Conclusion: Politics Matter

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Globalization and the Future of the Welfare State

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of company welfare. Insofar as the decline in company welfare is the result of firms’ strategies toward global competition, the growth of public welfare is closely associated with globalization. As companies recede from welfare provisions, the state begins to emerge.

What light, then, does the Korean case shed on the effects of globalization on social policy? It seems likely that the progress in social protection is attributable not only to economic openness and globalization but also to democratization. Democratic governments in Korea have had to reform and expand the social policy regime in order to improve social performance, viewed as important for the consolidation of democracy (O'Donnell and Valenzuela 1992; Schmitter and Karl 1991; Choi 1997; Im 1994). Democracy is more easily sustained when it is accompanied by policies that improve the standard of living and income equality, and which eliminate structural and regional discrimination in the society (Diamond and Plattner 1991; Diamond and Gunther 2001). The gradual expansion of social policy in Korea is a joint result of the maladjustment to globalization that resulted in the financial crisis, and the timely emergence of democratic government, which permitted the rise to power of a progressive and labor-friendly leadership.

Conclusion

Politics Matters

MIGUEL GLATZER AND DIETRICH RUESCHEMEYER

In this concluding essay, we return to the questions raised in the opening chapter. We will closely review each of the studies that form the main body of this project. But at the same time, we will try to come to broader conclusions about the impact of globalization on welfare state development and will do so by exploring the social and economic mechanisms through which economic openness may affect social welfare policy. Of particular importance is how different aspects of economic globalization are related to the domestic factors that shape welfare state development.

A First Look at the Results

The studies assembled in this volume portray a great variety of social policy developments in countries experiencing increased economic openness. What stands out is, first of all, the relative immunity to the undermining effects of economic globalization displayed by the welfare states of northwestern Europe. Questions remain about the consequences of greater capital mobility for macroeconomic policy options and, more generally, for the balance of power in these societies as well as for the particular “coordinated” versions of capitalism that have been associated with their social welfare systems. Nonetheless, with the exception of Britain these countries have largely retained their overall patterns of social protection. This in spite of the serious problems they face for reasons other than economic openness, problems that derive from a changing age structure, increases in the cost of medical care, high levels of unemployment, and the emergence of new problems related to changing family patterns and increasing levels of immigra-
tion. The welfare states of northwestern Europe were the point of departure for our comparative analysis (see Stephens, this volume; Huber and Stephens 2001a). They defined the dimensions of vulnerability and resilience on which the examination of the middle-income countries in different regions focused.

Among the countries and regions examined in this project, the strongest negative impact of economic globalization on social welfare policies is found in Latin America. Here the protectionist policies of import substitution industrialization (ISI) were prolonged in the 1970s with the help of easy credit, which derived from the massive gains of the oil-producing countries organized into the OPEC cartel. This led abruptly into the debt crisis of the 1980s, when interest rates rose and the international banks stopped making new loans as Mexico, Argentina, and Brazil faced serious repayment difficulties. The debt crisis opened most Latin American countries to very strong pressures from the international financial institutions to international trade, which many enterprises did not survive. If the 1980s became "the lost decade" for most of Latin America, the 1990s saw some economic recovery; but this decade also witnessed new inflows and outflows of short-term capital that were held responsible for the financial crises of Mexico and Argentina in 1994–1995 and of Brazil in 1998–1999. The broad picture of change in Latin America during the last generation is clear: States were weakened in their capacity to intervene on behalf of the weaker strata. Among the more important social and economic outcomes was an increase in the informal economy, removing more people not only from taxation but also from social regulation and support, as well as persistently high levels of unemployment, poverty, and income inequality. The results in social policy were decade-long cuts in social expenditures and policy reforms that emphasized privatization and targeted help for the poor rather than universal programs.

Yet the differences among Latin American countries are as instructive as this overall picture. Costa Rica as well as Uruguay and Panama increased their already high level of social spending as a share of the gross domestic product even during the 1980s. "Costa Rica and Uruguay ... were consistently different from the other Latin American countries in spending efforts and outcomes, and ... they were also different in some aspects of their traditional systems of social protection and in their approach to social policy reform" (Huber, this volume). In contrast to Chile, where neoliberal transformation of social policy led to privatization, reductions of universalistic benefits, more means-tested programs, and an overall decline in social expenditures by more than a quarter, Costa Rica did not opt for a similar individualization and privatization of social policy; instead, it strengthened the universalistic character of its pension and health policies and sought to put them on a sounder financial basis. Evelyne Huber traces these differences convincingly to the structure and capacity of the state and to the balance of social and political power. And these factors not only account for the differences between the extreme cases but are shown to shape the more mixed policy developments in other countries as well.

Spain and Portugal offer the clearest evidence that a social policy trajectory very different from neoliberal minimalism can be associated with increased economic openness. Since the 1970s, both countries significantly opened their economies to international trade and capital flows. Yet at the same time they developed comprehensive welfare states, taking off from the rather austere foundations that were the legacy of the previous authoritarian corporatist regimes.

Post-Communist Eastern Europe presents a very different picture from the other regions. Until the collapse of Communism in 1989–1990, countries under Soviet control had comprehensive—if in their absolute levels of provision, austere—social welfare systems. These systems were, however, tied to a centrally planned economy. With the rapid disintegration of that economy and with the policy of establishing market economies in a very short period of time, the Communist welfare systems ran into mounting difficulties. The old social welfare provisions were cut loose from their institutional moorings in industrial enterprises; centrally provided benefits such as pensions became too expensive, and new problems such as unemployment had to be dealt with. At the same time, the expectations engendered by the old system made cutbacks and restructuring politically difficult. In Russia, these difficulties led in the Yeltsin period to a stalemate between the reformist presidential executive, advised by the World Bank, and the Communist-dominated Parliament (Cook, this volume). In east-central Europe there were a variety of policy responses until the middle 1990s, when policies began to converge in response to increasing budgetary constraints and guided by the World Bank and other international institutions (Orenstein and Haas, this volume). As in Latin America, the international financial institutions urged a policy direction defined by privatization and strict targeting of social supports. Another similarity is, however, equally noteworthy: After initially neglecting social policy altogether, the international financial institutions became concerned with the disruptive potential of a lack of social protection for economic openness and for market-oriented reform in general.

