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Did globalization restrict partisan politics? An empirical evaluation of social expenditures in a panel of OECD countries

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Abstract This paper evaluates empirically how, in the course of globalization, partisan politics affected social expenditures in a panel of OECD countries. I introduce an updated indicator of government ideology and investigate its interaction with the KOF index of globalization. Two basic results emerge: First, at times when globalization proceeded at an average pace, partisan politics had no effect on social expenditures, but leftist governments increased social expenditures when globalization was proceeding rapidly. Second, policies differed in the 1980s and 1990s: Leftist governments pursued expansionary policies in the 1980s. Yet partisan politics disappeared in the 1990s, but not because of globalization.

Keywords Partisan politics · Globalization · Social expenditures · Welfare state · Panel data

JEL Classification H53 · H87 · I38 · D72 · F02 · C23

1 Introduction

In the media it is often claimed that globalization counteracts partisan politics, or even restricts politicians' options or abilities to maneuver. Leftist governments are, for example, believed to have lost the ability to implement their preferred policies such as income redistribution. The available empirical evidence for the OECD countries does, however, not indicate that globalization restricted partisan macroeconomic politics. Unfortunately, the existing studies do not focus on social expenditures even though it is exactly the welfare state that is believed to be under siege and would be extended by leftist governments as a response to globalization, if this were a viable option.

Two schools of thought relate to the globalization-welfare state nexus. The partisan approach predicts that leftist governments respond to globalization by implementing higher social expenditures than rightwing governments, whereas non-partisan economic reasoning

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either suggests that the welfare state collapses (via the supply side or efficiency effect) or that the welfare state is extended (via the demand side or compensation effect). Hence, without any clear theoretical prediction, it remains an empirical issue how globalization affects social expenditures. In the empirical literature on the determinants of social expenditures, globalization and government ideology have been analyzed separately, i.e. the interaction of globalization and government ideology has not been investigated up to now. This is a serious shortcoming, because, as the partisan approach suggests, globalization-induced policy responses may well depend on political ideology. This study therefore carefully investigates interaction effects of globalization and ideology.

Empirical research on the globalization-welfare state nexus progressed mainly along three lines. First, globalization indices emerged that portray globalization as a multifaceted concept that cannot be captured by a single economic indicator such as international trade, foreign direct investments or capital account restrictions. The KOF index of globalization is a case in point (KOF is an abbreviation for "Konjunkturforschungsstelle"—Swiss Economic Institute). Second, much progress has been made in applied econometrics with the result that the views on the appropriate econometric techniques for investigating the impact of globalization on the welfare state appear to converge. Third, new data sets are collected which allow testing for policy differences until the beginning of this millennium. The OECD Social Expenditure Database (OECD 2007), for example, allows one to investigate partisan politics in sub periods. Apart from the specific focus on interaction effects of globalization and ideology, this study takes advantage of these three developments by using the most adequate globalization index (the KOF index), the most advanced econometric techniques and the best available data on social expenditures. Moreover, I introduce an updated indicator of government ideology that explicitly refers to the left-right scale of the parties. This indicator is consistent across time but does not attempt to capture differences between the party-families across countries.

Two basic results emerge from the empirical analysis of the 1980–2003 period: First, at times when globalization proceeded at an average pace, partisan politics had no effect on social expenditures, but leftist governments increased social expenditures when globalization was proceeding rapidly. Second, policies differed in the 1980s and 1990s: Leftist governments pursued expansionary policies in the 1980s. In contrast, partisan politics disappeared in the 1990s, but not because of globalization.

The paper is organized as follows: Sect. 2 discusses the theoretical background, the related empirical literature on partisan politics, and potential globalization-induced restrictions with a view to their impact on the welfare state. Section 3 presents the data and variables, and specifies the empirical model. Section 4 reports the estimation results. Section 5 discusses the implications of the empirical results, investigates their robustness, relates the empirical findings to historical incidents in individual countries, and provides suggestions for further research.

2 Theoretical background and related empirical literature

2.1 The parties-do-matter-hypothesis

Political economic theory provides various arguments as to why different politicians will implement different policies—Downs' (1957) fundamental convergence result notwithstanding. If politicians are not motivated only by self-interest but also care about the political outcomes as such, probabilistic voting models exhibit equilibria in which leftwing and rightwing politicians offer different platforms.[1] The empirical political science literature provides interesting insights into why we ought not to expect modern parties to be ideological in any pure sense of the word. This literature, in particular, dismisses the move of ideologically leftwing and rightwing parties towards "catch-all" parties (e.g. Katz and Mair 1995; Blyth and Katz 2005).[2] In spite of these developments, politicians' behavior is still expected to affect economic policy. The political business cycle approaches and the partisan theory indicate how politicians influence economic outcomes. The partisan approach focuses on the role of party ideology and shows to what extent leftwing and rightwing politicians will provide different policies that reflect the preferences of their partisans.[3] The leftist party appeals more to the labor base and promotes expansionary policies, whereas the rightwing party appeals more to capital owners, and is therefore more concerned with reducing inflation. This holds for both branches of the partisan theory—for the classical approach (Hibbs 1977) and for the rational approach (Alesina 1987). For a survey of the literature see e.g. Alesina et al. (1997).

The 'parties do matter hypothesis' was scrutinized in several empirical studies. For example, higher public expenditures under leftist governments were reported by e.g. Blais et al. (1993, 1996) and Cusack (1997) for panels of OECD countries. But overall, previous research does not provide consistent empirical evidence that leftist governments increased public spending. The empirical results also suggest that partisan politics became less important during the last years, in particular since the beginning of the 1990s. In fact, the meta analysis including 43 empirical studies by Imbeau et al. (2001) shows that the average correlation between the party composition of government and policy outputs is not significantly different from zero. Interestingly, in the pre-1973 period, the leftwing-rightwing partisan composition of government predicts welfare spending better than policy outputs in other domains. But, in the post-1973 period, when economic growth was lower and unemployment rates were higher, partisan conflicts focused on the appropriate size of the public sector rather than social expenditures in particular (Imbeau et al. 2001: 24). Thus, the question remains as to why there were only weak policy differences and why they became less pronounced over time.

