

# **Crafting Sustainable Social Contracts in Latin America: Political Economy, Public Attitudes, and Social Policy\***

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## **Abstract**

This paper focuses on the need to develop social contracts as a means to address the challenge posed by widespread insecurity and extensive inequality. Even the winners in the best performing countries in the region are vulnerable to negative shocks, such as those related to volatility in international capital markets. In the advanced economies, permanent safety nets and social insurance systems are part of a fiscally and politically sustainable social contract. Ultimately, developing social contracts and sustainable welfare systems - no matter how limited - will be integral to the region's economies becoming competitive and stable participants in the global economy. The paper highlights the importance of public attitudes - about the causes of poverty, about the distribution of opportunities, and about redistribution, among others - in crafting such contracts. It provides an analysis of Latin American public attitudes compared to those in the United States.

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## **Crafting Sustainable Social Contracts in Latin America**

After almost two decades of extensive macroeconomic and structural reforms, which in some countries included the targeting of public expenditures to the poorest sectors, Latin America as a region has made tremendous strides in achieving sounder macroeconomic fundamentals. Most observers agree that without this progress, the poor of the region would have fared much worse. They were the least able to protect themselves from high levels of inflation and other kinds of macroeconomic volatility, and from the erosion of public expenditures that accompanied the deteriorating economic conditions of the 1980's.

Yet there is still a great deal of debate about the effects of the reforms on poverty and inequality. One reason for this is that the effects of the reforms have been two-fold. On the one hand, the market reforms and trade liberalization undertaken by the countries in the region create extensive new opportunities in these economies – particularly for the poor.<sup>1</sup> Yet they also create new vulnerabilities - especially for those that are in the near poor or middle strata.

My recent research with Stefano Pettinato finds that the most negative perceptions about globalization and market policies are found in this latter group rather than among the poor of the region.<sup>2</sup> These negative perceptions are prevalent even among individuals that are doing well in objective economic terms. Among other plausible explanations for these negative perceptions, three are particularly compelling: concerns about insecurity given the absence of adequate safety nets and social insurance; changing rewards to different skill and education levels; and inequality driven by trends at the top, e.g. large gaps between the very wealthy and the rest of the population.

This paper focuses on the need to develop a social contract in most countries in the region as a means to address the challenge posed by widespread insecurity and extensive inequality. Even the winners – those individuals that exit poverty and have upward income mobility - in the best performing developing countries are vulnerable to negative shocks, such as those related to volatility in international capital markets. Yet most developing economies lack any kind of unemployment insurance or other formal safety net for individuals to fall back on.

In the advanced economies, permanent safety nets and social insurance systems are part and parcel of a fiscally and politically sustainable social contract. This is quite distinct from the short-term, externally financed safety net programs that are implemented during crisis periods in many developing economies. Ultimately, developing social contracts and sustainable welfare systems - no matter how limited - will be integral to the region's economies becoming competitive and stable participants in the global economy, as well as to ensuring that a broader

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<sup>1</sup> For a summary of the effects of the reforms in the region, see, among others, Nancy Birdsall and Carol Graham, *New Markets, New Opportunities: Economic and Social Mobility in a Changing World* (Washington, D.C.: The Brookings Institution Press and the Carnegie Endowment, 2000); and *Latin America After a Decade of Reforms* (Washington, D.C.: Inter-American Development Bank, 1997).

<sup>2</sup> See Carol Graham and Stefano Pettinato, *Happiness and Hardship: Opportunity and Insecurity in New Market Economies* (Washington, D.C.: The Brookings Institution Press, 2002).

base of the region's population benefits from the potential gains from market reforms and international economic integration.

More broadly, social contracts – which include the middle class as well as the poor – are critical underpinnings of both markets and democracies in most developed economies. A similar development is necessary for Latin American countries to become competitive participants in the global economy over the long term. Without such social contracts, it will be difficult to maintain sustained and broad-based public support for markets and democracy in the region.<sup>3</sup>

Survey data show that the absence of adequate social insurance is one of the principle causes of public frustration with market policies, and with globalization more generally, in many of these countries.<sup>4</sup> While this absence has always been a public concern, a succession of crises in some of the “best” performing emerging market economies - Mexico in 1995, the Asian countries in 1997, Brazil in 1998, and Argentina in 2001 – have highlighted the extent to which a wide range of countries can face periodic crises and/or external shocks, and that at these times even those citizens who have fared very well under market policies can suffer very large downturns.

In the 1980's and 1990's, market reformers focused on getting the macroeconomic fundamentals right, and on narrowing the scope and increasing the efficiency of public expenditures. This included a major effort to target public social expenditure to the poorest groups, an effort which was very effective at protecting the poor during crisis and adjustment in many countries.<sup>5</sup> Yet the new focus on the poor was often accompanied by a reduction in the quality and quantity of services available to those in the middle of the income strata (the wealthy in Latin America rarely rely on public social services). At a time when governments were stabilizing high and hyper levels of inflation and reversing years of negative economic growth, the focus on the poorest made economic and political sense, and in many cases resulted in the poor benefiting substantially from public social expenditures for the first time.

By the late 1990's, however, as the collective memory of hyper-inflation and other pre-reform conditions faded, politics “as usual” began to re-surface throughout the region. In addition, it became increasingly clear that there were losers as well as winners with the turn to the market, and the losers tended to be in the middle of the income spectrum rather than among the poor. While many individuals moved out of poverty and up the economic ladder with the turn to the market, others – many of whom had previously led fairly stable “middle class” lives - fell to near or below poverty levels. The vulnerability of this latter group was heightened by the successive

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<sup>3</sup> Research in the advanced industrial economies finds that public support for free trade is stronger in those countries where there are sufficient safety nets for displaced workers. See Robert Bates, Philip Brock, and Jill Tiefenthaler, “Risk and Trade Regimes: Another Exploration,” *International Organization* 45, 1 (Winter 1991).; Lori Kletzer and Robert Litan, “A Prescription to Relieve Worker Anxiety”, *Brookings Policy Brief*, # 73, March 2001; and Kevin Scheve and Matthew Slaughter, *Globalization and the Perceptions of American Workers* (Washington, D.C.: Institute for International Economics, 2001).

<sup>4</sup> See Graham and Pettinato (2002).

<sup>5</sup> For a discussion of experiences protecting the poor across countries and regions, see Carol Graham, *Safety Nets, Politics, and the Poor: Transitions to Market Economies* (Washington, D.C.: The Brookings Institution, 1994). For an excellent discussion of the extent to which social expenditures in the region have been targeted to the poorest sectors, see Tarsicio Castañeda, “Tendencias de Largo Plazo en Tamaño, Eficiencia, y Focalizacion del Gasto Social en America Latina y el Caribe”, Paper prepared for the Inter-American Development Bank, February 2002.

crises in a number of countries, crises which had spillover effects well beyond their respective national borders.

Not surprisingly, these trends have affected public perceptions about markets and democracy in the region. Observers increasingly warn of “reform fatigue” and of the potential for a public backlash against globalization more generally. The extent of these sentiments may be exaggerated by the popular press. Yet there certainly is some public questioning of the results of both market reforms and democracy, as is evident from a number of public opinion polls in most countries in the region, and, more recently and vividly, by protests in the streets of Argentina.<sup>6</sup>

My own research with Stefano Pettinato, which compares public perceptions with objective economic conditions in Latin America and Russia, also raises some concern about public support for market policies in the region. We find that the most upwardly mobile respondents (the “winners”) are frequently more negative than the “losers” as they assess their economic progress over the past ten years. The frustrated achievers – those with upward mobility but negative perceptions – tend to be in the middle and lower middle of the income spectrum, rather than at the bottom. The frustrated achievers are also, on average, less supportive of democracy and of market policies.<sup>7</sup>

There is probably some percentage of every population that is negative regardless of objective trends. Yet it is quite likely that these negative attitudes also stem from trends that can be influenced by policy, such as insecurity, changing rewards to skill and education, and relative income differences. This paper highlights the need for domestically crafted social contracts to address these issues.

The paper begins with the assumption that the region needs more extensive safety nets and social insurance systems, yet that for these systems to be sustainable, choices about the appropriate policies must be made – and financed – domestically. This suggests a major paradigm shift, which changes the focus from external to internal actors. This does not discount the important value added contributed by external donors and multilateral banks in the social welfare and social protection arena; rather it emphasizes the need for domestic choices about policies and the allocation of scarce public resources.

Short-term safety nets are of critical importance at particular times. But because developing countries can often finance temporary programs with support from external funds, particularly at times of crisis, they usually do not require the kinds of political economy choices that are necessary for longer term programs.<sup>8</sup> The establishment of permanent social assistance and social insurance systems ultimately requires the development of a politically sustainable social contract, and therefore fundamental public choices about the allocation of scarce resources. In addition, it is increasingly clear that even model economic reformers are vulnerable to volatility driven by fluctuations in international trade and capital flows, and that countries need to have

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<sup>6</sup> Support for democracy and for a number of market reforms such as privatization, for example, fell slightly from 1995-2001 according to the only region-wide opinion poll, the Latinobarometro, as reported by the *Economist* in July 2001. The author’s own tabulations using the same data support this general conclusion.

<sup>7</sup> See Graham and Pettinato (2002).

<sup>8</sup> This, of course, applies to democratic governments. Authoritarian regimes are less likely to get external support but also less likely to face the same political economy constraints.

permanent safety net systems in place that can expand and contract as necessary to provide social protection during periodic downturns.<sup>9</sup>

The design of social welfare systems must take into account cross country differences in public attitudes – as well as economic and fiscal constraints. This paper is a first step towards analyzing the objective conditions and public choices that are necessary for the development of broader and more effective social contracts in the Latin American economies. As a first step, it draws from the experience of the OECD countries and the United States in establishing social contracts and sustainable social welfare systems.

Developing sustainable social contracts will entail societies' making fundamental choices about the allocation of scarce public resources, choices that will have to be made within the constraints (or opportunities) posed by the need to remain competitive in the global economy. In other words, what is desirable and what is feasible may be quite distinct, and the parameters will be set by fiscal constraints and by the need to compete in a global economic climate that rewards lean and efficient public sectors and relatively inexpensive labor costs.

This inevitably raises questions about how extensive the social contract should be and who should benefit most from it. This project starts from the assumption that the participation of a sufficiently large and thriving middle class was key to the advance of democracy and to the development of social contracts in the advanced industrial economies, and that it is also likely to be key to sustained growth in the developing economies. Thus public policy must pay attention to the needs of the middle strata, in addition to those of the poor. There will also be additional choices about the appropriate balance of expenditures on investments in the human capital of younger generations versus on protecting the poor and vulnerable, many but not all of whom are in older generations.<sup>10</sup>

Another set of questions concerns the changing distribution of income within countries. Many developing economies – and particularly those in Latin America – have much higher levels of inequality than is typical for even the most unequal advanced economies. The same economies rely on flat or even regressive forms of taxation – such as the VAT – to generate fiscal revenues. Addressing the issue of income inequality – and the extent to which redistribution is feasible and desirable – will be an integral part of crafting sustainable social contracts in these countries. The paper's focus on political economy and public attitudes will provide some initial parameters for thinking about redistribution as part and parcel of the discussion of social contracts.

### Political Economy and Public Attitudes

Framing the discussion of social contracts in concrete policy terms is difficult in that it entails understanding of diverse countries' political cultures and attitudes about social justice and

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<sup>9</sup> I provide a number of detailed reasons why more permanent systems are necessary in "Stemming the Backlash Against Globalization, *Brookings Policy Brief*, No. 78, April 2001. See also Nora Lustig, ed., *Shielding the Poor: Social Protection in the Developing World* (Washington: D.C.: The Brookings Institution Press and the Inter-American Development Bank, 2000).

<sup>10</sup> Older workers, for example, are less likely to have the skills or the capacity to retrain to benefit from the high technology, high growth sectors of the economy, while only a fraction of retirees in the region are covered by social security.

redistribution, in addition to taking their macroeconomic and public institutional framework into account. Publics differ widely across countries in their views about the government's role in the provision of public services and about the extent to which there is a collective responsibility for individuals who are unable to provide for themselves.<sup>11</sup> There are also persistent differences in attitudes about how opportunities are distributed, and the government's role in equalizing both opportunities and outcomes.<sup>12</sup> These differences in attitudes, meanwhile, often develop into persistent patterns of political and economic behavior, and are of particular importance to the degree of political support that can be generated for redistribution or other forms of public assistance.

While these are broad and philosophical issues, they have important effects on the political economy of social welfare and other social policies. Little wonder that policymakers do not have a clear recipe for dealing with them. Yet they make a difference in whether or not particular policies are politically feasible and sustainable, for example in decisions about targeted versus universal approaches, permanent versus temporary programs, and the balance between investments in education and human capital and assistance to displaced workers or the elderly.

