WHAT DOES DEVELOPMENT HAVE TO DO WITH IT? DISAGGREGATING THE IMPACT OF ECONOMIC GLOBALIZATION ON THE WELFARE STATE

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Abstract

This study examines the relationship between economic globalization and the welfare state for the time period of 2000-2014 by employing a cross-sectional time-series regression analysis. The main findings indicate that the effect of economic globalization on the welfare state varies based on countries' levels of economic development. While the effect is positive for advanced economies, the opposite is true in the case of the developing ones. Furthermore, this study makes an original contribution to the literature by dividing the developing economies into two distinct groups – the emerging and the least developed economies – in order to examine whether globalization affects them differently. The findings suggest that the emerging economies are more adversely affected compared to their least developed counterparts. Finally, the last part of the study finds the effect of globalization on the welfare state varies by region. Europe and Central Asia have generally seen an increase in social spending in the face of increased globalization, countries in East Asia and the Pacific, Latin America and the Caribbean, as well as North America have witnessed welfare state retrenchment, while a negligible positive effect was detected for African states.

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1. Introduction

What are the implications of increased market liberalization and economic interdependence for the welfare state? Will this institution survive recent globalization[1] trends or it will succumb to the pressures of international markets? These are some of the questions academics posed at the turn of the century, framing the debate around the globalization-welfare nexus and providing theoretical foundations for numerous empirical inquires that followed. Early doomsday scenarios – backed by economic theory of international trade -- had suggested that increased trade liberalization and factor mobility will induce a 'race to the bottom' between countries, as governments will be compelled to lower their taxes in order to keep existing investors and attract new ones. As a result of lower tax rates, governments' fiscal power will be reduced, in turn leading to the retrenchment of welfare policies. However, several early analyses had refuted the race to the bottom theory, providing extensive empirical evidence suggesting that social spending did not decline as a result of increased market exposure.[2] Moreover, most of the studies found a positive relationship between globalization and social spending, implying that the welfare state had not only survived but also significantly expanded in the context of increased globalization. At the heart of the argument of the above studies was the ability of labor and other interest groups to effectively organize and pressure government into offering generous welfare transfers to help alleviate the inevitable short-term pain caused by opening up to the international market.

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[1] Globalization, economic globalization and market liberalization are used interchangeably throughout this paper

[2] Dani Rodrik, "Has Globalization Gone Too Far?," *California Management Review* 39, no. 3 (April 1, 1997): 29–53; Geoffrey Garrett, "Shrinking States? Globalization and National Autonomy in the Oecd," *Oxford Development Studies* 26, no. 1 (February 1, 1998): 71–97; Layna Mosley, "Room to Move: International Financial Markets and National Welfare States," *International Organization* 54, no. 04 (September 2000): 737–73; Duane Swank, *Global Capital, Political Institutions, and Policy Change in Developed Welfare States* (Cambridge University Press, 2002); Vito Tanzi, "Globalization and the Future of Social Protection," *Scottish Journal of Political Economy* 49, no. 1 (February 1, 2002): 116–27.

However, while globalization has penetrated much of the world, all initial studies disproving race to the bottom –for lack of comparable data in the rest of the world – had focused on a small group of the world's most advanced economies, while at the same time attempting to generalize their findings and the underlying mechanisms. This is particularly problematic, as a crucial link in the causal path suggesting that globalization increases social spending relies on the strength of labor or other organized interests, which are generally weaker outside of the advanced world. Nita Rudra was the first scholar who noted and investigated the discrepancy in the welfare spending between the OECD nations and the developing world.[3] As seen in her graph below, at the beginning of the 1970s, government welfare expenditure in the developing countries was roughly comparable to that of world's most developed nations. However, over the next few decades, the two groups of countries have significantly diverged with respect to their spending on social policies. While there was a slow but steady increase in the overall welfare expenditure in the developed countries, the developing ones have shown stagnation or even decline in their spending on social policies. Based on more recent data collected for this analysis, this gap remains and there in no sign of convergence (see Figure 5).

This persistent gap in the average amount of the gross domestic product (GDP) that developed and developing countries allocate to spending on social policies is the main motivation behind my analysis. At the same time, the majority of existing studies focused on the developing world did not manage to fully explain the variation in social spending trends nor come to a consensus with regard to the underlying mechanisms driving the relationship between globalization and welfare state in this group of countries.[4] In addition, while most studies did find a positive

[3] Nita Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries," *International Organization* 56, no. 02 (March 2002): 411–45.

[4] Studies focusing on the welfare state in the developing countries are discussed in detail in the theoretical framework below

effect, a few made claims of the opposite direction and even of no significance in the effect of globalization on welfare spending.[5] The inconsistent findings, together with more comprehensive welfare spending data available since Rudra's study was published provide a compelling reason to revisit the globalization-welfare state nexus in the context of the developing world. In addition, I attempt to contribute to the literature by further dividing the developing countries into two subgroups: the emerging and the less developed economies. Given the different stages of economic, as well as welfare state development between the two groups, I predict that the mechanisms driving social spending policies might be impacted by different sets of factors. Finally, inspired by several arguments of region-specific differences -- with regard to the development and the generosity of the welfare state -- I investigate whether the effects of economic globalization on social spending vary by region.

Taking into account both the theoretical background as well as key empirical inquiries conducted to date, I hypothesized that globalization has a negative effect on the welfare state in the developing countries. The rationale behind this claim is based on several factors which indicate different mechanisms in the developing countries compared to their developed counterparts. First, most studies of OECD countries have cited labor power, as well as the formation of interest groups consisting of welfare consumers that were able to successfully bargain with the government to prevent the retrenchment of social policies. However, the developing countries are generally characterized by low levels of labor centralization, resulting in low bargaining power and the inability

[5] Robert R. Kaufman and Alex Segura-Ubiergo, "Globalization, Domestic Politics, and Social Spending in Latin America: A Time-Series Cross-Section Analysis, 1973–97," *World Politics* 53, no. 04 (July 2001): 553–87; Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries"; George Avelino, David S. Brown, and Wendy Hunter, "The Effects of Capital Mobility, Trade Openness, and Democracy on Social Spending in Latin America, 1980–1999," *American Journal of Political Science* 49, no. 3 (July 1, 2005): 625–41; Erik Wibbels, "Dependency Revisited: International Markets, Business Cycles, and Social Spending in the Developing World," *International Organization* 60, no. 02 (April 2006): 433–68.

to coerce the government into maintaining a constant level of benefit spending in the face of increased market exposure.

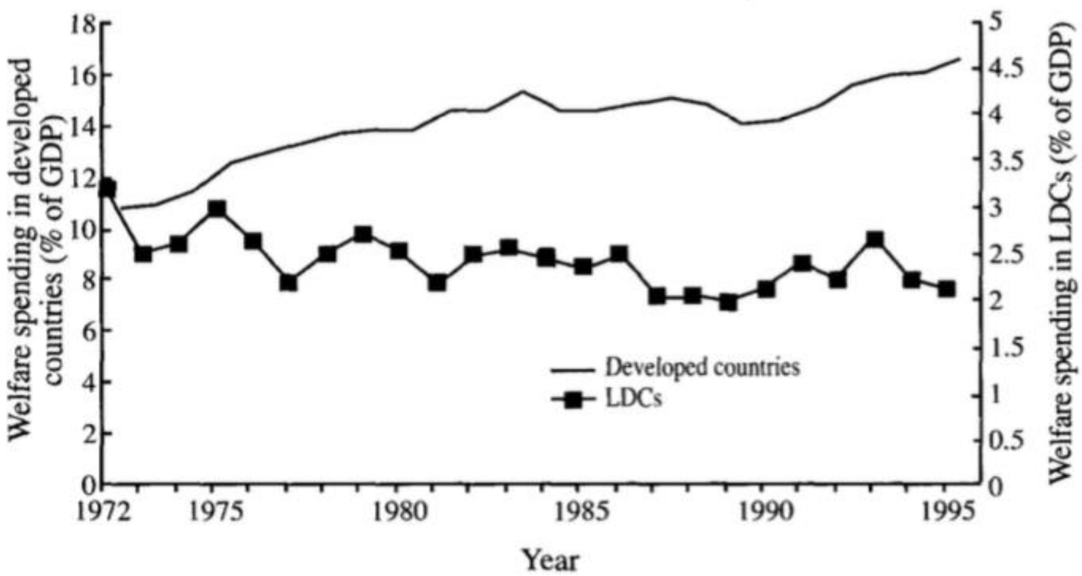

Figure 1: *Contrast in government welfare spending between developed and developing countries (1972-1995), adopted from Rudra (2002)*

In addition, the world's most advanced nations are well-established longstanding democracies, in which elected governments have stronger incentives to compensate their constituencies for the hardships generated by globalization in order to win their support for market liberalization. In contrast, many of the developing countries are relatively weak democracies, some with significant levels of institutionalized autocracy, and thus might not feel as obliged to mitigate their citizens' suffering as a result of market liberalization. Finally, different factor endowments dictate inherently diverse integration paths into the global market for the two groups of countries. The developing countries have both lower access to capital markets and higher imperative to maintain balanced budgets. As a result, unlike their advanced counterparts who are more easily able to borrow money, they are compelled to resort to welfare state contraction in order to keep a balanced budget during economic downturns.

My main findings indicate a significant and negative effect of economic globalization on the welfare state in the analysis conducted on a global sample for the period between 2000 and 2014. At the same time, the analysis involving developed economies was in line with the previous studies, suggesting a positive and significant effect for this group of countries. Furthermore, I find that globalization has a statistically significant negative impact on both of the developing countries' subgroups, but the negative effect is significantly stronger in the emerging economies compared to the least developed ones. Finally, by using interaction terms between several regions and the KOF index, this study finds that regional differences are statistically significant. On average, the impact of globalization on welfare spending was positive in Europe and Central Asia, as well as Africa, while negative in all other regions. Based on these findings, my research contributes to the debate around the globalization-welfare nexus by specifying that the effects of globalization on the welfare state vary by the level of development. While globalization prompts governments to compensate their citizens through welfare benefits in advanced economies, its effects tend to deteriorate social benefits in less developed countries and, even more severely, in emerging economies. The nuanced effects of globalization detected in this research suggest caution in generalizing findings from advanced economies and emphasize the need for research specifically focused on emerging and less developed economies.

This thesis proceeds as follows: First, I frame the debate around the globalization-welfare state nexus, following with a literature review of the empirical studies conducted in the developing world. Then, I present a theoretical framework used to analyze the impact of globalization on the welfare state in the developing countries and build a statistical model to empirically assess my assumptions. Furthermore, I present the results of my regression and comment on the differences in welfare spending between the advanced nations and developing countries, as well as the differences between the two subgroups of the developing countries. Finally, I conduct an analysis to examine whether there are significant regional differences in the effect globalization has on the welfare state and comment on the results. I conclude by summarizing the main findings, discussing the limitations of my study, and giving suggestions for further research.

2. Theoretical Framework

2.1 The Globalization-Welfare State Nexus in the Literature

When it comes to the globalization-welfare state nexus, there is plethora of disagreements in the literature. The conventional wisdom -- supported by economic theory -- suggests that, in the age of globalization, national governments have to prioritize being competitive on the international market. In order to do so, they are forced to adopt *laissez-faire* policies, which are likely to have an adverse effect on welfare spending.[6] For one, the existence of generous welfare benefits is likely to reduce individuals' incentives to work and put upward pressures on labor costs, both of which is claimed to have a negative effect on export competitiveness. At the same time, market liberalization allows for higher level of capital mobility, thus making it easier for owners to move their means of production across countries seeking lower costs. Finally, governments are becoming reluctant to borrow in times of crisis, as higher government debt and an increase in interest rates on government bonds can potentially deter investment. As a result of all this, lowering tax rates on capital and labor becomes an imperative for national governments in order to increase exports, attract foreign investment, and prevent capital flight, leading to what has been labeled as the 'race to the bottom' in the literature. Therefore, according to the proponents of this theory – also known as the efficiency hypothesis – the welfare state's ability to intervene and provide a safety net for its citizens in the instances where the market has failed to do so is limited by the fact that it too becomes vulnerable to the same market forces.

