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Consumption and Social Welfare Politics: The Effect of Credit and China

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ABSTRACT

Analyzing data from 20 OECD countries over the period of 1995-2007, the present article investigates whether the factors that contributed to households' consumption opportunities have had any impact on the way governments in advanced societies respond to income inequalities. In addressing this question, the article particularly focuses on access to credit, and low-wage imports, from China in particular, as two mechanisms that have contributed to an increase in household consumption opportunities. The results show a highly significant inverse relation between these two factors and social welfare effort. As imports from China and availability of credit increase, the social welfare effort seems to decrease. These findings prompt us to think beyond the established arguments about progressive politics in the neoliberal era. The article also contributes to the burgeoning literature on the political and social implications of credit expansion, and of the rise of China in world trade.

I. INTRODUCTION

Income inequality has increased substantially in advanced nations over the past few decades, particularly in the liberal market economies (Kenworthy and Pontusson 2005; Krueger and Perri 2006; OECD 2008; Bartels 2009). For many intellectuals and policymakers this constitutes an inherently undemocratic trend, which needs to be countered with augmented social welfare effort in the form of social spending, and/or progressive taxation (Krugman 2007; Bartels 2009). Others meanwhile argue that worries about income inequality and calls for progressive politics remain unwarranted, for what matters is the actual material welfare of citizens, which, they argue, has increased across the board (Slesnick 2001; Nye 2002; Wilkinson 2009). According to this latter view, the increase in consumption opportunities among middle and lower income households implies redistribution of living standards, which in turn makes redistribution of income a lesser deal as a social and political objective.

The purpose of this article is not to normatively engage with these ideas, which happen to animate heated debates in the worlds of scholarship, advocacy and policymaking. The goal here is to examine empirically whether this so-called material welfare that comes with increasing consumption opportunities—what one might call the "consumer welfare"—has any bearing on the governments' response to inequalities in income distribution. To be more precise, we would like to know if there is an inverse relationship between consumer welfare and social welfare effort.

There are reasons to think that this might indeed be the case. Referring specifically to the US where income inequality has been especially rampant over the past few decades, Rajan (2010) has argued that although politicians have recognized the problem posed by rising inequality, they have not addressed it through social spending or taxation. Growing inequalities have rather been dealt with through mechanisms—"easy credit" in particular—that allowed middle-class households to sustain their levels of consumption (Rajan 2010:31). Enacting real policy change in an area where too many vested interests favor the *status qu*o would be hard, and would require years to take effect, not really resolving the electorate's current anxiety," whereas consumption has offered a quicker way to "mollify the constituents" (Rajan 2010:8). In short, "whether carefully planned or an unpremeditated reaction to constituent demands," Rajan argues, the political response to rising inequality and job insecurity has been to support the mechanisms that would allow households to keep up their consumption (2010:8-9).

One might say that this new politics shaped around consumption offered a convenient way to reconcile what seemed irreconcilable—that is, markets and equality. Markets seemed to bring individuals and households closer in consumption, even if not in income. As consumption has increased, and begun to follow a somewhat more equal pattern across income groups, inequalities in income distribution have become somewhat less conspicuous.[1]

To date, there has not been an empirical analysis of whether the factors that contributed to increases in households' consumption opportunities have had any bearing on the way governments in advanced societies respond to income inequality. Analyzing data from 20 OECD countries over the period 1995-2007 we investigate this question. In doing so, we particularly focus on "access to credit" and "imports from China" as two mechanisms that have boosted citizens' access to consumption. Is it possible, we ask, that high level of consumer welfare resulting from access to credit, and access to highly affordable imported products from outside the OECD zone, from China in particular, has been a political substitute for social welfare effort

[1]The jury is out on the question of whether consumption inequality has actually increased, stayed stable, or decreased, and how much it has done so. However, there seems to be a general consensus that consumption inequality has remained much less pronounced than income inequality (Cutler and Katz 1992; Krueger and Perri 2006; Johnson, Smeeding, and Torrey, 2005; Meyer and Sullivan 2010).

in the form of social spending and taxation? Could it be that "redistribution of living standards" has rendered "redistribution of income" less salient in the political-economic equation of advanced societies? The results of the present analysis seem to provide support for this view. Access to credit availability and access to cheap imports from China—factors that have contributed to expansion in consumption opportunities—show a highly significant inverse relationship with social welfare effort, and that this holds true when controlling for a range of political, economic, and social variables, as well as unobservable country-specific effects.

These findings prompt us to think anew about the factors that shaped the way progressive politics played out in advanced societies over the past fifteen years or so. They suggest that in the recent neoliberal era, politics of redistribution and welfare has had to do with consumption as well. What this means at the very least is that our discussions of why redistribution has been least available where and when it has been most needed (Lindert 2004), or how governments in advanced nations have actually managed to undertake retrenchment politics in the face of increasing public need and demand for various redistributive and social programs, should start involving consumption-related factors.

In what follows, we first outline the theoretical framework. The third section provides detailed information about the data, discusses the methodology used, and provides empirical findings. The article concludes by briefly discussing the implications of the findings for theory and politics.

