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Introduction

> The welfare state is the culmination of a centuries-old struggle for social protection and security in the industrialized countries. It may justly be regarded as one of their proudest achievements in the post-war period. It set a model and a standard for aspiration for the newly industrializing and transitional countries as also for the poorer countries.[1]

Let us narrowly define the welfare state as a repertoire of state-led policies aimed at securing a minimum of welfare to its citizens – that is, protecting them against the risks of unemployment, sickness, maternity, and old age – and providing an adequate accumulation of human capital through public investments in health and education. As such, the importance of the welfare state can hardly be overstated. Welfare states are a fundamental part of advanced modern capitalism in the West. They affect income inequality and poverty rates, they shape labor markets, they change public perceptions of how citizens perceive what the role of the state in the economy should be, and they influence the long-term prospects for economic growth through their investments in human capital and their legitimizing role for the political system.[2] It is therefore not surprising that in recent years there has been a proliferation of studies related to the origins, development, and crises of the welfare state.

Researchers have focused on the economic and demographic transformations related to the expansion of welfare effort[3]; on the effects of state

[1] See Ghai (1996).
[2] This discussion draws on Pierson (2000a), who provides a review of the literature on the main effects associated with welfare states. Pierson discusses mainly political effects. The economic effects of welfare states have been also extensively studied by, among others, Atkinson (1999), Barr (1992, 2004), Feldstein (2005), Sala-i-Martin (1999), and Mulligan and Sala-i-Martin (2003).
[3] See, for example, Boix (2001) and Pampel and Williamson (1989).

structure[4]; on the importance of policy legacies[5]; on how the distribution of power among political parties and interest associations generates different "types" of welfare states[6]; on the connection among economic openness, domestic vulnerability, and the establishment of social safety nets[7]; on the relationships among deindustrialization, technological change, and welfare state expansion[8]; and on the impact of aging on the sustainability of the welfare state.[9] Hence, it is not an exaggeration to claim that over the last three decades, the welfare state has been one of the most widely studied objects of inquiry in the political economy literature of advanced capitalist countries.[10]

Unfortunately, however, the welfare state has been one of the least studied topics in the political economy of the developing world.[11] Why, how, and with what consequences have some developing countries institutionalized much more extensive systems of social protection than others? Why do some countries at similar levels of economic development give much more fiscal priority to social security and human capital expenditures than others? How have the recent processes of economic globalization and democratic transition transformed the scope and role of the state for social insurance and human capital accumulation? These are important questions that have received little attention in the study of the political economy of third-world development.[12]

[4] The most notable examples are Huber, Ragin, and Stephens (1993); Pierson (1995); and Castles (1998).

[5] Heclo (1974), Skocpol (1986), Orloff (1993), and Pierson (1996).

[6] See Stephens (1979), Korpi (1983), Esping-Andersen (1991), and Hicks and Swank (1992).

[7] See, for example, Cameron (1978), Katzenstein (1985), Rodrik (1997), and Garrett (1998, 2000a, 2001).

[8] Iversen (2000) and Iversen and Cusack (2000).

[9] See, for example, Heller (2003), Diamond (2005), and Modigliani and Muralidhar (2005).

[10] In addition, the political economy literature comprises a number of related works that have influenced our understanding of political and institutional factors that affect economic policies, including welfare state development. These include, among others, Acemoglu (2003, 2005), Acemoglu and Robinson (2000, 2001, 2006), Acemoglu and Johnson (2005), and Aghion, Alesina, and Trevi (2004).

[11] This is somewhat understandable because social safety nets and systems of public investment in health and education are relatively weak in the developing world, especially in the poorest countries. However, even within the set of developing countries, there is significant variation in the scope and role of the state for social insurance. Further research on this topic is therefore needed to understand why some states in the developing world have more advanced systems of social protection than others, which is precisely one of the main objectives of this book.

[12] Most of the existing literature is somewhat descriptive or based on single case studies that make it difficult to establish causal patterns. The most widely cited source of social security analysis in Latin America is Mesa-Lago (1978, 1989, 2000). Although Mesa-Lago

In an attempt to advance our understanding of these questions, this book has three aims: first, to examine the different paths through which countries in the developing world – especially in Latin America[13] – have constructed (or failed to construct) their welfare systems; second, to analyze the effects of globalization and domestic politics on governments' fiscal commitment to social security, health, and education; and third, to offer a methodology that combines Qualitative Comparative Analysis (QCA), time-series cross-section (TSCS) data, and three in-depth case studies – Chile, Costa Rica, and Peru – to provide new insights into these questions and go beyond the limitations of previous approaches to the subject matter.