2.2 The impact of globalization on partisan politics

The hypothesized interactions between government ideology and economic policy might be weakened by globalization, since globalization may diminish the power of nation-states. Some commentators even fear that economic integration and market forces may induce a downward spiral in welfare provision irrespective of ideology because international tax competition is expected to result in a race to the bottom of (capital and corporate) tax rates.[4]

[1] See, e.g., Mueller (2003: Chaps. 11–13) and Persson and Tabellini (2000: Chaps. 3 and 5) for surveys of the fundamental literature on party competition.

[2] This so called catch-all party concept was developed by Otto Kirchheimer (see Krouwel 2003 for a description of Otto Kirchheimer's ideas). As factors in the rise of catch-all parties, he points to the erosion of parliamentary democracy and the vanishing of political opposition, he also was concerned about the so called 'state-party cartel' and the professional approach of party organizations and the personalization of the party-voter link.

[3] In contrast, one implication of the political business cycle theories of Nordhaus (1975) and Rogoff and Sibert (1988), among others, is that all politicians will implement the same expansionary economic policy before elections. Stated differently, political ideology becomes somewhat irrelevant, and policies converge.

[4] In fact, there is no race to the bottom of capital tax rates. For recent empirical evidence for OECD countries see e.g. Plümper et al. (2009).

As a consequence, the size of government and expenditures on social affairs are reduced (see Schulze and Ursprung 1999 and Ursprung 2008 for surveys of the literature on the globalization-welfare state nexus). Governments' ability to regulate markets is also expected to become more restricted because market structures change in the course of globalization. Cerny (1994) argues that financial globalization increasingly constrains policymakers and reduces the policy capacity of the state. In particular, the change in the technological infrastructure of the economic-institutional system influences the impact of financial globalization. It is not only the volume of capital flows but the structure of markets that allows the actors in the financial system to stay ahead of the state as a regulator. Moreover, in telecommunications, authority has shifted away from the governments to the managers of the private providers (Strange 1995: 301). Financial integration also creates pressure for cross-national convergence in monetary policy. As a response, interest rates could be harmonized in fixed exchange rate systems to avoid capital flight in a single country ("capital-mobility hypothesis"—see e.g. Andrews 1994a).[5] According to an especially pessimistic view, globalization is responsible for the fact that the differences between government and opposition policies are about to disappear (Strange 1995: 291). Leftist parties and governments lost their ability to pursue their preferred economic policies and "the environment has changed in such a way that traditional social democratic instruments are no longer effective" (Moses 1994: 133). But there is empirical evidence that contradicts this hypothesis. Partisan cycles in fiscal and monetary policies exist even in open economies.[6] Oatley's (1999) results, which apply to a panel of 14 OECD countries in the period 1970 to 1994, for example, suggest that capital mobility did not prevent governments from pursuing distinctly partisan macroeconomic policies. In the beginning of the 1990s partisan effects do however weaken in countries with fixed exchange rates. Oatley (1999) argues that this finding can be attributed to the recession of the early 1990s and to important institutional changes in the European Union. Moreover, compared to fiscal and monetary policy, the impact of globalization on social policy seems to be different. Supply-side policies of transfers and services do not appear to be constrained as long as tax revenues continue to flow and are not associated with high debt levels (Garrett and Lange 1991). Retrenchment initiatives are associated with high electoral costs, which explain the persistence of the welfare state (Piersson 1996).

In contrast to this literature on the dark side of globalization, many other studies arrive at the conclusion that globalization does not tie politicians' hands at all. This view corresponds with the compensation hypothesis that predicts increasing social expenditures because the national governments try to protect their citizens against the risks of globalization (e.g. Rodrik 1997, 1998). Garrett (1998: 1) argues "that the relationship between the political power

[5]This hypothesis was only confirmed by case studies for some OECD countries: Goodman and Pauly (1993: 81) conclude from their case studies of Germany, Japan, France and Italy that capital liberalization reduced the ability of governments to set autonomous economic policies. Walsh (1994) also argues that international capital mobility imposed constraints on national economic policies and led to policy convergence, but at least in France, policymakers too were able to design and partially implement a strategy of domestic adjustment. Andrews (1994b) analyses the impact of heightened international capital mobility for ten industrial Western European countries in the period 1973 to 1991 and concludes that there was a remarkable similarity of policies eventually adopted: The external constraint imposed upon each of the ten states by financial integration had become severe.

[6]Besides the effects of the interaction between partisan politics and globalization on economic policy, Hicks (2004) examines the likelihood of central bank reform in a sample of 48 developed and developing countries over the period 1973 to 1998. The results illustrate that leftwing governments are more likely to grant independence to the central bank as exposure to the international economy increases. He interprets this finding in the way that leftwing parties are concerned about the effect their economic policy has on international investment and will take steps to mollify investors.

of the left and economic policies that reduce market-generated inequalities has not been weakened by globalization; indeed, it has been strengthened in important respects". Globalization does not only increase competition between nation states but also increases market dislocations. This causes a greater demand for interventionist policies which leftist governments are happy to supply. Therefore, globalization does not restrict, but rather encourages partisan politics. Garrett (1998—and previously Garrett 1995) finds empirical support for this claim for different macroeconomic indicators in a panel dataset of 14 OECD countries in the period 1966 to 1990. He uses two measures of globalization: international trade as a share of GDP as well as government restrictions on cross-border capital flows. Policy differences are measured with an additive "left-labor power" index because, according to Garrett, it is not only leftist governments which try to gratify their clients but also governments allied with powerful labor unions. Garrett infers from his analysis that the redistribution of wealth and social risk generated by the economic policies of social democratic corporatism in response to globalization was not achieved at the expense of overall macroeconomic performance (p. 107). In a similar vein, Boix (1998: 3 f.) argues that "as a matter of fact, the increasing globalization of the economy has forced the convergence of national macroeconomic policies, has, on the contrary, magnified the role of (competing) supply-side economic strategies and intensified the importance of parties and partisan agency in the selection of the policies". However, Clark (2003) re-analyzes data from Garrett (1998) and concludes that there is little evidence of partisan differences and that the recent increase in international integration has done little to change this. He interprets these results as indirect evidence in support of the partisan model's main political economic competitor (the electoral model). Leftist governments did not respond to increased demands for protection from the risks of the international economy; it is rather the structure of democratic capitalism that has discouraged partisan differences.

