of support, as in India, labor policy in South Korea for decades involved extensive repression of workers' rights. The government was "quick and ruthless" in reacting to any signs of labor unrest (Koo, 2001; Deyo, 1989). Factory and working conditions constituted "virtual prisons," and scholars have often compared labor's plight to slavery (Lie, 1998). Demands for government protection for labor long went unheeded. Put simply, in the first four decades after independence the government's economic and political

32 "Business Leaders Ask Gov't Not to Interfere in Labor Issues," *Korea Times* (Seoul), February 12, 1999.

33 "Business Leaders Ask," February 12, 1999.

strategy did not require protective welfare benefits to "buy" labor's political support. As Koo (2000: 19) explains:

> Although the South Korean labor regime is usually described as a corporatist system, its actual operation was based on a crude repressive form of control rather than a sophisticated corporatist system. Unlike the situation of most corporatist labor regimes, in which officially sanctioned unions are allowed to channel worker representation, the South Korean government was primarily interested in keeping workers unorganized and controlling them through security forces rather than though labor branches of the government… [T]he South Korean government relied primarily on threats and punishment, using security ideology to control labor agitation… This exclusionary approach produced a cadre of hard-core unionists by driving them out of the industrial arena – many union activists were fired and blacklisted from future employment – and by pushing them, inadvertently, to develop close ties with political activists and student radicals.

This government–labor relationship and the resulting effects on policy stand in stark contrast with India, in that welfare benefits have not served as a great source of clientelistic support and patronage. Rather, the government's past disregard of worker needs and demands has created an extremely adversarial industrial relations environment. Employer–employee relations tend to be hostile, and independent labor groups maintain a deep-seated distrust of the government. As Lie (1998: 114) describes it, after decades of harsh labor repression "[T]he accumulation of human tragedies – physical and spiritual anguish – [has] manifested itself in the cultural expression of *han*, which can be loosely translated as *ressentiment* [resentment]." The consequence is that current social policy negotiations are characterized by long-running disagreements between government, employers, and labor, making it particularly difficult to change the welfare status quo. Policy compromises that might allow the government to balance social interventionism with macroeconomic stability are unlikely in this environment.

The most telling example of this contentious government–labor relationship is the malfunctioning of the Tripartite Council, which was set up to facilitate dialogue and compromise between government, business, and labor representatives on issues related to globalization and social reform. It was hailed both nationally and overseas as a promising development for labor relations. Labor's disaffection with the forum rapidly escalated, however, and not much more than one year later one of labor's leading confederations, the KCTU, withdrew from the council. The KCTU president, Lee Kap Yong, remarked that "[i]t is not a genuine mechanism of social cooperation but a capitalist tool of control to prevent labor resistance and to carry out their own plan of structural restructuring effectively" (Koo, 2000: 246). The council has failed to live up to its potential as an effective tool for engaging labor's cooperation (Henderson *et al.*, 2002; Lee and Lee, 2003; Koo, 2000; Song, 1999).

Divisions within South Korea's labor movement add to this institutional paralysis. The country's national labor market institutions are not sufficiently encompassing to overcome labor's collective action problems. Although PLP in South Korea has increased over the decades it has not approached the levels of European countries, and workers are unable to promote policies that mitigate the negative effects of globalization. The distrustful government–labor relationship also reinforces the divisions within South Korea's labor movement. Early attempts to depoliticize labor gave rise to ideological rifts and the formation of radical labor movements. The Federation of Korean Trade Unions (FKTU) was originally formed in 1946 by right-wing groups backed by the US military forces, only to be taken over in 1961 by General Park's Plan for the Reorganization of Labor Groups. Park took control of the FKTU leadership to "establish a system of unified industrial unionism to overcome organizational disorder and to prevent undisciplined labor disputes" (Guillen, 2001: 141). Park's efforts to control labor through the FKTU backfired, however, and increased labor dissidence. Because the dominant union confederation was a puppet organization, defections to more radical, combative, but illegal unions ultimately culminated in more militant labor organizations, such as the KCTU.

The KCTU is perceived as being militant and progressive, while the FKTU, which for many years was the only official union recognized by the government, is generally more conservative and viewed as being sympathetic to the government. Union rivalries increased in the late 1990s as the FKTU began to compete with the now legally recognized KCTU for membership and loyalties. In interviews conducted for this analysis, both FKTU and KCTU officials made it clear that cooperation is not likely in the near future. Henderson *et al.* (2002: 25–6) draw a similar conclusion:

> [T]he historical and ideological and political differences between the FKTU and KCTU remain and the experiences of economic crisis seem to have done little to alter the situation. While particular issues sometime result in a "common front", for the most part mutual distrust prevents the coherent response to business and government policy that might otherwise have been anticipated.

The fragmented nature of the labor movement is exacerbated by the high percentage of unions representing workers from big companies (chaebols), while the large numbers of non-standard workers tend to avoid unionization. Furthermore, the status differentials between the two groups are deeply rooted in institutional practices and will not disappear easily.[34] Finally, their cohesion is further undermined by not having viable leftist or class-based parties around which to rally (Buchanan and Nicholls, 2003).

One prominent example of this labor rivalry is the long and heated pension debate that persisted throughout the 1990s. The KCTU supported a single-pillar pension plan, which would unite wage-earners and the self-employed in an effort to pool risks and contribute to social integration (Kim, 2006; Yang, 2004). The FKTU, on the other hand, threw its weight behind a plan that would adopt separate management systems and avoid income transfers between the two groups. Such ideological divisions inhibit workers from presenting themselves to the government as a coherent political group. Even in the rare circumstances when labor has been more unified, it has lost. Both labor organizations fought in vain against the reduction of social security and labor benefits.[35]

A similar scenario of union conflict characterizes the health reform debate. The KCTU strongly supported centralization of the 350 medical insurance societies as a means to reduce inequality between the rich and poor. The FKTU, on the opposite side of the issue, preferred decentralization without government regulation (Lee, 2003; Joo, 1999). Its members feared that centralization would result in industrial employers and employees bearing a greater burden than the self-employed, because the latter had premiums that were inadequate to cover their expenses (Lee, 2003). Overall, organized labor played a small part in pushing for a greater government involvement in providing health care, as well as in the introduction and extension of national health insurance (Kwon, 2003).

Taken together, the three intervening domestic institutions (national social policy configurations that privilege political access to select groups, an uncooperative government–labor relationship, and fragmented labor institutions) have helped to fortify a productive welfare regime that continues to direct state welfare efforts towards education and maintains minimum government investment in protective welfare schemes. South Korea's development strategy created interest groups (i.e. chaebols) that supported this type of welfare state, while subordinate groups remained divided and left without the same privileged access to the political process. The government–labor relationship as it evolved in the early decades after independence has made it particularly difficult today to adopt policy compromises between labor and capital. South Korea's fragmented labor movements add to this environment, because they lack the

[34] See also Koo (2001), who makes a similar point.
[35] "Pension Reform Faces Challenges," *Korea Herald* (Seoul), February 17, 2004.

institutional clout to prevent a race to the bottom and to ensure that social policies in the globalizing environment are beneficial for all labor groups.

6.4 Who really gets hurt?

The crowning question is: who has been hurt by the retrenchment reforms since globalization? I demonstrate that it is not the poor, as anticipated by RTB analysts, but the middle class, as argued earlier in this book. To begin, I identify which groups constitute "the disadvantaged," since the international approach to the definition of poverty (e.g. the population living on less than $1 per day) poses problems in the South Korean case: with the rapid income growth since the 1960s, groups living below the international absolute poverty line have been extremely small. Next, I explore the various categories of reforms, and show that it is, in fact, not these groups that are losing benefits alongside globalization, but their more privileged counterparts.

The numbers of absolute poor in South Korea are low in comparison to other developing countries, representing approximately 8.5 percent of the population by official government estimates (Lee and Kim, 2003). This group generally consists of "non-standard workers," who are part-time employees, short-term, or temporary workers, "dispatch employment," and the self-employed (Betcherman, Luinstra, and Ogawa, 2001).[36] Labor groups add to this category workers in informal enterprises (i.e. micro and/or unregistered) who anticipate lasting employment relations but whose working conditions are poor. Certainly, not all non-standard workers are destitute, and far more in South Korea fall into the indigent category, which the government regards as better off than the extremely poor, but whose income still falls below a specified standard.[37] Betcherman, Luinstra, and Ogawa (2001) point out that, when compared to OECD countries, South Korea has a relatively large share of self-employed and those in unpaid family work. Standard workers, or full-time wage-earners, are estimated to comprise only 30 percent of the working population (OECD, 2004).

To determine, then, whether it is the poor or the more privileged who are most affected by social policy reform, it is necessary to look at the effects on the absolute poor, the gains or losses for non-standard workers, and any improvement or worsening in the conditions for standard

[36] Note that it appears that each country has different terms for part-time, contract, and informal-sector workers. India refers to this group as "casual workers."

[37] Non-standard workers may also include lawyers, entrepreneurs, and other self-employed professionals. The data are not available.

workers. Since detailed data on the absolute poor are both limited and difficult to access, however, I focus on changes in protections for non-standard workers. Moreover, in the South Korean case it is reasonable to assume that better conditions for non-standard workers bode well for the destitute, who are a subcomponent of this group.[38]

6.4.1 Labor market protections

The RTB effects in labor market protections involve formal dismantling of the lifetime employment regime and the Labor Standards Act, which provided formal codification of lay-offs. These cutbacks have mostly affected the standard workers, not South Korea's more disadvantaged sectors. They have had a minimal effect on the country's non-standard workers for one simple reason: only management and highly skilled workers ever qualified for permanent employment. In an extensive study of labor market behavior in South Korea, Lindauer (1984) shows that the bulk of employees, production workers, and unskilled operatives did not have lifetime employment protections. Obviously, then, the formal dismantling of the lifetime employment system has the most direct effect on South Korea's more privileged labor groups. By the same logic, since non-standard workers are "subject to pre-negotiated termination dates and can be replaced at the whim of management without prohibitive costs like union interference or severance obligations," the few protections that the LSA provides against lay-offs to permanent workers do not apply to them (Kitt, 2003: 560).[39]

Furthermore, preferences for hiring non-standard workers are increasing as employers avoid compliance with the LSA. To help reduce costs and compete better in the globalizing economy, large firms increasingly subcontract production to small firms (Abe and Kawakame, 1997). This affects the coverage of a very small percentage of workers, since small business owners are reluctant to enroll workers in welfare programs, and the workers themselves in these firms tend not to be covered by collective contracts (Yang, 2006).

[38] Determining the exact percentage of non-standard workers in South Korea is problematic. Scholars, government officials, and labor groups disagree upon the definition, and, as a consequence, produce different estimates of non-standard workers. For example, in August 2005 the Ministry of Labor reported the share of non-standard workers to be 36.6 percent of total wage-earners, while labor groups claimed it to be 57.1 percent (nodong jaryo [Labor Data] 2005). Consequently, references to non-standard workers in the following sections should be interpreted with this caveat in mind.

[39] Kitt (2003) notes that temporary workers with certain longer-term contracts have some protections under the LSA. Also, see Kitt (2003) for a discussion of employers' frustrations with the LSA.

Labor market protections have always excluded non-standard workers, and thus their erosion under the influences of race to the bottom pressures has minimal effect on this group. Instead, it is the more privileged workers who are harmed by the cutbacks. The same trend can be observed in social security, health, and labor market reforms.

6.4.2 Social security (and social assistance)

Since 1988 social insurance has slowly moved towards universal coverage de jure. The implementation of the National Pension Service and unemployment and health insurance have clearly made remarkable advancements towards protecting greater numbers of standard workers (see table 6.1). The percentage of non-standard workers covered in all these sectors is still small, however and, to make matters worse, coverage has decreased in recent years (see table 6.1). The poor amongst the elderly have also failed to benefit from the recent social security reforms (see Kwon, 2001).

Kim (2006: 22) observes that the NPS is experiencing great difficulty in "maintaining the institutional characteristic of an occupationally inclusive system due to increasing coverage gaps." Despite the broadening of statutory rights and access to such programs, the attractiveness of hiring (unprotected) non-standard workers is increasing under the conditions of globalization, as government and employers alike are facing pressures to keep total wage costs down (Kim and Kim, 2003; You and Lee, 2000; Kim, Bae, and Lee 2000). A recent report provides a comprehensive assessment on the state of non-standard workers in South Korea. The authors demonstrate the limitation of the legal approach to expand social

Table 6.1 *Comparison of social insurance coverage: standard versus non-standard workers*

Welfare programs	Employment types	2002	2003	2004	2005
National Pension Service	Total wage-earners	52.7	57.7	59.5	61.4
	Standard workers	62.9	70.8	72.5	75.7
	Non-standard workers	25.7	30.5	37.5	36.6
National Health Insurance	Total wage-earners	55.5	59.5	61.3	61.9
	Standard workers	66.6	72.5	73.8	75.9
	Non-standard workers	28.8	32.6	40.1	37.7
National Unemployment Insurance	Total wage-earners	48.0	49.8	52.1	53.1
	Standard workers	56.2	59.7	61.5	63.8
	Non-standard workers	26.2	29.2	36.1	34.5

Source: Kang (2005: 61).

security coverage for non-standard workers by pointing out pervasive non-compliant behaviors by both employers and low-income employees (Sohn, Koh, and Kang, *et al.*, 2004).[40] The problem is exacerbated by the fact that governments fail to enforce penalties for employers who neglect their legal obligation (Sung, 2006).

The newly implemented unemployment insurance has problems not only because of low benefits and the low duration of pay (OECD, 2000), but the poor are excluded, since temporary workers, the self-employed, and unpaid family workers are not covered. The OECD reports (2000: 83) that over a half of those unemployed do not receive benefits because they were not previously covered by the Employment Insurance Scheme. Table 6.1 confirms that the percentage of non-standard workers covered has declined under this scheme as well. It is no surprise that Lee, Hur, and Kim (2001) and Bidet (2004) conclude that unemployment benefits cannot be considered a primary safety net against unemployment.

Turning to South Korea's poverty alleviation programs, how have recent reforms helped the poor? As discussed earlier, the Livelihood Protection System formed the basis of public assistance from the 1960s until the Temporary Livelihood Protection System and NBLS were introduced in the late 1990s.[41] Figure 6.2 reveals that the number of beneficiaries always was small, however, and shrank even further in the 1990s. This is striking, as the percentage of poor people in South Korea increased by almost 80 percent following the financial crisis (Kakwani, Khandker, and Son, 2003). The OECD (2000) concludes that the number of beneficiaries has declined because of strict eligibility criteria, the low levels of benefits, and administration problems. For example, the income capacity of the entire extended family is taken into account when assessing entitlement to the NBLS. Only 3 percent of the population is covered by the new public assistance program (see Kwon and Holliday, 2007). According to the OECD (2000: 19):

> It is important to stress that many low-income individuals will remain unprotected under NBLS… [B]enefit criteria [are] subject to unusually strict income criteria, based on the income capacity (and not actual income) of the extended family. This particular provision of the law will have to be revised if the official target of providing benefits of last resort to those in need is to be reached. Also, despite the increase, benefits remain very modest. The authorities should consider raising them, perhaps in stages, so that they at least reach the poverty line.

[40] Non-standard workers are intentionally neglecting to enroll to meet immediate living expenses (Sohn, Koh, and Kang, *et al.*, 2004: 298).

[41] The Temporary Livelihood Protection System was similar to the Livelihood Protection System but had a higher property level for eligibility.

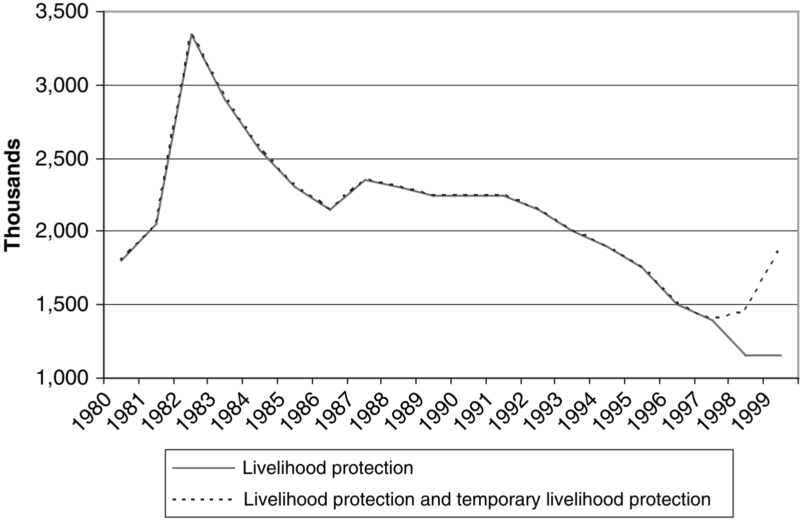

Figure 6.2 Beneficiaries of livelihood protection benefits, 1980–99
Source: OECD (2000).

In addition, Lee and Kim (2003) find that the total income benefits for households with small incomes have decreased compared with the former system. Households with special needs, such as those with a disabled member, are at the greatest disadvantage under the current system.

The retrenchments made in the late 1980s did not directly affect non-standard workers. It is South Korea's standard workers who bear the brunt of the recent cutbacks in social security, while the implementation of unemployment benefits has been of little benefit to subordinate groups.

6.4.3 *Health care*

The expansion of health insurance has actually worsened the situation of the poor, on account of the growing cost. As has been noted in the Indian case as well, however, this trend existed before economic liberalization. The health sector has witnessed two major reforms. The first is the transition from private voluntary health insurance (initiated in 1977) to the 1989 legislation requiring mandatory coverage in an employer-based plan for all workers. In December 1999 the second major reform required all South Korea's 350 health insurance societies to merge into a single insurer in a national health insurance system. The rationale behind both the social security and health insurance reforms was that the pooling of risks would make pensions and health care affordable for all. These are certainly significant developments. The problem is that, while costs have increased, coverage has not been universal in practice.

Both the small numbers of non-standard workers who are now included in the scheme and the majority of those who remain without protections are grappling with the increasing financial pressures. Out-of-pocket expenses have risen alongside the implementation of universal health insurance, for several reasons (Flynn and Chung, 1990; Kim, 2005; Kwon, 2003; Peabody, Lee, and Bickel, 1995). First, in addition to high co-payments, the benefit coverage is extremely low. This is an issue in South Korea, because the cost of health care tends to be exceptionally high and is now rising further.[42] With low benefits, private health insurance is ultimately providing the bulk of coverage for services at unregulated market prices. Kwon and Holliday (2007) argue that the merger of social health insurance societies has not ultimately changed the benefit package previously offered.

Second, government attempts to control skyrocketing expenditures by limiting doctors' fees have had adverse consequences. In an effort to avoid the effects of fee regulation, physicians began increasing the volume of uninsured medical services that were not regulated (OECD, 2004; Peabody, Lee, and Bickel, 1995; Kwon, 2003). Finally, the government still allowed physician charges to increase by 45 percent in 2000, as a means to dampen their overwhelming protests against the mandated separation of drug prescription and dispensation.

In addition to the low coverage of non-standard workers, health insurance protections targeted to the absolute poor are minimal. The Medical Assistance Program, funded by government subsidies to cover the fees of the indigent, reaches only 3 percent of the population (see Jo and Choi, 2002: 7, and OECD, 2004: 63). This is far from sufficient, given that it is estimated that more than 8 percent of the population live below the poverty line.

6.4.4 Education

Finally, unlike India, the recent education reform efforts have also failed to alter the conditions affecting the poor. While the South Korean

[42] Two primary reasons why prices are high are the overuse of advanced medical technology and the promotion of expensive antibiotics and other drugs (Lee, 2003; You and Lee, 2000).

government has consistently made improvements towards greater access to lower education institutions, the poor still face the same constraints to pursuing university education that they did throughout the 1960s and 1970s. Overall, even though recent presidents have recognized the urgent need for reform in this area, education opportunities for the poor have remained unchanged. Changing the quality of educational instruction to meet the demands of a globalizing environment ultimately took greater priority on the policy agenda than promoting more equitable access to higher education.

Government efforts to ensure universal access to primary and secondary education, and to promote equity between schools, have had the unintended effect of creating unequal opportunities for college-level education.[43] The university-level quota system and pressure to perform well on college entrance exams have generated an extremely high demand for out-of-school private tutoring. Given that, as a result of South Korea's government intervention, all students are receiving the same level and type of education, private tuition becomes the only means for individuals to gain a competitive edge. This allows the students who can afford extensive extra-curricular learning to earn higher marks on the entrance examination and gain an advantage in finding employment in competitive jobs. This particular aspect of the South Korean education system has a regressive effect, since the poor are spending a disproportionate share of their income on private tutoring, and the rich still outspend them.[44] Sorenson (1994: 34) reports, "Poor parents resent the advantages of tutoring and other extracurricular help affluent parents are able to provide their children." A 1980 ban on private tutoring has been largely ineffective.

To address this financial pressure on the poor, reform advocates have insisted that the government significantly increase education spending and invest in improving the quality of educational institutions so that demand for private tutoring decreases concomitantly.[45] Other proposed measures included further expanding student quotas, reforming the state entrance exam, and granting greater autonomy to private schools and universities. As discussed earlier, however, reforms in these areas were

[43] The government has ensured equal access to primary and secondary education, and maintained uniform academic standards across schools, by such policies as minimizing differences in tuition rates, randomly assigning students by computer to attend private and public schools, setting the curriculum in both types of institutions, and attempting to limit competition between higher education institutions by putting quotas on the total number of new admissions (Lee, 2002; Kim, 2001).

[44] Note that private tutoring is not limited to the wealthy population in South Korea.

[45] "People's Coalition for Education Reform," *Hankyoreh* (Seoul), May 7, 1995.

relatively minor and did not effect a major change in the government's approach to education.

The objective of decreasing private spending on education has been embraced by the government. It was an important part of former President Kim Young Sam's education reform initiative, launched in 1995. This reform effort, however, was eventually put on the back-burner (Seth, 2002) and took second place to making educational instruction more compatible with the demands of globalization. The Presidential Commission on Education Reform 1995 began its final document with the words: "A nation's economic survival and prosperity would depend on its global competitiveness" (Kim, S.K., 2004: 524). Reforms have since focused on achieving greater effectiveness in local education systems and preparing students for an information-oriented global economy. One example is the Brain Korea 21 program, introduced in 1999.[46] Equity reform advocates have criticized these programs for fostering greater elitism (Seth, 2002).

As a result, private education expenditures (as a percentage of GDP) have steadily increased alongside globalization, almost doubling between 1993 and 2001.[47] Private expenditure on education in South Korea is now among the highest in the world, reaching 3.4 percent of GDP in 2001 (World Bank, 2006).[48] Ultimately, the South Korean government has neither improved the quality of public education nor contained private education expenditures.[49]

Consistent with the past, however, the government has continued to maintain its focus on equality in the lower levels of schooling. For example, in 1985 the government introduced free middle-school education for students living in remote areas, and by 2004 the plan was for completely free education.[50] Although elementary school had been free and compulsory since 1959, compulsory middle-school education had been delayed for decades. Other examples are the extension of low-interest college loans and the 1999 plan to exempt large numbers of students from low-income families from fees (Seth, 2002). President Park Chung Hee's vision has thus been sustained into the present for primary and secondary education, but not for the higher levels.