The political economies of Japan and the more recent industrializing countries of East Asia are in still other ways set off from the advanced capitalist countries of Europe and the English-speaking settler countries. These differences are evidenced in the social problems generated by a capitalist economy; in the rapid economic growth these countries experienced since the 1950s and 1960s, respectively; and in their emerging social policy patterns. Among the major similarities relevant for social welfare policy in East Asian countries were the following: widespread poverty after the Second World War and the Korean War, which was, however,
combined with low income inequality; an education system of high quality; a strong policy priority given to fast income growth rather than special social policies; low unemployment; encouragement of corporate welfare; and adoption of the classic social programs with little emphasis on generous funding.

Song's chapter sees South Korea as a laggard in social welfare policies that finds itself now at a crossroads. During the 1960s and 1970s, rapid economic growth substituted for social welfare policies beyond education, health care, and pension programs for privileged groups (the military, government employees, and teachers). Unions were politically constrained and limited to single enterprises; not unexpectedly they supported corporate welfare programs in the larger chaebol, which were also strongly encouraged by the military government. Democratization since the late 1980s, even though less than complete in the freedom provided for self-organization of society, encouraged the institutional rounding out of the classic social welfare programs, though these remain still at a low level of spending. At the same time, Korea's economy opened itself to freer import trade and later to an open capital account. The financial crisis of 1997–1998 made increases in social spending both for general assistance and, above all, for unemployment compensation imperative. Whether a more democratic and economically open Korea will move toward stronger welfare state development on the basis of tripartite political cooperation is at this point an open question. If it does, it will join the Iberian countries in a social policy trajectory in which democratization and economic opening jointly encourage rather than undermine welfare state development. But a much more limited version of social welfare policy seems equally possible.

Geoffrey Garrett and David Nickerson offer a cross-national examination of relevant indicators for a large number of middle-income countries. They focus on the compensation and efficiency hypotheses that defined one of the primary themes of our project. The conclusion that middle-income countries with more open economies have larger public economies extends earlier work (Cameron 1978; Rodrik 1997). Garrett and Nickerson show that capital mobility is positively associated with public spending. Their analysis strongly suggests that there may be a positive effect of globalization on social policy worth investigating. They distinguish between level of openness to capital mobility and increases in capital mobility and find different effects of the two: while the former is associated with higher levels of public spending, the latter correlates negatively with growth in public spending. Their chapter, then, points to fascinating complexities in the relationship between openness and size of government. These complexities as well as the important variation among middle-income countries make a good case for the comparative case studies that comprise the bulk of this volume.

The conclusions that can be reached from this set of interregional comparisons are inherently tentative because of the recurrent problem of macro-comparative social analysis—too many potentially important factors, too few cases. Careful causal tracing within countries, based on many observations, can ease these problems. Furthermore, since welfare state development has been the subject of much theoretical and empirical comparative work during the past twenty years, we can approach the limited number of cases and comparisons with quite specific theoretical expectations and interpretations and thus improve the plausibility of our conclusions.

Our cases share important similarities: All the mid-income countries and regions saw in the last generation significant advances in democratization, though the realities of democratic politics varied considerably from country to country. All increased their openness to the international economy, though there were important variations in this dimension as well. These latter variations included differences in the pace of opening to both trade and capital mobility and, importantly, the incidence of economic crises that were related to a country's greater integration into the international markets for goods, services, and capital. Yet with the possible exception of the latter—an issue to which we will return—it seems that these differences in exposure to the international economy do not offer the key for understanding the variety of outcomes in social policy.

The results of our cross-regional inquiries suggest two first-order conclusions: The very variability of outcomes implies that the advances of international economic integration during the past two decades do not constitute a development that defines the future of social welfare policy worldwide. Equally important is another strongly supported claim: Politics makes a decisive difference for the consequences of economic globalization for social policy in a given country. "Politics" here, of course, must not be understood as a matter of sheer political will. What politics can accomplish is always mediated by the historical background of political and economic structures, by the resultant balance of power within a country, and by a country's insertion into its geopolitical environment and the structures of the international political economy. Yet within those constraints politics does indeed seem to make a decisive difference.

What does the pattern of findings in our cross-regional comparison of mid-income countries suggest about the two opposed master hypotheses on the relation between economic openness and social welfare policies? Those hypotheses are the compensation thesis, which claims that economic openness induces social protection measures, and the efficiency thesis, which holds that welfare state policies make economies less efficient in international competition.

Neither of the two broad arguments can account for the whole set of outcomes. However, there is an important asymmetry in the implications our cases have for the two views, and this entails a third preliminary result: The radical formulations of the efficiency view are simply mistaken. It is impossible to maintain
in the face of our results that expanding free trade and free flows of capital always undermine social welfare policies.

The compensation view, to begin with, does not have a radical version that could be falsified by a few instances. While the compensation view does not explain the cases where severe cutbacks in social provisions came about in response to international economic pressures, it can point to important other instances where increasing opening to the international economy did not lead to such cutbacks but actually went along with extensive welfare state building.

Even more significant is another asymmetry. The efficiency view is basically at odds with our claim that politics matters. In its pure—or perhaps better, fundamentalist—form, the efficiency hypothesis denies that politics can truly modify the impact of market forces. Advocates of the efficiency view often assume that market forces are by far the more powerful and that in conflict with social needs and policies, market forces always win out in the end. By contrast, the compensation view inherently involves politics, at least implicitly, unless one assumes in functionalist fashion that policy responses will come forth uniformly and succeed regularly in compensating for the impact of international market forces. Our understanding of the impact of economic globalization on social welfare policies will be deepened if we examine the causal mechanisms underlying the outcomes claimed by the two views. These more detailed underlying mechanisms give us insight into the conditions under which one or the other takes place.

