Welfare States and the Economy

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The literature on welfare states or, more modestly, systems of social protection, has expanded rapidly over the past few decades. Since the publication of the first edition of this Handbook, major progress has been made in three research areas: the relationship between welfare states and production regimes, gendered determinants and outcomes of welfare state regimes, and the distributive outcomes of welfare states. Esping-Andersen ended his chapter in the first edition with a call for an embedded approach to the study of welfare states, for a relational analysis of the welfare state – economy nexus. Two developments have contributed to the advancement of such an approach: progress in research on production regimes in advanced industrial societies, and the dramatic impact of economic transformations on the systems of social protection in ex-communist countries and in Latin America. Progress in research on the gender dimension of the welfare state- economy nexus has been spurred by changes in demographic structures, particularly falling fertility rates and the decline of the traditional male breadwinner family that had been at the center of many welfare state programs. Finally, progress in research on distributive outcomes has been heavily driven by the greater availability of reliable and comparable data and new statistical techniques, specifically the Luxembourg Income Surveys and techniques for the analysis of unbalanced panel data.

Of course, the progress made in the 1990s was possible because researchers could build on knowledge accumulated by previous studies of welfare states, spanning a quarter century. These earlier studies had taken the form of quantitative analyses on the one hand and case studies or comparative analyses of a small number of cases on the other hand. The former had begun with a focus on the determinants of welfare state expenditures (Wilensky 1975, Stephens 1979; Korpi 1983) and gradually added measures of specific benefits and public employment (Myles 1984, Pampel and Williamson 1989). The latter progressed from comparing welfare states in two or three countries or individual welfare state programs in a larger number of countries to studying configurations of programs or welfare state regimes in the universe of advanced industrial democracies (Esping-Andersen 1990).

Theories of Welfare State Formation and Retrenchment

Theories of welfare state formation can be grouped into three categories, according to the emphasis they put on clusters of causal variables: the "logic of industrialism," "state-centric," and "political class struggle" approaches.[1] The authors proposing the logic of industrialism approach argued that industrialization and urbanization broke up traditional systems of social protection through the family and local communities and required the state to take on the responsibility for the welfare of industrial workers. At the same time, the growing affluence resulting from advances in industrialization made the resources available to the state to perform these functions. Thus, both the growth and cross-national differences in welfare state effort could be explained by industrialization and its demographic and social organizational consequences (Wilensky 1975; Pampel and Williamson 1989). A related influential point of view held that economic openness caused vulnerability of workers to external shocks and thus led governments to build extensive systems of social protection (Cameron 1978). Since small countries generally had a higher degree of economic openness, welfare states grew particularly generous there (Katzenstein 1985).

The state-centric approach is internally quite diverse, with some authors focusing on the initiatives of state bureaucrats who were assumed to have a high degree of autonomy (Heclo 1974), and others on state capacity, state structure, and policy legacies (Skocpol 1988; Weir, Orloff, and Skocpol 1988; Immergut 1992; Orloff 1993a; Amenta 1998; Maioni 1998). In this perspective, cross-national differences in the development of comprehensive welfare state programs are a result of differential state capacity, the degree of power dispersion and the consequent availability of veto points, and the structure of welfare state programs set at their origin, before the period of expansion.

The political class struggle approach – also known as power resources approach (Korpi 1980, 1983) – is based on the premise that state policy is heavily shaped by the distribution of power in civil society and in government. The balance of power between organized labor and left-wing parties on the one hand, and capital and center and right-wing parties on the other hand accounts for the extent of government correction of market outcomes through the welfare state (Stephens 1979; Castles 1982; Hicks and Swank 1984; Myles 1984; Esping-Andersen 1985, 1990; Korpi 1989). The focus on incumbency produced early on the insight that Christian democracy is also associated with generous welfare states but with a less progressive profile than welfare states built under left or social democratic auspices (Stephens 1979; Wilensky 1981).

There is some theoretical overlap among these perspectives. The political class struggle perspective emphasizes density and centralization of labor organization, and centralization of collective bargaining, along with strength of pro-labor parties as indicators of left/ labor power. Density and centralization of labor organization, or labor strength, is also seen as a cause of corporatism, that is, institutionalized tripartite consultation between capital, labor, and the government on essential policy issues (Stephens 1979; Western 1991). Corporatism, then, has been treated as an institutional variable that, once established, becomes a cause of welfare state expansion in its own right (Hicks 1999; Swank 2002; Wilensky 2002). Since these dimensions of left/ labor power are so closely related, it is impossible to adjudicate the competing theoretical

[1] For a recent review of political theories of the welfare state see Myles and Quadagno (2002).

claims on statistical grounds. Comparative historical evidence indicates that incumbency of left parties is crucial for welfare state development (Huber and Stephens 2001a).

Quantitative studies have found that variables emphasized in all three theoretical schools are statistically significant predictors of welfare state effort (Huber, Ragin and Stephens 1993; Hicks 1999; Swank 2002). Demographic variables matter because, at any given level of entitlements, a larger number of old people or unemployed drive up expenditures. Level of GDP per capita, as a measure of economic development, tends not to explain much variation in welfare state effort among advanced industrial democracies, but if the comparison encompasses developing countries, then its importance increases. The provision of multiple veto points in the constitutional structure, that is, dispersion of power through presidentialism, strong bicameralism, federalism, and popular referenda, is one of the most consistent and important obstacles to expansion of welfare state effort (Huber and Stephens 2001a). Finally, the strength of organized labor and length of incumbency of left-wing or Christian democratic parties is associated in a highly consistent and significant manner with various dimensions of welfare state effort.

Focusing on dimensions of welfare state effort, or on social rights directly, rather than simply on aggregate welfare state spending, was the key to Esping-Andersen's (1990) seminal contribution of the concept of welfare state regimes. He built on other, in part common, efforts to measure social rights and explain their determinants (Myles 1984; Korpi 1989), and he identified different dimensions or characteristics of the way in which welfare states provide social rights. He argued that these dimensions or characteristics were linked in systematic patterns and clustered around three types, a social democratic or institutional type, a conservative or "corporativistic" type, and a liberal or residual type. With some modifications, specifically the renaming of the conservative as Christian democratic type and the addition of a fourth wage earner welfare state regime (Castles and Mitchell 1993) and sometimes a fifth Southern European regime (Leibfried 1992; Ferrera 1996), this welfare state regime typology has shaped most subsequent research.

Social democratic welfare state regimes are characterized by universalism in coverage and in the nature of benefits, by rights to a large array of benefits based on citizenship or (more recently) residence, and by public provision of a large array of services. Christian democratic welfare states are characterized by universalism in coverage but (at least historically) with different benefits under different programs, by rights to benefits based on employment categories, and by public financing of privately provided services. Liberal welfare states are characterized by partial or residual coverage with different benefits, by rights to most benefits based on need and thus means testing, and by the scarcity of publicly provided or financed social services. These regime types correspond to value commitments and particular views on the desirable relationship between state, market, community, and family. The social democratic type reflects the values of solidarity and equality, and the view that the state is charged with counteracting market forces to realize these values. The Christian democratic type reflects the Catholic doctrine of harmony and subsidiarity, where the state is charged with keeping people out of poverty but not changing the social order, and with performing only the functions that are not performed well by the family or civil society (van Kersbergen 1995). The liberal type reflects the values of individual responsibility and efficiency, and the view that the state should primarily rely on market forces and work with these forces to prevent destitution and provide essential social services. The groups of countries corresponding to the three regime types are the Nordic countries, the continental European countries, and the Anglo-American countries, respectively. In reality, of course, several countries have somewhat mixed welfare state characteristics, reflecting the influence of different political forces involved in their formation.