The focus on Latin American countries is appropriate for two reasons. First, because unlike in many other developing countries, some Latin American countries have long had welfare systems modeled along European lines, with benefit pension plans, health services, and family allowances. In Chile, Uruguay, and Argentina, for example, these programs began to evolve in the 1920s and even preceded the United States in health-maternity insurance, family allowances, and unemployment compensation.[14]

The second reason is the great process of economic and political change that has swept Latin America during the past three decades. The programs of economic reform and structural adjustment of the 1980s led to the

is a fundamental source of information on social security systems in Latin America, his analysis tends to be somewhat descriptive. The same occurs in other excellent single case studies that bring to the fore the importance of specific country-level factors but have more limited value to make broader generalizations, such as Malloy (1979), Raczynski (1994), and Filgueira (1995). Hence, in the context of the developing world, there is little quantitative and comparative research on the origins and development of income security programs and other policies usually associated with the welfare state. Also, unlike researchers who focus on OECD countries, students of developing countries have hardly made use of some of the most advanced statistical techniques (e.g., regression with panel data) or recent developments in the use of the comparative method (e.g., Boolean algebra), which are able to overcome the problem of "too many variables, too few cases." Some exceptions would be Huber (1996), who provides a qualitative comparative analysis of the origins and recent development of social policies in five major Latin American countries; and Brown and Hunter (1999), Kaufman and Segura-Ubiergo (2001), Huber et al. (2004), and Hunter and Brown (2005), who use quantitative methods.

[13] The reasons for choosing Latin America as the main regional focus of this study are provided herein.

[14] See Mesa-Lago (1989, xv). Also, if we focus on more recent data, in the 1990s, pension spending as a percentage of GDP reached 15 percent in Uruguay – a larger percentage than in every OECD country except Italy. Argentina, Brazil, Chile, Nicaragua, and Panama ranged from 4 to about 6 percent of GDP. These figures are similar to those of a number of OECD countries such as Australia (4.6), Canada (5.4), Iceland (5.7), Ireland (7.1), and New Zealand (6.2). For a comprehensive analysis of pension systems around the world, see Palacios and Pallares-Miralles (2000, 29–42).

abandonment of the previous model of development based on import substitution industrialization (ISI).[15] The ISI model, which had characterized at least the largest Latin American economies since the 1930s and 1940s, has given way to a new economic model based on a much closer integration of Latin American societies into international trade and capital markets. At the same time, Latin American countries were among the first to join the so-called third wave of democratization.[16] Thus, the fact that these democratic transitions took place more or less concurrently with the process of economic integration into trade and capital markets brings to the fore the question of whether democracies can mitigate the potentially negative effects of globalization on social spending. In short, the focus on Latin America is appropriate because, as Mesa-Lago noted, it "has been a leader of social security development in the Third World."[17]

The book is structured in three interrelated but substantively and methodologically different parts. The first part, focusing on the preglobalization period (i.e., 1920–1979), analyzes why some Latin American countries have historically developed more comprehensive systems of social protection than others. Using QCA,[18] two alternative paths to the welfare state in Latin America are identified: with and without favorable economic conditions. Favorable economic conditions include economic development and protection from international market competition. Under these circumstances, only one political condition – democracy or left-labor power – was necessary to develop a welfare state. Four of the five cases of relatively more developed welfare systems followed this path: Argentina, which had a strong left-labor movement but little history of continuous democracy; Brazil, which had relatively weak Left parties and dependent labor unions, but remained

[15] ISI was an inward-looking model of economic development that rested on a mix of policies regarding tariffs, licenses, quotas, and exchange rates that shielded domestic producers (especially in manufacturing) from international-market competition. For a comprehensive analysis of ISI policies within a cross-regional comparative framework, see Haggard (1990).

[16] The original notion of the "third wave" of democratization comes from Huntington (1991). Huntington is referring to the wave of democratization that started in Portugal in 1974, swept Southern Europe and Latin America in the 1980s, and also transformed the political systems of most Eastern European countries and some African countries in the 1990s. For a review of the enormous literature on the third wave of democratization, see Geddes (1999).

[17] Mesa-Lago (1989, xv).