These more specific hypotheses relating economic globalization to social welfare policies must also be integrated with the body of earlier work seeking to explain the rise and consolidation of welfare states. Remarkably, this earlier work has largely focused on internal, domestic factors—the logic of industrialism, the power resources of contending groups and classes, the autonomy and capacity of states and, more recently, on the more or less coordinated character of the political economy of a country. Bringing the consideration of internal and external factors shaping social policy development together seems to hold significant promise for both sides, though it is our contention that such an integration will have a more decisive impact on the views about the consequences of economic openness.

Causal Mechanisms Shaping Social Policy

What are the more detailed causal hypotheses that have been advanced on the link between openness to the international economy and the extent of social welfare policy? The efficiency view provides a robust and fairly detailed theory that is plausible but not broadly corroborated by empirical evidence. The compensation view, by contrast, is supported by multiple correlation results but relies for their interpretation on rather underspecified and sometimes functionalist ideas.

The Efficiency Theory

The causal mechanisms associated with the efficiency theory need only a brief review. International markets, more than local and national ones, are beyond the control of national governments, while limiting a country’s participation in free trade often means foregoing important economic gains. A first causal mechanism invoked by the efficiency view involves the effects of competition from countries with lower costs. Low-cost and especially low-wage competition can force wage and benefit cuts or lead to the elimination of jobs and unemployment in the affected sectors. The threat of such competition may, however, be balanced by productivity advantages of more advanced capitalist countries and especially of countries with effective welfare states policies. If high earnings and workers’ benefits are not compensated by productivity levels that leave the labor costs per unit low, low-wage competition can be an effective pressure for lowering welfare benefits.

Increased capital mobility has multiple consequences. It gives capital owners a wider choice of profitable investment, and it lowers the cost of capital in countries with scarce savings. Rapid changes in the availability and price of capital can lead to devastating financial crises, as happened in the 1980s in Latin America and again in the 1990s in Latin America, East Asia, and Russia. More fundamentally, increased capital mobility is likely to increase the power of capital in relation to labor and government, both of which are inherently less mobile. Specifically, some claim that capital mobility reins in the space for governmental action because it constrains national macroeconomic policy as well as, albeit more indirectly, subsidized investment and above-average levels of taxation and public expenditures. These results are, however, contingent on the extent to which increased mobility of capital results in a truly international capital market with homogeneously shaped interest rates. Furthermore, it is important to remember in this context that the productivity-enhancing consequences of public expenditures may be attractive to investors as well as labor, though they may be irrelevant to the interests of capital owners seeking short-term interest gains. As already mentioned, Garrett and Nickerson (this volume) found in their examination of middle-income countries that recent increases in capital mobility were indeed associated with lower public expenditures, but that the levels of openness to capital mobility and public expenditures were positively correlated with each other.

While overall there is only very limited support for the claim that economic openness as such is at odds with generous social provisions, there is a special constellation in which economic opening does seem to have a strong negative impact on social welfare policy. Sudden opening—to trade or capital flows or both—constitutes such a constellation and can produce wrenching change that destroys previously well-established policies and institutions. Where institutional arrange-
ments had been built on insulation from market forces with which they would be incompatible, a sudden economic opening can wreck them, while new ones are not easily built. This has been identified as a major cause of the radical restructuring of the welfare state of New Zealand (Huber and Stephens 2001a; Stephens, this volume). If we allow for different kinds of institutional dislocations with various implications for social policy, it seems that this causal mechanism pertains to a wide range of circumstances: Most severe cutbacks appear to be associated with radical institutional dislocations due to sudden opening—Latin America's extended and then abruptly ended ISI; the disruption of privileged trade flows in the antipodes; even the post-Communist countries of east-central Europe fit here. 6

This may well be the most important direct negative effect of economic openness on social welfare policy.

While the causal mechanisms primarily associated with the efficiency view do not involve politics, it is important to realize that politics enters the picture nonetheless. This is obvious in the case of social dumping—a politically induced variety of low-cost trade competition and similar competitive moves designed to attract foreign direct investment. Furthermore, the negative impact of openness on social welfare policies involves political choice and requires political enforcement; the build-down of welfare states is clearly a matter of politics. 7 Multinational corporations and other strong corporate actors give political "voice" to pro-market pressures (in contrast to the "voiceless" working of competitive markets), though it must be kept in mind that corporate actors are not uniformly opposed to social welfare policies. The political element in the spread of neoliberal policies is most obvious when policy ideas are imposed as conditions for credits by the IFIs and private banks. Finally, the views that set international markets against politics and vice versa overlook another important fact. The expansion of an open international economy is itself the product of political action by many states, albeit states of quite varied power resources. The international market needs infrastructural guarantees as much as any national market, and these requisite elements of the rule of law are ultimately based on the coercive power of states. Thus, even a closer look at the efficiency view provides important evidence for the claim that "politics matters," contradicting the inclination of its advocates to give politics only a marginal role.

The Compensation Hypothesis

The compensation hypothesis, as already indicated, puts politics at the center of attention. It must do so unless one assumes in naively functionalist fashion that all needs arising from an opening to the international economy will invariably call forth protective responses. It is true, however, that the ways in which domestic factors shape political responses remain rather shadowy.

The compensation hypothesis is supported by positive correlations repeatedly found in different sets of countries between trade and public expenditures, including expenditures on social protection (Cameron 1978; Rodrik 1997). In their examination of mid-income countries, Garrett and Nickerson (this volume) report that the same relationship holds for capital mobility and public expenditures. Furthermore, they found that democracy increased the association. These correlations are just that—statistical associations between numerical indicators, not causal accounts, but they are significant empirical findings that need explanation. The compensation view seeks to provide that.