The main theoretical contribution from a feminist perspective was to draw attention to the fact that these welfare state typologies were essentially built on the assumption of standard citizens, with low, average, or high earnings, and that this assumption fit predominantly males. Gender did not figure as a dimension in the original conceptualization of welfare state regimes, and it was obviously crucial to understand gender specific impacts of these regimes (Orloff 1993b). A number of studies have investigated the extent to which regime types are useful in explaining systematic differences in outcomes for women (Lewis 1992; Hobson 1994; Orloff 1997; Sainsbury 1999), and though there is no real consensus, there is considerable evidence supporting the usefulness of the regime approach. Numerous studies have also investigated the role of women's mobilization and pressures for welfare state expansion or what Hernes (1987) called women-friendly policies (Jenson and Mahon 1993; Lewis 1994; Hill and Tigges 1995; Stetson and Mazur 1995; Hobson and Lindholm 1997; Bergquist 1998; O'Connor, Orloff, and Shaver 1999). Most of their findings are compatible with a power resources approach, but power based on gender mobilization, not on class. Generally, progress in policies promoting gender equity was the result of women organizing inside and outside of political parties, in independent women's movements, and fostering a commitment to the goal of gender equity within incumbent left-wing parties.

Whether the traditional theories of welfare state formation are also useful for an analysis of the period of welfare state retrenchment or defense, which began in the 1980s, is a contested issue. Pierson (1994, 1996) has argued for a "new politics of the welfare state," and indeed quantitative studies have shown that the magnitude of partisan effects decreased greatly (Stephens, Huber and Ray 1999). In the context of slower economic growth than in the first three post-WW II decades, higher unemployment, comprehensive and mature welfare state programs and consequent high expenditures, both the left and the right have been constrained in their reform efforts. The right has been constrained in efforts to cut welfare state entitlements significantly, because the entitlements that affect large numbers of people are widely popular. The left has been constrained in efforts to expand entitlements because raising taxes has not been popular and deficit financing out of the question. Still, in qualitative studies differences between governments of different color remain visible; right-wing governments have been more likely to push an agenda of welfare state austerity and tax cuts, whereas left-wing governments have been more intent on protecting entitlements (Huber and Stephens 2001a). Demographic and state structure variables have remained important as well, but have tended to work in the opposite direction from the one during the period of welfare state expansion. Whereas multiple veto points had slowed down expansion, now they have slowed down retrenchment (Bonoli and Mach 2000). Whereas episodes of high unemployment had given the impetus for improvements in unemployment insurance, now sustained levels of higher unemployment have given the impetus for cuts in entitlements.

Among the developing areas of the world, Latin America has seen the strongest thrust towards welfare state development. At least the most advanced countries had built systems of social protection by 1980 that could be called welfare states.[2] The volume of literature on the formation of welfare states in Latin America is small, and a theoretical debate is largely absent. There is a sizable number of studies that describe the evolution of systems of social protection, but they tend to focus on economic and organizational aspects and neglect the question why systems were formed in a certain way (Mesa-Lago 1978, 1989; Raczynski 1994). The picture that emerges from these studies is one of highly fragmented and often inegalitarian systems, where entitlements were based on the insurance principle and differed greatly between occupational categories. The main programs were old age and disability pensions and health care insurance, and in some countries family allowances. These systems resembled the Christian democratic type characteristic of continental Europe, but were much less generous and more inegalitarian and restricted in coverage. Coverage depended on employment in the formal sector, and the rural and informal sectors were very large in most of these countries, with the result that in the vast majority of countries less than 60% of the population had coverage as of 1980.

Most studies of social policy formation emphasize preemptive, or paternalistic action on the part of the state to incorporate the most important occupational groups and gain their political support (Mesa-Lago 1978; Malloy 1979; Spalding 1978). Another perspective emphasizes diffusion of models of social insurance from more advanced countries via international organizations, particularly the International Labor Office (ILO) (Collier and Messik 1975). However, there was clearly differential adoption of these models, and this variation needs to be explained. Even under authoritarian rule, the strength and political importance of pressure groups mattered, and thus to understand the expansion of social protection to a large part of the population, the mobilization capacity of organized labor and its importance as a support base of governments have to be taken into account (Dion 2002). Coverage expanded most during periods of strong growth of import substitution industrialization (ISI) behind high tariff walls and with strong government intervention in capital markets to support industrialization. These were periods of growth of the industrial labor force and often also of labor movements. Labor organization and mobilization is most likely to grow under democratic regimes, specifically in the presence of strong reformist parties, and/or

[2] In Asia, Japan belongs to the set of advanced industrial countries, but lagged behind in welfare state development. A large part of the social safety net was based on employment in large corporations, which included some 25-30% of the work force, and on redistribution of benefits through the family. Despite the establishment of national pension and health insurance programs in the 1960s and a push for welfare state expansion in the 1970s, public social expenditures remained low compared to those of other advanced industrial societies. In the East Asian newly industrialized countries, serious efforts to establish national welfare state programs began only in the 1970s (Korea) or in the 1980s (Taiwan) (Goodman and Peng 1996; Pempel 2002). In other East Asian countries, public welfare state efforts came similarly late and remained low (Haggard and Kaufman 2002).

under authoritarian leaders who deliberately promote labor organization.[3] Indeed, of the five Latin American countries (not counting Cuba) with most extensive coverage of social security, that is, above 60% of the population as of 1980, three had the longest democratic experiences and comparatively strong reformist parties (Uruguay, Chile, Costa Rica) and two had historical episodes of leaders attempting to build organized labor into a power base (Perón in Argentina, Vargas in Brazil). Compared to Europe, then, the much lower size and generosity of Latin American systems of social protection can be attributed to a combination of lower levels of industrialization, the scarcity of democratic periods, and the weaker position of reformist parties and organized labor.[4]

Theoretical accounts of retrenchment of systems of social protection in Latin America, which has been much more dramatic than in advanced industrial democracies, have emphasized the debt crisis and consequent economic transformations as common causes. They have explained differences between countries in the extent and nature of social policy reforms with the extent of liberalization of markets for goods and capital, power concentration in the hands of the executive versus fragmentation of political institutions and power, the influence of international financial institutions (IFIs), specifically the International Monetary Fund, the World Bank and the Inter-American Development Bank, the financial pressures on the established systems, policy legacies, and the balance of power between proponents (large capital interests, technocrats, executives) and opponents (organized labor, pensioners, the political left) of reforms, with emphasis on these different factors varying by author (Weyland 2002; Huber 1996, forthcoming; Kay 1998; Madrid 2002; Dion 2002).

A final theoretical perspective to be considered is the economic one. This literature does not really address theoretical questions of the causes of welfare state formation and of cross-national differences in welfare state design. The classical liberal and neoliberal perspectives take a normative position, that market allocation should not be distorted by state intervention, and they claim that there is a fundamental trade-off between equity and efficiency (Okun 1975). In particular, they argue that state intervention and redistribution distort incentives and thus efficiency of resource allocation (Lindbeck 1994). Less dogmatic economists distinguish between the goals of welfare states, which they attribute to the realm of politics or norms, and the means by which these goals are to be achieved, which they regard as a technical question and the proper field of study for economics (Barr 1998). There is considerable research on the work disincentive effects of generous social safety nets in the case of sickness and unemployment, but the findings are often ambiguous and mostly weak (Atkinson and Mogensen 1993; Atkinson and Mickelwright 1991).

[3] We choose the term “reformist” to include all left of center parties, ranging from mildly social democratic to radical left.

[4] Haggard and Kaufman (2002) emphasize primarily regime type and secondarily strength of left-of-center parties, but discount strength of labor movements in their analysis of welfare state expansion in Latin America.

Welfare States, Production Regimes, and Globalization

As we have mentioned, by the early 1990s, a number of authors had noted that there was strong affinity and perhaps a causal relationship between corporatism, often indexed by the degree of bargaining centralization, and welfare state generosity. Esping-Andersen (1990) and Kolberg and Esping-Andersen (1992) drew attention to other links between labor market arrangements and welfare state types: high levels of public social service employment and of female labor force participation in the social democratic welfare states, high levels of private service employment in liberal welfare states, low levels of service employment and female employment in Christian democratic welfare states, and high levels of early retirement in Christian democratic welfare states. In the course of the 1990s, a new line of thinking, the varieties of capitalism approach, emerged which stressed other dimensions of variation among advanced capitalist economies (e.g. Soskice 1990, 1999, Albert 1991, Hollingsworth, Schmitter, and Streek 1994, Hollingsworth and Boyer 1997).