This paper will propose a framework for incorporating public attitudes about social welfare into policy debates and choices. An underlying premise is that understanding such public attitudes will facilitate policymakers' ability to assess, frame, and navigate their respective political economy contexts as they attempt to craft social policies that are part of a fiscally sustainable social contract.

There are, without a doubt, other factors that influence the political economy of social policies, including the public institutional framework and the structure and balance of power of political institutions, among others. These are, no doubt, as important as attitudes in determining policy outcomes. This paper proposes using public attitudes as a framework for analysis, which then must take these and other factors – such as fiscal constraints – into account. While some previous political economy analysis has focused on the role of public attitudes in shaping social welfare policies, this analysis has been limited to the advanced industrial economies. To date, such an approach has not been taken in the analysis of developing economies. The paper is thus an attempt to go beyond the usual parameters in thinking about social policies, and thus whatever contributions it makes are also tempered by the risks that come from operating in unknown territory.

The paper posits that differences in political attitudes about redistribution - and equality of opportunity versus equality of outcomes - affect the design of social welfare structures, and that in turn yields insights into what social policies are likely to be successful and politically sustainable in a particular context. It then discusses how different contexts in Latin America have resulted in very different public expenditure outcomes. The second half of the paper discusses

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<sup>11</sup> I explore this in detail in *Private Markets for Public Goods: Raising the Stakes in Economic Reform* (Brookings, 1998).

<sup>12</sup> For a detailed discussion of government policy towards opportunity versus outcomes, see the introductory chapter in Nancy Birdsall and Carol Graham, *New Markets, New Opportunities? Economic and Social Mobility in a Changing World* (Brookings and Carnegie, 2000). For the effects of these attitudes on patterns of political behavior, see Chapter 1 in Carol Graham and Stefano Pettinato, *Happiness and Hardship: Opportunity and Insecurity in New Market Economies* (Brookings, forthcoming).

the instruments available to policymakers for evaluating their own political context; provides a set of themes around which program design choices can be framed; and suggests some strategies for navigating diverse political contexts in individual countries, based on lessons from experience.

### **Do Public Attitudes Matter for Social Assistance? A Cross Country Perspective**

Differences in public attitudes among advanced industrial economies are reflected in the structure of their social welfare systems. Americans, Japanese, and Australians, for example, spend much lower proportions of their gross national product on social welfare than do their European counterparts in the OECD. [Figure 1] Expenditure patterns in Japan (and other Asian countries) reflect a stronger reliance on the family as a safety net.<sup>13</sup> The lower levels of welfare expenditure in the United States reflect American's long held attitudes about individual responsibility and opportunities for upward mobility which contrast to European's beliefs about society's collective responsibility for those individuals that fall behind.

These contrasts result in a higher tolerance for inequality among Americans than Europeans, as well as a much more extensive social welfare system in the latter. While these are generalizations that obviously do not apply to all individuals, they have been well documented in numerous public opinion surveys, and have been noted since the writings of deTocqueville.<sup>14</sup> One of the most recent papers along these lines is by Alberto Alesina, Rafael di Tella, and Robert MacCulloch, who find that, holding other variables constant, inequality has significant and negative effects on the subjective well being of all income groups in a selection of European countries, and particularly strong effects for the poor, which is what one would expect. In contrast, in the United States, the only group that is made less "happy" by inequality is left-leaning wealthy people.<sup>15</sup>

We based our analysis on data from the U.S. General Social Survey (GSS). The cumulative database of the GSS covers 30,000 individuals for the years 1972-93.<sup>16</sup> Controlling for the usual socio-demographic variables (age, gender, race, and marital and employment status) as well as

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<sup>13</sup> Indeed, these attitudes are so strong that in the aftermath of the Asia crisis, one of the constraints cited to broader international financial institution support for safety nets was local resistance to the expansion of public support and fears of erosion of the family-based system. See Nancy Birdsall and Stephan Haggard, *After the Crisis: The Social Contract and the Middle Class in East Asia* (Washington, D.C.: The Carnegie Endowment for International Peace, 2000).

<sup>14</sup> See, for example, Alexis deToqueville, *Democracy in America* (New York: Anchor Press, 1969); for a more recent discussion of actual trends as well as U.S. attitudes about individual mobility, see Daniel McMurrer and Isabel Sawhill, *Getting Ahead: Economic and Social Mobility in America* (Washington, D.C.: Urban Institute Press, 1998).

<sup>15</sup> Alesina, diTella, and MaCulloch, "Inequality and Happiness: Are Europeans and Americans Different?", Mimeo, Harvard University, (2000).

<sup>16</sup> The GSS is not a panel, and therefore does not cover the same individuals over time. It is the same data set that is used by Oswald and colleagues to analyze happiness in the U.S. Because income was only surveyed for part of the sample for each year, we could only examine the effects of income on various dependent variables for specific segments of the sample at a time.

income and education, we find that individuals who favor redistribution in the United States are, on average, less happy or satisfied with their lives than those who do not. [Table 1] <sup>17</sup>

Perhaps what is most remarkable about these attitudes is their persistence, despite a fair amount of evidence suggesting that actual mobility rates in the United States and Europe are not that different.<sup>18</sup> Public perceptions in the United States reflect a belief in high prospects for upward mobility. Recent work on voting by Roland Benabou and Efe Ok, for example, finds that even though the majority of Americans are well below mean income, many of them choose not to vote for redistribution because they believe that they will be above it in the future. They support their theoretical work with empirical data from the PSID.<sup>19</sup> Supporting the general direction of these findings, Alberto Alesina and Eliana La Ferrara find that those who believe that American society offers equal opportunities to all oppose redistribution, while those that believe that the mobility process is biased support redistribution.<sup>20</sup>

Given the relatively high levels of American income inequality and that a majority of the population is below mean income, a surprisingly small proportion of Americans support redistribution. Forty percent of respondents in the GSS agree that the government should reduce inequalities, while 33% disagree and 20% are neutral. Thomas Piketty shows theoretically how past mobility experiences influence political attitudes.<sup>21</sup> Giacomo Corneo and Hans Peter Gruner test his theory using empirical evidence for the U.S. and Europe, and find that those individuals that have had upward inter-generational mobility tend to oppose government redistribution of income.<sup>22</sup>

They also find that cross-country differences in attitudes about redistribution are explained by what they call “social rivalry effects” and “public values effects”, in addition to standard individual pecuniary motives. The first has to do with how individuals in a particular society view themselves relative to others in their neighborhood, and therefore whether they will benefit from redistribution. The second has to do with individual perceptions of how fairly opportunities are distributed in society. Those that think that non-work related characteristics such as family background matter are more likely to support redistribution. Again, American attitudes about fairness of opportunity seem to distinguish the U.S. from the European countries in the study.

Americans also express more limited support for government responsibility for social welfare: lower percentages of Americans see jobs, health care, the elderly, and housing as essential

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<sup>17</sup> The question on the redistribution variable – EQWLTH – asks whether respondents agree that the government should reduce income differences, with possible answers on a seven point scale. The lowest score on the scale is opposition to redistribution and the highest score is support for it. The question about redistribution of wealth is asked in most but not all of the survey years.

<sup>18</sup> McMurrer and Sawhill (1998); Robert Erikson and John H. Goldthorpe, “Are American Rates of Social Mobility Exceptionally High? New Evidence on an Old Issue”, *European Sociological Review*, Vol.1, No.1, 1985.

<sup>19</sup> Roland Benabou and Efe Ok, “Social Mobility and the Demand for Redistribution: The POUM Hypothesis”, NBER Working Paper No.6795, 1998.

<sup>20</sup> Alberto Alesina and Eliana LeFerrara, “Preferences for Redistribution in the Land of Opportunities”, Mimeo, Harvard University, July 2000.

<sup>21</sup> Thomas Piketty, “Social Mobility and Redistributive Politics”, *Quarterly Journal of Economics*, Vol.110 (1995), pp.551-585.

<sup>22</sup> Giacomo Corneo and Hans Peter Gruner, “Individual Preferences for Political Redistribution”, Mimeo, University of Osnabruck, Munich, 2000.



government responsibilities than do Europeans.<sup>23</sup> [Table 2] A recent survey of European attitudes, meanwhile, finds that the majority are content with their social welfare systems as they are – and do not want them altered, even in instances where respondents say they know that their pension systems are headed for insolvency.<sup>24</sup>

There is also clear evidence that public attitudes in turn shape American welfare policy. An influential study by Benjamin Page and Robert Shapiro found that over a forty-five year period, changes in public opinion often preceded changes in government policy across a whole range of substantive issues. Of course it is also possible that policy changes can shape public attitudes, but this seems to occur less often and in less notable a manner.<sup>25</sup> A brief look at trends in U.S. welfare policy highlights the role of public attitudes in influencing policy.

The U.S. welfare system was set up quite late compared to most European systems. Pensions were only introduced in with the New Deal, and health insurance for government employees in the 1960's. Today, more than one in seven Americans – or 42 million people – lack health care insurance.<sup>26</sup> In contrast, the first social security system in Europe dates back to the era of Bismarck in Germany, and national health systems were in place in many countries by the first half of the 20<sup>th</sup> century.

In the United States, after the New Deal establishment of social security and public works employment, as a response to the Great Depression, the next sustained expansion of welfare policy occurred in the 1960's, with President Johnson's war on poverty. A major departure at this juncture was aid to families with dependent children (AFDC), which was the first national scale effort to provide assistance for the *non-working* poor. By the early 1990's (prior to the 1996 reform) AFDC accounted for 9.4% of all welfare expenditures, with over 12 million people on the rolls, a number which had continued to expand despite the sustained economic growth of the 1990's.<sup>27</sup> Questions about the effectiveness of the welfare system began to increase, even among analysts sympathetic to its objectives and the poor.

There were several failed attempts at welfare reform in the 1980's – in part due to the complicated politics of welfare reform in almost all countries. By the mid-1990's, however, President Clinton, a Democrat who came into office promising to “end welfare as we know it”, was able to pass a major welfare reform law.

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<sup>23</sup> Gilens (1999), p.25.

<sup>24</sup> Tito Boeri, Axel Borsh-Supan, and Guido Tabellini, “Welfare State Reform: A Survey of What Europeans Want”, *Economic Policy*, Vol.x, No.X, 2001.

<sup>25</sup> Page and Shapiro study, cited in Gilens (1999), p.25. Other studies come to the same conclusion, based on differences between state-based programs. These studies find that, controlling for differences in income, education, and urbanization, state policies across a range of issues reflect differences in attitudes (on a liberal to conservative scale) across states. See Gilens, p.25.

<sup>26</sup> The 42 million figure is for individuals that lacked health care coverage in ALL 12 months of 1999. See Gary Burtless and Sarah Siegel, “Medical Spending, Health Insurance, and the Measurement of American Poverty”, *CSED Working Paper Series No.22*, The Brookings Institution, June 2001.

<sup>27</sup> Mark Murray, Marilyn Werber Serafini, and Megan Twohey, “Untested Safety Net”, *National Journal*, March 10, 2001 for the roll numbers. Budget figures are from the Congressional Budget Office's *Economic and Budget Outlook*, 1995 and 2000. The percentage figures translate into \$18 billion out of a budget of \$191 billion for 1995.

While the details of the reform law are well beyond the scope of this paper, its major underpinning features are important to the discussion.<sup>28</sup> First of all, the reform hinged on the objective of ending long-term dependency and getting welfare recipients back into the work force. For the first time, time-limits of five years were imposed on welfare recipients, and AFDC became TANF – temporary assistance to needy families.<sup>29</sup> At the same time, most states made efforts to make work pay.<sup>30</sup> Second, the law gave a great deal more freedom to the states for designing and implementing welfare programs, who received block grants – albeit to be spent according to federally set guidelines - from the federal government.

A remarkable number of observers – including those who were initially strongly critical of the reform – note that the reform has been remarkably successful thus far, cutting welfare rolls by a half by 2000.<sup>31</sup> Even supporters of the reform, however, caution that some of this progress is due to the unprecedented expansion of the US economy, and that in the event of a serious recession, many of the low-skilled jobs held by post-welfare recipients will be the first to be cut.<sup>32</sup>

The most important distinction that seems to underlie both the logic of the 1996 welfare reform and that of American attitudes about welfare more generally, is that between the *deserving* (working and/or disabled, elderly, or children) and *non-deserving* (able-bodied non-working) poor. This distinction has resulted in a tension between two objectives: that of getting welfare recipients back to work and that of improving the lives of poor families and children.<sup>33</sup> It is clear that there are tradeoffs, for example, when single mothers of small children must struggle to find sub-optimal child care arrangements so that they can work at jobs that provide marginally more income than their welfare payments did. On the other hand, there is a fair amount of evidence that the pre-reform system encouraged dependence and at least implicitly rewarded out-of-wedlock child-rearing.