Further arguments regarding the interaction of globalization and partisan politics vary between the beliefs that a) nothing has changed and b) that there is still a role for policy and ideology, but parties will adjust somewhat to the process of integration. Iversen and Cusack (2000) argue that most of the risks being generated in modern industrialized societies are the product of technologically induced structural transformations inside national labor markets. Their empirical results for 16 OECD countries in the period 1962 to 1993 suggest that it is not trade or capital market openness, but instead deindustrialization that is the driving force behind the expansion of government spending on both transfers and services. Crepaz (2001: 2) argues that whatever happens in the international arena will be filtered and refracted through domestic political institutions. He analyses a panel of 15 OECD countries and finds that globalization is positively related to the state's redistributive capacity as measured by the difference in the share of households living below 50% of the median income before and after taxes and transfers. Moreover, there is a debate on the causes of retrenchment. Piersson (1996, 2001), for example, identifies post-industrial changes as a potential reason and distinguishes four profound transitions: employment profiles of affluent societies becoming increasingly service-based, maturing of the welfare state, population aging and changes in household structures. His "new politics" argument indicates that national policy differences do not vanish entirely, but do become less pronounced over time, parties and institutions continue to be important players, but their role has changed (Kitschelt 2001). In conclusion, the interaction of globalization and partisan politics still requires further empirical evaluations.

2.3 Globalization, partisan politics and the welfare state

In the empirical literature on the determinants of social expenditures, the impact of globalization and the impact of government ideology have been considered in two separate strands of the literature, implying that their combined effect has not been investigated. The first strand of literature focuses on the influence of government ideology. Hicks and Swank (1992), for example, analyze a panel of 18 OECD countries in the period 1960 to 1982 and find that leftist governments generated higher welfare effort than rightwing governments. Huber et al. (1993) also focus on the impact of partisan politics on the welfare state. They investigate different measures of welfare state policies and detect significantly different effects of Christian democrat and social democrat governments on transfer payments, social benefits expenditure, and total government revenue. Overall, there is a large number of studies concerning the topic of whether leftist governments indeed spend more on social programs than their rightwing counterparts. The evidence is somewhat ambiguous and partisan effects are shown to have declined in the beginning of the 1990s (e.g. Iversen 2001; Kittel and Obinger 2003).

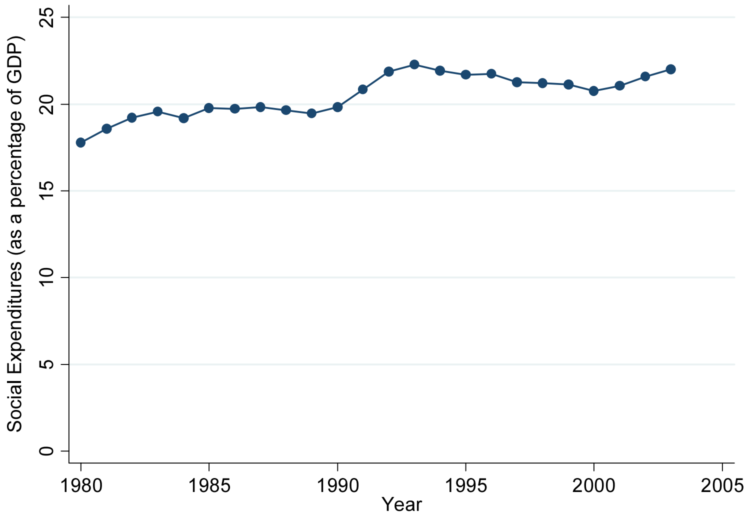
Garrett and Mitchell's (2001) famous contribution relates to the second strand of literature and focuses on the impact of globalization on the welfare state. In their panel analysis for OECD countries in the period 1961 to 1993, Garrett and Mitchell (2001) incorporate globalization as measured by the terms of total trade, imports from low wage economies, foreign direct investments and financial market integration. These variables are shown to have different effects on welfare expenditures. Subsequent re-estimations by Plümper et al. (2005) and Kittel and Winner (2005) revealed that social expenditures are affected mostly by national economic determinants, such as GDP and unemployment. Kumpmann's (2004) results rather suggest that social expenditures decrease with increasing international trade, whereas the results by Gemmell et al. (2008) suggest that foreign direct investments shift the expenditure composition to social affairs, thus supporting the compensation hypothesis. Applying the KOF-globalization index, Dreher (2006a) and Dreher et al. (2008a) could not detect any significant relationship between globalization and social expenditures in the OECD countries. In contrast, Dreher et al. (2008b) and Vaubel (2000) as well as Vaubel (2005) report a positive relationship between globalization and social expenditures. In conclusion, the more recent empirical studies appear to support the compensation hypothesis. The following crucial question thus remains: Is the persistence of the welfare state a consequence of the policies pursued by leftist governments, or, more generally, do globalization-induced policy responses depend on political ideology?

3 Data and empirical strategy

3.1 Data on social expenditures

I use data provided by the OECD Social Expenditure database (OECD 2007). The dataset contains yearly data on public social expenditures (as a percentage of GDP) for 20 OECD countries. The countries included are Australia, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Portugal, Spain, Sweden, Switzerland, the United Kingdom and the USA. The observation period runs from 1980 to 2003. The panel is balanced.[7] In principle, the examination of

[7] Data for Austria, the Czech Republic, Hungary, Iceland, Korea and Poland are available from 1990. For Mexico there are data from 1985 to 2003 and for Norway from 1988 to 2003 without gaps. To keep the panel balanced, I do not include these countries.