The most influential typology has been that of Soskice (1999, Hall and Soskice 2001). Soskice shifts from the focus on unions and union confederations characteristic of the corporatism literature to a focus on employers and firms and their capacity to coordinate their actions. In his view, employer organization takes three distinctive forms: coordination at the industry or sub-industry level in Germany and in most northern European economies (industry-coordinated market economies; CMEs); coordination among groups of companies across industries in Japan and Korea (group coordinated market economies); or absence of coordination in the deregulated systems of the Anglo-American countries (liberal market economies; LMEs). In coordinated economies, employers are able to organize collectively in training their labor force, sharing technology, providing export marketing services and advice for R&D and for product innovation, setting product standards, and bargaining with employees. The capacity for collective action on the part of employers shapes stable patterns of economic governance encompassing a country's financial system, its vocational training, and its system of industrial relations. In liberal market economies, in contrast to both types of coordinated economy, training for lower level workers is not undertaken by private business and is generally ineffective. Bank - industry ties are weak and industries have to rely on competitive markets to raise capital.

It is obvious that theses types of production regimes are associated with Esping-Andersen's types of welfare state regimes. Moreover, it is arguable that there is at least a "mutually enabling fit" between the welfare state and production regimes types (Huber and Stephens 2001a: Chapter 4): Specifically, wage levels and benefit levels have to fit, and labor market and social policies have to be in accord such as not to create perverse incentives. In addition, the type of production for the world market has to fit with the qualification of the labor force and with wage and benefit levels. In CMEs, business/ labor/ government coordination in R&D, training, and wage setting makes it possible to engage in high quality production and thus to sustain high wages and a high social wage.

Recent work suggests an even tighter fit between welfare state and production regimes. Iversen and Soskice (2001) argue that the industry and firm specific nature of many of the skills acquired in vocational education systems characteristic of CMEs results in higher support for social spending as workers with these skills are vulnerable to longer spells of unemployment and to loss of income if forced to move between jobs with different skill requirements (also see Estevez-Abe et al. 2001). In their view, employers as well as workers have an interest in such social spending because it insures that worker will in fact invest in acquisition of the specific skills which the employers require. Swenson (2002) also argues that the varying interests of cross class coalitions of employers and workers account for differences in social policy. He argues that in Sweden employers and workers both supported the expansion of social insurance because social insurance removes private employer benefits from wage competition.

This recent work would appear to sharply conflict with power resources theory, which is widely perceived by comparative welfare states specialists (e.g. see Orloff 1993b; Myles and Quadagno 2002) to be the currently dominant explanation of welfare state development. This is a dispute that is unlikely to be resolved by statistical analysis because of the strong intercorrelations between the potential causal factors. The centralization of employer confederations, the centralization of union confederations, union density, long term patterns of partisan government, the extent of vocational education, and various measures of welfare state effort are moderately to strongly correlated to each other and the multiple correlations of two or three of these indicators with another of them are invariably extremely high.

The resolution of this debate will have to await the kind of careful comparative historical work which has been done on the development of the welfare state but which has not been done on the development of production regimes. Thelen's (forthcoming a) work on the development of vocational training in Germany, Britain, Japan, and the US is probably indicative of the kind of answers such analyses will reveal. For example, she finds that the German employers initially introduced the system with the intention of dividing the nascent working class movement, but that over the course of the past hundred odd years the system has been progressively transformed by shifting coalitions of labor market and political forces. [5] The functional fit one observes by taking a single cut in time is, she argues, quite misleading. It is our hunch that the early organization of employers will figure as an important factor in the development of coordinated market economies, as employer organization as of 1914 identifies post World War II CMEs quite well (Crouch 1993: 112, also see Hicks 1999: Chapter 5). In dialectical fashion, employer organization seems to have stimulated union organization and centralization which in turn increased the political strength of the left at a later period of time (Stephens 1979, Kjellberg 1983). In the post war period, left party power facilitated union organization and vice versa (Western 1997, Wallerstein 1989), and these two factors in turn propelled welfare state expansion. This kind of causal account squares much better with the historical record of consistent right-wing (the parties representing employer interests) opposition to tax increases for welfare state financing than accounts stressing employer-worker coalitions in support of the welfare state.

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[5] For a general exposition of the analytical strategy she pursues, see Thelen (forthcoming b).

It is important not to exaggerate the fit between welfare state and production regime. Above all, CMEs are equally compatible with social democratic or Christian democratic welfare states, and these two welfare state types have distinctive characteristics which have a major impact on their future viability. As we have noted in passing above, the social democratic welfare states are characterized by very high levels of public health, education, and welfare (HEW) employment. This high level of public HEW employment is both a result and cause of the high levels of women's labor force participation. The growth of women's labor force participation beginning in the 1960s stimulated demands by women for the expansion of day care and other social services which, along with social democratic governance, helped fuel the growth of public social service sector employment. These public social service jobs were filled very disproportionately by women, so this in turn stimulated a further expansion of women's labor force participation. The continental Christian democratic welfare states followed a quite different trajectory. Foreign labor was imported in large numbers, arguably due to a combination of Christian democratic emphasis on the traditional male breadwinner family and weaker union influence on labor recruitment policies. Moreover, in these countries, union contracts cover a large proportion of the labor force, which prevented a rapid expansion of a low wage service sector, a source of employment for women in liberal welfare states (Esping-Andersen 1990). As a result, women's labor force participation was the lowest in the continental Christian democratic welfare states of the three welfare state types.

A related difference between social democratic and Christian democratic welfare states is the much greater emphasis on active labor market measures as a response to unemployment in the social democratic welfare states. By contrast, as mentioned above, the Christian democratic welfare states have tended to resort to labor supply reduction measures, such as early retirement and easy access to disability pensions, in response to rising unemployment after 1973. Together these policy differences have resulted in much higher levels of labor force participation of both men and women in social democratic welfare states.

Australia and New Zealand are generally classified as liberal market economies and liberal welfare states in the varieties of capitalism and welfare state literatures, which is a correct characterization of the contemporary political economies of these countries. However, prior to the reform process initiated in the early eighties, these countries had distinctive systems of social protection, as Castles (1985) has argued. In the nineteenth century, these countries' economies were dominated by exports from the pastoral sector, later to be supplemented by mineral exports in the Australian case. The industrial sector developed behind high tariff barriers, thus these political economies were ISI economies similar to Latin America. In the early twentieth century, the labor movements of these countries, which were very powerful by international standards, secured systems of compulsory arbitration which delivered high "male breadwinner" wages and later benefits such as sickpay, which in other advanced capital countries were delivered by the welfare states. Thus, these two countries resembled Latin America, as formal sector urban workers received comparatively high wages and benefits due to protective tariffs, with the important difference that the informal sector was quite small compared to Latin America.

Production regimes in Latin America were characterized by extensive state intervention in all areas of economic life up to the 1980s. As a result of the Depression, governments in the more advanced Latin American countries had become convinced that they needed to promote domestic industrialization. They did so through high protective tariffs, subsidized credit from state development banks, preferential allocation of foreign exchange, and other kinds of incentives. Of course, ISI required significant imports of capital goods and other industrial inputs, which were financed by raw material exports. There were differences in the timing of ISI and in the extent of state involvement, but virtually all countries followed this model by the late 1960s. The social security systems for disability and old age pensions and for health care developed in tandem with ISI, as governments also became heavily involved in regulating labor relations and saw social security as a tool to foster labor compliance. Financing depended heavily on employer contributions, which were tolerable because they could be passed on to consumers in these highly protected markets. However, only in Uruguay did the percentage of the labor force in industry surpass 30% by 1980; in seven more countries the percentage was between 20 and 30%, and in the rest even lower (World Bank 1982). Since most of agriculture and the entire large informal part of the service sector were without coverage, this is a good gauge of the restricted reach of social protection.

In the last two decades, almost all advanced welfare states have experienced at least some retrenchment, reversing the trend of the previous three decades, which was one of unprecedented welfare state growth in all of these countries. Many journalists and political observers and some academics, particularly economists, have attributed this retrenchment to "globalization," the increasing economic openness of the national economies and integration of the world economy. In this view, the emergence of a single global market and global competition has reduced the political latitude for action of national states and imposed neo-liberal policies on all governments. Proponents contend that as markets for goods, capital, and more recently labor, have become more open, all countries have been exposed to more competition and the liabilities of state economic intervention and deviation from market oriented "best practices" have become more apparent because these raise the cost of production. As capital markets have become more open and capital controls increasingly unworkable, capital in these countries moves elsewhere in search of lower production costs. Thus, governments must respond and reduce state intervention to stem the outflow of capital. There is also a social democratic version of the globalization thesis, essentially an extension of the structural dependence of the state on capital argument. In this view, the opening of international capital markets beginning in the 1970s and accelerating in the 1980s and 1990s greatly increased the power of capital to do "regime shopping" and thus to force national states to retreat from effective interventionist policies and generous, egalitarian welfare state policies.