Regardless of what position one takes on the issue of deserving versus non-deserving poor, it is very clear that American public opinion in general is much more in favor of providing welfare support to the former than to the latter, and that Americans of all income levels – including the poor (defined as those with incomes below 200% of the official poverty line) - question the effectiveness of welfare. For example, a recent NPR/Kaiser/Kennedy School survey finds no statistically significant difference between the poor and the rest of society when answering

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<sup>28</sup> For an excellent description of the 1996 welfare reform, see the Spring 2001 issue of the *Brookings Review*, guest-edited by Isabel Sawhill.

<sup>29</sup> States could exempt up to 20% of recipients from these limits.

<sup>30</sup> An additional (and federal) effort to make work pay was the expansion of the Earned Income Tax Credit (EITC).

<sup>31</sup> During that period, 6.5 million people moved off welfare. Murray et al (2001); and author's attendance at the Children's Roundtable, a semi-annual discussion of experts on welfare issues that pertain to children, The Brookings Institution, Washington, D.C., May 25, 2001. Budget figures have not changed that much, meanwhile, as most spending takes the form of block grants to states. Thus TANF and other "family support" now composes 8.9% of means tested entitlements, or \$21 billion out of a \$236 billion budget. Figures are again from CBO.

<sup>32</sup> The evidence of the effects of the reform on children of single working parents who have had to go to work or risk losing their benefits is mixed to date. Part of the problem is that it is too early to fully evaluate the effects. But the few studies that do exist find no evidence of any marked deterioration, and in some instances there have been improvements in school performance for some age groups. See Pamela A. Morris, Aletha C. Huston, Greg J. Duncan, Danielle A. Crosby, and Johannes M. Bos, *How Welfare and Work Policies Affect Children: A Synthesis of Research*. New York: Manpower Demonstration Research Corporation, 2000.

<sup>33</sup> See the discussion by Isabel Sawhill in the Spring 2001 *Brookings Review*.

questions about the relationship between the welfare system and poverty: 47% of non-poor respondents and 45% of poor respondents say that the welfare system is a major cause of poverty.<sup>34</sup>

More generally, Americans are divided over the causes of poverty. Roughly half of those polled by the NPR/Kaiser/Kennedy School survey said that the poor are not doing enough to get themselves out of poverty and the other half said that circumstances beyond their control cause them to be poor. And, rather surprisingly, low income Americans (those making less than 200% of the official poverty level or \$34,000 per year for a family of four) are only slightly more likely to feel it is due to circumstances.<sup>35</sup>

Our own analysis is based on two questions in the GSS about the causes of poverty, which were asked of 1330 respondents in 1990 only. We found that blacks, low-income respondents, and those that place themselves on the liberal (left) side of the political spectrum are more likely to say that poverty is due to lack of jobs. In contrast, only less educated respondents and those that place themselves on the conservative (right) side of the political spectrum say that poverty is due to lack of effort, while income level has no significant effects. (Table 3a/b)

A comprehensive analysis of American opinions about welfare by Martin Gilens finds that Americans are more concerned about helping the poor become self-sufficient than they are about saving taxpayer dollars.<sup>36</sup> While support for welfare in general varies slightly by income group, support for means-tested programs does not. Most people do not think welfare benefits are too high. Yet many think that the rolls are filled with undeserving respondents.<sup>37</sup>

The distinction between deserving and non-deserving poor may be a more important determinant of public support for welfare in the United States than is that between targeted and universal programs, which has received much more attention, at least in the academic literature. This latter issue has caused a great deal of debate, with scholars such as Theda Skocpol making the very effective argument that unless programs are universal – or at least benefit the middle class as well as the poor – they will not be politically sustainable. She cites the growth – and seeming sacrosanct nature – of programs such as social security and medicare, and contrasts that with the cuts to targeted welfare programs. Others, such as Robert Greenstein, say that Americans will support targeted programs if they are deemed to be effective and targeted at a politically salient group, such as children, and cites the Head Start program as an example.<sup>38</sup>

There is a great deal of merit to both of these arguments, and they apply across countries and political cultures. The relative importance of either given a particular context depends in part on public views about redistribution. A related issue is the proximity between the middle class and

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<sup>34</sup> NPR/Kaiser Family Foundation/Kennedy School Poll on Poverty in America, John F. Kennedy School of Government, Harvard University, 2001. This was a nation-wide telephone survey, based on a random representative sample of 1,952 respondents 18 years of age and older.

<sup>35</sup> NPR/Kaiser/Kennedy School Poll on Poverty in America.

<sup>36</sup> Martin Gilens, *Why Americans Hate Welfare* (Chicago: University of Chicago Press, 1999).

<sup>37</sup> Gilens (1999), p.57.

<sup>38</sup> For an excellent summary of this debate, see Theda Skocpol, “Universal Appeal: Politically Viable Policies to Combat Poverty”, *The Brookings Review*, Vol.9, Summer 1991, pp.28-33; and Robert Greenstein, “Relieving Poverty: An Alternative View”, pp.34-35 in the same edition.

the poor. In theory, greater proximity and /or similarity between the middle class and the poor should translate into broader political support for redistribution in favor of the poor. This is a particularly important issue when thinking about social contracts more broadly.

Joan Nelson's work on developing economies suggests that social policies and social welfare policies which have the support of the politically relevant middle strata, as well as the poor when they have overlapping interests, are more likely to be sustainable.<sup>39</sup> Peter Lindert finds that differences among industrial countries' political tendencies to spend on social transfers are largely explained by income skewness: the size of the gap between the rich and the middle versus that between the middle and the poor. A wider lower gap means less affinity of the middle class for the poor, and therefore less social spending. The U.S., which has a large gap between the middle and the poor, has the lowest level of social spending of the countries in the sample.<sup>40</sup>

"Most Americans consider themselves middle class, and the self-interest thesis would therefore lead us to expect that the public would be more supportive of government help for the middle class than for the poor."<sup>41</sup> Yet American support for welfare still seems to hinge on the concept of welfare as support for the deserving poor rather than as a more general social safety net or social insurance system. Gilens, for example, finds that most of the U.S. public supports welfare for the poor but not for the middle class. This is distinct from the Europeans' universal vision of social welfare policies and safety nets.

Thus despite the large gap between the middle class and the poor in the U.S., public support for welfare seems to hinge on the recipients of welfare being "deserving" poor and not middle class. The concept of "deserving" poor varies among respondents, however. Because of the large gap between the poor and the middle, one might expect support for means-tested support for the poor to decline when there are economic downturns and those in the middle feel more vulnerable. Yet that is not the case: support for welfare increases. It may be that at times of downturns, those in the middle may feel more sympathetic to the plight of the poor precisely because they are more vulnerable to becoming "deserving poor" themselves. In addition, Gilens finds that support for welfare – even among higher income respondents - is higher among Americans who are related to or know someone who has been on welfare.

One factor that clearly affects American attitudes about welfare – and is also an issue when comparing the political economy of support for welfare across different societies – is race. Americans' support for welfare is directly linked to their perceptions of the racial composition of poverty. While blacks are disproportionately poor compared to whites, they only compose 27% of all poor people. In contrast, in a recent survey cited by Gilens, the median response to a question asking respondents to estimate the percent of the poor population that is black is 50%. Other surveys confirm this tendency to overestimate.<sup>42</sup> A separate study by Erzo Luttmer, based

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<sup>39</sup> See Joan M. Nelson, "Grounds for Alliance? Overlapping Interests of the Poor and Not-so-Poor" in Peter Houtzager and Mick Moore, eds., *Changing Paths: The New Politics of Inclusion* (Ann Arbor: University of Michigan Press, forthcoming).

<sup>40</sup> See Peter Lindert, "What Limits Social Spending", *Explorations in Economic History*, Vol.33, No.1, January 1996, pp.1-34.

<sup>41</sup> Gilens (1999), p.43.

<sup>42</sup> Gilens, pp.68-69. Gilens also finds that the more likely that Americans are to overestimate the percent of the poor population that is black, the less likely they are to support welfare. There is a strong association, for example,

on GSS data, finds evidence of “racial group loyalty”: individuals increase their support for welfare spending as the share of local recipients from their own racial group rises. Differences in resource allocations across states confirm the effects of these attitudes on policy. Luttmer notes that relatively racially heterogeneous states provide lower welfare benefits.<sup>43</sup>

Attitudes about welfare spending also have effects on how individuals vote on questions pertaining to welfare spending. In a study based on approximately 20,000 census blocks in California, and a 1992 proposal to limit welfare spending (Proposition 165), Luttmer shows that actual voting outcomes can be extraordinarily well explained by predicted welfare support, even when controlling for county fixed effects, census tract fixed effects, and the fraction black in the census block group.<sup>44</sup> Not all electoral decisions about welfare expenditures are as clearly phrased referendums on cutting benefits, as Proposition 165 was. Yet the strength of the results suggests that survey data on attitudes about welfare can be a useful predictor of political support for welfare policies in a number of contexts.

Beyond the issue of welfare spending, ethnic or racial fragmentation seems to have effects on the allocation of public goods in general. Alesina, Baqir, and Easterly, in a study of U.S. cities, metropolitan areas, and urban counties, find that the shares of spending on productive public goods – education, roads, sewers, and trash pickup – are inversely related to the city’s (or larger metro area’s) ethnic fragmentation, even after controlling for other socioeconomic and demographic determinants.<sup>45</sup>

This discussion is not intended to imply that U.S. attitudes about welfare apply across countries, nor that the U.S. welfare system is a model for other countries. It uses the U.S. example – for which we have a great deal of data – to demonstrate the extent to which attitudes about redistribution have effects on welfare policy. In addition, the discussion has highlighted a number of issues which are generic to the political economy of social welfare and other social

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between welfare spending preferences and the belief that “if blacks would only try harder they could be just as well off as whites”. Over 50% of white Americans who agree with this statement think that welfare should be cut, while only 20% of those who disagree with the statement think that spending should be cut. The same does not occur with other immigrant groups, meanwhile.

<sup>43</sup> Erzo Luttmer, “Group Loyalty and the Taste for Redistribution”, *Journal of Political Economy*, Vol.109, No.3, 2000, pp.500-527. I thank Ed Glaeser for pointing out this citation. An earlier study by Larry Orr, controlling for average state income and for regional differences, finds that a state with an all white case-load would offer almost \$2000 per year more in AFDC support than would one with an all black case-load. State policies for the “deserving” poor, in contrast, do not differ by race. See Larry Orr, “Income Transfers as a Public Good: An Application to AFDC”, *The American Economic Review*, Vol.66, No.3, June 1976, pp.359-71. A separate study cited by Gilens, by Christopher Howard, finds that there are no racially-linked differences between states on unemployment insurance benefit levels. See Christopher Howard, “A Bridge Too Far? Linking the Study of National and State-Level Social Policy in the United States”, Paper presented to the annual meeting of the American Political Science Association, Washington, D.C., August 1997.

<sup>44</sup> The dependent variable was a “no” vote on Proposition 165, and the dependent variable was predicted support for welfare based on GSS data, along with a number of control variables. The adjusted R-squared ranged from .40 to .75, depending on the specification. See Luttmer (2001).

<sup>45</sup> Alberto Alesina, Reza Baqir, and William Easterly, “Public Goods and Ethnic Divisions”, *Quarterly Journal of Economics*, 114, November 1999, pp.1243-84. Easterly, in a separate article with Ross Levine, finds that ethnic fragmentation is negatively correlated with economic growth in a selection of African economies. Easterly and Levine, “Africa’s Growth Tragedy: Policies and Ethnic Divisions”, *Quarterly Journal of Economics*, 112, November 1997, pp.1203-50.

policies across all country contexts. These are: targeted versus universal assistance; the deserving versus the “undeserving” poor; protecting the elderly versus investing in children; racial heterogeneity and immigration; and tradeoffs between objectives, such as discouraging dependency and improving the lives of children and families. All of these issues differ across countries and cultures. Yet they must be taken into account for social contracts to be politically sustainable over time.

### **Attitudes and Outcomes in Latin America**

An obvious problem in taking public attitudes into account in political economy issues is the absence of adequate data, data which is particularly rare for the developing economies. We have collaborated in the development of such a data set for Latin America. While we obviously cannot assume that lessons from Latin American will apply directly to other regions, they can help us in further developing our framework for thinking about these issues. In addition, the diversity of the 17 Latin American economies in the sample – as well as their different welfare systems – allows us further room for drawing more generally applicable conclusions.

The Latinobarometro survey covers all of the Spanish speaking countries with the exception of the Dominican Republic and Cuba, and including Brazil – a total of 17 countries with approximately 17,000 observations each year - and has been conducted annually from 1997 to 2000.<sup>46</sup> Unless otherwise specified, the results reported here are from the final year of the sample, 2000, which has the most complete questionnaire. Where possible, we used the entire pooled sample to check the robustness of findings. The pooled sample has the advantage of being a time series, but the disadvantage that several of the most pertinent questions are not included in all of the years.