[46] Brain Korea 21 involved increasing investment in engineering, science, and technical programs at select universities.

[47] See World Bank's EdStats (Education Statistics) database: Thematic Data, table 1.1, Private education expenditures as a percentage of GDP. Available at http://data.worldbank.org/edstats/td7.asp (accessed June 21, 2006).

[48] World Bank's EdStats database: Thematic Data, table 1.1.

[49] "Government Urged to Shift Focus," *Korea Herald* (Seoul), June 8, 2006.

[50] "Education Reforms Needed," *Korea Herald* (Seoul), January 20, 2001.

We must build up society where no privilege in education is tolerated in the education field. Education privilege for the rich and the strong alone should be entirely eliminated. The door of education should be wide open to all talents regardless of wealth, background or family lineage. (Park, 1962: 209)

This outcome is surprising, since the analysis in chapter 3 predicts that pro-poor reforms are most likely to occur in education under conditions of globalization, because of greater information about its benefits and cross-class cooperation towards this end. Why did this not happen in the case of access to upper-level education in South Korea? Information was certainly widespread for the need for education reform in general. As President Kim Young Sam emphasized, "Education reform is the top priority in globalization policy and the type of education needed in the new era is to depart from the existing system."[51] Civil society groups and representatives of labor and business are in complete agreement that the quality of South Korea's current education system is a problem and cannot meet the demands of creating a competitive workforce in the globalizing environment; the prevailing sense is that the need for reform is urgent. An FKI poll shows that companies distrust university education.[52] In recent elections the three major presidential candidates criticized the quality of South Korea's education, and were unanimous in stressing "the importance of creative and talented manpower to better cope with a rapidly changing world at the dawn of the 21st century."[53] Reforms in higher education are currently *the* most important concern of the entire nation (Han, 2003).

Problems have emerged, however, because the need to improve *equity* in South Korea's higher education system lacked cross-class consensus. Only teachers' unions and labor and civil groups demand that the government increase the amount of resources spent on education *and* limit the expansion of private schools in order to promote equity. They argue that the expansion of such elite "self-reliant" schools will impair the central tenet of the South Korean education system: the guarantee of equal opportunities for education.[54] More generous state subsidies, on the other hand, could increase the number of public universities as well as

[51] "President Kim Ordered Education Reform Programs in the First Half of the Year," *Daily Donga* (Seoul), January 17, 1995.

[52] "Firms Want *Education* Market Opening," *Korea Times* (Seoul), August 20, 2004.

[53] "Nominees Pledge Reform of College Admission System," *Korea Times* (Seoul), November 25, 1997.

[54] "Schooling the Brightest," *Yonhap* (Seoul), December 29, 2005. Note that the Korean Teachers and Education Workers' Union supports greater school autonomy; see, for example, the views of its new hard-line leader in the following: "Hard-line Woman Leads Teachers' Union," *Korea Times* (Seoul), April 1, 2006.

hasten the development of innovative and high-quality programs. This would have the effect of improving public university education without having to charge more for tuition. It would also subdue the fierce competition amongst students to enter the relatively few but prestigious public universities, and thus deflate the need for households to spend extra finances on private tutoring costs. The Federation of Korean Industries, however, protests that the government should enhance competition between schools rather than increase government expenditures (Park, J.-C., 1998). Thus, in the absence of cross-class interest convergence, equity-enhancing reform in South Korea's higher education system has not been realized.

6.4.5 Summary

The more privileged standard workers in South Korea are the ones getting hurt by RTB pressures, since non-standard workers never enjoyed many benefits in the first place. In the late 1980s the government made concerted efforts to provide some labor market protections and further develop public assistance programs (NBLS), as well as create a more redistributive social and health insurance system. These attempts at redistribution were more far-reaching than any made by the Indian government under the conditions of globalization. The great majority of non-standard workers in South Korea remain with minimal protections after economic liberalization, however. In education, reforms have granted the poor even greater access to lower education, but they continue to find it difficult to obtain high-quality university education. This pattern has been a long-standing problem in South Korea's education sector.

Only education at the lower levels has provided and continues to provide benefits to South Korea's disadvantaged sectors. Recent reforms in social insurance schemes, however, have had a minimal effect, as the non-standard workers were never really included in them to start with. Rather, the middle-class standard workers are the ones most affected by welfare retrenchment (and expansions) in labor market protections, social security, and health care. This is a common trend in both productive and protective welfare states.

6.5 Other factors: democracy, civil society groups, and Japanese influences

Do other factors help explain why the primary elements of South Korea's productive welfare state persist and why important protective elements (e.g. social insurance policies and labor freedoms in 1988) were also introduced? Here, again, democracy plays an intervening role. First, South Korea's turn to democracy in the late 1980s increased the pressures on the government for greater accountability to a diverse electorate (Wong, 2004).[55] With growing public discontent over the close government–business relationship, recent presidents have sought to distance themselves from the chaebols and create alliances with other civic groups (Nam, 1995). The second major impact of democracy is the expanding influence of major civic groups that have allied with labor in endorsing progressive welfare programs such as the NBLS (see Jung, 2005, and Kwon, 2003). It is not a coincidence that many of these protective reforms were implemented soon after the inception of democracy in 1987. Democracy, however, cannot fully explain why labor benefits increased initially after democratization, but then experienced cutbacks much later, in the late 1990s.

The influence of Japan also plays a large role in the development of South Korea's productive welfare state. Many of the social insurance programs adopted were shaped by Japanese models, particularly in health. Japan appears to maintain similar principles of a productive welfare state, such as generalized attempts to discourage state dependence. White and Goodman's (1998) analysis, however, suggests that South Korea does maintain a distinct national form of welfare, and cautions that "it is misleading to think in terms of one homogeneous, overarching 'East Asian welfare model'" (14).

6.6 Implications

The South Korean case provides important insights into the interplay of globalization and domestic institutions and the effects that this has on social policies. Market expansion brings race to the bottom pressures even in productive welfare states. In the case of South Korea, these effects have been most evident in social security and labor market protections. Nonetheless, this case study once again confirms that retrenchment in these sectors is not a sign that South Korea is advancing towards the neoliberal bottom. Two factors support the contention that the core elements of the country's productive welfare state remain more or less intact: (1) the government still encourages market dependency by actively prioritizing and intervening in (lower) education, and by implementing new protection schemes that are primarily employment-based; and (2) South Korea's disadvantaged sectors continue to receive minimum

[55] Wong (2004) presents an excellent account of the role of democracy in South Korea's welfare reforms.

protections from market adversities. Similarly to the Indian case, welfare cutbacks have been concentrated in South Korea's comparatively new social programs.

What is the future of the productive welfare state in twenty-first-century globalization? The South Korean case makes it clear that, even in light of recent cutbacks, government dedication to the productive welfare state continues; at the same time, attention to more protective welfare schemes has increased since the turn towards open markets. It can be argued, then, that South Korea is experiencing some incremental changes, but along a productivist path. At the same time, though, the evidence thus far suggests that the likelihood that these new changes will be more universalistic de facto is relatively low. Demands for non-standard workers, who come to employers free of onerous costs and protections, are increasing steadily. The mediating role of domestic institutions may be the primary reason why the race to the bottom is not hurting (or helping) the poor, but globalization is certainly making it more difficult for new programs to include them. If the European social democratic states serve as a guide, *both* encompassing labor organizations and government investment in universalistic welfare programs are fundamental prerequisites for paradigmatic change in this era of globalization. South Korea falls short on both counts.

7 Globalization and the dual welfare state: case study of Brazil

Analyzing details from the case of Brazil, this chapter explores the impacts of globalization on weak dual welfare states. Specifically, the Brazilian case responds to the three core questions of this book as they apply to dual welfare states. How and why do globalization and race to the bottom pressures lead to welfare retrenchment in dual welfare states? Do cutbacks mean that dual welfare states are undergoing institutional transformation towards a neoliberal welfare state (i.e. convergence)? In dual welfare states, who really gets hurt by welfare reforms in the current era of globalization?

This type of welfare regime, as discussed in chapter 4, pursues a mixed strategy of protective and productive social policies.[1] On the productive side, Brazil emphasizes (near-)universal primary enrollment; the quality of education is poor and gets worse at the secondary level, however. Brazil's protective schemes are focused on the provision of social security and labor market protections. As with India and South Korea, RTB pressures have resulted in cutbacks in some of its welfare programs. In contrast to the other welfare regime types, however, Brazil's welfare regime appears to be the most dynamic, in that retrenchment has occurred in some of its long-standing welfare programs with the intent of improving equity. In fact, significant changes to *both* the protective and productive components have occurred. While these advancements are promising, several elements of institutional continuity remain: (1) Brazil's recent advancements in education – both in terms of quality and quantity – have still not progressed beyond the primary level; (2) the reforms in Brazil's protective welfare schemes have been parametric and not structural; and (3) the middle class continue to receive the bulk of the benefits while the urban poor, long neglected by Brazil's welfare state,

[1] Based on the logic in chapter 4, I label Brazil a weak, rather than strong, dual welfare state, since the latter implies that governments emphasize both productive and protective welfare strategies to a greater degree than governments of either productive or protective regimes. Outputs in strong dual welfare states would theoretically favor universalistic redistribution programs (both productive and protective).

persist with limited access to these protections. Thus, similarly to India and South Korea, ongoing cutbacks in welfare are really hurting the more privileged sectors of Brazilian society.

Given Brazil's dual welfare status, each section discusses both productive and protective strategies. Section 7.1 discusses the primary features of Brazil's weak dual welfare state. Section 7.2 explores the impact of RTB pressures, while section 7.3 illustrates the extent to which these cutbacks amount to institutional continuity and change. The subsequent section (7.4) asks, "Who really gets hurt?" Section 7.5 explores other factors (particularly democracy), and section 7.6 draws some conclusions about the status of dual welfare states in this era of globalization.

7.1 Brazil's weak dual welfare state

Brazil's "weak dual welfare state" status is a result of the prioritization of decommodification policies alongside concerted government efforts towards creating a productive wage labor force. Like India, Brazil has a history of emphasizing protective welfare strategies to increase the dependence of particular citizens on the state. At the same time, Brazil has invested in commodification policies to a far greater extent than India, creating some degree of overlap with productive welfare regimes such as South Korea. Brazil falls into a distinct welfare category, however, precisely because commodification policies still take "second place" to protective welfare schemes. The stratification effects are unique. Rather more citizens receive social insurance protections; the welfare schemes vary by occupation, however, and preserve old status distinctions and hierarchy. Ultimately, the Brazilian welfare state falls between the two extremes of India's disproportional neglect of productive welfare policies and South Korea's long history of nurturing individual self-reliance and discouraging protective social schemes.

Brazil's social policy emphasis on decommodification coincided with policy-makers' turn away from free trade and the adoption of an import substitution strategy in the 1930s. The Getulio Vargas administrations (1930–45 and 1950–4) set the precedent for using labor policies and social insurance to encourage social peace by establishing the Ministry of Labor in 1930 and passing the Consolidation of Labor Act in 1943.[2] To maintain control of society, the state corporatist structure set up during that time offered decommodification-type benefits in exchange for labor

[2] Note that the 1923 *Lei Eloi Chaves* initiated the first labor laws governing dismissals and pensions for senior employees. It focused primarily on railway workers, however; the expansion of these laws occurred under the Vargas administration.

acquiescence and political passivity.[3] From their inception, benefits were aimed at the favored labor syndicates. The Ministry of Labor under Vargas in 1945 unified benefits into a single social insurance institution, the Instituto de Servicos Sociasis do Brasil (ISSB), although civil servants and the armed services retained separate and far superior pension schemes. While the social protection system emerged in part as a result of labor pressures, Brazil's welfare system was initiated in top-down paternalistic fashion to ensure social control (Malloy, 1979). The result is a system of elite-led social security and labor policies that maintains support from the groups they were originally designed to benefit.

Emphasis on a coordinated education strategy followed close behind, however, as Brazil became more export-oriented. To begin with, Brazil's development strategy was not as "closed" as that of protective welfare states such as India. Concomitant with the focus of protecting domestic firms from international market competition, the textile industry was still expanding its exports in the 1940s, and policies towards transnational firms were far more permissive than in either India or South Korea (Kaufman, 1990; Nayyar, 1978).[4] Ultimately, by the middle of the 1960s, although the development strategy was still primarily inward-oriented, full-fledged export-led growth strategies had also been adopted.[5] During this time, policy-makers began placing an emphasis on "human capital," and major innovations towards universal education were conceived (Haussman and Haar, 1978; Haar, 1977). In contrast, earlier attempts to establish a long-term comprehensive plan – during Brazil's more inward-oriented period – were grossly unsuccessful. As Haussman and Haar (1978: 37) put it, national education laws before the late 1960s were

[3] Schmitter (1974: 85) defines state corporatism as "a system of interest representation in which the constituent units are organized into a limited number of singular, compulsory, noncompetitive, hierarchically ordered and functionally differentiated categories, recognized or licensed (if not created) by the state and granted a deliberate representational monopoly in exchange for observing certain controls on their selection of leaders and articulation of demands and supports."

[4] Nayyar (1978) estimates that, by 1969, the share of transnational manufacturing firms in the export of manufactures in Brazil was 43 percent. In comparison, transnational firms' share of exports was only 5 percent in India, and in South Korea it was 15 percent.

[5] The central government of Brazil began promoting foreign investment and export-oriented growth as early as the late 1940s, and this became a central pillar of the economic policies of both President Juscelino Kubitschek in the late 1950s and Arthur da Costa e Silva in the late 1960s (Armijo and Ness, 2002; Baer, 1989; Alarcon and Mckinley, 1992). Armijo and Ness (2002) observe that, from the late 1960s through the 1970s, Brazil was one of the largest recipients of foreign direct investment and commercial loans among the developing nations. The focus of this case study commences in the late 1980s, since that was the first time that the leadership made significant efforts towards lifting import barriers and capital controls.

"both ambiguous and contradictory, watered down by numerous compromises and excessive revisions."[6]

Since the late 1960s, then, Brazil's welfare state has maintained very generous social protections towards elite members of the workforce and established a public education system that provides universal access to *primary* education. Suboptimal investments in terms of improving education, however, have resulted in poor-quality provision and instructional services. A large number of those eligible do not make use of the system because of its shortcomings, and those that do still lack basic skills. A significant unprotected informal sector still exists, and protective welfare policies maintain status distinctions alongside (slow) advancements in commodification.

7.1.1 Decommodification policies

Brazil's emphasis upon decommodification has its roots in the "revolution of 1930," brought about by Getulio Vargas. From the outset, Vargas's campaign invoked the "social question":

> One cannot negate the existence of a social question in Brazil as one of the problems that will have to be dealt with seriously by public authorities… We need to coordinate activities between the states and the federal government to study and adopt measures to create a national Labor Code… These measures include instruction, education, hygiene, diet, housing, protection of women and children, of invalids and old people, credit, salary relief…and so forth. (from the platform of the Liberal Alliance, 1930, as quoted in Levine, 1997: 146)[7]

Ultimately, Vargas's strategy for dealing with the social question led to a fundamental restructuring of the relationship between state and society that has left its mark on social policies today. Central to this restructuring process was the labor legislation (Consolidacao das Leis do Trabalho [Consolidation of Labor Laws] – CLT) and social security policies. These two welfare schemes set the foundation for excessive state intervention in labor–management relations. Brazilians welcomed the initiatives because they promised better working and living conditions, despite the trade-offs. Succeeding administrations have continued to focus on these two aspects of welfare policy to manage social peace. Housing subsidies and access to public employment have also served as important

[6] The primary debate was between those who supported public schooling versus the proponents of private education (Gadotti, 1997). The 1961 law presented an ambiguous document reconciling these two positions.

[7] Vargas was the presidential candidate for the Liberal Alliance in 1930.

welfare tools to "buy" labor support, but have not been central to Brazil's welfare strategy.

Using the model of Italian corporatism, policy-makers aim to bind workers to the system by providing job security and social insurance benefits in exchange for strict regulations on freedom of association. The strategy is supported by an elaborate body of regulations governing and controlling labor mobilization and overall employment relations (by the CLT). The institutionalization of the Labor Courts by the CLT, as well as the generous provision of benefits and entitlements to protect select groups of workers from "employers' exploitation," were trade-offs with restrictions on trade union freedoms (Amadeo and Camargo, 1993).[8] The goal of this paternalistic effort was to win workers' allegiance and remove them as a source of opposition.[9] With the state supporting, defining, and regulating the form and content of employment relations, the state and different components of civil society established a "forced harmony" (Levine, 1997; Malloy, 1979; French, 1998).

Pensions and job security are, therefore, central to Brazil's welfare system. Social security benefits have long comprised the bulk of welfare expenditures in Brazil. Federal government spending on social security, both as a percentage of GDP and total budget, ranks in the ninetieth percentile for developing countries. Over the last few decades Brazil has spent, on average, 7 percent of its GDP on social security, which is more than three times the average of LDCs.[10] On average, 31 percent of total government spending is allocated to this sector, which is four times the mean of developing countries. In 2002 Brazil spent more on social security as a percentage of GDP than the OECD average (OECD, 2005).

Job security is the second pillar that has roots in the Vargas regime. The CLT's labor code has often been categorized as one of the "world's most advanced [pieces of] labor legislation," given the breadth of matters covered with respect to hiring, firing, and guaranteed job tenure, among other aspects

[8] Labor courts decide any matter in the realm of labor law, and their primary goal is to protect the employee when resolving labor disputes.

[9] The CLT required strikes to be authorized by the Labor Court. Note that the 1964 military government reformed the CLT to reduce labor protections and increase control over collective bargaining, strikes, and wage determination.

[10] This average (1972–97) is based on the IMF's *Government Finance Statistics* data. Note that scholars concur that Brazil's spending data should be interpreted with caution (Lloyd-Sherlock, 1998; da Silva, Estache, and Jarvela, 2004). For various reasons, calculating the precise amount of investment in social sectors in Brazil is problematic. First, with data through 1995, any calculation of real expenditures is challenging, because Brazil has experienced such extreme rates of inflation. Second, it is extremely difficult to get a sense of total spending (at all levels of government), since Brazil has about 5,600 autonomous municipalities and twenty-seven state systems.

(see Levine, 1997). Until 1966 the termination of employee contracts after ten years was forbidden by law, except for "serious fault," and the employer had to bear the burden of proof (French, 1998). After 1966 the Ten-year Protection rule fell into disuse and was replaced by the FGTS (Fundo de Garantia do Tempo de Servico), which provided a severance fund for discharged workers. Since 1988 the penalty for dismissal has increased threefold. It is telling that, unlike in South Korea, economic reasons do not constitute "just cause" for dismissal (Vause and Palhano, 1995).

Firms do not have to seek permission to lay off workers, as is the case in India; Brazilian employers face the additional burden of the Labor Court system, however. Labor Courts tend to have a pro-labor bias and the burden of proof is, essentially, on the employer (Amadeo, Gill, and Neri, 2000). The number of cases received by the Labor Courts is extraordinary: Filho (2005) estimates that, over the last sixty-three years, they have received almost 49.1 million cases, and the complaints have been rising. Labor courts have significant policy-setting power, given that they legislate where labor laws (in the Labor Code or constitution) are ambiguous (Amadeo, Gill, and Neri, 2000). It is no surprise that Brazil maintains some of the highest labor market protections by international standards. Djankov *et al.* (2003) and Heckman and Pages (2003) rank Brazil among the highest in Latin America and the developing world, based on the low degree of flexibility of working conditions and conditions for termination of employment.

Housing, public employment, and means-tested benefits are less central to the Brazilian dual welfare state. Even though housing subsidies were part of the benefit package for organized workers during the Vargas administration, they became one of the expendable policy programs. Brazil's housing policy-making institution, the National Housing Bank, was abolished by the mid-1980s and clearly revealed "the government's lack of determination in facing the housing problem" (Valenca, 1992: 54). In terms of public employment, Brazil has a tradition of granting state employees job security and advancement without merit (Lambert, 1969). In overall terms, however, the percentage employed in the public sector is small (11 percent of the working population), far below the LDC average of 31 percent and India's high average of 70 percent. Consequently, when viewed in a comparative context, jobs in the public sector have not been the predominant means of garnering political support. Finally, although Brazil has made some important advancements in means-tested programs, such as Bolsa Escola,[11] it accounts for only roughly 1 percent of GDP (OECD, 2005), a

[11] Bolsa Escola, implemented in 1997, involves a cash transfer to poor households on the condition that the children are sent to school.

small amount, especially when compared to the social security budget. Nonetheless, it is telling that, relative to the other welfare regime types represented by India and South Korea, the dual welfare state spends relatively more on means-tested programs.

7.1.2 *Commodification policies*

Vargas's commitment to education was articulated in various speeches, the Liberal Alliance platform, and the National Education Plan that was part of the 1934 constitution.[12] The first general education law was proposed in 1948, but did not pass until 1961.[13] Nevertheless, Brazil has experienced an "extraordinary rate of growth in education provision" since the 1950s (Araújo e Oliveira, 2004). By 1965 Birdsall, Bruns, and Sabot (1996) estimate that, in comparison to other countries at its income level, Brazil had very high primary enrollment rates. Radical innovations to Brazil's Basic Education Law in the early 1970s prescribed some type of education training for *all*. The years between 1967, when the government founded MOBRAL (the Brazilian Literacy Movement), and 1971, with the overhauling of basic education, were the so-called years of "economic miracle" and of "educational inertia" (Gadotti, 1997: 127). The central government in Brazil retains responsibility for establishing policy guidance, monitoring, and providing financial support for education.

Brazil spends an average amount (both centrally and locally) on education compared to other developing countries. What is distinct is that a fair portion of this is allocated towards primary education. With approximately 40 percent of its total education expenditures on pre-primary and primary education in 1999–2002, Brazil ranks at par with the LDC average and surpasses India's average of 38 percent.[14] More telling, however, is the fact that Brazil's net primary enrollment rate of 80 percent in 1995 was higher than the global average and just below the average of high-income non-OECD countries.[15]

[12] The National Education Plan called for free and "semi-mandatory" education (Levine, 1997).

[13] The 1961 law formed the Federal Education Council Law and decentralized the education system.

[14] See USAID's Global Education Database, available at http://qesdb.usaid.gov/ged/index.html; accessed July 27, 2007. Note that South Korea's average proportion of education spending allocated towards primary education was 65 percent in the early 1970s, falling to 45 percent by 1995. After universal access to primary education had been achieved, South Korea shifted resources to the expansion of secondary education.

[15] Note that these figures were calculated using the USAID Global Education Database for non-OECD countries where 1990s data were available.

