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Trade and Welfare Compensation: The Missing Links

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This study uses theory from embedded liberalism to reorient the debate over efficiency versus compensation in the trade and welfare literature. We detail the causal mechanisms and provide empirical results that show how welfare spending can be a necessary condition to further trade liberalization. We argue that increases in welfare compensation lead to stronger public support for trade, which allows states to further advance along the path toward trade liberalization. Based on the 1995 and 2003 ISSP (International Social Survey Program) for 10 OECD countries, our multilevel statistical analyses (individual and country level) show that (1) workers in import-exposed sectors tend to strongly oppose trade, but this effect is substantially diminished when they receive unemployment compensation, and (2) public support for free trade is significantly associated with higher levels of trade openness.

KEYWORDS *spending, trade, welfare*

National responses to trade liberalization have been studied extensively, and decades of scholarship have consistently produced two opposing arguments, what we will call the "efficiency" and the "compensation" arguments. The efficiency argument posits that increased openness to trade by a given nation leads to a *decrease* in welfare spending in that same nation, since generous welfare expenditures, such as unemployment compensation, are seen as incompatible with the need to remain competitive in an integrated world market (Allan and Scruggs 2004; Aspinwall 1996; Busemeyer 2009; Korpi and Palme 2003; Rodrik 1997). In contrast, the compensation argument maintains that trade liberalization pressures states to expand welfare spending.

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In this understanding, greater openness leads to harm for certain groups of workers, which in turn drives up welfare spending as policymakers respond to increased demand from their constituents (Cameron 1978; Garrett 1998; Gizelis 2005; Ha 2008; Hays 2009; Rodrik 1998).

Although most of the trade and welfare literature focuses on the impact of trade on welfare spending, we argue that the causal relationship is inverted and that welfare spending can help states to pursue trade liberalization. Increased market competition under an integrated world market may put pressure on policymakers to retrench welfare provisions. Yet, this retrenchment in turn adversely affects the public support for free trade, which constrains government ability to pursue further trade liberalization. In this fashion, welfare expansion is not just a result but in fact a necessary condition for free trade. To provide support for this argument we examine two critical causal links: (1) how welfare expenditures influence citizen support for free trade, and (2) how increased public support allows policymakers to further trade liberalization. This leads us to find that policymakers who wish to foster trade liberalization should work to increase unemployment compensation targeted at workers who are directly harmed by free trade. Our empirical analyses, which encompass country-level and individual-level drivers, support our main arguments. We find that:

1. Higher levels of unemployment compensation for workers in import-exposed sectors are significantly associated with higher levels of individual support for free trade (multilevel analysis); and
2. Higher levels of public support for free trade are significantly associated with further trade liberalization (country-level analysis).

This article is organized into five parts. First, we critically review the efficiency and compensation strands of the trade and welfare literature and propose how the article can improve it. Second, we discuss how workers in import-exposed industries are more likely to oppose market liberalization, but their opposition can be moderated by unemployment compensation. In the next two sections, we describe the data and multilevel models employed, present the findings, and discuss the robustness of the results. Lastly, we outline how higher levels of citizen support are strongly associated with higher levels of trade openness. Finally, we conclude by discussing the implications of our results.

TRADE AND WELFARE SPENDING

The *efficiency* argument maintains that trade openness inevitably forces states to cut back on welfare expenditures (Allan and Scruggs 2004;

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Busemeyer 2009; Korpi and Palme 2003; Rodrik 1997). According to the argument, to remain competitive against trading partners with lower labor costs, governments in advanced countries have little choice but to lower corporate taxes and downsize social welfare programs as payroll taxes on these programs add to overall labor costs (Huber and Stephens 2001). Trade liberalization also weakens the power of important sources of political support for redistributive policies, notably labor unions, social corporatist institutions, and leftist parties (Huber and Stephens 2001). To remain viable, many social democratic and leftist parties adopted more centrist policies and amended their electoral strategy to draw political support from nonlabor constituents (Piazza 2001).

In contrast, the *compensation* argument proposes that trade openness positively affects welfare spending, as governments are forced to compensate for the problems of income inequality and economic insecurity that their citizens face in the aftermath of trade liberalization (Cameron 1978; Garrett 1998; Gizelis 2005; Ha 2008; Hays 2009; Rodrik 1998). Standard trade theory (that is, Stolper-Samuelson theory) predicts that international trade raises the incomes of owners of relatively abundant factors of production, while lowering the incomes of owners of relatively scarce factors (Stolper and Samuelson 1941). Consistent with the theory, several studies find that trade liberalization has significantly increased wage gaps between skilled and unskilled workers in advanced countries, who have, respectively, relatively abundant and scarce factors (Ha 2007; Jerzmanowski and Nabar 2008; Wood 1995).[1] Governments address the legitimate concerns of these workers and reduce income uncertainty by providing safety nets.

Although the current studies on trade and welfare spending have generated useful research, the literature overlooks the possibility that causation can be in both directions of trade and welfare spending. As the efficiency argument proposes, the competitive pressures of the integrated world market push policymakers to cut welfare spending. However, at the same time, welfare compensation is a necessary condition for policymakers to expedite trade liberalization (that is, the opposite causation from welfare spending to trade). Historically, we can see the basis for this pattern of development in Europe. According to Peter Katzenstein (1985), small corporatist European states (for example, Austria and Sweden) were compelled to open their markets after the Second World War. Being democratic, however, they also had to

[1]We note that the impact of trade on inequality is still subject to debate. For example, Cline (1997) argues that growing inequality in advanced economies is caused by technological change, de-unionization, and lower real minimum wages. A few others (especially, Iversen and Cusack 2000) argue that trade is not related to welfare spending but that the transition from manufacturing and agriculture to services or "de-industrialization" has created demands for government spending. Job losses in the manufacturing sector force workers to learn an entirely new skill set to be able to work in the service sector. The uncertainty and insecurity generated during the transition raises the demand for social protection.

expand their social protection in order to ensure popular consent for trade liberalization. John Ruggie (1982) terms this "embedded liberalism," a system in which states asked citizens to embrace international liberalization but cushioned the negative effects by providing sizable social protections, thus making welfare expansion effectively into a cause of liberalization. Likewise, embedded liberalism thesis proposes that welfare spending is a precondition for market integration, not just a result of it.