[18] For a detailed analysis of the method of QCA, see Ragin (1987). For a comparison of QCA versus other quantitative and qualitative methods of inquiry in comparative cross-national research, see Janoski and Hicks (1994). For a more recent application of QCA to the consolidation of welfare systems in advanced industrial countries, see Hicks (1999).

continuously democratic for eighteen years during the period under study; and Chile and Uruguay, which had both a long history of continuous democracy and a strong left-labor movement. However, in the absence of left-labor power, the "type" of welfare system that developed (as in Brazil) was more fragmented and regressive than when both political conditions where present (as in Chile and Uruguay). Alternatively, when economic conditions were unfavorable (i.e., low levels of economic development and high levels of trade openness), both political conditions – democracy and left-labor power – were necessary to develop a welfare state. This is the path followed by Costa Rica – the only country in Latin America that constructed a welfare state in the absence of a relatively high level of development.

The second part studies the relationship among globalization, domestic political institutions, and one of the most important aspects of the welfare state: social expenditures. The focus is on the 1973–2003 period – the longest period for which relatively reliable cross-national time-series of fiscal data are available for most Latin American countries.[19] The analysis uses a TSCS data set based on annual observations of public expenditures on health, education, and social security programs. The discussion revolves around a few fundamental economic and political hypotheses.

The economic hypotheses study the relationships among economic growth, the fiscal capacity of the state, and the growing integration into trade and capital markets on governments' fiscal commitment to social security and human capital expenditures. The political hypotheses analyze the effects of democracy and the balance of power between political parties and interest associations on the consolidation and development of different levels of welfare effort. The results show that growing levels of trade openness have been associated with significant reductions in social spending. However, this effect is not the same for all categories of social spending: the negative impact of trade openness operates entirely through its effect on social security expenditures, with no statistically significant impact on health and education. By contrast, the shift to democracy had either no impact or a negative impact on social security expenditures (which tend to be relatively regressive in the region) but was associated with an increase in

[19] As of mid-2005, the 1973–2003 period maximizes the number of annual observations that can be obtained from the IMF's *Government Finance Statistics* series. Most countries began to systematically report data on government expenditures to the IMF in 1972–1973. Data coverage after 2003 is not generally available for most countries. The study of this period is particularly important because it covers both the process of international-market integration (usually known as "globalization") and the "third wave" of democratic transitions that began in the mid-1970s.

health and education spending (which tends to reach a broader segment of the population). Openness to capital markets had a negative effect on social spending only when the fiscal deficit was relatively high, making it difficult to reduce it without cuts in social programs.

The third part of the book is based on three case studies of Chile, Costa Rica, and Peru. The rationale for the case studies and justification for the selection of them are also provided. The remainder of this chapter is organized in four sections. The first section is a brief review of the main theories of the welfare state; the second section explains how the idea of the welfare state can be applied to the developing world and situates the Latin American welfare states in comparative perspective with other regions; the third section describes the methodological approach followed in the book; and, finally, the last section summarizes each chapter.

1.1 The Welfare State: Review of Main Theories

In advanced industrial democracies, the welfare state can be seen as the culmination of a long process that began in the eighteenth century with the establishment of legal–civil rights, continued in the nineteenth century with the emergence of political rights, and culminated in the twentieth century with the consolidation of what Marshall called social citizenship.[20] However, the welfare state did not necessarily emerge gradually as the natural or automatic consequence of economic and political development. In fact, the origins of the modern welfare state in most countries can hardly be understood without taking into account the role of reformist political elites who either responded to the demands of an increasingly mobilized working class or acted preemptively to defuse labor agitation. The most notable example is Germany, where, in the 1880s, Chancellor Otto Von Bismarck – founder of the first modern welfare state – pursued a variety of political motives through state-sponsored social insurance.[21] According to Steinmetz, Bismarck had a combination of motives that included bypassing the Reichstag, splitting the liberals, and binding workers directly to the state.[22]

After World War II, the welfare state and its attendant income security programs became an intrinsic part of capitalism's postwar "Golden Age" – an era in which "prosperity, equality and full employment seemed in perfect

[20] See Marshall (1963).
[21] For an extensive review of the rise of social spending in the 1880–1930 period, see Lindert (1994). He argues against the conventional wisdom that the leader in welfare state development was not Germany but rather Denmark and Ireland (p. 15).
[22] For a detailed analysis of Bismarck's motives, see Beck (1995) and Steinmetz (1996).