II. THEORETICAL FRAMEWORK

On February 10, 2008 two Federal Reserve economists, Michael Cox and Richard Alm, published an op-ed piece in the *New York Times* with the title "You are what you spend." There, they argued that the renewed attention being given to the gap between the haves and have-nots in

America is misdirected as it is focused on the wrong measurement of financial well-being: income statistics. Income statistics, Cox and Alm argued, "don't tell the whole story of Americans' living standards." A far more direct measure of American families' economic status, they argued, is household consumption, which shows that "the gap between rich and poor is far less than most assume." Cox and Alm were not the first to make this argument. Indeed, this consumption-based view of welfare had been rather popular among libertarian circles for some time. Irving Kristol (1997) had made a similar point about a decade ago in the *Wall Street Journal* in his essay "Income Inequality without Class Conflict." On the academic front Slesnick (2001) had argued that switching the focus to consumption trends leads to an entirely different, and much more optimistic, picture of the growth of living standards and the decrease in inequality and poverty in the US. More recently, the same argument that "the dispersion of incomes at any given time has, at best, a tenuous connection to human welfare or social justice" was picked up by Wilkinson[2] (2009). Wilkinson argued that to get an accurate picture of overall material well-being, what we really should be looking at is the quantity of goods and services a person is able to consume, and the value to that person of all those goods and services. "Fixating on income inequality," he noted, "may have caused us to miss one of the biggest stories of modern times: America may have become materially more equal, and no one noticed (2009:4)."

Here, we coin the term "consumer welfare" to refer to this view of wellbeing which takes material standards of living as a reference point. This is very different from social welfare, at the heart of which are several core principles: (1) that citizens will be insured against economic risks and insecurities (insurance); (2) that there will be mechanisms in place to decrease their dependence on markets (decommodification); and (3) that the distance between the poor and the rich in a society will not get too wide (redistribution).

[2] Will Wilkinson is the current director of the libertarian Cato Institute in Washington, DC.

As stated before, the purpose of this article is not to discuss normatively whether consumption could be a viable substitute for social welfare, or whether trends in consumption are what we have to care about rather than trends in income distribution. What this article is interested in investigating is a rather straightforward empirical question: are these trends related? Is there a relationship—an inverse relationship, to be more precise—between factors that have led to increasing consumption opportunities for lower and middle class households and the way governments have dealt with income inequalities? Although there is a vast literature dedicated to explaining why governments intervene in market-driven inequalities in such different degrees and ways, the questions specified in this article have not been investigated.

In the existing literature, one line of thought—*the power resources approach*— has emphasized the role of labor unions and left parties in driving social welfare effort (Stephens 1979; Korpi 1983, 1989, 2006; Esping-Andersen 1990; Hicks and Swank 1992; Huber and Stephens 2001; Kwon and Pontusson 2005). Another line of thought—*the median voter approach*— has argued that it is the high levels of earnings inequality that fuel demand for redistribution (Meltzer and Richard 1981; Perotti 1996; Milanovic 2000; Moene and Wallerstein 2001, 2003). [3] A third line of scholarship linked social welfare effort to economic openness. Scholars who see this relationship from a *compensation perspective* have argued that the states redistribute wealth and risk so as to cushion the dislocations triggered by economic openness (Rodrik 1998; Garrett 1998; Barr 1998, 2003). Scholars who view this relationship from an *efficiency perspective* on the other hand have argued that economic openness and social welfare effort are negatively

[3] Empirical evidence does not allow for a clear consensus on this thesis. While some scholars provide evidence in favour of this argument (Milanovic 2000), others show that income inequality is negatively associated with redistributive effort: the more unequal is the primary income distribution, the less support is there for the poor (Moffitt et.al. 1998; Perotti 1996; Lindert 199; Alesina and Glaeser 2004; Moene and Wallerstein 2001).

associated. They have argued that competitive pressures posed by economic integration make it impossible to sustain social welfare effort (Huber and Stephens 2001). [4]

It has also been argued that shifts in the sectoral occupational structure might trigger more social welfare effort on the part of the government. In this vein, Iversen and Cusack (2000) highlighted the role of labor market dislocations associated with deindustrialization in the expansion of social welfare effort in the 1960s and 1970s[5].

During the last two decades, in the context of economic changes, political shifts to the right, and rising costs associated with demographic shifts, it has become common place to acknowledge the challenges that mature welfare states are facing, and the prospect for extended austerity. In this context, various scholars, most notably Pierson (1996) questioned the usefulness of earlier theories that were designed to explain the expansion in social welfare effort in accounting for the austerity politics that contemporary welfare states remain subject to. Following Pierson's seminal work, the focus of the literature has shifted to some degree to explaining to what extent and how governments remain able to implement retrenchment policies that remain rather unpopular with the public.

This article contributes new insights into these questions by examining whether those factors that have increased the consumption opportunities of lower income households had any bearing on

[4] Other scholars yet take a more balanced approach (Hicks 1999; Brady 2005; Brady, Beckfield and Seelib-Keiser 2005). Hicks (1999), for instance, argues that globalization's effect on welfare states is curvilinear[4], and Brady(2005) argues that "globalization does not have one overall effect on the welfare state, and what effect it has are most certainly relatively small" (p.945). For further discussion see also Genschel (2002); Wibbels and Arce (2003); Mosley (2000); Brady, Beckfield and Zhan (2007).

[5] In deeming deindustrialization and the decline of the blue-color working class responsible for welfare development, Iversen and Cusack (2000) also challenge the power resources theory, which associates welfare growth with the organizational or legislative strength of labor.

the changing politics of social welfare. Is it possible that the increasing consumption opportunities, by way of moderating the effects of real income inequalities, have affected governments' drive to redistribute?

The starting point of such an analysis must be to specify the factors that have increased lower and middle income households consumption capacities over the past few decades. We posit here that two factors[6] have been particularly operative in this regard over the past fifteen years or so: (1) households' access to credit, which has substantially increased since the early 1990s, albeit to different degrees in different nations; (2) households' access to low-wage imports from outside the OECD zone—notably from China, which has brought down the prices of a range of products that constitute a large portion of household consumption. Let me explain.