The Hypothetical Sequence Model

A hypothetical sequence model makes clear that compensation policies must not be taken for granted and conceived as an automatic or modal response. Inspecting this model suggests that there will be great variability in possible compensatory responses. Response and nonresponse as well as different kinds of responses are determined at various critical points: the diagnosis of risk; the definition and articulation of affected interests; the conception of possible policies against the background of existing policies and institutional arrangements (even at the level of conceiving possible responses, this background will make for a variety of responses across countries); the relative power of interests (including the role of a state more or less autonomous from dominant interests and more or less responsive to weaker interests) in defining the situation; and finally the relative power of interests in deciding about diverse compensatory measures and implementing them.

International exposure is likely to lead to compensating policy responses through the following sequence.

- Actual or anticipated exposure to international markets for goods, services, and capital
- Anticipation of social and economic risks
- Actual changes in the market position of different economic sectors
- Job losses, unemployment, job insecurity, and income volatility in the different branches affected
- Various actors—affected groups and their organizations, political parties, governments—assess risks, ascertain outcomes, and promote policies. Since other actors have interests opposed to these policies, the balance of power among the contending sides shapes diagnosis, decision making, and implementation of policies
- These policies may concern unemployment compensation, retraining, and active labor market policies, but they may also take quite different forms,
for instance increasing income streams not related to market developments such as minimum pensions, welfare in the narrow sense, or generous child support.

Given this variability of compensating reactions, one might be tempted to conclude that the compensation hypothesis faces so many contingencies that it has little value as a master hypothesis. But that conclusion runs into an empirical stumbling block already mentioned repeatedly—the correlations between economic openness and public spending. These correlations are only correlations, but they do exist, and any explanation of social policy developments must account for them.

Two other implications of the hypothetical model are equally important. First, the very contingent character of compensatory responses underlines the decisive role played by the internal balance of power and the capacity to act responsively. Balance of power and the capacity to act have also been identified as the most important factors in the advancement of social welfare policies generally.

Second, quite a few measures that might be considered compensatory may in fact already be in force for other reasons grounded in internal politics. Many features of established welfare states as well as of less established, but domestically rooted social policy projects are “preemptively compensatory.” This probably explains why Miguel Glatzer (this volume) found in his causal tracing of welfare state development in Portugal and Spain few indications of a direct link between exposure to the international economy and social policy proposals.

By contrast, the lower level of social welfare policy in the United States and in particular the much more limited protection against job loss in North America explain why any expansion of free trade runs here into vocal opposition and generates demands for special provisions. Similarly, the fact that small farmers have in many countries—including the United States, Germany, France, and Italy—rather poor social security provisions goes hand in hand with the exemption of farming from most free trade agreements (Rieger and Leibfried 2000, 87–88; see also Rieger and Leibfried 2003). Last but not least, a similar reasoning made the IFIs pay attention to social policy issues after initial neglect in Latin America and Eastern Europe (Huber, and Orenstein and Haas, this volume). The neoliberal character of the policies they recommend should not obscure the fact that these are conceived as compensatory if minimalist social welfare policies. In short, welfare policies are most manifestly compensatory in character where the alternative is no or only a weak social protection against the risks of dislocation.

The compensation view can also invoke two other causal mechanisms. The first is the by now familiar idea that certain social welfare provisions such as high-quality public education, retraining programs, and other active labor market interventions improve the competitiveness of a political economy. Again, these measures may not have evolved as direct responses to international competition, though it is interesting to see that in the United States, a political economy with poorer provisions, education is being discussed as one of the more promising long-term responses to competitive pressures from the international market.

The other causal mechanism worth mentioning in connection with the compensation view is that more openness to the international economy promises—and often delivers—wealth increases that can pay for more generous systems of social security. This certainly is a major reason why the leaders of all advanced welfare states do not seriously consider retreating from economic openness.

### Integration with the Classic Theories of the Welfare State

Finally, it is time to link the causal mechanisms associated with the compensation view and the efficiency view to the classic analyses of the welfare states of advanced capitalist political economies. To simplify, these can be said to have followed three different, though arguably complementary, approaches—the logic of industrialism approach, the state-centered approach, and the power resources approach.

National social policies address in different ways a broad spectrum of risks that became more serious as the capitalist economy intensified its creative destruction of established economic and social patterns, were less amenable to self-help solutions due to changes in family and community structures, and could be tackled with increased economic resources available for collective security projects. These three considerations inform the logic of industrialism approach to explaining the growth of welfare states, though they are quite compatible with the state-centered and power resources approaches as well. Analysts looking at the state as an independently important causal factor focus on the structure of political decision making (for example, checks and balances versus concentration of power in democracies), on the autonomy of the state from—and its responsiveness to—various interests in society, and on the capacity of the state to extract resources and to devise and implement policies. This research has identified important constraints and opportunities for social policy developments. Its interest in the autonomy of the state from dominant interests in society overlaps with the perspective of the power resources approach. The latter, however—concentrating in particular on the balance of class power and detailing the role of unions, parties, and governing political coalitions—has contributed most to the explanation why different forms of social provisions developed in different advanced capitalist countries.

The power resources framework for understanding social welfare policies has been challenged more recently by what some call the “institutional turn” of comparative political economy. This literature emphasizes intraclass divisions of interest and interclass alliances against too simplistic versions of class analysis, and
it focuses on the coordinating capacities of business, government, and labor. More broadly, it sees advanced welfare state systems as indivisible parts of advanced capitalist political economies rather than as protective and redistributing responses of social policy to economic developments from which they remain separate. This certainly has added an important nuance to the balance of class power perspective, emphasizing that the beneficiaries of policies are not necessarily their initiators, that the beneficiaries of social protection are not homogeneous in their interests, and that policy outcomes are almost always affected by the powerful interests of employers and capital owners. These considerations are particularly important for the analysis of welfare policies that have become a fully institutionalized feature of a political economy, and they are therefore especially useful in studying the politics of downward pressure on established social welfare systems.