The embedded liberalism argument can help explain the observed presence of a pair of seemingly conflicting goals: the desire to open markets and pursue trade liberalization, on the one hand, while keeping or even expanding generous welfare benefits, on the other. Failure to cut welfare spending may compromise efficiency and competitiveness, but welfare retrenchment triggers social dislocations, which lead to citizen discontent and backlash against free trade (Hays 2009). Expanding welfare expenditures and other means of social cushion can allow policymakers to win back public support for free trade and continue market liberalization. In this sense, Ruggie's theory provides one of the two simultaneous links between trade and welfare spending, which is compatible with the efficiency thesis.[2]

If national policies in support of free trade are constrained by public support for trade, which is driven by welfare spending (as predicted by embedded liberalism), this microlevel research has significant implications for the macrolevel debate over trade and welfare spending. However, by far, most microlevel studies have focused on the compensation thesis—the effect of trade on economic insecurity-to-welfare spending (Rehm 2007, 2009; Scheve and Slaughter 2004; Walter 2010). For example, Phillipp Rehm (2007, 2009) finds that sectoral exposure to international competition has no significant effects on individual preferences for welfare policy. Yet, Kenneth Scheve and Matthew Slaughter (2004) find that foreign direct investment flows have significantly increased insecurity in the United Kingdom. Exploring the separate causal links from trade exposure to welfare policy preferences in Switzerland, Stefanie Walter (2010) finds that exposure to trade (measured by industry-specific trade exposure, industry-specific FDI exposure, and occupation-specific offshoring potential) is strongly associated with a stronger individual-level feeling of economic insecurity. This, in turn, sets the preferences for welfare expansion, which in turn increases popular support for leftist parties. However, none of these studies tests the

[2]Existing studies, with a few exceptions, have not explored the simultaneous relationship between free trade and welfare spending. Eunyoung Ha and George Tsebelis (2010) develop a dynamic model where they find that globalization is negatively and significantly associated with social security transfers (% GDP), while social security transfers are positively and strongly related with globalization. While not reported, we also found the similar results: Trade openness (% GDP) is negatively and strongly associated with unemployment compensation (% GDP), while unemployment compensation is positively related to trade openness.

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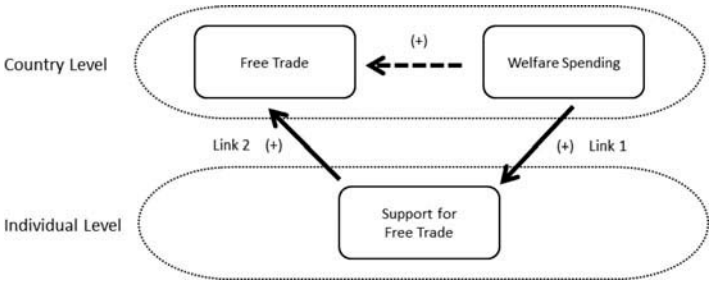

FIGURE 1 The effect of welfare spending on trade liberalization.

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reverse causal relationship—the effect of welfare spending on public support for trade-to-trade openness.

This article improves the current literature by focusing on whether embedded liberalism explains inconsistencies in the existing trade and welfare literature. As Figure 1 shows, the effect of welfare spending on trade liberalization is connected with two underlying theoretical hypotheses: (Link 1) Welfare expansion (at the country level) increases citizen support for free trade (at the individual level), and (Link 2) stronger support (at the individual level) in turn allows governments to further trade liberalization (at the country level). We examine evidence to support these links at both micro and macro levels and therefore use a multilevel model (See data and model section for a discussion of the advantages of this method). Our empirical results show that welfare compensation (granted for workers who are harmed by trade liberalization) is significantly and positively associated with individual support for free trade, which in turn is strongly related with trade openness.

THE IMPACT OF UNEMPLOYMENT COMPENSATION ON PUBLIC SUPPORT FOR TRADE

Who are the ones most likely harmed by trade? Most economists believe that losses from trade liberalization are concentrated in certain sectors, groups, and geographic regions, while the gains accrue to a wide cross-section of economic sectors and actors. The benefits of trade are also slow to diffuse across economic sectors, while the harmful effects of trade are felt more quickly. According to the Ricardo-Viner model, free trade leads to falling incomes and jobs for workers in import-oriented industries but increasing incomes and jobs for those in the export-oriented industries. In advanced economies, the import-exposed industries are usually low-skill, labor-intensive industries such as manufacturing, which are geographically clustered (Bernard and Jensen 2001). Because manufacturing workers are

typically older and less educated, they experience larger earning losses even if they return to work, compared to those in the nontradable sectors (Kletzer and Litan 2001). In this sense, workers in import-exposed sectors are more likely to oppose trade liberalization. On the other hand, workers in export-exposed sectors may not necessarily support free trade ardently because even the firms in export-oriented sectors sell their products in both foreign and domestic markets and thus workers in export-oriented sectors can see the import restrictions as protection against their own job losses. In the microlevel studies on the determinants of individual support for trade, Anna Maria Mayda and Dani Rodrik (2005) find that individuals in import-competing industries are less likely to support policies of free trade, while those in export-competing industries are not necessarily willing to support free trade more.[3] Because the losses from trade are concentrated not only on industries but also on certain regions (Bernard and Jensen 2001), the workers in import-exposed sectors in advanced economies tend to be more organized and thus have substantial political power (Olson 1971).[4]

Workers in import-competing sectors can also have significant influences on the public opinion against trade (Margalit 2011). Public attitudes toward free trade are significantly affected by the degree to which the public perceives trade as being responsible for causing national unemployment (Mansfield and Mutz 2009). If citizens perceive increased foreign trade as responsible for high national unemployment rates, citizens would be less likely to support trade liberalization policies. John Aldrich, Claire Kramer, Peter Lange, Renan Levine, Jennifer Merolla, Laura Stephenson, and Elizabeth Zechmeister (2002) find that individuals' preferences on trade policy are substantially influenced by negative information as compared to positive information. Research by Edward Mansfield and Diana Mutz (2009) finds that individuals in the United States tend to perceive trade policies negatively when trade-related job loss or wage cuts affect their acquaintances—even if they do not personally experience any hardship.

The press and the media, which significantly influence public perception, tend to emphasize the harmful aspects of free trade rather than the beneficial ones. Bad economic conditions in general get much more media coverage and attention compared to good economic conditions (Shah,

[3]We tested if other groups adversely affected by international economic competition (for example, unemployed workers, unskilled workers, low-income earners) are more likely to support trade regardless of their employment sectors. The results show that none of them necessarily supports trade more even if they receive unemployment compensation.