ACCESS TO CREDIT

One of the most distinct features of the last few decades of capitalist development in advanced countries has been the expansion in households' access to credit. In the US, credit had been central to the maintenance of middle-class Americans' living standards since the end of the Second World War (Logemann 2007; Trumbull 2010). In recent decades, however, this role has become even more pronounced. The socio-economic base of credit usage has expanded tremendously.[7] This recent increase in use of credit has occurred in tandem with the increase in income inequality, as Krueger and Perri (2006) have shown. As different types of credit with varying characteristics have become available, households, especially lower and middle-class

[6] This is not to say that these two factors are the only ones that matter. Other scholars might suggest other factors and mechanisms to play a role in increasing lower and middle class households' consumption opportunities.

[7] The widening in the socio-economic base of credit usage is often described as part of a "democratization of finance." This implies that access to credit, which has been a privilege of only a certain part of the population (i.e., white, upper and middle classes), has now become available to a large part of the population.

households, have increasingly turned to these financing tools to enjoy consumption opportunities that would have not been available otherwise (Krugman 2007).

This trend of increasing credit usage has not necessarily remained an American phenomenon. As Rajan (2010) argues, since the early 1990s, "easy credit" has emerged, in other rich countries as well, as a "seductive" way of improving the material lives of voters whose income distribution was getting increasingly unequal. This has happened at varying degrees, as shown in Figure 1 with the increase in household loans included as part of GDP across the advanced countries between 1995 and 2007.

Figure 1 here

Recently, economic sociologists and political economists have begun to offer important theoretical and empirical insights into the causes and implications of credit use for socio-economic processes. Crouch (2009), for instance, has argued that excessive credit use over the last two or three decades must be seen as the rise of "privatised Keynesianism"—a policy regime whereby households and individuals, rather than governments, take up debt so as to stimulate the economy and create economic stability. Schwartz and Seabrooke (2008) have talked about "housing and the welfare trade off," discussing how residential property ownership interacts with welfare regimes. Prasad (2010) in a similar framework, and taking a more historical perspective, asked if there is a "credit-welfare tradeoff" in advanced nations.

This article contributes to this recent body of work by inquiring whether credit, through its effect on consumer welfare, has any implications for the way governments dealt with income inequalities. We hypothesize that *household access to credit* has an inverse relationship with social welfare effort.

Hypothesis 1: As access to credit increases, social welfare effort decreases.

LOW-WAGE IMPORTS AND "MADE IN CHINA"

The second factor that has increased households' consumption opportunities, arguably, is the continuous decrease in price of a wide range of products that households use. It is a well-known argument[8] that many products that until only recently were affordable only to the mega-rich are now enjoyed by households even in lower-income brackets in today's advanced nations (Nye 2002). According to the Montgomery Ward catalog for instance, while it took 260 hours for an average worker to earn a one-speed bike in 1895, in 2000 it took only 7.2 hours. While buying a hundred-piece dinner set meant 44 hours of labor for an average worker in 1895, in 2000 it was only a matter of 3.6 hours.

While the downward trend in the prices of goods that make up a large portion of household consumption has been an ongoing trend for some time, thanks largely to technological advances, advanced nations have seen an overflow in the availability of highly affordable consumer products in the past two decades. Recent research has noted the role of low-wage imports—China's rapid export expansion, in particular—as a major source of the decline in the aggregate price of trade manufactures recorded by the IMF after the mid-1990s, seen in Figure 2 (Lai 2004; Zhang and Kaplinsky 2006; Fu and Gong 2008; Villoria 2009; Auer et al. 2011).

Thanks to its low-cost labor and sustained productivity growth, China has become the world's factory floor. The share of advanced country imports accounted for by China has risen substantially over the last two decades, with particularly sharp increases since the early 1990s in Japan, the United States, and the European Union (Rumbaugh and Blancher 2004). As Table 1 shows, while in 1980, China accounted for only 0.5 percent of all US imports, this number was up to 11 percent by 2002. In the same period China's share in total world exports increased approximately four times (Rodrik 2006).

[8] This argument often animates discussions of poverty and inequality in libertarian circles.

Figure 2 and Table 1 here

This article posits that low-wage imports—from China, in particular—increased the affordability of a large range of products, increasing as a result lower and middle income households' access to consumption. The rise in the share of OECD imports accounted by low-wage countries and China must thus be considered as a factor which has moderated the effects of real income inequalities. We posit that this might have had consequences for the way governments in advanced nations have dealt with rising income inequalities.

Hypothesis 2: As countries' imports from low-wage countries and China increase, social welfare effort decreases.

As briefly discussed in the preceding section, international trade-social welfare nexus has been studied extensively, although the impact of China, specifically, has not been addressed. Scholars who view this relationship from an efficiency perspective predict an inverse relationship between low-wage imports and social welfare effort arguing that competition from low-wage countries makes it difficult for nations to support generous social policies. Those who view this relationship from a compensation perspective, on the other hand, predict a positive relationship arguing that low-wage competition undercuts the market position of low-skilled workers in advanced countries, spurring demand for compensation. Our expectations of the direction of the relationship between low-wage imports and social welfare effort remain in line with the latter of these two approaches. Our logic of inference, however, differs. We hypothesize that low-wage imports remain inversely related to social spending and are redistributive not because of efficiency/competition reasons, but because they contribute to an increase in the consumption opportunities of households; as a result real income inequalities become less conspicuous, and the political consequence of not responding to those real income inequalities becomes less taxing, electorally speaking.