Despite these efforts at improving primary education, however, Brazil's education system suffers from significant shortcomings. First, despite the commitment to primary education, Brazil spends proportionately more per student on tertiary education. Like India, Brazil is notorious for this elitist bias in education and spending resources at the expense of more progressive policies. Second, the *quality* of primary education in Brazil is very poor; and, third, the government lacks a commitment towards improving both the access to and quality of secondary education. Repetition, absenteeism, and high dropout rates are the main problems that plague Brazil's schools. To give an idea of the extent of repetition rates in secondary education, over a half of those enrolled are above the appropriate school age (Araújo e Oliveira, 2004). Dropout rates then become a particular problem once students reach this level. A recent World Bank study estimates that only one out of three students who join the ninth grade will successfully complete higher secondary education (Herran and Rodriguez, 2000). Only 66 percent of students currently in first grade are expected to complete lower secondary education. The consequence of these staggering dropout rates is that a large percentage of Brazilian workers are functionally illiterate, with the average worker having only about five years of education (de Castro, 2000). In 1997 a national assessment test for the system for Evaluation of Basic Education (SAEB) revealed that only 26 percent of students enrolled in (upper) secondary education are achieving at the expected level for their grade (Herran and Rodriguez, 2000). With only 20 percent of its public expenditure devoted to secondary education, Brazil falls fifteen percentage points below the global average and ten percentage points less than the average for LDCs in its income categories.[16] Brazilian scholars regard the current rise in enrollments as the natural consequence of increasing primary enrollment rates.

In terms of health provision, as with South Korea and India, policy-makers have taken minimal responsibility in providing preventative care and have let private industry play the dominant role. The Ministry of Health, established in the 1950s, develops and coordinates national health policy, and has primary responsibility for preventative care. Access to health services until the late 1980s was reserved for those enrolled in the social security program, however. Brazil's public health spending ranks below the LDC average and has decreased in recent years.[17] Barreto de

[16] See USAID's Global Education Database. This refers to 1995 data, or 1996 data if 1995 data were missing. Countries have been included based on data availability.

[17] The LDC average spending on health in 1998 was 1.5 percent of GDP and 6 percent of total government expenditures. Brazil's 1998 total health spending as a percentage of GDP and total government spending was 1.2 and 3 percent, respectively. These estimates are based

Oliveira, Beltrão, and Medici (1994) estimate that health care spending would have to increase by at least 25 percent in order for Brazilians to have a minimal resource base to pay the costs of minimum health care.[18] Health care today is still a neglected issue, which is reflected by indicators in which Brazil lags behind countries in its income group. Infant mortality, for instance, is considerably higher than in Paraguay, Colombia, the Philippines and the Dominican Republic. One-third of the population still lacked basic health care services by the mid-1990s (Nelson, 2004).

To summarize, Brazil's weak dual welfare state, correlated with its mixed development strategy, is associated with an emphasis on social security, labor market protections, and universal access to primary education *in comparison to other developing countries*. Primarily because the quality of its education system is still below par, Brazil ranks below South Korea's productive welfare status. The next section investigates the impact of race to the bottom pressures on Brazil's weak dual welfare state.

7.2 Race to the bottom

Brazil began adopting policies aimed at both trade and capital liberalization in 1988, but the pace of reforms did not accelerate until the Fernando Collor de Melo administration (1990–2). After a period of failed stabilization plans and high inflation during the 1980s, the 1990s has been recognized as "the decade of market-oriented reforms" (Campos and Pinheiro, 2002: 3). The beginnings of this period were marked by the elimination of the majority of non-tariff barriers from the ISI period, a greater than 50 percent reduction in tariff rates, the abolition of special import regimes, a floating exchange rate, and a fairly substantial easing of inward capital controls (Campos and Pinheiro, 2002; Armijo and Ness, 2002).[19]

7.2.1 Social security

In consonance with RTB predictions, social security and labor market protections experienced cutbacks after an initial expansion in the 1980s. Reforms in both these sectors have dominated debates in Congress since globalization reforms began to be implemented. Of these two sectors,

on the IMF's *Government Finance Statistics* data. Data from the Human Development Indicators, United Nations, and the Economic Commission for Latin America and the Caribbean (ECLAC) similarly indicate that Brazil's health spending is below the average.

18 Barreto de Oliveira, Beltrão, and Medici (1994) base this prediction on 1989 data. According to the IMF's *Government Finance Statistics*, however, public spending on health in 1989 and in 1998 is roughly equivalent.

19 Note that tariffs on capital goods are still above those in east Asia (Moreira, 2004).

social security has experienced the greatest pressures for reform. Analysts predict that recent reforms in social security will cause government expenditures in this sector to decline soon. Indeed, globalization pressures were not the only – and perhaps not even the primary – impetus for reform. Two big domestic-level motives for social security reform were to address financial problems created by the expansions stipulated in the 1988 constitution and to correct gross inequities in the social security system. The key point here is that the rising pressures of globalization (e.g. the late 1990s financial crisis and rising private-sector demands) added to this list stronger demands for fiscal discipline, and ultimately became pivotal to the success of long-stalled social security reforms.

As stated earlier, allocations to the social security sector have comprised the lion's share (almost 50 percent) of the total government budget and equal almost the entire budget of education and health taken together. The level of social security spending doubled after the 1988 constitution initiated policies aimed at universalizing social security benefits. The constitution called for a substantial increase in rural workers' benefits, established the minimum wage as the minimum pension level, recalculated pensions to compensate for the value eroded by inflation, and instituted lax eligibility criteria for both private and public workers (Barreto de Oliviera and Beltrão, 2001). After 1988 Brazil also became one of the few countries in the developing world to offer unemployment insurance.

Not surprisingly, as a consequence, Brazil has one of the highest payroll taxes in the world, and, since the 1990s, high levels of public and pension debts (World Bank, 2001a). Indeed, as RTB hypotheses would predict, international market expansion placed additional pressure on Brazil to reduce its social security spending and curb its pension debt. Reforms aimed at cutting back social security expenditures were finally passed in 1998, 1999, and 2003, and are estimated to reduce pensions over the next several decades (World Bank, 2005a).

Passing the first set of reforms in 1998 and 1999 involved a long, protracted political battle. Congress had voted down the reform measures proposed by President Fernando Henrique Cardoso (1995–2002) four times in the previous four years. The recent cutbacks have been aimed at decreasing the cost of social security, although the final outcome was significantly watered down from the original proposal. Reforms included measures to discourage early retirement, an increase in mandated contributions collected from all public servants, a tax on higher-level civil service pensions, a new benefit formula to calculate benefits based on actual lifetime contributions, benefit ceilings, stricter eligibility requirements, and a minimum vesting period of ten years for civil servants to receive pension benefits (World Bank, 2005a, 2001a; Kay, 2001).[20] The changes also paved the way for the easier passage of future reforms by removing from the Constitution much of the detailed provisions regarding the social security system.[21]

The 2003 reforms pushed through by President Luiz Inácio Lula da Silva marked a milestone, because they aimed at reducing the gross inequities between the pensions received by the private sector and the civil servants at the national and sub-national levels (Pension Regime for Government Workers, or RJU). Stricter rules and conditions for pension eligibility, contribution and benefit levels were applied to the RJU. More specifically, the major changes revolved around discouraging early retirement and leveling the public- and private-sector pension systems by implementing such measures as overall wage and benefit caps, a reduction in survivor pensions, a benefit/contribution ceiling equal to that received by private-sector workers (2,400 reals), and a new benefit formula that changed the pension base from the last wage to the average of 80 percent of the highest real wages after 1994 (Medici, 2004; World Bank, 2005a). The most controversial reform required an 11 percent tax on all current pensioners receiving more than 1,058 reals ($360) a month in benefits.[22]

Globalization's influence on social security reform in the 1990s was evident in several ways. First, crises have been positively linked with financial liberalization (Tornell, Westermann, and Martinez, 2004; Radelet and Sachs, 1999). President Cardoso was able to use the urgency of the late 1990s financial crisis to push the 1999 reforms through Congress (Huber, 2005; Souza, 1999). Second, the Brazilian government has been increasingly concerned about the reactions of international investors to the ongoing social security negotiations. Wary of his strong leftist credentials, international investors watched Brazilian President Lula's efforts to push through reforms particularly closely.[23] Markets plunged several times as investors panicked in response to setbacks in

[20] The reforms based benefits on actual levels instead of the last thirty-six months of work. This was significant, given that the previous system encouraged workers retiring early, particularly the self-employed, to declare a higher salary amount just before retirement and declare a lower income prior to the last thirty-six months of their career (Kay, 2001).

[21] Pension reform between 1988 and 1998 was particularly difficult because a three-fifths majority in Congress was required to make changes. Note that the increase in total social security expenditures immediately after the reforms were implemented was primarily due to increases in disability-related pension expenditures, as well as a race to early retirement from a number of Brazil's civil servants, who were goaded by the threat of pension reform (see World Bank, 2005a).

[22] "Editorial Assesses Obstacles to Lula's Social Security Reform," *World News Connection*, April 18, 2003.

[23] "Pensions Cause Investor Caution," *Gazeta Mercantil Invest News* (São Paulo), January 15, 2003.

the reform negotiation process, which were viewed as reflective of Brazil's inability to bring the budget deficit under control.[24] Investors anticipated that successful reforms would reduce interest rates and bring down the deficits. Despite (or perhaps because of) his leftist base of support, President Lula has focused on mollifying investor demands. He spent the first part of his administration courting international investors by pushing through neoliberal reforms and encouraging fiscal constraint.[25] Both during the campaign and after the elections, Lula and leaders of his party, the Partido dos Trabalhadores (PT), promised "ad nauseum" to please markets by implementing a responsible fiscal policy, honoring all debt contracts, and pushing through social security and tax reform.[26]

7.2.2 Labor market protections

As with South Korea, Brazil's labor market reforms occurred in two stages, initially moving in a pro-labor direction, but eventually leading to some retrenchment. With the onset of democracy in 1985, and before market reforms were consolidated, several pro-labor reforms and workers' rights were adopted into labor law. The most significant changes related to the right to strike (including for public-sector workers), the freedom to register unions, and prohibitions on state intervention in union affairs and conflicts (Amadeo and Camargo, 1993). With respect to job security, the employer contribution to the FGTS (the severance fund) was increased from 8 percent to 40 percent, the maximum working week reduced to forty-four hours, and the maximum length of daily work was reduced to eight hours (Amadeo *et al.*, 1995).

Once economic openness policy reforms had been implemented, however, followed by an economic crisis in 1994, President Cardoso began to push for labor flexibility between 1995 and 1999. He began by denouncing Brazil's ratification of ILO convention 158 on the termination of employment, arguing that labor market flexibility was needed (Cook, 2002). Congress also permitted part-time contracts and the temporary suspension of employees for up to six months. The temporary worker contracts were particularly controversial, as labor organizations argued that it would increase dualism between "those who have rights and those

[24] "Market Uneasy on Pension Reform Discussions," *Gazeta Mercantil Invest News* (São Paulo), July 14, 2003, and "Pensions Cause Investor Caution," January 15, 2003.

[25] "Brazil Returns Successfully to Bond Markets," *Financial Times* (London), April 29, 2003.

[26] "Delicate Balancing Act Still Required," *Latin America Regional Report* (London), November 19, 2002.

who do not" in the Brazilian labor market.[27] Brazil's business sector's response was that they wanted "the country's labor laws to be made 'flexible' in order to strengthen international competition and attract international investments."[28] Interestingly, based on interviews conducted for this study, workers and union leaders of Brazil's major labor confederations stated that their greatest concern was not the risk of losing social security benefits, but the pressure that international market competition was putting on them to give up their job protections. As a former deputy, Marcio Moreira Alves explained to a local newspaper, "There is a sort of liturgy imposed by the economic globalization of the developing countries." He continued, "Firstly, the opening of borders to foreign trade and capital, followed by the increase of industrial production, the privatization of state companies and, finally, the reduction of the social cost of jobs."[29]

7.2.3 Health care

In direct contrast to reforms in social security and labor, policies and expenditures related to health and education show minimal signs of RTB effects. Since the adoption of globalization policies, the 1988 constitution includes a declaration of the right to health care for all persons regardless of occupation and income, and the right to education (which could be claimed in court). Policies to fulfill the constitutional mandate in health care took two (albeit related) tracks, both of which defied RTB expectations. First, significant government interventions and institutional changes aimed directly at increasing access to health care were initiated. Second, linked to access, was the establishment of the Unified Health System (SUS), which was a reform aimed at decentralizing health care. Decentralization reforms have shifted some of the financial burden of the central government to states and municipalities. Importantly, both efforts ensure the government's (central or local) rising involvement in the financing, distribution, and provision of health care in Brazil.

Prior to 1988 access to high-quality health care was limited to those enrolled in compulsory health insurance (social security) schemes administered by a federal agency, the Instituto Nacional de Assistencia Medica da Previdencia Social (INAMPS). Those not paying social security

[27] "Temporary Job Contract Demonstration Ends without Incident," *Gazeta Mercantil Invest News* (São Paulo), January 21, 1998.
[28] "Job Security Threatened, Unions Say," *Inter Press Service* (Rome), November 19, 1996.
[29] "Brazil: Labor Deregulation Crosses the Border," *Inter Press Service* (Rome), January 13, 1998.

contributions, such as many in the rural and informal sectors, as well as the (lower-income) self-employed, had to rely on the overburdened and underequipped public health care system. The private sector's role in the provision of health care grew progressively more important, as the INAMPS would contract its services to help care for the insured clientele.

After the constitutional change, access was encouraged by emphasizing the public sector and preventative care, making private-sector services complementary. First, the institutional autonomy of the INAMPS was curtailed by absorbing it into the Health Ministry (Arretche, 2004).[30] Second, government revenues, rather than the social security budget, were responsible for financing health care through social security arrangements (Elias and Cohn, 2003).[31] Finally, a 2001 amendment required the federal government to spend an amount equal to the previous year's budget, while state and municipal governments were required to spend 12 and 15 percent of their budgets, respectively (Elias and Cohn, 2003).

The decentralization of health care has been another goal of the recent reforms. The SUS involves integrating a regionalized and decentralized system of health care, with coordinated management at each level of government (Almeida *et al.*, 2000). As a result of the decentralization measures, state and local provision of primary health care increased, while federal health expenditures decreased. Elias and Cohn (2003) report that, by 1996, although the federal share of health spending witnessed a 53.7 percent drop, municipal financing increased approximately 12 percent per capita. Importantly, the federal government retains significant responsibility over financing and coordination, even though the municipalities are in charge of the management of the health care systems, and even surpassed 15 percent of their budgets in some cases (Arretche, 2004; Almeida *et al.*, 2000).

7.2.4 Education

In addition to health reforms, major reforms aimed at improving Brazil's investment in the education sector have also been adopted since liberalization. To begin with, Brazil's average spending on education as a percentage of GDP before liberalization (5 percent) was higher than the regional Latin America average (3 percent), and even above the average

[30] The Ministry of Health had been responsible for developing and coordinating national health policy, and for public health and preventative medicine. It was financed by government revenues.

[31] From 1996–2001, in order to fund this constitutional change, the Ministry of Health relied on a tax on all financial transactions (Elias and Cohn, 2003).

of the European Union. Since 1988 significant reforms have been accompanied by a marked increase in education expenditures. First, the constitution mandated minimum spending levels at all levels of government. The federal government must spend 18 percent of its resources on education, and the state and local governments are required to spend 25 percent. Second, in the mid-1990s the government instituted a wide-ranging set of reforms aimed at improving the resources for and quality of education, focusing for the most part on the primary level. The federal government took the lead role in national education policy formulation, guaranteeing equity and quality assurance, and ensuring that the specific responsibilities of various levels of government were clearly specified, particularly with the *Lei de Diretrizes e Bases da Educacao Nacional* (LDB), approved in 1996 (World Bank, 2002a).

7.2.5 Summary

In conclusion, pensions and labor market protections appear to be more affected by RTB pressures than health and education sectors. The next area of inquiry is twofold. First, are these current reforms (cutbacks or otherwise) an indication of institutional change? In other words, do the cutbacks in social security suggest that Brazil is moving towards convergence in policies akin to the liberal welfare state? Or is it the case that improvements in commodifying policies (education and health) indicate that Brazil is advancing towards a productive welfare state?

7.3 Institutional change

This section illustrates how the dual welfare state exhibits a greater dynamism than either the productive or protective welfare regimes analyzed in this book. Landmark policy reforms in some of its long-standing institutions (e.g. social security) as well as expansions in select means-tested programs represent important changes to Brazil's status quo. Nevertheless, despite the reforms in social security, labor markets protections, and health and education, social policy changes during globalization still reflect important elements of institutional continuity. Cutbacks are not leading to a liberal welfare state, nor do expansions indicate a significant step towards a productive welfare state or universalism in benefits (a social democratic welfare state).

The first part of this section thus focuses on institutional continuity in Brazil's welfare state, and the ways in which it is manifested. Next, in the second subsection, I explore reasons *why* institutional continuity persists. I demonstrate how and why the impact of globalization on welfare schemes is contingent upon the mediating effects of Brazil's long-standing domestic institutions.

7.3.1 Welfare regime change?

As discussed in previous chapters, I use four main criteria to determine institutional change: (1) significant increases in the reliance on means testing; (2) dramatic reductions in benefit and eligibility rules; (3) major transfers of responsibility to the private sector; and (4) the persistence of institutional legacies. This section looks at these criteria as applied to Brazil's particular experience. The Brazilian welfare state is marked by both institutional continuity and change. The cutbacks (and expansion) of welfare benefits in the globalizing environment do not suggest convergence towards "the bottom," however, or the liberal welfare state.

While Brazil's welfare policies have changed to increase the reliance on means testing, these changes have not been so radical in practice. Brazil's most effective means-testing strategy since globalization policies were adopted is rural pensions (OECD, 2005). These are considered social assistance because of the weak link between contribution and benefits. The new provisions aimed directly at redistribution by expanding coverage and relaxing eligibility requirements for the rural poor as follows: a doubling of all social assistance and rural benefit values; a reduction of five years in age limits for benefits (to sixty for men, fifty-five for women); equalization of the benefit for the entire rural population (men and women receive equal access); and setting values of the minimum social insurance and social assistance benefits equal to the minimum wage.[32]

Other programs that expanded the reliance on means testing include benefits to the elderly and disabled, as well as income support programs, such as Bolsa Familia (BF), implemented in 2003. Bolsa Familia, which builds on President Cardoso's earlier Bolsa Escola program, targets the poor and provides incentives to improve their health and education status, contributing to both the productive and protective elements of Brazil's dual welfare state status.[33] Despite these important advances, means-tested programs still constituted only 0.9 percent of GDP in 2002. This amount is in stark contrast with the 10.7 percent that Brazil spends on pensions. More recently, President Lula's most dramatic

[32] Pension benefits are disbursed to rural workers on the condition that they can indicate a minimum of ten years of rural activities, regardless of whether they have contributed to the system previously (Bonturi, 2002).

[33] Bolsa Escola provides cash (45 reals per month) to poor families that send their children to school.

initiative, the "Zero Hunger" anti-poverty initiative, has been hampered by poor management and disagreements over the distribution of benefits.[34]

The second criterion involves decreases in benefit and eligibility rules. Benefits and eligibility in labor market protections have experienced minimal change. While cuts have been made, such as the changes in means-tested programs, they have not been radical in practice. If anything, benefits have been reduced for the labor force as a whole by default. Existing labor laws apply to formal-sector workers only, excluding the large informal-sector population of the Brazilian economy. As the Brazilian informal labor force expands, then, labor market protections apply overall to an increasingly small percentage of workers.

Benefit and eligibility rules for social security have altered in Brazil since globalization, however. Eligibility and benefits have been reduced for the upper income levels, while expanding at the lower income levels, particularly for the rural poor. Rather than necessarily symbolizing regime change, however, recent reforms reflect the first efforts towards reining in the excesses of the Brazilian dual welfare state. Both benefit and eligibility rules have been excessively generous for certain groups of Brazilian workers, particularly those in the public sector. First, prior to reform, the average retirement age in Brazil was very low. President Cardoso provoked strong reactions when he criticized those who retire under fifty as "layabouts who take advantage of a country of poor and destitute people."[35] Cardoso argued that the average age of retirement was forty-nine, and many retire as early as thirty-four.[36] Second, the benefits of public-sector workers have been touted as "the most generous in the world."[37] The average pension benefit for civil servant retirees was twenty-six times higher than that of their counterparts in the private sector (World Bank, 2001a). Furthermore, it was not uncommon for the pensions of high-ranking government officials to be equivalent to four or five times their salaries.

While the new reforms provide somewhat more stringent eligibility conditions and benefit formulae for these upper-income groups, they represent only a first step (albeit an important one) towards mitigating the excesses of Brazil's social insurance scheme; the stratifying effects remain. No doubt the reforms have a redistributive effect upon the

[34] "Zero Hunger Runs into Problems," *Latinnews Daily* (London), June 9, 2003.
[35] "Social Security Reform Advances," *Latin American Weekly Report* (London), May 19, 1998.
[36] "Brazil Chamber of Deputies Approves Social Security Reforms," Associated Press, February 13, 1998.
[37] "Lula's Great Pension Battle," *The Economist* (US edition), April 5, 2003.

existing beneficiaries of the system, particularly the rural sector, which has received an expansion of benefits since 1988. Social insurance remains predominantly contribution-financed and reserved for formal-sector workers, however (OECD, 2005). Different social security systems continue to coexist, and the constitution maintains generous rules for specific categories of workers (Pinheiro, 2005). Workers in several sectors (e.g. education, health care, and social assistance institutions) continue to enjoy exemptions and lower contribution rates, and civil servants continue to benefit from more generous pension entitlements than their counterparts in the private sector (OECD, 2005). It must be emphasized that pre-reform benefits for public-sector workers were exceptionally high.

The recent developments, then, are radical by Brazilian standards, but not when placed in a comparative context. The major advances are to require workers to work longer for benefits and to bring replacement ratios more in line with the more generous OECD standards. By the same token, although recent reforms boost the retirement age, Brazil still has a long way to go to reach the international average (see Bonturi, 2002).[38] It is for reasons such as these that capital market analysts claim that Brazil's pension reforms have simply not been enough.[39] As Velloso, a public-finance specialist in Brasilia recently lamented, "Under Lula, nothing has changed."[40]

Thus, under the new rules, the upper-income groups that have long been covered by social security are indeed now more vulnerable to the risks and uncertainties of globalization. Nonetheless, benefits for current workers (civil servants, and even new entrants to the public sector) are still extremely high by both Brazilian and international standards. Recent social security reforms can be viewed as an important first step in the very long process towards promoting a more equitable pension system.

The third criterion, that of major transfers of responsibility to the private sector, certainly does not hold. As in South Korea's case, a significant *change* in the responsibilities of the private sector has not occurred since globalization. The recent reforms in social security have been parametric (Kay, 2001; Medici, 2004). It is telling that, like South Korea, Brazil resisted World Bank pressure and opted to maintain

38 Bonturi (2002) reports that the average retirement age in Brazil in 2000 was fifty-six.

39 "Pension Bill Seen Only Resolving Immediate Problems," *Gazeta Mercantil* (São Paulo), April 23, 2003.

