Introduction: The Politics of Advanced Capitalism

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In the concluding chapter of the 1999 volume *Continuity and Change in Contemporary Capitalism*, the then-editors affirmed that the most challenging part in the characterization of contemporary capitalism is to determine “how the cross-sectional patterns of variation, locked in through intricate pathways of industrialization and democratization, are shaped by growing global interdependence and domestic political and socioeconomic change” (Kitschelt et al. 1999: 427). Today, almost two decades later, the task at hand seems even more daunting, as advanced capitalism is caught up in an accelerating flux, induced by both external constraints as well as the internal dynamics of its political forces and institutional reforms.

In a process accelerated by the Great Recession, virtually every essential aspect of advanced political economies is undergoing fundamental, and potentially far-reaching, transformations. From the demographic tenets of society, through partisan loyalties or the organization of labor markets and economic institutions, to education, tax, and social protection systems, everything seems to be in a process of fundamental change and in need of either adaptation or radical reform. The cross-national variation in institutional arrangements seems to have shifted from frozen landscapes to a complex, hybrid, and morphing configuration of elements taken from different places and “models.” What was previously understood as stable
and rather self-contained “models” of economic growth, distribution, and risk management is now giving way to unprecedented combinations across such models with unanticipated consequences for economic performance as much as individual citizens’ life chances.

A full understanding of these processes requires revisiting existing accounts of the cross-national variation among advanced political economies. While the current reconfiguration may no longer conform to any of the models highlighted in the previous literature on the post–World War II past of today’s most affluent democracies, and while current developments may even make us go back and reconsider how these models need to be characterized in the first place, the stream of new evidence does not, however, warrant the conclusion that current transformations are either random or a signal of convergence on a single institutional equilibrium. The challenge is to theorize structured diversity in a world with changing policy preferences, policy options, and exogenous constraints. Moving away from some earlier approaches, we aim to incorporate the following considerations to capture these movements:

1. We recast the constraints and institutional conditions that shape the feasibility set in which partisan politics explains policy strategies. Thereby, we consider both the changing supply and demand sides of politics, that is, politicians’ political-economic policy proposals and commitments, but also citizens’ policy preferences.

2. We operate with a two-dimensional policy space that considers (1) the scope of public policy efforts to shape economic processes, but adds (2) the differential emphasis of such policy efforts devoted to either investment or consumption oriented policies. The former (in particular investments in education, child care, or research and development) prioritize long-term returns; the latter (most notably welfare transfers) prioritize short-term direct economic returns to voters.
Agency and decisions matter: We theorize how politicians can move beyond the status quo and embrace genuine innovation that breaks with political continuity. Pursuing their own survival in office, politicians experiment with building winning coalitions backed by alignments of constituencies with specific preferences over the two dimensions of public policy. But in each polity constraints still matter, both as policy legacies of past coalitions and sunk costs of policy, as well as limited capabilities of states to realize new policies.

We place politics, in the sense of partisan competition and electoral accountability, and hence the actions of vote- and office-seeking politicians, at center stage, more so than interest groups as the associational representatives of economic factors, sectors, or occupations.

Policy outputs and outcomes then emerge from the interaction between political supply (politicians offering policy prospects) and demand (citizens with preferences over the two dimensions of political economy), restricted by political constraints (i.e., legacies of coalitions and institutions, state capacities).

We refer to our analytical framework as a model of constrained partisanship. We build on the premise that parties’ preferences and strategies are a joint function of two, hierarchically ranked goals: First, parties seek to gain and retain office for as long a period as feasible. Second, we assume that they do so to pursue a particular policy portfolio, and not just for the mere purpose of extracting personal rents (Dixit and Londregan 1996, 1998). As a result, parties must often sacrifice ideological goals for the sake of electoral viability. This is no new dilemma (Przeworski and Sprague 1986; Kitschelt 1994) and the fundamental premises in this account remain true today. There is no reason to believe that political parties today seek less to gain and retain office than they did before. However, the crafting of electoral coalitions has become more complicated.
The dimensionality of the political space has increased and electorates are more fragmented. As a consequence, models built around dichotomous constituencies (Left vs. Right, labor vs. capital) in one dimension provide limited analytical leverage. Politicians have to build electoral coalitions in an at least two-dimensional space. In fact, the openness and possibility of innovation in the constrained partisanship model may derive from the condition that competing parties cannot find stable, coalitional equilibrium strategies in a more than unidimensional world. The possibility of party entry, voter abstention, and differential time horizons of interest maximization, among other behavioral complications, may further subvert the stability of coalitions.¹