III. EMPIRICAL ANALYSIS

METHODOLOGICAL ISSUES

For this article a panel data analysis was conducted to examine the relationship between the main explanatory variables of interest—namely, access to credit, and access to “made in China”—and the dependent variable, social welfare effort. The analysis involves data from 20 OECD countries for the period of 1995-2007. The units of observation of dependent and independent variables are the country-years.

Panel data analysis offers many well-known benefits for political economic inquiries of a comparative nature. Mainly, it increases the total number of observations and the degrees of freedom, allowing for estimation of more fully specified models, and makes it possible to examine the observed variance across space and time (Plumper, Troeger and Manow 2005). On the other hand, it presents several statistical challenges—most notably, that of autocorrelation and heteroskedasticity in the error term. Following Beck and Katz (1995), this study calculated panel-corrected standard errors to circumvent the problem of heteroskedasticity. Potential autocorrelation problems have been addressed by allowing for an AR (1) structure in the error term.[9]

[9] Following Beck and Katz (1995), the inclusion of a lagged dependent variable to the right side of the equation has become a common way of dealing with autocorrelation. We do not follow this approach here, for several reasons. First, our time span is rather short (thirteen years), which renders inclusion of a lagged dependent variable rather problematic. Second, the inclusion of a lagged dependent variable runs the risk of suppressing the power of other independent variables. Achen (2000) and Plumper et al. (2005) discuss this issue extensively, demonstrating how lagged dependent variables may “dominate a regression.” To avoid the outcome that a significant part of the trend in the dependent variable would be absorbed, although not

To help isolate the relationship between the main explanatory variables and the dependent variable, this article includes in its analysis several control variables derived from the literature, namely: left party power, union density, elderly as a percentage of total population, economic openness (measured in terms of financial as well as trade openness), economic growth rate, share of manufacturing in total employment, rate of unemployment, budget deficit, and gross income inequality. This article also includes dummy variables for each of the countries in the dataset, so as to reduce the omitted variable bias that would occur due to unobservable country effects.

The main structural equation takes the following general form:

$$\mathbf{Y}_{it} = \boldsymbol{\beta}_1\mathbf{CREDIT}_{it} + \boldsymbol{\beta}_2\mathbf{CHINA}_{it} + \boldsymbol{\lambda}\mathbf{Z}_{it} + \boldsymbol{f}_i + \boldsymbol{\mu}_{it}$$

In this equation, Y is the dependent variable, social welfare effort; the β's are parameter estimates; the subscripts i and t denote the country and year of observations; access to credit "CREDIT," and access to Chinese imports "CHINA" are the primary explanatory variables of interest; Z_{it} contains the exogenous controls; f_i represents country-specific fixed effects, and μ is the error term.

Two of the variables included on the right hand side of the equation may be suspected of being endogenous to social spending and redistribution: budget deficit and income inequality. We do not believe that this poses a problem for this analysis, however. First of all, the concern in this article is not with accurately measuring the impact of any these factors on social welfare effort. These are merely control variables. Their endogeneity would only matter if they altered the results, which is not the case here. Moreover, the inequality variable (gross GINI) that we

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explained, by the lagged dependent variable, we chose to address the potential autocorrelation problems by estimating a panel-specific AR (1) model.

included in the analysis captures the distribution of market income—that is, income before taxes and social spending, which in effect is exogenous to both spending and redistributive effort.

DESCRIPTION OF DATA AND VARIABLES

Dependent Variable: Social Welfare Effort

This study measures *social welfare effort* primarily in terms of social transfers as a percentage of GDP. The data comes from the widely-used comparative political data set compiled by Armingeon et al. (2010). The study uses two alternative measures. The first of these is the total public and mandatory private social expenditure as a percentage of GDP, which also comes from Armingeon et al. (2010). The second one is a degree of redistribution variable, calculated from Solt's (2009) gross and net GINI measures. Solt's gross GINI measure captures the distribution of market incomes, whereas the net GINI measure captures income distribution after social transfers and taxes. To calculate the degree of redistribution in a nation in a given year, the difference between gross and net GINI values is divided by gross GINI so that nations' actual redistributive efforts can be measured in proportion to the initial inequality level observed in the distribution of market income.

Primary Explanatory Variables of Interest:

Household Access to Credit

Following Prasad (2010), this study calculated *household access to credit* using OECD's net lending/net borrowing in the household sector data and inverting the negative and positive values. This variable essentially captures households' credit-based net debt. As an alternative measure, the study used OECD data on short-term credit, which includes household loans up to one year.[10]

[10] This measure includes various forms of short-term consumer credit, including credit card debts.

Household Access to Low-wage Imports and "Made in China"

This study measured households' *access to "made in China"* products in terms of China's exports to individual countries as a percentage of the importing country's GDP. The data comes from IMF's Direction of Trade (DOT) statistics. The study also uses the more comprehensive variable of *low-wage imports* that measures the ratio to GDP of low-wage imports to individual countries. The data comes from OECD's bilateral trade statistics. It measures imports from non-OECD countries excluding OPEC countries and Saudi Arabia.

Consumer Welfare

Although the study runs regressions separately on both credit and China variables, it seems conceptually convenient for the purposes of the present article to have an aggregated *consumer welfare* variable that measures both of these variables at the same time; so a compound consumer welfare variable was constructed out of these two variables. In order to do this, both variables were first converted into standardized *z* scores. Then the average value was calculated and standardized. The unit of measurement for the consumer welfare variable, hence, is the standard deviation.

