DEMOCRATIZATION AND SOCIAL SPENDING PRIORITY IN LATIN AMERICA; 1980-1994

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This paper investigates the impact of democracy over social spending – controlling for economic and demographic variables – through a times-series cross-sectional data set for seventeen Latin American countries between 1980 and 1994. The central question relates to the consequences of democratization over the share of social spending in the composition of the public budget, its budgetary priority, in a period of economic crisis and adjustment. Results show that democracies had a positive impact over the budgetary priority of social spending, a finding that held up to a battery of checks. These findings stand against the current disenchantment with Latin American democracies; however imperfect these democracies are, during a most critical period of these countries' history, they have shown a greater commitment to social issues than their authoritarian counterparts.

INTRODUCTION

The eighties mark the beginning of a disturbing period for most of the developing world. After the second oil shock in 1979, the world economy entered one of its worst recessions since the Great Depression characterized by a contracting international trade, declining of non-petroleum commodity prices, and a sharp increase in the worldwide interest rates. These adverse external conditions left most developing countries unable to service an increasing external debt, triggering the debt default in 1982. After 1982, these countries virtually lost access to international financial markets, considerably aggravating the duration and severity of the crisis.

This shortage of international lending made it exceedingly difficult for governments to finance both their external and internal debts. As governments had a limited capacity either to borrow from the domestic private sector or to raise taxes, they tried to restore fiscal equilibrium by adopting policies designed to restrain general consumption, particularly by reducing public spending.[1] As expected, this process of public retrenchment combined with the economic recession and growing unemployment severely affected the poor. Poverty rates increased almost everywhere, and the obstacles to reduce poverty and income inequality were strengthened.

Politically, however, the picture could not be more different. Beginning with the inauguration of Jaime Roldós as the president of the Ecuador in 1979, a new and more extensive democratic wave has swept away authoritarian regimes throughout developing countries.[2] These democracies constituted in a significant break with the authoritarian tradition of most developing countries since they entitled larger extents of the poorest to vote for the first time. Consequently, this process of democratization raised hopes for a better life and generated expectations that new democratic regimes, by promoting political equality, would lead to broad gains in social welfare.

What, then, have been the combined effects of these contrasting influences on social spending? How has the need to cope with increasing budget deficits interacted with the expansion of the political arena?

This paper focuses on the impact of democratization over social spending, particularly over the budgetary priority of social spending. Social spending is worth studying for at least three reasons. First, it usually accounts for a large part of the public budget and, as such, cannot be left out in any attempt to reach fiscal adjustment.[3] Second, social spending performs a crucial role in widening the access to human capital and, as such, it affects the chances of reaching a long-term and more equitable path of economic growth, the ultimate goal of reforms. Finally, investments in human capital address distributive conflicts, allowing social expenditures to have a potentially great capacity in mitigating the political polarization and instability that loom over unequal societies, thereby reinforcing the durability of democratic life.

CAN WE EXPECT ANY EFFECT FROM DEMOCRACIES?

In the light of the inconclusive findings about the effects of democracy over such different areas as income inequality,[4] the probability to undertaking economic adjustments,[5] or other general indexes of economic performance,[6] some authors have suggested that "political regime" is a too broad a category to assess the relevant political aspects (Remmer, 1986 and 1990; Haggard and Kaufman, 1992; Przeworski and Limongi, 1993; Alesina and Rodrik, 1994; Geddes, 1995; and Schneider, 1995). Although it is important to consider political factors other than regime type, ssues relating to regime type and regime transition still deserve attention from comparative students. Below, I offer five reasons that help to justify my claim.

First, presuming that democracy is desirable, we need to know more about the conditions that make it work – that is the conditions that enable it to achieve economic growth, material security, freedom of arbitrary violence, and other widely desirable objectives. (Przeworski et all, 1995) Due to the endemic political instability that has characterized developing countries, much of the comparative work on democratization departed from an assumption that these regimes were inherently fragile. Hence, these works were mostly concerned in constructing etiologies of regime change or of emerging democratic regimes, rather than with the impact of democratization over public policies.[7]

The recent political and economic transformations experienced by many countries in the developing world offer a rich opportunity to explore questions about the capabilities of different types of political regimes to react to external economic shocks by implementing policies considered necessary for economic recovery (Rodrik, 1999). Even if the type of political regime offered little explanatory power for broad areas this does not imply that regimes are not important in explaining less aggregate types of policy choice. As developing countries comprise most of the recent wave of democratization, they provide a great opportunity to analyze the effects of different political regimes over specific policy options.