There is very little empirical evidence to support the neo-liberal version of the globalization thesis (Garrett 1998, Swank 2002). The generous welfare states of northern Europe were developed in economies which were always very open to trade and very dependent on exports. Thus, for example, in the mid-nineties, at the very moment when the German and Swedish governments were cutting welfare state benefits, albeit modestly, the German and Swedish export sectors were turning in outstanding performances. The absence of any relationship between exposed sector employment performance and the level of taxes and social security contributions also argues against the thesis that generous welfare states makes export industries uncompetitive (Scharpf 2000: 78).

On the other hand, there is some evidence in favor of the social democratic version of the globalization thesis. To identify the causes of retrenchment, we draw on case studies of twelve countries (Huber and Stephens 2001a: Chapter 7; Stephens, Huber, and Ray 1999) as well as studies of additional countries in Scharpf and Schmidt (2000), thus covering all but a few of the advanced industrial democracies. These country studies indicate two different dynamics: ideologically driven cuts, which occurred in only a few cases, and unemployment driven cuts, which were pervasive. The question then becomes what caused the increases in unemployment? [6] As Glyn (1995) points out, it was not the low level of job creation, since employment growth after 1973 was as rapid as before. Rather, rising labor force participation due to the entry of women into the labor force is one proximate cause of the increase in unemployment. As mentioned previously, the inability of the Christian democratic welfare states to absorb this increase either through an expansion of low wage private service employment as in the liberal welfare states or through the expansion of public services as in the social democratic welfare states is one reason why the unemployment problem in these countries has been particularly severe. The other proximate cause is the lower levels of growth in the post 1973 period. This in turn can be linked in part to lower levels of investment which in turn can be linked in part to lower levels of savings, to lower levels of profit, and to higher interest rates.

It is on this point that we find some support for the social democratic globalization thesis on the negative impact of financial market deregulation. Real interest rates increased from 1.4% in the sixties to 5.6% in the early nineties (OECD 1995: 108). The deregulation of international and domestic financial markets is partly responsible for this increase in interest rates.[7] As a result of the elimination of controls on capital flows between countries, governments cannot control both the interest rate and exchange rate. If a government decides to pursue a stable exchange rate, it must accept the interest rate which is determined by international financial markets. As a result of decontrol of domestic financial markets (which was in many cases stimulated by international financial deregulation), government's ability to privilege business investors over other borrowers also became more limited. Countries which relied on financial control to target business investment were particularly hard hit as businesses moved from a situation in which real interest rates offered to them via government subsidies, tax concessions, and regulations were actually negative to a situation in which they had to pay the rates set by international markets. External financial decontrol also limits a government's ability to employ fiscal stimulation as a tool, as fiscal deficits are considered risky by financial markets and either require a risk premium on interest rates or put downward pressure on

[6] The following few paragraphs summarize our arguments in Huber and Stephens (2001a: Chapter 7).
[7] Another part of the reason is competition from non-OECD countries for investment funds (Rowthorn 1995) and the world wide debt build up in the wake to the two oil shocks.

foreign exchange reserves. Thus, at least a portion of the increase in unemployment can be linked to globalization in the form of deregulated capital markets.

There were only a few cases of large-scale ideologically driven cuts. The most dramatic were Thatcher in Britain, the National (conservative) government in New Zealand, and the Reagan administration in the United States. In the case of the Reagan administration the cuts were focused on cash and in kind benefits to the poor, a small but highly vulnerable minority, while Social Security was preserved by a large increase in the contributions. In any case, the United States cannot have been said to have made a "system shift" if only because it already had the least generous welfare state of any advanced industrial democracy. Only in Britain and New Zealand could one speak of an actual system shift from welfare state regimes that used to provide basic income security to welfare state regimes that are essentially residualist, relying heavily on means-testing. We argue that the exceptional nature of these two cases can be traced to their political systems which concentrate power (unicameral or very weakly bicameral parliamentary governments in unitary political systems) and make it possible to rule without a majority of popular support (single member districts and plurality elections which allow parties with a minority of votes to enjoy large parliamentary majorities). Thus, in both cases, the conservative governments were able to pass legislation which was deeply unpopular.

In contrast to welfare states in advanced industrial societies, globalization had a dramatic impact on systems of social protection in Latin America. Globalization was a major contributor to the debt crisis that spurred a transformation of the economies, a process largely guided by the international financial institutions, and economic transformation in turn required reforms of the traditional social security systems. The ISI model began to run into balance of payments problems in the 1950s. It was given a new lease on life in the 1970s because of the easy availability of cheap loans on the expanding international capital markets. However, these markets imposed rapidly rising interest rates in the early 1980s, at the same time as commodity prices fell. When the big international banks reacted to solvency problems of some major debtors with a complete stop of new lending, Latin America was plunged into the debt crisis (Dornbusch 1989). This crisis gave great leverage to the IFIs and the American Treasury, and these institutions pushed for a radical liberalization of the Latin American economies. They were influential not only through their imposition of conditionality on debt renegotiations (Stallings and Kaufman 1989; Kahler 1989), but also because of another aspect of globalization, the spread of educational circuits that brought talented Latin Americans to graduate schools in economics in the United States, where they absorbed the hegemonic neoliberal view of the world. Many of the leading government officials shared such backgrounds with officials in the IFIs, and many had worked for some time in the IFIs as well. This facilitated the formation of networks involving technocrats in the IFIS and national governments, where reform ideas were discussed over long periods of time and the neoliberal solutions were advocated (Teichman 2001).

At first, governments and IFIs were preoccupied with economic stabilization and structural adjustment, but by the late 1980s, when the costs of the crisis and the austerity and adjustment measures became clear, they developed an acute concern with the political sustainability of reforms and thus “adjustment with a human face.” The economic austerity programs entailed devaluation, reduction of public expenditures, wage freezes, and restrictive monetary policies. Together with the structural adjustment policies, they fundamentally transformed the Latin American production regimes. The main points of the structural adjustment agenda were liberalization of markets for goods and capital, privatization of state enterprises, and deregulation of all kinds of economic activity. On average, the countries in the region pushed ahead rapidly with trade liberalization and financial liberalization; less in privatization, and mixed in general deregulation. The average tariff rate was lowered from 49% in the mid-1980s to 11% in 1999, and non-tariff restrictions were reduced from covering 38% of imports in the pre-reform period to 6% of imports in the mid-1990s (Lora 2001). Though these tariff levels remain higher than in advanced industrial countries, the lowering had a dramatic impact on many Latin American economies, particularly where it was done in a very short period of time. Many enterprises went bankrupt, which meant that many formal sector jobs were lost. Liberalization of capital markets stimulated significant inflows of capital in the early 1990s, but also rendered the economies vulnerable to rapid changes in investor confidence and thus renewed balance of payments crises.

Social expenditures had decreased as part of the austerity programs. Unemployment had increased greatly due to austerity-induced recession and liberalization of imports. The combination of high inflation and high unemployment had played havoc with the financial base of the social security systems, and employers rebelled against high social security contributions in the new open economic environment.[8] The reforms pushed by the IFIs included privatization of the pension systems and large parts of the health care systems, decentralization of social services, and targeting of public expenditures on the poor, particularly through demand driven social emergency funds. The degree to which countries followed these prescriptions, though, varied greatly, more so than in the economic reforms proper.

Chile implemented these reforms earlier and to a greater extent than any other country under the military dictatorship. Power was highly concentrated in the hands of Pinochet and opposition was dealt with ruthlessly. The neoliberal project was attractive to the military not only for economic but also for political reasons, because it would atomize civil society and remove the state as a target for collective action (Garretón 1989). In addition to slashing tariffs and financial regulation and privatizing a large number of state controlled enterprises, the government fully privatized the pension system and transformed a large part of the public into a private health insurance and delivery system. The reduced public expenditures were targeted on preventive and nutritional programs and a temporary employment program for the poor (Raczynski 1994). In the wake of the high economic growth rates – and thus high rates of return on the individual private pension accounts – achieved in Chile from the mid-1980s to the mid-1990s, the Chilean model became the poster child for neoliberals and was held up as a model to emulate for other Latin American countries.