Control Variables:

Left Party Power and Union Density

As discussed before, the power resources theory sees social welfare effort as a function of working-class power. Thus, *union density* and *left party power* variables were included in the analysis as control variables. The data for both of these variables come from Armingeon et al. (2010).

Economic Openness

The economic openness variables also come from Armingeon et al. (2010). One of these variables, *kaopen*, measures the extent of openness in capital account transactions, while the other one, *openc*, measures the openness of the economy in current prices, measured as total trade (sum of import and export) as a percentage of GDP.

Share of Manufacturing in Total Employment

The study includes the *share of manufacturing in total employment* as a control variable. This is for two reasons. First, the sectoral composition of the economy might matter for social welfare effort. Second, following Iversen and Cusack (2000), changes in the manufacturing's share of employment might play an especially important role, and must thus be controlled for.[11]

Gross GINI

Following the median voter theory which sees social welfare effort to depend in part on the distribution of market incomes, an inequality variable (gross GINI) was included in the analysis. The data for this comes from Solt's (2009) Standardized World Income Inequality Database. It measures the distribution of market income—that is, income before taxes and social transfers.

Economic Growth, the Rate of Unemployment, Budget Deficit, and Percent Elderly

The data on economic growth, rate of unemployment, budget deficit, and percentage of elderly in the total population all come from Armingeon et al. (2010). *Economic growth* is measured in terms of the growth of real GDP (percentage change from previous year). *Rate of employment* is

[11] We should note that in accounting for the role of deindustrialization, Iversen and Cusack (2000) do not simply use data on manufacturing's share in total employment, as we do here. Their argument is that labor market dislocations associated with major shifts in the sectoral occupational structure between the 1960s and 1990s remained a driving force in expansion of transfers and social spending. Accordingly, their measurement takes into account percentage of the population employed in both the agricultural and industrial sectors over all the active age population. Our argument, however, is not about welfare expansion in the post-1960s era, but about recent changes. We do not think that factors such as the drastically changing size of the agricultural labor force are as relevant to our time frame and question as it is to Iversen and Cusack (2000).

measured as a percentage of the civilian labor force. *Budget deficit* measures annual deficit (government primary balance) as a percentage of GDP. And finally, *percent elderly* measures population 65 and over as a percentage of the total population.

RESULTS

The regression results on which the present analysis rests provide Prais-Winsten coefficients with panel-corrected standard errors. The findings provide support for the two hypotheses outlined in the previous pages regarding the consumer welfare-social welfare relationship. Access to credit, and access to "made in China"—factors that have contributed to an expansion in households' consumption opportunities—seem to have had a bearing on the politics of welfare and redistribution in the neoliberal era. Figure 3 provides a basic scatter plot to display the negative association between consumer welfare and social welfare effort.

Figure 3 here

Regressions in Table 2 examine whether this relationship holds when controlling for other theoretically relevant factors. The dependent variable in Column 1 is the social welfare effort measured in terms of social security transfers as a percentage of GDP. Controlling for political influence variables, economic openness variables, economic growth rate, rate of unemployment, share of manufacturing in total employment, and percent elderly, the results indicate that consumer welfare displays a highly significant negative association with social welfare effort ($p=.000$). A one standard deviation increase in consumer welfare is associated with a .62 percent increase in the social welfare effort. In Column 2 the study includes the inequality (gross GINI) and deficit variables in the model. We also include dummy variables for each of the countries in the data set, although the study does not report the coefficient estimates for these variables. Country dummies account for a significant portion of the variance. After their inclusion the adjusted R-squared goes up by a substantial 8 percentage points. This is not surprising given the large importance of country-specific effects such as history and culture. Nevertheless, despite the strong effects of the control variables, including country-specific effects, consumer welfare still displays a highly significant (p=0.000) effect on the social welfare effort—although its substantive effect decreases slightly.

Table 2 here

To check the stability of this finding, we re-estimate the same model using alternative measures of the dependent variable. In Column 3 we measure social welfare effort in terms of total public and mandatory private social expenditure as a percentage of GDP, and in Column 4 social welfare effort is measured in terms of the degree of redistribution. The results reinforce the statistical patterns found in the previous two exercises regarding the consumer welfare-social welfare link. Consumer welfare displays a significant association with social expenditure as a percentage of GDP (p=0.035) and redistribution (p=0.007). For an increase of one standard deviation in consumer welfare, social expenditure increases .38 percent, and redistributive effort increases .72 percent.

Looking across Table 2, unemployment, percent elderly, trade, and manufacturing employment consistently display a highly significant relationship with social welfare effort as well. The effect of manufacturing employment on social welfare effort seems to be negative. This is in line with the predictions of Iversen and Cusack (2000). The effect of trade on social welfare effort consistently turns up highly significant as well. The direction of the relationship here is in line with the efficiency thesis, which expects to see a negative relationship.

Table 3 indicates whether the two main explanatory variables of interest—namely, households' access to credit and households' access to low-wage imports—have any effect on social welfare effort. In Column 1 we examine this question including the full set of control variables but excluding the country fixed-effects. The dependent variable is measured in terms of social security transfers as a percentage of GDP. If Hypothesis 1 holds, then it follows that access to credit has a negative effect on the social welfare effort. Likewise, if Hypothesis 2 holds, then it follows that access to "made in China" has a negative effect on the social welfare effort. This is indeed the case. Both variables display a significant negative association with the social welfare effort at p=0.04 and p=0.002 levels respectively.