Second, in spite of the increasing importance given to the role of public spending in the comparative literature on economic growth, there is a limited understanding of the politics of budget allocation among developing countries. As economists have heretofore dominated the study of the subject, most discussions about public spending have assumed an ideal social planner, who represents the public interest and maximizes the aggregate welfare while allocating scarce resources.

While these assumptions may represent an important analytical tool, by explicitly determining an optimal solution, they ignore the political subtleties of policy-making and, consequently, are unable to explain the observed variation in empirical outcomes.[8] It is necessary to take into account the political constraints that shape the incentives that confront decision-makers and influence their policy choices. In this sense, democratization represents a major change in the political institutions – a change that may have significant consequences for the past political equilibria that skewed spending against the poor. I believe that the type of political regime, because of its conceptual simplicity, is a suitable starting point.

Third, the spread of democracy in the developing world can also help to improve governmental programs at the grassroots. As reported by some authors, community participation may play an important role in creating or strengthening accountability and, consequently, in improving the efficiency of public programs.[9] By the same token, giving voice to new actors – especially the poor – can also enhance also the effectiveness and the political sustainability of social programs.

Fourth, despite the euphoria sparked by the widespread democratization among developing countries, current feelings toward new democracies are mixed. Although they represent an important change in comparison to previous authoritarian institutions, new democracies have been criticized for not having fulfilled many of expectations they generated. This democratic disenchantment is particularly acute in the social area, where democratization was expected to make a tangible effect on the welfare of the poor.[10]

As the empirical literature makes clear, democracies alone are unlikely to reverse deeply entrenched patterns of inequality. Nevertheless, democracies may demonstrate a greater concern with the issue than their authoritarian predecessors – a much less demanding performance standard – for instance, by giving a greater priority to social spending.[11] By focusing on these less aggregate issues and comparing across regimes, we will not necessarily demonstrate that it is easier to deal with inequality problems in democracies, but we may be able to ascertain the relative performance of democratic regimes regarding their commitment to tackle the problem.

Finally, empirical evidence has suggested that the sustainability of democratic regimes may be intrinsically related to their ability to cope with income inequality (Muller, 1988 and 1998; Przeworski et all, 1995). That is, democracies increase their chances of survival if they are able to break the vicious cycle that plagues most developing countries, in which the inability to address inequality gives rise to political instability and democratic breakdown. To accomplish this task, democratic governments need to overhaul their public policies, particularly social policies, which are the most important instruments governments have to deal with inequality. In other words, although the main question is whether democratization influences the allocation of public resources in a more equitable and productive way, an improvement in expenditure allocation would also improve democracy sustainability.

CASE SELECTION, ESTIMATION PROCEDURE, AND MODEL SPECIFICATION

Comparable data on social spending for developing countries has been virtually non-existent, making it difficult to undertake broader comparative analysis about how countries differ in their choices in allocating social expenditures.

To test the hypotheses about the influence of democratization over the budgetary priority of social spending, I examined annual data for the 17 Latin American countries between 1980 and 1994, compiled by Cominetti and Ruiz (1997).[12] This data set provides a unique opportunity to study the relationship between democratization and social spending for two reasons. First, with the exception of Cuba, the Dominican Republic, and Haiti, the set includes all Latin American countries. Second the recurrent problem of data comparability is minimized by the effort made by the ECLAC, the United Nation's Economic Commission for Latin American and the Caribbean, who led a country study project to produce comparable data on social spending across Latin America.[13]

ESTIMATION PROCEDURE

The data form a Times-Series Cross-Sectional (TSCS) data set in which each country-year represents a single observation. Although pooling the data has the obvious benefit of increasing the number of observations, it can violate at least two of the basic assumptions that underlie Ordinary Least Squares (OLS) estimation. First the temporal structure of the data increases the chance of autocorrelation of the error terms along the periods of each country, which would violate the OLS assumption that the errors are independent of each other. Second the cross-sectional structure of the data increases the chance that the variance in the error terms may differ across countries, due to country-specific factors, which would violate the OLS assumption that the error terms have a constant variance; that is, errors' variance would not be homoscedastic. The consequence of these violations is that OLS coefficient estimates are still unbiased but inefficient.

In order to deal with these problems I included a lagged dependent variable and a set of "n" country dummies. The inclusion of a lagged dependent variable is based on two assumptions. First the autocorrelation problem is limited to the first-order correlation, a plausible assumption given the short period covered by the data. Second the autocorrelation is not unit specific; rather it is assumed to be common across all pooled units.[14] Finally, but not less important, including a lagged dependent variable allows one to address autocorrelation without transforming the data, which may complicate the interpretation of regression coefficients.