The surveys are nationally representative in most countries, although not in some, such as Brazil and Bolivia, which have large remote rural populations, posing much bigger challenges to achieving representative coverage. The latter surveys have an urban bias, but still have a rural component. In respective years of the survey, we have been able to suggest a number of questions about perceived social status, subjective well being, and attitudes about redistribution and individual mobility.

One of the most striking things that comes out of the Latin American data is a marked similarity between Latin American and United States attitudes about the causes of poverty, about redistribution, and about intergenerational mobility. When Americans (in the GSS) are asked about the causes of poverty, for example in the question “a major cause of poverty is lack of effort by the poor themselves, 36% say that lack of effort is very important, while 43% say that it is somewhat important and 21% say that it is not important.”<sup>47</sup> When Latin Americans are asked a

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<sup>46</sup> There are approximately 1000 interviews per country. The poll is conducted by a respected non-profit corporation, the Latinobarometro, which is based in Chile and directed by Marta Lagos. It began with some initial and limited support from the European Commission and then from the Inter-American Development Bank. The effort began in 1995 with a sub-set of countries, full coverage began in 1997. I was involved in the survey while spending time on a fellowship at the IDB, and continue to provide input on the design of the questionnaire each year, and therefore have access to the data. Because Latinobarometro still has to cover costs, the data is available to the public for purchase.

<sup>47</sup> Author’s calculations based on GSS data.

similar question about the causes of poverty, a surprisingly similar 36% say that poverty is due to no effort on the part of the poor, while 63% say that it is due to bad circumstances.

When we look at the determinants of attributing poverty to lack of effort, as we did in the United States, regressing a positive response on poverty due to lack of effort as the dependent variable, we find that the only significant variables are wealth and leaning to the right on the political scale (the latter is self-reported). The unemployed, meanwhile, are more likely to answer negatively. [Table 4] As discussed above, for the U.S., believing that a lack of jobs is important as a cause of poverty is negatively and significantly correlated with being on the right of the political spectrum, as well as with income, education, and being male.<sup>48</sup> [Table 3a] We do not have this question for Latin America.

A rather interesting finding is that when we include happiness in the equation on poverty being due to lack of effort, we find that happier people, on average, believe that poverty is due to lack of effort in both Latin America and the U.S. (including the happiness variable renders both wealth and unemployment variables insignificant for both). While an explanation for this is beyond the scope of this paper, one could posit that believing poverty is a phenomenon that is inflicted on people creates more distress than believing that it is a result of lack of individual effort.<sup>49</sup>

In an earlier paper, we found that in Latin America those who believe that there are high prospects for future upward mobility - and believe that opportunities for equal advancement in one's country are equally shared - are more likely to be satisfied with their lives in general.<sup>50</sup> (The equal opportunity variable is discussed in greater detail below). We do not have a similar prospects of upward mobility question for the U.S.

When we look at attitudes about inter-generational mobility, we find remarkable similarities between the United States and Latin America. When Americans are asked about their children's future standard of living compared to their own today, 57% say that their children will do better and 23% say that they will live the same. In Latin America, for the same question, 58% of respondents say that their children will live better while 26% say the same. When respondents in Latin America are asked about their own economic status in the future, 41% say better and 42% say the same. Unfortunately, we do not have a comparable question for the GSS.

A rather striking contrast occurs when respondents are asked about their own status compared to that of their parents. In the U.S., 64% of respondents say that they live better, 21% say the same, and 15% say worse. In Latin America, in contrast, only 16% of respondents said that they lived better than their parents, while 21% said the same and 59% said worse. Given the economic crises of the 1980's, the difficult adjustments that were then necessary in the late 1980's and

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<sup>48</sup> Regression results for both sets of conclusions are available from the author on request.

<sup>49</sup> For both Latin America and the United States, we find that reporting leaning toward the right rather than to the left of the political scale is positively and significantly correlated with happiness, although the direction of causality is far from clear. We expand on issues of subjective well being and their relation to macro and micro-economic phenomenon in several other papers, which are best summarized in Graham and Pettinato (forthcoming).

<sup>50</sup> Graham and Pettinato, "Happiness, Markets, and Democracy: Latin America in Comparative Perspective", *Journal of Happiness Studies*, Vol. 2, No. 3, 2001.

early 1990's, and that concerns about stable employment remain high and real wages are still not back to their 1970's levels in many countries in the region, this is not a surprise.

Do attitudes about inter-generational mobility affect attitudes about redistribution? In our analysis of GSS data for the US, neither attitudes about parents or children's standard of living has a significant effect on attitudes about the government's role in redistribution (EQWLTH). For Latin America, for the 1998 survey only, we have a question about what the country needs most to get ahead: productivity growth or more redistribution. When we use the response to that question as the dependent variable and include views about inter-generational mobility on the right hand side, the only significant variable is wealth level, which is not surprisingly positively correlated with supporting productivity.<sup>51</sup>

When one looks at mean levels of support for productivity versus redistribution region-wide, however, we find that a surprisingly high 53% of respondents support productivity over redistribution. Across countries, mean levels of support for productivity are higher in poorer and more unequal countries. [Figure 2] Within countries, it is wealthier people that, on average, are more likely to support productivity over redistribution, which is what one would expect.

We explain the across country differences in two ways. The first is a timing of reform explanation. Most poor and unequal countries in the region (mainly in Central America) are earlier along in the process of market reform, and most citizens recognize the need to establish sustainable growth as a pre-requisite to getting ahead, particularly given the region's experience with high levels of debt and inflation and stagnant growth. Secondly, it is these same countries that have very weak state institutions and underdeveloped social welfare structures. Thus the average citizen is probably quite skeptical about redistributive policies being either fair or efficient.<sup>52</sup>

The same question was not in the year 2000 survey. There is a question about how equally opportunities are shared in the respondent's particular country. When we include a dummy for being poor (below .45 on the wealth index for the sample), it has significant and negative effects. In other words, the poor are less likely to believe that opportunities are equally shared than are the non-poor, which is not surprising. The more educated, meanwhile, are also less likely to believe that opportunities are equally shared, while the wealthy are more likely to believe that they are. [Table 5] When we include attitudes about inter-generational mobility in the equation, we find that respondent's evaluation of their situation compared to their parents has no affect, but that believing that one's children will live better is significantly and positively correlated with believing opportunities are equally available.

## Outcomes

At a very general level, attitudes about redistribution in Latin America seem remarkably similar to those in the U.S. and therefore quite different from those in the average European country with a more developed social safety net. While the explanations for this are no doubt

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<sup>51</sup> Regression results available from the author.

<sup>52</sup> We discuss this in detail in Graham and Pettinato, "Hardship and Happiness: Mobility and Public Perceptions During Market Reforms", *World Economics*, November-December 2000.



complex, it is plausible that some of the strong faith in individual effort over state redistribution in Latin America comes from a very weak tradition of effective redistribution in the region, with countless attempts in the past being captured by relatively privileged interest groups at the expense of the very poor.<sup>53</sup>

The record was not only regressive, but also inefficient, with many countries spending high percentages of their public expenditures on the social sectors, but with very little to show for it in terms of effects on poverty reduction. In addition, misallocated public expenditures were often accompanied by unsustainable fiscal deficits, resulting in high levels of inflation and high levels of external debt, further discrediting state redistribution in many countries.

The weak record of redistribution in large part comes from weakness in public sector institutions and underdeveloped social insurance systems. Thus in many countries, such programs were piece-meal or sector specific, and led to general tax revenues being redistributed to some sectors of the labor force (usually a minority) and not to others. Organized workers in the public sector and those in strategic industrial sectors, such as minerals or oil, were the most likely to have coverage. While workers in these sectors are not privileged by industrial country standards, they are relative to the majority of workers in their own countries, particularly those in the informal sector. In Brazil, for example, only 18% of the poorest income groups – who account for over 40% of the population – are covered by the public social security system, and receive only 3% of the benefits that the system pays out. In Venezuela, personnel expenditures absorb over 90% of the education budget, reflecting the power of the teachers' unions there.<sup>54</sup>

Little wonder, then, that two trends dominated the debate on social expenditures in the region in the 1980's. The first was a move towards more targeted policies and programs and away from universal forms of social insurance.<sup>55</sup> The second, in part an outgrowth of the first, was the introduction and proliferation of the social funds of the 80's and 90's – lean, semi-autonomous social programs which allocated funds based in large part on the demand of local level organizations and municipalities. Some of these funds, although not all of them, played an important role in cushioning the impact of adjustment policies for poor – although not the poorest – groups.<sup>56</sup>

With almost two decades of experience with both targeted programs and social funds, there is still strong consensus on the need to target the limited public funds that are available for social

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<sup>53</sup> For numerous accounts of clientelism or politics dominating allocation decisions in public safety net programs, see Graham (1994).

<sup>54</sup> See Nancy Birdsall and Estelle James, "Efficiency and Equity in Social Spending: How and When Governments Misbehave", *World Bank Working Papers* #274, May 1990; and Alan Angell and Carol Graham, "Can Social Sector Reform Make Adjustment Sustainable and Equitable? Lessons from Chile and Venezuela", *Journal of Latin American Studies*, Vol.27, pp.189-219.

<sup>55</sup> For a review of the record in this area, as well as the philosophical debates, see Margaret Grosh, *Administering Targeted Social Programs in Latin America: From Platitudes to Practice* (Washington, D.C.: The World Bank, 1994); and Dominique van de Walle and Kimberly Nead, eds., *Public Spending and the Poor: Theory and Evidence* (Washington, D.C.: The World Bank and Johns Hopkins University Press, 1995).

<sup>56</sup> For a critical review of social funds, see Judith Tendler, "Why Social Policy is Condemned to a Residual Category of Safety Nets, and What to do about it", Comments for the UNRISD Meeting in Stockholm, 23-24 September 2000.

sector spending to the neediest sectors.<sup>57</sup> There is less consensus on the merits of social funds. Programs that operate largely outside the mainstream public sector institutions and allocate expenditures according to demand-based criteria, while having a number of advantages, have limited capacity to target and a great deal of heterogeneity in outcomes. In addition, such programs usually are not part of a broader social contract, and cannot replace more broadly based social assistance and insurance systems in the long term.

Given the extent of need and limited public funds, some targeting will always be necessary. On the other hand, too much emphasis on targeting in the context of high numbers of eligible poor can result in the very poorest being left out. This is a particular concern if the program uses demand-based criteria in the allocation process, as the experience of the Trabajar program in Argentina suggests. A recent study of an effort to limit Trabajar funds found that it was the poorest recipients that ended up losing program support, as the more vocal demands of more organized, less poor groups were more successful at accessing increasingly limited funds.<sup>58</sup> In other words, effective targeting of the poorest in the context of high levels of eligible poor requires sufficient funds.

Public attitudes about redistribution, the causes of poverty, and about opportunities for mobility will be critical to developing such a social contract – and more permanent forms of social assistance – in most countries in the region. Differences AMONG individual Latin American countries will also be definitive. These differences are in part reflected in the level and composition of public expenditures, which vary a great deal among countries. There are countries in the region with a long tradition of social welfare and social insurance systems, and for the most part these are countries where these programs are still largely intact, even if they have been altered substantially to incorporate concerns about efficiency as well as new thinking about the role of the private sector, about individual contributions, and about targeting expenditures on the neediest groups.

Table 6 provides a snapshot of the different levels of public resources devoted to social sector expenditures in the region. It does not, however, reflect how or if the expenditures are targeted. Thus countries that have not made much effort to target expenditures to the poor, such as Brazil, spend a similar high percentage of their public expenditures on the social sectors (and a higher percent of their GDP on social expenditures) than countries such as Chile, which have made major in-roads in targeting expenditures to the poorest, with consequent effects on poverty reduction.<sup>59</sup>

### The Chilean Experience

Chile has perhaps gone the furthest of any country in the region in reforming its social sector institutions, re-vamping its social security, education, health, and social welfare institutions along these lines, with different degrees of success depending on the sector. As a result of its

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<sup>57</sup> For the record so far in the region, see Castañeda (2002).

<sup>58</sup> Martin Ravallion, “Is More Targeting Consistent with Less Spending?”, *Policy Research Working Paper #2079*, The World Bank, Washington, D.C., March 1999.