Source OECD (2007): Social Expenditure Database (SOCX 2007)

Fig. 1 Social Expenditures (as a percentage of GDP) from 1980 to 2003; average of the 20 OECD countries examined in the current paper

social expenditures across countries is problematic, since the social benefits, and above all, their classification, differ across countries. The OECD, however, specifically addresses this problem. In the category "total expenditures"[8] the OECD includes transfers in nine different fields and defines these transfers as follows: "Social expenditure is the provision by public and private institutions of benefits to, and financial contributions targeted at, households and individuals in order to provide support during circumstances which adversely affect their welfare, provided that the provision of the benefits and financial contributions constitutes neither a direct payment for a particular good or service nor an individual contract or transfer" (OECD 2007). Using the SOCX appears to be the best available procedure for analyzing social expenditures in a cross-country study.

Figure 1 illustrates that on average, social expenditures as a share of GDP increased from about 17.8% in 1980 to about 22.0% in 2003. In the period 1991–1995, the share increased especially fast from 19.4% to 22.3%. These descriptive statistics do not indicate erosion but rather extension of the welfare state during the last few decades. I will use these series as dependent variables in the econometric model and evaluate whether partisan politics in the course of globalization provides an explanation for this development.

3.2 The empirical model

The basic static panel data model has the following appearance:

$$\begin{aligned}&\Delta\ln\ \text{'Social Expenditures'}_{it} = \alpha\ \text{'Ideology'}_{it} + \beta\Delta\ln\ \text{'KOF Index of Globalization'}_{it}\\&+\gamma\ \text{'Ideology'}_{it} * \Delta\ln\ \text{'KOF Index of Globalization'}_{it} + \Sigma_m\delta_m\Delta\ln X_{imt} + \eta_i + \varepsilon_t + u_{it}\end{aligned}$$

[8]Note that this general definition refers to total social expenditures, but I examine only publicly financed social expenditures in the current paper.

with $i = 1, \ldots, 20$; $m = 1, \ldots, 3$; $t = 1, \ldots, 23$, where the dependent variable $\Delta \ln$ 'Social Expenditures'$_{it}$ denotes the growth rate of social expenditures (as a share of GDP).[9] 'Ideology'$_{it}$ describes the ideological orientation of the respective government and 'KOF Index of Globalization'$_{it}$ captures the globalization process. In the next paragraphs I describe these variables and their coding in detail. I include the interaction of the ideology and the globalization variable in order to identify potential differences between leftwing and rightwing governments facing high globalization. $\Sigma_m \delta_m \Delta \ln X_{imt}$ contains three exogenous control variables (as well as a constant if the estimation method calls for one). I follow the related literature by including the growth rate of real GDP per capita ($\Delta \ln \mathrm{GDP}_{it}$), the growth rate of the unemployment rate ($\Delta \ln \mathrm{Unemployment}_{it}$), and the growth rate of the dependency ratio measured as the share of the citizens aged above 64 and below 14 ($\Delta \ln$ Dependency Ratio_{it}). Thus, the general economic situation, the situation of the labor market, and the demographic development are taken into account. Note that the level of the dependent variable is expressed in shares, so that deflating is not an issue. Lastly, η_i represents a (potential) fixed country effect, ε_t is a fixed period effect and u_{it} describes an error term.

An important challenge for testing the partisan theory in an OECD panel is found in the heterogeneity of the parties and parliamentary systems in the individual nation states. Hence, the question arises as to what kinds of governments should be labeled leftwing or rightwing—especially when there are more than two parties in the government with different ideological roots. Scholars often use the index of Budge et al. (1993), updated by Woldendorp et al. (1998, 2000), as a measure of the governments' ideological positions. This index places the cabinet on a left-right scale with values between 1 and 5. It takes the value 1 if the share of governing rightwing parties in terms of seats in the cabinet and in parliament is larger than $2/3$, and 2 if it is between $1/3$ and $2/3$. The index is 3 if the share of centre parties is 50%, or if the leftwing and rightwing parties form a coalition government not dominated by one side or the other. The index is symmetric and takes the values 4 and 5 if the leftwing parties dominate. Adopting that classification, I construct an ideology index for the 20 examined countries over the period from 1980 to 2003. However, my coding explicitly refers to the left-right scale of the parties. This indicator is consistent across time but does not attempt to capture differences between the party-families across countries. The years in which the government changed are labeled according to the government that was in office for a longer period, e.g. when a rightwing government followed a leftwing government in August, I label this year as leftwing. Note that the coding of the ideology variable gives rise to the expectation that social expenditures vary positively with the ideology index. Furthermore, I normalize the ideology variable (mean zero, variance one), so that I can directly interpret the coefficients and marginal effects across the specifications.[10]

Globalization is a multifaceted concept that cannot be captured fully by a single economic indicator such as international trade, foreign direct investment or capital account restrictions. That is why the overall KOF index of globalization was introduced. This index represents an attempt to measure globalization in the broad sense that has been accepted in the recent empirical literature. The KOF index was first presented in 2002 (Dreher 2006b), it covers 123 countries and includes 23 variables. The index embraces the economic, social and political dimensions of globalization. Each of these three dimensions has further sub-dimensions. For example, economic globalization is described by actual flows (trade,

[9] Panel unit root tests indicate that these variables are stationary. Hence there is reason to be concerned about spurious regression.

[10] Note that I also normalize the variables for the respective sub-periods explicitly (see Sect. 4.2).

foreign direct investment, portfolio investment and income payments to foreign nationals each measured as a percentage of GDP) and restrictions (hidden import barriers, mean tariff rate, taxes on international trade and capital account restrictions). Social globalization covers, among others, items such as international tourism, number of internet hosts and users as well as the number of McDonald's restaurants and the number of IKEA shops (per capita). Political globalization is described by the number of foreign embassies, membership in international organizations and the participation in U.N. Security Council missions (see Dreher et al. 2008b: 43 ff. for further details). In this study, I use the updated 2007 KOF index of globalization which measures globalization on a scale of 1 to 100, where higher values represent higher levels of globalization. I use growth rates of the normalized index because the index is not stationary in levels. Table 5 in the Appendix reports descriptive statistics and data sources of all variables.