The inclusion of a set of "n" country dummies controls for country-specific effects. It assumes that these effects are fixed during the covered period, allowing a different intercept for each country.[15] This statistical technique, usually called Least Squares with Dummy Variables (LSDV), has two other consequences that are worth mentioning.

On one side the combination of these dummy variables may be highly correlated with other independent variables, enhancing multicollinearity problems within the model and reducing the efficiency of the coefficient estimates. Multicollinearity problems will be particularly acute in relation to variables that can be regarded as relatively invariant, or fixed, within each country along the 15-year period covered by the data. This prevents the inclusion of some variables traditionally used in cross-sectional models aiming to explain welfare spending variation in OECD countries, such as the institutional characteristics of the social programs.

On the other side the exclusion of relevant variables from the model specification should lead to bias in the coefficient estimators. From this perspective the set of dummies summarizes the differences between countries caused by all relevant variables that can be considered as fixed over the 15-year period covered by this study. It accounts even for the differences caused by unmeasured relevant variables, a very common situation among developing countries, for which it is hard to find comparable data.

In sum, while the inclusion of country dummies has the disadvantage of preventing inference about fixed cross-sectional characteristics, it has the advantage of assuring that no relevant, and relatively stable, cross-sectional variable is excluded from the model.[16]

Model Specification

Despite its theoretical and practical interest, the use of social expenditure's budget share as a dependent variable has been scarce in the specialized literature. A main consequence of this lacuna is that one is left with no standard model to follow. In general, researchers have data only on expenditures, which are an outcome of a two-step process: budget drafting and budget implementation. Therefore, one can have at least two alternative models. The first treats expenditures as a proxy for budgetary choices, thus emphasizing the effects at the time of budget drafting (year t-1). The other treats actual expenditures; thus focusing on the budget that is actually implemented in year t.

The issue is not easy to settle; and it is ultimately grounded on how one conceives of budget making in Latin America. Conventional wisdom usually exaggerates the freedom Latin American governments have to manipulate the budget, conveying the impression that expenditures have no relationship to previous budgetary choices. Admittedly, governments in Latin America have a greater room for budget manipulation than exists in the OECD countries; nevertheless, budget manipulation is hardly free from institutional constraints.[17] The problem, then, is the lack of consensus about both the differences between the budget that is drafted and the one that is implemented.

Regarding the effects of democratization, one can argue that most effects should be examined at the time of budget drafting, as the interesting question is whether democratization results in a significant shift in budgetary priorities. Alternatively, assuming large disparities between budget drafting and implementation, one can argue that most of the effects of democratization should be examined at time of budget implementation, as the interesting question is whether democratization results in different expenditures' priorities in the end.

In sum, each model focuses on an equally important but distinct aspect. The first model sees the political variables as causing a structural change in the budget composition. The second focuses on whether democratization entails a different way to manage opportunities to manipulate the budget given an environment with poor information and high macroeconomic volatility.

As my purpose is to explore whether democratization leads to changes in budgetary priorities, I decided to use the first model.[18] In addition, lagging the independent variables would make the causality direction unambiguous, as budgetary priorities may influence not only the economic variables but also the time and pace of regime transitions. Therefore, I will employ the following baseline equation:

$$S/T_{i,t} = \alpha_i + b_1 S/T_{i,t-1} + b_2\,\text{Age65}^{+}_{i,\,t-1} + b_3\,\text{Unemployment}_{i,\,t-1} + b_4\,\text{Growth}_{i,\,t-1} + b_5\,\text{Public Deficit}_{i,\,t-1} + b_6\,\text{Democratization}_{i,\,t-1} + \varepsilon_{i,\,t.}$$

In this equation, **S/T** is the share, measured as a percentage, of social expenditure in the total public budget, with a lagged form included in the right hand side of the equation. The term α_i represents the country dummies, the **b's** are the parameter estimates, ε represents the error term, and, finally, the subscripts $_i$ and $_t$ represent the country and year of observations respectively.