[6] Fritz W. Scharpf, "Games Real Actors Could Play: Positive and Negative Coordination in Embedded Negotiations," *Journal of Theoretical Politics* 6, no. 1 (January 1, 1994): 27–53; Philip G. Cerny, "Globalization and the Changing Logic of Collective Action," *International Organization* 49, no. 04 (September 1995): 595–625; Anne Gray, "New Labour—new Labour Discipline," *Capital & Class* 22, no. 2 (July 1, 1998): 1–8; Swank, *Global Capital, Political Institutions, and Policy Change in Developed Welfare States*; Tanzi, "Globalization and the Future of Social Protection."

However, the conventional wisdom behind this theory has been challenged by several studies suggesting that there is neither theoretical nor empirical evidence linking the increase in economic globalization to welfare state retrenchment.[7] Scholars who support this view (i.e., the compensation hypothesis) believe that, rather than retrenching its welfare spending in the process of market liberalization, governments are more likely to increase expenditure on social policies in order to provide adequate compensation for those who lost from the process of globalization. As Geoffrey Garrett points out, the welfare state has not lost its significance and there still exists a leftist alternative to free market capitalism which emphasizes the importance of government regulations and the provision of social policies. In his study of the welfare state in fourteen OECD countries, Garrett came to a conclusion that market liberalization results in higher government spending on different redistribution programs aimed at compensating for the injustices generated by free markets.[8] However, Garrett argues, this is conditioned by the level of labor market centralization, as only well-developed and highly institutionalized labor markets can effectively negotiate with the government to ensure that inequities created as a result of market liberalization are adequately compensated for.[9] While this mechanism is relatively well-established in the literature, its sustainability seems less secure given that liberalization has also affected industrial relations to varying degrees.[10]

In addition to Garrett's emphasis on labor as a key factor contributing to the resilience of the welfare state across developed nations, some scholars have offered other institutional

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[7] Garrett, "Shrinking States?"; Evelyne Huber and John D. Stephens, *Development and Crisis of the Welfare State: Parties and Policies in Global Markets* (University of Chicago Press, 2001); Francis G. Castles, *The Future of the Welfare State: Crisis Myths and Crisis Realities* (OUP Oxford, 2004).

[8] Garrett, "Shrinking States?"

[9] Ibid.

[10] Rebecca Kolins Givan and Chris Howell, "Rethinking Institutions and Institutional Change in European Industrial Relations," British Journal of Industrial Relations 49, no. 2 (2011): 231–55; Kathleen Thelen, Varieties of Liberalization and the New Politics of Social Solidarity (Cambridge University Press, 2014).

explanations, such as deindustrialization or the influence of various interest groups.[11] For example, Pierson argued that those groups of citizens which are likely to be dependent on welfare benefits, such as the elderly, disabled or unemployed, had mobilized in order to prevent the deterioration of the welfare state.[12] At the same time, several other studies have claimed that, although essential, organized labor institutions alone are not always strong enough to resist the change in social spending and they need to seek strategic allies in various middle-class groups[13]or political parties.[14] However, as Nita Rudra notes, by focusing on other important factors, these studies have "de-emphasize[d]" and taken for granted the role that well-institutionalized labor unions still play in preventing welfare state retrenchment in developed nations.[15] In case of atomized labor groups, argues Rudra, coalition-building with other interest groups as well as their ability to influence policy-making are significantly limited, a finding that has important implication for the developing world.[16]

2.2 Evidence from the Developing Countries

Most of the aforementioned studies that empirically refuted the race to the bottom theory -- rejecting causality between globalization and the welfare state retrenchment -- have focused on the developed countries. In other words, it is well-established in the surveyed literature that, in the developed nations, those groups which are negatively affected by globalization have access to formal

[11] Paul Pierson, "The New Politics of the Welfare State," *World Politics* 48, no. 02 (January 1996): 143–79.

[12] Ibid.

[13] Gøsta Esping-Andersen, "The Three Political Economies of the Welfare State," *International Journal of Sociology* 20, no. 3 (1990): 92–123.

[14] Alexander M. Hicks, *Social Democracy & Welfare Capitalism: A Century of Income Security Politics* (Cornell University Press, 1999); Huber and Stephens, *Development and Crisis of the Welfare State*, 2001; Karen L. Remmer, "The Politics of Economic Policy and Performance in Latin America," *Journal of Public Policy* 22, no. 01 (January 2002): 29–59.

[15] Nita Rudra, *Globalization and the Race to the Bottom in Developing Countries: Who Really Gets Hurt?* (Cambridge University Press, 2008).

[16] Ibid.

democratic means which enable them to effectively negotiate with governments. Taking this into account, some researchers have expressed their surprise at the scholarly neglect of not only the potential implications of globalization, but more generally the origins, the development, and the dynamics of social spending policies in the developing world. As Alex Segura-Ubiergo notes, some of the richer countries in Latin America -- such as Argentina, Uruguay and Chile -- had established welfare systems before their OECD counterparts, yet there have been very few theoretical and empirical inquiries into the welfare state in the region, or the developing world in general.[17] While problems with finding comparable data outside of OECD had posed a serious challenge to the researchers, this has changed in the past few decades as both domestic and international agencies have begun to collect reliable statistics and assemble more comprehensive datasets.

In the first major study focusing on the developing world, Kaufman and Segura-Ubiergo tested their theoretical assumption that increased market liberalization should compel governments in the developing world to increase welfare spending, in line with Garrett's argument confirmed by the OECD data.[18] First, neoliberal economic reforms are likely to be painful in the short run, as the economy adjusts to the demands of international competition and establishes itself on the international market. This, in turn, could lead to social and political instability, with citizens expressing disapproval towards the government pursuing market-oriented policies. In order to prevent popular backlash against liberalization, it is in the interest of the government and businesses to ensure generous welfare transfers to those who are negatively affected in the process.[19] Similarly,

[17] Alex Segura-Ubiergo, *The Political Economy of the Welfare State in Latin America: Globalization, Democracy, and Development* (Cambridge University Press, 2007).

[18] Kaufman and Segura-Ubiergo, "Globalization, Domestic Politics, and Social Spending in Latin America."

[19] Ibid.

as being internationally competitive becomes vital for the economy, governments should feel compelled to invest in human capital in order to enhance labor skills and productivity.[20]

However, when testing these hypotheses on their sample consisting of 14 Latin American countries for the period between 1973 and 1997, the authors found that liberalization had constantly negative effects on social spending. Moreover, political factors proved to be important determinants of social spending, especially when it was disaggregated into social security transfers (pensions and unemployment benefits) and human capital expenditure (health and education). The study found that the negative effects of market liberalization have mainly affected social security transfers, while the expenditure on human capital was less influenced. At the same time, they showed that popularly based governments tended to maintain the levels of welfare transfers -- which cater to the middle-class and union members -- despite increased liberalization.[21] Finally, the study found that democratic governments were likely to spend more on health and education compared to their autocratic counterparts, confirming the results of a similar study done by Brown and Hunter, which also examined the connection between regime type and welfare spending.[22]

In another seminal study, this time encompassing developing countries from all over the world, Nita Rudra noted that trends in government welfare spending between developed and developing countries have been steadily diverging since the early 1970s. In order to examine this discrepancy, she used data from 53 developing countries for the period 1972-1995 to show that welfare spending in these countries was indeed reduced as a result of market liberalization.[23] Market openness, argued Rudra, makes domestic firms vulnerable to international competition and, in order

[20] Ibid.

[21] Ibid.

[22] David S. Brown and Wendy Hunter, "Democracy and Social Spending in Latin America, 1980–92," *American Political Science Review* 93, no. 04 (December 1999): 779–90.

[23] Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries."

to maintain competitiveness, the government is often pressured to significantly cut its social spending programs. Her main argument pointed to the lack of "strong labor institutions" in the developing nations -- characteristic of the OECD nations -- which impedes workers' ability to negotiate with the government and ensure favorable welfare policies to adequately mitigate the pressures of globalization.[24] The rationale behind this conclusion is that the ratio of non-skilled to skilled workers increased significantly in the developing countries, exacerbating the collective action problem[25] and making it increasingly difficult for labor to organize effectively in order to gain political leverage to bargain with the government. This, in turn, resulted in the decline (or in some cases, stagnation) in welfare spending across the developing world -- a conclusion providing evidence in favor of the race to the bottom theory.[26]

Inspired by these two initial studies, several other scholars conducted their own inquiries into correlation between globalization and welfare spending outside of the developed world, outlining several domestic factors that might help explain the nature of this relationship. However, it is important to note that the overwhelming majority of recent studies dealing with developing countries have focused on the region of Latin America, where countries have a long history of pension plans, health services and other social policies modelled along their OECD counterparts, while at the same time having attempted to implement market liberalization reforms. In accordance with Rudra's findings, Wibbels and Arce emphasize the importance of unions, as well as partisanship (i.e. the political orientation of the governing party), arguing that strong left-leaning political parties are much more reluctant to shift tax burden from capital to labor in the wake of globalization[27]. At

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[24] Ibid.

[25] Mancur Olson, *The Logic of Collective Action,* (Harvard University Press, 1971).

[26] Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries."

[27] Erik Wibbels and Moisés Arce, "Globalization, Taxation, and Burden-Shifting in Latin America," *International Organization* 57, no. 01 (December 2003): 111–36.

the same time, using an updated dataset with more sophisticated and comprehensive measure of financial openness, as well as PPP-adjusted measure of trade openness, George Avelino, David Brown and Wendy Hunter sought to build upon the previous studies. While confirming the positive relationship between democracy and spending on social policies in Latin America, their main finding directly contradicts Kaufman and Segura-Ubiergo's study, as they report that increased trade openness has a "strong positive impact" on welfare spending.[28]

Moreover, Wibbels argued that developed and developing countries have "distinct patterns of integration into global markets," where latter are much more vulnerable to income shocks.[29] As a result, the OECD nations can relatively easily borrow money in times of crises and spend on social policies aimed at counteracting the effects of shocks. At the same time, this strategy is generally not available to the developing nations -- characterized by limited access to capital markets and the need to keep balanced budgets in times of financial downturns -- which have to resort to procyclical fiscal spending, implying retrenchment of social policies (Wibbles, 2006). In yet another study focusing on Latin America, Evelyne Huber, Thomas Mustillo and John Stephens analyzed social spending in using rich data encompassing determinants such as regime type, partisanship, state structure, as well as a wide range of demographic and economic variables, making their welfare state analysis more thorough and comparable to those conducted in the developed world. Again, they find that democracy matters in the long run for both social security and human capital expenditure. Similarly, they confirm previous findings that authoritarian regimes cut spending on health and education, but

[28] Avelino, Brown, and Hunter, "The Effects of Capital Mobility, Trade Openness, and Democracy on Social Spending in Latin America, 1980–1999."