<sup>59</sup> For a more extensive analysis of the extent to which expenditures are targeted in a number of countries in the region, see Castañeda (2002).

high degree of pre-existing administrative capacity in the social sectors, coupled with the targeting efforts, Chile's record in protecting the welfare of the poorest of the poor during the extensive economic crisis of the early 1980's, both through public works employment programs and also through targeted mother and child nutrition programs, has received a great deal of positive attention, and attempts have been made in a number of countries to copy different elements of its social sector reforms.<sup>60</sup>

Despite this record, over time Chile has had to adapt its social welfare policies to changing realities as its economy has developed extensively and per capita income has increased, as well as to changing political circumstances and attitudes. The targeting of social welfare expenditures, for example, occurred in the 1970's and 1980's, under the auspices of an authoritarian political regime, when political debate was repressed and labor unions were outlawed. With the democratic transition in 1990, policymakers had to adapt the system to broader and more "normal" political pressures, while still maintaining an emphasis on targeted programs. The concerns of teachers' unions, for example, were pre-eminent in the adaptations to the education reforms that were made in the post-authoritarian era.<sup>61</sup>

Social expenditure in general increased at an effective annual rate of 8.5% from 1991 to 1995, in contrast to the previous decade, when it actually declined (but increased for the very poorest groups). The post 1990 increases, meanwhile, while maintaining support for targeted and means-tested expenditures, were the largest for more universally available services: health, education, and social security.<sup>62</sup> The increase was made possible through a bipartisan consensus on an increase in taxes on business profits.<sup>63</sup> It was a response, meanwhile, to the government's need to address the genuine concerns of the middle strata and the near poor who had not fared as well as the poorest in many of the reforms, particularly in the health and social security arenas.<sup>64</sup>

Now, after almost a decade of sustained high levels of growth, in keeping with Chile's past record of using public works employment as a safety net, the Lagos government is re-instating a number of public works employment programs to deal with an unemployment rate of over 8%

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<sup>60</sup> See, for example, Kevin Cowan and Jose de Gregorio, "Distribution and Poverty in Chile: Have We Gained or Lost Ground?" in Solimano, Aninat, and Birdsall (2000); and the chapters on Chile in Graham (1994) and (1998).

<sup>61</sup> These changes were not without criticism, meanwhile, as many critics argue that the centralization of personnel relations that occurred eroded the effectiveness and flexibility that was introduced by the voucher reforms. For detail, see Varun Gauri, *School Choice in Chile* (Pittsburgh: University of Pittsburgh Press, 1999).

<sup>62</sup> Jose Pablo Arrellano, "Economic Growth, Fiscal Policy, and Social Impact" in Andres Solimano, Eduardo Aninat, and Nancy Birdsall, *Distributive Justice and Economic Development: The Case of Chile and Developing Countries* (Ann Arbor: University of Michigan Press, 2000); and author's attendance at the conference at which draft papers for the project were presented and discussed, Santiago, July 1997.

<sup>63</sup> For a detailed discussion of this tax reform, see Delia Boylan, "Taxation and Transition: The Politics of the 1990 Chilean Tax Reform," *Latin American Research Review*, Vol. 31/, 1996: 7-31.

<sup>64</sup> For the trade-offs for the middle strata in the social security reform, see Estelle James, "Efficiency and Equity Tradeoffs in Social Security Reform" in Nancy Birdsall, Carol Graham, and Richard Sabot, *Beyond Tradeoffs: Market Reforms and Equitable Growth in Latin America* (Washington, D.C.: The Brookings Institution and the Inter-American Development Bank, 1998). For the fate of the middle strata and the near poor more generally with market reforms, see Nancy Birdsall, Carol Graham, and Stefano Pettinato, "Stuck in the Tunnel: Is Globalization Muddling the Middle Class?", *CSED Working Paper Series*, No.14, The Brookings Institution, August 2000.

and several years of slow growth. Plans are being laid to create well over 100,000 extra jobs via a number of public sector agencies, including the Social Contingency Fund.<sup>65</sup>

### Other Examples

Uruguay and Costa Rica are two other countries noted for their social welfare structures. While Uruguay has not gone as far as Chile in terms of targeting expenditures and introducing private sector involvement and choice into the delivery of services, it has introduced individual accounts in its social security system, as well as a major education reform with some elements of decentralized management. Costa Rica, meanwhile, continues to maintain a more universally based system, but in recent years has been confronted with issues of declining quality of services due to the inability to keep up with the scale and scope of demand for services. Argentina also has had a very well developed social insurance system for decades, but it is heavily tilted towards the middle strata rather than the poor.<sup>66</sup>

Mexico, meanwhile, with its Progresa program, has undertaken a major experiment in targeting social assistance to the rural poor – and linking it to better health and education outcomes by delivering the assistance to women in poor households. Initial evaluations of the program are very positive about its ability to combine targeting objectives with broader health and education objectives.<sup>67</sup>

Given the discussion above about racial and group loyalty and welfare expenditures in the United States, as well as the more general effects of ethnic and racial fragmentation on spending on public goods, it is noteworthy there is a great deal of racial homogeneity in the countries where social insurance systems were developed early on. This contrasts quite sharply with many of the Andean countries, for example, where there the indigenous population constitutes a much higher proportion of the total.

In historical terms, while the former set of countries were far from the center of the Spanish colonial empire, the latter were very much at the core of the administration of a colonial elite that was notorious for its exploitation of the local population. Brazil, meanwhile, also a country with a very limited safety net and high levels of inequality and poverty, is both very large, and racially and geographically fragmented. At a very general level, those countries that have the most developed social insurance and safety net systems in the region are much more like the homogenous countries of Europe, and those that do not are more like the racially and geographically heterogeneous United States.

These are very broad generalizations. Yet they find an echo in different attitudes about redistribution among the countries in Latin America. Argentina, Chile, and Uruguay, for

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<sup>65</sup> “Mensaje del Presidente de la Republica, Ricardo Lagos, Al Congreso Nacional, 21 de mayo 2001, *El Mercurio*, 21 mayo 2001; and discussions with Kirsten Sehnbruch, doctoral candidate, University of Cambridge, June 2001.

<sup>66</sup> To a large extent this reflects the power of the Peronist labor movement at the time that it was established. Even the semi-private pension system, established in the 1990’s, is much more favorable to middle income workers than to lower income ones.

<sup>67</sup> For an excellent evaluation of the Progresa program, see Paul Gertler and Simone Boyce, “An Experiment in Incentive-Based Welfare: The Impact of PROGRESA on Health in Mexico”, Mimeo, University of California at Berkeley, April 2001.

example, are among the strongest supporters of redistribution in the region.[Figure2] And all three countries have lower than average mean scores for believing that opportunities are equally shared.[Table 7] In other words, publics in these countries are more likely than the average Latin American respondent to support some sort of government role in redistribution and/or the provision of a safety net.

In addition, only a few countries in the region – Argentina and Brazil - have unemployment insurance systems – at least as traditionally defined – and of the two, only Brazil’s provides coverage on a significant scale.<sup>68</sup> Chile only passed unemployment insurance legislation in 2001, and the system is still in the developing stages. At best, the system, which is based on employer and employee contributions to individual accounts, will cover 10% of the labor force.<sup>69</sup> One reason for the lack of unemployment insurance in the region is that it is designed to cover workers with stable jobs in the formal sector, while a large proportion of the labor force – including most poor workers - is in the informal sector.

Not surprisingly, fear of unemployment has strong and consistently negative effects on perceived well being among respondents of all income levels. These concerns are slightly stronger for those at the lower end of the income ladder than for the wealthy. They are also stronger for those that are less educated and those that work in the private sector.<sup>70</sup> Mean scores for fear of unemployment are also lower in the countries that have more developed safety nets and/or unemployment insurance than they are in most other countries in the region. While these fears are, no doubt, also driven by overall macroeconomic conditions and open unemployment rates, the existence of a safety net must help ameliorate them. [Table 8]

Thus far, this paper has attempted to show how public attitudes - about redistribution, causes of poverty, and opportunities for upward mobility - have effects on the political viability of social welfare policies. They can also influence the design and choice of policies. The analysis also suggests that attitudes in Latin America are much more like those of the U.S. than they are those of European countries. This suggests that more limited, individual contribution and work-based safety nets are more likely to be politically sustainable in those countries.

Such an approach also makes sense given the large informal sectors and the limited fiscal capacity of these economies. In particular, the continued reliance on the VAT to generate most general revenues is a regressive form of taxation in general, which presents a number of tradeoffs when designing social assistance policies that are funded by these revenues. Thus the development of more permanent and broad-based social assistance systems will be limited and gradual by necessity. This should not, however, discount the importance of the need to make progress on this agenda.

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<sup>68</sup> Ecuador has a small, non-traditional system; Venezuela has a severance pay system that is in flux, and in the Caribbean, Barbados has a traditional scheme. For an excellent overview of unemployment insurance and related systems in the region, see Jaqueline Mazza, “Unemployment Insurance: Case Studies and Lessons for Latin America and the Caribbean”, IADB Research Department Working Paper Series #411, Inter-American Development Bank, Washington, D.C., October 1999.

<sup>69</sup> The law has been the subject of much debate, with a great deal of opposition from the right. Depending on how one reads the law, as little as 7% of the labor force will have coverage.

<sup>70</sup> We report these results fully in Graham and Pettinato, “Happiness, Markets, and Democracy: Latin America in Comparative Perspective”, op cit.

## **Crafting Social Contracts: Managing Political Economy Constraints**

Social welfare and social policy more generally are particularly vulnerable to political attitudes and political context. Most publics have fairly broad consensus on the “public” nature of goods such as education and health, as the broader benefits for society as a whole are fairly obvious. Yet assistance to those unable to provide for themselves, especially those that are able-bodied, is more controversial, at least in some societies. This is a particularly difficult issue in the developing countries, where established social contracts and broadly based social insurance systems are the exception, and at the same time there is a great deal of poverty. In most countries, the nature of the social contract still needs to be established, including reaching agreement on how to finance it, which will ultimately entail redistribution from some sectors to others, and achieving a balance between investments in human capital and assisting the poor and vulnerable. This again entails tradeoffs among social sectors and between generations.

To date there has been much thinking about the debate over targeted versus more universal services. In the developing countries, given the extent of need and limited public funds, some targeting will always be necessary. The political choices that need to be highlighted may not always be between targeted and universal services, but rather about the near poor and the poor, and the poor and the poorest; about the working poor versus the non-working poor; about central versus locally financed and implemented programs; about the formal versus the informal sector. Resolving these issues will ultimately be key for developing countries to move from temporary and usually externally financed social assistance strategies to social welfare structures which are part of a domestically financed social contract.

There are very few developing countries where such issues have been resolved, and this paper only suggests ways of thinking about them. What is clear is that public attitudes about these issues, in addition to the socioeconomic and institutional structures in particular countries, will play a determining role in the process. Dismissing or neglecting deeply entrenched public attitudes is likely to result in unsustainable programs. This does not mean that new approaches cannot be introduced, nor that public opinion cannot change over time. But strategies for implementing reform must include navigating the constraints posed by public opinion and attitudes, as well as recognizing windows of opportunity.

This section of the paper attempts to provide policymakers with three sets of tools. The first of these is tools with which to assess public attitudes – and the broader political economy context – in a particular country setting. The second is a set of themes around which to frame choices about the feasibility of particular kinds of programs, given a country setting. The third is a menu of strategies for navigating the political context, options which are organized around three context-dependent variables: the structure and capacity of public institutions; the nature of public attitudes about social assistance; and the balance between centrally-driven and decentralized reform initiatives. The international financial institutions (IFIs) can play a role in improving these tools by collecting and analyzing the cross-country experience, and by disseminating the lessons learned.

## Assessing Public Attitudes

An obvious question for policymakers is how to measure or assess public attitudes, and how to apply these assessments to concrete policy questions. The most obvious assessment instruments are public opinion surveys. As the study of California voting patterns discussed above suggests, public attitudes about social welfare spending, as expressed in surveys, can be a fairly accurate predictor of political support for policies or proposed changes in policies.

The Latinobarometro is a good example of the kind of survey instrument that can play such a role. It is the most extensive survey of its kind in the developing economies; similar survey data for other developing countries and regions would be extremely valuable. At present there are efforts to develop an Asia-barometro, as well as similar surveying efforts in a few selected African countries. An issue that is critical to these and related data collection efforts, meanwhile, is adequate financing. As the information that these surveys provide is important public knowledge, an obvious role for the IFI's is the provision of supplemental financing for the surveys, as well as assistance in the dissemination of the results.

A major limitation for the Latinobarometro, for example, is that due to cost constraints, in many countries the surveys are not nationally representative. They are particularly skewed for countries with large and remote rural populations which are both difficult and very costly to reach, such as in Bolivia and Brazil.<sup>71</sup> The Latinobarometro is also missing some important questions for which we have analogous data for the developed economies, and which have an influence on the design of policies. One key issue, for example, is the extent to which Latin publics are willing to pay taxes – and progressive taxes in particular – to support the development of more effective and permanent forms of social insurance. Yet additional resources are necessary to increase the number of questions in such surveys, to closer approximate national representation, and for the data to be made publicly available.

In addition to survey instruments, each country's own history of trajectory of social assistance efforts (or lack thereof) is surely a helpful guide to determining what scope and scale of effort is politically feasible. Publics in countries that have traditionally relied heavily on family systems of support, such as the East Asian economies, are unlikely to be comfortable with very large-scale, generous public programs, as was well demonstrated by reluctance in these to set up new safety nets in the aftermath of the 1997 economic crisis.