[8] Kaufman and Segura (2002), in a pooled cross-section and time series analysis of changes in social expenditure in Latin America, found a statistically significant negative effect of trade opening; in other words, the faster a country opened its economy, the more likely it was to lower social expenditure.

No other country carried out reforms quite as rapidly and comprehensively as Chile. Argentina under Menem moved very rapidly on economic reforms and on a plan to privatize social security, but opposition was strong enough to force concessions on keeping a public basic tier and leaving a large part of the health insurance system under the control of the unions. Altogether, nine Latin American countries have implemented and a tenth has legislated full or partial privatization of their pension system. In five cases, privatization was total and the public system was closed down; in five cases it was partial and the private system remained a supplementary or a parallel option (Muller 2002). Reforms in health care have been more heterogeneous, though in general the private sector has expanded its role, sometimes by design and sometimes by default as a result of serious underfunding of the public system. In the 1980s, there was virtually no investment in public health care facilities, and wages for public health care professionals declined precipitously. In the 1990s, most countries raised their social expenditures, so that they increased from 10.4% of GDP to 13.1% (CEPAL 2002), slightly above the level of 1980. Growth in the various categories of social expenditure, that is, education, health care and nutrition, social security, and housing and sanitation was roughly similar, with social security continuing to absorb the bulk of social expenditure, at 4.8% of GDP in 1998-99, followed by education with 3.9% and health care and nutrition with 2.9% (CEPAL 2002: 26). Clearly, these levels of expenditure remain far below what would be needed for a concerted and successful attack on poverty and improvement of the human capital base.

In order to raise expenditures significantly, tax collection systems would need to be improved. Latin America as a whole is clearly undertaxed, with an average tax burden of 14% of GDP in the first half of the 1990s, compared to 17% of GDP in a group of East and Southeast Asian countries (IADB 1996: 128). Tax reform has been part of structural adjustment, but it has emphasized lowering marginal tax rates for individuals and corporations and raising the value added tax. Tax collection rates are still very poor. Direct taxes amount to about 25% of tax revenue only, and of this amount some 60-80% come from corporate tax payments, while only 10-15% come from private individuals (CEPAL 1998: 72). Interestingly, the situation in the English-speaking Caribbean is very different, with an average tax burden in the first half of the 1990s of 27-28% of GDP, essentially double the rate of Latin America, and direct taxation accounting for 40% of tax revenue (CEPAL 1998: 66-72). This contrast suggests that the fundamental reasons for the poor tax collection performance in Latin America are political, rather than related to low levels of economic development and technological capacity.

Demography, Gender, and Welfare States

In contrast to the dominant view in the political debate that paints globalization as an inexorable force undermining the bases of the welfare state everywhere, the strongest current in the academic debate squares with our arguments about the limited impact of globalization on welfare states in advanced industrial societies. Instead, this current identifies domestic pressures, specifically changing demographics and changes in lifestyles and labor markets, as major factors that demand adaptation of welfare state structures now and will do so even more urgently in the future

(Esping-Andersen 1999; essays in Pierson 2001). The most obvious of these pressures is the growing share of the aged in the population. The growth in life expectancy has meant a higher share of pensioners and thus greater financial pressures on the pension and the health care systems. In the social democratic and the liberal welfare states increasing female labor force participation counterbalanced the growth of the aged population and actually improved the ratio between the economically active and the total dependent population, old and young, from 1960 to 1989. In the Christian democratic welfare states, however, where female labor force participation has remained lower, this ratio has remained at a significantly lower level (Huber and Stephens 2001a: 238-9). As mentioned above, in Christian democratic welfare states the growing unemployment pressures in the 1980s and 1990s were in part handled through early retirement and generous disability pensions, which in combination with the low female labor force participation led to a real and perceived crisis of inactivity.

The real crisis for Christian democratic welfare states, though, is ahead. Whereas in 1960 the average fertility rate in Western Europe stood at 2.6, by the 1990s it had fallen to 1.5; in Italy and Spain it had fallen to 1.3 and in Germany to 1.4, in contrast to Sweden with 2.1 (Esping-Andersen 1999: 68). The social democratic welfare states provide a significant array of family services and thus make it possible for women to combine paid work with raising a family. Liberal welfare states don't provide these services but their unregulated labor markets have generated a considerable private market for day care, though with a lower end of questionable quality. Christian democratic welfare states don't provide these services and their comparatively high floor of wages and payroll taxes prevent the emergence of a significant private market in family services, which essentially forces women to choose family or career. The response of an increasing number of women has been to opt for a career. The societal level consequences are falling fertility rates and future dependency ratios with possibly disastrous implications for welfare states. Allowing higher rates of immigration, for which there is great external demand, would be a solution to this problem, but the strength of internal anti-immigrant sentiment makes this a politically highly controversial solution.

Rising female labor force participation and rising divorce rates have also contributed to a greater share of single parent households. Single parent households, in turn, are more likely to be poor than households with both parents, thus putting greater demands on the welfare state. This situation calls for a change in the organization of welfare state programs, away from the traditional male breadwinner model whose dependents are protected through his employment-based entitlements, to a structure of entitlements for individuals based on citizenship or residency and their responsibilities.

Still other developments have rendered welfare state structures designed in the 1960s and 1970s and based on the assumption of a typical male industrial worker with life-long employment and a wife and children obsolete. The shift from employment growth in manufacturing to services has brought more frequent interruptions in jobs and the need for additional training, that is, a greater likelihood of interruption of gainful employment. In this situation, job-based entitlements both for workers and their dependents are not an effective safety net (Esping-Andersen et al. 2002). What these pressures call for is adaptation of welfare state designs, not retrenchment per se. However, given the macroeconomic context, these adaptations can be at best cost neutral. The adaptations have the greatest potential to sustain generous welfare states if they are aimed at improving the human capital base and raising overall activity levels.

In Latin America the domestic pressures are somewhat different. In the more advanced countries, an aging population has increased pressures on the pension systems and on curative health care. In many cases, these pressures were dealt with by adjusting the retirement age upward from 60 or even lower to 62 or 65, and by restricting pension entitlements based on length of service. The proportion of female headed households varies greatly between countries and across social classes, being higher among the lower classes and in the Caribbean, where it ranged mostly between 30% and 40% in the period 1985-97 (UN 1997). In the more advanced countries, it has not changed much since 1980, ranging from 17% to 25% (UN 1997). Lack of data prevents a more systematic historical view, but the anthropological literature suggests that female headed households have a long tradition among the lower classes and particularly in the Caribbean. Given that these heads of households typically work in the informal sector, they and their children have long been excluded from employment based pension and health care entitlements.

The problems of restricted coverage of systems of social protection in Latin America have been aggravated by the economic transformations discussed above. Thus, the challenge for these systems remains a widening of coverage and an introduction of unemployment insurance. The key change needed is also a transition from entitlements for a breadwinner and dependents based on employment to entitlements for individuals based on citizenship and responsibilities for dependents. Given the macroeconomic situation of these countries, the level of benefits obviously has to be very basic. However, as we will argue below, such basic benefits are essential for a strengthening of the human capital base and thus economic development.

Outcomes of Welfare States for Human Welfare

There are several ways to look at the outcomes of welfare states with regard to human welfare. Arguably the most fundamental outcome is poverty reduction. Whereas advocates of social democratic, Christian democratic, and liberal welfare state regimes disagree on other goals, particularly the goal of reducing inequality, they do agree on the goal of reducing poverty – at least among the “deserving poor” who because of adverse circumstances cannot keep themselves out of poverty (Goodin et al. 1999). Thus, the question is which welfare state regime performs best on this indicator. A second relevant outcome is reduction of inequality. As Esping-Andersen pointed out in his contribution to the last edition of this Handbook, there is a lot of conceptual confusion with regard to equality and equity as orienting principles of welfare state construction. Only social democrats embrace the principle of equality outright, but advocates of all political persuasions use the concept of equity to legitimize welfare state programs with very different distributional implications. A third important outcome concerns gender equity, another contested concept. Proponents of shared and equal gender roles advocate equity in the sense of welfare state structures that facilitate the combination of career and family for both men and women. Proponents of separate gender roles advocate equity in the sense of welfare state structures that recognize and reward women's responsibility for care of family members and entitle women to benefits of their own on this basis, rather than treating them as dependents of their husbands.