[29] Wibbels, "Dependency Revisited."

not social security. However, their arguably most important result is that partisanship does not matter, a finding which is in stark contrast to the studies of OECD countries.[30]

While Latin American countries have received more attention in the past two decades, the rest of the developing regions have often been neglected. In one of the few studies focusing on the countries in East Asia, Huck-ju Kwon examines how different welfare systems in the region cope with pressures brought about by globalization. His main finding is that East Asian countries have showed that it is possible to "maintain developmentalist social policies while enhancing social inclusiveness."[31] In other words, during the East Asian economic crisis -- often considered as a prime example of the challenges globalization poses for the developing world -- social provision was "extended in terms of coverage," as well as "strengthened in terms of quality" in some countries.[32] In a study focusing on Europe, Markus Liebrecht, Michael Klien and Oezlem Onaran use Eurostat dataset to compare the effects of globalization on Europe's different country groups characterized by different welfare regimes. Their main results indicate that, in Western Europe, citizens' demand for protection outweighs the efficiency pressures of globalization, and the evidence from this subregion generally supports the compensation hypothesis (i.e. more spending to account for the negative effects of globalization). However, the countries of Central and Eastern Europe show decline in social spending as a consequence of increased globalization -- a finding that goes in line with the efficiency hypothesis.[33]

[30] Evelyne Huber, Thomas Mustillo, and John D. Stephens, "Politics and Social Spending in Latin America," *The Journal of Politics* 70, no. 02 (April 2008): 420–36.

[31] Huck-ju Kwon, "The Reform of the Developmental Welfare State in East Asia," *International Journal of Social Welfare* 18 (April 1, 2009).

[32] Ibid.

[33] Markus Leibrecht, Michael Klien, and Oezlem Onaran, "Globalization, Welfare Regimes and Social Protection Expenditures in Western and Eastern European Countries," *Public Choice* 148, no. 3–4 (July 10, 2010): 569–94.

At the same time, very few studies have tried to analyze data from all regions of the developing world, mostly due to difficulties with finding comparable data. Using a global sample of developing countries, Rudra and Haggard came to the conclusion that social spending is generally more sensitive to increases in globalization in full autocracies compared to democratic or intermediate regimes. However, they conclude that, while autocratic governments clearly cut their spending, the data does not support previous studies which indicated the tendency of democratic governments to expand their social spending when faced with increased trade openness.[34] In an updated study published in her book, Rudra criticizes analyses which focus solely on other factors without taking the power of labor into account. She argues that, although factors such as democracy or the existence of interest groups can indeed prevent a retrenchment in social spending in "mature" welfare states with already strong labor organization, labor centralization is still a crucial precondition in the developing countries, where welfare states have not reached the same advanced stage.[35] Finally, in another global study, Meinhard and Potrafke revisited the globalization-welfare state nexus by using data from 186 countries -- both developed and developing -- coming to a conclusion that globalization led to the expansion of welfare state around the world, albeit more significantly in the OECD nations compared to the rest of the world.[36]

Finally, it is important to note several studies dealing with embedded neoliberalism, another concept often used to describe the mechanisms between the compensation hypothesis. This concept is an updated version of Ruggie's "embedded liberalism,"[37] which built on Karl Polanyi's work.[38]

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[34] Nita Rudra and Stephan Haggard, "Globalization, Democracy, and Effective Welfare Spending in the Developing World," *Comparative Political Studies* 38, no. 9 (November 1, 2005): 1015–49.

[35] Ibid.

[36] Stephanie Meinhard and Niklas Potrafke, "The Globalization–Welfare State Nexus Reconsidered," *Review of International Economics* 20, no. 2 (May 1, 2012): 271–87.

[37] John Gerard Ruggie, "International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order," *International Organization* 36, no. 02 (March 1982): 379–415.

Embedded neoliberalism predicts that, in order to earn the consent of their population to pursue market liberalization, international market pressures will always be secondary to domestic economic transformations. In other words, in order to earn the consent of their population to pursue market liberalization, governments are compelled to provide social protection to their citizens in order to mitigate its negative consequences. This, much like the compensation hypothesis, implies that the government (and by extension, the welfare state) become more important with the increase in economic globalization, contrary to the very meaning of *laissez-faire*. In this context, a study done by Kurtz and Brooks confirm that in some Latin American countries, the role of state intervention was expanded "within the context of deep economic liberalization."[39] Moreover, they found that embedded neoliberal policies were much more pronounced in those countries that pursued the autarkic import substitution industrialization (ISI) prior to liberalization, a strategy which produced severe inequalities in income and access to education thus requiring significant redistribution programs in attempts to correct them.[40] Similarly, Wibbles and Ahquist confirm this finding on a global sample, concluding that the protectionist ISI strategies, rather than export-oriented ones, are more likely to emphasize and implement social security policies. Due to the long lasting legacy of social protection in countries that have pursued ISI in the past, it has proven difficult for governments to retrench spending in protected sectors without facing resistance from labor markets.[41] Finally, in their latest analysis, Nooruddin and Rudra also tackle the concept of embedded neoliberalism, arguing that developing countries have unique ways of building domestic support for liberalization, depending on their histories and politics. Some developing countries, they argue,

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[38] Karl Polanyi, *The Great Transformation: The political and economic origins of our time,* (Boston: Beacon Press, 1944)

[39] Nathaniel Beck and Jonathan N. Katz, "What To Do (and Not to Do) with Time-Series Cross-Section Data," *American Political Science Review* 89, no. 03 (September 1995): 634–47.

[40] Ibid.

[41] Erik Wibbels and John S. Ahlquist, "Development, Trade, and Social Insurance," *International Studies Quarterly* 55, no. 1 (March 1, 2011): 125–49.

resort to increasing public employment in order to compensate for the insecurities that come with market liberalization, especially in world's poorest countries that have "weak or non-existent social insurance," which is traditionally the primary compensation channel.[42]

2.2 The Argument

While globalization is a world-encompassing phenomenon, studies of welfare state throughout the past few decades exhibit significant discrepancies in how this process affected countries around the world. The conventional wisdom backed by economic theory -- formulated in the efficiency hypothesis – suggested that opening up to free trade will leave very little space for governments to play a significant role in providing a social safety net for their citizens. However, this was challenged in numerous studies conducted in the developed nations. These studies have provided firm empirical evidence indicating that, rather than cutting social benefits expense, governments of advanced nations actually increased their spending on social policies in order to compensate their citizens for the market-induced injustices. And while scholars cite different factors that contributed to the expansion of social spending in the developed world – such as the high degree of labor institutionalization, deindustrialization, as well as influence of various interest groups – there is a consensus that the national fiscal autonomy did not decrease and the welfare state did not lose its significance in the context of a globalized world. However, the discourse on globalization-welfare nexus had for a long time been limited to world's most developed nations. While some scholars noted that mechanisms dictating social spending in the developing world might be different, lack of comparable data made it difficult to assess the impact of globalization on the welfare state in these countries.

[42] Irfan Nooruddin and Nita Rudra, "Are Developing Countries Really Defying the Embedded Liberalism Compact?," *World Politics* 66, no. 04 (October 2014): 603–40.

When hypothesizing the relationship between the two in the developing countries, one needs to consider several factors. First, the economic theory – captured by the Stolper-Samuelson theorem – suggesting that low-skilled labor, usually an abundant factor in the developing counties, will experience gains (i.e. wage increase and higher employment) when exposed to international markets.[43] These economic gains, it is hypothesized, should then translate into political gains mirrored in higher institutionalization and increased bargaining power, which workers could then use to negotiate higher welfare spending.[44] However, virtually all studies on labor power in the developing world come to a unanimous conclusion that labor unions in these countries are highly fragmented and, as such, lack the bargaining power of their OECD counterparts. Rudra argues that this is due to the fact that large numbers of low-skilled workers are susceptible to the collective action problem, while at the same time lacking labor institutions on a national level characteristic of the developed nations. In addition, the existence of surplus low-skilled labor in many developing countries makes it harder to overcome the collective action problem and mobilize as it is impossible for union leaders to offer them "selected incentives"[45] in the form of secure employment, and thus the unemployed workers are more concerned with securing jobs than seeking higher welfare benefits. This breaks the causal chain linking globalization to higher social expenditure in developing countries

At the same time, it is important to note another crucial difference between advanced countries and their developing counterparts, which is cited in the literature as one of the most important determinants of welfare spending – the level of democracy. While the overwhelming

[43] Ronald Rogowski. "Commerce and Coallitions: How Trade Affects Domestic Political Alignments" in *International Political Economy: Perspectives on Global Power and Wealth* ed. Jeffry A. Frieden and David A. Lake (New York: Routledge, 2000): 318-326.

[44] "Polity IV Project: Political Regime Characteristics and Transitions, 1800-2013,," accessed May 28, 2016, http://www.systemicpeace.org/polity/polity4.htm.

[45] Mancur Olson, *The Logic of Collective Action,* (Harvard University Press, 1971).

majority of the advanced economies are longstanding stable democracies, as indicated by high (in most cases, maximum) Polity II score, many of developing countries are new democracies and some have high levels of institutionalized autocracy. At the same time, market liberalization reforms tend to be painful in the short run, until a country is able to establish itself on the international market. As a result, in order to gain popular support for further liberalization reforms, governments in advanced countries feel compelled to expand social spending in order to compensate their citizens for hardships created in the process of market liberalization. At the same time, in well-established democracies, incumbent governments' reelection largely depends on their performance in office, and cutting social spending is likely to render them unpopular among the consumers of welfare, which represent a significant part of the voting constituency. In contrast, many of the developing countries are relatively new weak democracies, with significant institutional legacies of their past regimes, or non-democracies. Given this, while governments in this group of countries certainly care about their constituencies, they might not necessarily feel as threatened by a potential popular backlash, and thus not compelled to prioritize citizens' welfare to the same extent their advanced counterparts do.

These two groups of economies follow fundamentally different paths of integration into the global market -- conditioned by their factor endowments -- which then determines the way they enact social policies in times of economic downturns. While the developed nations can easily borrow money which can be used to increase welfare spending to counteract the effects of shocks, developing countries have much more limited access to capital markets. At the same time, they are compelled to maintain balanced budgets in order to project the image of stability to both existing and potential investors. As a result of this, governments in the developing world are likely to spend pro-cyclically in times of economic contractions, resulting in the retrenchment of welfare policies. Therefore, due to these fundamental differences, it was hypothesized that globalization is likely to have a disparate effect on social spending in the developing countries compared to their developed counterparts. However while increased data availability opened way for empirical inquiry, the results were often inconclusive or even contradictory, as causal effects suggested by studies proved to be contingent to specifications of the models, different operationalizations and measurements of the key concepts, as well as the types of data used.[46] Therefore, this analysis seeks to revisit and empirically assess the globalization-welfare state nexus in the context of the developing world by using the latest available data.

This study aims to contribute to the existing literature by further dividing the developing countries into two distinct groups: the emerging economies and the least developed countries. While the overwhelming majority of studies dedicated to the developing countries treats them all as roughly comparable, I argue that there are significant differences among them, which could in turn result in different mechanisms dictating social spending policies. While the emerging economies have undergone rapid market liberalization in the last few decades in order to catch up with the developed world, their least developed counterparts are still significantly lagging behind. Given their relatively higher level of GDP-per capita, emerging economies are more likely to devote a higher share of their GDP to public spending compared to less developed economies, which would arguably make it somewhat easier for governments to retrench welfare spending without meeting significant resistance from their citizens. At the same time, many emerging economies -- especially in Latin America and Eastern Europe -- had established elaborate social security schemes as early as the OECD nations, having historically allocated significant percentage of government spending to providing a safety net for their citizens. In contrast, the world's poorest countries often lack even the most essential social security programs and generally have very low levels of social spending, again making it really hard for them to retrench the most basic social security programs.

[46] Peter Starke, "The Politics of Welfare State Retrenchment: A Literature Review," *Social Policy & Administration* 40, no. 1 (February 1, 2006): 104–20.

Finally, conditioned by significant regional differences in the development of the welfare state – in terms of extent and the variety of social policies – pointed out in the literature focused on the developing world, the impact of globalization on social spending may also vary across regions. Governments in Europe and Central Asia, North America, and Latin America, given their histories of extensive welfare provision, will find it difficult to extensively cut spending, and the evidence from these two regions is likely to support the compensation hypothesis. On the other hand, due to the development-oriented welfare state, East Asian countries are likely to retrench social spending in order to remain competitive on the international market. Finally, given the chronic underdevelopment of their social policies, countries in Africa are not expected to significantly alter the extent of their current social provision in the face of increased globalization.