Table 3 here

In Column 2 we re-estimate the same model, this time including the country-specific effects. Access to "made in China" still displays a highly significant relationship with the social welfare effort at p=0.003 level. The effect of access to credit on social welfare effort, however, seems to have diminished somewhat after the inclusion of country-specific effects (p=0.059).

In Column 3, we re-estimate the same model replacing the access to "made in China" variable with access to low-wage imports. A highly significant negative relationship appears between low-wage imports and social welfare effort; but the effect of low-wage imports is not quite as strong as the effect of the access to "made in China" variable. This is not entirely surprising. Other research has shown that not all low-wage imports have the same effect. Auer (2010) shows, for instance, that low-wage competition has strong price effects, but this is largely driven by Chinese exports. According to Auer (2010) when Chinese exporters capture 1% of European market share, producer prices decrease about 2%, whereas no such effect is present for import competition from low-wage countries in Central and Eastern Europe.

In Column 4 we replace the access to credit variable with short-term credit—that includes household loans up to one year. Consistent with the previous results, short-term credit has a negative relationship with social welfare effort; however, the statistical effect is borderline significant with $p=0.098$.

IV. DISCUSSION

As Pierson (1996) and Brady et al. (2005) note, the causal factors that shaped social welfare politics earlier—most notably in the period of welfare expansion after the Second World War—cannot be expected to fully explain social welfare politics today. To make sense of the contemporary politics of social welfare, it is important to take into account the factors that have drastically changed the way capitalist economies function in more recent periods. By examining the welfare and redistributive effects of credit expansion and China's export-oriented growth, this article has made an attempt in that direction. It has offered a new way of thinking about social welfare politics that go beyond the existing arguments about the strength of social democratic parties, median voter preferences, demographic challenges, or globalization variables.

Looking into the linkages between consumer welfare and social welfare effort, which might not appear so intuitive at first, may help to shed new light on some of the prevailing puzzles in political science. Why has social welfare effort remained the least in places where it has been needed the most over the last few decades? Why is it that despite rampant inequalities in the US over the past twenty years, there has not been a decisive attempt to counter these trends through spending and taxation, and why has public support for such policies remained rather limited still? The investigation of 20 OECD countries from 1995 to 2007 suggests that the answer to these questions might have something to do with consumption patterns.

This analysis has shown that consumer welfare is inversely related to social welfare effort, and that this relationship holds true when controlling for a variety of factors including country-specific effects. Our interpretation of these results is that those factors, such as access to credit and low-wage imports, which allowed lower and middle-class households to keep up their consumption, in other words, material welfare, might have lessened the salience of the increasingly stagnant paychecks and economic insecurities, and diminish the political urgency for policymakers to respond to them.

The suggestion here is not that these factors have actually decreased the relevance of the income inequality question in rich societies. This argument, which has been made time and again by libertarian economists and neoliberal politicians, sees inequality, as Crouch (2011) notes, only in terms of consumption and ignores the long-term consequences of widening income disparities for democracy, social trust, and power dynamics in society. It also obliterates the role of state intervention in dealing with these socio-economic issues. However, instead of discussing the inherent problems of this argument, the article focuses on observable effects. It argues that in order to make sense of contemporary politics of social welfare—to explain, for instance, how it is that in the face of rising inequalities, social welfare effort has remained stagnant, if not declined, in most advanced societies—it is necessary to look into consumption also.

Admittedly, the article fails to provide a full account of the consumer welfare / social welfare nexus. What exactly is the mechanism here, one might legitimately ask. While we are not pursuing this question empirically in this article, we argue that there are two possible mechanisms in place linking consumption and social welfare.

First, it might be that policymakers in advanced countries have increasingly embraced, in different degrees, this particular view of social welfare, which sees inequality merely as a matter of consumption. In other words, in the past decade or so policymakers might have come to believe that in the rich societies which they govern, income disparities do not matter anymore because the great majority is materially well off. Crouch (2011) notes, for instance, that previous British Prime Minister Tony Blair held this view, and expressed it frequently.

Another possible mechanism might be the changing attitudes to inequality among the electorate. The increase in household consumption opportunities, due to factors such as increasing access to credit and to products “made in China,” might have had an impact on how individuals themselves view questions of inequality and social welfare, and this in turn might have affected societal demand for social welfare effort. Although the space and data limitations of this article do not allow an examination of these specific underlying mechanisms, it is important to note that such mechanisms might be operative.

Although this analysis has been limited to explaining politics of social welfare in the neoliberal era, the findings suggest revisiting existing knowledge of the historical development of welfare systems, and their categorical differences as they are described in the “three worlds of welfare capitalism” thesis. In these comparative models, the US, along with several other liberal market economies, is depicted as a residual welfare state that does relatively so little by way of social security provision, redistribution and decommodification. This characterization stands accurate on many accounts. In terms of social spending as a percentage of GDP, the American welfare state happens to be smaller by comparison to the other advanced countries. Various surveys about people’s attitudes towards welfare have also shown that Americans are much less willing to redistribute from the rich to the poor than Europeans. Nevertheless, the differences between welfare regimes might be running deeper than this characterization suggests. From its early origins onwards, the exceptionalism of the American welfare state lay not simply in its meager spending in comparison to other advanced nations but in the fact that redistribution of living standards rather than redistribution of income has remained its main organizing logic. It might make more sense, therefore, to characterize the American welfare regime as a consumer welfare regime, rather than a residual social welfare regime. The early development of the credit system in the US and its role in creating material affluence for working citizens must be considered carefully vis-à-vis the un-development of generous social welfare policy. Several scholars have already started to contribute to our comparative understandings of social welfare regimes along these lines (Logemann 2007; Trumbull 2010; Prasad 2010). This is all to say that at the very least, we should think more closely about the historical linkages between the political economy of consumption and political economy of social welfare.