The three classic approaches worked nearly exclusively with domestic factors, and yet they arrived at impressive accounts of welfare state development. The more recent emphasis on the institutional capacity for coordination is partly inspired by the challenges of international openness, though it, too, focuses on internal institutional patterns. This suggests that it would be a big mistake to discuss the impact of economic openness on social policy in isolation from internal factors. A number of considerations stand out when we look at the impact of international openness on social policy against the background of the domestic roots of systems of social provision.

First, the risks created by international openness are only one subset of the broader spectrum of risks addressed by social welfare policies. Thus, the problems of old age, illness, and disability, which together account for the bulk of social expenditures in all welfare systems, are unrelated to international involvement.

Furthermore, protection against some of the internal risks also protects against international market risks. Dislocation and creative destruction of established economic activities are not only due to international openness but derive from the internal working of capitalism as well. Thus, the problems of job insecurity and income volatility may in a given country well have been addressed independent of international economic openness. However, there appears to be a significant difference between external and internal risks when it comes to perceiving and evaluating them as problems requiring governmental action. This is not only due to the greater difficulty of regulating international markets. Both the fact that foreign competition comes from outside the political community and that boundary maintenance is one of government's established responsibilities tend to make the pressure for protectionist or compensatory state action stronger. This might very well be considered a specific mechanism supporting the compensation view especially, as noted above, in conditions where social policy measures dealing with dislocation and unemployment are as yet nonexistent or weak.

The classic welfare state policies also have important consequences for improving an economy's ability to move toward high remuneration, high-quality production and thus preserve its international competitiveness. Education and public health measures are most relevant here. Income maintenance and transfer policies are less immediately pertinent, though they may affect inequality and poverty levels and thus shape skill levels in the long run. Measures to improve labor force participation occupy a middling position.

Compensation policies require a willingness and capacity to respond to external risks. That is, they require economic resources, a favorable power constellation, and an adequate organizational capability that make a compensatory response possible and effective. Where these conditions exist, social policy responses to internal risks are likely to develop as well. That means that compensatory responses to external risks will often have been preempted by internally motivated policies or take the form of some rounding out of existing measures rather than a de novo policy development.

Where international competition does put downward pressure on welfare state measures, the same domestic factors that the classic studies of welfare state development identified will be important for the consequences. The balance of power, now affected by typically broad popular support for existing policies, is important for resisting these pressures, for developing policy adjustments aimed at the systemic maintenance of social protection, as well as for policies of retrenchment. State capacity is a critical factor as well because it defines options for redesigning social policy as well as tax policy and the financing of social welfare policies. Defense of existing protection, expansion of social policy, and retrenchment rely on the state's capacity for innovation and adaptation. Responses to downward pressures are likely affected by the degree of coordination among the economic, social, and political institutions of a country. Finally, advances or reductions in the available economic resources may be crucial for decisions to cut back welfare provisions or can, in turn, enable a state to finance countermeasures, bridge transition periods, and tackle new problems.

In sum, neither the efficiency hypothesis nor the compensation hypothesis seems by itself to be a major determinant of welfare state development. Both identify potential pressures and outcomes, but these tendencies must be seen in the context of domestic conditions shaping social welfare policies. The actual trajectories of social policy development will rely primarily on conditions within countries. Welfare states are in the first instance shaped by the wealth of nations, by state-society and state-economy relations, and by power relations within countries. If these factors are fundamentally changed by international openness of the economy, we should expect fundamental changes in social welfare policy. The impact of increased capital mobility on the freedom of action of states and the balance of power within societies may have such potential.
The Cases Revisited: Openness and Domestic Conditions

At this point it may be useful to briefly revisit our cases and examine the interplay of international openness and domestic conditions in shaping social policy developments. Are the domestic factors identified by classic welfare state theories as central in the causal accounts of these national and regional developments as they emerged in the preceding discussion of the causal mechanisms underlying social welfare policies?

Latin America

Latin America has seen the greatest negative impact of economic globalization on social policy, and it came about in the wake of sudden and deep economic crises. Both the long-term background and the factors shaping current developments reveal that domestic factors played a critical role in shaping the social policy developments in response to these crises.

Prominent among the long-term conditions are factors—prevalent in many Latin American countries—that do not bode well for compensatory policies or a vigorous defense of existing social protection: a smaller working class in the formal sector; weaker self-organization of subordinate interests in unions and parties; in some countries (for instance, Argentina and Mexico) unions dependent on parties not devoted to subordinate interests; unevenly efficient state bureaucracies that frequently use what autonomy they enjoy to favor particular and often well-to-do groups and strata and often treat subordinate interests with neglectful inefficiency; and finally a legacy of social policies that were overall quite limited and often favored particular interests with special programs. The exceptional cases exemplified by Costa Rica prove the rule: They responded to increased openness with an expansion of social welfare policies, and their long-term historical background is characterized by more effective and more universali-stically oriented state organizations and by a balance of social and political power more favorable to subordinate popular interests.

Domestic factors were also decisive in current developments. The apparent paradox that the spread of formal democracy went hand in hand with a deterioration of social protection finds its explanation in changes that are typical of the majority of Latin American countries: A consequence of deindustrialization, marketization, and the privatization of productive assets is a weakening of unions and popular social and political participation as well as a concentration of economic power. These changes are also related to, and reinforced by, a de facto weakening of parliaments and parties in comparison to executives, a development Guillermo O’Donnell (1994) has aptly called “delegative democracy” (Huber, Rueschemeyer, and Stephens 1997; see also Weyland 1996). Again, the exceptional cases with different social policy developments as well as the details of policy changes in countries that did retrench their social protection confirm that the current balance of social and political power and the structure and capabilities of the state are of critical importance for developments in social policy (Huber, this volume).