Relying on the existing theory, as well as the most influential empirical studies, I hypothesize the following:

Hypothesis 1a: Globalization has a positive effect on social expenditure in advanced economies (i.e. compensation hypothesis).

Hypothesis 1b: Globalization has a negative effect on social expenditure in developing economies (i.e. efficiency hypothesis).

Hypothesis 2: Globalization has a more adverse effect on social expenditure in the emerging economies compared to the less developed ones.

Hypothesis 3a: Globalization has a positive effect on social expenditure in Europe and Central Asia and North America.

Hypothesis 3b: Globalization has a positive effect on social expenditure in Latin America and the Caribbean.

Hypothesis 3c: Globalization has a negative effect on social expenditure in East Asia and the Pacific.

Hypothesis 3d: Globalization has no significant effect on social expenditure in Africa.

3. Methodology

In order to examine the globalization-welfare state nexus in the developing world context, this paper engages in a quantitative study – cross-national time series regression analysis – looking at how indicators of economic globalization affect government welfare spending indicators. In addition, due to the large number of missing observations for the developing countries for earlier years, which would potentially skew the results towards trends characteristic of the advanced nations, this analysis is limited to a period of fourteen years (2000-2014). I apply times-series cross sectional regression analysis and utilize panel corrected standard errors[47] to account for the panel structure of the data. This type of regression analysis allows for the analysis of multiple units (countries) over time with a method that accounts for the non-independence of observations from the same unit. Finally, after presenting a model including all countries with available data in order to examine general trends, I proceed in two different ways. First, I reproduce the regression analyses done by key studies assessing the impact of economic globalization on the welfare state by comparing spending trends in the developing world to those of the advanced nations. This allows me to check whether the same findings (i.e. positive effect in advanced nations, negative in the developing countries) hold with the most recent data available. Furthermore, in order to investigate the differences within a very large and diverse group of the developing nations, the second part of my analysis will focus solely on this group, comparing welfare spending trends in emerging and less developed economies.

Coined by a World Bank economist Antione Van Agtamel in the 1980s, the term 'emerging economy' was meant to signify those countries in a transition phase from less developed to an

[47] Nathaniel Beck and Jonathan N. Katz, "What To Do (and Not to Do) with Time-Series Cross-Section Data," *American Political Science Review* 89, no. 03 (September 1995): 634–47.

advanced economy.[48] While there has been much controversy around the usage of the term, as there is no clear-cut explanation of what makes a country an emerging economy, the term has gained traction in economics and the literature. Today, it is widely used to describe countries that went through periods of rapid economic development in the past two decades, most notably including the so-called BRICS (Brazil, Russia, India, China and South Africa), as well as a number of other Latin American, Asian and Eastern European Countries. It can be argued that, in terms of economic development, emerging economies are much closer to the advanced nations than less developed ones. However, unlike advanced countries that generally have stable economies, the emerging ones are much more susceptible to macroeconomic shocks, which is likely to lead to more volatility in government spending (and by extension welfare spending) levels.

Finally, the countries were allocated to one of the three income groups taking the following order into consideration:

1. the list of emerging economies was adopted from the IMF[49]
2. the OECD nations were coded as advanced economies, with the exception of Chile and Turkey, as they were listed as emerging economies by the previously mentioned IMF listing[50]
3. all remaining developing nations were allocated to the less developed economies group[51]

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[48] "The Long View: How Adventurous Are Emerging Markets?," *Financial Times*, October 20, 2006,.

[49] The list of emerging economies was adopted from the *International Monetary Fund*. Unfortunately, the social expenditure data was unavailable for some countries, including key emerging economies such as Brazil, China and India. As a result, this analysis is limited to the following emerging economies: Bulgaria, Chile, Colombia, Hungary, Indonesia, Peru, Poland, Romania, Russian Federation, Slovakia, South Africa, Thailand, Turkey and Ukraine

[50] Following countries were allocated to the advanced economies group: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Island, Ireland, Israel, Italy, Japan, Korea Republic, Luxembourg, Monaco, Netherlands, New Zealand, Norway, Portugal, San Marino, Singapore, Slovenia, Spain, Sweden, Switzerland, United Kingdom and United States

[51] The less developed countries featured in this analysis include: Afghanistan, Albania, Armenia, Azerbaijan, Bahrain, Barbados, Belarus, Bhutan, Bolivia, Bosnia and Herzegovina, Cabo Verde, Democratic Republic of Congo, Costa Rica, Croatia, Cyprus, Egypt, El Salvador, Georgia, Honduras, Iran, Jamaica, Jordan, Kazakhstan, Kuwait, Latvia, Lesotho, Lithuania, Macedonia, Maldives, Malta, Mauritius, Mongolia, Morocco, Paraguay, Serbia, Seychelles, Tanzania, Timor-Leste, Tunisia, United Arab Emirates and Yemen

3.1 The Variables and the Model

3.1.1 Social Spending

In this study, social spending pertains to government spending on policies designed to protect the wellbeing of citizens and provide for those in financial and social need through several channels, such as unemployment benefits, old-age pensions, disability pensions, maternity leave and sick leave. While the majority of studies assessing the impact of globalization have focused on total level of government spending as their main dependent variable, some studies have noted that this is somewhat misleading[52] Given that total government expenditure includes a broad range of items -- military spending, capital and current account-related spending, as well as employment compensation -- its levels can undoubtedly fluctuate independently of welfare expenditure. As a result, this study uses a more specific indicator – social benefits expenditure expressed as a percentage of GDP -- which is able to capture welfare state effort more efficiently.

However, expressing welfare generosity in terms of GDP can also be problematic in the sense that any sudden fluctuations in GDP would cause the indicator to change without any direct change in the level of social spending. In order to control for this possibility, GDP growth is included as a control variable. The data for social benefits expenditure was obtained from the IMF's *Government Finance Statistics (GFS)* database.[53] The data for OECD countries are generally available from 2000, while many emerging, as well as less developed economies have data available for a much shorter period of time. Some countries did not have any data available, and were thus excluded from this study. Finally, it is important to note that a significant limitation of the data on

[52] Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries."

[53] International Monetary Fund, *Government Finance Statistics* (Washington D.C.: IMF, various years)

social spending in the developing world is that they are only available on the central government level, thus excluding social programs carried out on sub-national levels, which are characteristic of many federal states.[54] However, although there are a wider range of indicators for social benefit generosity in the welfare state literature, social benefit expenditure is the only one available for enough countries for this analysis that aims to be global in scope.

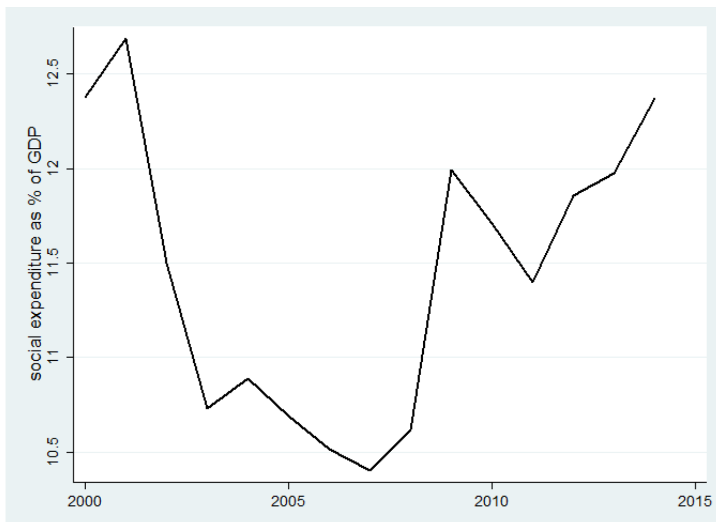

Figure 2: *Global trends in social expenditure, 2000-2014*

3.1.2 Globalization

While defining globalization has proven a difficult undertaking in the past, prompting Thomas Friedman to describe it as "everything and its opposite,"[55] this study focuses exclusively on the economic aspects of the phenomenon, leaving out its social, cultural and political implications.

[54] Segura-Ubiergo, *The Political Economy of the Welfare State in Latin America.*

[55] Thomas L. Friedman, *The Lexus and the Olive Tree: Understanding Globalization* (Macmillan, 2000).

Therefore, economic globalization is defined as the increasing economic interdependence through an intensification of cross-border movement of goods, services, technologies, and capital. The conventional practice in the globalization literature suggests the use of trade-to-GDP ratio as a measure of a nation's trade integration, while the level of foreign direct investment (FDI) inflows is utilized to measure the degree of openness to international capital markets. However, as it has been noted in the literature, there are certain limitations to using both of these variables to capture the effect of economic globalization. Just as any other ratio, trade-to-GDP depends on both of its components and, as such, it is also affected by the size of country's economy. As a result, all else equal, smaller economies are much likely to have higher trade-to-GDP ratios without not necessarily being more integrated into the global markets. At the same time, trade-to-GDP is highly responsive to changes in the exchange rate. Similarly, FDI flows are problematic because they focus only on one aspect of mobile capital, while at the same time ignoring others. Small economies, for example, might not receive large amounts of FDI due to unfavorable location, but can at the same time be considered open due to high levels of portfolio investment, as well as other types of capital.[56]

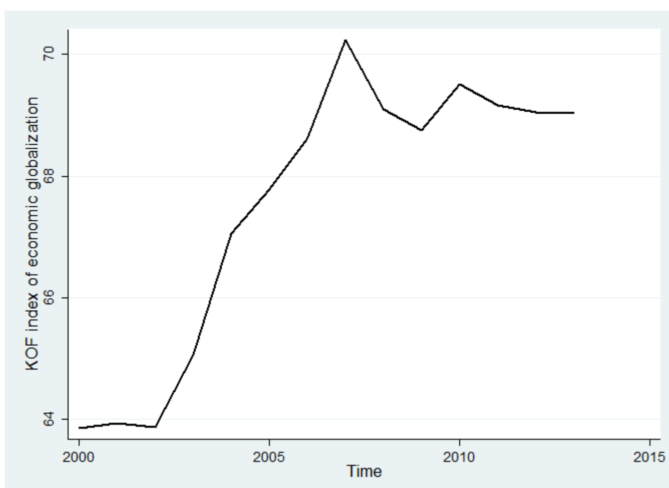

Figure 3: *Global trends in economic globalization, 2000-2014*

[56] Leibrecht, Klien, and Onaran, "Globalization, Welfare Regimes and Social Protection Expenditures in Western and Eastern European Countries."

In an attempt to better capture the multifaceted nature of globalization, a different measure of globalization - the KOF index of economic globalization - is introduced. KOF index of economic globalization is one of several weighted indices -- together with social globalization, political globalization, as well as the broader overall index of globalization -- developed by Dreher[57] in order to capture different dimensions of globalization more efficiently. In addition to bringing together flows of goods, services and capital (traditionally captured separately by trade-to-GDP ratio and FDI flows), this index also incorporates portfolio investment as well as income payments made to foreign nationals, as well as legal restrictions on trade and financial flows. While the overall KOF index of globalization is commonly used in the literature, it includes other two sub-indices – social and political globalization – which are less relevant for this study. As a result, the analysis in this thesis relies on the economic sub-index the main independent variable. Finally, the data for KOF index was obtained from the Swiss Institute of Technology's website[58].