[4]Andy Baker (2005) views "consumption patterns" as a source of preferences for free trade. Trade liberalization raises the prices of exportable goods, while reducing those of imported goods. Therefore, consumers of exportable goods are more likely to be protectionist than consumers of import-competing goods. He finds that high-income citizens in skill-scarce countries (which import high-skilled products) tend to support free trade, while those in skill-abundant countries (which export high-skilled products) tend to oppose it. Because this article focuses only on skill-abundant industrialized countries, we use income levels and individual skill endowments to control for consumer preference.

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Domke, and Wackman 1997).[5] Due to the visible threat, trade-related job loss attracts substantial media coverage. For example, when a company shuts down a manufacturing plant and relocates jobs abroad, local communities and plant workers often mobilize to protest the closure, which in turn often draws heavy media coverage. This negative media coverage not only fosters negative public perceptions about trade, but it also can inspire feelings of economic nationalism (Mansfield and Mutz 2009). In this sense, compensating workers in import-exposed sectors is likely to ameliorate the public's negative perception toward trade as well as their opposition to trade, consequently increasing their support for free trade.

However, there are very few studies on how welfare compensation has changed the anti-trade attitude of the workers in import-exposed sectors. Jude Hays (2009) and Jude Hays, Sean Ehrlich, and Clint Peinhardt (2005) provide exceptions and have explored the effect of welfare spending on public support for trade. They find that workers in tradable sectors tend to oppose free trade, while welfare protection, measured by social security transfers (% GDP) (SST), net replacement rate of unemployment (NRR), and active labor market programs (ALM), is significantly associated with higher support for free trade. However, they have studied the effect of working in "tradable" sectors on the support for free trade, although workers in export-exposed sectors have different policy preferences from those in import-exposed sectors.

By aggregating these two groups of workers with opposite policy interests, Hays (2009) finds that welfare spending, such as SST and NRR, for workers in tradable sectors has no significant effects on their support for trade, which implies that workers in tradable sectors do *not* change their negative policy attitude toward free trade *even if* they receive SST and NRR.[6] Furthermore, ALM for the workers in tradable sectors even produce negative and significant effects on their support for trade, which implies that workers in tradable sectors are even more likely to oppose free trade if they receive ALM.[7] Hays et al. (2005) do not examine these interactive effects at all.[8]

[5]It might be because bad news "sells better" than good news (Haller and Norpoth 1997). However, it is also possible that negative news represent the public's existing views on trade and offshoring (Fogarty 2005). That is, the media may only be reporting the news that the public wishes to see and hear.

[6]Hays (2009) instead includes a triple dummy, "net exports," which codes import-exposed sectors as –1, nontradable sectors as 0, and export-exposed sectors as 1. Still, he does not directly explore how workers in import-exposed sectors would change their attitudes toward free trade as they receive the welfare compensations (that is, the interactive effects of the two major variables), which is the key component of the embedded liberalism thesis.

[7]Hays (2009) explains this puzzling result, arguing that workers who lose their jobs and get ALM programs are expected to find jobs in new sectors in a country with generous ALM programs, and workers try to avoid it.

[8]Neither Hays (2009) nor Hays et al. (2005) have examined the other theoretical link of the embedded liberalism thesis: the impact of the public support for trade on trade openness.

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In this article we examine the effect of unemployment compensation for workers in import-exposed sectors on public support for free trade. Workers who are "directly" harmed by trade liberalization (that is, workers in import-exposed sectors) are most likely to oppose free trade, and thus compensating their job losses "directly" (for example, through unemployment compensation) would be the most effective way to ensure favorable public support for trade. We use unemployment compensation as a direct measure of the protection for trade-induced job loss instead of aggregate welfare compensation (for example, SST). Although aggregate welfare spending data encompass the beneficiaries' broad interests, the policy evaluation derived from aggregated social service indicators can be misleading when different types of welfare states are highlighted (Castles 2009; Esping-Anderson 1990). Unemployment compensation provides immediate support for those recently out of a job, is typically subject to less-stringent criteria, and can thus be considered as a more fungible type of aid money. We also consider unemployment spending (% GDP) as a more direct measure of compensation than NRR. Although welfare entitlements data (replacement rates) provide welfare policy changes, they do not show if social services are actually delivered to welfare recipients (Bambra 2005; Kautto 2002). Social services are considered as more important than social expenditures in some countries, while the opposite is true in other countries (Ha 2008). Our interests lie more in "actual delivery of social services" to the workers in import-exposed sectors, which are better represented by unemployment spending data.[9] We expect that workers in import-exposed sectors are more likely to oppose free trade, but this negative attitude is significantly diminished as they receive unemployment compensation.

DATA AND MODELS FOR ANALYSIS

To measure the impact of unemployment compensation on the public support for free trade, the following variables and both individual-level and country-level data sources were used. Please see online Appendix A for a detailed description of the variables and data sources.

[9]ALM can be another type of direct unemployment compensation. ALM requires participation either in training institutions or workplaces that provide special support for apprenticeship. However, ALM is often found to be ineffective as a means to help the long-term unemployed and particular groups with labor market disadvantages. Firms hire workers in ALM because they receive government subsides, but they can lay off the workers once the subsidy period ends. Because workers in ALM are substituted for those unsubsidized workers who would have been hired otherwise, ALM is also considered to be cost-ineffective to reduce the unemployment rate (Dar and Tzannatos 1999). We tested our empirical models with ALM as well as with SST and NNR. Because the results were inconsistent and insignificant, we confine our report to unemployment compensation, but the result tables are available upon request.

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Public Support for Free Trade

The individual-level data on public support for free trade that we use for our study are available from the International Social Survey Program (ISSP). The ISSP surveys investigate cross-national differences in individual attitudes toward free trade, and data are available for 1995 and 2003.[10] They include the following 10 advanced countries: Australia, Austria, Canada, Germany, New Zealand, Norway, Sweden, Spain, the United Kingdom, and the United States. The ISSP asks respondents the following question: *How much do you agree or disagree with the following statement: (respondent's country) should limit the import of foreign products in order to protect its national economy*?