As discussed above, lagging the independent variables is consistent with the underlying assumption that expenditures at a year (t) represent budgetary choices made at year (t-1) plus some unpredictable effects that may occur during budget implementation. In other words, expenditures of any year are strongly determined by the budget devised in the preceding year, as governments need to respect budgetary prescriptions for spending. Moreover, besides addressing the autocorrelation problem, the lagged dependent variable works as a control variable, taking into account that last year's expenditures constrain this year's budgetary options. In general then the model assumes that politicians devise this year's budget with expectations generated by last year's economic performance. This is a reasonable assumption considering the highly volatile macroeconomic environment that plagued the region after the Debt Crisis, which considerably thwarts the efficiency of economic forecasts.

THE DEPENDENT VARIABLE: THE BUDGETARY PRIORITY OF SOCIAL SPENDING

One can find at least three different measures of social expenditure in the literature. Each focuses on a distinct aspect, and the choice for one of them depends on the goal of the analysis. The first, and most traditional, focuses on social expenditure as a proportion of the gross domestic product (GDP). This measure has the advantage of addressing the macroeconomic importance of social spending, independently of variations in the size of the economy. The second is spending per capita, which focuses on the dollar value of services delivered to the average person by the government. Finally, the third measurement is the share of social expenditure on the total public budget, which focuses on its fiscal priority relatively to other types of public expenditure.

Since I am interested in the effects of political variables over budget composition rather than over its size, I have chosen to use the last measurement, the share of social expenditure in the public budget. Four reasons help to justify my decision.

First, it is well known that one of the biggest problems of fiscal adjustments is the impact of deficit-cutting measures on income distribution and poverty. Once the decision to adjust has been taken, the next crucial step is to decide how to make it less painful. In theory, it is possible to achieve fiscal consolidation while protecting the redistributive of the poor. Depending on the initial conditions, adjustments could even enhance, rather than hinder, equity objectives of government intervention. The simultaneous attainment of these objectives, however, presupposes a change in budget composition, with increasing priority being given to social expenditure. More specifically, if coping with a fiscal deficit requires trimming public expenditure, it is equally important to know how much of this effort will be accomplished through cuts in social expenditure. We would want to know whether social expenditures were protected from fiscal cuts relative to other areas of government spending.

Having budgetary priority does not mean that these sectors were immune from expenditure cuts. Rather, it means that if they experience decline, this decline will be proportionally smaller than the one experienced by the total public budget. Conversely, in times of budget expansion, protection means that social expenditure should increase at a higher rate than the budget as a whole. Therefore, if policy-makers had reasons to reject a pure across-the-board rule for the cutoffs – since it could entail unacceptable economic and social costs – we would want to understand the role of politics in explaining their choices about budget composition.

Second, as Esping-Andersen (1994) points out, this is a better measure to study the twin issues of democratization and redistribution, since the classical fear regarding democracies is that they would allow the poor to subordinate governments to their own redistributive purposes. Moreover, compared to the other two measures, the percent of the public budget devoted to social spending captures more accurately the commitment of governments to social welfare by providing "a yardstick of a country's progress toward the Welfare State" (Esping-Andersen, 1994:115). Finally, this way of measuring social expenditure is particularly useful in times of fiscal expansion or adjustment when governments are more likely to reorder their expenditure priorities.

Third, this definition of the dependent variable also allows us to address the equity and growth issue. Since expenditure is perhaps the most important instruments that governments have to influence income distribution, a larger share of social expenditure in the public budget can be a way to achieve the goal of a more equitable and sustainable economic growth. The potential benefits from a better use of public spending should be more salient among developing countries, whose characteristic distortions in the effectiveness of public expenditure portray a situation in which changes in the budget composition can generate substantial economic and social returns.

Last, but not least, this variable has the convenient characteristic of allowing a straightforward interpretation inasmuch as an increase (decrease) in the share of social expenditure clearly indicates an increase (decrease) in its fiscal priority.[19]

DEFINING INDEPENDENT VARIABLES

The measure for democracy conceives democratization as a clear-cut process and measures its effects by using a dummy variable for the political regime, which codes one for democracies and zero for the residual category of authoritarian regimes. This measure is drawn from Alvarez et all (1996). Following Dahl's (1971) minimalist definition of a democratic regime, the authors focus on contestation as the essential institutional feature of democracies.[20] I generally followed Alvarez et all in their classification;[21] moreover, as the authors' codification ends in 1990, I completed the codification for the period between 1991 and 1994 using the same operational rules and information from the comparative literature on Latin American politics.