3.1.3 Control Variables

In addition to the main independent variable, a number of control variables were included to account for many other factors that can influence welfare spending, but are not directly associated with the process of economic globalization. Primarily, in line with Geoffrey Garrett's argument about the importance of labor organization as a shield against the lowering of welfare spending, the model ideally would include a variable which captures the degree of labor institutionalization. In her analysis, Nita Rudra devises a separate indicator -- potential labor power (PLP) -- in order to measure labor's bargaining power in the developing world. The PLP, predominantly dependent on

[57] Dreher, Axel, *KOF Index of Globalization*, (Zurich: Konjunkturforschungsstelle ETH Zurich, 2006)

[58] ETH Zurich, "KOF Index of Globalization," accessed May 28, 2016, http://globalization.kof.ethz.ch/

the ratio of skilled to unskilled labor, is able capture variations in labor strengths regardless of the regime type and state-labor relations.[59] However, due to the unavailability of the PLP data,[60] this study intended to use trade union density (i.e. the number of trade union members per number of employed persons), as it is the indicator indicator of labor power. However, the data for this variable also proved to be scarce, especially in the case of the developing countries and it was only utilized in the model including only the advanced nations. Furthermore, given the numerous links made between democracy and the level of social spending in the surveyed literature, this study includes the Polity II score, which measures each country's level of democracy on a scale from -10 to +10 (scores from -10 to -6 correspond to autocracies, from -5 to 5 to anocracies, and 6 to 10 to democracies).[61] In addition, a number of other demographic and economic control variables were included, either because they seemed conceptually important or were proven to be significant determinants of social spending in the developing countries by previous studies. These controls include the number of elderly dependents (age dependency ratio), the level of urbanization, GDP-per-capita and annual GDP growth, tax revenue, debt levels, inflation and current account balance. While Rudra and some others exclude unemployment rate from their analysis due to the unreliability of the data in the developing countries, it is still included in this study, given that is one of the most important predictors of welfare spending levels in a country. Finally, the data for control variables were extracted from several different sources: trade union density was collected from the International Labor Organization (ILO)'s Industrial Relations Database,[62] Polity II score was extracted from the

[59] Rudra, "Globalization and the Decline of the Welfare State in Less-Developed Countries."

[60] I did not manage to gain access to the PLP data, despite having kindly requested Ms. Rudra to provide it so that I could reproduce her analysis.

[61] "Polity IV Project: Political Regime Characteristics and Transitions, 1800-2013," accessed May 28, 2016, http://www.systemicpeace.org/polity/polity4.htm.

[62] International Labor Organization, "Industrial Relations Data (IRData)," Database, (September 28, 2015), http://www.ilo.org/global/docs/WCMS_408983/lang--en/index.htm.

Polity IV Database, while age dependency ratio, the level of urbanization, GDP-per-capita, annual GDP growth and tax revenue were all obtained from World Bank's WDI Database.[63]

[63] The World Bank, *World Development Indicators* (Washington D.C.: The World Bank, various years).

3.1.4 Regression Model

In order to estimate the effect of globalization on the welfare state, this study uses the following generic model:

$$sbexp_{it} = \beta_0 + \ \beta_1 \ ecglo + \Sigma\beta_j X_{jit} + \ \varepsilon_{it}$$

where *sbexp* is social benefits expenditure for country *i* in time *t* β_1 the coefficient indicating the effect of economic globalization (measured by the KOF index), $\Sigma\beta_j X_{jit}$ represents the vector of control variables (Polity II score, GDP-per-capita, annual GDP growth, inflation levels, current account balance, age dependency ratio, and level of urbanization), while ε_{it} represents the remainder error term. This generic model is subjected to four different specifications which will be presented and discussed in the following chapter: an overall regression including all countries treating them as one group, a regression distinguishing between developing and the developed, a regression focusing only on the two subgroups of the developing countries (i.e. emerging and less developed economies), as well as a regression investigating regional differences with respect to welfare spending. Finally, due to the missing observations on some key variables, all regressions were checked by using the multiple imputation method, and the majority of the findings were consistent with the original, non-imputed data.[64]

[64] Williams, Richard, "Missing Data Part II: Multiple Imputation," (Notre Dame: University of Notre Dame, 2015)

4. Empirical Analysis

4.1 Assessing the Overall Impact of Globalization across the World

Before moving onto comparing the effects of globalization on the welfare state between advanced and developing economies, I look at the overall trend of welfare spending across the world. The results of this analysis are presented in *Table 1*, including three different model specifications which differ by independent variables included.

Table 1 *The relationship between globalization and welfare spending across the world*

	Dependent variable: Social benefits expenditure as % of GDP	
Independent variables	*Model 1*	*Model 2*
KOF index	-0.027 ***	-0.124 ***
	(0.009)	(0.014)
Polity II score	0.150 ***	0.045
	(0.045)	(0.027)
Age dependency ratio	0.007	-0.147 ***
	(0.014)	(0.023)
Urbanization levels	-0.007	0.079 ***
	(0.007)	(0.009)
Logged GDP-per-capita	6.960 ***	2.838 ***
	(0.356)	(0.692)
Annual GDP growth	-0.266 ***	-0.045
	(0.052)	(0.044)
Inflation	0.031	0.063 ***
	(0.030)	(0.019)
Current account balance	-0.084 ***	-0.129 ***
	(0.014)	(0.018)
Unemployment	0.305 ***	0.143 ***
	(0.021)	(0.019)
Tax revenue		0.134 ***
		0.026
Government debt		3.7e-12 ***
		-1.6e-12
N	763	247
R-squared	0.586	0.602

Notes: The models are linear regressions with panel-corrected standard errors.
*** *p<0.01*
** *p<0.05*
* *p<0.1*

Table 1: *The Relationship between globalization and welfare spending across the world*

Both models in *Table 1* indicate that an increase in economic globalization has a significant negative effect on the full country sample for the time period captured by my study, providing evidence in support of efficiency theory. However, due to the fact that different mechanisms behind social spending policies in advanced and the developing countries were established early on, most studies had avoided producing analyses on a global sample. At the same, the data collected in the developing world, apart from being scarce, are often not as comprehensive or as detailed as data collected by the OECD, for example. As a result, there are very few studies that tried to combine these two sets of countries in order to perform a joint analysis, making it difficult to compare my results. The only global study surveyed in the literature above, using data for 186 countries for the period 1970-2004, came to an opposite conclusion indicating a significant positive effect of globalization on welfare spending.[65] Given that the effect of globalization is expected to vary across country groups, then the overall direction of the effect may be sensitive to changes in the model.

From the control variables, Polity II score was positive and statistically significant, indicating that the level of democracy is a significant determinant of welfare spending. This finding, in turn, supports the conventional theory confirmed by many empirical studies indicating that, on average, democracies allocate a higher percentage of their GDP to social spending policies compared to their non-democratic counterparts. Furthermore, unemployment expectedly had a positive and significant effect on welfare spending, as welfare needs increase as unemployment increases. In addition, the findings also suggested that GDP-per-capita and annual GDP growth had a statistically significant positive effect, while current account balance had a statistically significant negative effect, which are all conceptually sound findings. Finally, age dependency ratio, the degree of urbanization and well as inflation levels were not statistically significant in explaining the variation in social spending trends in

[65] Meinhard and Potrafke, "The Globalization–Welfare State Nexus Reconsidered."

this model. *Model 2* presented differs slightly from the previous one, as includes tax revenue and government debt levels in the list of control variables, both of which have limited number of observations. As a result, while overall findings don't change when these two variables are included, the number of observations drops significantly. Tax revenue has the expected impact as it significantly increases welfare spending. Tax revenue has the expected impact as it significantly increases welfare spending. Government debt also has a positive impact on welfare spending, suggesting that governments that can borrow are likely to spend more. Most importantly, these baseline models show that the effects are generally in the expected directions.

4.2 Comparing the Impact of Globalization on Developed and Developing Countries

After assessing overall trends in welfare spending, the next step in my study is to compare the impact economic globalization has on the welfare state in advanced and developing economies. The main aim of this analysis was to reproduce Rudra's (2002) study in order to asses whether her main findings regarding the impact of globalization on the welfare state held when using the newest available data. The results of this analysis are presented in *Table 2*, including three different model specifications. Just as in the first regression, globalization was found to have a significant negative impact on welfare spending between 2000 and 2014. However, the main difference between the two models is that the later one included a dummy variable separating advanced economies from the rest, as well as the interaction term between this dummy variable and the KOF index of economic globalization, both with the purpose of investigating potential differences in social spending between the two groups.

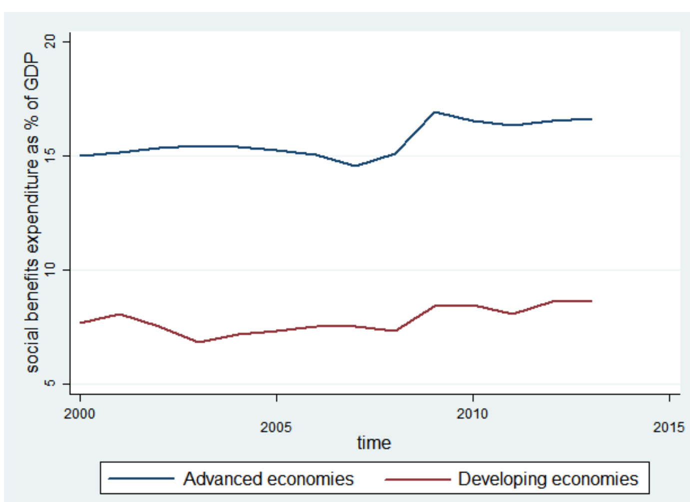

Figure 4: *Persisting gap in social expenditure between advanced and developing economies*

The findings in *Model 1* confirm the main assumptions behind my first hypothesis. While the overall results indicate a negative effect of globalization on welfare spending, the positive and statistically significant coefficient for the interaction term between the advanced economy dummy variable and the KOF index of economic globalization suggests that the globalization effect varies significantly between advanced and developing countries. Given that the interaction is positive, this means that the impact of globalization is less negative or even positive for the advanced economies. *Figure 5* displays the significantly different effect of globalization across groups. This goes to confirm the predominant findings in the literature on the advanced nations, suggesting that governments do not reduce spending in the face of globalization. Rather these governments compensate their constituencies for the hardships that usually come hand in hand with market liberalization. As mentioned in the theoretical framework, this is usually due to the existence of strong labor unions and other domestic interest groups which are able to exert pressure on the government to step up and mitigate the negative consequences of economic globalization, as well as governments' desire to win their constituencies support for further liberalization and to improve favorability rates among citizens. At the same time, the statistically significant negative coefficient against the KOF index confirms that governments in the developing countries are likely to decrease welfare spending when faced increased globalization – a finding confirming hypothesis 1b and supporting the efficiency hypothesis often cited in the literature in the context of the developing countries. So my analysis suggests that the effect of globalization on the welfare spending varies across country groups, meaning that attempts to determine the overall effect of globalization are misguided. The non-uniform effect of globalization also explains why there has been such discrepancies in the analyses in the literature.