The respondents' answers are categorized using a 5-point Likert scale: 1 (*agree strongly*), 2 (*agree*), 3 (*neither agree nor disagree*), 4 (*disagree*), and 5 (*disagree strongly*). We reversed the coding so that a score of 5 indicates that the respondent *strongly supports free trade*, while a score of 1 indicates that the respondent *strongly opposes free trade*. However, this ordered categorical dependent variable introduces inadmissible variance into the multilevel analysis and causes convergence problems with unacceptably high computational costs (Debrick, Ferron, Hess, Hogarty, Kromey, Lang, Niles, and Lee 2009). Therefore, we transformed the 5-point scale into a binary one, where we coded 1 for the respondents who support or at least do not oppose free trade (that is, who are indifferent or in favor of free trade) and 0 otherwise. According to the data, 45% of the respondents in the sample support free trade.[11]

Government Expenditures on Unemployment Compensation

As noted in the previous section, welfare spending is measured by unemployment compensation as a share of GDP. Unemployment compensation chiefly consists of both unemployment insurance and severance pay. Unemployment insurance is a form of financial support provided by the government during periods of unemployment. Severance payments are financial support entitled to those workers who have been dismissed not because of their own fault but because of the shutdown or business cutdown of an enterprise. While the provision of unemployment insurance takes a work-oriented approach to support income losses during the period of unemployment, severance pay is subject to government regulation on

[10] Although the World Value Survey (WVS) periodically polls public opinion on socioeconomic conditions across countries, it does not have a specific question on public attitudes toward trade liberalization. The Pew Global Attitudes Project has data on attitudes toward free trade, but the data are available only from 2007.

[11] We may lose some information by transforming the 5-point scale to a binary variable; however, statistical software packages are unavailable to estimate multiple ordered responses in generalized mixed effects models. The main results are robust when we use different thresholds for a dichotomous scale.

assisting the newly unemployed to remain in regular pay for a short run. We use average unemployment compensation over the previous 5 years of the two survey years (1991–1995 AND 1999–2003) to reduce the effects of the business cycle and unmeasured economic fluctuations. A country's fiscal commitment to unemployment compensation is expected to have a positive relationship with public support for free trade.

Workers in Import-Competing Sectors

Individuals working in import-competing industries are usually more harmed by trade liberalization, as compared to workers in export-oriented industries, and thus are more likely to oppose free trade. Using codes provided by the ILO's International Standard Classification of Occupation (ISCO), Hays (2009) identifies a respondent's (or spouse's) industry of employment according to their occupation type. He then categorizes these industries into three types based on their contribution to a country's net exports: export-oriented industries (above the 75th percentile), import-oriented industries (below the 25th percentile), and others (between the 25th and the 75th percentile). Following Hays, we first distinguish the respondents' sector exposure between tradable and nontradable industries. For those in tradable industries, we further divided them along import-competing sectors or not, which is coded 1 if tradable industries in which a respondent is employed contributes to below the 75th percentile of a country's net export. While not reported, the results are also robust when we use the 25th percentile as a threshold.

Unemployment Benefits for Workers in Import-Competing Sectors

This variable is designed to examine how welfare endowment effects for individuals working in import-exposed sectors vary across countries. According to our hypothesis, workers in import-exposed sectors tend to be less worried about their job security and more supportive of free trade if they receive a higher level of unemployment compensation.

Individual-Level Controls

To isolate the effects of unemployment compensation and public support for free trade, we also include common sociodemographic indicators as control variables. First, skilled workers are more likely to support free trade because they can sell their skills to foreign buyers. Skill endowment is measured by the level of education using a 5-point scale with 1 indicating primary education and 5 a completed university degree.[12] This 5-point

[12]One may consider the 5-point scale as meaningless because most individuals go beyond primary education in advanced countries. However, our data show that about 19% of the survey respondents attained

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scale may conflate skills and educational attainment because in some countries vocational schools would provide the same level of skill as a university degree. To distinguish between individual skills and higher degrees obtained through various educational institutions, our model also accounts for the skill specificity of the respondents. Following Torben Iversen and David Soskice (2001), the specialization of an individual worker's skill is measured in terms of how easily that individual can adjust himself or herself to trade-induced job dislocation. This measure scales continuously from 0 (*no skill-specific*) to 7 (*most skill-specific*). The scale is determined by two integrated functions: (1) the size of the labor market segment pertinent to an individual's occupation category identified by the International Standard Classification of Occupations (based on ISCO-88 Occupation Codes), and (2) the degree of homogeneity among these occupation categories. An individual's skill specificity is high when the size of the labor market segment associated with an individual's occupation category is small and skills among occupations are, on average, homogeneous. This alternative factor specificity variable is in fact weakly and negatively correlated with education level ($r = -.112$), implying that highly educated people are not necessarily skill specific. Workers with high degrees of skill specificity may not support free trade because it is hard for them to find employment across industries during global economic downturns.

Second, high-income earners, who have higher capital endowments, are likely to have positive attitudes toward trade openness because of their relative advantages in terms of factor endowment. Following Michael Hiscox and Brian Burgoon (2003), we use an income dummy variable, which is coded 1 if the respondent's annual family income is greater than the median family income, $35,000, in 1995 dollars (that is, high-income earners) and 0 otherwise.[13]

Third, we also control for other individual characteristics such as gender, marital status, parental status, age, and unemployment status. Males and single persons are expected to support free trade given their relative advantages in the areas of job mobility and flexibility of working hours. Those individual respondents without a dependent child are more likely to support trade liberalization because parents are more sensitive to the consequences of possible job loss and thus are more likely opposed to free trade (Hays 2009). Unemployed and older individuals, on the other hand, are more likely to resist free trade owing to the higher relative impacts of income loss and outdated skills (Hiscox and Burgoon 2003).

primary education only. This proportion is not miniscule, compared to other education attainment categories varying from qualification above primary but below entry requirement for universities (21%) to completing technical or vocational degrees (42%) or having full university degrees completed (18%).

[13]The threshold value of $35,000 is based on the median family income level ($35,000–$39,999) defined by the 2005 American Community Survey, and local currencies of the other countries are converted into US dollars using appropriate exchange rates.

Fourth, political ideology and religiousness may affect the level of public support for trade. People with a conservative political ideology are more likely to view open trade favorably since they tend to support laissez-faire market economies. A highly religious person is unlikely to favor free trade because religious values often emphasize reducing economic inequality and fostering economic justice (Hiscox and Burgoon 2003).

Fifth, citizens with nationalistic attitudes are more likely to oppose market integration because national pride and feelings of patriotism can create protectionist tendencies (Mayda, O'Rourke, and Sinnott 2007). National attitudes are measured by Mayda et al. (2007)'s index, which is created based on the respondents' self-identification in three different categories: patriotic, nationalistic, and/or chauvinistic attitudes.