The structural transformations of the past decades have promoted this two-dimensionality and complexity of coalition formation. On the side of preference formation, even stylized accounts can no longer plausibly build on a “democratic class struggle” model that dichotomizes the world of political economy between rich and poor or trichotomizes it among rich, middle, and poor, with one side wanting less scope of public intervention and the other more. The transformation of the workforce through technological change, globalization, and the stratification effects of welfare states themselves has created a more complex set of divides that involves divisions of sectors, occupations, and skills, as well as among different gradations of labor market integration. These complications force politicians to assemble electoral coalitions in a more ad hoc manner and to propose and pursue polices in an at least two-dimensional policy space.

But in choosing policy options, politicians are not only hemmed in by citizens’ preference distributions on the demand side, but also by supply-side constraints, that is, by the differential

¹We are relying here on Laver’s (2005) critique of the precariousness and fragility of equilibrium results in formal models of party competition.
capabilities of incumbents across political economies to offer an adequate response to changes in policy demand. This is key to our model of constrained partisanship. With respect to the political supply side, our analysis emphasizes constraints induced by previous policy decisions, and the feedback effects deriving from existing institutional arrangements. The strategic adaptation of actors and the institutional feedback from the context in which they operate mediate the ways in which political demands are actually articulated, and ultimately the responses in terms of political supply by collective actors and governments. Moreover, in some polities, state capacities—for tax extraction and policy implementation requiring professionalized bureaucracies—may simply be too limited to make credible policy commitments.

The emphasis on electoral politics—understood as the dynamics of constrained coalition formation in a two-dimensional policy space against the background of changing voter preferences—sets our approach apart from much of the literature that has focused on interest groups, in particular producer groups, as the key actors of the politics of advanced capitalism. We certainly do not argue that these actors are irrelevant. However, the recent literature has tended to neglect the electoral arena, precisely because most of it still assumes a uni-dimensional conceptualization of partisan competition between Right (capital) and Left (labor), which—indeed—is not very helpful to understanding current dynamics of coalition formation and policy choice. By contrast, explicitly conceptualizing the two-dimensionality of partisan competition and policy strategies allows us to shed light on the complexity of partisan coalition formation in advanced capitalist democracies. In our view, an updated electoral-partisan approach regains analytical leverage. This volume is intended to advocate and contribute to an “electoral turn” in current political economy research.

Let us point out one more important analytical premise that frames our argument before proceeding. In agreement with much of the established political economy literature, almost all
contributions to this volume treat advanced capitalist democracies as an object of theoretical analysis sui generis, separable from a treatment of political challenges of economic development and distribution more generally. We focus on advanced industrial democracies: countries whose democracies have been in operation for more than one generation, whose purchasing power parity assessed affluence (per capita GDP) according to World Bank data exceeded $25,000 international dollars in 2011, and whose population is greater than 4 million inhabitants.\footnote{We are relying here on the World Development Indicator databank, as last updated on April 16, 2013, accessed on June 4, 2013. \url{http://databank.worldbank.org/data/home.aspx}} While there are significant differences among them in terms of the legal and fiscal capacity of the state and development indicators (Besley and Persson \citeyear{BesleyPersson2011}), advanced industrial societies are separated by a surprisingly wide gulf from most middle income countries.\footnote{The only larger democracies with per capita incomes in 2011 between $15,000 and $25,000 and more than 10 million inhabitants were Hungary ($22,000); Poland ($21,000); Chile, Turkey, and Mexico (all around $17,000); and Romania ($16,000). Taking all large countries – regardless of regime and regime legacy – into account, our list excludes only two affluent countries (Korea and Taiwan) and a handful of upper middle-income nondemocratic countries (Russia at $22,000 and Malaysia at $16,000). The majority of populous middle-income countries – democratic or not – have well below half of the income level chosen as the lower cutoff point of our affluent group, $25,000.} They industrialized and democratized significantly earlier than the rest and as a result have enjoyed, with the partial exception of Southern Europe, much higher levels of institutional stability. Two chapters in the volume (those by Boix and by Rueda, Wibbels, and Altamirano) reinforce this point by situating this group of countries within a global and historical context.