Due to the availability of Luxembourg Income Studies (LIS) data, it is possible to look at before tax and transfer income of individuals and households and after tax and transfer income separately. It is also possible to look at specific age and gender categories. Finally, there are by now several waves of LIS data, which makes it possible to go beyond the traditional cross-sectional research designs and use an unbalanced pooled cross-sections and time series design. Researchers have found that the overall amount of welfare state spending is a good predictor of poverty reduction (Kenworthy 1999; Smeeding et al. 2000). As Table 1 demonstrates, poverty levels are highest and poverty reduction is lowest in liberal welfare states, where spending is lowest. This is so despite the fact that many programs are means tested and thus directed at the poor. These means tested programs are simply not generous enough to combat poverty effectively. Poverty levels are lowest and poverty reduction highest in social democratic welfare states, even when pensioners are excluded from the calculations (Moller et al. 2003). Excluding pensioners is important because in countries with comprehensive and generous public pension systems large percentages of pensioners have no other income and thus are poor according to before tax and transfer income (Mäkkinen 1999). The Christian democratic welfare states are between the other two types; most of them start with higher poverty levels than social democratic welfare states, comparable to poverty levels in liberal welfare states, but they reduce poverty more effectively than liberal welfare states and thus end up with lower poverty levels, though still higher than in social democratic welfare states.[9] Since Christian democratic welfare states spend similar overall amounts to social democratic welfare states, their lower effectiveness in reducing poverty stems from a less progressive structure of the tax and transfer system than in social democratic welfare states.

Table 1 about here

The difference in the distributive profile of the Christian democratic and social democratic welfare states is largely governed by the differential commitment of their political promoters to the goal of redistribution and equality. Social democratic commitments have historically been shaped by their deep anchoring in labor movements, whereas Christian democratic commitments reflect their cross-class social base, held together by religious appeals (van Kersbergen 1995). The former have promoted values of equality, the latter of harmony and conciliation of interests. Long-term incumbency of these political forces has indeed resulted in welfare states with a distinctively different structure. Countries with social democratic welfare states start out with a more equal income distribution than countries with Christian democratic welfare states, and the difference increases after taxes and transfers are taken into account.[10] The tax and

[9] Pre tax and transfer poverty levels are largely a result of labor market variables, specifically the size of industrial employment and the level of unemployment (Moller et al. 2003).

[10] The differences in before tax and transfer inequality are accounted for by levels of unemployment, proportion of single mother families, and union density (Bradley et al. 2003).

transfer systems of social democratic welfare states redistribute income to a greater extent than those of Christian democratic welfare states and thus reduce the Gini index of income inequality to a greater extent (Bradley et al. 2003). If social services were included in the measurements, the difference would be even more pronounced. Social democratic welfare states provide a wider array of free or subsidized services, entitlement to which is based on citizenship or residence and thus universally available. By analyzing data for the working age population only, these recent studies based on LIS data have conclusively refuted the critique that welfare states are at best redistributive across the life-cycle but not across income classes. By demonstrating the importance of social democratic incumbency, they have also provided strong support for the power resources theoretical tradition (Bradley et al. 2003).

Countries with liberal welfare states start out and end up with the highest levels of income inequality, as their welfare states are too small to effect much redistribution, despite the wide-spread use of targeting of benefits. On the face of it, the heavy reliance on earnings-related benefits in Christian democratic welfare states would lead one to expect less redistribution on average there than in liberal welfare states. Korpi and Palme (1998) call this the paradox of redistribution. The paradox can be explained with the fact that the generous public schemes in Christian democratic welfare states crowd out private alternatives which are invariably even more inegalitarian than earnings-related public schemes (Kangas and Palme 1993).

Given the different notions of gender equity, many analysts prefer the concept of "women-friendly" policies (Hernes 1987), which accommodates policies from support for mother's employment to pension credits for child rearing. Interestingly, looking at individual policies separately, there is often no clear clustering according to welfare state regimes. In particular, the Christian democratic welfare states are very heterogeneous with regard to services and transfers that affect women differently from men (Sainsbury 1999). However, if one looks at the big picture, such as a number of policies summarized by one index of support for mother's employment (Gornick, Meyers and Ross 1998), or actual outcomes like the proportion of single mothers in poverty (Huber et al. 2001), one does find a consistent pattern. The social democratic welfare states as a group perform best, with Norway being a laggard; the liberal welfare states perform worst; the Christian democratic welfare states are in the middle, with France and Belgium coming close to the social democratic model in their support for mothers' employment (Gornick, Meyers and Ross 1998). In women's labor market participation and women's share of total earnings, again the social democratic regimes perform best, with Norway lagging a bit, but here the Christian democratic welfare state regimes are at the bottom and the liberal regimes in the middle (Sainsbury 1999). In the level of poverty among single mothers, a good indicator of the crucial gender equity dimension of women's capacity to form autonomous households (Orloff 1993b), social democratic welfare state regimes effect the greatest reduction from pre to post tax and transfer poverty and thus produce roughly three times lower poverty levels than Christian democratic welfare states and five times lower levels than liberal welfare state regimes (Huber et al. 2001). What is behind these findings is support for equality of gender roles and thus women's integration into the labor market in social democratic parties, support for separate gender roles and women's responsibility for family care combined with a commitment to keeping women and children out of poverty in Christian democratic parties, and little support for welfare state services and transfers in secular center and right-wing parties.

Critics of the welfare state might argue that its achievements in reducing poverty and inequality do little more than repair the damage done to pre tax and transfer poverty by generous income support systems that serve as work disincentives. We have already pointed to the weak and inconsistent results of research on work disincentives (Atkinson and Mogensen 1993). Here we can add the evidence from the LIS-based studies on pre-tax and transfer household income. Countries with social democratic welfare state regimes have the lowest pre tax and transfer levels of poverty and inequality among the working age population and poverty among single mothers. The difference between countries with Christian democratic and with liberal welfare state regimes is less clear, as the Christian democratic category is quite heterogeneous, but the former perform somewhat better on average on inequality and single mothers in poverty, and are about comparable on poverty among the working age population (Moller et al. 2003, Bradley et al. 2003, Huber et al. 2001). In other words, there is no evidence that generous welfare states are associated with higher levels of pre tax and transfer poverty and inequality. Moreover, a direct statistical test of the effect of welfare state generosity on pre tax and transfer inequality showed no such effect (Bradley et al. 2003). We will take up the question of a possible indirect effect via unemployment below.

For Latin America, the literature on welfare state outcomes is again rather scarce. The poor quality of data is a major obstacle; there simply are no reliable data on social expenditures for the pre-1980 period, and even for the past two decades the comparability of the data is poor (Cominetti 1994). Moreover, reliable and comparable data on poverty levels are a rather scarce commodity, not to speak of income distribution. This should not be surprising, if we keep in mind that the LIS data, which are the first truly comparable data for advanced industrial democracies, have only been collected over the past three decades and are only available for one time point for some of them. Latin American case studies for the pre-1980 period suggest that the pension part of social security systems was highly inegalitarian because of the highly unequal benefits received by different occupational groups, the restricted coverage of pension systems, and the fact that the uninsured paid part of the cost through general taxes and through higher prices resulting from employers passing on the cost of their social security contributions to consumers (Borzutzky 1983: 98-113; Mesa-Lago 1989: 130). The health care part of social security tended to be more progressive, and the most progressive kinds of social expenditures were public health expenditures.