Lastly, we include a dummy variable for the 2003 survey data to control for period-specific effects such as economic fluctuations between the survey periods.

Models

Most of the current microlevel studies ignore the variances across the multilevel data (Hays 2009; Hays et al. 2005; Rehm 2007, 2009; Scheve and Slaughter 2004; Walter 2010).[14] The lower- (or individual-) level data have variances among individual responses with characteristics that are homogenous to their own respective countries. The upper- (or country-) level data, on the other hand, have variances across different countries. By using the country mean of individual variables for regression estimates in individual-level analysis, existing empirical studies neglect endogenously correlated variances across these two levels and wrongly assume that individual characteristics vary only across different country means.

We employ multilevel models to analyze how working in import-exposed sectors (individual-level) interacts with unemployment compensation (country-level) to affect the support for trade (individual-level). There are several methodological advantages to multilevel modeling. First, it enables us to specify predictors at each level and combine multiple levels of analysis in a single comprehensive model. This allows us to examine cross-level effects with better precision (Bryk and Raudenbush 1992). Second,

[14]Brian Burgoon (2009) employs multilevel models to assess how national-level welfare compensation affects public support for EU-level welfare assistance and how EU-level welfare compensation affects support for national-level welfare assistance. He finds that individuals with higher job insecurity tend to support more EU-level welfare assistance, but this effect declines substantially when they receive national-level welfare assistance. Individuals with higher job insecurity also tend to support more national-level welfare assistance; however, this effect is not affected by EU-level welfare assistance. Our study is distinguished from Burgoon (2009) given that we focus on the impact of national-level welfare spending on the public support of trade, not on the support for supranational welfare spending. We are also more interested in individuals' de facto exposure to trade, rather than their "subjective perception" of job insecurity that Burgoon (2009) employs.

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compared to single-level models, multilevel approaches are less prone to model misspecification problems because unexplained variances are actually incorporated into estimation instead of becoming part of error terms (Steenburgen and Jones 2002). Third, multilevel models help us explore "causal heterogeneity" (Western 1998). Causal heterogeneity occurs when the causal effects of lower-level predictors are conditioned by higher-level predictors. This local condition significantly alters the causal story from one country to another. For example, by specifying a cross-level analysis, one can determine if the extent that workers in import-exposed sectors support free trade is mediated by the extent to which their respective government spends on unemployment compensation.

These methodological benefits help us define a varying slope model that allows a multivariate distribution to the vector of regression coefficients within each country. In particular, our multilevel modeling allows the effects of unemployment benefits for workers in import-competing sectors to vary by country group. The equation is specified as:

$$\Pr\left(\textit{Public support for trade}_{\,i} = 1\right) = \text{logit}^{-1}(\alpha_{j[i]}^{\text{country}} + b_{1j[i]}\textit{Workers in import-exposed sectors}_{\,i} + \sum b_k \text{ controls}_{\,i}) \quad (1)$$

$$\text{where } \alpha_j^{\text{country}} \sim \text{N}\left(r_{00} + r_{01}\textit{Unemployment compensation}_{j,}\ \sigma^2{}_{u0}\right)$$

$$b_{1j} \sim \text{N}(r_{10} + r_{11}\textit{Unemployment compensation}_{j,}\ \sigma^2{}_{u1})$$

As discussed earlier, the dependent variable is *public support for trade* (1 if a respondent is in favor of trade openness, 0 otherwise). The main independent variables are *workers in import-exposed sectors* (1 if a respondent is working in import-competing sectors, 0 otherwise), and *unemployment compensation* (the amount of benefits endowment as a share of GDP). b_K is a vector of parameters to be estimated for the effects of individual-level control variables. The subscript *i* denotes each individual respondent, and *j* denotes 20 country groups (that is, 10 countries in the 1995 survey and the other 10 in the 2003 survey). Most importantly, should we allow the slope coefficient for the main independent variable, *workers in import-exposed sectors*, to vary across countries, we can identify $b_{1j[i]}$ *workers in import-exposed sectors*$_i$ as a way of capturing the interaction between individual-level and country-level variables. The parameter b_{1j} accounts for *unemployment compensation* as a country-level predictor in the regression for the slopes. b_{1j} is normally distributed with the average effect of $r_{10} + r_{11}$ *unemployment compensation*$_j$ and the constant variance of u_1. r_{10} denotes the slope coefficient for the relationship between *workers in import-exposed sector* and *public support for trade*. r_{11} corresponds to the interaction between *workers in import-exposed*

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sectors and *unemployment compensation*. On the other hand, the varying intercept $\alpha_j^{country}$ captures country-fixed effects, where $\alpha_j^{country}$ has a normal distribution with the average effect of $r_{00} + r_{01}$ *unemployment compensation*$_j$ and the constant variance of u_0. r_{00} corresponds to the country-level average intercept estimate. r_{01} is the slope coefficient for the relationship between *unemployment compensation* and *public support for free trade*.

MULTILEVEL DATA ANALYSIS RESULTS

Table 1 presents the results of the multilevel data analysis.[15] The intraclass correlation (ICC) examines the degree of dependences among individual-level data within a country, ranged from 0 (*perfectly independent*) to 1 (*perfectly dependent*). The high ICC values in Table 1 indicate that individual-level observations are highly correlated within a country, and it is necessary to analyze the data in the multilevel. To show the robustness of our main results with different controls, we report empirical results from three different models: Model 1 includes minimum controls such as income, education, additional job-related information (the level of skill specificity and unemployment status), and basic demographic characteristics that are strictly exogenous to the model (gender and age); Model 2 includes additional sociodemographic controls (marital status, parental status, political ideology, religiosity, and degree of nationalist attitudes); and Model 3 includes the year dummy for the survey in 2003. The Bayesian information criterion (BIC) shows the goodness of model fits, which introduces a penalty term for overfitting with unnecessary parameters. The smaller BIC is, the better the model fits to the data. The BICs in Table 1 show that model fits are improved as we include the additional parameters from Model 1 to Model 2.

The empirical results strongly support our main argument that a country's commitment to distributing unemployment benefits to workers who are directly harmed by trade is an effective way to reduce public resistance to free trade policies. In all three models, *working in import-exposed sectors* is strongly and negatively associated with support for trade openness, but *unemployment benefits for workers in import-exposed sector* (that is, the cross–level interaction) is strongly and positively related with the support. The empirical results are also substantively meaningful. For example,

[15]We use lme4 package available in R software to estimate our model. See details for model specification variations at http://www.rensenieuwenhuis.nl/r-sessions-16-multilevel-model-specification-lme4/. Andrew Gelman and Jennifer Hill (2007) provide additional information about lmer() function and its applications for multilevel modeling setups.