40 Raul Velloso, "Bloated, Wasteful, Rigid and Unfair," *The Economist* (US edition), September 2, 2004.

its pay-as-you-go public pension system rather than embracing individual accounts, despite efforts by both the Collor (1990–2) and Cardoso administrations (1995–2002).[41] Instead, as a way to increase the pension value above the ceiling, a complementary pension fund was created for public employees. In 2003 social security minister Ricardo Berzoini was quick to stress that the complementary pension funds for civil servants are not related to the privatization issue.[42]

The private sector played an important role in both education and health decades before globalization policies were adopted. Public policies have long favored private schools in Brazil (Plank, 1996). In contrast to South Korea, the private sector has been a major provider of educational services in lower education levels as well as higher. Until 1964 schools at the secondary level had been predominantly (over 58 percent) private. The long-run trend in Brazil has actually been towards limiting rather than expanding the role of the private sector (Haussman and Haar, 1978; James, King, and Suryadi, 1996), although high-income families continue to maintain a strong demand for high-quality private primary and secondary education (Plank, 1996; James, King, and Suryadi, 1996: 493).

Reforms in health provision ultimately perpetuated the dual system of private and public health care, resulting in an increased role for the former, while the Brazilian government continues its practice of minimum spending on preventative care. The large role for the private sector has its roots in the early 1960s, when access to health care was linked to social security contributions. The INAMPS contracted with the private sector to provide its clientele with health services (Lobato and Burlandy, 2001). In addition, privileged income groups dissatisfied with the public health care system increasingly turned to private insurance, leading to a growing supply (Arretche, 2004). Almeida *et al.* (2000) estimate that private health insurance coverage increased by 73 percent from 1987 to 1996. Despite growing demands by reform advocates to curtail the role of the private sector in health care, the 1988 constitution permitted private institutions to continue to play a complementary role to SUS with limited government regulation.[43] On average, private spending on health is 43 percent greater than public spending (UN, 2004). Total private spending on health, as a

[41] Matijascic and Kay, 2006; "World Bank Will Not Interfere in Brazil's Reform," *Gazeta Mercantil Invest News* (São Paulo), May 27, 2003.

[42] "Pension Reforms Are Not Related to Privatization," *Gazeta Mercantil Invest News* (São Paulo), July 1, 2003.

[43] Article 199 included the private sector in reform as follows: "Private practice of medicine was permitted, and private institutions could play a complementary role in the SUS, with priority going to philanthropic and not-for-profit organizations" (Elias and Cohn, 2003: 45).

percentage of GDP, is roughly equal to that of India, although the ratio of public to private spending is far lower in India.

In terms of the fourth criterion, the persistence of institutional legacies, Brazil continues to pursue the weak dual welfare strategy: commodification efforts still focus on primary education and lag behind Brazil's generous protective (decommodification) welfare schemes. Overall, reforms during the globalizing era have not changed the structure of Brazil's welfare system. To begin with, social security spending still constitutes the largest percentage of general government social spending. Spending on pensions still greatly exceeds spending on health and education combined (see figure 7.1), and the proportions are not expected to change

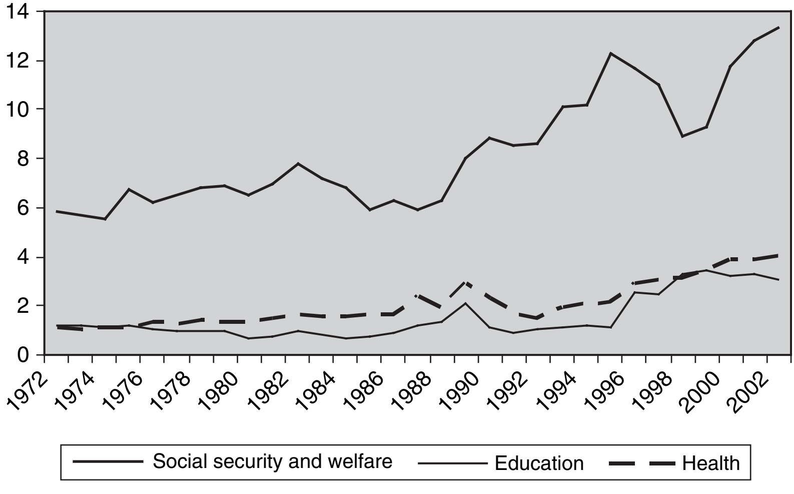

Figure 7.1 Government social spending as a percentage of GDP, 1972–2003

Note: Spending as a percentage of total government expenditures and per capita spending show parallel trends.
Sources: IMF, *Government Finance Statistics* (various years).
Central-level data: Ministerio da Fazenda, "Estatística – Contabilidade Governamental: Despesa da Uniao por Grupo de Natureza," available at www.stn.fazenda.gov.br/estatistica/est_contabil.asp (accessed August 28, 2005).
State-level data: Ministerio da Fazenda, "Estatística – Estados e Municipios: Financas do Brasil – Receita e Despesa dos Municipios" (various years), available at www.stn.fazenda.gov.br/estatistica/est_estados.asp (accessed August 28, 2005).
I would also like to thank George Avelino, David Brown, and Wendy Hunter for access to their ECLAC database, 2001, used in Avelino, Brown, and Hunter (2005).

much in the near future (see also OECD, 2005). Total government education expenditures have hovered around 4 percent of GDP, and even experienced a short-term decline in the early 1990s.

By the same token, labor market reforms on the whole have been relatively minor. Cook (2002: 45) concludes that, despite the erosion of union bargaining power, "while organized labor could not halt many of the changes, it managed to conserve core interests." The most far-reaching policy proposals aimed at expanding labor market flexibility have yet to be implemented. Brazilian businessmen still await a major overhaul of the CLT, which they see as the biggest obstacle towards improving international competitiveness.[44] Proposed changes are modifications to union structure, collective bargaining, union finances, and the power of the Labor Courts. All these reforms, it is hoped, will make it easier for companies to hire workers.[45]

Second, reforms in education have produced important changes on the primary level, but the secondary level still lags behind. Many studies indicate that recently implemented programs, such as the Development of Elementary Schooling and Valuing of Teachers (FUNDEF) and Bolsa Escola, have successfully improved the quality of and access to primary education. Similar programs focusing on secondary education have yet to be implemented, however. One of these, the Basic Education Maintenance and Development Fund (FUNDEB), is still in the negotiation phase. In addition, the president of the National Council of State Secretaries of Education, Gabriel Chalita, recently called the FUNDEB proposal "disrespectful," since the funds per child were so meager.[46]

Not surprisingly, a recent World Bank report (2000a) concludes that Brazil still faces "substantial challenges" in secondary education. The report finds that the continued problem of repetition leads to high rates of dropout, an overwhelmingly urban bias (25.9 percent of primary total enrollments are rural, while lower secondary enrollment in rural areas is only 5.2 percent), and poor instructional quality (World Bank, 2000a). Moreover, public financing continues to be skewed towards tertiary education. While higher education enrollments represent only 2 percent of total enrollment, it captured 22 percent of total expenditures (UN, 2005; World Bank, 2000a).

[44] "Brazilian Businessmen to Influence Construction of Union, Labor and Tax Reforms," *Gazeta Mercantil Invest News* (São Paulo), March 14, 2005.

[45] "Labor Unions," *LatinFinance* (Coral Gables, FL) March 2004.

[46] "Brazil's Finance Minister Announces Release of R$200 Million for Basic Education; Palocci Opens the Coffer for Education," *Gazeta Mercantil* (São Paulo), November 30, 2005. He stated that R$766.90 per child per year was minimal when compared to the R$200 million that the São Paulo state government spends in bonuses for teachers.

In conclusion, while changes have occurred, Brazil's welfare state has shown a great degree of institutional continuity. Although there have been increases in the reliance on means testing and decreases in benefit and eligibility rules, these changes have not been dramatic. Major transfers of responsibility to the private sector have not taken place. Finally, the institutional legacies associated with Brazil's dual welfare state continue to guide the direction and character of reforms under conditions of globalization.

7.3.2 Mediating role of domestic institutions

This section explores how and why long-standing domestic institutions make regime change difficult, even under the pressures of globalization. First, as predicted in the quantitative analyses, social policies instituted alongside early development efforts benefited certain interest groups and provided them privileged access to the political arena. These groups blocked the access of subordinate groups to policy-making and the rights of citizenship. Second, intent on both co-opting and controlling the labor movement, the government–labor relationship that evolved was one based on clientelism. Third, in an environment in which PLP is low and an environment of particularism prevails, it has been difficult for workers to form encompassing institutions that can negotiate on a par with business and government to block welfare reforms; neither can they ensure that reforms benefit the larger group of workers.

Brazil's protective welfare policies were implemented alongside the ISI strategy in the 1930s. The primary beneficiaries were large-scale industrial capitalists, organized labor, civil servants, and governing elites. Despite the fact that social legislative programs were costly, industrialists ultimately accepted them as a carrot-and-stick approach to manipulate the actions of emerging labor groups. In return, they were promised a more cooperative, stable workforce and other economic benefits. As Levine (1997: 11) explains, "Business leaders accepted this formula gratefully, because it assured that the state would play a mediating role between employers and their workers, and it promised to assure protection and a steady supply of capital." Not having to face pressures to compete for export markets, as was required of South Korean firms, public and private Brazilian firms could recoup the high labor costs by raising prices in domestic markets (Birdsall, Bruns, and Sabot, 1996).[47]

[47] As Leff (1968) notes, the Brazilian government operated under an implicit "export surplus" theory of trade. Accordingly, firms had to turn to international markets only after domestic industry had been "adequately" supplied.

Organized labor, civil servants, and governing officials benefited most directly from the social welfare legislation, while the urban poor and rural workers were excluded originally. Civil servants had the advantage of policies designed to protect their job and income security. Organized labor gained from official government recognition of its legitimate status as well as social policies that provided concrete benefits (Malloy, 1979: 55). Finally, by the mid-1940s, responsibility over social welfare and labor activity helped increased federal power, and governing elites began to gain advantage by using these resources as a means of mobilizing public support (Kaufman, 1990; Skidmore, 1967; see also Weyland, 1996a, 1996b). Rural workers were the last to be included, in 1963, when CONTAG (the Confederação Nacional dos Trabalhadores na Agricultura – or National Confederation of Agricultural Workers) came into being, and the rural sector was incorporated into the scope of social security legislation (Beltrão, Pinheiro, and Barreto de Oliveria, 2004).[48] The urban poor did not have a similar organization, however, and were never included in the umbrella of social protections.

Of these groups, civil servants, governing elites, and some organized labor groups have the greatest interest in preserving the status quo. This is because benefits are unequally distributed both within and between occupational categories, reflecting the bargaining power of various groups (Malloy, 1979). The rural sector, for instance, receives meager benefits compared to urban wage-earners (Huber, 1996; Weyland, 1996a). The servants of the state, on the other hand, have traditionally received extremely generous protections (Kay, 2001). Party politicians have also been strong defenders of the status quo, since they rely on their control over the distribution of benefits (and jobs in these sectors) to maintain support (Weyland, 1996b).

These narrow coalitions have lobbied against reforms of Brazil's social welfare scheme initiated in the 1970s, and consequently prevented marginalized groups from securing access to modern social policies and citizenship (see Weyland, 1996b). Civil servants launched fierce protests against the recent social security reforms, succeeding in delaying their implementation during the Cardoso administration and watering down many of the final proposals. Public officials have tried to maintain the extent of their

[48] Consistent with its objective to be in command of emerging groups, the state promoted CONTAG in order to control the rural population (Weyland, 1996a). Beltrão, Pinheiro, and Barreto de Oliveria (2004) note that the first efforts to include the rural sector began in 1955, with the creation of the Rural Social Service. The aim of this agency was to provide social assistance to the rural sector. The Rural Workers' Edict created the Fund for Social Security and Asssitance of Rural Workers (FUNRURAL) in 1963 (Beltrão, Pinheiro, and Barreto de Oliveria 2004).

control over benefits by defending traditional operating procedures. For example, the Ministries of Finance and Planning opposed social security reform proposals, as did many bureaucrats, who specifically resisted the plan to delink social insurance from labor registration and questioned the net benefits of the social security taxes (Weyland, 1996b). Similarly, government agencies such as the INAMPS and the private health sector succeeded in maintaining many of the elements of the existing system (Weyland, 1995; Arretche, 2004). They lobbied against extensive decentralization of the health care system and for maintaining a continued role for the private sector. In the end, decentralization reforms did occur, but the role of the private sector was preserved. President Cardoso encapsulated the political constraints well in his reference to social security reforms:

> [P]ension reform is a thorny issue. It is not easy to say: do it as in such and such country because each country has its peculiarities and there is a problem here which is the transition. Even if we imagined a different system from the current one, it is necessary to see what is going to be done about those who have already contributed, those with expectations of rights, those that organized their lives around such and such pension benefits. (President Cardoso, quoted in Melo, 2004: 334)

Ultimately, then, efforts to cooperate and compromise with these vested interest groups have guided the direction of reforms, resulting in mostly incremental changes to the status quo.

The historical nature of the government–labor relationship in Brazil presents a second reason why institutional change is difficult. The institutional constraints posed by the relationship impede the implementation of more universal benefits. Unlike South Korea, but like India, political leaders opted to incorporate the labor movement during the early ISI period, aiming to mobilize workers as a major political constituency (Collier and Collier, 1991). For example, at a Labor Day 1951 event, President Vargas stated:

> The Labor Day celebration has a symbolic importance both for me and for you: it represents a new coming together of workers and the government. It is with deep emotion that we restore this relationship… I can repeat today from my heart what I said once before: that the workers never disappointed me. They never came to me seeking selfish or private favors. They always spoke in the name of the collectivity to which they belong, for the recognition of their rights, for improvement in their living conditions, for redress of grievances of members of their class, and for the well-being of those sharing these difficulties… I need you, workers of Brazil, my friends, my companion in our long journey, as much as you need me. (President Vargas, quoted in Levine, 1997: 150)

The important distinction with Brazil's form of labor incorporation, in comparison to India, is that the principal goal is to control and prevent the emergence of autonomous labor groups (i.e. depoliticization), thereby keeping society weak and divided to ensure greater state control and power.[49]

Recall that it was fundamental to President Vargas's welfare strategy to reward or win the allegiance of servants of the state and actively employed labor (Levine, 1997; Mesa Lago, 1985). From the onset, the expansion of benefits was exclusionary and tailored according to occupational status. This co-optation strategy introduced the logic of clientelism into the formerly rational legal state structures (Malloy, 1993). In other words, the state corporatist system encouraged the advancement of narrow interest through direct links with the state, instead of class action. Only specific groups could enter into direct negotiations with the ministry to demand protection and bargain for better schemes of social protection (Malloy, 1979: 69). Elites were thus able to guarantee the obedience and support of workers in exchange for particularistic benefits (Weyland, 1996b).

The character of the government–labor relationship in Brazil is also linked to explanations as to why productive welfare policies (education) implemented during the turn towards a more export-oriented strategy did not advance much beyond achieving universal primary enrollment. First, as Schneider (2004) suggests, state intervention on behalf of labor reinforces barriers to lasting business coalitions. Firms are forced to dispute state power individually rather than act collectively to counterbalance labor. Indeed, business associations in Brazil are weak and fragmented (Schneider, 2004; Weyland, 1996a).[50] As Leff (1968) puts it, "The relatively poorly organized business leaders compete and advance incompatible proposals," and their response to education policies was no exception. For instance, the *salario-educacão*, introduced in 1964, was a tax on firms to fund primary education. The fact that such financing was legislated and enforced was certainly a marked distinction from India, which never had clear financing policies on education until the 1990s. Brazil's school finance system fared poorly, however, because it was open to political manipulation and firms would seek special loopholes from the government to avoid the tax (Plank, 1996).

[49] It could be argued that, in contrast to Brazil, a weak and fragmented society was not a *deliberate* consequence of the incorporation approach in India. Candland (1995) argues that the term "party incorporation" best describes India's form of labor mobilization. Each of India's ten large labor unions is affiliated with a different party. Depoliticization of labor, then, has not been a goal in India as it has been in Brazil. At the same time, it is possible that, because of state corporatism, benefits in Brazil are more generous and have wider coverage than is the case in India.

[50] This is certainly not to suggest that state intervention on behalf of workers is the only reason why business is weak in Brazil (see Schneider, 2004).

The turn towards an emphasis upon commodification-type policies thus occurred under conditions very different from those in South Korea. Many of the jobs in education were based on patronage ties. As Birdsall, Bruns, and Sabot (1996: 14) explain:

> The education system, the largest employer in Brazil and a rich source of jobs, has been hampered by the political system: teaching, administrative and maintenance appointments have been treated as political spoils. This clientelistic system perpetuates incontestable patronage, with those outside denied access to power and the benefits of economic growth.

Under such conditions, Brazil's advancements in education more or less stagnated at the primary level. The government–labor relationship overall continues to reinforce the status quo and make it difficult for marginalized groups to be primary beneficiaries of Brazil's distribution regime.

Finally, divisions among labor movements, reinforced by Brazil's government–labor relations, undermine emerging efforts at class solidarity and present an explanation for some successful retrenchment efforts as well as institutional continuity. Fragmented labor is unable to form encompassing institutions capable of negotiating on behalf of workers' wider interests. Consistent with the other cases, they are able neither to present a united front, nor to prevent RTB reforms as workers in some European social democracies do by balancing efficiency and equity concerns. Weyland (1996b: 5) explains:

> To promote rapid industrialization, the Brazilian state imposed in the 1930s and 1940s a segmented state-corporatist system which forced urban workers into a welter of different unions and thus kept them divided and weak. Since the state and business sought to limit labor militancy and since many union leaders had a stake in the established system, crucial features of this fragmented pattern of organization have survived even in new democracy. For instance, several union peak associations compete with each other… Remnants of corporatism and persistent clientelism have greatly intensified problems in organizing collective action. They have impeded the emergence of encompassing associations and social movements through which the poor could press their interest in redistributive reform.

Certainly, labor groups in Brazil have been adamantly opposed to social security reform proposals, and were particularly disappointed by President Lula's determination to implement them. The issue is that Brazil's largest labor confederations have not cooperated on these issues and the character of reforms. With respect to labor flexibility, leftist confederations such as the Central Unica dos Trabalhadores (CUT) and Confederação General dos Trabalhadores (CGT) have remained opposed to the reforms. But the CUT's main conservative rival, Forca Sindical (FS), has supported more flexible contracts and was viewed as more consonant with the changes that the government and employers wanted in labor reform. As Cook (2002: 14) notes, "Forca's actions undermined the CUT's position and curried favor with the Cardoso administration. Indeed, Forca Sindical's allies in Congress were instrumental in backing labor legislation during this period." In interviews conducted for this study, high-ranking officials of the CUT stated clearly that FS cooperation with the government on flexible contracts solidified the rift between the two rival confederations.

Labor groups were similarly divided over the debate on pension reform. The CUT, which represents public-sector workers, advocated maintenance of the existing social security rules for public servants. For example, they submitted proposals for expanding state-managed social security, making eligibility conditions more flexible, and increasing the value of benefits (Pinheiro, 2005). FS, on the other hand, representing mostly private-sector workers, advocated the unification of social welfare schemes for private- and public-sector workers. They mobilized public opinion against public servants by painting them as a privileged few and stated, "It was not fair that only private sector employees pay the price of economic adjustment and face unemployment, wage restraint and other sacrifices" (Cardoso, 2002). Parenthetically, while labor leaders have agreed upon the need for social security reform in general,[51] they have angrily protested the introduction of such measures that make it easier for employers to dismiss workers.[52] Regardless, in both cases the institutional fragmentation of Brazil's labor unions undermined organized labor's ability to present a united front against retrenchment. In the unusual cases where unions were more encompassing, such as CONTAG, the rural workers' union, retrenchment has been averted *and* equity-enhancing reforms have been more successful.

To summarize, Brazil's dual welfare strategy is supported and reinforced by the well-entrenched interest groups formed during the implementation of the country's early industrialization. Organized labor, civil servants, and governing officials were the traditional beneficiaries, and soon afterwards, in large part due to CONTAG, the rural sector gained some access. This distribution pattern has been reinforced by the clientelistic government–labor relationship encouraged by the Vargas administration, and has prevented the implementation of more universalistic welfare benefits. Division within Brazil's labor movement was a deliberate outcome that still exists today, and, as a result, some retrenchment

[51] "Brazilian Labor Unions Reject Government Social Security Reform Proposal," *World News Connection* (Washington, DC), April 16, 2003.
[52] "Job Security Threatened, Unions Say," *Inter Press Service* (Rome), November 19, 1996.

policies have been successful, but not to the extent that they have challenged the fundamental structures of the dual welfare state.

7.4 Who really gets hurt?

At this point, it is clear that civil servants have been the primary beneficiaries of welfare benefits, followed by organized labor in the formal sector, and, lastly, in terms of social security, the rural sector. Labor market protections apply to formal-sector workers only, excluding over 50 percent of the population that belongs to Brazil's informal sector. It is obvious, then, that the most privileged groups, the servants of the state, are the ones the most "hurt" by globalization pressures on social security, while formal-sector workers are vulnerable to the effects of reforms in labor market policies. Recent social security changes, in fact, were designed precisely to curtail the benefits of the most privileged strata and bring them more in line with the rest of those covered by insurance.

Poor rural workers, on the other hand, clearly gained from increases in non-contributory pensions (i.e. social assistance) in the late 1980s.[53] It should be stressed, however, that some social security provisions for this sector date back as far as 1963. The poor *urban* informal workers have been the least affected by the reforms, excluded from both the cutbacks and expansions in line with globalization.[54] The exclusion of the urban informal sector has been the case for decades in Brazil, however, and cannot be regarded as an outcome of globalization. One important exception has been improvements in primary education (the BF program), which is consistent with the findings from chapter 3. This section thus pays particular attention to how welfare reforms accompanying globalization have affected a subset of Brazil's poor, the urban informal-sector workers.

7.4.1 Social security and labor market protections (and social assistance)

While it is not difficult to establish that race to the bottom pressures have affected civil servants by reducing the extent of their privileges and benefits relative to pre-globalization levels, did the reforms directly hurt or help the poor? The Lula government argued that the 2003 reforms would redress broad inequalities and free up money for pro-poor social

[53] Recall that non-contributory pensions are classified as social assistance in Brazil because of the weak link between benefits and contributions.