On the other hand, publics such as those in the former communist countries, who are accustomed to comprehensive public schemes, are unlikely to favor highly targeted assistance policies, at least in the short term. While certainly attitudes can and do change over time – and are often influenced by success stories from other countries, attention to past trajectories can at the least provide useful information about the intersection between public attitudes and assistance policies.

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<sup>71</sup> For this reason, in some of our regression analysis, both here and in other work, we treat the entire survey as one region-wide sample rather than one which is representative at the country level. For most specifications, we find that the results are very similar whether or not we include country dummies.

## From Attitudes to Policy Choices: A Frame for Making Choices

One issue is how to gather sufficient information. Another is how to apply that knowledge to political questions. These questions will, no doubt, vary according to country context. Yet there are several issues which are generic to the political economy of all social assistance policies, and will help determine key choices, such as whether a targeted or more universal approach is optimal, or whether programs should be federally or locally funded and administered.

To a large extent, these issues will hinge on the question of who the public deems to be deserving of assistance and to what extent that choice is dictated by similarities and differences between those needing assistance and the general public. The greater the fiscal constraints, the more likely that attitudes about who “deserves” assistance will play a role. Such attitudes, as well as the political debate, can also be swayed by the lobby or influence of particular interest groups with a claim on social assistance benefits. These groups are rarely the neediest.

First of all, how close (in the income distribution) and similar (in terms of type of employment, residence, etc) are the poor and the middle strata. In some countries – particularly more developed economies, the poor are a distinct “underclass”. In others, and in most emerging market countries, there is a fair amount of movement in and out of poverty from the ranks of the middle strata.<sup>72</sup> While in such cases there is usually a separate category of extremely poor people, who do not share traits with the middle strata (and who may require separate sorts of assistance policies), the political economy of social policy should be seen in terms of the congruence of interests between the poor and the middle.<sup>73</sup>

An important question is the degree of racial homo or heterogeneity between the poor and the rest of society. As the earlier discussion about the U.S. notes, while much of the public supports broad-based policies such as health and education regardless of the racial composition of society, large racial differences seem to create political divisions when it comes to means-tested assistance for the “non-deserving” (able-bodied unemployed) poor. In such circumstances, crafty packaging and marketing of assistance policies – as well as public education - may be necessary (for example, the U.S. public’s misperceptions about the extent of the poor population).

A related question is the extent to which poverty is regionally concentrated. Again, it may be more difficult to marshal political support for assistance policies for populations that are remote or “invisible” to the average citizen as opposed to those that are closer and with whom there is some sense of affinity. Remote populations are much less likely to have representation in organized and influential interest groups, meanwhile.

Another issue is that of the ideological or political orientation of the majority of the public. It is very clear from both our U.S. and Latin America analysis that those respondents that place themselves on the right or conservative side of the political spectrum are much less likely to

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<sup>72</sup> For documentation of this, see Birdsall, Graham, and Pettinato (2000); and Lant Pritchett, Asep Suryahadi, and Sudarno Suarto, “Quantifying Vulnerability to Poverty: A Proposed Measure with Application to Indonesia”, Mimeo, The World Bank, Washington, D.C., January 2000.

<sup>73</sup> A good description of the different needs of the extreme poor is found in Michael Lipton, “The Poor and the Poorest: Some Interim Findings”, *World Bank Discussion Paper #25*, Washington, D.C., 1988.



support redistribution to the poor or needy, and are more likely to believe that the poor are poor due to lack of effort rather than to circumstances beyond their control. Research by Corneo and Gruner, discussed above, suggests that the effects of these aggregate, country-level attitudes, are as strong if not stronger than individual level economic concerns in explaining intra-country differences in attitudes about redistribution in a selection of European countries and the United States.<sup>74</sup>

This research, in addition to case-study based work, suggests that country level differences in attitudes about social welfare do matter a great deal, and that assistance policies with a self-help or work requirement component (such as the new U.S. welfare law) are more likely to be politically viable among conservative or right-leaning publics than are other sorts of policies, such as European-style welfare policies. Again, how programs are packaged and marketed will also matter.

Program design reflects the objectives of policymakers and the public, and differences among them can have major effects on different groups of beneficiaries. Programs such as the U.S. welfare system, which hinge on the objective of getting the poor back to work trade-off other objectives, such as the status of poor children in general. In other words, the children of “undeserving” poor who do not go back to work are much more vulnerable under a U.S.-style system, where the non-working poor risk losing their benefits, than they are under a European-style system, which provide assistance based on the number of people in poor families that need support. A risk associated with this latter type of system, however, is that it is difficult to discourage dependence on welfare.

Without making a judgement about which kind of system is better, policymakers need to be aware of the tradeoffs that exist, as well as public attitudes about these tradeoffs. In some Eastern European and former communist economies, for example, it is much less acceptable politically to cut pension benefits than it is to cut family assistance.<sup>75</sup> Some of this is, no doubt, determined by the relative weight of interest groups (pensioners both have time and are highly organized; parents of poor children are not). Some is also determined by public attitudes. Yet establishing clarity on the objectives of the program and the choices entailed will make it much easier for policymakers to navigate the political context when presenting and implementing the program.

A more general question, which must be answered by academic research rather than by public opinion polls, is what kinds of social assistance systems are feasible and sustainable in contexts of high levels of poverty and inequality. Regardless of their design and scope, social welfare systems must be implemented in the context of growth-oriented macroeconomic policies, as at best they can only complement growth and development in reducing poverty. Yet they can serve as important supplements to the growth process by protecting the vulnerable at times of economic downturn and, equally important, providing insurance from risk of unemployment for those that take up new opportunities for upward mobility. In this latter role, they can enhance broader based participation in the growth process. Even then, particularly in very poor contexts,

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<sup>74</sup> Corneo and Gruner (2000).

<sup>75</sup> I discuss this in detail in Graham (1994) and Graham (1998); see the chapters on Poland in the former and the Czech Republic on the latter.

there may be difficult choices about investments in children's education versus providing protection for unemployed adults.<sup>76</sup>

Another related tradeoff is between investments in children's education and health and those in the security of the elderly and retired population. Certainly these are not diametrically opposed tradeoffs, and, particularly in Latin America, the poor elderly and the children of the poor often co-exist in the same household. However, there certainly are tradeoffs at the aggregate public expenditure level between investments in reforming and improving social security systems, which for the most part cover formal sector workers, and in investments and expansions in primary health and education systems, which benefit children disproportionately. While Latin America's current demographic profile and labor force requirements certainly favors greater investments in the education and skills of the next generation, the demographic transition over the next few decades suggests that the proportionate size of the retired population will grow, and also increasingly become a concern for public policy.<sup>77</sup> The allocation of expenditure to each of these objectives will vary according to particular countries' attitudes and priorities. However, this is a good example of a policy area where the IDB can use its accumulated knowledge to better inform policy choices.

### Navigating the Political Context

Once choices about who the beneficiaries of social assistance and social policy should be, policymakers must still navigate diverse and often very difficult political contexts in order to implement policy changes. Nor is the political economy context the only constraint or concern facing policymakers when they design and implement such policies. Many of them are important but beyond the scope of this paper, such as the critical issue of fiscal constraints (which in the end dictates many political choices).

The focus here is three sets of issues which directly interact with the political economy context to determine the feasibility of particular social programs and social assistance policies, as well as strategies for implementing them. These are the administrative capacity of public sector institutions, the extent to which public attitudes about social assistance are entrenched or framed around particular kinds of policies, and the balance between full blown and centrally-driven reform initiatives and lower key, ad hoc, and/or pilot initiatives. Understanding the lay of the land in these three issue areas will assist policymakers in navigating the political economy context.

### The Institutional Framework

The choice of social policies is often dictated by the capacity of public sector institutions. In countries with very weak public institutions and very little administrative capacity, policies which rely on very little central level administration and much more on local institutions and organizations (including non-government organizations) to both identify and implement projects, such as the social fund model, are usually more appropriate. There is clearly a trade-off,

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<sup>76</sup> Of course, the unemployed often have children, and thus the tradeoffs are not always straightforward.

<sup>77</sup> See the chapter on demography in *Development Beyond Economics* (Washington, D.C.: Inter-American Development Bank, 2000).

however, as such policies are much less effective at targeting particular groups, particularly the poorest, who are the least likely to present viable project proposals.

Thus, while decentralized, demand-based programs have a great deal of appeal in many contexts, and often has positive externalities in terms of local capacity-building and the creation of local level stakeholders, they usually cannot provide a fail-safe safety net. This must be kept in mind if protecting the most vulnerable is a major objective. That said, in many contexts where central level administrative capacity is preclusive to other approaches, this may be the only feasible alternative, at least in the short term.

In addition, if the political context is hostile to redistribution or to assistance strategies, then this model also has the appeal of demonstrating that those who receive assistance must take initiative and contribute substantial effort in order to receive it. Another advantage is that the devolution of responsibility for the program from central to local level can often help diffuse the political debate and political opposition, as was the case in the United States in 1996, when states were given block grants and a great deal of flexibility in setting the rules for TANF.

Over the longer term, the demand-based model of social assistance can be further developed to create greater linkages with the mainstream public sector, which can meet institution-building objectives, as was attempted in the second stage of Bolivia's Emergency Social Fund. As always, this approach also entails tradeoffs, as the greater the linkages with the mainstream bureaucracy, the less agile and flexible the assistance program is likely to be.

The alternative model is a centrally implemented program within the mainstream public sector bureaucracy, as is the case with social welfare policies in Chile, Costa Rica, and Uruguay (even though many of them have local level components). This may be the most effective approach if targeting the poorest is an objective, as Chile's experience in the 1980's demonstrates. Administrative capacity is a pre-requisite for this kind of approach, however. There are also other advantages from a poverty reduction perspective. In addition to targeting, it is possible to coordinate various kinds of assistance, such as tying means-tested assistance for low-income mothers to regular visits to the health posts for their children. It is also more possible to guarantee uniformity and regional balance in assistance policies, although these objectives are, of course, contingent on sufficient funding and political commitment, in addition to administrative capacity. With demand-based, locally driven approaches, heterogeneity in outcomes is a given. At the same time, as noted above, the latter may have an advantage in circumventing or avoiding national level political controversies.

A centrally driven approach is also easier to maintain on a permanent, as-needed basis which can respond to macroeconomic cycles and/or external shocks. Coordination at the central level makes it more likely that economic downturns can be foreseen more easily and planned for. Chile's recent implementation of public works employment, for example, called for the cooperation and participation of various ministries, as well as coordination with the private sector. This would be more difficult – although not impossible - to achieve with a demand-based and semi-autonomous assistance fund.

While administratively lean and decentralized programs are better suited to “hostile” political environments, centrally-based assistance programs – which are usually larger - require at least a minimum degree of political support, as they are much more likely to be the focus of national-level political debates. It is therefore no surprise that the countries that have the most developed systems of this kind also have political cultures that emphasize at least some degree of social solidarity and collective responsibility for assisting those that fall behind. They are also, as noted above, fairly homogenous in terms of race and tend to be smaller in geographic terms.<sup>78</sup>

Two integrally linked and important issues are the structure of political institutions and the organization and/or relative strength of particular interest groups. In a few contexts, executives have a great deal of freedom to implement changes in the social assistance arena. In most, however, social assistance policies are closely linked to social sector policies such as health and education, over which publics usually have very strong views, and legislative approval is required for making changes or implementing reforms. Unlike macroeconomic reforms, which can often be implemented by executive decree, social sector and social welfare reforms usually require legislative approval. Thus the nature and relative balance of political institutions will play a role in determining the kinds and scope of reforms that are feasible. In contexts where the legislature is relatively strong, building a broad base of support for reforms – and/or a more incremental and decentralized approach – may be necessary.

Related to this is the role of interest groups. In countries where organized labor or other such interest groups are very strong, it will be very difficult to dismiss their interests – and claims on social assistance benefits – in any kind of centrally driven, comprehensive reform initiative. Again, the balance of interests will interact with public attitudes about who is deserving of assistance to determine the kinds of policies that are feasible and sustainable.

None of this implies that particular countries are pre-destined to have a particular kind of safety policy or social assistance program. It does suggest, however, that certain kinds of programs are easier to implement in particular administrative and political contexts.

### Entrenched Public Attitudes

The second issue is how policymakers can navigate political attitudes or political cultures when attempting to implement new kinds of or changes in social assistance policies. Many observers have noted the difficulties that external actors had in convincing policymakers in Asia of the need for social safety net policies during the 1997-98 economic crisis.<sup>79</sup> The reason was the fear that those nation’s strong tradition of family-based responsibility for social assistance would be eroded by the introduction of public programs. While those fears were probably justified to some extent, it is also clear that a large amount of human suffering and increases in poverty could have been avoided had more effective public safety nets been in place. And had the recovery from the crisis not been so rapid, these issues would have been even more salient.

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<sup>78</sup> Other large scale public assistance programs, such as public works programs in India, have been implemented on a regional basis.

<sup>79</sup> See, for example, Birdsall and Haggard (2000).