harmony."[23] Some of the first conceptualizations of the "welfare state" are due to the English historian Asa Briggs.[24] According to Briggs, a state can only qualify as a "welfare state" if it undertakes three kinds of activity. First, it must provide individuals and families with the necessary income guarantees to escape poverty. Second, it must remove or significantly mitigate social risks associated with sickness, old age, and unemployment. And, third, it has to offer all citizens access to a certain range of social services.[25] As Castles points out, in contemporary welfare states, the first and second objectives have been accomplished through social security transfers, which provide assistance to the poor and income maintenance to those who fall under a wide variety of social risks. The third objective has been accomplished through high-quality public health and educational systems that have progressively been regarded as a social right of citizenship.[26] According to these criteria, the welfare state is a postwar creation.[27]

But, what factors account for the development of the welfare state? Scholars have generally identified four main theoretical perspectives. On the one hand, the "logic of industrialism" theory and economic-openness theory, which emphasize economic factors; on the other, the class analytical tradition and state-centric approaches, which emphasize political factors. First, theories that refer to the "logic of industrialism" emphasize how the welfare state emerges in the process of industrialization to respond to exogenous economic imperatives. Industrialization is associated with a deep transformation of socioeconomic structures and with transitions from agriculture to industrialism, from rural life to urban life, and from personal relations to abstract exchange relations.[28] This process involves dislocations in the family and work relations. As Pampel and Williamson noted, because many

[23] See Esping-Andersen (1991, 1).

[24] For a discussion of Briggs's contribution, see Castles (1998). This discussion draws on Castles's analysis.

[25] Another broadly used definition of the welfare state was provided by Wilensky, who argued that the essence of the welfare state is a series of "government-protected minimum standards of income, nutrition, health, housing and education, assured to every citizen as a political right, not charity" (1975, 6–7).

[26] Castles (1998, 146).

[27] These criteria need to be applied with care, however. A stringent application would lead to a small sample of welfare states even in advanced capitalist democracies. The criteria provide a general view to analyze the great deal of variations among countries at each level of development in the scope of their income-maintenance programs and social services. According to this view, the idea of the welfare state can be applied to any country. We need, then, to explore how and to what degree a given country satisfies these functions of income maintenance, protection against poverty, and social-service provision.

[28] Hicks (1999, 17).

vulnerable persons are unable to obtain traditional support from family members, the state expands to provide social welfare support.[29] A related argument is Wagner's well-known law of "increasing state activity."[30] According to this law, the size of the public sector grows with real per capita income as a response to the expanded administrative needs of an increasingly complex industrial society.[31] Furthermore, economic development fosters changes in the demographic structure of society that are important for the growth of the welfare state. Because of the loss of traditional family support, an increasing part of the social welfare effort of governments is directed to the aged in the form of pension transfers.[32] This is, first and foremost, a functionalist theory. The state expands because of exogenous technological and industrial pressures and responds (almost automatically) to the economic and demographic needs of the population. As such, this theory cannot specify the mechanisms that link industrial needs and the problems of the aged with welfare state expansion.

The second economic perspective (not necessarily in opposition to the first) emphasizes the relationship between economic openness and the welfare state. This perspective focuses on why and how social welfare expands to compensate the losers of international-market competition. Supported by a substantial body of empirical research on advanced industrial countries, the main argument is that globalization is associated with the expansion of the welfare state. The mechanism that connects globalization with the expansion of the welfare state can be summarized in three steps: first, growing exposure to international markets increases economic insecurity and inequality[33]; second, as a result, vulnerable economic actors – for example, those who have lost their jobs or work in industries that cannot face up to the challenges of international competition – will use political channels such as trade unions and political parties to press the governments for

29 Pampel and Williamson (1989, 26).
30 Wagner, A. 1883. *Finanzwissenschaft*. Translated and reprinted as "Three Extracts on Public Finance." In R. A. Musgrave and A. T. Peacock, eds., *Classics on the Theory of Public Finance*. London: Macmillan.
31 For a more recent analysis of Wagner's Law and how economic development combined with other political factors is associated with an expansion of the public sector, see Boix (2001, 1–17).
32 Wilensky (1975).
33 According to the Hecksher-Ohlin-Samuelson factor-endowments model, expanding levels of trade will increase the demand for the relatively abundant factor of production and reduce the demand for the relatively scarce one. Because in developed countries skilled labor is the relatively abundant factor and unskilled labor the relatively scarce one, expanding trade, especially with developing countries, is likely to widen the wage differential between skilled and unskilled workers.