Finally, a few words must be said about the "made in China" effect found here. There is an interesting literature developing around the question of China's influence on the political economy of advanced and developing countries. A part of this literature established that China has played an important role in bringing consumer prices down in OECD countries. This article expanded on this scholarship. We argued that China has increased households' access to affordable products, albeit in different degrees in different nations depending on the level of trade, and this has had consequences for social welfare politics,. More specifically, by making it possible for lower and middle class households to continue having access to a large range of products despite their shrinking returns from the labor market, China helped moderate the effects of real income inequalities. What this means is that China's export-oriented growth might have indirectly been one of the reasons why governments in advanced nations could actually avoid dealing with rising inequalities through social spending and/or taxation. Indeed, the effect of China is likely to stretch further, given that China today is the biggest financier of debt in many advanced nations, most prominently the US. This is to say that China is not only one of the chief suppliers of affordable products to advanced nations but also one of the chief suppliers of credit. Without the significant rise of China as an economic power over the past fifteen years or so, this political-economic tradeoff between consumption and redistribution, between consumer welfare and social welfare, which we have discussed here, might not have been possible at all. More research is needed on this question, to be sure, to reach more robust conclusions.

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TABLES & FIGURES

Figure-1: Household indebtedness as % of GDP

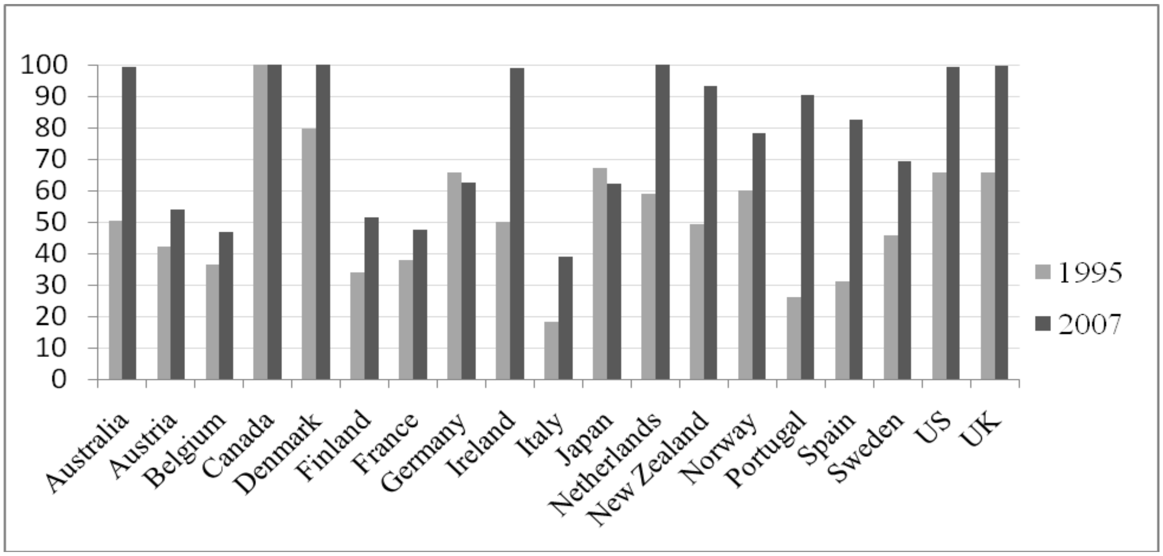
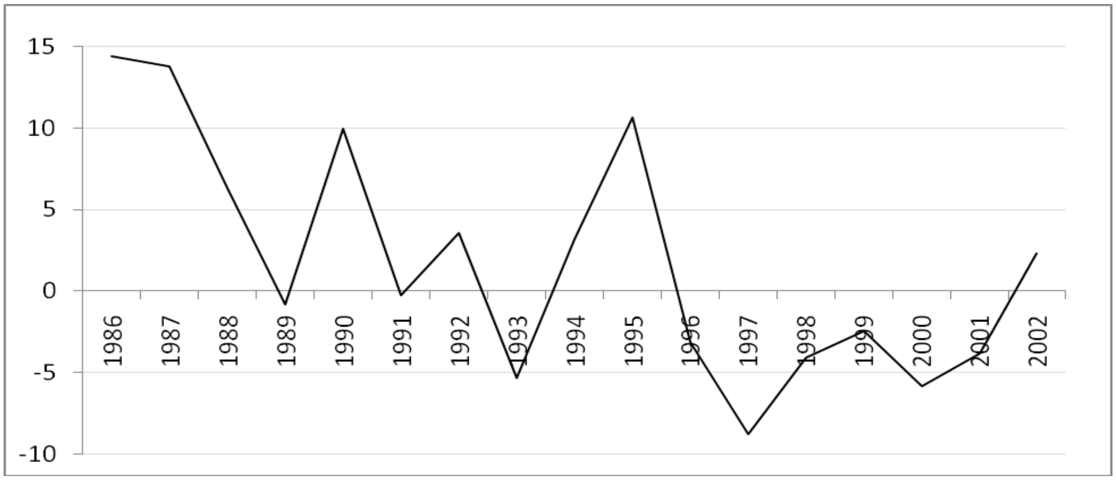


Table-1: Chinese Exports Markets Shares in Major Markets

	1980	1990	2000	2002
Japan	3.1	5.1	14.5	18.3
USA	0.5	3.2	8.6	11.1
EU	0.7	2.0	6.2	7.5

Source: World Economic Outlook (2004)