Additionally to the political variables, I employ two control variables traditionally used in the social spending empirical literature. The first is the demographic structure (**age65$^+$**), which defined as the percentage the total population that is 65 years or older. Due to the impact of demographic characteristics over health care and social security I expect a higher percentage of elderly people in the population to be positively related to social spending.[22]

The second traditional control variable is the **unemployment** rate. As in the case of the demographic structure, the unemployment coefficient has an expected positive sign; the greater the unemployment rate is in a country the greater are the demands on governmental social spending. The data for both variables have been drawn from various issues of ECLAC's yearly report on the Statistical Yearbook of Latin America.[23]

Two other variables try to control for the effects of economic volatility during the period. The first is the annual **growth rate of the GDP per capita**, also taken from the same ECLAC's Statistical Yearbook, which captures other effects of the economic crisis than unemployment. It has an expected negative sign. More specifically, although fiscal policy in Latin America has been pro-cyclical,[24] social spending is expected to have a smaller elasticity to economic growth than other public spending areas: it should increase less in periods of growth and decrease less in periods of economic downturns.

The second measure is the **public deficit**, which captures government's fiscal performance and the extension of adjustments. It is measured as government's expenditure less revenue expressed as a percentage of the GDP; therefore, a minus sign represents fiscal surplus.[25] The data have been drawn from Table I.14 in ECLAC (1996), which has the most complete coverage for the period. The expected sign of this last variable is hard to predict since the issue has been the subject of an intense debate in the literature either when the subject is developing countries in general or when the focus is on Latin America. [26]

RESULTS

To test the effects of democratization over social spending I start from the baseline model. Then, I check the stability of the results either by varying the model specification or using alternative codings of democracy. The dependent variable in all regressions is the percentage share of social spending in the total public budget between 1980 and 1994. Moreover, all models include country dummies [27] Table 5.1 below presents the results.

Column 1 shows results for the baseline model. In general these findings support the idea that democratic regimes are more likely to give a greater budgetary priority to social spending. The coefficient has the expected positive sign and it is almost significant at the 95 percent confidence level (p-value = 0.066). A shift in the type of political regime toward democracy, therefore, should be associated with an increase of about 1.9 percent in the share of social spending.[28]

In a first effort to check the stability of the results, I deleted one country at a time and ran 17 regressions. This is a very demanding test, since it requires the deletion of all observations from each country. Nevertheless the coefficient for democracy retained its sign in all regressions and its magnitude varied from a lowest 1.324, when Costa Rica was excluded, to a highest 2.791, when I excluded observations from Guatemala.[29]

Also noticeable is the coefficient for the public deficit variable: it is negative and significant at the 95 percent confidence level (p-value = 0.024). An increase of 1 percent in the public deficit would represent a decrease of 0.24 percent in the share of government spending devoted to social programs. One can extract at least two conclusions from these results. First, as the public deficit increases, policy-makers decide to spend less on social spending. Second, and more importantly, social spending has been relatively protected during fiscal adjustments, as a decline in public deficit would represent an increase in the share of social spending in the total public spending.

All remaining regressors have the expected sign. Age 65^+, the share of population that is 65 and older, is positive and has a considerable magnitude; despite its expected high collinearity, it is significant at the 95 percent confidence level (p-value = 0.037).

The growth rate of the GDP per capita is negative and almost significant at the 95 percent level of confidence (p-value = 0.059). Each percentage point of growth is expected to decrease the budgetary share of social spending by 0.15 percent. Consequently, though some authors have identified a strong pro-cyclical character in Latin American public spending,[30] the evidence presented here suggests social spending may respond differently to economic growth.

TABLE 5.1
POLITICAL REGIMES AND THE BUDGETARY PRIORITY OF SOCIAL SPENDING

	Dependent Variable: S/T (the Percentage Share Of Social Spending in the Public Budget)				
	(1)	(2)	(3)	(4)	(5)
Country Dummies	Yes	Yes	Yes	Yes	Yes
Year Dummies	No	No	No	No	**Yes**
S/T_{t-1}	0.681*** (0.052)	0.674*** (0.052)	0.683*** (0.052)	0.679*** (0.052)	0.656*** (0.055)
$Age65^+_{t-1}$	2.924** (1.391)	2.935** (1.391)	2.680* (1.461)	2.989** (1.407)	0.822 (2.108)
$Unemployment_{t-1}$	0.012 (0.090)	0.003 (0.091)	0.018 (0.091)	0.012 (0.090)	0.083 (0.105)
$Growth_{t-1}$	-0.149* (0.079)	-0.168** (0.081)	-0.154* (0.079)	-0.151* (0.079)	-0.149* (0.086)
$Deficit_{t-1}$	-0.237** (0.104)	-0.215** (0.107)	-0.229** (0.105)	-0.232** (0.105)	-0.201* (0.117)
Log of $Inflation_{t-1}$		-0.618 (0.677)			
$Openness_{t-1}$			0.023 (0.042)		
Civil War_{t-1}				-0.482 (1.445)	
$Regime_{t-1}$	1.928* (1.045)	2.184** (1.082)	2.034* (1.064)	1.866* (1.063)	2.284* (1.184)
N	225	225	225	225	225
Adjusted R Square	0.988	0.988	0.988	0.988	0.988

Notes: numbers in parentheses are standard errors.
Asterisks indicate levels of statistical significance: * 90 percent, ** 95 percent, and *** 99 percent.