I now turn to discussing my choice of the panel data estimation methods. First, taking growth rates of the dependent variable eliminates time-invariant fixed effects in levels. But in case of individual time trends in each country, computing growth rates just eliminates the time-invariant country effects, but not the individual time components. Thus, it is also sensible to apply the least squares dummy variable estimator (fixed-effects) on the growth rates. Random effects could be present also, because I do not examine all OECD countries. In addition, I implement heteroscedastic and autocorrelation consistent (HAC) Newey-West type (Newey and West 1987) standard errors and variance-covariance estimates, because the Wooldridge test (Wooldridge 2002: 176–177) for serial correlation in the idiosyncratic errors of a linear panel-data model implies the existence of arbitrary serial correlation. Moreover, to control for contemporaneous correlation across the countries I present the results of a regression with panel corrected standard errors according to Beck and Katz (1996). Alternatively, the model can be estimated using a dynamic panel data framework. However, in the context of dynamic estimation, the common fixed-effect estimator is biased. As Behr (2003) states, the estimators taking into account the resulting bias can be grouped broadly into the class of instrumental estimators and the class of direct bias corrected estimators. In accordance with large sample properties of the GMM methods, e.g. the estimator proposed by Arellano and Bond (1991) will be biased in the current framework with $N = 20$. For this reason, bias corrected estimators are appropriate (see also Adolph et al. 2005). Bruno (2005a, 2005b) presents a bias corrected least squares dummy variable estimator for dynamic panel data models with small N. I intend to test for the impact of partisan politics in the course of globalization in a robust econometric framework, and the following section will present results of different estimation methods, and thereby clarify the soundness of the results.

4 Results

4.1 Basic scenario: 1980 to 2003

Table 1 contains the regression results for the period 1980 to 2003. Compared to a regression with a common constant, I can reject the null hypothesis of the F-Test that all the fixed time and country effects are zero. Furthermore, I cannot reject the Hausman-Test in favor of the random effects model. Hence, in this case, the random effects estimator (RE) is efficient as well as consistent. The second column refers to the model estimated by panel corrected standard errors (PCSE) and the third column refers to the dynamic specification including

Table 1 Regression results 1980–2003. Dependent variable: Δ ln Social Expenditures. Fixed period effects included

	(1) RE	(2) PCSE	(3) DYN
Ideology (leftwing)	0.001	0.001	0.004*
	[0.93]	[0.70]	[1.85]
Δ ln KOF Index	–0.001	-3×10^{-4}	-3×10^{-4}
	[0.22]	[0.14]	[0.12]
Ideology* Δln KOF Index	0.003	0.003*	0.004**
	[1.27]	[1.92]	[2.49]
Δ ln GDP (per capita)	–0.690***	–0.703***	–0.689***
	[5.58]	[5.63]	[5.88]
Δ ln Unemployment	0.049***	0.047***	0.045***
	[3.28]	[3.30]	[3.13]
Δ ln Dependency Ratio	–0.049	–0.049	0.052
	[0.27]	[0.23]	[0.27]
Lagged Dependent Variable			0.137***
			[3.08]
Constant	0.035***	0.035***	
	[3.62]	[4.02]	
Observations	455	455	435
Number of n	20	20	20
R-squared (overall)	0.40	0.38	

Notes: Absolute value of t statistics in brackets (absolute values); * significant at 10%; ** significant at 5%; *** significant at 1%

a lagged dependent variable (DYN).[11] Table 1 reports the coefficients and t-statistics (in absolute terms) for every single equation.

The control variables display the expected sign and their impact is highly robust across the different econometric specifications. The negative elasticity of real per capita income as well as the positive impact of the unemployment rate on social expenditures corroborates that, in recessions, the government will provide compensating transfer payments. The estimated coefficients imply that social expenditures (as a share of GDP) decreased by about 0.7% when the real per capita GDP increased by one percent and increased by about 0.05% when the unemployment rate increased by one percent. In contrast, the dependency ratio is statistically insignificant. This result also corroborates the findings of the related literature.

As can be seen from Table 1, the coefficients of the ideology variable are positive but statistically insignificant in specifications (1) and (2) and the ideology variable is weakly significant in the dynamic model (column 3). The overall KOF globalization index indicates a negative but statistically insignificant effect on social expenditures. The interaction

[11] The results refer to the Blundell and Bond (1998) estimator as the initial one with which the instruments are collapsed as suggested by Roodman (2006). Following Bloom et al. (2007) I undertake 50 repetitions of the procedure to bootstrap the estimated standard errors. Note that the results do not change qualitatively with more repetitions such as 100, 200 or 500 as well as when the Arellano and Bond (1991) estimator is chosen as initial one.

Table 2 Marginal effects of government ideology (leftwing) at a minimum and maximum level of the overall KOF index of globalization (growth rate, normalized) 1980–2003

RE		PCSE		DYN	
min (–3.83)	max (4.89)	min (–3.83)	max (4.89)	min (–3.83)	max (4.89)
–0.010	0.016	–0.012*	0.017**	–0.013**	0.025***
[–1.10]	[1.37]	[–1.67]	[2.03]	[–2.03]	[2.69]

Notes: Absolute value of t statistics in brackets (absolute values); * significant at 10%; ** significant at 5%; *** significant at 1%

terms, however, suggest a positive overall impact. The marginal effects of the political variables have to be interpreted conditionally on the interaction with globalization (see Friedrich 1982). In principle, there are two sensible ways to evaluate the marginal effects. I follow Dreher and Gassebner (2007), evaluating the marginal effects at the minimum as well as the maximum of the interacted variable, i.e. globalization (Table 2). Using this method we are able to distinguish between the impacts of government ideology on the growth of social expenditures when globalization was proceeding slowly and quickly. If one chooses to evaluate the marginal effects at the average level of globalization, the statistical significance of these average effects corresponds to the t-statistics of the ideology-variable. Thus, regarding the time period 1980 to 2003, there were hardly, if any, partisan political effects at an average level of globalization. In contrast, Table 2 indicates that there were significant marginal effects at either the minimum or maximum level of globalization.