Spain and Portugal

Spain and Portugal developed comprehensive welfare states after opening to the international economy in the 1970s. In both countries, the baseline of these developments over the course of the last generation was a rejection of past authoritarian regimes. The democratization of these countries went hand in hand with their new economic and social policies and the balance of power shifted in favor of subordinate interests. Competing unions saw a rapid expansion of their membership, and union power was leveraged by politically instituted extensions of collective bargaining to whole industries. In addition, state elites also were receptive to building a more comprehensive welfare state. In part this seems related to the rejection of the old regime; in Portugal, the threat of Communism played a significant role, and the western European countries offered attractive models as well as supportive advice. The balance of power was favorable for building comprehensive welfare states, and the international political context supported the same policy thrust.

Eastern Europe and Russia

The post-Communist countries of Eastern Europe present a very different picture, though in one formal respect there is an interesting similarity: the current phase of their political and economic histories opened with a radical regime change—the breakdown of East European Communism. Among the cases we considered (and perhaps in all of recorded economic history), this was by far the greatest sudden dislocation of whole political economies. Orenstein and Haas (this volume) emphasize the radical changes the transition entailed. They point to the dramatic differences in economic development and social policy between east-central Europe and the countries of the former Soviet Union. They show that the political economies of east-central Europe became at the same time most internationally integrated and emerged with the most generous new social welfare programs. They describe how during the first years small groups of experts, primarily located in the executive branch, responded to chaotic conditions and uncertain prospects with idiosyncratic policy decisions that had long-term consequences. And they emphasize that international policy influences, including the prospect of joining the European Union as well as very forceful and direct interventions by the World Bank, brought about some convergence in the most recent years even
though the influence of European models and requirements stand in some tension with the thrusts of World Bank advice.

The difference between east-central Europe and the countries of the former Soviet Union (on Russia, see Cook, this volume) seems to an important extent related to the greater international involvement of the Polish, Czech, and Hungarian economies; but it also reflects the longer history of capitalist development that preceded the Communist period in these countries as well as the presence of far more efficient state apparatuses and more propitious state-society relations than are characteristic of today's Russia, Ukraine, and Belarus. The Europe effect, to use Orenstein and Haas's term, as well as the "strong agenda-setting influence" of the World Bank (Orenstein and Haas, this volume) represent a powerful impact of globalization on the East European transition. However, as Orenstein (2001) points out, the abiding orientation of the east-central European countries toward western Europe must not be taken for granted; it has to be seen as a long-term state project whose pursuit gives continuity to post-Communist policy making. Similarly, the pervasive influence of the neoliberal policy ideas of the World Bank cannot be understood simply as an imposition from abroad but has strong roots in the experience with the failing state socialist economy. In Russia, while economic policies and social policy proposals were heavily influenced by international advice, the dilapidated condition of the Russian state, the limited economic recovery from the shock of transition, and the prolonged stalemate between the executive branch and parliament about the restructuring of social welfare policy all point to the major role of internal factors. Overall, there is little doubt that historical experience, the previous structures of the economy and the state, as well as current power relations are playing a major part in shaping the impact of economic globalization on the transitions of post-Communist political economies.

South Korea

Contrary to conventional views, South Korea opened itself late to foreign imports and free capital flows, even though its phenomenal economic development was due to state-managed export-led growth. The later opening to economic globalization coincided with a democratization of its military dictatorship. In the course of these dual developments, South Korean social policy changed from a growth and power maintenance orientation to the provision of an austere but comprehensive system of social protection. Some of this transformation responded to dislocations associated with import competition and capital outflows. That was very clear in the case of policies dealing with unemployment and impoverishment in the wake of the financial crisis of 1997–1998. The transformation as a whole, however, is hardly conceivable without the concurrent process of democratization, which opened the door to some advances in the power of labor. At the same time, it seems that the legacy of segmented social provisions for privileged parts of the population and the as-yet limited transformation of the balance of class power may well mean that the recent welfare policies along compensatory lines will converge more with the residual welfare state of the United States than with the continental European welfare systems.

A second look at the developments in middle-income countries, then, confirms that internal, domestic factors are critical for the consequences of the impact of economic globalization. It also specifies that—and how—politics matters. The critical background factors determining the role of politics seem to be four: the balance of power in society, the capacity for effective state action, the condition and the prospects of the economy, and the legacy effects of earlier social policies. These four conditioning factors accord precisely with the classic theories of welfare state development that were worked out in the European context. The Latin American experience as well as current Korean developments suggest that democratization as such does not seem to favor unequivocally a deepening of social welfare policy. It does so only if it is accompanied by a change in the social and political balance of power in society.

That politics matters and that it in turn is shaped by the background factors identified is strongly backed up by the northwestern European experience. This not only emerges from the overview of John Stephens (this volume; see also Huber and Stephens 2001a). Examining the advanced welfare states in greater detail and more skeptically, Scharpf and Schmidt (2000) arrive at a similar conclusion in their important study of advanced welfare states: differences among these political economies and among their policies matter decisively for the ways in which they adjust to the challenges of changed economic environment (see also Scharpf 2000).

Some Broader Reflections

The compensation hypothesis and the efficiency hypothesis are offsprings of broader conceptions about the role of the market. In its radical version, the efficiency hypothesis derives from the view that the workings of the market are not only more powerful than political action but also provide the best answers to virtually all problems in economy and society. This "market fundamentalism" is not the dominant position among sophisticated economists, but it does prevail in neoliberal policy circles. Beliefs in the market as the primary ordering principle of social and economic life were famously challenged by Karl Polanyi (1957/1944) in his analysis of the decline of the international liberal economic order of the late nineteenth century. And the conception of an "embedded liberalism" (Ruggie 1982; Katzenstein 1985), which we discussed in the introduction, developed these
Neoliberal market fundamentalism represents in our view the intellectually weaker position. We set out with the conviction that the ideas of embedded liberalism offered a more fruitful framework for understanding the interrelations between market functioning, social practices and institutions, and political policy initiatives. We see these initial hunches reinforced by the interregionally comparative chapters as well as by our examination of the social and economic mechanisms that seem to underlie the claims of the compensation and the efficiency view.