For the 1990s, CEPAL (2002) comes to a largely similar assessment: Social security expenditures, which continue to absorb the largest part of social expenditures, have a less redistributive impact than expenditures on primary and secondary education and on health and nutrition, because they provide relatively greater benefits to middle and upper income groups. In a study of eight countries, CEPAL found that on average lower-income strata receive transfers and free or subsidized services, including social security, equivalent to 43% of total household income, compared to 13% and 7% for the fourth and fifth income quintiles. Nevertheless, in some of these countries the actual amount of the transfers to the richest stratum was twice as much as that going to the poorest stratum (CEPAL 2002: 28). If social security is excluded, households in the lowest quintile, with 4.8% of total before tax and transfer income, receive 28% of total social expenditure, whereas the highest quintile, with 51% of pre tax and transfer income, receives 12% of total expenditure (CEPAL 2002: 27).

After having reduced social expenditures significantly in the 1980s, most countries raised them again in the 1990s in both absolute terms and as a percentage of GDP. On average, social expenditure rose from 10.4% of GDP in 1990 to 13.1% in 1999 (CEPAL 2002: 23). This increase, however, even combined with economic growth, was not nearly sufficient to lower poverty effectively and undo the damage done in the 1980s. Poverty did decrease from 48.3% of the population in 1990 to 43.8% in 1999, but this figure remained above the 40.5% of the population who had been poor in 1980. In absolute terms, the number of poor people increased by 11 million in the 1990s (CEPAL 2002: 14-15). Progress in reducing inequality was nil; Latin America remains the region with the most unequal income distribution. Inequality had increased in most countries in the 1980s, and in some countries it continued to increase in the 1990s. It is worth pointing out here that the two countries that performed clearly best in protecting the lowest levels of inequality were Uruguay and Costa Rica (CEPAL 2002: 18). These two countries spent the highest percentage of GDP on social expenditures, along with Argentina and Brazil, but in contrast to Argentina and Brazil, they had built up more solidaristic social security systems and health care systems, with larger coverage, before the 1980s, and then reformed them only slowly and cautiously.

Growth and Employment Outcomes of Welfare State Regimes

The impact of the welfare state on growth and employment is contested terrain both politically and academically. Indeed, it would be no exaggeration to say that this is the central issue separating the left and the right in advanced industrial democracies, with the right contending that increasing social spending (and taxes) retards economic growth and employment growth and thus results in welfare losses, while the left argues that increasing spending does not affect growth and employment and may even have positive effects on them. Neo-classical economists argue that intervening in markets will create inefficiency and lower economic performance; there is a "big trade off" between "equality and efficiency" (Okun 1975, also see Bacon and Eltis 1976, Lindbeck 1981). Even new growth theorists who argue that economic institutions and government policies can theoretically have a positive effect on growth, are generally hostile to high taxation and social welfare spending. For instance, new growth theorists hypothesize that inequality retards growth because "in an unequal society, with many poor agents relative to the average, the majority will then vote for high taxation, which . . . will discourage investment and therefore growth" (Alesina and Perotti 1997: 27).

Welfare state detractors point to negative work incentives created by high taxes which reduce the return on additional hours of work, and generous benefit levels which discourage from seeking work or returning to work. High taxes also crowd out productive investment, in their view. Supporters of generous welfare states counter that spending on health and education, active labor market policy, and policies which enable combining work and family, such as parental leave and day care, improve human capital and increase labor supply. It can also be argued that skill levels at the bottom are in part a direct product of welfare state redistribution, as average skill levels at the 5th, 25th, and 50th percentile of the skill level as measured by the OECD/HRDC literacy study are very highly negatively correlated with post tax and transfer inequality and not very highly correlated with public educational expenditure, public and private educational expenditure, or secondary school completion rates (Huber and Stephens 2001b). As to the micro incentives question, Atkinson and Mogensen's (1993) comprehensive survey of research on Denmark, Sweden, Germany, and Britain on the impact of taxes and social policy on work incentives finds some evidence for both sides in this debate but notes that in most cases the effects were quite small.

Given the centrality of the debate on welfare state generosity and economic growth to contemporary politics, it is surprising that there is not a rich quantitative literature and that, as Saunders (1986) points out, the few early studies were plagued by underspecification, in part because of the small number of cases in the cross sectional designs in these studies. Castles and Dowrick's (1990) pooled time series analysis of growth over four time periods from 1950 to 1985 stands out as the single most comprehensive attempt to test the hypothesis that welfare spending has a negative (positive) effect on medium term growth (also see Korpi 1985).[11] Their results "rule virtually out of court any interpretation that argues for a statistically significant negative relationship between the level of government revenues or the components of government expenditure and medium-term growth" (p. 200-01). On the other hand, they do find some support for a positive relationship between transfers and growth, but it is weak.

Castles and Dowrick's study was published the same year as Esping-Andersen's study and does not reflect the shift in the welfare state literature from the study of variations in welfare state generosity to the study of welfare state regimes. However, the literature on social democratic corporatism and growth is highly relevant here because of the previously mentioned high correlation between corporatism and the welfare state and production regime types. The seminal Lange and Garrett (1985) piece spawned a series of articles (Garrett and Lange 1986; Jackman 1987, 1989, Hicks 1988; Hicks and Patterson 1989; Alvarez, Lange, and Garrett 1991, Beck et al. 1993; Grier 1997; Garrett 1998; also see Schmidt 1983; Cameron 1984; Wilensky 2002), culminating in Scruggs' (2002) recent contribution which summarizes, improves on, and updates the previous contributions to this debate. Scruggs improves on previous contributions by using the Summers and Heston (1991) measure of per capita growth measured at purchasing power parities and by including variables measuring alternative causes of growth, such as initial level of economic development (Hicks 1988, Barro and Lee 1994), firm level cooperation (Hicks and Kenworthy 1998), and consensual democratic institutions (Crepaz 1996). He confirms the central hypothesis of Lange and Garrett (1985) that strong and centralized union confederations combined with left government

[11] The hypothesis is properly tested on medium term growth which eliminates business cycle effects. Friedland and Sanders (1985) find little support for the neo-liberal view even on short term growth.

yield better growth than the inconsistent regimes of left government and no corporatism or corporatism and right government. However, he contests the implication that most of the social democratic corporatism advocates draw, that social democratic corporatism performs better than the other consistent regime, liberal market capitalism (no corporatism and right government). He finds that social democratic corporatist regimes performed no better than the liberal market capitalist regimes in the 1974-84 period and worse in the 1985-95 period.

How does one reconcile Scruggs' findings with those of Castles and Dowrick? One might conclude that social democratic corporatism and generous welfare states have become an economic liability in the post 1985 era of globalization. However, it is likely that Scruggs' results for 1985-95 are heavily driven by the economic crises in Finland and Sweden. The very strong economic performance of these two economies in the late 1990s and early 2000s indicates that economic mismanagement and cyclical features and not institutional arrangements were responsible for these crises. OECD data for 1995-2002 indicate that one could not replicate the finding for this period. It is our conclusion that there is no evidence that one of the welfare state and production regimes performs better than the others with regard to economic growth. This is also the conclusion of Hall and Soskice (2001: 21). They argue that the differential institutional structures of CMEs and LMEs result in comparative institutional advantages in producing different products: "the institutional frameworks of liberal market economies provide companies with better capacities for radical innovation, while those of coordinated market economies provide superior capacities for incremental innovation" (p. 41). They contend that globalization should sharpen these differences resulting in further divergence rather than the convergence predicted by neo-liberals.

With regard to unemployment, the social democratic corporatism literature usually but not invariably (e.g. see Beck et al. 1993) showed a positive effect of corporatism on unemployment. The shift to an analysis by regime type and a focus on employment rather than unemployment yields a much clearer picture (e.g see Esping-Andersen 1990, 1999, Scharpf 2000, Huber and Stephens 2001a). The shift to a focus on the total level of employment, usually measured as the employed population as a percentage of those aged 15 to 64, was motivated by the fact that many Christian democratic welfare states had resorted to placing able bodied workers below retirement age in early pension schemes or disability schemes in order to reduce unemployment, thus hiding the true unemployment level. Because of its policies facilitating combining work and family, the related high level of public sector employment, and active labor market policies, the social democratic regime clearly outperformed the other two regimes in overall employment levels. The high levels of wage dispersion characteristic of liberal welfare states have facilitated the development of a large low wage private service sector in these countries, resulting in employment levels higher than the Christian democratic welfare states but lower than the social democratic welfare states. The OECD figures for unemployment in 2001 show a similar pattern, with the social democratic welfare states (5.4%) and liberal welfare states (5.5%) performing better than the Christian democratic welfare states (6.8%).