[54] Unfortunately, no reliable data on the size of the urban informal sector in Brazil are available.

programs. The clearest answer at this point is that the benefits are far from immediate. The World Bank (2005a) estimates that it will take almost fifty years for the first set of social security reforms to halve the pension deficit of the social security system for private workers (RGPS) from 12 to about 6 percent. The 2003 reforms will reduce the projected RGPS pension deficit by approximately one-third in the first fifty years (World Bank, 2005: 13). The long-run deficit of the RJU is to be reduced by an even smaller amount. A recent OECD (2005) report concludes that, despite improvements in social security, the long-term pressures on the budget have not been eliminated. Significantly, however, the rural poor have experienced important gains with the late 1980s reforms. The social security policies that followed were designed cautiously to ensure that the poorest beneficiaries – predominantly the rural poor – were protected from the cutbacks (World Bank, 2005a).

The problem is that, so far, the benefits for the urban informal-sector workers have remained largely unaffected, despite the series of reforms. They have long operated without either social security or labor market protections. Since Brazil maintains one of the largest non-contributory pension schemes in the developing world, it is particularly striking that the principles of rural social security have not been applied to the urban informal sector. According to one report, 54.3 percent of the working-age population does not pay into the social security system, and many of them are still unable to collect a pension.[55] Weyland (1996a, 1996b) also argues that, while social security reform has helped the rural poor, the means-tested element for the urban population is too stringent, and thereby excludes a large percentage of urban informal-sector workers. A recent comparative analysis of non-contributory pensions in Brazil and South Africa finds that the conditions for entitlement are much tougher for the 1993 social security scheme (the Beneficio de Prestacao Continuada) that applies to the Brazilian urban informal sector than it is for the rural sector scheme, the Prevedencia Rural (HelpAge International, 2003). In sum, increasing openness has failed to improve social security protections significantly for the urban working poor. The situation is made worse by the fact that the number of workers in the unprotected informal sector has been increasing (Carneiro and Arbache, 2003; Portes and Hoffman, 2003). Brazil's urban poor have yet to gain (or lose) from the current social security and labor market reforms in this era of globalization.

[55] "Pensions: An Impossible Dream for Most Workers," *Inter Press Service* (Rome), June 23, 2003.

7.4.2 Health care

Health reforms under the conditions of globalization have not hurt the poor, but have not really helped them either. The middle and upper classes have long demanded, and have had access to, superior private health care, and this has not changed since the reforms. The poor, on the other hand, continue to receive low-quality health services. This is a trend that began in the late 1960s, however, with the rapid development of the private sector, which was the focus at that time. Health care reforms under globalization have served only to continue this trend.

The fight against Brazil's unequal health care system began in the mid-1970s. Brazil's military regime (1964–85) installed a model that emphasized curative care and provided sophisticated, high-quality health services accessible only to the middle and upper classes. Reformers belonging to the "sanitary movement" (Movimento Sanitarista), formed in the 1970s by medical professionals, local health authorities, and experts from academia and research institutes, argued that the root of the problem was the rapid development of the social-insurance-based system of health care, which favored the private health care providers. With the population's growing reliance on the private sector, the publicly provided systems became outmoded, and had low standards, long queues and inefficient facilities (see Baer, 2001). As a result, the middle and upper classes preferred to buy into private health care. The reform movement thus demanded changes that would serve the needs of the urban and rural poor by strengthening the public sector and shifting the emphasis to primary and preventative health care, such as vaccinations and sanitation (Weyland, 1996a; Arretche, 2004).

Yet, as Weyland's (1996a) thorough analysis of Brazil's health reform movements indicate, efforts in the 1970s met with limited success. Policy changes to improve efficiency and coverage were limited to some administrative reforms that put one institution in charge of both rural and urban health care.[56] Consequently, Weyland (1995) argues that the relationship between the public and private health sectors remained intact and continued to sustain Brazil's inequitable dual health care system.[57]

The 1988 constitution thus represented a landmark opportunity for the Sanitarista movement to push forward their proposals for improved equity

[56] FUNRURAL was abolished as an independent agency, the National Institute of Social Insurance (INPS), was placed in charge of health insurance, and INAMPS was put in charge of administering health care (Weyland, 1996a, 1995).

[57] The most successful redistributive reform was the Programa de Interiorizacao das Acoes de Saude e Saneamento (PIASS), which brought sanitary and basic medical facilities to rural poor in the northeast.

and efficiency in Brazil's health system. The constitution declared free and universal entitlement to all levels of health care, increased spending at all levels of government, and encouraged the formation of participatory councils. The Sanitaristas also supported decentralization, since Brazil's centralized, social-insurance-based system of health care was perceived to favor private, large, and well-organized health care providers and perpetuate the dual system (Arretche, 2004).

An overwhelming number of studies reveal that the recent reforms, however, have been unsuccessful in either changing the inegalitarian nature of health provision or improving access to health services (see, for example, Medici, 2003, Alves and Timmins, 2001, Almeida *et al.*, 2000, and Elias and Cohn, 2003). The primary problem was that, ultimately, the constitution ensured institutional continuity; private institutions continue to play a complementary role to the Unified Health System, subject to limited regulation. This perpetuated the dual system, for two important reasons. First, the upper and middle classes, previously covered by INAMPS, remained unsatisfied with the quality of public health care provided by the SUS, and increasingly sought private health care plans (Collins, Araujo, and Barbosa, 2000).[58] This effectively continued the mandate of granting the poor low-quality public health care facilities (Almeida *et al.*, 2000; Carneir and Arbache, 2003). Elias and Cohn (2003: 46) conclude, "Both the provision of and access to health services operate according to a logic of private practice and market principles, to the detriment of a logic that aims to fulfill the needs of the population."

The second reason that health reforms have had a limited impact on equity involves problems related to decentralization (see Arretche, 2004). Decentralization has favored the well-off areas that have greater revenue-generating capacity, predominantly located in the southeast (Collins, Araujo, and Barbosa, 2000). Local government was given greater responsibility, but did not have the resources or capabilities to target the poor (Alves and Timmins, 2001). In the first four years, for example, much of the construction boom for public clinics was incomplete due to insufficient funds (Baer, 2001). Finally, the constitution was vague about the exact responsibility of each level of government (Baer,

[58] Article 198 helped maintain the dual system by establishing a Unified Health System and a Complementary Medical Care System (SPAM). While the SUS provides health services primarily to the higher-risk population of poor, the SPAM is similar to its social security predecessor (INAMPS) and provides health services to a limited segment of the population (Elias and Cohn, 2003).

2001). There was no guarantee that the local system would provide health care based on equity.[59]

Why didn't globalization increase the incentives for successful health care reform? As predicted in chapter 3, the health sector faced much lobbying and clientelism, which ultimately prevented reform. And, as was discussed earlier, bureaucrats and the private sector had a particular interest in maintaining the status quo. Weyland concludes that these vested interests ultimately "made a drastic reorientation of Brazil's health care system impossible. Conservative forces celebrated their victory, while the health reform movement lamented its defeat" (Weyland, 1995: 1708).

7.4.3 Education

In contrast, the incremental expansion of primary education has been directly beneficial to the poor. Reforms in this sector have been implemented relatively successfully over the last two decades. Two of the programs mentioned earlier were groundbreaking: the Development of Elementary Schooling and Valuing of Teachers and Bolsa Escola, which evolved into Bolsa Familia. To promote equity directly, FUNDEF contained special measures to address within-state spending inequalities (i.e. revenues were distributed to states and municipalities based on enrollments). It also guaranteed a minimum per-pupil expenditure in primary schools, and built in incentives for teachers (increased wages) (Gordon and Vegas, 2005).[60] Studies have since documented the positive effects on enrollment, especially in poor regions, and positive trends in repetition and dropout rates (World Bank, 2002a; de Mello and Hoppe, 2005). Bolsa Escola, which provided low-income families with children with a small stipend, also had an effect on reducing poverty for the families that it reached (Lavinas *et al.*, 2000). While there is still much room for improvement in terms of targeting and policy design (Schwartzman, 2005; Rawlings and Rubio, 2005), most scholars and international organizations view Bolsa Escola as an important step towards improvement in

[59] This is not to suggest that there were no successes for the reform movement. For example, Elias and Cohn (2003) point out that, even though universality is far from being achieved, decentralization has improved the capability of basic health care programs, such as the Family Health Program. Almeida *et al.* (2000) point out that the basic health services network has undergone a marked expansion since the early 1980s. What is significant for this analysis, however, is that the salient features of the pre-reform health system (e.g. dualism between public and private health care), which prevent access for the majority of the poor, remain, despite increased spending.

[60] Importantly, FUNDEF resources could not be used to pay pensions (World Bank, 2002a).

education for the poor (Araujo and do Nascimento, 2001; Criança, 2001; Aguiar and Araujo, 2002).

Did globalization play a role in increasing the incentives for equity-enhancing education reform, as predicted in chapter 3? Indeed, a significant amount of information on the benefits of education in a globalizing environment has become available. Kaufman and Nelson (2004: 252–3) discuss how “conclaves, conferences, and studies” led to increasing prioritization of education throughout Latin America. Not surprisingly, then, the Latinobarometro public survey recently revealed that the broader public has recognized the importance of education in the current environment (Kaufman and Nelson, 2004). Contrary to the general pattern of increasing cross-class interest convergence on education reform, however, there is little evidence that support for education reforms came from the business sector (Tendler, 2002).[61] Rather, education reforms were more of a top-down initiative from technocrats and bureaucrats in Brazil. How, then, were administrators able to overcome the institutional constraints of clientelism to make reform such as FUNDEF and Bolsa Escola possible? It is worth emphasizing that business did not resist the reforms, as was the case in South Korea, where business actively protested proposals to increase the *level* of education spending.

7.4.4 Summary

In conclusion, who has been most affected by globalization-driven reforms in Brazil? The poorest segments of the population – the informal workers, the unemployed, and the underemployed – have historically been excluded from any sort of welfare protections, and thus rollbacks of those protections can have little effect on these groups. It is, in fact, the more privileged groups, the formal-sector workers and the servants of the state, who have been the most hurt by RTB pressures to reform social security and labor market policies. In the case of education, on the other hand, globalization has provided incentives for some expansion, which has had a directly beneficial effect on the poor.

7.5 Other factors: democracy and partisanship

The end of military rule in 1985 clearly played a role in explaining recent welfare reforms, particularly in social insurance schemes, labor market protections, and education. Unlike the case of South Korea, however,

[61] As Kaufman and Nelson (2004: 503) point out, however, recent business support for public education campaigns suggests that their interest may be growing.

scholars are more cautious about the effects of democracy on these reforms. While some have observed a correlation between democracy and redistribution of resources, such as in education (Brown, 2002), several others have emphasized the complex relationship between democracy and equity-enhancing reform in Brazil (Grindle, 2000; Kaufman and Nelson, 2004; Weyland, 1996b). Certainly, progressive reforms to labor market protections, health, and social security were passed in the drafting of the 1988 constitution. Scholars have surmised that the interplay between reform-minded bureaucrats and democratization brought many of these issues to the agenda (see Weyland, 1996a, and Grindle, 2000). Significant education reforms did not take effect until more than a decade later (see Draibe, 2004), though, and the race to the bottom effects discussed earlier also took place more than a decade after democracy was introduced. One possibility perhaps worth investigating in future research is that it is not democracy per se that mediates the effects of globalization on welfare policies, but "new democracy."

Perhaps other factors must be observed, in addition to the broad category of democracy. Remmer's (2002) intriguing analysis, for instance, suggests that, contrary to conventional expectations, leftist partisanship might be a factor in implementing conservative fiscal policies. The implementation of the 2003 reforms in social security by a leftist president, Lula, was indeed impressive, particularly since his more conservative predecessors had not been so successful. Lula was also responsible for "Fome Zero" (Zero Hunger) and greater Bolsa Escola/Bolsa Familia initiatives.

7.6 Implications

As in the other cases, market integration brings some RTB-type reforms in dual welfare states. Contrary to the examples of the protective and productive welfare states represented by India and South Korea, respectively, however, Brazil's dual welfare state is somewhat more dynamic; a significant portion of the welfare cutbacks in Brazil occurred in some of its most well-entrenched programs, such as social security. Thus, in comparison, the dual welfare state appears to maintain rather greater promise for path-breaking reforms in the current era of globalization. Notable changes in both productive and protective welfare sectors have indeed occurred. Some advancements in means-tested programs have occurred concomitant with the advent of globalization, and Lula has managed to introduce equity-enhancing reforms in the historically regressive social security system, as well as important reforms in primary education, since economic liberalization.

Nonetheless, important elements of institutional continuity remain, in terms of the failure to improve higher education and the continued prioritization of protective welfare schemes that have significant stratifying effects. Thus, the primary issues of concern are the following: (1) commodification schemes still need considerable improvement; and (2) domestic institutions in Brazil still do not provide the urban informal sector with adequate social security, health, and labor market protections.

8 Conclusions

> The governments of the South…are in any case deprived of the resources required for the financing of social policies or for redistribution. They are in effect victims of…the *unbridled race to reduce taxation and social expenditures*. [B]y constraining the governments of the South to respond to the market and the international financial institutions rather than to the aspirations of the peoples, the present globalization…has built a world where persons and people are put to the service of economic growth, productivity and financial profitability.
>
> (Global Call to Action against Poverty [GCAP], March 2005, emphasis added)[1]

> Globalization wrecks…communities, impoverishes our people and fosters exclusion and individualism.
>
> (Donald Kasongi of Tanzania World Social Forum, 2004, Agency for Co-operation and Research in Development [ACORD])

Along with optimism for progress, the ascendance of global capitalism has given rise to fears of decreased welfare protections and benefits, as well as a loss of sovereign power for individual nations. Academics, journalists, policy-makers, and activists around the world caution that globalization will inevitably lead to a race to the bottom. According to the RTB hypothesis, in a world unhindered by restrictions on trade and capital flows, investors will pursue the highest rate of return, wherever that may be found. Nations that go counter to the market by protecting their citizens from the worst of its effects could lose out in the competition for global business and funds. Safety nets, environmental standards, and acceptable labor costs and protections could all raise production costs or risk lower profit margins. Governments therefore cannot initiate, or even maintain, policies that promote a higher quality of life for their people. Domestic politics becomes irrelevant in the face of global commerce.

The high demand for capital in developing countries increases concerns that citizens of these nations are at particular risk in the face of global

[1] The GCAP is a worldwide alliance of almost 1,000 non-profit organizations, activists, and non-governmental organizations.

market pressures. Even though a considerable number of scholars ultimately reject the RTB hypothesis, based on data from the developed world, which shows significant *divergence* in the ways that these nations provide for various levels of social welfare alongside market expansion (Esping-Anderson, 1990; Hall and Soskice, 2001; Huber and Stephens, 2001; Kitschelt *et al.*, 1999; Iversen, 2005; Garrett, 1998), this book shows that there is some validity to these fears for the less developed nations.

In this study, I have challenged prevailing conceptions about the impacts of globalization on citizens of developing countries. It is the poor who have been widely perceived as the victims of the "unbridled race to reduce taxation and social expenditures." Fundamentally, the race to the bottom debate in LDCs has been set up as a zero-sum game between states and markets. Reality is much more complex. While globalization does indeed lead to a race to the bottom in developing economies, institutions are *not* undergoing radical transformation and it is *not* the poor who are worse off. In fact, it is the more privileged lower to upper middle classes who take the brunt of the direct effects of the race to the bottom.

It is, therefore, the middle class and not the poor who are directly impacted by welfare reforms, and the reason can be found in distinct and persistent institutional arrangements. Essentially, LDC welfare states have long been geared towards the middle and upper classes, and, in fact, were never originally designed to protect the poor. Globalization *by itself* does not determine policies that help (or hurt) the poor in the developing world; it is domestic institutions that structure responses to the challenges of economic openness. As the current consumers of welfare state services fight to defend the status quo, distinct institutional configurations generate systematically different reactions. The end result is that developing countries experience cutbacks in some areas of welfare, while retaining continued protection in others. Defying zero-sum predictions, the race to the bottom does not signify the end of domestic politics, and national differences are far from extinct. Current LDC welfare policies therefore reflect *both* external market pressures *and* domestic institutional arrangements. As a consequence of this interaction, in the final analysis, globalization is not leading to institutional convergence at the "neoliberal bottom," and the effects of any RTB cuts in welfare policies are primarily impacting the middle classes and largely bypassing the poor.

8.1 The case studies in perspective: globalization, domestic institutions, and social policies

This book demonstrates three important findings. First, the race to the bottom has important effects on social policies in developing countries.

The clearest impact has been to pressure governments to cut back on social programs that can directly affect the bottom line of firms. This has largely been a result of trade, and not capital liberalization. Chapter 2 and the case study illustrations indicate that social security and labor market protections are the programs most susceptible to change. Race to the bottom pressures result in some degree of retrenchment in these two categories in all three welfare regimes (productive, protective, and dual). The Indian case study, however, suggests a differential impact from RTB pressures in other welfare states. Rather than official policy changes, the retrenchment of labor market protections occurs "by stealth" (or de facto). Additionally, expenditures on health and education may also experience cutbacks. This is not surprising, since protective welfare states tend to place less priority on commodification-type policies. The case studies thus present the added insight that cutbacks in human-capital-type programs in response to globalization pressures are more likely in protective welfare states, where they are not as well supported by entrenched interest groups.

The reason why RTB pressures have affected social policies in developing countries is the relatively decentralized condition of their labor movements. The experiences of the OECD countries have shown us that the effects of globalization on the welfare state are either absent or positive when labor movements are encompassing. In this scenario, labor groups coordinate policies with government and capital representatives (e.g. wage restraint in accordance with productivity, labor peace) so that they can enjoy the benefits of generous social policies without compromising efficiency. By contrast, since labor movements tend towards disunity in LDCs, policies are not coordinated, and welfare schemes yield adverse political and economic consequences. Narrow groups of workers from the formal sector fight to maintain their comparatively generous labor protections and benefits, pushing up labor costs and effectively feeding the demand for non-standard and informal-sector workers. This creates a classic insider–outsider problem that also serves to cement labor's political differences. Labor demands thus remain unfulfilled, as governments face mounting pressure for fiscal discipline. To avoid punishment from mobile asset-holders, and to help promote export markets, the government implements welfare reform. These cutbacks are generally not colossal and yet still, as in the example of President Lula's 2003 reforms in Brazil, they can serve to mollify investors. Clearly, even if isolated groups of workers are important government allies, their collective weakness (i.e. low PLP) eventually translates into some degree of welfare retrenchment.

The second major finding exposes the big paradox: the race to the bottom is not impacting the poor. Chapter 3 reveals that the nature of the (historical) government–labor relationship gives rise to institutional constraints that prevent the implementation of pro-poor social policies. Often used as vehicles of clientelism, political elites distribute social benefits to co-opt the more powerful labor groups. Thus, social benefits are used on a discretionary basis in exchange for political favors and labor quiescence. These findings suggest that, in addition to the problem of low PLP discussed in chapter 2, the government–labor relationship is also a factor reinforcing the insider–outsider problem. Both the Indian and Brazilian case studies illustrate these trends.

The South Korean case study, however, suggests an alternative to this type of government–labor relationship. Rather than using welfare benefits to pacify labor groups and foster clientelistic relations, the government–labor relationship may evolve solely on the basis of harassment and repression, thus limiting the extent of labor-friendly benefits.[2] This form of government–labor arrangement also results in weaker institutional support for welfare policies that protect the poor. Whether the nature of this government–labor relationship is subject to generalization across all productive welfare regimes is a future research topic worthy of investigation.

Chapter 4 delves deeper into the race to the bottom paradox and reveals that, in fact, none of the distribution regimes in developing countries were originally designed to protect the poor in the first place. Productive welfare states, such as South Korea, emphasize market reliance and promote commodification policies, focusing on education. Given that this regime type supports policies that discourage citizens' dependence on the state, programs designed to protect the poor are discouraged.

Protective welfare states, such as India, attempt to minimize citizen dependence on the market and prioritize decommodification-type policies. One might logically predict that regime types with these ideological foundations would prioritize policies that protect the poor. The Indian government has certainly sustained strong rhetoric in support of a pro-poor welfare regime, particularly after independence. Because decommodification-type policies were pursued before successful commodification took place (i.e. the majority of workers are dependent upon wage labor), however, only welfare protections for a very small, relatively privileged subset of the larger workforce, such as civil servants, the military, and organized labor, have found political and institutional backing.

[2] The government–labor relationship in Brazil involved harassment and repression as well (see Collier and Collier, 1991), but, at the same time, labor was "bought off" with a somewhat broader range of welfare protections.

The third regime type, the weak dual welfare state, which is a blend of both regime types, also tends to neglect the poor. Nevertheless, it is very interesting that the dual welfare state investigated in this analysis, Brazil, revealed greater pro-poor protective benefits when analyzed alongside India and South Korea. Important examples are Brazil's social insurance program, which includes the rural population, and the rather greater resources devoted to improving education for the poor, such as Bolsa Escola.

The one situation in which the poor were directly affected by race to the bottom pressures had positive redistributive consequences: improvements in primary education. In the cases in which either access to or the quality of primary education was pitiful, pro-poor redistributive policies have been adopted. Chapter 3 establishes that globalization provides incentives for overcoming institutional constraints to equity-enhancing reforms in education through the spread of information and cross-class interest convergence. These predictions hold true in India's protective welfare case, and mostly true in Brazil's dual welfare state. The difference is that, in Brazil's dual welfare state, business did not actively support redistributive reform in primary education. Nonetheless, it was equally critical that business did not actively lobby against reform, as was the case in South Korea's productive welfare state.

The South Korean case thus suggests that the politics of education reform under globalizing conditions is quite different in productive welfare states. The goal of business interests in this scenario is to improve the quality of education rather than to promote redistribution; both access to and the quality of lower levels of education in South Korea are, and have been, quite high by international standards. For example, South Korea's business associations did not support policy proposals that would help decrease the demand for private tutoring and thereby improve the access of lower income groups to tertiary-level education. In essence, the goal of current education reform seems to be one of ensuring access to a prescribed minimum level of education as a means to satisfy business needs for an educated labor force rather than from any inherent interest in promoting educational equality.

The third major finding is that RTB pressures do not lead to institutional convergence. In fact, none of the regime types reflected advances towards the neoliberal bottom; institutional diversity prevails in the developing world. Chapter 4 first supports this discovery using cluster analysis to verify that three distinct clusters of LDC welfare states persist well into twenty-first-century globalization. The nature of these welfare regimes is linked to the different ways in which their governments chose to respond to the earlier challenges of growth in the global economy – aiming either to expose domestic industries to or to protect them from international markets. Developing countries implemented welfare policies compatible with their particular development strategies, making welfare states endogenous to initial development models. Those who benefited from these programs became part of the dominant coalition and developed a vested interest in upholding some degree of institutional continuity.[3]

This book does not suggest, however, that the fate of LDC distribution regimes is one of overdetermined path dependence. The case illustrations reveal that globalization has indeed resulted in some movement away from both the productive and protective baselines, although the primary structural features of all three regime types remain intact. By adopting some education reforms, the Indian case suggests that protective welfare states are making incremental changes in the productive direction. In interesting contrast, South Korea's adoption of universal health and social insurance schemes shows that the productive welfare states appear to have adopted more protective welfare schemes.[4] The dual welfare state reveals some advancement on both fronts. Brazil has adopted important education reforms and made significant efforts towards improving the redistributive impact of the existing social insurance schemes.