Our delineation of the observational universe is more than an inconvenient pragmatic choice of focus due to data or length restrictions. Rather, it is only this set of countries that exhibits an institutional integrity and stability, and a cumulative experience of collective action and interest aggregation, that holds constant many fundamental variables that shape policy
making and policy outcomes elsewhere all over the world. Whereas elsewhere the fragility and variability of the rule of law and citizens' and politicians' basic compliance with universal, institutionalized rules and civil liberties are precarious and account for much of the variance in observed patterns of policy and outcomes, such matters can be taken for granted in advanced capitalist democracies. Moreover, all of the polities we are dealing with have a long history of collective mobilization of economic interest groups. For this reason, explaining variance across policy and outcomes within the restricted group and across the entire global universe of cases would face a problem of causal heterogeneity. In other words, the relevant set of drivers of policy and outcomes is conditional on the level of development: The factors accounting for differences among developed societies either do not explain differences between developed and developing democracies or work differently in the latter. ⁴

The rest of this introductory chapter is organized as follows: Section 1.1. begins with a selective overview of major structural changes, policy strategies, and outcomes observable in advanced capitalist societies over the last decades. It provides the empirical and conceptual background, against which we then develop the elements of our model of constrained partisanship in section 1.2.: We introduce the supply and demand side of politics, including a justification of focusing on parties and elections more than interest groups, before developing in section 1.3. how their combination and interaction shape and restrict the feasibility sets for governments in different countries. This will allow us to generate an alternative interpretation of

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⁴An early empirical example in the political economy literature illuminating this causal heterogeneity is Harold Wilensky's (1975) analysis of global social expenditure patterns. In global comparison, all that accounts for expenditure variance are demand side factors (percentage of the elderly, sanitation/hygiene levels), whereas political processes and divisions come into view only when Wilensky turns to the variance among the advanced capitalist democracies alone. For more recent evidence on causal heterogeneity between the developed and the developing world, see Wibbels (2006).
the evolution of advanced capitalism over the last three decades. Section 1.4. follows up on the
exposition of our approach with a brief consideration of existing alternatives. Section 1.5. closes
this chapter by outlining the organization of the rest of the book.

1.1. Advanced Capitalism Twenty Years Later: Patterns and Puzzles

For several decades advanced capitalist democracies have undergone massive structural
transformations in the domestic and international divisions of labor. The connection between
the transition from a manufacturing to a service economy and the size of the welfare state is a
well-established finding. Whether the major engine of the transition lies in endogenous
productivity changes (Rowthorn and Ramaswamy 1997, 1999), increasing international
competition (Wood 1995), or an interaction between the two continues to be an object of debate
among labor and international economists. The facts remain, however, that advanced capitalism
has deindustrialized and tertiarized, thus producing significant changes in its occupational
structure and the demand side of the welfare state (Iversen and Cusack 2000). While routine and
medium-skilled occupations, especially in the industrial sector, are shrinking massively,
occupation in some countries expands strongly in the low-skilled service sector and – throughout
advanced capitalist countries – strong job growth is observable in the high-skilled high-quality
professions of the private and public service sectors (Goos and Manning 2007; Oesch and
Rodriguez Menés 2011; Oesch 2013). Alongside these processes of generalized upgrading and
differential polarization of the employment structure, advanced capitalism has become more
integrated for capital and labor alike (Rodrik 2011) with differential migration in- and outflows
contributing to major transformations in the employment structure.
The first few chapters in this volume lay out and explain the dynamics of this postindustrial transformation of advanced capitalism, as well as its consequences for the structural and institutional context of the politics of advanced capitalism. In his chapter, Boix points to sectoral shifts as the main determinants of cross-country and longitudinal developments of economic growth and productivity. He finds substantial cross-country variation in the extent to which countries have adapted to the decline of the manufacturing sector, that is, to deindustrialization, but he also emphasizes that the loss of employment in the manufacturing sector is universal across advanced capitalist economies: From about 20 percent of the total working age population, employment in the manufacturing sector declined to around 10 to 15 percent on average in Europe and the United States, whereas the service sector provides employment for about 50 to 70 percent of people of working age. This sectoral shift has entailed a substantial slowdown in growth and brings about a number of political-economic consequences that are likely to challenge existing postwar capitalist arrangements fundamentally. The most straightforward consequence is a harder constraint on public finances, especially in countries that have not managed to readjust to deindustrialization through service sector growth – both low- and high-skilled – and suffer from poor productivity in the remaining industrial sector, notably the Southern European countries. As Rueda, Wibbels, and Altamirano (this volume) argue, the distributive implications of these sectoral shifts in terms of labor market performance and inclusiveness differ strongly among countries depending on their historical pathway of industrialization. Countries with a record of economic openness and interdependence have developed institutions that allow for a more flexible adaptation to structural shifts, while those countries that industrialized via protectionism institutionalized