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TABLE 1 Multilevel Analysis of the Impact of Unemployment Compensation on the Support for Free Trade

Dependent Variable: Support for Free Trade	Model 1	*dx/dy*	Model 2	*dx/dy*	Model 3	*dx/dy*
Key Variables						
Individual Level Effect						
Workers in import-exposed sector (Yes = 1, No = 0)	−0.700***	−0.172	−0.683***	−0.170	−0.685***	−0.170
	(0.202)		(0.179)		(0.177)	
Individual Level Effects Varying Across Countries						
Unemployment benefits for workers in import-exposed sectors	**0.284****	**0.070**	**0.285****	**0.071**	**0.287****	**0.071**
	(0.138)		**(0.122)**		**(0.120)**	
Country Level Effect						
Country's expenditure on unemployment compensation (% of GDP)	0.016	0.004	0.074	0.018	0.269	0.067
	(0.242)		(0.231)		(0.230)	
Control Variables						
Individual Level Effects						
Education (1 ∼ 5: College Degree)	0.288***	0.071	0.244***	0.061	0.243***	0.061
	(0.017)		(0.018)		(0.018)	
Income (annual family income > $35,000 = 1, otherwise = 0)	0.258***	0.063	0.309***	0.077	0.310***	0.077
	(0.044)		(0.046)		(0.046)	
Skill specificity (0∼7: highest skills)	−0.086***	−0.021	−0.081***	−0.020	−0.080***	−0.020
	(0.023)		(0.023)		(0.023)	
Unemployment status (unemployed = 1, otherwise = 0)	−0.185*	−0.046	−0.222*	−0.055	−0.223**	−0.055
	(0.107)		(0.109)		(0.109)	
Gender (male = 1, female = 0)	0.436***	0.107	0.465***	0.115	0.466***	0.116
	(0.040)		(0.041)		(0.041)	
Age	−0.009***	−0.002	−0.004***	−0.001	−0.004***	−0.001
	(0.001)		(0.001)		(0.001)	
Marital status (single = 1, otherwise = 0)			0.098**	0.024	0.098**	0.024
			(0.045)		(0.045)	
Parental status (no children = 1, otherwise = 0)			0.046	0.011	0.046	0.011
			(0.047)		(0.047)	
Political ideology (1: left ∼ 5: right)			0.044**	0.011	0.043**	0.011
			(0.021)		(0.021)	

(*Continued*)

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TABLE 1 (Continued)

Dependent Variable: Support for Free Trade	Model 1	*dx/dy*	Model 2	*dx/dy*	Model 3	*dx/dy*
Religiosity (religious denomination = 1, otherwise = 0)			−0.148***	−0.037	−0.147***	−0.037
			(0.051)		(0.051)	
Degree of nationalist attitudes			−0.449***	−0.112	−0.449***	−0.112
			(0.021)		(0.021)	
Year 2003 (ISSP survey in 2003 = 1, otherwise = 0)					0.697**	0.173
					(0.333)	
Intercept (Country Average)	−0.759**		−1.048***		−1.650***	
	(0.380)		(0.372)		(0.449)	
Number of Total Survey Respondents in 1995, 2003	12,940		12,940		12,940	
Number of Groups (10 Countries in Survey 1995, 2003)	20		20		20	
Variance of Country Specific Intercepts	0.674		0.609		0.505	
Bayesian Information Criterion (BIC)	15,863		15,412		15,418	
Intraclass Correlation (ICC)	0.881		0.921		0.910	

Note. The dependent variable is the support for free trade (support = 1, otherwise = 0), with a mean = 0.45 and a standard deviation = 0.50. Statistical significance is based on two-tailed tests: $^{**}p < .01$, $^{**}p < .05$, $^{*}p < .1$. Standard errors are in parentheses.

according to the marginal effects[16] in the full model (Model 3), an individual's support for free trade is likely to reduce by 17% if s/he works in import-competing sectors. However, the negative attitude is reduced to 9.9% (17–7.1) when s/he receives unemployment benefits (equivalent to increase by additional 1% of GDP). This reduction (7.1%) is substantively significant given that it is almost 16% of the average support (45%).

Figure 2 graphically shows how the predicted probabilities of working in import-competing sectors on support for free trade increases as the level of unemployment compensation increases. At lower levels of unemployment compensation spending, individuals working in import-competing sectors

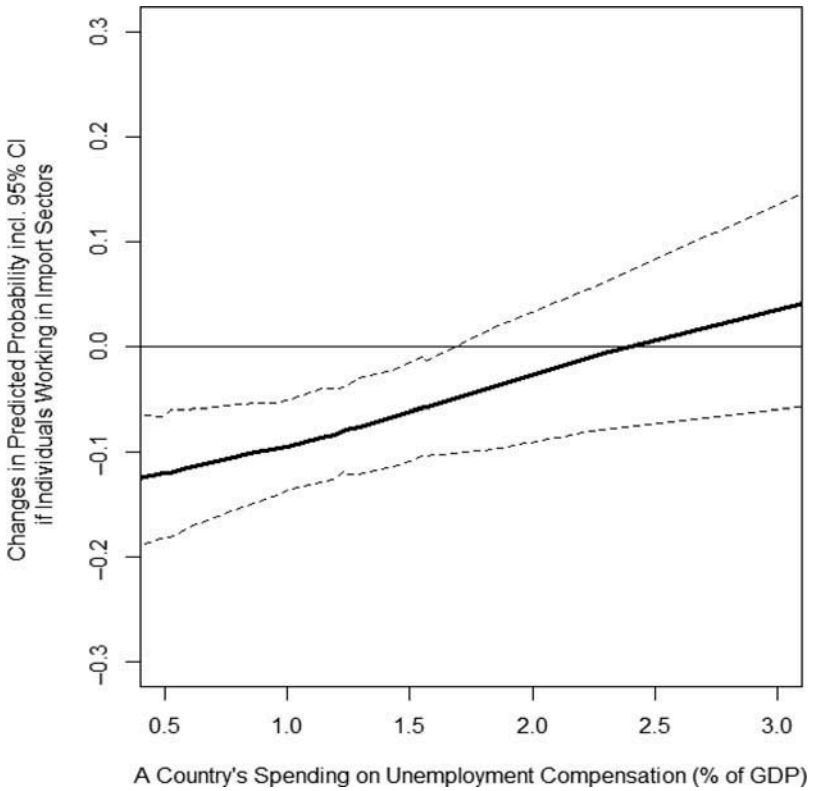

FIGURE 2 Changes in predicted probability of protrade attitudes in import-exposed workers as unemployment compensation increases.