Nonetheless, important elements of institutional continuity remain in all three regimes. In India, the core protective welfare schemes remain intact, as evidenced by the safeguarding of desirable public-sector jobs in its overstaffed bureaucracy. The government in South Korea maintains education as its top budgetary priority, and the state's extensive regulatory role in the education sector continues unabated. Brazil has experienced the greatest amount of change, with significant reforms to its social security program. With a disproportionate amount of state resources still budgeted to the social security sector, however, and lackluster improvements to secondary education, Brazil maintains its status as a weak dual welfare state.

Finally, all the welfare regimes reveal institutional continuity in terms of weak safety nets for the disadvantaged. Groups in India, South Korea, and

[3] In the case studies, I point out that the government–labor relationship may also be influenced by the early development strategy. In protective welfare states, for instance, the government is more likely to incorporate labor into the dominant coalition, because its closed development strategy created the political and economic space to do so.

[4] This is not to suggest that South Korea is advancing towards a protective welfare state. Recall from chapter 4 that productive welfare regimes, if successful, cannot become protective, since the latter uphold decommodification policies *before* the workforce has become dependent upon wage labor. Since South Korea is at or past the stage of commodification, the direction of welfare change is an open question. Advancement towards the liberal welfare state is unlikely, given the highly interventionist role of the state and the still weak means-tested programs. A social democratic welfare state is also unlikely in the country, since labor movements are not encompassing and protective welfare programs are still primarily employment-based.

Brazil that were left without protections in the earlier stages of development remain with limited protections today. These are primarily the groups that comprise casual labor in India, non-standard workers in South Korea, and the urban informal sector in Brazil. Globalization has not changed matters in this regard.

8.2 Questioning prevailing assumptions and future research

The analysis in this book both draws upon and contributes to various debates in the social sciences related to globalization, domestic politics, welfare, and poverty. It represents a concerted effort to bring the great majority of the countries in the world into the study of welfare states, a research tradition long focused upon the experiences of a small number of advanced industrialized nations. In the process, by observing the unique experience of developing country welfare regimes and how they have been coping with the pressures of globalization, the limitations of conventional views have been exposed. This book has only just begun to unveil the complex relationships surrounding globalization, domestic institutions, and social policy in developing nations, however. A rich research agenda lies ahead for those interested in exploring and advocating social protections for the poor in twenty-first-century globalization.

8.2.1 Rethinking the trade-off between states and markets in developing economies

Many of the recent debates have centered on whether international markets or the state are the key drivers of policy under the conditions of globalization. The real concern is whether globalization has eroded the authority of the state to maintain and promote policies that respond to local needs and interests. Any welfare-policy-related changes that appear to please foreign investors have led scholars and activists alike to conclude that the balance of power between capital and labor has shifted and that state control over domestic policies has been compromised.

This book challenges this zero-sum dichotomy, however. The analysis in this book reveals that developing nations are clearly more sensitive to international economic pressures than the OECD countries. Some policy outcomes from international market pressures are indeed deterministic, in the sense that divided labor movements in LDCs cannot successfully negotiate win-win outcomes for capital and labor as globalization advances. At the same time, political reactions are indeterminate, because globalization pressures are also mediated by other types of domestic institutions, such as the type of distribution regime. Regimes represent an "interdependent web of an institutional matrix" that induces complementary organization forms and institutions that tend to be self-sustaining (see North, 1990: 95, and Hall and Soskice, 2001).[5] As a result, different distribution regimes guide the direction of policy in different ways as markets expand. Thus, while globalization does indeed impact domestic policies, local needs and politics do still matter.

A third complicating factor challenging the simple states-versus-markets view of developing countries is that domestic institutions can also change under the pressures of international market expansion. For example, we have seen that the institutional constraints posed by the government–labor relationship in many LDCs were to some extent transformed in the education sector and resulted in equity-enhancing reforms. Hence, the big picture that emerges from this analysis is that developing nations are moving along well-trodden, country-specific paths, invoking elements of both continuity and (guided) change.

8.2.2 Rethinking the political economies of developing countries

The existing literature has (implicitly) assumed that developing countries either maintain similar political economies, or that they are so vastly different from one another that general policy prescriptions are of little use. Both views scoff at the idea of a "welfare state" in countries at such low levels of economic, social, and political development, and the possibility of distinct distribution regimes has similarly been overlooked. With little recourse, then, we have been focusing on social policies that have been the mainstay of welfare regimes in OECD nations and ignoring the spectrum of welfare policies pursued by LDC governments.

The broader consequence has been that, for developing countries, we have had no real starting point to analyze either existing or potentially politically viable social policies. This analysis underscores the importance of removing this black box surrounding redistribution policies in developing countries. It takes seriously the literature indicating that distribution (and production) regimes are what affect economic performance and social well-being, not vice versa. By asking if, how, and why the principle of embedded liberalism has been just as much a reality for developing countries as it has been for the advanced industrialized nations, this book makes two important policy-relevant discoveries about the uniqueness of LDC political economies.

[5] The adoption of costly welfare benefits and a development strategy that tends to be less (economically) open is an example of a complementary organization form.

First, unlike the OECD countries, most developing countries face a trade-off between pursuing policies that encourage human capital investment and adopting welfare schemes that protect isolated groups from market risks. Even more fundamentally, this choice among welfare strategies turns out to be systematic. I argue in chapter 4 that there was a "founding moment of institutional formation" which sent countries along different welfare paths, and that this moment is critical to understanding the nature of regime diversity today.[6] Linking the choice of early development strategies with differing welfare regimes sheds some light on why a certain set of welfare policies is consistently favored in some developing countries but not in others. This is why the promotion of human capital investment has been more difficult in some countries (e.g. India) than in others (e.g. South Korea).

Second, the particular institutions and structures created in the formative period have narrowed the possible range of outcomes *for the poor* in the contemporary period. Welfare regimes empowered certain groups at the expense of others and helped reinforce the power structure within society. The important feedback mechanism identified in this book is thus the "power-distributional effect," wherein those who benefit from the existing system have a vested interest in sustaining it (see Weiss, 2003: 23).[7] Marginalized groups continue to be excluded, not only because they lack class mobilization, but because the existing structure actively reinforces their subordinate position by facilitating the organization and empowerment of other "insider" groups.

Nonetheless, institutions do not necessarily completely lock policymakers into a particular set of choices (see Pierson, 2000, and Thelen, 2004). The incremental changes in welfare strategies discussed earlier are a clear illustration of this point. This analysis, however, can only pique scholarly interest in the exact mechanisms of welfare regime change. A productive inquiry for the successful implementation of pro-poor policies would benefit immensely from developing more sophisticated tools for understanding institutional change. For instance, more detailed historical work exploring the cohesiveness and strategic skill of the dominant coalitions in upholding particular welfare strategies would significantly further discourse in this area. Finding weak points or sources of divisions in the elite group can be an important source of institutional change (Mahoney, 2000).

6 See Thelen's (1999: 387) discussion of critical junctures.

7 See Pierson (2000) and Mahoney (2000) for informative discussions on different institutional feedback mechanisms.

8.2.3 Rethinking the capital–labor dichotomy

The welfare literature has long relied upon power resource theories to explain the emergence and expansion of welfare states based on the power of labor and the left. As scholars such as Swensen (2002), Mares (2003a, 2003b, 2005), and Thelen (2004) have recently pointed out, however, studies that assume that capitalist and labor interests are always at odds are incorrect. The findings in this book ultimately attune to the recent literature that questions this tenet of power resource theory by positing that capitalists may not be opposed to social policies and that their preferences can vary in different countries. To begin with, the findings in chapter 2 hint that labor in developing countries is too weak to be responsible for the existing social policies and programs of these nations.[8] They simply could not have acted alone, however skewed social legislation might be in terms or redistribution.

As it turns out, in each of the three welfare regime types, capitalist preferences are compatible with the welfare policies employed. In the protective welfare states, capitalists are amenable to social-insurance-type policies because of the benefits they gain in return – more labor peace. They can also afford to do so, since governments can compensate them in other ways in the closed economic environment. In productive welfare states, capitalists support welfare arrangements that eschew protectionist welfare policies and keep labor costs to a minimum. Additionally, this book highlights the critical importance of cross-class alliances in effecting equity-enhancing policy changes in the current phase of globalization, particularly in education. To be sure, policy-makers also play an important role, as entrepreneurs that facilitate these alliances in the various circumstances.

Further investigating whether and how the role and interests of capitalists change with globalization would thus be instrumental to developing a better understanding of the dynamics of institutional change. Given the role played by business interests in social welfare legislation, it is worthwhile to explore if and how globalization has affected their support for social policies other than just education. For example, while capitalists and organized labor might have once settled on social policies adopted in the protective welfare regimes, if and how has this agreement changed since the adoption of economic openness policies? Chapter 2 highlights indications that, absent encompassing labor movements, it has become more and more difficult for capital and labor to agree on social policies. The case studies

[8] Note that chapter 2 focuses on the role of labor in welfare retrenchment, and not welfare expansion. Nonetheless, the low PLP findings raise questions about the independent role of labor in welfare expansion.

further present instances where capitalist support for protective social policies such as social security appear to be waning (e.g. Brazil). It would be meaningful to focus more specifically on how the impact of such changes in business support might affect specific welfare regimes.

8.2.4 Broader questions for future research

This book leaves open three broader research questions for further analysis. First, the arguments refer to "developing countries" as a group, which includes the least developed. Because of data limitations, however, several of them are excluded. A future research task is to choose a case study from this group and assess if, how, and to what extent the typology of welfare states fits even the world's poorest countries, such as the Central African Republic. Second, it was noted in the case studies that, within the broader category of "productive" and "protective" welfare states, countries vary in the specific types of welfare programs they pursue. It would be worthwhile to assess whether there are systematic reasons (e.g. related to economic development, democracy) for choosing certain types of protective (or productive) strategies over another.

Finally, the case studies also revealed that democracy and democratization play a more complex role in the development and expansion of welfare regimes than predicted by existing analyses. Is it the broad category of regime type, or is it actually "new democracy," or simultaneous transitions (democratization and globalization) that provide the impetus for welfare reforms? Being able to predict the ways in which democracy systematically affects distributive politics and policies will be particularly important as democracy matures (or fails to do so) and globalization advances in the twenty-first century.

8.3 Prospects for the future?

Polanyi (1944: 3) warned that balancing the institutionalization of the self-regulating market with social protectionism is no easy task:

> Our thesis is the idea that a self-adjusting market implied a stark utopia. Such an institution could not exist for any length of time without annihilating the human and natural substance of society; it would have physically destroyed man and transformed his surroundings into a wilderness. Inevitably, society took measures to protect itself, but whatever measures it took impaired the self-regulation of the market, disorganized industrial life and thus endangered society in yet another way.

Developing countries have certainly struggled to find this balance, and now face a double bind in the face of twenty-first-century globalization.

On the one hand, the measures that society took "to protect itself" in developing countries have been limited to the more privileged sectors of society. These measures, according to Polanyi's logic, disorganize industrial life and endanger society. Now, under globalization, not only are demands rising for a self-regulating market and an investment-friendly environment, but these pressures are also impacting the middle class and making it even harder for welfare regimes to shift in a pro-poor direction. If the final goal is the market–society balance to which Polanyi refers, it is imperative that current reforms favor the poor, who tend to be the absolute majority in most LDCs.

Are prospects for the future so dim? Perhaps not. Positive developments have emerged from this analysis, which ought not to be lost in the process of untangling the complex relationship between globalization, domestic politics, and LDC welfare strategies. Certainly, advancement in education reform is one encouraging sign of progress for the poor. Evidence that cross-class alliances in favor of progressive change can be facilitated when subordinate groups mobilize is also encouraging. For example, in addition to unqualified endorsement from business, India's poor also mobilized en masse in favor of the 2001 Education for All legislation. Additionally, democracy can provide an environment more conducive to promoting reforms. As discussed above, some of the case studies, specifically Brazil and South Korea, highlighted the potential positive impact of "new democracy," particularly when accompanied by the efforts of reform-minded bureaucrats. Finally, scholars, activists, and policy-makers alike should not lose sight of the power that they hold by virtue of their ability to disseminate information. Educating the populace about the importance of education and, in the case of Brazil, providing information about the benefits of social security reform affected the introduction of equity-enhancing change. The resonance of this type of information lies in its ability to persuade a broad range of groups of the potential benefits. This is a powerful tool, and one that can be used by all those invested in ensuring, as Rodrik (1997a: 2) puts it, that "international economic integration does not contribute to domestic social *dis*integration."

Appendix A: LDC social spending[1]

Table A.1 *Social security and welfare spending*

SS and welfare (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Bangladesh	0.495	0.497	–	–	Low-income
Cameroon	1.084	1.005	0.596	−0.488	Low-income
Ghana	1.530	0.715	1.034	−0.497	Low-income
India	0.368	0.682	0.746	0.378	Low-income
Kenya	0.210	0.036	0.020	−0.190	Low-income
Lesotho	0.067	0.781	0.785	0.717	Low-income
Liberia	0.370	0.319	–	–	Low-income
Malawi	0.640	0.258	–	–	Low-income
Mali	0.996	1.106	–	–	Low-income
Mozambique	–	–	–	–	Low-income
Nepal	0.068	0.102	0.260	0.192	Low-income
Nicaragua	2.253	1.284	4.672	2.419	Low-income
Nigeria	–	–	–	–	Low-income
Pakistan	0.334	0.948	–	–	Low-income
Panama	3.208	3.823	5.518	2.310	Low-income
Tanzania	0.205	0.179	–	–	Low-income
Zambia	0.558	0.629	0.442	−0.116	Low-income
Zimbabwe	1.881	1.685	3.345	1.464	Low-income
Bolivia	0.343	1.388	3.683	3.340	Lower middle-income
Brazil	6.291	6.765	9.546	3.255	Lower middle-income
China	–	–	0.008	–	Lower middle-income
Colombia	–	2.842	1.266	–	Lower middle-income
Dominican Republic	0.984	0.928	0.620	−0.364	Lower middle-income
Ecuador	0.120	0.197	0.280	0.161	Lower middle-income
Egypt	4.490	5.054	2.980	−1.511	Lower middle-income
El Salvador	0.575	0.529	0.668	0.093	Lower middle-income
Fiji	0.796	1.446	1.267	0.471	Lower middle-income
Guatemala	0.675	0.391	0.458	−0.217	Lower middle-income

[1] Note that income categories in the appendix tables are based on the 2006 classification by the World Bank. In tables 2.2 and 2.4, and figures 2.2 and 2.3, the high-income countries are included as upper middle-income countries.

Table A.1 (*cont.*)

SS and welfare (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Guyana	2.073	2.612	–	–	Lower middle-income
Honduras	0.980	–	–	–	Lower middle-income
Indonesia	–	–	0.972	–	Lower middle-income
Iran	1.638	2.790	2.996	1.358	Lower middle-income
Jordan	3.978	3.898	5.261	1.283	Lower middle-income
Morocco	1.903	1.799	1.925	0.022	Lower middle-income
Paraguay	1.951	2.497	1.779	−0.172	Lower middle-income
Peru	0.042	0.027	–	–	Lower middle-income
Philippines	0.340	0.215	0.447	0.108	Lower middle-income
Sri Lanka	6.093	3.496	4.354	−1.738	Lower middle-income
Syria	1.613	1.878	0.531	−1.082	Lower middle-income
Thailand	0.595	0.561	0.577	−0.018	Lower middle-income
Tunisia	3.269	3.604	4.994	1.725	Lower middle-income
Argentina	4.663	4.724	6.674	2.011	Upper middle-income
Botswana	0.167	0.805	0.714	0.547	Upper middle-income
Chile	8.208	10.663	7.041	−1.168	Upper middle-income
Costa Rica	4.094	2.997	4.357	0.263	Upper middle-income
Malaysia	0.768	1.203	1.458	0.690	Upper middle-income
Mauritius	5.181	4.161	3.717	−1.464	Upper middle-income
Mexico	3.417	2.431	3.002	−0.415	Upper middle-income
South Africa	–	1.600	–	–	Upper middle-income
Trinidad and Tobago	1.777	1.767	4.350	2.572	Upper middle-income
Turkey	0.473	0.255	0.971	0.499	Upper middle-income
Uruguay	10.654	12.932	17.970	7.316	Upper middle-income
Venezuela	1.496	1.645	–	–	Upper middle-income
Cyprus	4.691	5.429	7.526	0.028	High-income
Greece	8.091	11.260	6.017	−2.074	High-income
Israel	9.505	9.076	11.311	1.806	High-income
Kuwait	1.379	4.457	8.917	7.538	High-income
Singapore	0.200	0.366	0.714	0.514	High-income
South Korea	0.815	1.130	1.722	0.907	High-income

Table A.2 *Education spending*

Education (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Bangladesh	1.134	1.138	–	–	Low-income
Cameroon	2.639	2.582	2.958	0.319	Low-income
Ghana	3.506	2.681	3.884	0.378	Low-income
India	0.272	0.336	0.333	0.061	Low-income
Kenya	4.690	5.457	5.475	0.785	Low-income
Lesotho	6.596	8.156	10.215	3.618	Low-income

Table A.2 (*cont.*)

Education (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Liberia	3.706	4.153	–	–	Low-income
Malawi	2.913	3.599	–	–	Low-income
Mali	3.766	2.840	–	–	Low-income
Mozambique	–	–	–	–	Low-income
Nepal	1.112	1.871	2.219	1.106	Low-income
Nicaragua	1.244	1.766	4.663	3.419	Low-income
Nigeria	–	–	–	–	Low-income
Pakistan	0.348	0.547	–	–	Low-income
Panama	5.388	4.497	4.560	−0.828	Low-income
Tanzania	3.675	3.239	–	–	Low-income
Zambia	5.577	4.076	2.890	−2.687	Low-income
Zimbabwe	3.925	6.778	6.312	2.387	Low-income
Bolivia	3.111	3.203	3.788	0.676	Lower middle-income
Brazil	1.083	1.027	1.091	0.008	Lower middle-income
China	–	–	0.182	–	Lower middle-income
Colombia	–	3.163	2.985	–	Lower middle-income
Dominican Republic	2.084	1.791	1.685	−0.400	Lower middle-income
Ecuador	3.131	3.874	2.669	−0.462	Lower middle-income
Egypt	4.813	4.428	4.401	−0.412	Lower middle-income
El Salvador	3.044	2.625	1.899	−1.145	Lower middle-income
Fiji	5.058	5.893	5.586	0.528	Lower middle-income
Guatemala	1.617	1.597	1.567	−0.050	Lower middle-income
Guyana	6.015	6.666	–	–	Lower middle-income
Honduras	3.257	–	–	–	Lower middle-income
Indonesia	1.689	1.918	1.543	−0.146	Lower middle-income
Iran	3.831	4.482	4.478	0.647	Lower middle-income
Jordan	4.365	4.364	4.942	0.577	Lower middle-income
Morocco	5.026	5.493	5.353	0.328	Lower middle-income
Paraguay	1.458	1.183	1.991	0.534	Lower middle-income
Peru	3.576	2.656	–	–	Lower middle-income
Philippines	1.877	2.347	3.194	1.317	Lower middle-income
Sri Lanka	2.881	2.663	2.781	−0.100	Lower middle-income
Syria	3.393	2.659	2.183	−1.210	Lower middle-income
Thailand	3.203	3.617	3.344	0.141	Lower middle-income
Tunisia	6.560	5.433	5.805	−0.755	Lower middle-income
Argentina	1.756	1.041	0.810	−0.947	Upper middle-income
Botswana	5.906	7.003	8.542	2.636	Upper middle-income
Chile	4.501	3.678	2.951	−1.550	Upper middle-income
Costa Rica	5.611	4.741	5.307	−0.304	Upper middle-income
Malaysia	5.601	5.787	5.174	−0.427	Upper middle-income
Mauritius	3.578	3.776	3.582	0.004	Upper middle-income
Mexico	2.620	2.885	3.501	0.881	Upper middle-income
South Africa	–	1.835	–	–	Upper middle-income
Trinidad and Tobago	4.108	3.516	3.737	−0.371	Upper middle-income

Table A.2 (*cont.*)

Education (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Turkey	3.717	2.440	3.400	−0.317	Upper middle-income
Uruguay	2.463	1.874	2.078	−0.385	Upper middle-income
Venezuela	3.809	4.414	–	–	Upper middle-income
Cyprus	3.062	3.303	3.656	0.594	High-income
Greece	2.844	3.696	2.967	0.123	High-income
Israel	5.455	5.627	5.712	0.257	High-income
Kuwait	3.319	5.137	5.778	2.459	High-income
Singapore	3.002	4.619	3.760	0.758	High-income
South Korea	2.459	3.043	3.353	0.894	High-income

Table A.3 *Health spending*

Health (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Bangladesh	0.485	0.617	–	–	Low-income
Cameroon	0.813	0.806	0.786	−0.027	Low-income
Ghana	1.365	1.015	1.348	−0.016	Low-income
India	0.248	0.305	0.248	0.000	Low-income
Kenya	1.666	1.767	1.533	−0.133	Low-income
Lesotho	1.915	3.979	5.382	3.468	Low-income
Liberia	2.123	1.800	–	–	Low-income
Malawi	1.414	2.000	–	–	Low-income
Mali	0.995	0.696	–	–	Low-income
Mozambique	–	–	–	–	Low-income
Nepal	0.586	0.777	0.688	0.102	Low-income
Nicaragua	0.718	2.223	4.161	3.443	Low-income
Nigeria	–	–	–	–	Low-income
Pakistan	0.244	0.225	–	–	Low-income
Panama	4.386	4.703	5.004	0.618	Low-income
Tanzania	1.834	1.483	–	–	Low-income
Zambia	2.191	2.176	1.793	−0.398	Low-income
Zimbabwe	1.821	2.148	2.411	0.590	Low-income
Bolivia	0.961	0.830	1.104	0.143	Lower middle-income
Brazil	1.227	1.809	1.916	0.689	Lower middle-income
China	–	–	0.027	–	Lower middle-income
Colombia	–	0.651	1.143	–	Lower middle-income
Dominican Republic	1.586	1.549	1.662	0.076	Lower middle-income
Ecuador	0.848	1.264	1.621	0.773	Lower middle-income
Egypt	1.509	1.037	0.875	−0.634	Lower middle-income
El Salvador	1.293	1.184	1.100	−0.193	Lower middle-income
Fiji	2.284	2.240	2.386	0.102	Lower middle-income

Table A.3 (*cont.*)

Health (% GDP)	1970s	1980s	1990s	Change 1970s–1990s	Income classification
Guatemala	0.846	0.886	0.945	0.100	Lower middle-income
Guyana	2.327	3.954	–	–	Lower middle-income
Honduras	1.821	–	–	–	Lower middle-income
Indonesia	0.410	0.462	0.433	0.023	Lower middle-income
Iran	1.301	1.661	1.744	0.442	Lower middle-income
Jordan	1.792	1.522	2.393	0.600	Lower middle-income
Morocco	1.151	0.942	0.945	−0.205	Lower middle-income
Paraguay	0.339	0.422	0.705	0.366	Lower middle-income
Peru	1.018	0.956	–	–	Lower middle-income
Philippines	0.572	0.678	0.629	0.057	Lower middle-income
Sri Lanka	1.608	1.514	1.503	−0.105	Lower middle-income
Syria	0.363	0.398	0.634	0.272	Lower middle-income
Thailand	0.637	0.985	1.223	0.585	Lower middle-income
Tunisia	1.985	2.319	2.191	0.205	Lower middle-income
Argentina	0.499	0.236	0.309	−0.190	Upper middle-income
Botswana	1.867	2.029	1.967	0.100	Upper middle-income
Chile	2.407	1.901	2.418	0.012	Upper middle-income
Costa Rica	2.087	5.906	6.664	4.577	Upper middle-income
Malaysia	1.674	1.495	1.426	−0.249	Upper middle-income
Mauritius	2.109	1.952	1.941	−0.168	Upper middle-income
Mexico	0.620	0.353	0.463	−0.157	Upper middle-income
South Africa	–	0.538	–	–	Upper middle-income
Trinidad and Tobago	2.018	1.803	2.258	0.241	Upper middle-income
Turkey	0.506	0.431	0.716	0.210	Upper middle-income
Uruguay	0.961	1.053	1.666	0.705	Upper middle-income
Venezuela	2.124	2.003	–	–	Upper middle-income
Cyprus	1.532	1.946	2.045	0.513	High-income
Greece	2.630	3.949	2.461	−0.169	High-income
Israel	2.711	2.481	3.404	0.693	High-income
Kuwait	1.568	2.893	2.984	1.416	High-income
Singapore	1.452	1.401	1.128	−0.324	High-income
South Korea	0.197	0.266	0.188	−0.009	High-income

Appendix B: Assessing potential labor power

Few efforts have been made to measure and compare labor power across developing countries and over time. Union density is the most commonly used cross-national indicator of labor power. As noted earlier, however, union density is more appropriately applied in the developed world than in the LDCs. Most LDCs are still far from attaining strong and independent unions. Even in LDCs with (relatively) high union density, labor is rife with collective action problems and often subject to a broad range of government controls. For more details on PLP – its connection with marketplace bargaining power, the different country rankings on PLP, its strengths and weaknesses – see Rudra (2005).