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5These numbers are calculated over the entire working age population (active population), not only the employed. Since several countries have rather low employment rates, the numbers do not add up to 100 percent.
strong elements of employment protection. Over time, this has led to increasing dualization of their labor markets with a growing share of politically and economically marginalized labor market outsiders.

Deindustrialization is induced by technological innovation in competitive markets, as well as by the globalization of production, often in interaction with each other. Dancygier and Walter (this volume) argue that low-skilled labor is increasingly threatened not only by such a globalization of production and the threat that jobs can be moved abroad, but also by the globalization of labor. The inflow of substantial numbers of low-skilled migrant workers, most notably into non-tradable service sector occupations, has led to globalization pressures both from abroad and from within. As a result, low-skilled labor in manufacturing and service sector jobs constitutes a group of “globalization losers.” These workers not only voice increased needs and demands for protection and compensation by regulative and redistributive public policies; they also form an important (electoral) segment of anti-globalization and anti-immigration voters, further constraining politics in advanced capitalism.

But the increasing scarcity of low-skill jobs is not the only feature of postindustrial occupational structures. At the other end of the skill distribution, deindustrialization has gone hand in hand with a massive growth in service sector employment, much of it in medium- and high-skilled professions. Oesch (this volume) examines this process of “upgrading” of the employment structure, which affects mostly the expansion of employment in the high-skilled financial business sector, and in creative businesses, as well as in public and private social services, notably education, health, and welfare state services for families, the unemployed, and the youth more generally. Job creation in high-skilled employment has outnumbered the decline in low-skilled manufacturing jobs across Europe. This development in turn changes the electoral landscape governments face in advanced capitalist countries, as it produces a large segment of
(public and private) highly educated managerial, technical, and client interactive professions, while it erodes employment prospects of production workers and office clerks. As with deindustrialization, this process impacts on the needs and electoral demands governments face. On the one hand, much of the upgrading job growth is tied to the public sector and strengthens the support for and demand for extensive public services in times of fiscal constraint. This development is partly driven by the female educational revolution and the massive entry of women into the labor force. The incorporation of women into the labor market has produced a revolution across firms, public sectors, and households (Esping Andersen 2009; Iversen and Rosenbluth 2010). Oesch explains why and how female employment changes the occupational structure of advanced capitalism, while Esping-Andersen (this volume) points to the consequences of this development in terms of household formation and distribution. Esping-Andersen argues that occupational upgrading and changing gender roles in the society will eventually lead to a reconfiguration of household composition around more educational homogamy. He calls this process the “return of the family.” The political consequences are obvious: More homogeneous dual earner households lead to increasing household income inequality, and to increasing social policy demands for policies that support labor market participation.

This brief overview has shown that the politics of advanced capitalism unfold in a context, which differs deeply from the context of the politics of industrial capitalism, in terms of its economic, socio-structural and institutional features. How have governments coped with the changing context? We present here some simple empirical results, distinguishing two dimensions to motivate our theoretical treatment in the next section of the introduction. Consider as the roughest measure of government response the total “effort” governments are making to address citizens’ quest for income, measured in terms of the financial resources
extracted from the private economy and channeled back into society, as a percentage of GDP, through a myriad of programs for social transfers and services. A large social policy-related resource flow through the government sector does not characterize a specific policy program structure or profile of distributive effects on society, but it does make possible certain effects, whether they concern equality, (un)employment, earnings, or quality of life.

Then, as a second dimension, divide up these state expenditures into two categories, those that empower people to earn a living in the labor market—with policies classified under the rubrics of education, child care, labor market activation, research and development, and public infrastructure—and those that help people cope with the loss of income, whether due to old age (pensions), skill redundancy (unemployment insurance) or illness (disability benefits and sick leave from employment, medical diagnostics and therapy). We refer to social expenditures aimed at immediate income restoration as “consumption” and to policies aimed at increasing people’s capacity for future earnings as “investment.”