On the other hand, some publics feel very strongly about collective responsibility for certain goods, ranging from social assistance to education. In much of Eastern Europe, for example, it has been extremely difficult to implement social security reforms based on individual contributions due to the entrenched belief that pension systems should be public, even though it is increasingly clear that the current systems are insolvent and continued public support for them is encroaching upon other essential government expenditures. This contrasts with the large number of Latin American countries which, following Chile's example, have introduced private or partially private social security systems. In the Eastern European context, where pensions have been universally provided and the responsibility of the state for decades, introducing change was much more difficult than in Latin America, where large parts of the public were not covered by the public pension system to begin with, and where the role of the state in providing social services was more limited.

How then to navigate deeply entrenched attitudes when crafting broader social contracts? As a starting point, it is clear that they cannot simply be dismissed. If attitudes favor the private sector, then private sector involvement - either in the provision of services or playing a role in hiring temporary labor - may make programs more politically feasible. If there are strong attitudes about the deserving versus the non-deserving poor, then work requirements and other forms of self-help may help make programs politically feasible. In contrast, in the case where there are strongly entrenched views about certain services being public goods, then reforms which seek to increase things such as voice and choice must be introduced cautiously and with strong public relations components - or even better on a pilot basis - to avoid polemical political debates which can jeopardize broader reform efforts.<sup>80</sup>

### Big Bang Efforts versus Reforms by Stealth

The literature and debate on the implementation of macroeconomic reforms has focused on the pros and cons of big bang versus gradual approaches to reform. Similar arguments could be made about the timing and scale of social policy reforms in the social assistance arena, and in determining whether the crafting of a social contract will be a coherent effort or more ad hoc. An analogous but slightly different distinction applies to social welfare reforms, between centrally driven, clearly defined reform efforts and ad hoc or decentralized reforms by stealth.

Success in reforming social welfare and other social sectors usually entails extensive efforts to publicize and explain reforms to the public; clear consensus on their direction; and central level commitment and priority setting. Multiple cases of failed social welfare reform in the United States versus the success of the 1996 reform are case in point. An additional advantage was that Clinton was a democrat pursuing what seemed a classic republican agenda (getting welfare recipients to work and ending dependence). He had a "window" of opportunity, during which his relative political advantage coincided with a very clear national consensus on the need to reform welfare.<sup>81</sup> Yet the success with welfare reform contrasts sharply with the same

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<sup>80</sup> Public opposition to reforms to social assistance programs, as in the case of targeting rice subsidies in Sri Lanka and maize meal subsidies in Zambia, can jeopardize governments efforts at macroeconomic reform.

<sup>81</sup> For detail on the politics of U.S. welfare reform, see Kent Weaver, *Ending Welfare as We Know It* (Washington, D.C.: The Brookings Institution Press, 2000).

administration's failure at health reform, in part because in the latter case there was so little consensus on the direction of the reform.

Similar examples abound in the developing economies. Uruguay's success in reforming education in the early 1990's was driven in part by clear consensus on the direction of the reform and in part by the leadership and political skills of its education minister, German Rama.<sup>82</sup> Again, there was a window of opportunity in part created by the clear public consensus on the need for education reform. This contrasts sharply with a failed health reform in Uruguay at the same time. In Colombia, meanwhile, a very ambitious health reform was passed in the early 1990's. The reform was based on separating the financing from the provision of health care, the introduction of competition in provision, and the extension of insurance to hundreds of thousands of low-income individuals. The effort was in large part possible because of the vision and commitment of the then health minister, Juan Luis Londono.<sup>83</sup> While leadership does not translate easily into a policy recommendation, it matters.

Yet there are also instances where even the most effective of reformers and communicators are unable to pass reforms due to entrenched public attitudes. The case of Vaclav Klaus and the reform of the social assistance system in the Czech Republic is an example. Here a leader who was able to turn a centrally planned economy into a market one over-night, and who implemented the first full blown attempt at voucher privatization in the region, was unable to reform the social benefits system.

Klaus initially wanted to target family benefits (which were universal in the Czech Republic) to families at 1.25 times the minimum wage and below. After widespread opposition, the government backed off its proposal, agreeing to stagger benefits (higher) for the poorest families, but pay benefits to all those earning up to 2 times the minimum – which meant all families except the wealthiest 5%.<sup>84</sup> Klaus realized that a wider public debate on targeting social policy would jeopardize other parts of his reform program. This was due to deeply entrenched attitudes about universal rights to social assistance benefits. From that point on, the government backed off more extensive efforts, and reform of social assistance programs became a process of tinkering at the margin.

In such contexts, it may well be impossible to get political approval for particular kinds of reforms – at least at particular political junctures – as the political cost may be so high as to jeopardize important government objective in other arenas, such as macroeconomic reform. In these cases, the only way to make progress towards reform and/or introducing new approaches to social service delivery is to take a strategy of “reform by stealth”.<sup>85</sup>

Here the strategy is exactly the opposite of the one described above. Instead of a centrally driven effort that receives a lot of attention in the national political debate, reform efforts in this

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<sup>82</sup> See Fernando Filgueira and Juan Andres Moraes, “Political Environments, Sector Specific Configurations, and Strategic Devices: Understanding Institutional Reform in Uruguay”, Office of the Chief Economist Discussion Paper # R351, Inter-American Development Bank, Washington, D.C., 1999.

<sup>83</sup> See Carol Graham, Merilee Grindle, Eduardo Lora, and Jessica Seddon, *Improving the Odds: Political Strategies for Institutional Reform in Latin America* (Washington, D.C.: Inter-American Development Bank, 2000).

<sup>84</sup> I discuss this in detail in the chapter on the Czech Republic in Graham (1998).

<sup>85</sup> We introduced this term in Graham, Grindle, Lora, and Seddon (2000).

instance take place as pilot programs within a particular ministry or agency, and are implemented primarily at the local level. If and when they are successful, they then can attain national attention (and national level implementation) precisely because their record takes away the most powerful weapon for critics of reforms – fear of uncertain outcomes.

Case in point is the CLAS health program in Peru. The CLAS (Comites Locales para la Administracion del Salud) were community run and administered boards set up to manage local health posts in rural Peru. The program began as a pilot and then expanded dramatically, covering approximately two-thirds of the rural health posts in Peru. The boards, which were supervised by the central ministry and composed of a ministry representative, a respected local doctor, and other locally elected officials, were fully responsible for management of health posts, including the administration of fees. Peruvians have always paid at least nominal fees for health services. The major change with CLAS is that instead of sending the fees back to the regional health offices and receiving a small percentage of them back, they kept all of the fees and managed and allocated them locally.

The CLAS were allowed to use the funds that they generated to purchase additional supplies and other necessary goods, as well as to hire additional workers – or pay existing public health workers for working more hours. A major problem prior to the CLAS was that the posts were only open for a few hours a day, and rural users would travel long distances at a very high cost (in terms of their time and relative income levels), only to find the posts closed and/or lacking drugs. In the areas where CLAS were implemented, local usage of health posts increased, and early studies find evidence of improvements in health indicators, such as infant mortality, in areas where the CLAS operate.<sup>86</sup>

Local public health workers, originally opposed to the program on job security grounds, soon became major supporters once they realized they could work many more hours and get paid. Thus local health workers, along with the users of health posts, became stakeholders, and thus an important new base of political support for the program. At present, there are many more villages requesting CLAS than the government is able (or willing) to implement.<sup>87</sup>

Among other things, three were essential to the success of the CLAS. The first of these was a major local level outreach program, to educate and inform rural people about the CLAS and to encourage health post usage. The second was the commitment of the minister of health at the time the reform was implemented, as there was much opposition, both within the ministry and at the regional health sector level. Finally, equally important was the fact that the CLAS did not get much publicity at the central level and/or enter into the national political debate.

President Fujimori, who feared devolving authority of any kind to the local level, may well have been opposed to the program had he known more about it. At the same time, privatization of social services had become a political “bete noir” in Peru due to the opposition’s campaign

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<sup>86</sup> See Patricia Paredes-Solari, “Shared Administration in Primary Health Care Facilities: The Case of Peru”, Johns Hopkins University, School of Hygiene and Public Health, Mimeo, 1995; and Carl E. Taylor, “Report to the Honorable Minister of Public Health of Peru: An Evaluation of CLAS”, Johns Hopkins University, January 2-15, 1996.

<sup>87</sup> I discuss the CLAS program in detail in the chapter on Peru in Graham (1998). The fate of the program during the political uncertainty in Peru since then is somewhat unclear.

against a voucher-based education proposal, which was modeled on Chile's reform. The opposition effectively focused on the poor state of rural schools in Chile, and the Fujimori government came close to losing a constitutional referendum over the education reform issue.<sup>88</sup> The government subsequently dropped the reform initiative for fear of continued political reverberations. The CLAS was implemented during this period and, given greater publicity, the opposition might have included it in its campaign in protest of "privatization" of social services.

The point here is not the particulars of the CLAS and/or other reforms, but rather that if and when political attitudes are fairly entrenched – and at times they may become more so in response to other even unrelated reform attempts, such as education in Peru – there are political "minefields" that policymakers should avoid. When and if that is the case, reform by stealth, on a quiet, pilot basis, is the most effective way to proceed. This again highlights the importance of policymakers being aware of the particulars of the political context at the moment, as well as of political attitudes more generally.

### **Conclusion**

The purpose of this paper has been to generate new thinking on the need for broader social contracts in Latin America, as well as to suggest strategies for navigating particular political economy contexts when crafting those contracts. It highlights the importance of public attitudes about the causes of poverty, about the distribution of opportunities, and about redistribution, among others. It posits that such attitudes are not only key to the current allocation of public expenditures among different cohorts, but that they are likely to influence the design and future direction of policies. While temporary and externally financed safety net programs can avoid these concerns more easily, social policies that form part of a longer term social contract must take them into account.

These attitudes will have particular relevance and importance for allocation issues. The usual focus of attention when discussing such issues is whether or not programs should be targeted or universal. While recognizing the importance of this distinction, this paper posits that deeply held public attitudes often require a broadening of this dichotomy to include other potential conflicts (or intersections) of interests between the near poor and the poor, the poor and the poorest; the working poor versus the non-working poor; the young versus the elderly, and formal versus the informal sector workers. In addition, institutional context may dictate other choices (or intersections) between central financed and implemented programs and more decentralized, demand-based ones.

In order for policymakers to incorporate public attitudes into the policy process, they need more and better instruments for assessing public opinion. This requires both supporting and strengthening ongoing efforts to measure public opinion. This is an area where the international institutions could play a major role in helping to generate and disseminate information, both within and across national boundaries.

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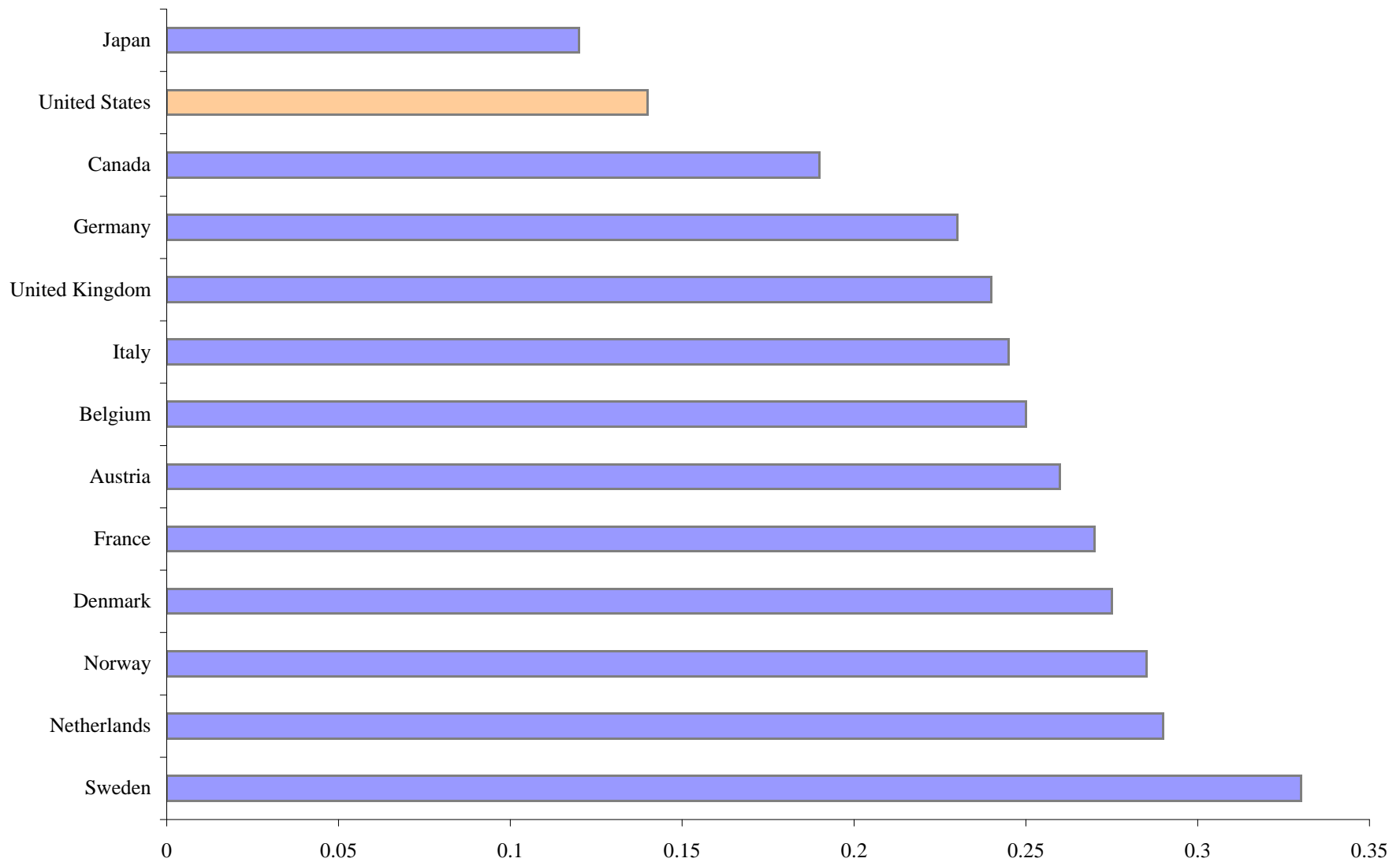
<sup>88</sup> There is debate over the effects of the voucher reform on poor rural schools in Chile, which were in a poor state even prior to reform. See Gauri (1999). Still, it made for a powerful political weapon for the Peruvian opposition.