Finally the coefficient on the unemployment rate, despite showing the positive expected sign, has a negligible magnitude and it is not significant at any conventional level. This is somewhat surprising given the traditionally positive and significant effects in models focused on the OECD countries. One possible explanation for this result is that only four Latin American countries have public unemployment programs: Brazil (after 1986), Chile, Ecuador, and Uruguay. Moreover, as in the OECD cases, these programs are directed to help workers in the formal sector, which hardly are the most hurt by economic recessions (Mesa-Lago, 1991).

Columns 2 to 5 in Table 5.1 add other potential explanatory variables to the model to further check the stability of the results.[31] Despite an environment of high multicollinearity the addition of new control variables do not cause a substantial change in any of the estimates.

Testing Alternative Codings for Democracy

As usually occurs in a contested field any classification of types of political regimes is subject to debate, and the one made by Alvarez et all (1996) is not an exception. Therefore, using different classifications for democratic regimes constitutes another way to check for the stability of the estimates presented here.

In looking for alternative codings for democracy, I will employ information from the Polity III data set of Jaggers and Gurr (1996).[32] This source contains annual scores for democracy (DEMOC) and autocracy (AUTOC). The scores are subjectively coded and range from 0 to 10. Following Londregan and Poole (1996), I combine both scores in a new index by subtracting the autocracy score from the democracy one generating a 21-point scale measure that goes from a most authoritarian score (-10) to a most democratic one (+10). Finally, I transformed the 21-point index into a dummy variable in which cases above 0 (zero) were coded as democratic regimes.[33]

TABLE 5.2
EMPLOYING ALTERNATIVE CODINGS FOR DEMOCRACY

	(1)	(2)	(3)
Democracy $_{t-1}$	1.928*	2.006*	2.611**
	(1.045)	(1.109)	(1.091)
N	225	225	219

Notes: numbers in parentheses are standard errors.
Asterisks indicate levels of statistical significance: * 90 percent, ** 95 percent, and *** 99 percent

Table 5.2 above compares the results of using distinct codings for democracy. The first column simply reproduces the estimate from the baseline model in Table 5.1, the other two columns employ the same model. The second column shows the estimate for the original classification made by Alvarez et al. (1996). The last column shows the estimate for the dichotomized form from the Polity III data set.

As one can observe, results are very similar: the coefficients have the same sign, roughly the same magnitude as well as standard errors. Table 5.2, therefore, reinforces one's confidence in the estimate for democracy, since it is stable even when democracy is defined in different ways.

CONCLUSION

The central question of this paper is about the consequences of democratization over the budgetary priority of social in a period of economic crisis and adjustment. To answer this question, I analyzed a Times-Series Cross-Sectional data set – controlling for economic and demographic variables –for seventeen Latin American countries between 1980 and 1994. The results show that democracies had a positive impact over the budgetary priority of social spending, a finding that held up to a battery of checks, which include varying the model specification and using alternative codings for democracy. These findings stand against the current disenchantment with Latin American democracies; however imperfect these democracies are, during a most critical period of these countries' history, they have shown a greater commitment to social issues than their authoritarian counterparts.

Regarding next steps, the model developed in this paper employed a simple dichotomous variable to examine the differences between types of political regimes. Yet one can analyze the effect of political variables in more specific ways. First, keeping one's attention to regime transitions, it is possible to go a step further by exploring effects democratic transitions. The more authoritarian incumbents need to negotiate the regime transition with democratic opposition, the greater would be their incentive to employ social spending as a political resource.