Let us begin with an inspection of countries’ efforts to dedicate funds to social investments and consumption (figure 1.1.). Overall, countries spend more money on social consumption than on economic and social investment policies. While consumption expenditures account for between 6 and 18 percent of GDP, investment expenditures for education, public and private research and development, child care services, and active labor market policies only sum up to between 2 and 8 percent of GDP. The second point of interest in Figure 1.1 concerns the considerable stability of investment-oriented spending over the past two or three decades (investment-oriented data are available only from the early 1990s onward and unavailable for Norway and Switzerland). Nevertheless, there are more countries above the diagonal line, indicating that, over time, a greater share of countries managed to increase their investment expenditure. The inter-temporal continuity of expenditure is similarly high on consumption,
albeit some countries exhibit substantial changes: The Netherlands has strongly reduced consumption-oriented social spending, together with Ireland, whereas countries such as Portugal, Greece, Japan, Switzerland, and Norway have increased consumption spending. Both the Anglo-Saxon and the Southern European countries cluster at the lower end of consumption spending generosity. Overall, there does not seem to be a uniform trend, nor is there convergence or group clustering. Regarding investment, the distribution of countries is rather stable over time, but there is wide variation of levels across countries: The Southern European countries are clearly the lowest spenders on investment, whereas the Nordic countries spend the highest part of their GDP on investment. In the middle, however, we have a heterogeneous mixture of countries.

Figure 1.1.
Public expenditure on public consumption and investment as a percentage of GDP over time.


We turn now to the analysis of the relationship between the overall spending effort (the sum of spending on both investment and consumption) and its composition, measured by the relative importance countries attribute to investment versus consumption. Figure 1.2 shows roughly four groups of countries. In the upper right-hand quadrant of the graph, we see the Nordic countries Denmark, Finland, and Sweden with high overall levels of expenditures as well as a strong accent on investment (investment-related expenditures account for about 30–40 percent of total expenditures). In their emphasis on investment-related expenditures, these

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6 Since we do not have data on public expenditure on infrastructure, we include expenditure on private research and development in our measure of investment, the idea being that investments in infrastructure attract private investments in R&D.
countries resemble the liberal market economies in the upper left-hand quadrant. In Canada and the United States, investment counts for about half of total expenditures. We also see the Netherlands and Japan in this quadrant: In combination with Figure 1.1 earlier, it appears clearly that the Netherlands has “moved” over time to the upper left-hand quadrant by reducing its consumption expenditures while maintaining a strong emphasis on investment. Japan, on the other hand, has expanded both consumption and investment expenditures jointly. In the lower right-hand quadrant we see two groups of countries: The continental countries France, Austria, Germany, and Belgium are “big” and generous welfare states, but investment accounts for only about 20 to 30 percent of their efforts. Finally, the Southern European countries Greece, Spain, Portugal, and Italy show both the lowest levels of overall spending among the continental countries and the most consumption-oriented pattern of expenditure.

Figure 1.2.
Total expenditures for consumption and investment in the mid-2000s and the weight of spending on investment in total expenditure.
(2003–2007, OECD data)

Critically, Figure 1.2 shows that advanced capitalist democracies are highly different in terms of their profile of public spending. These patterns have been relatively stable over time, even though some countries have shifted their emphasis, but we do not see signs of convergence in these data.

Finally, let us consider employment protection as an important aspect of consumption policy in capitalist democracies. Employment protection indicators are possibly best suited to evaluate the extent of convergence and regime stability, as they directly reflect the way governments attempt to coordinate the functioning of labor markets. The left-hand panel of Figure 1.3 focuses on regular employment protection. Once again we find a pattern that defies
expectations of convergence, as levels of protection of regular employment contracts are mostly stable. Only Portugal and Spain have considerably lowered the level of employment protection between the 1980s and 2000s, although they did so from very high levels, which they by and large retain. All other countries have maintained preexisting levels. Overall, we again face a strong divergence among the various polities and very limited support for convergence. The right-hand panel of Figure 1.3 completes the analysis of regulation. It shows the level of protection of temporary employment by country, which reflects the degree of the employers’ difficulty in hiring temporary workers. The pattern of this panel provides evidence for convergence toward the liberalization of temporary employment in most coordinated market economies, most notably in Germany, Sweden, Italy, Denmark, Belgium, and Greece. The resulting disjuncture of the regulations for regular and temporary work has been interpreted as a sign of a trend in coordinated market economies toward “dualization,” that is, the liberalization of conditions for the marginally employed and the preservation of existing levels of regulation for the core workforce (Emmenegger et al. 2012). But a careful look at the way different countries combine both types of protection shows no uniform pattern of convergence: While some countries combine high levels of regular employment protection with a move toward the deregulation of temporary employment (e.g., Sweden), other countries combine very high levels of protection for both types of workers (e.g., Spain, Portugal). Accordingly, the extent to which insiders manage to capture economic opportunities and secure their consumption levels in the labor market continues to vary considerably from one country to another.