compensation; and, third, governments will respond to these pressures by expanding the welfare state to protect the domestic economy, control political unrest, and put into place programs designed to raise the skills of the labor force and make it more competitive in international markets. Until recently, this theory had been considered one of the most important determinants of welfare expansion in advanced industrial economies. However, recent work by Iversen and Cussack has cast some doubt on this hypothesis. These authors argue that most of the risks associated with modern industrial societies are the result of technologically induced structural transformations in national labor markets, such as increases in productivity, changes in consumption patterns, and saturated demand for products from the traditional sectors of the economy. According to these authors, it is these structural sources of risk that fuel demands for state compensation and risk sharing.[34]

The third and fourth theoretical perspectives highlight political factors. The "class analytical tradition" or "power-resource theory" focuses on how working-class actors, union organization, and worker representation by broadly socialist parties are the key determinants for development and expansion of the welfare state. In this perspective, what matters for welfare state development is working-class mobilization, combined with various political–institutional conditions.[35] This theory further assumes that the basic cleavage in society is between capitalists and the working class, and that it is reflected in political behavior: low-income people will vote for parties of the Left and high-income people will vote for parties of the Right.[36] The degree of working-class power and the size and centralization of labor unions determine whether left-oriented parties will be elected and will expand social welfare to favor the working class.[37] The core of this theory is best captured by Huber and Stephens, who argue that the struggle of the welfare state is a struggle over distribution. Hence, what is crucial is the organizational power of those standing to benefit from redistribution – that is, the working and middle classes.[38] An initial empirical problem with this theory, however, is that authors seem to disagree as to whether what matters

[34] Iversen and Cussack (2000, 303).

[35] Hicks (1999, 20).

[36] For the classical statement about the relationship among class identity, party systems, and voter alignments in a number of advanced industrial democracies, see Lipset and Rokkan (1967); for an analysis of class identity and the welfare state, see Korpi (1983).

[37] The main problem with this theory is that in most countries, the unionized constituency of leftist parties is too small to gain control of the government without strategic alliances with other groups. These alliances may compromise Social Democratic ideals associated with the welfare state. For a comprehensive analysis of this argument, see Przeworki (1985).

[38] Huber and Stephens (2001, 17).

is the percentage of Left votes, Left seats in parliament, or union organization. Some recent empirical analyses demonstrate, however, that the best predictor of welfare state generosity is the long-run partisan character of the government.[39]

Finally, the fourth theoretical approach to the origins and development of the welfare state focuses on the paternalistic actions of state autocrats and the policy-making capabilities and orientation of state institutions.[40] This perspective highlights two fundamental state characteristics associated in different ways with the welfare state. The first is *state centralization*, which makes it easier for state managers to develop and implement welfare policies. Some have argued, for example, that federalism – with its decentralization of finances and dispersion of authority – dampens the degree of expansion of the public economy,[41] or that competitive deregulation in a decentralized system could fuel a downward spiral in social provision, leading to "lowest common denominator" social policies.[42] According to this view, the concentration of decision making in the central government minimizes the veto power of subnational governments or the blocking potential of a fragmented opposition. Second, the welfare state may also expand as a function of the bureaucratic strength of administrative agencies. As Niskanen noted, government bureaucracies struggle to expand their budgets in order to be in a better position to reach their goals.[43] Hence, welfare state expansion will also be related to the power of welfare state agencies. Evidence from the American States and the industrialized democracies provides some empirical support to the idea that budget-maximizing state bureaucrats may act collectively to maximize public spending.[44]

1.2 The Welfare State: Latin America in Comparative Perspective

Whereas economists and political scientists are still debating the "origins," "worlds," "developments," and "consequences" of welfare state expansion, a growing number of studies from the Organization for Economic Cooperation and Development (OECD) have now changed their analytical focus to emphasize the "transitions," "contradictions," or "crises" of the welfare state.

39 Huber, Ragin, and Stephens (1993) and Huber and Stephens (2001).
40 See Hicks (1999) and Hicks and Swanke (1992).
41 Cameron (1978, 1253).
42 Pierson (1995, 452).
43 Niskanen (1987).
44 See Korpi (1989).