Leaving regime transitions behind, another alternative is to explore effects of different types of democratic regime. As discussed earlier, the former endemic political instability led much of the comparative work on democratization to assume that these regimes were inherently fragile and this assumption drove most of this literature to be more concerned with the survival of new democratic regimes than with their impact on public policies. As we know, social spending will be more effective and sustainable if we can enhance the voice of new actors, particularly the poor. Since the ability of the poor to make effective demands depends on the institutional design of democratic regimes, a natural extension of the work done here is to test the impact of different types of democratic institutions over public policies.[34] As Przeworski (1991) puts it:

> "What seems to matter for economic performance and social welfare, then, is not just 'democracy' in general but specific democratic institutions and policies. Indeed, the correct question is not whether democracy as we have known it will develop in the countries that have recently experienced a collapse of authoritarianism, but rather which sorts of democratic institutions, and with what economic outcomes, are likely to emerge." (p. 54)

Another way to develop the model employed in this paper is related to the dependent variable. A collection of systematic data would allow us to compare the efficacy of each program in more solid comparative grounds, particularly as regards spending in human capital.[35] As stressed many times, however, reaching the poor is not the same as fighting poverty. Even if we know that spending is going to programs that supposedly are more accessible to the poor, we need to know more about the distributive impacts of this spending and whether political institutions affect these impacts.

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[1] In many senses, the economic crisis in developing countries continued through the 1990s as well. The modest success in restoring economic growth, and continuing vulnerability of these economies to external shocks, has kept concerns about finding sustainable sources of external and internal financing among top priorities for macroeconomic policy-makers.

[2] Actually, the newest democratic wave began with Portugal's Revolution of Carnations in 1974 and it seems to not have ended yet, as attested by the recent democratization of Nigeria and the process of regime transition in Indonesia. For a more comprehensive discussion about this wave see, among others, Huntington (1991).

[3] The issue of the overall fiscal effects of social expenditures is not specific to developing countries, since increasing fiscal deficits has led to a focus on social entitlements in developed countries as well. See for instance, the works by Alesina and Perotti (1995, 1997), and Alesina, Perotti, and Tavares (1998) on fiscal adjustment in OECD countries.

[4] See the works surveyed by Inkeles and Sirowy (1991).

[5] See Haggard and Kaufman (1992 and 1995).

[6] For the relationship between political regimes and growth see Przeworski and Limongi (1993) and Heliwell (1994); for research on other aspects of performance, such as inflation rate and public deficit, see Remmer (1990) and Lindeberg and Devarajan (1993).

[7] The partial exception is the literature about the impact of democratization on economic reform, with the restrictions discussed above. For a survey of different "types of democracy", mostly based on institutional characteristics, see Collier and Levistky (1997). As the ability of the poor to make effective demands depends on the institutional design of democratic regimes, a natural extension of the work done here is to test the impact of different types of democracy over public policies.

[8] To be fair, there are many economists who already have been trying to build theoretical models that incorporate political variables; some of their works can be found among the bibliographical references for this paper.

[9] See, for instance, Paul (1992); Isham, Narayan and Pritchett (1995); and Isham, Kaufmann, and Pritchett (1997).

[10] This type of democratic disenchantment does not imply in disregarding that changes in democracies are usually moderate and incremental as claimed by many authors (Huntington, 1989; Schmitter and Karl, 1991). In most cases, however, the disenchantment stems from the perception that new democracies have not represented a shift in government priorities, even an incremental one, toward the interests of the poor.

[11] Although it is an equally important question, as it is hard to conceive any sustained process of inequality reduction without resorting social spending.

[12] The countries are Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay, and Venezuela.

[13] The project yielded two publications: Cominetti and Di Gropello (1994), where most methodological procedures are discussed, and Cominetti and Ruiz (1997), which updates and expands the original data set. As stated before, I draw all data on social spending from this last publication.

[14] As argued by Beck and Katz, (1995: 638), "The assumption of unit-specific serial correlations also seems odd at a theoretical level. Time-series cross-section analysis assume that the 'interesting' parameters of the model, β, do not vary across units; this assumption of pooling is at the heart of TSCS analysis. Why not should we expect the 'nuisance' ρ to not show similar pooling? ρ can be interpreted as how long it takes for prior shocks to be removed from the system. Why should this 'memory' be the only model parameter that varies from unit to unit?" See also, Beck and Katz (1996).

[15] In a variation of the same technique, some authors include a set with "n-1" dummies and the intercept, which would represent the omitted country; therefore, the coefficient for each country dummy represents the difference between that respective country and the omitted one. I preferred to include a set of "n" dummies, without the intercept, since the results for each country are easier to interpret.