**Figure 1.3.**

Employment protection of regular and temporary employment contracts in the mid-1980s and mid-2000s,

The motivating evidence presented here does not reveal an obvious simple pattern, say a convergence of all countries over time or a clustering into clearly distinct groups of countries. We now explore whether we can nevertheless discern principles that may govern the distribution of cases and the dynamics within polities over time. We home in on certain exogenous constraints on the supply side (legacies, state capacities), but then focus on the interplay of political partisan supply of policy options and citizens’ demands that sets the stage for winning political coalitions to make policy choices, albeit under conditions of constraint, therefore “constrained partisanship.”

1.2. A Model of Constrained Partisanship: Two-dimensional Policy Options, Preferences, and Institutional Constraints

Observable patterns of variation in terms of policies and outcomes reflect the nature of the different responses advanced capitalist polities have provided to the structural transformations of demography, technology, and globalization. These responses are conditioned by certain constraints that result from the trajectory of past decisions and political coalitions, congealed around policies and institutions enacting them. At the same time, actors choose among alternative policy responses with some degrees of freedom. We need first to understand what range of policy options is relevant in the feasibility sets of political parties competing for office in the various democracies (the supply side of policy alternatives). We then consider the distribution of political demand, as reflected in citizens’ political preferences over different policy options. Supply and demand then meet and produce binding policy choices. Our approach puts a deliberately strong focus on political parties, governments, and electoral politics, because
the electoral arena is the locus where institutional and structural constraints meet public demands.

1.2.1. Constraints Imposed on the Political Space. Past Choices and Agency Loss

Government choices and strategies in advanced capitalism face two sets of constraints. First, there are the sunk costs of past policy choices that have solidified around legal codes, bureaucratic institutions, and political coalitions. Moreover, past policy choices indirectly affect contemporary preference distributions, and thus the current political demand side, by shaping the profile of production regimes and thus the occupational and social structure (Pierson 1994; Häusermann 2010; Gingrich and Ansell 2012; Beramendi and Rehm 2013). At any given moment, except during profound social crises and catastrophes, political choices, therefore, evolve as an incremental modification of the status quo. As we show below when discussing feasibility sets and political dynamics in four specific institutional settings, the starting point from where political coalitions attempt to innovate, matters tremendously. It restricts what types of policy outcomes are available within the space of theoretical alternatives. Only in the long run, through trajectories involving multiple steps, may all points in a policy space become available, regardless of the starting point status quo ante. Concretely, polities that start with social policies emphasizing social consumption and devoting scant resources to social investment cannot reverse these priorities from one electoral term to the next. Established policies involve lock-in effects, often operating through power asymmetries between supporters and opponents of the effective policy. These asymmetries may be reinforced over time through institutional feedback effects.
Second, also on the supply side, the size and capacity of the state restrict the political "feasibility set" of choices at any moment in time. State capacity is also conditioned by past policy choices and cannot be undone quickly. It constrains the available policy options of politicians who attempt to build winning coalitions (Besley and Persson 2011). We understand state capacity as a set of administrative, fiscal, and legal capabilities that allow politicians to effect the translation of policies into binding and authoritative public policies. Weak state capacity involves "agency losses" that undermine politicians' programmatic credibility in the electoral game, as they lack the possibility of offering and then implementing policies in a uniform and impartial way. Polities with high agency loss in the state apparatus have weaker capacity to intervene in the capitalist economy. The implications of this divide have been largely overlooked in the comparative political economy of advanced capitalism. Our approach in this book helps bridge this increasingly important gap, especially in light of the extensive scholarly attention issues of state capacity continue to attract within the political economy of development.