[16]The baseline is set for the average of either continuous or interval variables (education, skill specific, age, political ideology, and nationalist attitudes) and for 1 for the all dummies (income, unemployment status, gender, marital status, parental status, religiosity, and the 2003 survey). Changing this baseline set may move the marginal effect graph parallel, but it should not affect the size of the effect. For example, if we set employment status from unemployed to employed, the graph will move upward, but the slope will remain same.

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are less likely to support free trade. However, as a country's unemployment compensation increases, individual attitudes toward free trade become less negative, and at the highest level of unemployment compensation, the negative attitudes toward free trade become insignificant.

Our regression results spotlight two seemingly contradictory aspects of the unemployment compensation thesis. On the one hand, unemployment compensation at the country level alone does not have any statistically significant impact on public support for open trade policies. This suggests that the aggregate level of unemployment compensation in a country does not necessarily lead to favorable views on free trade. Put differently, a higher level of unemployment assistance is a necessary, but not sufficient, precondition for increasing citizen support for market liberalization policies. On the other hand, the cross-level interaction between a country's commitment to unemployment compensation and citizens receiving such welfare benefits (especially, workers in import-competing industries) allows us to estimate the variance of welfare effects cross-nationally. The estimated effects make it clear that a country's welfare spending granted to those who were directly harmed by trade plays a significant role in alleviating antitrade sentiment and effectively mobilizing public support for further market liberalization.

The effects of individual-level control variables in the model behave as we anticipated. We find that economically well-off individuals with higher levels of education tend to show *protrade attitudes*, holding other conditions in the model fixed at their mean values. Those individuals that hold specific skills or have lost a job tend to *oppose market openness*, in part because of the inflexibility of their skills and inability to find new employment. Work flexibility and ability also appear to play a role in some demographic determinants: male (or single) respondents are more supportive of free trade than females (or married). Older respondents are less supportive than their younger counterparts. Significantly, negative attitudes toward trade openness are more likely to arise among individuals affiliated with a religious denomination (due to concerns about economic equality), or among those who hold nationalist views (due to concerns about market protection). Finally, respondents who are affiliated with rightist political parties are more likely to favor market liberalization and free trade.

We ran several robustness tests to verify our main findings on the conditional effects of unemployment compensation. First, we checked if sampling from the 2003 survey may yield different results as compared to the 1995 survey (See online Appendix B and C). The regression results show that our main results hold in the separate samples: Workers in import-exposed sectors tend to oppose free trade, but the effect is moderated as unemployment compensation enlarges. Still, the effect is stronger and larger in recent years (2003) than in the past (1995). The marginal effect graphs for each sample (1995 and 2003) also showed that the conditional effect of unemployment compensation is statistically more significant for the 2003 survey as compared

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to the 1995 survey. This suggests that the workers who are exposed to trade liberalization have become more sensitive to the unemployment protection toward them.

Second, strong labor unions may increase public support for trade by expanding unemployment compensation. Yet, labor union density is weakly correlated with unemployment compensation in the sample (r = .18). The cross-level interaction between labor union density and workers in import-competing sectors in multilevel data analysis also show that labor union power has no significant effect on promoting public support for free trade (See online Appendix D). On the other hand, even when controlling for the conditional effect of labor union density, the cross-level interaction between unemployment compensation and workers in import-competing sectors still shows a consistent, positive effect on public attitudes toward trade. The results confirm that unemployment compensation, not labor union density, is a major factor in helping workers in import-competing sectors support (or at least show less resistance to) free trade.

THE IMPACT OF PUBLIC SUPPORT FOR FREE TRADE ON LIBERALIZATION

Policymakers are likely to be constrained by the interests of their constituencies and will take voter preferences into account when designing policies. So, higher levels of citizen support for free trade may provide more leeway for policymakers to liberalize markets. The dependent variable is trade openness, measured by the sum of imports and exports as share of GDP. We use average trade openness over the previous 5 years (1991–1995 and 1999–2003) to draw inferences from observing a trend in trade openness not necessarily determined by the events of 1995 and 2003 alone. The results are robust when we use the single-year measure. The independent variable is public support for free trade, measured as the proportion of individuals supporting open trade policies in each country. We have country averages for 1995 and 2003, which return a total of 20 observations (See online Appendix E).

Table 2 reports the empirical results. First, the pairwise correlation shows that public support for free trade and trade openness are strongly and positively related with each other (r = .496, $p < .05$). The bivariate OLS regression also shows that the public attitude toward free trade is positively and significantly associated with the level of trade openness. The effect is also substantively meaningful. According to the coefficient (0.577) in the first column, if support for free trade in a country increases by 16.3% (one standard deviation of the sample), trade openness is likely to increase by 9.41% of GDP, which is about 16% of the average trade openness in the

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TABLE 2 The Impact of Public Support for Free Trade on Trade Openness

	Trade Openness (Imports and Exports as % of GDP)	Tariff Rates (Customs and Import Duties as % of Total Tax Revenue)
Pairwise Correlation	0.496**	−0.574**
Binary OLS regression estimate	0.577**	−0.025***
(standard error)	(0.238)	(0.009)
Tests for heteroskedasticity. H_o: Constant variance		
Breusch-Pagan/Cook-Weisberg test for heteroskedasticity (*p* value)	.652	.105
White's general test statistic (*p* value)	.831	.172
Tests for Normality of Residuals. H_o: Normal distribution in residuals		
Shapiro-Wilk W test (*p* value)	.809	.115
Jarque-Bera normality test (*p* value)	.966	.409
Samples from Indifferent, Agree, or Strongly Agree	20	20

Note. ISSP Survey in 1995, 2003 for 10 OECD countries. Support for free trade: 5 = Strongly agree; 4 = Agree; 3 = Indifferent; 2 = Disagree; 1 = Strongly disagree.
The dependent variable is trade openness, measured by the sum of import and exports as a share of GDP. The trade openness ranges from 21.43% (US in 1995) to 91.26% (Austria in 2003) with a mean of 57.94 and a standard deviation of 18.95.

sample (that is, 57.94% of GDP).[17] The results are robust even when we measure trade openness with trade policies (that is, tariff rates) instead of trade flows. The second column in Table 2 shows that higher public support for free trade is significantly associated with lower tariff rates.[18] The results suggest that a country with a higher public support for free trade tends to have a lower level of trade barriers and a higher level of trade flows.