Given the unreliability of direct organizational measures, as Encarnation's (1989) analysis suggests, alternative assessments of labor's bargaining power tend to be tautological. According to Encarnation (1989), bargaining power is generally defined by the outcome, and so it is difficult to tell which party had more bargaining power if negotiations are "won by those who win." This approach makes it virtually impossible to differentiate between power and negotiated outcomes. Consequently, Encarnation (1989: 20) concludes that bargaining power must refer to the ability of laborers to "improve the range of plausible outcomes available to each [negotiator], and to improve the probability of securing the outcome that each prefers."

Importantly, the measure of PLP used in this analysis avoids the tautology problem. It does so by getting some sense of labor's *propensity* for collective action rather than collective action per se. After all, since labor discontent can be costly for political leaders (and workers), governments often respond to labor demands before strikes or other militant actions occur. Offe and Wiesenthal (1985: 216) argue that in such circumstances "the organization then has become strong enough to derive some power (i.e. control over its environment) from its recognized *potential* of power. In other words, concessions are likely to be made not because members have struck, but in order to avoid a strike."

To assess whether PLP serves as an indirect measure of workers' political power, additional steps must be taken. Comparing PLP to other non-tautological assessments of labor's bargaining power is the most precise way to accomplish this. McGuire's (1999) creation of the Labor Strength Index (LSI) represents the only other effort to assess the "real" magnitude of labor's bargaining power in LDCs and compare it across countries. Because of data limitations, however, it represents only one period of time (the 1990s). LSI is based on four dimensions: (1) union membership as a percentage of the non-agricultural labor force; (2) the proportion of formal-sector workers covered by collective contracts; (3) the level of collective bargaining power (national/sectoral, enterprise, or both); and (4) the number of major ILO conventions ratified.[1] This is a multifaceted attempt to capture several important dimensions of labor strength that are not directly measured by PLP.

The comparison of PLP and LSI in table B1 significantly increases confidence in the reliability of PLP as an indicator of labor's bargaining power. The correlation coefficient, excluding the outliers, is 0.61 (see figure B1). The correlation is actually higher than expected, since LSI includes unionization data (and its inherent weaknesses), and because PLP captures some important non-traditional sources of labor's bargaining power.[2]

For the great majority of cases, the PLP rankings are similar to LSI. Interestingly, it is mostly the east Asian cases – e.g. Singapore, South Korea, Malaysia, and Thailand – that show the most contrast.[3] Their PLP score is "high," which is certainly contrary to conventional wisdom on labor in these nations. The PLP scores are consistent with more recent analyses by Yap (2003) and Brown (2004), though, who bring important new insights on labor in the east Asian countries and explain why labor's political influence in these authoritarian nations has commonly been misinterpreted.

According to both Yap (2003) and Brown (2004), workers in these nations have been in a very unusual position in the developing world because of the central economic role they have played in the countries'

[1] The number of ILO ratifications is, arguably, the weakest component of LSI, since ratification does not necessarily ensure enforcement. A detailed evaluation of the strengths and weaknesses of LSI is a subject for a future study, however.

[2] Interestingly, LSI closely resembles Silver's (2003: 13) reference to "associational power" (most importantly, trade unions and political parties). The comparisons in table B1 and figure B1 suggest that marketplace bargaining power and associational power are closely related.

[3] LSI and PLP also differ in some of the African cases, where LSI tends to be higher than PLP (Ghana, Mali). This is most probably because data availability for all four components of LSI is apt to be limited in these countries, and so these scores may be biased upward (see McGuire, 1999: 12).

Table B.1 *Comparing potential labor power and labor strength index*

Countries	PLP	LSI (McGuire)
Argentina	high	high
Bangladesh	low	low
Bolivia	med–low	low
Botswana	low	low
Brazil	high	high
Cameroon	low	med–high
Chile	med–high	low
China	high	med–high
Colombia	med–high	med–low
Costa Rica	med–high	med–high
Cyprus	med–high	high
Ecuador	med–low	med–low
Egypt	med–high	med–high
El Salvador	low	low
Ghana	med–high	med–low
Greece	med–high	high
Guatemala	med–high	med–low
Honduras	low	low
India	med–low	med–low
Indonesia	med–low	low
Israel	high	med–high
Kenya	med–high	med–high
Malaysia	high	low
Mali	med–low	high
Mauritius	low	med–low
Mexico	med–high	med–high
Morocco	low	low
Nicaragua	med–low	med–high
Nigeria	med–low	med–low
Pakistan	low	low
Panama	low	low
Paraguay	med–low	low
Peru	med–low	med–low
Philippines	high	med–low
Singapore	high	low
South Africa	high	med–low
South Korea	high	low
Thailand	high	med–low
Tunisia	med–low	low
Turkey	med–high	med–high
Uruguay	high	med–high
Venezuela	med–high	med–low
Zambia	med–low	med–high
Zimbabwe	med–low	med–low

Table B.1 (*cont.*)

Percentile range	Value
Below 25th	low
25th–50th	mid-low
50th–75th	med-high
Above 75th	high

Note: To facilitate direct comparison with McGuire (1999), the PLP values in the table are averages for 1990–7 only. Several LDCs had to be dropped from the comparison because they were not included in LSI data. Also, because McGuire's index additionally includes developed and eastern European nations, I eliminated these countries from the sample, recalculated the percentiles, and rechecked the comparison. The results were almost identical to those reported above.

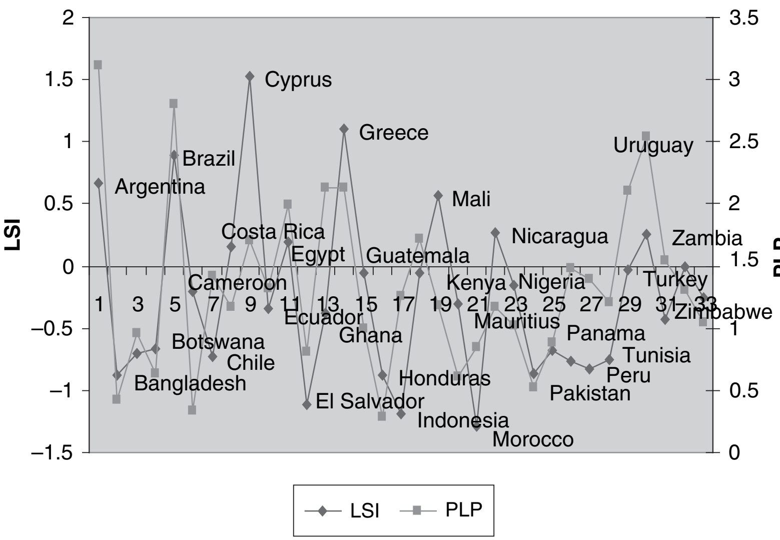

Figure B.1 Potential labor power and labor strength index

Note: Some of the countries have been dropped from the figure in order to reduce clustering.

development. Repressive labor strategies have been part and parcel of the east Asian nations' export-oriented industrialization strategy for economic development (see also Kuruvilla, (1996). Somewhat paradoxically, however, precisely because of this dependence on labor, the state has had to accommodate labor in different ways.[4] Labor's collective political consciousness has thereby evolved differently in these countries, while the more familiar signs of political power (e.g. strikes, unionization, centralization of bargaining power) have been conspicuously absent.[5] As Young (2004: 552) argues, "In studies [...] where the forms of consciousness and organization are found not to conform to these [familiar] expectations, labor is deemed to be 'weak' or 'immature', and seen to be peripheral to the development of state, society and the economy [...] The outcome may not conform to very generalized theoretical expectations, but that calls for re-evaluation and refinement of theory, rather than a dismissal of the significance of working class struggles." One important advancement of the PLP indicator, then, is that it can approximate labor movements that do not develop the familiar institutional forms.

Ultimately, the indicator applied in this study, PLP, offers three broad advantages: (1) it corresponds to conditions specific to labor in developing countries; (2) it is comparable across LDCs; and (3) it has a time-series component that can capture the dynamic aspects of bargaining power. The first advantage privileges PLP as an indicator of labor strength because its logic is based on the particular circumstances faced by labor in LDCs. The desirability of the second two characteristics is more obvious. A standardized measure available over time and across countries greatly reduces the biases that can affect empirical analyses of labor in the developing world.

[4] Yap (2003), for instance, discusses "credible apologies" that east Asian governments make to labor. They may dismiss, demote, or replace certain government officials deemed responsible for the policies that "hurt" labor, downsize or eliminate the relevant agency, or offer reparations. Additionally, representatives from academia, labor, or business may be invited in to review, evaluate, or oversee changes to government.

[5] For example, Yap (2003) draws from Bates (1981) and argues that labor can withdraw economic resources (e.g. alter their production mix, engage in the black market) to protest against the government's economic policies. In reference to workers in Thailand, Brown (2004) discusses the importance of taking account of industrial workers and their organization as *potential political actors*. He argues that "even when labor is invisible, in the sense of not being a public, organized actor overtly engaged in formal political processes, the politics of the working class is nonetheless there and is significant. For, behind the scenes, there has been a continual jockeying to channel and control workers and their struggles. This is to ensure that they either do not emerge as a public, organized force, or if they do, they are organized in a manner that is in keeping with the broader economic, ideological and political interests of those dominating contests for state power" (Brown, 2004: 133).

Appendix C: Additional tests for the RTB hypothesis

Table C.1 *Education spending in LDCs*

	Model C.1		Model C.2		Model C.3	
	Educ. (% GDP)	Educ. per capita	Educ. (% GDP)	Educ. per capita	Educ. (% GDP)	Educ. per capita
PLP	0.02(0.06)	1.47(2.60)	0.04(0.06)	2.24(2.31)	0.13*(0.08)	1.33(2.37)
Trade_{t-1} × PLP	−0.001(0.001)	0.052*(0.027)	−0.001(0.001)	0.03(0.03)	−0.001(0.001)	0.08***(0.03)
Portfolio_{t-1} × PLP	0.02*(0.01)	1.28***(0.41)	0.015(0.010)	1.05***(0.38)	0.007(0.013)	1.52***(0.43)
FDI_{t-1} × PLP	−0.005(0.004)	−0.95***(0.17)	–	–	0.02(0.02)	−2.01**(0.98)
Trade_{t-1}	−0.003(0.003)	−0.19***(0.06)	−0.003(0.003)	−0.18***(0.06)	−0.003(0.002)	−0.16***(0.05)
Portfolio_{t-1}	−0.04(0.04)	−2.69*(1.42)	−0.03(0.04)	−2.17*(1.31)	0.01(0.05)	−3.59***(1.28)
FDI_{t-1}	0.01(0.02)	1.44***(0.55)	–	–	0.01(0.02)	−0.14(0.49)
GDP per capita	−0.07(0.20)	68.28***(6.20)	−0.08(0.20)	69.47***(6.43)	−0.53***(0.20)	82.07***(7.72)
Growth	−0.012***(0.004)	−0.19***(0.08)	−0.012***(0.004)	−0.17**(0.08)	−0.009***(0.004)	−0.24***(0.08)
Democracy	−0.04(0.07)	0.89(2.25)	−0.03(0.07)	−.41(2.22)	0.08(0.08)	6.63***(1.93)
Youth pop. (0–14)	−0.04*(0.02)	−2.02***(0.56)	−0.04*(0.02)	−2.08***(0.59)	−0.01(0.02)	−1.37**(0.60)
Debt_{t-1}	−0.005***(0.001)	−0.10***(0.03)	−0.005***(0.001)	−0.11***(0.03)	−0.004***(0.001)	−0.15***(0.03)
R^2	0.91	0.90	0.91	0.90	0.94	0.93
N	787	787	791	791	618	618

Notes: *** = $p < 0.01$; ** = $p < 0.05$; * = $p < 0.10$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

Table C.2 *Health spending in LDCs*

	Model C.4		Model C.5		Model C.6	
	Health (% GDP)	Health per capita	Health (% GDP)	Health per capita	Health (% GDP)	Health per capita
PLP	0.042*(0.025)	−2.28***(0.56)	0.043(0.02)	−2.13***(0.57)	0.11***(0.03)	−0.07(0.79)
$Trade_{t-1}$ × PLP	−0.001**(0.0003)	0.03***(0.01)	−0.001***(0.0003)	0.019***(0.006)	−0.001**(0.0004)	0.01(0.01)
$Portfolio_{t-1}$ × PLP	0.002(0.004)	−0.03(0.12)	0.002(0.004)	−0.02(0.12)	−0.010*(0.005)	−0.30**(0.14)
FDI_{t-1} × PLP	−0.001(0.003)	−0.16***(0.06)	–	–	0.012(0.013)	0.01(0.33)
$Trade_{t-1}$	−0.001(0.003)	−0.069**(0.035)	−0.001(0.002)	−0.065*(0.035)	−0.001(0.002)	−0.02(0.04)
$Portfolio_{t-1}$	−0.007(0.020)	−0.06(0.57)	−0.01(0.02)	−0.06(0.56)	0.03(0.02)	0.99*(0.57)
FDI_{t-1}	0.003(0.011)	0.07(0.26)	–	–	0.01(0.01)	−0.12(0.28)
GDP per capita	0.12(0.11)	27.81***(2.96)	0.12(0.11)	28.05***(2.77)	−0.00(0.00)	24.20***(3.43)
Growth	−0.006***(0.002)	−0.10***(0.04)	−0.006***(0.002)	−0.10***(0.04)	−0.005***(0.002)	−0.08(0.05)
Democracy	−0.01(0.04)	1.23(1.21)	−0.01(0.04)	0.89(1.22)	−0.02(0.05)	1.52(1.20)
Elderly population	−0.06(0.05)	3.21***(1.14)	−0.07(0.05)	3.34***(1.23)	−0.02(0.05)	2.84***(1.14)
$Debt_{t-1}$	−0.001(0.001)	−0.04**(0.02)	−0.001(0.001)	−0.037**(0.018)	−0.001(0.001)	−0.05**(0.02)
R^2	0.92	0.93	0.92	0.93	0.94	0.94
N	786	786	790	790	617	617

Notes: *** = $p < 0.01$; ** = $p < 0.05$; * = $p < 0.10$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

Table C.3 *Education spending in OECD countries*

	Model C.7		Model C.8	
	Educ. (% GDP)	Educ. per capita	Educ. (% GDP)	Educ. per capita
PLP	0.03(0.02)	5.12(4.48)	0.005**(0.002)	1.20*(0.66)
$Trade_{t-1}$ × PLP	−0.0003(0.0003)	−0.06(0.07)	–	–
$Portfolio_{t-1}$ × PLP	0.03(0.03)	7.08(5.10)	0.03(0.03)	8.84*(5.05)
FDI_{t-1} × PLP	0.003**(0.002)	0.81***(0.31)	0.004***(0.002)	0.95***(0.32)
$Trade_{t-1}$	−0.01(0.01)	−3.77(2.64)	–	–
$Portfolio_{t-1}$	−3.15(2.53)	−840.44*(467.72)	−3.21(2.53)	−889.24*(472.42)
FDI_{t-1}	−0.30**(0.14)	−55.22**(24.44)	−0.38***(0.13)	−71.91***(24.09)
Growth	−0.07***(0.02)	−7.73*(4.12)	−0.07***(0.02)	−8.63**(4.24)
Youth pop. (0–14)	−0.26***(0.07)	−93.97***(13.91)	−0.23***(0.07)	−84.14***(12.82)
Unemployment	0.07**(0.03)	−0.43(5.80)	0.08**(0.03)	0.87(5.94)
R2	0.81	0.91	0.83	0.91
N	348	348	348	348

Notes: *** = $p < 0.01$; ** = $p < 0.05$; * = $p < 0.10$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

Table C.4 *Health spending in OECD countries*

	Model C.9		Model C.10	
	Health (% GDP)	Health per capita	Health (% GDP)	Health per capita
PLP	0.03*(0.01)	5.15*(2.97)	0.002(0.002)	0.74(0.70)
$Trade_{t-1}$ × PLP	−0.0004*(0.0002)	−0.07(0.05)	–	–
$Portfolio_{t-1}$ × PLP	−0.01(0.03)	10.73(7.62)	0.001(0.03)	11.81(7.73)
FDI_{t-1} × PLP	0.001(0.002)	0.20(0.32)	0.002(0.002)	0.28(0.33)
$Trade_{t-1}$	−0.01(0.02)	3.67(2.73)	–	–
$Portfolio_{t-1}$	−1.13(3.64)	−1611.03*(891.33)	−0.97(3.65)	−1593.51*(895.33)
FDI_{t-1}	−0.08(0.15)	0.52(31.05)	−0.13(0.15)	−3.94(30.87)
Growth	−0.07***(0.02)	−3.58(4.28)	−0.07***(0.02)	−3.32(4.39)
Youth pop. (0–14)	–	–	–	–
Elderly pop.	0.59***(0.17)	157.43***(32.34)	0.58***(0.17)	164.71***(32.86)
Unemployment	0.11***(0.04)	8.70(7.67)	0.12***(0.05)	8.34(8.00)
R2	0.92	0.91	0.92	0.91
N	348	348	348	348

Notes: *** = $p < 0.01$; * = $p < 0.10$. Fixed-effects regression estimates. Figures in parenthesis are standard errors.

Appendix D: Variables in the inequality model

Variables	Description	Sources
Dependent variable:		
Inequality	Gini coefficients of household income distribution	Deninger and Squire (1996)
Quintile 1 data	Concentration of income in the lowest quintile	Deninger and Squire (1996)
Independent variables:		
Welfare spending per capita	Spending on social security and welfare, education, and health per capita	IMF, *Government Finance Statistics*, various editions
Trade	Amount of total trade (EX+IM) as percentage of GDP; trade ratios above median of 50 percent considered "open"	World Bank (2000a) and World Development Indicators CD-ROM
Portfolio flows	Amount of portfolio flows as percentage of GDP	World Bank (2000a) and World Development Indicators CD-ROM
The percentage of aged [POP65]	"Aged" = number of persons over sixty-five as percentage of total population	World Bank (2000a) and World Development Indicators CD-ROM
Growth	Annual percentage growth rate of GDP at market prices based on constant 1987 local currency	World Bank (2000a) and World Development Indicators CD-ROM
GDP per capita	GDP per capita (constant 1995 US dollar)	World Bank (2000a) and World Development Indicators CD-ROM
Democracy	Scale 0–10; 10 = strong democracy; countries rating 7 and above labeled "democracy" (indicator derived from the codings of the competitiveness of political participation, the openness and competitiveness of executive recruitment, and constraints on the chief executive)	CIDCM (2000): political regime characteristics and transitions, 1800–2000 (M. G. Marshall and K. Jaggers, principal investigators)
Urbanization	Urban population as percentage of total	World Bank (2000a) and World Development Indicators CD-ROM

Appendix E: Technical notes on Gini coefficients

Recipient unit: applies to either the household or the individual.

Given that the difference is not too large, we conclude that there is no reason to expect a large systematic bias in empirical work as a result of using both household-based and individual-based Gini coefficients (Deninger and Squire, 1996: 580)

Income: either gross or net income for developing countries; only net income for OECD countries.

Although the distinction between gross income and net income may affect the level of measured inequality in a cross-country sample, the quantitative importance of this effect will depend on the progressivity and effectiveness of the tax system and might therefore be of less relevance for developing countries to the degree that the role of redistributive taxation is smaller in these countries. (Deninger and Squire, 1996: 580)

Variable measured: either income or expenditure (with 6.6 added to the expenditure-based Ginis).

One way of avoiding the exclusion of thirty-nine countries for which Gini coefficients are based on expenditures would be to add the difference of 6.6 between expenditure-based and income-based coefficients to the 136 expenditure-based Gini coefficients in the sample. (Deninger and Squire, 1996: 582)

Coverage: comprehensive coverage of the population.