Table 2 *The relationship between globalization and welfare spending in advanced and developing economies*

Independent variables	*Model 1*	*Model 2*	*Model 3* *Advanced countries only*
	Dependent variable: Social benefits expenditure as % of GDP		
KOF index	-0.080 ***	-0.100 ***	0.062
	(0.016)	(0.016)	(0.040)
Polity II score	0.101 ***	-0.058 *	0.090
	(0.034	(0.033)	(0.220)
Age dependency ratio	-0.030 *	-0.043 ***	0.700 ***
	(0.017)	(0.016)	(0.048)
Urbanization levels	-0.025	-0.005	-0.039
	(0.006)	(0.006)	(0.028)
Logged GDP-per-capita	4.808 ***	5.397 ***	-0.874
	(0.467)	(0.404)	(0.935)
Annual GDP growth	-0.250 ***	-0.207 ***	-0.208 ***
	(0.051)	(0.052)	(0.072)
Inflation	0.055 **	0.040 *	-0.209 ***
	(0.025)	(0.021)	(0.060)
Current account balance	-0.090 ***	-0.099 ***	0.095 ***
	(0.013)	(0.017)	(0.020) ***
Unemployment	0.287 ***	0.283 ***	0.128
	(0.020)	(0.014)	(0.062)
Tax revenue		0.037 ***	0.014
		(0.011)	(0.021)
Trade union density			-0.001
			(0.003)
OECD dummy variable	-0.062	-1.298	
	(1.381)	(2.013)	
Interaction between OECD dummy and KOF index	0.062 ***	0.075 ***	
	(0.015)	(0.025)	
N	763	247	140
R-squared	0.631	0.602	0.659

Notes: The models are linear regressions with panel-corrected standard errors.
*** *p<0.01*
** *p<0.05*
* *p<0.1*

Table 2: *Differences in effects of economic globalization on the welfare state in advanced and developing economies*

Model 2 differs only slightly from the previous one, as it adds government tax revenue to the list of control variables. The main reason for presenting separate regression results is that, due to missing data, the overall number of observations drops significantly when tax revenue is included. However, the key findings remain unaltered regardless. Finally, it is important to note that this study attempted to introduce government external debt levels into the list of controls. However due to missing observations on all the advanced countries, the regression results omitted the coefficients against advanced economy dummy variable, as well as its interaction with the KOF index because of collinearity. Given that this rendered my analysis useless in comparing the impact of globalization on the two groups of countries, this variable was excluded from the models presented above.

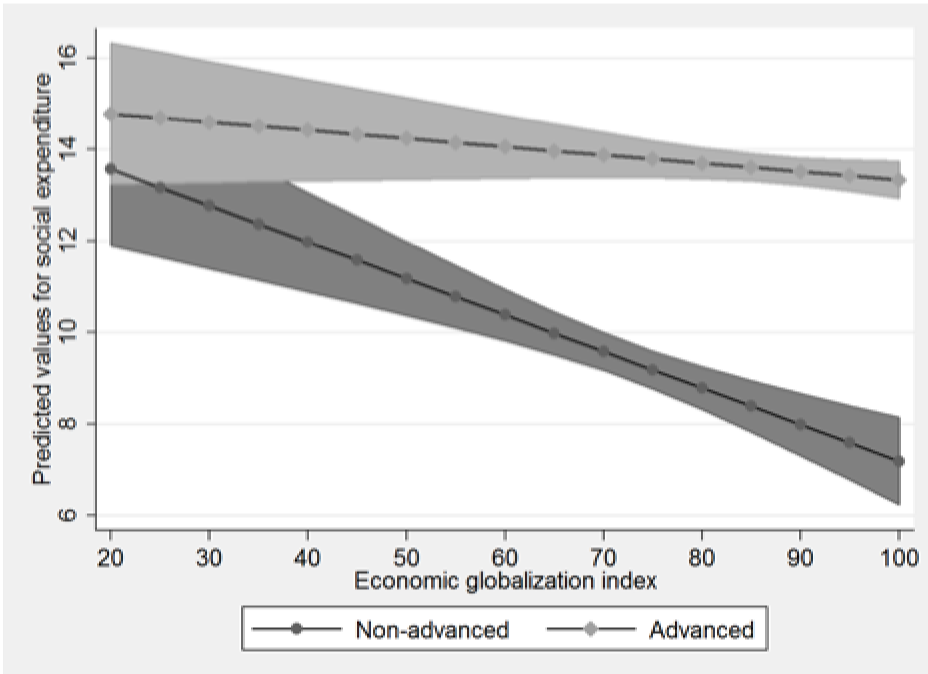

Figure 5: *Comparing predicted values of social expenditure for advanced and non-advanced countries based on Model 1 in Table 2 with 95% confidence interval*

In addition, a significant limitation of this analysis was the inability to test Rudra's labor power hypothesis, due to the lack of data on the level of unionization, which made it impossible to run the full sample regression including this variable. Given that acquiring potential labor power (PLP) data used by Rudra proved impossible, this study had planned to utilize the alternative measure of labor centralization -- trade union density. This measure is often criticized in the literature given that many governments, especially in non-democratic regimes, mandate compulsory union membership while at the same time restricting labor power. As a result, high level of union density would imply high degree of labor power even in non-democratic regimes where labor is highly suppressed by the government. However, the data on trade union density proved to be very scarce, especially in the developing world and, as a result, it was impossible to test its effects on the global sample. Due to this, the study was unable to test Rudra's main hypothesis – empirically confirmed using her PLP data -- indicating that, in the developing countries, the low-skilled labor that is most conducive to effects of globalization is highly fragmented as it suffers from a collective action problem, making it impossible for union leaders to successfully mobilize workers in order to increase their bargaining power *vis-à-vis* the government. Because of labor's low bargaining power, governments in the developing countries do not feel pressured to compensate their citizens and alleviate globalization pressures. As a result, that this difference in the degree of labor institutionalization is the main determinant of the diverging trends in welfare expenditure between developing and developed countries.

However, a separate regression including data on trade union density was run for the advanced countries only, as they had sufficient number of observation on this variable. The result of this regression are presented *Model 3*. Surprisingly, trade union density, which in theory should serve as a reliable proxy for labor power in advanced economies due to their high level of democracy, has a statistically insignificant effect on social spending. However, although against claims made in Rudra's earlier studies, this finding (or lack thereof) is not at all surprising. As mentioned in the literature review, several studies have indicated that organized labor institutions are often insufficient, as they are unable to exert enough pressure on the government to prevent the retrenchment of social policies. Instead, they argued that it is essential for labor union leaders to seek other strategic allies (i.e. other consumers of welfare or political parties) in order to resist changes in welfare spending.[66] Finally, for the analysis of advanced countries only with the inclusion of trade union density, the main findings of the previous two models are significantly altered, as the

[66] Esping-Andersen, "The Three Political Economies of the Welfare State"; Hicks, *Social Democracy & Welfare Capitalism*; Evelyne Huber and John D. Stephens, *Development and Crisis of the Welfare State: Parties and Policies in Global Markets* (University of Chicago Press, 2001).

effect of KOF index becomes statistically insignificant. So, whereas the effect of globalization on welfare spending was clearly negative in developing countries, for advanced countries, the effect is ambiguous according to this model.

In this section, I have demonstrated a clear negative effect of globalization on welfare spending in developing countries. In advanced countries, the effect is significantly more positive (which can mean no effect or a positive effect). *Model 3* indicated no statistically significant effect, which suggests that governments at least maintain spending levels in the face of globalization.

4.3 Comparing the Impact of Globalization on Emerging and Less Developed Economies

The majority of the existing literature on globalization in the developing countries –empirical studies in particular—has regarded this large group of countries as similar to each other, failing to highlight significant differences between them. Therefore, this analysis intends to make an original contribution to the literature by dividing the developing countries in two distinguished groups – the emerging and less developed economies – in order to assess whether globalization affects the welfare state in these two groups of countries differently. Due to the focus on the developing countries, the advanced economies have been excluded from this analysis altogether. I hypothesized that economic globalization will have a more adverse effect on the emerging economies. For one, given their higher level of GDP-per-capita, the emerging economies are likely to allocate a higher share of government spending to welfare policies. At the same time, many emerging economies in Latin America and Eastern Europe had established elaborate welfare states during their socialist times, which left them the legacies of a wide array of social security programs. As a result, their welfare states are richer and more diverse, making it easier for governments to retrench spending on the less essential programs. In contrast, governments in the least developed economies, where meagre welfare states barely cover basic needs, will find it difficult to reduce spending without facing serious popular backlash.

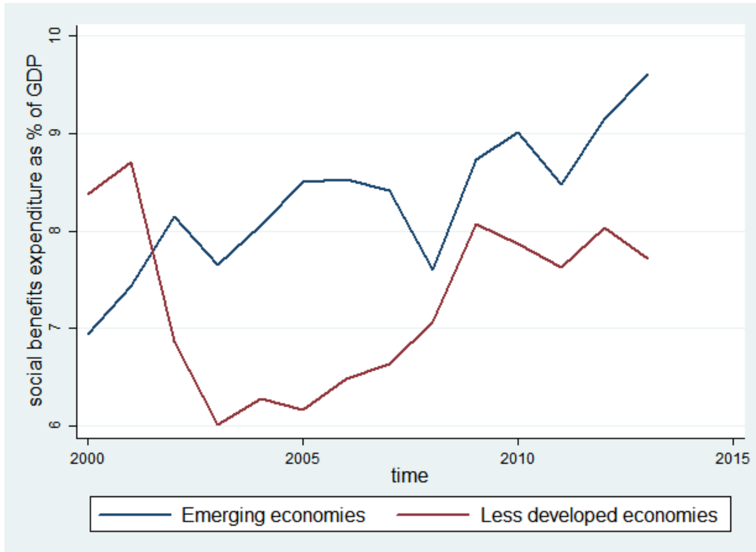

Figure 6: *Comparison of social expenditure trends in emerging and less developed economies*

The main findings, presented in *Table 3,* support the underlying assumptions behind my first and second hypotheses. The statistically significant negative coefficient against the KOF index indicates that economic globalization has a negative effect on welfare spending for the full sample of developing countries for the time period captured in this study. This finding – supporting the efficiency hypothesis – is predominant in the surveyed literature on the developing countries, and it is consistent across different specifications of the model. Furthermore, GDP-per-capita was consistently significant and positive in all three models, suggesting that differences in economic development play a major role in determining welfare spending even within the group consisting of only developing countries. This indicates that the developing countries should not be treated as one uniform group of counties in the literature. In addition, the majority of other control variables proved to be significant determinants of welfare spending in the developing countries, which was also consistent across all models (with the exception of annual GDP growth in *Model 3*). Higher levels of democracy, urbanization, inflation, and unemployment implied more welfare spending, while current account balance and annual GDP growth (in *Models 1 and 3*) were negatively associated with levels of welfare spending. It is important to note that age dependency ratio was negatively associated with welfare spending -- suggesting that an increase in the number of dependents leads to a decrease in social spending -- which goes against conventional wisdom, but might be related to the fact that not all countries in the sample have pension systems. Tax revenue and government debt levels were included subsequently (in *Model 2* and *Model 3*, respectively) due to low number of observations. While introducing tax revenue did not alter the model significantly, including government debt in the regression made the interaction coefficient statistically insignificant, which is likely a result of lower number of observations for emerging economies.