Taking public attitudes into account has direct implications for reform implementation. In some contexts, clearly defined, bold, and rapid reform efforts are the most effective approach. In others, where public opinion is deeply entrenched and/or the subject of polemical political debates, reforms of social assistance or other social policies can have high political costs which can jeopardize broader macroeconomic efforts. In these cases, reform by “stealth”, which then gains public approval via the record of new policies and their demonstration effect, may be the only politically feasible strategy to begin crafting a broader and more inclusive set of social policies.

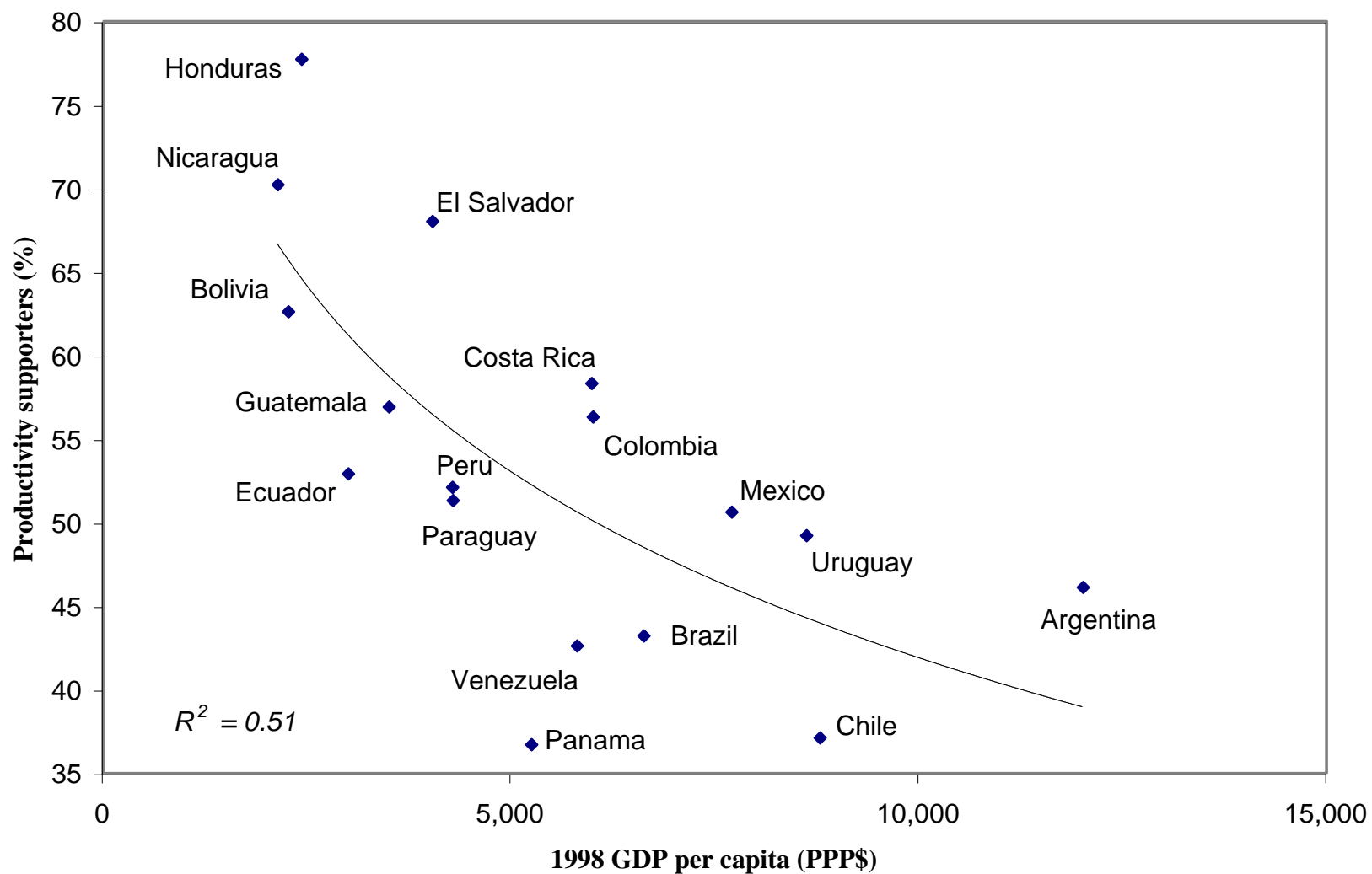
This paper also challenges the development banks to re-think their role in supporting social policies, to one which fosters domestic public debate and consensus building on the appropriate set of policies and on choices about allocation of expenditures among cohorts, rather than one of proposing particular policies. The outcomes in such a strategy will, no doubt, be heterogenous among countries. But they are also more likely to be fiscally and politically sustainable in the longer term than are externally designed and financed policies.

**Figure 1 Governmental Social Spending as a Percentage of GNP**



Source: Organization for Economic Cooperation and Development, *New Orientations in Social Policy*, pp. 59-60.

**Figure 2 . Productivity Supporters vs. GDP Per Capita  
Latin America, 1998**



<i>Dep.Var.: Happiness</i>				
	coeff.	z-stat	coeff.	z-stat
age	-0.042	-10.29	-0.054	-9.08
male	-0.143	-6.24	-0.126	-3.81
married	0.803	31.56	0.758	21.03
education	0.038	9.22	0.029	4.77
unemployment	-0.726	-10.72	-0.684	-6.80
retired	0.094	2.05	0.002	0.03
<i>Pseudo-R2</i>				
<i>Number of obs.</i>				

*Ordered logits with year dummies (coefficients not shown)*

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	<u>US</u>	<u>Germany</u>	<u>Italy</u>	<u>Britain</u>
How much responsibility does the government have for...				
Seeing to it that everyone who wants a job can have one?				
Essential Responsibility	34%	60%	79%	55%
Important Responsibility	37	34	15	31
Some Responsibility	24	6	5	13
No Responsibility	4	1	1	2
Providing good medical care?				
Essential Responsibility	42	63	79	74
Important Responsibility	36	32	16	21
Some Responsibility	20	6	4	5
No Responsibility	3	0	1	0
Looking after old people?				
Essential Responsibility	41	51	69	58
Important Responsibility	40	42	23	31
Some Responsibility	18	6	8	11
No Responsibility	1	1	1	1
Providing adequate housing?				
Essential Responsibility	25	39	69	61
Important Responsibility	38	46	22	27
Some Responsibility	32	14	7	12
No Responsibility	5	1	1	1

<i>Dep. Var.: Poverty Due to Lack of Jobs</i>		
	coeff.	z-stat
age	0.003	0.150
male	-0.279	-2.450
married	-0.043	-0.350
education	-0.077	-3.650
unemployment	0.389	0.980
political view	-0.169	-4.030
<i>Pseudo-R2</i>	<i>0.0394</i>	
<i>Number of obs.</i>	<i>1165</i>	

*Ordered logit estimates*

<i>Dep. Var.: Poverty Due to Lack of Effort</i>		
	coeff.	z-stat
age	0.015	0.71
male	-0.017	-0.15
married	0.124	0.97
education	-0.080	-3.68
unemployment	0.329	0.82
political view	0.167	3.86
<i>Pseudo-R2</i>	<i>0.0219</i>	
<i>Number of obs.</i>	<i>1170</i>	

*Ordered logit estimates*

<i>Dep. Var.: Poverty Due to Lack of Effort</i>			
	coeff.	z-stat	coeff.
age	-0.004	-0.53	-0.001
male	0.081	1.93	0.074
married	-0.061	-1.29	-0.077
wealth	0.353	3.21	0.210
year of education	-0.006	-0.93	-0.005
unemployment	-0.185	-2.06	-0.154
retired	0.050	0.48	0.073
political scale	0.051	5.50	0.047
happy	...	...	0.235

2017-2022



<i>Dep.Var.: Opportunties are Equally Shared</i>					
	coeff.	z-stat	coeff.	z-stat	coeff.
age	-0.023	-3.29	-0.023	-3.37	-0.019
year of education	-0.012	-2.21	-0.007	-1.35	-0.016
male	0.022	0.58	0.023	0.60	0.040
married	0.048	1.13	0.045	1.05	0.080
unemployment	0.015	0.19	0.004	0.05	0.034
retired	0.125	1.36	0.125	1.36	0.098
wealth	0.475	4.68	...	...	0.416
<i>Pseudo-R2</i>					
<i>Number of obs.</i>					

\* Ordered logit estimations with country dummies (not shown).

**Table 6**

	<b>Social Spending/ GPD</b>		<b>Social Spending/total public expenditure</b>	
	<b>1990-1991</b>	<b>1996-1997</b>	<b>1990-1991</b>	<b>1996-1997</b>
Argentina	17.7	17.9	62.2	65.1
Bolivia	6.0	12.0	25.8	44.2
Brazil	19.0	19.8	59.5	59.1
Chile	13.0	14.1	60.8	65.9
Colombia	8.1	14.3	29.7	38.2
El Salvador	5.4	7.7	21.9	26.5
Guatemala	3.3	4.2	29.8	42.1
Honduras	7.8	7.2	33.1	31.9
Mexico	6.5	8.5	41.6	52.9
Panama	18.6	21.9	40.0	39.9
Paraguay	3.0	7.9	39.9	47.1
Peru	2.3	5.8	16.7	40.9
Dominican Republic	4.5	6.0	36.9	39.0
Uruguay	18.7	22.5	62.3	69.8
Venezuela	9.0	8.4	33.9	39.0

<u>Country</u>	<u>Mean</u>	<u>Std. Dev.</u>	<u>Freq.</u>
Argentina	0.141	0.348	1187
Bolivia	0.211	0.408	1057
Brasil	0.147	0.354	979
Colombia	0.227	0.419	1183
Costa Ric	0.290	0.454	987
Chile	0.216	0.412	1171
Ecuador	0.242	0.429	1160
El Salvad	0.259	0.439	987
Guatemala	0.294	0.456	975
Honduras	0.322	0.467	994
México	0.309	0.462	1182
Nicaragua	0.217	0.413	989
Panamá	0.238	0.426	981
Paraguay	0.281	0.450	602
Perú	0.254	0.436	1031
Uruguay	0.250	0.433	1167
Venezuela	0.507	0.500	1142
<b>Total</b>	<b>0.259</b>	<b>0.438</b>	<b>17774</b>

<u>Country</u>	<u>Mean</u>	<u>Std. Dev.</u>	<u>Freq.</u>
Argentina	0.617	0.394	914
Bolivia	0.656	0.343	955
Brasil	0.677	0.381	829
Colombia	0.709	0.333	1049
Costa Ric	0.661	0.371	818
Chile	0.598	0.375	933
Ecuador	0.752	0.315	1084
El Salvad	0.545	0.375	768
Guatemala	0.685	0.352	878
Honduras	0.643	0.372	877
México	0.561	0.355	979
Nicaragua	0.720	0.344	799
Panamá	0.612	0.362	895
Paraguay	0.725	0.348	564
Perú	0.738	0.310	944
Uruguay	0.546	0.367	569
Venezuela	0.732	0.355	1032
<b>Total</b>	<b>0.661</b>	<b>0.361</b>	<b>14887</b>