The marginal effects presented in Table 2 can be interpreted as follows: At the minimum level of the overall KOF index of globalization of −3.83 (growth rate, normalized) an increase in the ideology variable by one point—say from 3 (leftwing and rightwing parties in government) to 4 (leftwing government)—decreases the growth rate of social expenditures by about 1.2%. At the maximum level of the overall KOF index of globalization of 4.89 (growth rate, normalized), an increase of the ideology variable by one point increases the growth rate of social expenditures by about 1.7%. Hence, these results indicate that when globalization was proceeding faster, leftwing governments implemented more compensating policies than rightwing governments. In conclusion: One cannot identify partisan effects on social expenditures in the period 1980 to 2003, if one focuses on averages. Thus, if it was not globalization that mitigated the hypothesized partisan effects in this period, there must be other explanations for why party ideology did not matter. A potential reason is differences between sub-periods.

4.2 Different policy periods: the 1980s versus the 1990s

The impact of partisan politics is expected to have changed in the course of globalization. Beginning with Kittel and Obinger (2003), panel regressions were conducted with relatively short samples. This strategy is motivated by the momentous historical events in the 1980–2003 period. In 1990, the "Iron Curtain" fell. Garrett (1998: 1) believes that "… one should be recitent to conclude differently about the 1990s because of the highly idiosyncratic nature of the decade in Europe". The European economies all went into a recession after 1989. In Germany, interest rates increased sharply as a consequence of the German Unification. This put a brake on economic activity throughout the continent—especially in the countries whose currencies were pegged to the Deutsche Mark: Finland and Sweden, for example. In these two countries, unemployment increased dramatically. The 1991 Gulf War added further instability und uncertainty to global markets. Garrett (1998: 133 f.) explicitly encourages the profession to test whether globalization restricted partisan politics in the 1990s: "Even if one were willing to accept my results, it could nonetheless be argued that it was only in the 1990s that globalization finally nailed shut the coffin for leftist alternatives to market liberalism. In time, it will be possible to test this claim…"

I follow this idea and distinguish between two sub-periods: 1980–1990 and 1991–2003.[12] Table 3 reports the regression results, and Table 4 the marginal effects. Tables 3 and 4 indicate that random effects are more appropriate than fixed country effects. Compared to the full sample, 1980–2003, we indeed observe significant differences across time. Leftwing governments increased social expenditures more than rightwing governments in the 1980s. Note that in column (3) of Table 3 the marginal effect of ideology almost reaches statistical significance at conventional levels at an average level of globalization. This evidence for partisan politics in the 1980s is also consistent with previously reported results. Interestingly, however, the overall globalization process did not have a significant impact in the 1980s: the interaction terms of ideology and globalization as well as the marginal effects evaluated at the minimum and the maximum level of globalization are statistically insignificant.

The political economic circumstances changed fundamentally in the 1990s. The regression results in Table 3, columns (4) to (6), demonstrate that, at the average level of globalization, social expenditures did not increase under leftist governments in the 1990s. However, the reported results allow us to conclude that leftwing governments increased spending when globalization deepened significantly. These results corroborate that in the 1990s globalization did not diminish politicians' room for maneuver.

Taking together the results for the sub-periods, one can conclude that, over time, partisan politics became less important, but politicians' options or abilities to maneuver in social policy space were not restricted by the globalization process; globalization-induced policy responses rather depended on political ideology. The estimation results put the results derived for the overall period into perspective. What remains to be done is to relate to the theoretical predictions and to historical events. This is done in the concluding section.

5 Discussion

5.1 Sensitivity to single countries and historical incidents

The reported effects could be magnified or mitigated by idiosyncratic circumstances in the individual countries. I therefore test whether the results are sensitive to the inclusion/exclusion of particular countries. This common sensitivity analysis also highlights the historical background and hence provides further interesting insights.

The results are, in particular, somewhat sensitive to the inclusion of the southern European countries, Greece, Spain and Portugal. In the 1990s, the impact of the ideology variable increases when Portugal is excluded. Moreover, partisan effects at an average level of globalization in the 1980s were driven by Spain, Ireland and the Netherlands. In the 1990s, Greece as well as Portugal strongly affect the results. When Portugal is excluded, the reported effect becomes stronger, leftist governments in Greece intensively extended social

[12] Note that the conclusions also hold when we consider the sub-periods from 1980 to 1989 and from 1990 to 2003.

Table 3 Regression results. Sub samples: 1980–1990, 1991–2003. Dependent variable: Δ ln Social Expenditures. Fixed period effects included

	1980–1990			1991–2003		
	(1)	(2)	(3)	(4)	(5)	(6)
	RE	PCSE	DYN	RE	PCSE	DYN
Ideology (leftwing)	0.005**	0.005*	0.008	-7×10^{-5}	–0.002	0.001
	[2.07]	[1.80]	[1.51]	[0.04]	[0.92]	[0.46]
Δ ln KOF Index	–0.003	–0.003	–0.003	0.002	0.004	0.001
	[0.92]	[1.01]	[0.76]	[0.90]	[1.44]	[0.34]
Ideology* Δ ln KOF Index	-2×10^{-4}	0.001	0.004	0.006**	0.006***	0.005*
	[0.06]	[0.29]	[0.98]	[2.21]	[2.84]	[1.81]
Δ ln GDP (per capita)	–0.710***	–0.739***	–0.577***	–0.753***	–0.647***	–0.818***
	[3.71]	[3.66]	[3.02]	[4.57]	[4.44]	[5.05]
Δ ln Unemployment	0.048**	0.044*	0.067**	0.040**	0.044***	0.027
	[2.15]	[1.74]	[2.28]	[2.09]	[2.67]	[1.33]
Δ ln Dependency Ratio	–0.089	–0.139	–0.258	0.125	0.014	0.282
	[0.24]	[0.46]	[0.62]	[0.71]	[0.06]	[1.03]
Lagged Dependent Variable			0.169*			0.131**
			[1.93]			[2.07]
Constant	0.036***	0.036***		0.044***	0.042***	
	[3.30]	[3.35]		[5.35]	[5.71]	
Observations	200	200	180	255	255	235
Number of *n*	20	20	20	20	20	20
R-squared (overall)	0.34	0.34		0.47	0.45	