To measure the inferential uncertainty, we use 100 simulations and generate the estimated OLS regression coefficients (Gelman and Hill 2007). This simulation technique allows us to draw a graph with uncertainties around the average effect (See the solid line in Figure 3). Figure 3 also marks 20 countries as individual coordinate points to reflect a binary relationship between trade volume and the proportion of public support for trade. These country-specific coordinates are mostly spread around a positive slope line. This means that public support for free trade is strongly and positively correlated with actual trade volumes.

[17]Since the sample size is small, we checked for any violations of the constant variance assumption in the regression errors as well as for normally distributed errors. The Breusch-Pagan/Cook-Weisberg test shows that there is little heteroskedasticity. Shapiro-Wilk W test (for small size data set) and Jacque-Bera normality test also show that there are no violations of the OLS assumptions.
[18]Similarly to our argument, Daniel Kono (2008) finds that higher public support for free trade is associated with lower tariffs in democratic countries.

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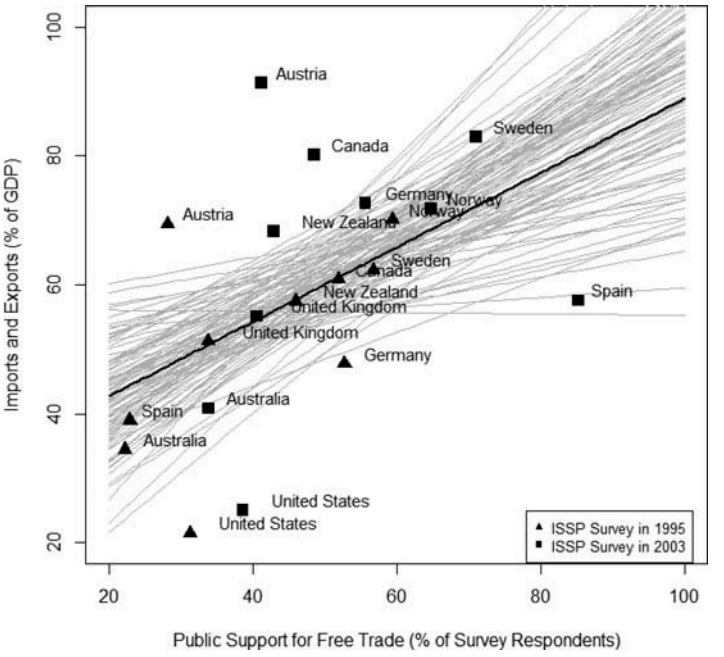

FIGURE 3 The impact of public support for free trade on trade openness.

CONCLUSION AND IMPLICATIONS

This article provides several important propositions and empirical findings with substantial relevance to the ongoing debate over trade and welfare spending. First, we establish and test the reversed causal chain of the compensation thesis, where welfare spending is necessary to further trade liberalization. Second, we deepen the discussion of trade and welfare spending by disentangling the two underlying theoretical links from the reversed causal chain. We find that higher welfare spending, in fact, is strongly associated with higher levels of public support for free trade, and that higher levels of public support are strongly related to higher level of trade openness. However, a large amount of country-level welfare spending is not necessarily the most efficient route to encourage stronger public support for free trade. Our multilevel data analysis has shown that unemployment compensation granted specifically toward workers in *import-exposed sectors* has the largest substantive effect in reducing negative attitudes toward free trade.

The empirical results of this article suggest two important policy implications. First, welfare spending should be considered as a necessary condition to support the expansion of free trade. Although policymakers have to make

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their decisions based on national welfare under the efficiency pressures of the competitive international market, they are also constrained by their national constituencies. They will face incentives to cut welfare programs to gain efficiency and competitiveness in the international market and reduce government debts. However, reducing social protections can lead to widespread discontent and the formation of negative attitudes toward market liberalization, which, in turn, increases the possibility of a backlash against free trade. In fact, antitrade sentiment in advanced countries has significantly increased in recent years (Quinn and Owen 2011), and these negative attitudes are strongly related to existing welfare protections. For example, citizens in countries with higher levels of unemployment protection, such as the Netherlands and Sweden, are far less worried about trade liberalization, as compared to those in the other countries such as France, Italy, the United Kingdom, and Ireland (European Commission 2005). US citizens are also increasingly concerned by the implications of free trade, as they feel that the amount of job loss in import-competing industries will outweigh the additional jobs generated from export-oriented sectors (CCFR 2004).

Second, targeting unemployment benefits to those who lose their jobs as a result of increased imports, via programs such as trade adjustment assistance (TAA), can be a productive route to ensuring public support for trade. Although TAA programs have been employed by only a few advanced countries (for example, United States, France, Canada, and Australia) in limited conditions, these programs do provide tangible and direct benefits to those who are harmed by liberalization (Ehrlich 2010). The cost of wage insurance under TAA is found to be very small compared to the estimated benefits from freer trade. For example, the Uruguay Round of trade liberalization has increased US GNP about $12.9 billion annually (Brown, Deardorff, and Stern 2001). Yet, the United States has spent less than $300 million annually for TAA and NAFTA-TAA payments (Kletzer and Litan 2001). Brian Burgoon and Michael Hiscox (2011) find that citizen support for trade liberalization in the United States is significantly related to the presence of TAA programs. Kara Reynolds and John Palatucci (2012) also find that TAA reduces political resistance by labor unions to free trade agreements (for example, NAFTA). Yortam Margalit (2011) finds that existence of accessible TAA improved President Bush's (who was considered protrade) electoral popularity in counties with high trade-related job losses, which otherwise were hostile to him.

At the end of the day, the effectiveness of the embedded liberalism agenda is undercut by the economic costs of financing higher unemployment benefits, especially since most OECD nations—and many developing ones—have high budget deficits and significant fiscal constraints (OECD 2011). At some point, governments will have to reconsider the cost of unemployment compensation and the additional taxes associated with funding the program, especially if it compromises the ability of domestic-owned

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firms to compete internationally. Based on our research, we believe the best approach to ensure public support for free trade, while minimizing fiscal impacts, is to focus on assisting those most directly harmed by trade liberalization.

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