Table 3 *The relationship between globalization and welfare spending in emerging and less developed economies*

	Dependent variable: Social benefits expenditure as % of GDP		
Independent variables	*Model 1*	*Model 2*	*Model 3*
KOF index	-0.080 ***	-0.127 ***	-0.136 ***
	(0.020)	(0.021)	(0.019)
Polity II score	0.138 ***	0.155 ***	0.080 **
	(0.032)	(0.037)	(0.036)
Age dependency ratio	-0.061 **	-0.111 ***	-0.148 ***
	(0.027)	(0.027)	(0.023)
Urbanization levels	0.049 ***	0.055 ***	0.082 ***
	(0.009)	(0.009)	(0.009)
Logged GDP-per-capita	4.575 ***	5.438 ***	2.983 ***
	(0.716)	(0.618)	(0.735)
Annual GDP growth	-0.186 ***	-0.102 **	-0.039
	(0.045)	(0.050)	(0.044)
Inflation	0.061 **	0.034 *	0.064 **
	(0.026)	(0.018)	(0.019)
Current account balance	-0.123 ***	-0.105 ***	-0.118 ***
	(0.023)	(0.020)	(0.019)
Unemployment	0.258	0.245 ***	0.145 ***
	(0.026)	(0.030)	(0.019)
Tax revenue		0.020	0.128 ***
		(0.032)	(0.026)
Government debt levels			6.42e-12 **
			(2.49e-12)
Emerging dummy variable	5.223	2.544	(-3.593)
	(1.761)	(2.018)	(3.450)
Interaction between emerging dummy	-0.108 **	-0.077 ***	0.044
and KOF index	(0.027)	(0.029)	(0.051)
N	380	328	247
R-squared	0.516	0.607	0.606

Notes: The models are linear regressions with panel-corrected standard errors.
*** *p<0.01*
** *p<0.05*
**p<0.1*

Table 3: *Differences in effects of economic globalization on the welfare state in emerging and less developed economies*

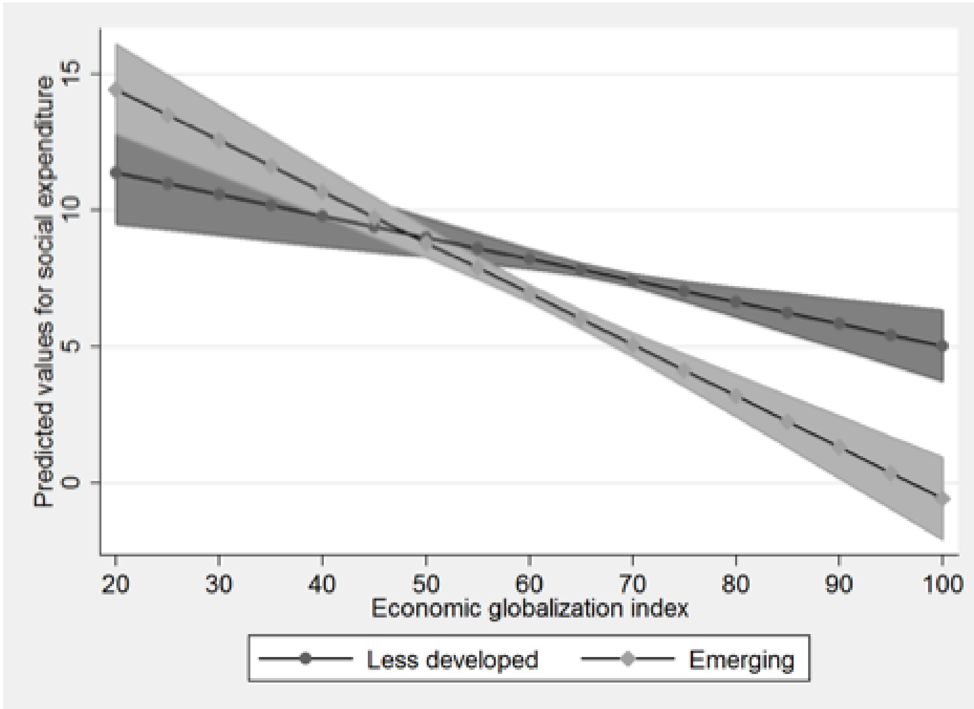

Figure 7: *Comparing predicted values of social expenditure between emerging and less developed countries based on Model 1 in Table 3 with 95% confidence interval*

Most importantly, the negative and statistically significant coefficient against the interaction term between the emerging economy dummy variable and the KOF index in the first two specifications suggests that the negative effect of globalization is even stronger for emerging economies compared to the less developed ones, as visualized in *Figure 7*. As it was explained in the theoretical framework, I suggested that the effect is likely to be more pronounced in the emerging economies, which have relatively higher level of wealth-per-capita and a longstanding tradition of elaborate social spending programs. In contrast, the less developed countries often have meagre welfare state, characterized by few very basic social spending schemes, while world's poorest countries often lack basic social protection programs, such as national pension system. As a result of this, governments in the emerging economies are able to retrench social spending on some of the less essential social security schemes when faced with increased globalization pressures. The less developed countries, however, do not have the same luxury.

4.4 Comparing the Impact of Globalization on the Welfare State across Regions

Apart from classifying countries into income groups, another common approach in the surveyed literature was to examine the impact of globalization on the welfare in a particular region. The majority of examined studies regarding the developing world have justified their regional focus by arguing that the welfare state – both in terms of universality and the extent of social security programs – often followed region-specific characteristics. While Esping-Andersen's typology[67] consisting of three distinct welfare systems – liberal, conservatist-corporatist and social-democratic – has been used to classify welfare regimes all around the world, many have argued that it is based on the examples of a handful of Western European states and, as such, it fails to effectively capture the dynamics of social provision outside of the developed West.[68]

For example, many of the surveyed studies have focused on Latin America, arguing that countries in this region, regardless of their level of economic development, have established elaborate social benefits schemes, some as early as the OECD nations. The emphasis on extensive social provision in the region is most likely due to the combined legacy of left-oriented governments[69] and the import substitution industrialization strategy (ISI)[70] of development, which was pursued by countries in the region prior turning to the export-oriented market liberalization. The ISI strategy generated considerable inequalities among citizens, forcing governments to establish extensive social benefits schemes in attempt to alleviate some of the disparities. However,

[67] Esping-Andersen, "The Three Political Economies of the Welfare State."

[68] John Hudson and Stefan Kuhner, "The welfare modelling business revisited: the case of East Asian welfare regimes," in *New Welfare States in East Asia: Global Challenges and Restructuring,* ed. Gyu-Jin Hwang (Edward Elgar Publishing, 2011): 35-60; Manuel Riesco, *Latin America: A New Developmental Welfare State Model in the Making?* (Palgrave Macmillan, 2007).

[69] Segura-Ubiergo, *The Political Economy of the Welfare State in Latin America*.

[70] Kurtz and Brooks, "Embedding Neoliberal Reform in Latin America."

this history of elaborate benefits programs made it very difficult to cut spending in post-ISI period, as any attempts to do so by the governments would generally be met with resistance by the citizens.[71]

At the same time, arguments of welfare state uniqueness have been put forward in the context of East Asia. It has been claimed in the literature that countries from this region have been shifting away from the kind of social welfare development that is characteristic of the West, instead developing a distinctive developmental welfare state model.[72] As Tang notes, East Asians firmly believe in the principle of trickle-down economics, a development strategy prescribing that, while economic growth must start from the top, it will eventually benefit everyone in the society. As a result, East Asian welfare state is characterized by low levels of government welfare spending (compared to advanced Welfare states), as well as very flexible labor markets – strategies aimed at increasing their international competitiveness.[73] This gave way to the development of a 'productivist' welfare state regime, in which social welfare development was subordinated to economic growth.[74] As a result, East Asian welfare state is characterized by a low levels of government welfare spending (compared to advanced Western welfare states), great emphasis on education, as well as the existence of flexible labor markets which guarantee cheap production costs, low wages and taxes, as well as flexible working hours in order to attract foreign investors. However, some scholars have pointed out that countries in this region have historically relied on private markets, as well as family

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[71] Wibbels and Ahlquist, "Development, Trade, and Social Insurance."

[72]. Kwong-Leung Tang, *Social Welfare Development in East Asia* (Palgrave, 2000); Gordon White and Roger Goodman, "Welfare Orientalism and the search for an East Asian Welfare Model," in *The East Asian Welfare Model: Welfare Orientalism and the State,* ed. Goodman, Kwon, and White, *The East Asian Welfare Model.*.

[73] Tang, *Social Welfare Development in East Asia*.

[74] Ian Holliday, "Productivist Welfare Capitalism: Social Policy in East Asia," *Political Studies* 48, no. 4 (September 1, 2000): 706–23; Riesco, *Latin America: A New Developmental Welfare State Model in the Making?*.

to be the principal providers of welfare, and that extremely low levels of public spending on social security programs paint a distorted image of what is a well-developed welfare system.[75]

Finally, due to the legacy of colonialism in Africa – which brought about social disruption, as well as economic and institutional underdevelopment -- the welfare state (if such term can be even employed in the African context) on this continent is yes to catch up with the rest of the world. While formal social security programs had been established during colonial times, they were extremely ineffective, compelling the poor to rely on their families for support.[76] In addition, decades of externally-imposed economic restructuring aimed at kick starting economic development has failed to industrialize the region. This, together with social tension between different ethnic groups and large informal sector characterized by illicit trade, has left limited capacity (in terms of both authority and resources) for the states to effectively provide social policies for its citizens.[77] As a result, the majority of African states have underdeveloped welfare systems, and many fail to provide even the basic protection schemes (such as health coverage or pension systems) to their people.

Given these fundamental differences in both the extent and the variety of social provision, I hypothesized that globalization is likely to affect welfare states differently in different regions, even after controlling for the level of development. The results of the regression analysis including regional dummy variables, as well as the interaction term of the region in question with the KOF index are presented in *Table 4*. Separate models are used to interact each of the regional dummy variables with KOF index in order to see whether the impact of globalization in the particular region is significantly different from the overall effect.

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[75] Christian Aspalter, "The East Asian Welfare Model," *International Journal of Social Welfare* 15, no. 4 (2006): 290–301.

[76] Philippa Bevan, "The dynamics of Africa's in/security regime," in *Insecurity and Welfare Regimes in Asia, Africa and Latin America: Social Policy in Development Contexts*, eds. Ian Gough and Geof Wood (Cambridge University Press, 2004): 202-249.

[77] Ibid.

In line with previous results, the main finding in *Model 1* suggests a statistically significant negative effect of globalization on the welfare state across the world. The most important control variables – Polity II score, logged GDP-per-capita, annual GDP growth and the level of urbanization -- proved to be consistently significant determinants of welfare spending. More importantly, all dummy variables signifying different regions are statistically significant, implying the existence of regional differences with respect to the size of the welfare state. However, while my hypothesis of regional distinctiveness proved accurate, the direction and the extent of the globalization effect was surprising in some cases.

In *Model 2,* the interaction term of KOF index and the region of Europe and Central Asia is included in order to compare whether the effect in this region differs significantly from the overall effect. The statistically significant and positive coefficient against the interaction term suggests that the effect of globalization on the level of social expenditure is more positive for countries in this region, providing evidence in favor of the compensation hypothesis. Given that the majority of Western European countries are advanced economies with strong labor unions, while Eastern Europe's socialist legacy implies a history of elaborate social provisions, this finding is not surprising. As a result, countries in this region increased spending on average in order to compensate their citizens for the hardships brought about by increased globalization. As discussed previously, the most likely motives behind such governments' actions are attempts to increase their favorability, as well as to secure domestic support for further liberalization (especially in the eastern part of the region).