Yet if market fundamentalism and the unqualified versions of the efficiency hypothesis are flawed intellectually, we cannot conclude that the worldwide outlook of social welfare policies is on balance positive. At least for the foreseeable future, one may well argue the opposite. In many low- and middle-income countries, the distribution of social and economic power is not favorable for the further development of social welfare policies or even for the maintenance of rather meager provisions. And that is often reinforced by various factors we have discussed earlier, prominent among them the increased mobility of capital and the strength of neoliberal policy ideas in the dominant rich countries and the transnational financial institutions. Similarly, the character of the state is in many countries such that one cannot expect the efficient pursuit of even rather elementary state tasks, not to mention the complex challenges raised by the deep interventions in social life that the creation of strong welfare policies entails. Finally, many countries do not have a policy history that encourages the active pursuit of social welfare, as was the case in the northwestern European countries that now have comprehensive welfare states.

One conclusion of earlier research on social welfare policies is strongly confirmed by our comparative examination of middle-income countries. Long-lasting structural features of society and politics, which typically have deep roots in history, shape and constrain current political action. Prominent among these characteristics of political economies that define the chances of social welfare policies are the long-term balance of power, the capacity of government for effective action, institutional arrangements that help social and economic actors to overcome collective action problems and realize joint “win-win” solutions, the history of past social welfare policies, and the favorable or problematic insertion of the national political economy into the international division of labor.

We have treated these structural constraints as the major qualification of our claim that politics matters: Politics must not be understood as the exertion of sheer political will but as a matter of collective choice that is made in an environment of given. From a different perspective, emphasizing these constraints rather than political action, one might be tempted to conclude that the future is largely determined by the limits they set on political choice. This, however, overlooks one of the most salient political experiences anywhere: To the chagrin of politicians and their commentators the future is far less predictable than the determinists claim.

To put this argument differently, within the constraints we have repeatedly identified, there is a role for agency, for political imagination, and for innovations in social policy that transcend the sheer reproduction of past patterns. This is most clearly expressed in the retrospective views of politicians (Broadbent 1999; Russell 1999; see also Birnbaum 2001).

The interaction of political agency and structural constraints becomes particularly visible in major crises. By definition, crises destroy some of the structural constraints and opportunities that were inherited from the past, and this provides openings for new departures. For the prospects of social welfare policies, the outcomes may be ambiguous. We have argued that sudden and crisis-induced shifts toward greater economic openness created the most important conditions for austere neoliberal social policies in much of Latin America, in New Zealand and Australia, as well as in the former Soviet Union. By contrast, the Great Depression of the 1930s dramatically advanced social welfare policies in the United States, and something similar seems to be happening in today’s South Korea in response to the financial crisis of 1997–1998. In all of these cases, however, political agency and policy ideas gained in importance, even though their success still depended on powerful structural conditions, both those remaining despite the crisis and those radically altered by it.

Our conclusions about the structural constraints and opportunities shaping the prospects of social welfare policies leave us with a number of critical questions about the long-term effects of economic globalization: Does globalization change the underlying structural conditions favoring and obstructing social welfare policies? Does it change the balance of power within nations and between them? Does it affect the capacity of states to make decisions about social policy and to implement them? Does economic globalization transform the structure of political economies and thereby affect the prospects of social policy? Does it enhance or constrain the ability to fund measures of social protection? This volume leaves us without definite answers to these questions, but the answers will determine whether the impact of globalization on social welfare policies will be negative, neutral, or even positive in the long run.

Rather than leaving these questions dangling without any further thought, we will offer a few responses that—however speculative—may be helpful in thinking about the future and, perhaps, in orienting further research. Among the structural changes that can reasonably be anticipated, the most favorable for advances in social welfare policies is probably the likely increase in economic resources. Despite major setbacks in Africa and in the former Soviet bloc, we can reasonably anticipate that most countries will experience long-term economic growth, and this is very likely to be enhanced by economic openness. Even if in many countries this greater openness is not accompanied by reductions in economic inequality (and in some may actually lead to a larger gap between the well-off and
the poor), the overall increase in production very likely makes more funds available for public expenditures, a point that has been forcefully made by Sen (1999).

The balance of power issue is probably the most difficult structural condition to reasonably anticipate. The enhanced mobility of capital, which could be somewhat reduced in the future but is unlikely to be radically curtailed as it was from the Great Depression through the 1960s, certainly represents itself a major shift in power vis-à-vis other interests. But two important qualifications must not be forgotten. First, as we have noted repeatedly, the interests of capital owners are not unambiguously opposed to social welfare policies because these policies are associated with significant direct and indirect productivity gains. The fact that the bulk of international investment goes to countries with substantial social welfare provisions is partly explained by these interests, which transcend simplistic bipolar class images. The second qualification derives from an apparently ineluctable consequence of capitalist development—a long-term shift in social power that favors the many. This is an uneven and in many ways contingent process that relies primarily on an increasing self-organization of society and in particular on the organization of subordinate interests. Contrary to much wishful thinking, which sees free markets and democracy as two sides of the same coin, this self-organization is not enhanced but rather obstructed by neoliberal marketization and the social policies accompanying it. However, in the long run, it is possible and even likely that capitalist development will transform social structures so as to enhance the social and economic power of the many.

The balance of power within countries is inevitably affected by shifts in power across nations. The concentration of geopolitical power in one country, the United States, and the rise of transnational institutions certainly have favored neoliberal policy ideas and undercut the prospects of more comprehensive welfare policies. But it is an open question whether this is a stable constellation. Ideologies and policy ideas are notoriously responsive to short- and medium-term developments in the world economy, and the single superpower as well as the international financial institutions under its sway may face increasing attempts at containment in the future. Certainly, the high degree of autonomy that they currently enjoy represents a worldwide deficit in democracy. One might see here an analogy to the tensions between European states and their societies during the nineteenth century that engendered the rise of modern national democracies, though it is difficult to imagine what form a worldwide equivalent of national democratization might take.