Notes: Absolute value of *t* statistics in brackets; * significant at 10%; ** significant at 5%; *** significant at 1%

Table 4 Marginal effects of government ideology (leftwing) at a minimum and maximum level of the overall KOF index of globalization (growth rate, normalized). Sub samples: 1980–1990, 1991–2003

	RE		PCSE		DYN	
1980–1990	min (–1.97)	max (4.21)	min (–1.97)	max (4.21)	min (–1.97)	max (3.96)
	0.005	0.004	0.003	0.008	0.001	0.023
	[0.79]	[0.30]	[0.53]	[0.71]	[0.13]	[1.41]
1991–2003	min (–3.80)	max (4.93)	min (–3.80)	max (4.93)	min (–3.80)	max (4.93)
	–0.021**	0.027**	–0.026***	0.029***	–0.016	0.024*
	[2.27]	[2.12]	[2.99]	[2.62]	[1.63]	[1.87]

Notes: Absolute value of t statistics in brackets; * significant at 10%; ** significant at 5%; *** significant at 1%

expenditures compared to rightwing governments. These findings correspond to political incidents that are well known and it is worthwhile to reflect on those that support the findings of the econometric model.

Greece is a prime example for partisan politics with respect to social policy. At the end of 1981, the Socialist Party (PASOK) won the elections. This change in the political balance of power marked the beginning of the third period of the Greek welfare state. In contrast to its conservative predecessors, the leftist government focused on the development of the welfare state and "accordingly, the increase in social protection expenditure was exceptional" (Katrougalos 1996: 53). The introduction of the National Health Service was one of PASOK's main achievements during their reign in the 1980s. When the conservatives came into power in 1990, they reduced social expenditures as a share of GDP from 18.6% in 1990 to 18.1% in 1992. This trend clearly was reversed when PASOK came back to power in 1993. Globalization was proceeding rapidly in the 1990s and the leftist government increased social expenditures steadily. These incidents are well in line with the changes in the regression results when Greece is excluded.

In Spain, the leftist government implemented a supply-side strategy to foster growth and reduce high unemployment in the beginning of the 1980s. It promoted the transformation of the supply conditions in the Spanish economy and increased the volume and quality of Spain's factors of production. At first, the leftist government enacted a reform of the Social Security system that reduced current benefits and even shifted some contributions to employees (Boix 1998: Chap. 5). But after 1989, the policies of the leftist government changed. Pressure from the unions as well as an attempt to avoid losing more popular support led the leftwing cabinet to increase social transfers (Boix 1998: 137). Thus, social expenditures were used to reach the redistribution goals of the leftist government. In Portugal, however, social expenditures were for a long time below the Southern Europe average. In 1984, the conservative government reorganized social protection and its anti-poverty policies received a boost after Portugal entered the EU in 1986: In the period 1986–1995, social expenditures increased from 11.8% to 18.1% under a rightwing government. The following leftwing government pursued a strategy of social modernization which was criticized by the opposition. However, back in office in 2002, the rightwing government did not decrease social expenditures at all (Capucha et al. 2006).

The following picture thus emerges: In Southern Europe (i.e. in Spain) leftist governments were elected to boost economic activity and equalize social conditions, and the trade liberalization process was accompanied by generous compensating policies (Boix 1998; Adserà and Boix 2002). Moreover, in the 1980s, leftist governments could resist economic globalization successfully by implementing additional policy regulation. Interestingly, Boix (2000: 70) points out that while nonsocialist governments quickly liberalized capital markets, leftist cabinets—"anticipating the constraining effects of dismantling capital controls on their own policy choices retarded the process of financial deregulation. France and Spain abolished capital controls only in the late 1980s. Greece did it in the 1990s". Garrett and Lange (1991: 564) conclude from their analysis that leftwing governments—in alliance with powerful labor movements—have been able to maintain their traditional goals of redistribution, welfarism, and full employment while simultaneously adjusting to the new exigencies of international economic competition. Globalization has also altered the policy instruments that allow governments to pursue their partisan objectives (Garrett and Lange 1991: 541).

Countries such as the United Kingdom, the United States and Germany neither impair nor strengthen the econometric results. At first glance, this might be surprising as the governments led by Margret Thatcher and Ronald Reagan are well known for their free market policies (Thatcherism and Reaganomics). In Britain, Margret Thatcher, Prime Minister in the period from 1979 to 1988, moved the Conservative Party sharply to the right. Ronald Reagan headed a strongly conservative government in the period from 1981 to 1989. After overall public spending had increased in the course of the recession at the beginning of the

1980s, these rightwing governments eventually curbed social transfers, cut public spending on capital formation and reduced industrial subsidies. However, spending for social affairs was not reduced. "Strict electoral calculations partially explain the Conservatives' conscious rejection of any substantial reduction in core welfare programs to achieve their overall goal of lower public expenditure. Popular support for the welfare state was just too strong" (Boix 1998: 192). The conservative Christian democrats in Germany came into power in October 1982 and followed rather restrictive fiscal policies in the 1980s but did not cut social expenditures such as on old age pensions. If we thus observe that leftwing governments spent more on welfare in the 1980s than rightwing governments did, this does not imply that rightwing governments reduced social expenditures; it implies that leftwing governments increased social expenditures more than rightwing governments.

The behavior of leftist government appears to have changed in from the 1980s to the 1990s. Leftist parties appear to have moved to the right in their rhetoric and policies (Ross 2000). A famous example is the joint statement by Tony Blair and Gerhard Schröder entitled 'Europe: The Third Way/Die Neue Mitte' (see e.g. Blyth and Katz 2005: 47). In the United States, the 1980s were an electoral disaster for the Democrats, and as a consequence they moved to the right. Overall, the historical background helps to explain why, on average, there were more expansionary social policies under leftist governments in the OECD countries in the 1980s, but no partisan effects in the 1990s. Globalization, however, did not reduce the room for maneuver in social policy affairs. Moreover, the empirical results suggest that leftist governments provided more compensatory social policies to combat inequality and insecurity when globalization was proceeding at a fast pace.