Figure-2: World Manufacturing Export Price Change (1986-2003)



Source: IMF World Economic Outlook Database

Figure-3: Consumer Welfare and Social Welfare

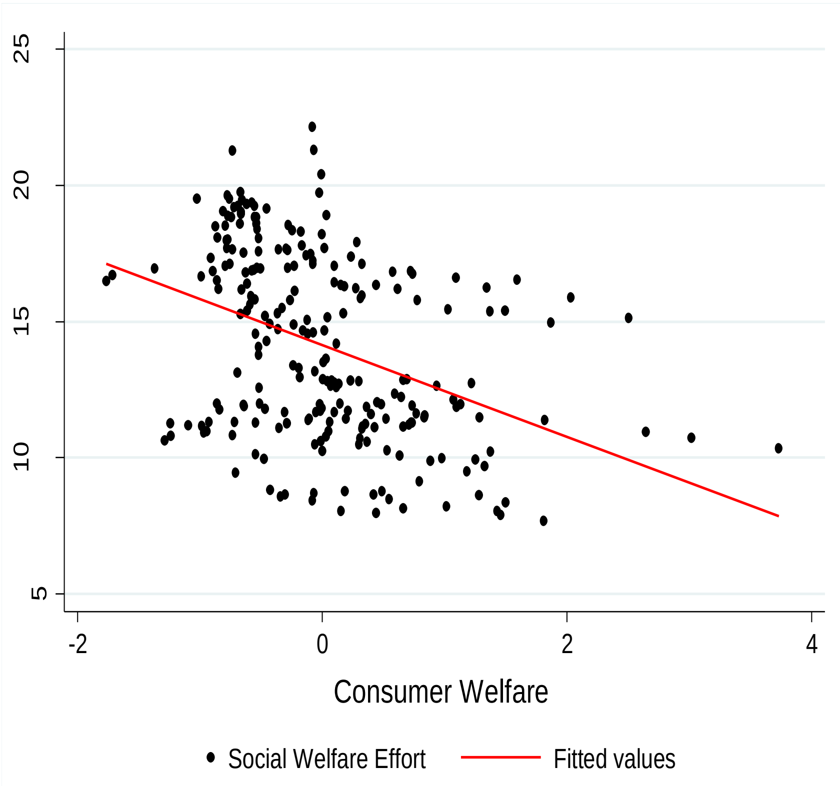


Table 2- Regression Estimates: Consumer Welfare and Social Welfare Effort

	Model 1	**Model 2**	**Model 3**	**Model 4**
Consumer welfare	-.624*** (.155)	-.420*** (.115)	-.377*** (.179)	-.716*** (.264)
Left party power	-.108 (.147)	.092 (.107)	-.172 (.136)	.723* (.386)
Union density	.076*** (.012)	.094*** (.028)	.040 (.055)	.032 (.128)
Financial openness	.206 (.313)	-.302 (.172)	.167 (.329)	1.582** (.740)
Trade	-.004 (.007)	.-.032*** (0.008)	.038*** (.009)	-.027 (.017)
Economic growth	-.047 (.039)	.014 (.029)	-.035 (.031)	.169* (.100)
Unemployment	.306*** (.048)	.285*** (.040)	.267*** (.053)	.422*** (.128)
Manufacturing employment	-.082*** (.062)	-.166*** (.064)	-.544 (.096)	.007 (.201)
Percent elderly	.524*** (.065)	.501*** (.077)	.508*** (.101)	-.119 (.278)
Gross GINI		.000 (.015)	.009 (.022)	.492*** (.128)
Budget deficit		-.113 (.019)	-.135 (.029)	.065*** (.057)
R-Squared	**.890**	**.972**	**.981**	**.965**

*p<0.10; **p<0.05; ***p<0.01.
Country dummies are included in models 2, 3 and 4 although results are not shown.
The dependent variable is social welfare effort.
In models 1 and 2, the dependent variable is measured in terms of social security transfers as a % of GDP.
In model 3, the dependent variable is measured in terms of total social expenditure as a % of GDP.
In Model 4, the dependent variable is the redistributive effort.

Table 3- Regression Estimates: Credit, China and Social Welfare Effort

	Model 1	Model 2	Model 3	Model 4
Credit	-.098** (.047)	-.062* (.033)	-.076** (.032)	
China	-.465*** (.153)	-.380*** (.128)		-.390*** (.152)
Low-wage imports			-.059*** (.021)	
Short-term loans				-.060* (.036)
Left party power	-.015 (.145)	.078 (.112)	.120 (.117)	-.027 (.102)
Union density	.075*** (.009)	.096*** (.029)	.102*** (.030)	.064** (.032)
Financial openness	.319 (.311)	-.325* (.173)	-.388** (.171)	-.168 (.155)
Trade	.003 (.006)	-.030*** (.009)	-.030*** (.008)	-.020** (.008)
Economic growth	-.029 (.037)	-.019 (.029)	-.015 (.027)	-.028 (.025)
Unemployment	.287*** (.046)	.285*** (.040)	.285*** (.040)	.250** (.030)
Manufacturing employment	-.067 (.049)	-.168*** (.065)	-.123** (.064)	-.122** (.060)
Percent elderly	.532*** (.062)	.503*** (.079)	.475*** (.076)	.312** (.133)
Gross GINI	.041 (.022)	-000 (.015)	.005 (.017)	-.009 (.011)
Budget deficit	-.108*** (.025)	-.116*** (.019)	-.117*** (.021)	-.130*** (.016)
R-Squared	**.895**	**.972**	**.971**	**.965**