Appendix F: LDC Gini coefficient statistics

Table F.1 *Summary statistics of Gini coefficients in developing countries*

Country	Mean	Median	Standard deviation	Minimum	Maximum	Year of maximum value	Year of minimum value
Bangladesh	35.85	35.73	1.65	33.3	39.0	1981	1977
Brazil	58.09	57.78	2.74	54.2	61.9	1974	1982
Chile	55.86	56.49	2.40	53.2	57.9	1989	1980
China	32.68	33.8	3.78	25.7	37.8	1992	1984
Colombia	51.25	51.32	3.24	46.0	54.5	1978	1974
Costa Rica	45.65	46.07	2.93	42.0	50.0	1977	1982/1986
Dominican Republic	46.94	47.00	3.35	43.3	50.5	1989	1984
Egypt	41.60	41.60	4.24	38.6	44.6	1975	1991
Ghana	41.73	41.54	1.42	40.5	43.3	1989	1992
Greece	41.13	41.71	1.07	39.9	41.8	1988	1981
Guatemala	55.68	58.26	5.18	49.7	59.1	1989	1979
Honduras	53.26	54.00	1.76	50.0	54.9	1986	1991
India	37.92	38.42	1.10	35.8	39.1	1991	1973
Indonesia	40.57	40.01	2.29	38.3	45.2	1978	1993
Iran	49.19	49.19	.44	48.9	49.5	1984	1972
Jordan	45.79	47.26	2.67	42.7	47.4	1980	1987
Malaysia	50.43	51.00	2.18	48.0	53.0	1976	1984
Mauritius	45.07	45.70	1.57	43.3	46.2	1986	1991
Mexico	54.07	54.98	3.62	50.0	57.9	1975	1977
Morocco	45.80	45.80	.01	45.79	45.8	1991	1984
Nigeria	45.15	44.07	2.27	43.6	47.8	1992	1986
Pakistan	38.46	38.73	.54	37.8	39.0	1985	1991
Panama	50.90	48.76	4.87	47.5	56.5	1989	1980
Peru	50.05	49.36	1.23	49.3	51.5	1994	1981
Philippines	45.60	45.73	.55	45.0	46.1	1985	1991
Singapore	40.12	40.85	1.81	37.0	42.0	1983	1978
South Korea	36.32	35.70	2.44	33.6	39.1	1976	1988
Sri Lanka	41.58	42.75	4.63	35.3	46.7	1987	1973
Tanzania	47.65	47.65	4.17	44.7	50.6	1977	1993
Thailand	46.66	47.40	3.63	41.7	51.5	1992	1975

Table F.1 (*cont.*)

Country	Mean	Median	Standard deviation	Minimum	Maximum	Year of maximum value	Year of minimum value
Trinidad and Tobago	43.91	43.91	3.09	41.7	46.1	1976	1981
Tunisia	49.16	49.60	1.62	46.8	50.6	1975	1990
Turkey	47.55	47.55	4.89	44.1	51.0	1973	1987
Venezuela	44.01	43.23	4.38	39.4	53.8	1990	1979
Zambia	54.53	54.50	4.62	50.1	59.0	1996	1991
Average	*46.22*	*46.21*	*2.64*	*25.7*	*61.9*	–	–

Appendix G: Robustness check

Table G.1 *Dependent variable: quintile 1 income in developing countries*

Variables	Model G.1	Model G.2	Model G.3
Social security and welfare (spending per capita)	0.0001 (0.0001)		
Education (spending per capita)		−0.0001 (0.0001)***	
Health (spending per capita)			−0.0003* (0.0002)
Trade	0.0002** (0.0001)	−0.0002* (0.0001)	−0.0001† (0.0001)
Trade × social security and welfare	−0.000002*** (0.000006)		
Trade × education		0.000003*** (0.000001)	
Trade × health			0.000005** (0.000002)
Democracy	−0.0049** (0.002)	−0.005** (0.002)	−0.005*** (0.002)
Democracy^2	0.0005** (0.0002)	0.0004* (0.0002)	0.0005** (0.0002)
GDPcap	−0.06** (0.03)	−0.02 (0.03)	−0.03 (0.03)
GDPcap^2	0.005** (0.002)	0.001 (0.002)	0.003 (0.002)
POP65	−0.01*** (0.003)	−0.01*** (0.003)	−0.01*** (0.003)
Urban	0.001*** (0.0004)	0.001*** (0.0003)	0.001*** (0.0003)
1970s	0.001 (0.003)	−0.003 (0.003)	−0.002 (0.003)
1980s	−0.001 (0.002)	−0.004** (0.002)	−0.003* (0.002)
N	90	100	100
R^2	0.98	0.98	0.98

Notes: *** = $p < 0.01$; ** = $p < 0.05$; * = $p < 0.10$; † = $p < 0.15$. Fixed-effects regression estimates. Figures in parentheses are standard errors.

The pattern of results for quintile data replicates the findings in table 3.4. Note that the expected signs for the primary and secondary results are now reversed. Under the conditions of globalization, increased government spending on education and health encourages a larger concentration of income for the poorest households, while greater social security spending lowers their income.

The primary difference with the regression results in table 3.4 is that the interaction of trade and health spending in this set of regressions is now significant (the sign is the same). On the one hand, it can be argued that the contrasting results confirm the weak effect of public health spending on the poor during globalization. This inconsistency in results warrants further investigation, however, and more data would be helpful to verify these findings. The signs for the first- and second-order polynomial functions of democracy and per capita GDP (Kuznets, 1955) are also reversed. In other words, income and democracy worsen the economic situation of the poorest households during the early stages of development. Over time, however, both democracy and higher aggregate income lead to a greater concentration of wealth in the lowest quintile.

Significantly, these democracy results corroborate with Burkhart (1997). It is also noteworthy that substituting the first- and second-order polynomial functions of democracy for the dummy democracy variable in the table 3.4 regressions does not change the (primary or secondary) results (not shown here).

Appendix H: Conditional impact of trade on inequality

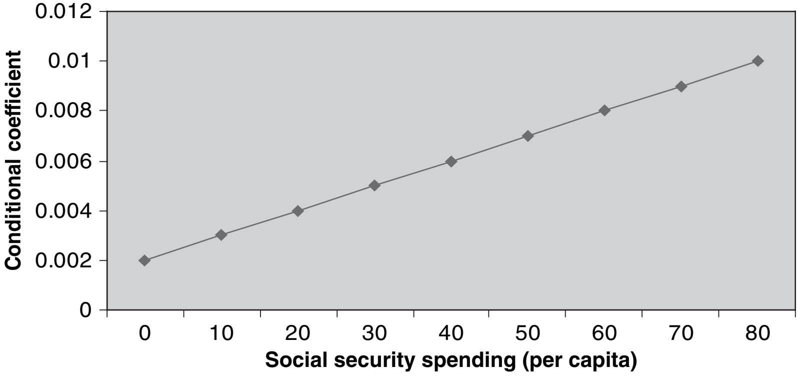

Figure H.1 Mediating effects of trade on inequality contingent upon the level of social security spending

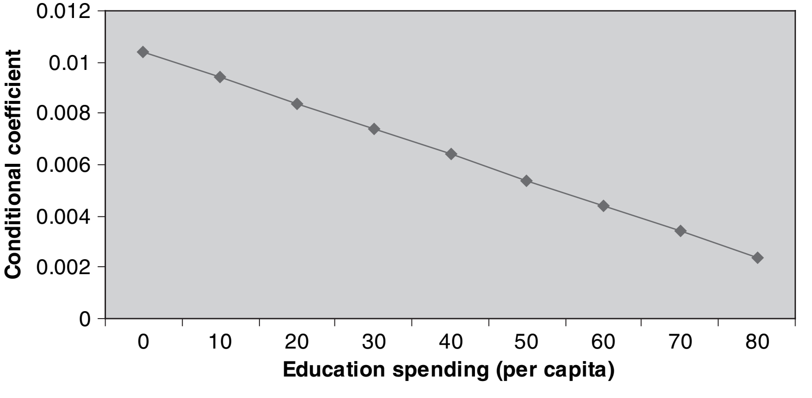

Figure H.2 Mediating effects of trade on inequality contingent upon the level of education spending

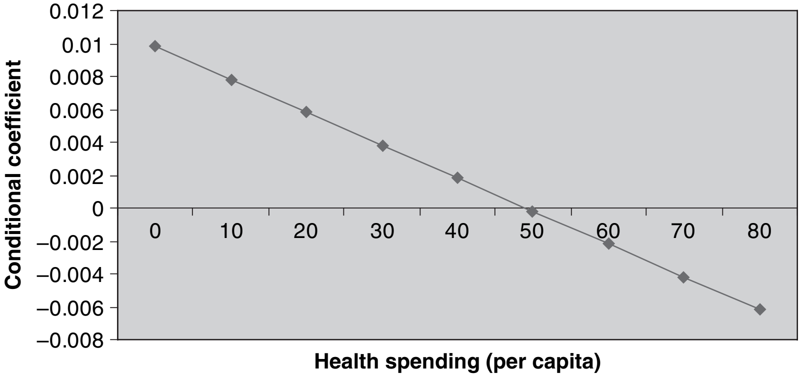

Figure H.3 Mediating effects of trade on inequality contingent upon the level of health spending

Note: These graphs have been created using the uninteracted coefficient for trade, and the interacted coefficients for trade and social spending variables. The uninteracted coefficient for trade measures the impact of trade when social spending is zero. Significance tests reveal that all conditional coefficients in figures H.1 and H.2 are significant. In figure H.3, conditional coefficients are significant until the level of trade increases beyond 40 percent.

Appendix I: Descriptions and sources of variables

Variable	Description	Source
Years	1990–7 average	
Measles, DPT	Percentage of children between twelve and twenty-three months vaccinated against measles, diphtheria, pertussis, and tetanus	World Bank World Development Indicators (CD-ROM)
Infant mortality	Infant mortality (per 1,000 live births)	World Bank World Development Indicators (CD-ROM)
Literacy rates	Adult total literacy rate (percentage of people aged fifteen and above)	World Bank World Development Indicators (CD-ROM)
Primary education spending	Government expenditures on pre-primary and primary education expenditures as percentage of total government expenditures; expenditure per student per GDP per capita also included	UNESCO *Statistical Yearbooks* (1970–99) and IMF *Government Finance Statistics* Yearbooks (1970–99)
Health spending	Government expenditure on health as percentage of total government expenditure	IMF *Government Finance Statistics*, various years
Housing spending	Government expenditure on housing as percentage of total government expenditure	IMF *Government Finance Statistics*, various years
ILOCNV	Cumulative number of ILO conventions ratified by a country	Rama and Artecona (2002) and www.national-academies.org/internationallabor
Wages and salaries spending	Government employment contributions as percentage of total government expenditure	IMF *Government Finance Statistics*
Social security and welfare spending	Government expenditure on social security and welfare as percentage of total government expenditure	IMF *Government Finance Statistics*
Tertiary education spending	Expenditures on tertiary education as percentage of GDP; tertiary expenditure per student per GDP per capita also included	World Bank World Development Indicators (CD-ROM)

Appendix J: Cluster results minus outcome variables

		Commodification			Decommodification					
	Country	Primary and secondary education spending	Health spending	*Country average*	Housing spending	ILO conventions	Wages and salaries spending	SS and welfare spending	Tertiary education spending	*Country average*
Cluster 1 (productive)	Chile	2	10	*6*	7	7	3	10	2	*6*
	Colombia	7	9	*8*	5	8	2	4	3	*4*
	Costa Rica	5	10	*8*	1	7	10	8	5	*6*
	Cyprus	9	5	*7*	6	7	6	9	1	*6*
	Israel	9	6	*8*	8	6	1	9	4	*6*
	Kuwait	9	3	*6*	6	3	4	5	9	*5*
	Malaysia	8	4	*6*	9	3	5	3	8	*6*
	Mauritius	7	8	*8*	7	4	7	7	9	*7*
	Panama	4	10	*7*	6	9	9	9	4	*7*
	Paraguay	2	4	*3*	5	5	9	6	7	*6*
	Singapore	5	5	*5*	9	3	6	1	5	*5*
	South Korea	6	1	*4*	4	1	1	5	1	*2*
	Sri Lanka	7	3	*5*	3	4	3	7	8	*5*
	Thailand	6	8	*7*	6	2	7	1	3	*4*
	Trinidad and Tobago	3	8	*6*	10	2	9	7	7	*7*
	Cluster average	***6***	***6***	*6*	***6***	***5***	***5***	***6***	***5***	*5*
Cluster 2 (dual)	Argentina	6	1	*4*	3	9	4	10	2	*6*
	Brazil	2	5	*4*	1	10	1	9	5	*5*
	Mexico	1	2	*2*	4	10	4	8	3	*6*
	Uruguay	4	4	*4*	1	10	2	10	3	*5*
	Greece	3	7	*5*	3	9	4	8	2	*5*
	Cluster average	***3***	***4***	*4*	***2***	***10***	***3***	***9***	***3***	*5*
Cluster 3 (protective)	Bolivia	1	3	*2*	2	6	7	8	6	*6*
	Dominican Republic	1	9	*5*	10	4	5	2	1	*4*
	Egypt	8	2	*5*	8	8	4	4	6	*6*
	El Salvador	1	9	*5*	5	1	10	3	1	*4*
	India	4	1	*3*	8	5	1	2	8	*5*
	Iran	3	7	*5*	9	1	10	5	7	*6*
	Lesotho	10	9	*10*	5	1	7	1	10	*5*
	Morocco	10	2	*6*	2	6	8	4	8	*6*
	Tunisia	9	6	*8*	7	8	7	6	9	*7*
	Turkey	5	3	*4*	3	5	9	2	5	*5*
	Zambia	2	6	*4*	2	6	2	1	10	*4*
	Zimbabwe	10	6	*8*	10	1	8	5	10	*7*
	Cluster average	***5***	***5***	*5*	***6***	***4***	***7***	***4***	***7***	*6*

Appendix K: Dendrogram for cluster analysis

Figure K.1 presents graphically the information concerning which countries are grouped together at various levels of dissimilarity. The vertical lines extend upwards for each observation, while the horizontal line connects to the lines from other observations at various dissimilarity values. The observations continue to combine until they are all grouped together at the top of the dendrogram. Significantly, the dendrogram gives visual clues about the strength of the clustering. Shorter vertical lines represent groups that are more similar to each other (e.g. Argentina and Uruguay; India and Bolivia; Morocco and Egypt), while longer lines indicate that these groups are more distinct from each other.

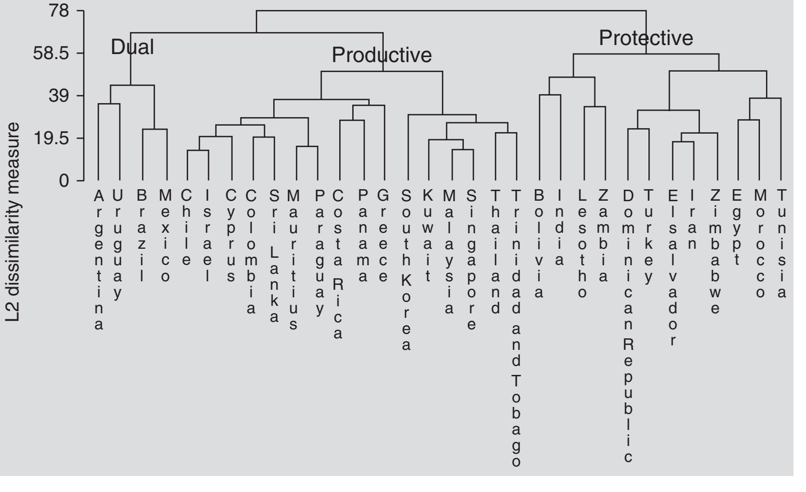

Figure K.1 Dendrogram for cluster analysis

Note: Weighted average linkage.

Appendix L: Poverty tables

Table L.1 *Poverty gap at $1 a day (PPP) (percent)*

Country	Poverty
Chile	0.5 (2000)
Colombia	3.07 (2003)
Costa Rica	0.8 (2001)
Cyprus	–
Greece	–
Israel	–
Kuwait	–
Malaysia	–
Mauritius	–
Panama	2.26 (2002)
Paraguay	7.384 (2002)
Singapore	–
South Korea	–
Sri Lanka	0.84 (2002)
Thailand	0.5 (2002)
Trinidad and Tobago	–
Argentina	–
Brazil	–
Mexico	–
Uruguay	0.5 (2004)
Bolivia	13.55 (2002)
Dominican Republic	0.77 (2003)
Egypt	0.5 (2000)
El Salvador	9.346 (2002)
India	8.2 (2000)
Iran	–
Lesotho	–
Morocco	–
Tunisia	0.5 (2000)
Turkey	0.79 (2004)
Zambia	36.398 (2002)
Zimbabwe	–

Notes: The "poverty gap" is the mean shortfall from the poverty line (counting the non-poor as having zero shortfall), expressed as a percentage of the poverty line, calculated on a purchasing power parity (PPP) basis. This measure reflects the depth of poverty as well as its incidence. Data showing as 0.5 signify a poverty gap of less than 0.5 percent. "Poverty" is defined as the population living below the national poverty line (1990–2002).
Source: World Bank, World Development Indicators.

Table L.2 *Poverty headcount ratio at $1 a day (PPP) (percentage of population)*

Country	Poverty
Chile	2.0 (2000)
Colombia	7.03 (2003)
Costa Rica	2.22 (2001)
Cyprus	–
Greece	–
Israel	–
Kuwait	–
Malaysia	–
Mauritius	–
Panama	6.52 (2002)
Paraguay	16.37 (2002)
Singapore	–
South Korea	–
Sri Lanka	5.552 (2002)
Thailand	2.0 (2002)
Trinidad and Tobago	–
Argentina	–
Brazil	–
Mexico	–
Uruguay	2.0 (2003)
Bolivia	23.2 (2002)
Dominican Republic	2.52 (2003)
Egypt	3.08 (2000)
El Salvador	19.04 (2002)
India	34.7 (2000)
Iran	–
Lesotho	–
Morocco	–
Tunisia	2.0 (2000)
Turkey	3.412 (2002)
Zambia	75.84 (2002)
Zimbabwe	–

Notes: The "Population below $1 a day" is the percentage of the population living on less than $1.08 a day at 1993 international prices. As a result of revisions in PPP exchange rates, poverty rates cannot be compared with poverty rates reported previously for individual countries. Data showing as 2.0 signify a poverty rate of less than 2.0 percent. "Poverty" is defined as the population living below the national poverty line (1990–2002).
Source: World Bank, World Development Indicators.

Table L.3 *Population living below $1 a day (1990–2003) (percentage)*

Country	Poverty
Chile	<2
Colombia	8.2
Costa Rica	2
Cyprus	–
Greece	–
Israel	–
Kuwait	–
Malaysia	<2
Mauritius	–
Panama	–
Paraguay	16.4
Singapore	–
South Korea	<2
Sri Lanka	5.552 (2002)
Thailand	2.0 (2002)
Trinidad and Tobago	–
Argentina	3.3
Brazil	8.2
Mexico	9.9
Uruguay	<2
Bolivia	14.4
Dominican Republic	<2
Egypt	3.1
El Salvador	31.1
India	34.7
Iran	<2
Lesotho	36.4
Morocco	<2
Tunisia	<2
Turkey	<2
Zambia	63.7
Zimbabwe	56.1

Note: "Poverty" is defined as the population living below the national poverty line (1990–2002).
Source: UNDP, *Human Development Reports*, various years.

Table L.4 *Population living below the national poverty line (1990–2002) (percentage)*

Country	Poverty
Chile	17
Columbia	64
Costa Rica	22
Cyprus	–
Greece	–
Israel	–
Kuwait	–
Malaysia	15.5
Mauritius	10.6
Panama	–
Paraguay	21.8
Singapore	–
South Korea	–
Sri Lanka	–
Thailand	13.1
Trinidad and Tobago	–
Argentina	–
Brazil	17.4
Mexico	10.1
Uruguay	–
Bolivia	62.7
Dominican Republic	28.6
Egypt	16.7
El Salvador	48.3
India	28.6
Iran	–
Lesotho	49.2
Morocco	19
Tunisia	7.6
Turkey	–
Zambia	72.9
Zimbabwe	34.9

Source: UNDP, *Human Development Reports*, various years.

Appendix M: Social expenditures on social security, health, and education in India (percent of GDP) based on national data

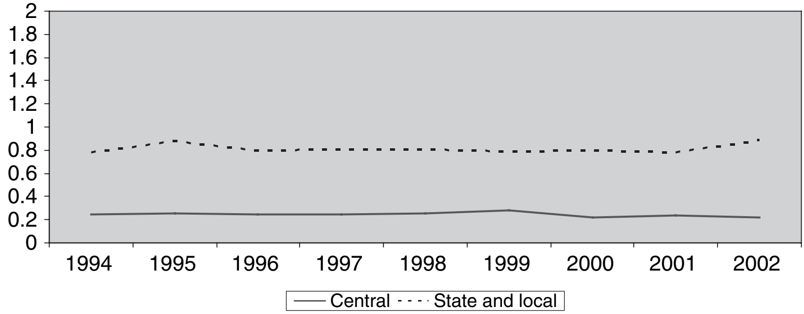

Figure M.1 Social security and welfare spending as a percentage of GDP, 1994–2002

Source: Ministry of Finance (2004).

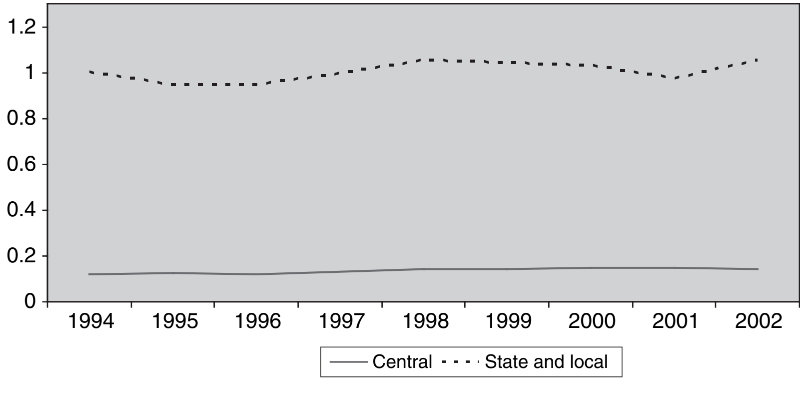

Figure M.2 Health spending as a percentage of GDP, 1994–2002

Source: Ministry of Finance (2004).

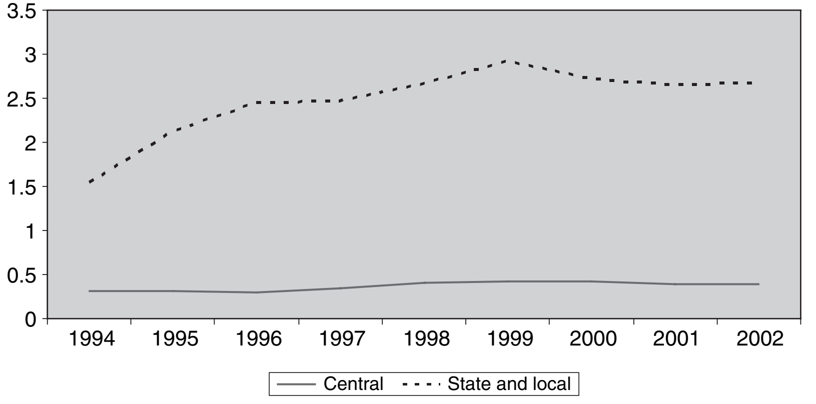

Figure M.3 Education spending as a percentage of GDP, 1994–2002
Source: Ministry of Finance (2004).

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