5.2 Party movements and globalization

Parties change over time, and they do so irrespective of globalization. This phenomenon transpires from historical development and, moreover, it is explained at length in the theoretical political science literature. The most visible changes are a decline in party polarization and a reduction in electoral cohesion. The constituencies of the political parties became less polarized over time and class voting has declined since the end of the 1970s (see e.g. Mair 2008: 218 ff.). The diminishing of electoral cohesion led the parties to propose less client-targeted policy alternatives. Mair (2008: 215) stresses that in the mid 1970s politics did not only reflect a marked degree of polarization and conflict, but it also see-sawed dramatically in terms of policy, with each new incumbent government seeking to undo the policies that had been promoted by its predecessor. However, so far, empirical studies do not take into account the fact that parties have undergone these changes which can only be captured by a dynamic index of voter polarization. See, for example, Potrafke (2008).

Globalization is likely to contribute to these changes in the nature of parties. Blyth and Katz (2005: 41) argue, for example, that globalization is associated with the progressive disembedding of market transactions from regulation; the role of the state—and thus of political parties—has therefore diminished. Moreover, parties' constituencies change in the course of globalization. "Employees in different firms and industries share more interests with owners and managers—because of their common position in the international division of labor—than they do with their nominal class allies" (Garrett 1998: 40). However, the impact of globalization on party transformations is different from globalization-induced changes in policies. In my econometric model, the included government ideology variable is static and does not control for party changes. It is possible that globalization has shifted party positions, for example, leftist parties may have moved more to the centre. But this does not change the relative positions of the parties on a left-right scale, and neither does the likely impact of globalization on government ideology. That is why these endogenous changes in party behavior are not likely to cause any problems with the chosen econometric specification and the question tackled in this paper. However, there is definitely need for further research dealing with the question how globalization affects government ideology and intraparty competition. Potential feedback effects of social expenditures on government ideology also need to be acknowledged, because politicians are election motivated and know that higher social expenditures could attract votes.

5.3 Further robustness checks

Globalization is a multifaceted concept, and it is the merit of the overall KOF index of globalization to capture many of its aspects. There are three subcategories of the KOF index of globalization, measuring economic, political, and social globalization. In an attempt to test the robustness of my results, I estimated all regressions with these sub-indices instead of the overall index. The results show that leftist governments provided more compensatory policies in response to economic and social globalization than in response to political globalization.

The reported partisan effects could be even weaker and mitigated by national-specific veto-points. The room for maneuver by national central governments depends on the level of checks and balances (e.g. Schmidt 1996: 169 ff.). The indicators of Schmidt (1996 and 2008) and Huber et al. (1993) shed light on deep-seated institutional differences in constraints on central state governments. However, these indicators are nearly time invariant and, thus, they can hardly help to explain the declining partisan effects over time. Anyhow, I nevertheless included these indices in the regressions to address the potential problem of mitigated partisan politics due to institutional constraints. Statistically, these indicators are insignificant and therefore suggest that institutional veto points do not affect the reported partisan effects.

5.4 Suggestions for future research

Some scholars argue that globalization should not be measured, but estimated using spatial lags of policies in neighboring countries. Franzese and Hays (2007: 141), for example, point out that: "Globalization, i.e. international economic integration, implies strategic and non-strategic interdependence across domestic politics and policies. Spatial interdependence is substantively central to the very concept of integration in general and to the fears and hopes surrounding globalization in particular". Analyzing the interaction of globalization via spatial units and political variables in a panel data model addresses an interesting topic, but it also requires addressing a number of challenges. It would have to tackle issues such as the inclusion of fixed and random effects as well as coefficients respectively, the inclusion of dynamic effects, and estimation via the maximum likelihood procedure or instrumental variables and so on. This literature is still developing (see e.g. Franzese and Hays 2007; Plümper and Neumayer 2008 and Elhorst 2009). Furthermore, the spatial lag should be interacted with the political variables—which results in further complications. So far, there are only a few empirical studies (e.g. Schaltegger and Küttel 2002; Solé-Ollé 2003) that use interactions of spatial lags and political variables. Elhorst and Fréret (2009) provide a new contribution to this literature using a two-regime spatial panel data model. The evaluation of the interaction of spatial units and government ideology will likely prove to become a hot topic in the future.

A final issue concerns the composition of welfare expenditures. Some governments might, for example, decrease spending for health, but simultaneously increase spending for old age pensions or vice versa. Therefore, I cannot conclude from the current analysis that partisan politics did not significantly affect any expenditure category. Examining the budget composition of overall public expenditure has enjoyed tremendous popularity in the recent empirical literature (e.g. Dreher et al. 2008a; Gemmell et al. 2008; Sanz and Velázquez 2007; Shelton 2007). In these studies, welfare effort is measured as one of the ten classifications of functions of government (COFOG). Issues of budget composition also apply to subcategories. Decomposing social expenditures focusing on health, social security, labor, family benefits and so on, in order to elucidate potential compensating effects would certainly be a worthwhile endeavor.

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Appendix

Table 5 Descriptive statistics and data sources

Variable	Obs	Mean	Std. Dev	Min	Max	Source
Public Social Expenditures (as a share of GDP)	480	20.50	5.17	10.32	36.17	OECD SOCX Database (2007)
Ideology	480	2.89	0.90	1	4	Own Calculation
KOF Index of (overall) Globalization	480	72.78	12.23	42.77	93.21	KOF—Swiss Economic Institute, Dreher (2006b)
GDP (real terms, per capita, local currencies)	480	212655.3	753087.1	6797.20	4013596	Worldbank (2007)
Unemployment Rate	475	7.70	4.17	0.2	23.9	OECD Health Data Base (2007)
Dependency Ratio	479	50.14	4.43	42.5	70	OECD Health Data Base (2007)

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