Many hold that globalization spells the end of the national state as we know it. A decisive weakening of the states’ roles would indeed affect the future of social welfare radically, since states are central to the past development of social policy. States are a major feature of the national landscape of power; they represent the arena in which politics is fought out; and their control is the prize of domestic politics. If national decision making becomes sharply constrained, the factors that shaped welfare state development in the past are similarly reduced in importance.

The main basis for the claim of the demise of the nation-state is the vast increase in the power of capital owners in a unified global capital market and the development of transnational economic institutions, from global corporations to the IFIs. Yet it seems that these claims simply extrapolate trends that may or may not continue along the same lines as they developed during the past generation. At present, there are many indications that capital markets are still far away from a worldwide integration. It seems reasonable to conclude for now that the jury is still out on the question of whether capital mobility constrains the degree of freedom of state action sufficiently to affect the potential for social welfare policies.

Furthermore, many overlook a particular leverage states have for influencing the international economy and its institutions. The very legal and institutional framework that underpins international economic transactions as well as the so-called transnational organizations rests on a system of law and regulation that ultimately requires coercive foundations. These are still provided by different ensembles of nation-states. It is true that the power and autonomy of the cooperating nation-states vary tremendously, but even small and medium powers have to make their contribution to let international transactions proceed smoothly. It is obviously hazardous to make predictions about the capacity of states for effective action. Yet it may not be unreasonable to see in their very participation in the international economic system an opportunity to advance organizational effectiveness, as Evans (1985) argued when it was fashionable to identify only negative consequences from international dependence and interdependence.

Will an increasingly integrated and competitive international economy lead to a decline of the forms of coordinated capitalism that have distinguished the continental and Scandinavian political economies from their Anglo-American counterparts? The argument that these more coordinated market economies articulate well with the wage and tax policies undergirding comprehensive welfare states is widely accepted. Deriving from this, pessimistic predictions about the welfare states of northwestern Europe as well as about the chances for social policy in less rich countries may be premature. We are inclined to think that welfare states tend to be overdetermined in their causal conditions, resting, so to speak, on more than one or a few pillars of support. Furthermore, it is not obvious that the cross-class cooperation arising from and reinforcing such economic coordination will be easily abandoned if it has proved advantageous in the past. Finally, even a superficial glance around the political economies of the world quickly encounters other varieties of capitalism that seem to have very sturdy powers of survival. Some of these—for instance, the political economies of Japan and Korea—might also be dubbed “coordinated market economies,” but it is significant to note that they are not accompanied by generous and comprehensive systems of welfare.
On the Value of Comprehensive Welfare States

The past century has seen huge and horrible disasters of collective human effort, whether those efforts were in large measure coerced or based on voluntary enthusiasm. Intentional transformation of societies has so often and so grossly failed in the past that, for many, grand political projects are now in thorough disrepute. James Scott’s *Seeing Like a State* (1998) seeks to describe and explain “how certain schemes to improve the human condition have failed,” as the subtitle puts it. Against this background of state-sponsored horrors, the rise of welfare states stands out as an astounding counterpoint: Comprehensive welfare policies represent profound and sustained transformations of whole societies through state action. Yet these are transformations that have been, and continue to be, embraced by vast majorities of the populations involved.

For Europe and more broadly for the Atlantic community of nations, social welfare policies supported social peace and democracy at critical junctures. This was true of the United States during the Great Depression. Equally important, social policy secured external and internal peace in Europe after the devastations of the Second World War (Broadbent 1999). A consequence of the democratizing shift of power in society, social welfare policy proved in turn to be the foundation of a stable democracy.

The strong grounding welfare state policies find in popular expectations provokes further reflection. We deem this to be a phenomenon of profound significance. Narrowly conceived, the “naturalization” of social welfare programs expressed in popular expectations that consider established benefits to be elementary rights may be construed as rigidities that make restructuring and adaptation of welfare provisions to new conditions and problems difficult. This is indeed the case where overall increases in social revenues are politically problematic, while social change creates new demands or expands old ones. Yet at the same time, such strongly supportive expectations are a critical ingredient in the resiliency of established welfare states. It is significant that Huber and Stephens (2001a) found that while the development of European welfare states was pushed forward in partisan fashion by some political forces against the resistance of others, this partisan effect weakened radically in the subsequent period of stagnation, restructuring, and maintenance.

This can be denounced as the “tyranny of the status quo,” as Milton Friedman did in an interview with the German news magazine *Der Spiegel* (October 9, 2000). But such labeling does not explain which status quo is stable and why. The decline of partisanship in the politics of welfare state maintenance can be taken as an indication of the “objective interests” of people. To argue that something is in the objective interest of people is to make a difficult claim, but it is clear that the pursued interests are not only subject to change and influence but experience transformations that are not easily turned back.” Huber and Stephens speak of a “ratchet effect” of welfare state policy:

Once the policy was instituted, its constituency expanded as its benefits became apparent to the citizenry. In countries such as the Nordic ones, this initiated a path-dependent interactive process in which the policy ratchet effect, labor movement counterhegemony, transformation of social consciousness, policy transformation, left governance, and consequent policies facilitating organization fed each other. As our analyses of the development of women’s movements and gender-egalitarian legislation showed, an exactly parallel path-dependent process developed later between women’s organization, policy developments, and consciousness transformation. (2001a, 343)

We believe that a plausible case for an approximation of actual interests to objective interests can be made if broad populations, and not only narrow segments of past beneficiaries, opt for the security that welfare states offer against risks that are beyond people’s control, provided that they have had the experience of risk as well as security and that they have the chance to consider and express their options.

These fundamental considerations about the resilience of established welfare states in a variety of countries also make us confident that the appeal of social welfare provisions transcends cultural boundaries. Even if the actual prospects for successful social policy are not good for many middle-income countries, not to mention their poorer developing counterparts, we are convinced that the idea of politically sponsored social welfare will remain on the global agenda for the indefinite future.