[16] As stressed by Stimson (1985), the estimated dummy coefficients are not explanation, but rather summary measures of our ignorance about the causes of between-units differences. In similar perspective, Przeworski and Teune (1970) would say that the dummies represent our inability to "substitute the name of variables for the names of social systems." (p.8)

[17] Regarding this last aspect, see Alesina, Hausmann, Hommes and Stein (1999), who focus on the budgetary procedures throughout Latin America between 1980 and 1992.

[18] Esping-Andersen (1994) employs a similar model to study the effects of regime change over social expenditure in Portugal and Spain.

[19] - Measurements of social expenditure either as a fraction of the GDP or per capita sometimes are easy to interpret, since reductions in their values, if accompanied by an increase in government efficiency, may not represent a decrease in the redistributive effort.

[20] "Our purpose is to distinguish regimes that allow some, even if limited, regularized competition among conflicting visions and interests from those in which some values or interests enjoy a monopoly buttressed by a threat or the actual use of force." (Alvarez et all, 1996: 4). See Huntington (1991: 266-67) for a similar theoretical point.

[21] My codification does not exactly match up the one employed by Alvarez et all in only two aspects. The first relates to the timing rule; in cases of regime transitions, I codify according the regime that prevailed at the 30th of June, instead of the 31st of December rule followed by the authors, as this rule represents better which type of political regime prevailed in that specific year. The second aspect relates to the codification for Brazil under Figueiredo. To my knowledge of the comparative literature on Latin America, this is the only case in which the authors' codification diverges from a virtually consensual interpretation; therefore, I recoded Brazil as non-democratic between 1980 and 1984. For a similar decision, see Hunter and Brown (1999).

[22] The same demographic impact leads one to expect a negative impact on education expenditures; however, this negative impact is outweighed by the positive one on social security and health, since these last two items represent a larger share of social spending.

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23 In the case of Age65$^+$, there is no information for 1981 and 1987; therefore, I interpolated data for these years by taking the average between the two closest years. In the case of unemployment, there are 3 missing data for El Salvador (1986-87) and Nicaragua (1986).

24 See Gavin, Hausmann, Perotti, and Talvi (1996); and Gavin and Perotti (1997).

25 The fiscal year of all countries ends at December 31st.

26 For developing countries in general, see Hicks and Kubisch (1984), Cornia et all (1987), and Ebel (1991). For Latin America in particular, see Grosh (1990) as well as Cominnetti and Di Gropello (1994).

27 Although the p-value for joint significance was smaller than 0.01, none of the country dummies was individually significant.

28 This is the expected short-term effect. According to Goldberg (1986), in a model that includes a lagged dependent variable term among its regressors ($y = b_1\ y_{t-1} + b_2\ X$), the effect of changing x from x* to x* + h as the number of periods goes to infinity is b_2 / [1- b_1]. Plugging coefficients from Column 1 in this formula yields the following result 1.928/(1-0.681) = 6.044, which would be the long-run multiplier. Of course, one should keep in mind that the larger the number of periods the greater the standard error. As my interest is in short-term effects, unless otherwise signaled the coefficients discussed throughout this paper will refer to short-term relationships.

29 These results can be possibly explained if one recalls that Costa Rica is perhaps the country with the strongest democratic tradition in Latin America and has devoted a high budgetary priority to social spending. By its turn, Guatemala, though being democratic since 1986, has devoted a lower than average share of its public spending to social areas.

30 See footnote 24.

31 I also tried to include a variable for the Level of Development, measured by the log of the GDP per capita, following the industrialization argument made by Wilenski (1975). Unfortunately, multicollinearity problems revealed insurmountable in this case. These estimation problems are hardly surprising, since the model already includes country dummies, the annual rate of growth of the GDP per capita, and other variables that are expected to be highly correlated with the level of development, such as Age65$^+$.

32 This is an updated version of former Polity I and II data sets. For a more detailed discussion of the indicators, see Gurr, Jaggers and Moore (1991), and Jaggers and Gurr (1995)

33 The zero value seemed to be a natural candidate for a break point; moreover, it divides the observations in roughly the same way (63.3% of the cases are coded as democracy) as does the regime variable used in Table 5.1 (59.6% coded as democracy). For a similar procedure, though the authors employ a different break point, see Hunter and Brown (1999).

34 Keeping the geographical scope limited to Latin America, it is possible to investigate effects from different types of Presidentialism, as discussed by Shugart and Carey (1992) and in Mainwaring and Shugart (1997), or party systems, as discussed in Mainwaring and Scully (1995).

35 For instance, according to the available evidence, the efficacy of spending on Education in Brazil and Venezuela, which is heavily skewed toward middle classes, is different than spending on the same program in other countries.