Table 4	*Relationship between globalization and welfare spending by region*					
	Dependent variable: Social benefits expenditure as % of GDP					
Independent variables	*Model 1*	*Model 2*	*Model 3*	*Model 4*	*Model 5*	*Model 6*
KOF index	-0.084 ***	-0.171 ***	-0.072 ***	-0.074 ***	-0.087 ***	-0.089 ***
	(0.007)	(0.0154)	(0.007)	(0.005)	(0.008)	(0.007)
Polity II score	0.227 ***	0.243 ***	0.220) ***	0.191 ***	0.233 ***	0.291 ***
	(0.025)	(0,024)	(0.027)	(0.025)	(0.027)	(0,027)
Urbanization levels	0.065 ***	0.077 ***	0.063 ***	0.065 ***	0.065 ***	0.059 ***
	(0.004)	(0.004)	(0.005)	(0.004)	(0.005)	(0.004)
Logged GDP-per-capita	3.287 ***	3.324 ***	3.276 ***	3.497 ***	3.260 ***	3.730 ***
	(0.299)	(0.254)	(0.287)	(0.296)	(0.297)	(0.314)
Annual GDP growth	-0.236 ***	-0.224 ***	-0.232 ***	-0.230 ***	-0.235 ***	-0.231 ***
	(0.040)	(0.039)	(0.039)	(0.040)	(0.039)	(0.039)
Inflation	-0.050 ***	-0.026	-0.043 *	-0.047 *	-0.049 *	-0.035 **
	(0.016)	(0.016)	(0.016)	(0.016)	(0.016)	(0.017)
Current account balance	-0.033	-0.046 **	-0.032	-0.044 **	0.029	-0.036 **
	(0.021)	(0.020)	(0.021)	(0.022)	(0.021)	(0.021)
Unemployment	0.123	0.134	0.128	0.137	0.126	0.134 ***
	(0.027)	(0.027)	(0.026)	(0.027)	(0.026)	(0.026)
Tax revenue	0.018	0.016	0.020	0.026 **	0.021	-0.002
	(0.014)	(0.014)	(0.013)	(0.013)	(0.013)	(0.016)
Europe and Central Asia	6.460 ***	-2.026 **	6.327 ***	6.402 ***	6.463 ***	4.597 ***
	(0.225)	(0.880)	(0.237)	(0.208)	(0.223)	(0.227)
Latin America and the Caribbean	-2.306 ***	-2.168 ***	5.764 ***	-2.039 ***	-2.330 ***	-3.845 ***
	(0.419)	(0.281)	(1.214)	(0.258)	(0.269)	(0.282)
East Asia and the Pacific	0.126	0.405	0.118	9.576 ***	0.119	-1.609
	(0.418	(0.418)	(0.419)	(2.775)	(0.419)	(0.377)
Africa	-1.723 ***	-1.279 **	-1.868 ***	-1.646 ***	-5.362 ***	-3.3-4 ***
	(0.386)	(0.548)	(0.391)	(0.359	(1.897)	(0.356)
Interaction between Europe and Cental Asia and KOF index		0.125 ***				
		(0.015)				
Interaction between Latin America and the Caribbean and KOF index			-0.122 ***			
			(0.017)			
Interaction between East Asia and the Pacific and KOF index				-0.138 ***		
				(0.035)		
Interaction between Africa and KOF index					0.053 **	
					(0.026)	
Interaction between North America and KOF index						-0.060 ***
						(0.004)
N	696	696	696	696	696	696
R-squared	0.774	0.784	0.778	0.778	0.775	0.782

Notes: The models are linear regressions with panel-corrected standard errors.
Base region for this analysis is North America
*** $p<0.01$
** $p<0.05$
*$p<0.1$

Table 4: *Regional differences in effects of economic globalization on the welfare state*

At the same time, the negative and statistically significant interaction term in *Model 3* indicates a stronger than average negative impact of globalization on social provision in the region of Latin America and the Caribbean. This second most negative effect (following the East Asia and the Pacific region) contradicts the theory which predicted that, although globalization might have a negative effect on the welfare state in Latin American countries, this effect will not be as pronounced as in some other regions. It was proposed that Latin American governments, due to the legacy of generous social programs established during the ISI times, will find it difficult to retrench the welfare state significantly without being faced with strong popular opposition from citizens who became accustomed to years of extensive welfare privileges. A negative effect of globalization suggests that Latin American governments in this region might be moving away from their longstanding strategy of compensation and instead opting for achieving (and maintaining) competitiveness on the international markets.

As mentioned previously, the stronger than average negative effect of globalization on the East Asian welfare states (presented in *Model 4*) was expected, given their development-oriented nature of social provision. As it was pointed out in the literature, the belief in trickle-down economics implies that citizens are often prepared to endure short-term difficulties in order to achieve economic growth and development in the long run. Taking into account the underlying logic behind market liberalization, promising long-term prosperity after a painful adjustment period, governments' decision to retrench spending can be expected. However, it is important to keep in mind that government expenditure represents only a fraction of overall welfare spending in the region, as private actors, as well as informal family networks play an important role in social provision. Therefore, a retrenchment of government social policies might not have as big of an effect in the countries in this region, compared to those where government social spending is the primary channel of welfare provision.

The findings in *Model 5* indicate a more positive effect of globalization on social spending in Africa (countries in Sub-Saharan Africa and North Africa were allocated into one group due to the small number of observations). A much smaller coefficient on the interaction term in this region compared to the others suggests, in accordance with the literature, that globalization did not have as much of an impact on social provision in this region as in the rest of the world due to the underdeveloped welfare system. At the same time, according to the *World Health Organization*, the region has seen a drastic increase in life expectancy in the period 2000-2015 (by 9.4 years), potentially increasing the number of elderly dependents and incurring higher welfare costs on the states.[78] However, given the lack of attention placed on the welfare state in Africa, more research is necessary in order to identify the exact mechanisms that drive welfare spending in this region.

Finally, in *Model 6,* the baseline region of North America was interacted with the KOF index in order to check if globalization has a significantly different effect on this region. The negative and statistically significant coefficient for the interaction term suggests that globalization has had a more adverse than average effect on the welfare state in this region (more precisely, in its only two countries: Canada and the United States). Contrasting this finding with the European one, this shows that the compensation approach is not universal for advanced economies.

The results in this analysis suggest that, when it comes to the effects of globalization on the welfare state, Europe is the exception rather than the rule. At the same time, the majority of studies that argue for the compensation hypothesis are focused on this region. However, the analysis above indicates that countries in other parts of the world might have different underlying mechanisms that determine their social spending policies and that, in most cases, findings outside of the European context are along the lines of the efficiency hypothesis. Overall, the significance of regions, even

[78] "WHO | Life Expectancy," (*WHO,* 2016), accessed May 30, 2016, http://www.who.int/gho/mortality_burden_disease/life_tables/situation_trends_text/en/.

when controlling for the level of economic development, suggests that historical development of welfare states or other region specific characteristics also influences the relationship between globalization and welfare spending.

5. Conclusion

The aim of this study was to investigate whether globalization has a different impact on the welfare state in countries at different stages of economic development. By doing so, it has attempted to shed light on the underexplored relationship between increased globalization and social spending in the developing world. In addition, it has attempted to contribute to the existing literature by separating the developing countries into two subgroups – emerging and less developed economies – in order to explore whether different stages of economic development in these two groups will condition distinctive effects of globalization on the welfare state. In addition, emulating numerous studies in the surveyed literature, the final part of this analysis has assessed the plausibility of regional distinctiveness with respect to the effects of economic globalization on social spending. The overall effect of economic globalization on social spending in this study was negative, implying that a restrictive influence on welfare policies took place around the world in the last fifteen years. However, once countries were disaggregated into groups based on their level of economic development and their geographical region, globalization was shown to have diverse effects on social spending policies.

The findings provide evidence in support of the primary hypotheses behind this research project. The results indicate that, on average, economic globalization has a positive effect on welfare state in the advanced countries, while the same effect for the developing countries is negative. At the same time, comparing the two subgroups of developing countries has shown that, while the effect for the group as a whole is negative, welfare states in the emerging economies are on average more adversely affected compared to their less developed counterparts.

The positive effects of globalization on the welfare state in the world's most advanced economies are consistent and thoroughly discussed findings in the literature. It is argued that the existence of highly centralized labor unions as well as strong interest groups consisting of consumers of welfare has resulted in high bargaining power *vis-à-vis* the government, in turn enabling them to effectively negotiate against the retrenchment of welfare policies. At the same time, most advanced nations have a status of longstanding healthy democracies in majority of the advanced nations where governments are democratically elected and accountable to their citizens. As such, they are likely to compensate their citizens for the hardships caused by globalization in order to build domestic support for further liberalization as well as to improve their popularity in cases when they are up for reelection.

At the same time, this study indicates a negative effect of globalization on the welfare state in the developing countries. A few other studies that came to similar conclusions suggested several plausible explanations for this finding. The most prominent one was put forward by Nita Rudra, who believed that the low level of labor centralization was the main reason behind the adverse effects of globalization on social spending in the developing world. She noted that, in the developing world, low skilled workers (which are generally more directly affected by globalization trends) are conducive to the collective action problem, making it extremely difficult for union leaders to effectively organize them. As a result, fragmented labor unions have limited bargaining power and are generally unable to dissuade their government from retrenching social spending.

At the same time, many developing countries are new, fragile democracies, some with significant institutionalized legacies of their authoritarian past, making governments in those countries less accountable (and arguably less concerned) for the wellbeing of citizens compared to the advanced economies. Finally, conditioned by different factor endowments (i.e. abundant capital in the advanced versus abundant labor in the developing countries), the two groups have different integration paths into the global economy. While the advanced countries have much easier access to capital markets and are able to borrow money more easily, the developing countries usually do not have the same luxury. Instead, during economics downturns such as the Great Recession (2007-2009), they are often compelled to keep balanced budgets and maintain the image of economic stability in order to attract investment. This, in turn, is likely to have an adverse effect on government spending in general and the welfare state in particular.

The main contribution of this study to the literature yielded statistically significant results indicating that social spending in the emerging economies is more adversely affected by the process of globalization compared to the least developed economies. My argument for why this is the case is twofold. Firstly, many emerging economies – especially those with significant socialist legacy-- have elaborate social security programs, having historically allocated a significant percentage of government spending to the provision of a wide array of social security programs. At the same time, higher income per capita in emerging economies provided governments with more financial resources that were partially used to improve the existing welfare programs, as well as introducing new ones. So the welfare spending was at a higher level to retrench from compared to their less developed counterparts. Furthermore, governments in this group of countries – characterized by developed welfare states but lacking high labor centralization characteristic of the advanced nations – find it easier to retrench spending without facing serious resistance from their citizens. In contrast, governments in the world's least developed countries have put only the basic welfare programs in place, leaving very little room for significant retrenchment of spending.

The last analysis in this study suggests that there are significant regional differences in the effect of globalization on the welfare state. While the effects for the regions of Europe and Central Asia, Africa, as well as East Asia and the Pacific were expected, the results obtained for Latin America were somewhat surprising. The average effect of globalization on the welfare state in Europe and Central Asia, due to the combined effect of advanced economies in the western part of the region and the socialist legacy in the eastern part, was positive. Similarly, due to their development- and growth-oriented social policies, governments in East Asia and the Pacific have expectedly retrenched their welfare spending in exchanged for remaining competitive on the global market. Surprisingly, the results also indicated that countries in Latin America have, on average, retrenched welfare spending in time of globalization, suggesting that they might be moving away from the compensation strategy typically associated with this region in order to successfully complete the process of market liberalization. Finally, the small positive effect of economic globalization of the welfare state in Africa suggests that countries in this region might have finally begun to invest in the development of the historically weak welfare state in their respective countries. The alternative explanation could be that, due to the dramatic increase in life expectancy on the continent in the past two decades, there has been an increasing number of elderly dependents eligible for government support. Based on this analysis, it seems that the compensation hypothesis applies primarily in Europe.

In addition, it is important to note several limitations of this study. Primarily, the lack of available data on several key variables, especially in the developing countries, has proven to be a significant obstacle in attaining credible regression results. In order to partially remedy this problem and avoid results that are biased towards the trends in the advanced nations due to more data availability, data for social benefit expense was imputed and regression results were compared to the non-imputed to make sure the results are not considerably different. At the same time, the data on social benefits expenditure was missing on some of the most prominent emerging economies, such as China, India and Brazil, which makes the generalizability of findings pertaining to the emerging economies group problematic in the context of these countries. Finally, the lack of data on trade union density has prevented this study to test one of the most important assumptions in most studies done on the developing world – that labor power is the most significant factor determining the effect of globalization on the welfare state.

Finally, some of the key findings presented in this study open new questions that should be addressed and explored in future research. While the possible reasons for different effects of globalization on the welfare state with respect to stages of development and geographical location have been suggested, case study examination is essential in order to identify underlying mechanisms behind such trends, as well as their generalizability across the particular group. This is especially necessary in the context of emerging economies, where welfare states have received very little scholarly attention. Finally, the impact of other potentially important factors, such as the Great Recession, should be examined in order to investigate whether the retrenchment of the welfare state on a global level was partially a byproduct of austerity measures employed by many governments in the wake of the economic crisis.

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