Our positive assessment of the employment performance of the social democratic welfare states is at variance with the evaluation of the OECD Jobs Study which touts the liberal model as the one best way and recommends that European countries increase wage dispersion, roll back welfare state benefits, especially for the unemployed, reduce employment protection, and cut taxes to facilitate the expansion of low wage employment. Our view is supported by Bradley's (2001) comprehensive test of the OECD diagnosis. In a pooled time series analysis with employment levels as the dependent variable, Bradley finds that wage dispersion, welfare state generosity, and employment protection laws are not related to employment levels. Total taxes, active labor market policies, high short term unemployment benefits, and bargaining centralization are positively related to employment levels, while payroll taxes and high long term unemployment benefits are negatively related to employment levels. This fits very well with our outline of the performance of the regime types (also see Scharpf 2000), as these positive features are all characteristics of social democratic welfare states while the negative features are characteristics of Christian democratic welfare states.

Advances in Welfare State Research and Future Directions

To summarize our discussion of progress in welfare state research, we can begin by pointing out that in terms of theoretical approaches, recent studies of welfare state formation tend to be synthetic. The main emphasis is on power distributions, but institutional factors are treated as essential explanatory factors as well. Considerations of power distribution include not only labor movements in the form of unions and left parties, but also political parties based on religious appeals with their own distinctive welfare state project. Moreover, gender is added to class and religion as a possible basis for organization and political mobilization in support of specific welfare state programs. Comparative research on gender mobilization is hampered by data problems, though. Whereas there are by now excellent data on unionization, there are only very spotty, survey based data on membership in women's groups, or on female membership in political parties.

A further theoretical advance is the use of welfare state regimes as essential analytical category. The conceptualization of regimes is based on constellations of social rights, or welfare state entitlements, given by the structure of the respective welfare states. Empirically, there has been considerable progress in measuring social rights (Korpi 1989, Esping-Andersen 1990), but these measurements are mainly tapping rights to transfers. Given the importance of social services and the great differences in the extent to which welfare states take responsibility for financing and/or delivering them, progress in developing good measures of rights to free or subsidized social services will be an essential contribution to welfare state research. They will also help us better to understand the gender-specific impact of different welfare state regimes.

Connecting welfare state regimes in a systematic way with production regimes has been another step forward in welfare state research. This connection is best seen as a mutually supportive or enabling one, not as a necessary correspondence. Indeed, it is important to emphasize that welfare state regimes can be adapted to changes in production regimes while protecting their essential features. The closest link between production and welfare state regimes we found in the countries with reliance on high tariff protection and state intervention in other areas to promote ISI. There, a turn away from this production regime made certain features of the welfare state regime unviable.

There has been considerable research on the impact of globalization on welfare state regimes. This research has found few if any direct effects on welfare state regimes in advanced industrial societies, but it has found some indirect effects via higher levels of unemployment, particularly in coordinated market economies where globalization deprived governments of some policy tools they had used to stimulate investment and employment. Qualitative research has added to this a shift in power relations in favor of capital and thus greater ability to pressure governments and labor movements for concessions on tax financing of welfare state provisions. Nevertheless, the general picture is one of remarkable resilience of welfare state regimes in advanced industrial societies. There have been cutbacks almost everywhere, and some of considerable magnitude, but one could really only talk of regime shifts in two cases, Britain and New Zealand. In contrast, the impact of globalization on countries with ISI production regimes, Australia and New Zealand and the Latin America countries, was quite dramatic. They had to restructure their systems of social protection, and in most cases this restructuration was governed by a neoliberal blueprint pushed by the international financial institutions. But even in these cases, the examples of Australia, Uruguay, and Costa Rica demonstrate that it is possible to adapt in a way that preserves more generous and solidaristic welfare state regimes than the neoliberal model prescribes. Comparative research on cases of countries that have been undergoing a transition from ISI to more open economies is scarce and is badly needed to elucidate the determinants of modes of adaptation that preserve or construct effective systems of social protection.

Notwithstanding the general picture of resilience of welfare state regimes in advanced industrial societies in the face of globalization, research has identified serious pressures from other sources that have the potential to escalate in the future. The most serious of these pressures are demographic, specifically the increase in life expectancy and consequent growth of the elderly proportion of the population. In countries with Christian democratic welfare states, particularly in Southern Europe, this problem is aggravated by declining fertility rates. Research is needed to identify solutions to this dilemma, that is, paths towards increasing female labor force participation rates while simultaneously facilitating the combination of paid work with family care obligations. Other pressures on established welfare state models, such as labor markets with more frequent interruptions of careers and changing household structures are not as dramatic but still call for research on creative adaptations of income support programs.

Given these pressures and the reliance by Christian democratic welfare state regimes on reduction of labor supply to deal with unemployment, there is considerable convergence towards the view that this regime type is the one confronting the most serious challenges. The turnaround in the Nordic countries after the crisis of the early 1990s, combined with overall low dependency ratios, suggests that the social democratic welfare state regime is a sustainable model. The liberal welfare state regime also appears sustainable, though it entails serious social costs in terms of high poverty and inequality. It is the Christian democratic welfare state regime, with its low overall labor force participation rate, unfavorable demographic trends, and great reliance on payroll taxes for welfare state financing that is in danger of becoming unsustainable. How to restructure that system and how to make the solutions politically palatable is a major research area for the near future.

A further area of major progress in welfare state research concerns outcomes for human welfare. The availability of comparable data over time for advanced industrial democracies has made it possible to demonstrate the differential effectiveness of welfare state regimes in reducing poverty and inequality. All three of them reduce both poverty and inequality, but social democratic welfare state regimes achieve consistently the best results and the liberal welfare state regimes the worst, with Christian democratic welfare state regimes in the middle. The difference between the social democratic and the Christian democratic welfare state regimes lies in the progressive structure of the tax and transfer systems, the difference between the Christian democratic and the liberal welfare state regimes lies in overall generosity. The liberal welfare states simply don't devote enough resources to combating poverty to achieve the same results as the Christian democratic welfare state regimes, regimes that are similarly oriented towards poverty reduction only and not towards reduction of inequality per se. Low spending on their systems of social protection, of course, constrained by low tax burdens, is what keeps the great majority of Latin American countries from combating poverty effectively.

In the literature on welfare states and growth and employment, we noted a surprising scarcity of tests of the growth relationship. The most comprehensive of the studies that have been done did not find any negative effects of government revenue or components of government expenditure on medium-term economic growth. Nor did researchers find any conclusive evidence that a particular combination of welfare state and production regimes performed better than another in economic growth. However, with regard to employment there is evidence that social democratic welfare state regimes and labor market policies performed better than both liberal and Christian democratic welfare state regimes. Moreover, the social democratic are the most redistributive welfare state regimes, and lower levels of inequality are closely associated with higher skill levels at the lower end of the skills distribution. This reinforces the overall assessment that the social democratic welfare state regimes do not only have the best consequences for human welfare in terms of poverty and inequality but are also economically sustainable because of their investment in human capital and in labor mobilization.

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Table 1
Poverty Rates Among the Working Age Population
(Advanced Industrial Democracies)

		1	2
	Year of LIS Survey	Pre tax and transfer Poverty	Post tax and transfer Poverty
Social Democratic Welfare States			
Sweden	1995	21.8	4.0
Norway	1995	15.6	4.3
Denmark	1992	19.0	4.4
Finland	1995	17.6	3.6
Mean		18.5	4.1
Christian Democratic Welfare States			
Austria	1987	n.a.	4.8
Belgium	1992	15.4	3.8
Netherlands	1994	18.2	6.8
Germany	1994	14.7	7.6
France	1994	23.6	7.8
Italy	1995	25.4	16.2
Switzerland	1992	13.2	11.0
Mean		18.4	8.3
Liberal Welfare States			
Canada	1994	19.4	11.2
Ireland	1987	26.7	13.4
UK	1979	24.8	11.9
USA	1997	18.1	15.5
Mean		22.3	13.0
"Wage Earner" Welfare States			
Australia	1994	19.3	9.4
Grand Mean		19.5	8.7

Data source: Luxembourg Income Studies, authors' own calculations.
Cell entries are percent of the population aged 25-59 with income less than 50% of the median.