In theorizing policy legacies and capacity as different sources of agency loss, the crucial distinction is between situations in which the political intervention in the economy reflects political 
\textit{choices} and situations in which the lack of intervention reflects the \textit{incapacity} to decide effectively the allocation of resources in society. When a new incumbent takes power in a context of strong state intervention, a high level of state capacity is implicit. This is not the case in situations of weak state intervention, as it may result from the 
\textit{choice} to pursue a market oriented policy strategy (which we will refer to as a \textit{competitiveness model} in Figure 1.4) even in the presence of high state capacity. These are states that might potentially intervene strongly in

\footnote{Among other features, low state capacity is characterized by civil servants who are ill trained; appointed and promoted for reasons other than qualification and professional skill, such as nepotism and partisan patronage; rely on nonsalarial forms of compensation; and have to act on an incomplete and contradictory web of statutes and legal regulations.}
the economy but have decided not to do so. By contrast, incumbents in low state capacity contexts do not have the necessary institutional leverage to regulate the economy more strongly. In these cases, low state intervention reveals inability, not choice. Low state capacity precludes a number of policy choices for institutional reasons, which may be feasible (though politically unlikely) in countries that have weak state intervention as a result of political choice. This distinction between low state capacity and low state intervention (by choice) is important in determining the feasibility set of countries, that is, the range of potential policy choice.

Policy legacies and state capacities both involve political institutions, such as electoral systems, executive-legislative relations, subnational delegation of jurisdictions (federalism), and other rules of the game. In order not to lose sight of the more basic argument about policy dimensions and political coalitions that act on such constraints, however, we deliberately de-emphasize such institutions in the current introduction.

1.2.2. The Two-dimensional space of Supply Side Policy Options

We propose to conceptualize key political choices over questions of political economy to take place in a two-dimensional space. Our conceptualization of the first dimension is on rather familiar ground: it refers to the scope of public policies designed to affect the income flow of market participants, whether they derive income from wages or profits, and of all citizens in their capacity as past or future labor and capital market participants. Taxing, spending, and regulatory policies affect these income flows, as compared to spontaneous market allocation. Since markets have a tendency to assign benefits in a skewed, unequal fashion that make some
highly vulnerable to existential crises due to low and/or uncertain income flows—for many reasons that have to do with people’s capacities, skills, endowments and plain fortune—, public policy intervention empirically has a tendency to further equality. Those who pursue broad market intervention, therefore, often do so under the banner of equalizing policy goals, even though the scope and precise shape of distributive effects of strong state intervention differ substantially depending on the specific policy instruments at stake.

On the second dimension, we distinguish whether government policy affects the size and certainty of citizens’ resource flows either immediately, as a consequence of current transfers and consumer services, or in the future, as the pay-off accruing to individuals from public policies that help them gain the capacity to participate in markets where they can earn an income. Add to this public policies advancing research and development and infrastructure through direct state funding/procurement of goods and services, or indirectly through incentives to invest, and not all future-directed effort is going to individuals, but also to companies.

In terms of spending, the government must choose how much to emphasize consumption compared to future returns via investments in education, research and development, and services such as child care. The distinction between consumption- and investment-oriented policies is substantiated in the recent welfare state literature on social investment, which analyzes the determinants and effects of transfers (consumption) as opposed to investment-oriented public transfers and services (Esping-Andersen 1999; Bonoli and Natali 2012; Morel et al. 2012; Hemerijck 2013; Gingrich and Ansell, this volume). We build on these contributions but conceive of the distinction between consumption and investment in a more comprehensive fashion. Ultimately, this distinction links back to different growth strategies. An innovation based strategy builds on skills upgrading in the medium run and aspires to increase productivity levels
and to sustain growth through “leading edge innovations” in Aghion and Howitt’s (2006) terms. In contrast, for countries behind the technology frontier growth occurs primarily via capital investments, the import of technologies developed elsewhere, and consumption oriented policies aimed at sustaining high levels of aggregate demand (Acemoglu et al. 2006). Accordingly we define “investment” not only in relation to social policy, but more widely as public expenditures that increase the productivity of the economy overall and of labor and capital in particular. The term “investment” refers to the future orientation of these expenditures. On the other hand, we define “consumption” as a function of both measures of regulatory protectionism (such as employment protection) and social transfers to beneficiaries that use them in order to cover current needs and demands. The balance between these two sets of policy instruments is critical to the understanding of policy effects, economic performance, and distributive outcomes in the postindustrial world (Beramendi, this volume).

In combination, the preexisting balance\(^8\) between policies promoting consumption and investment, on the one hand, and the inherited level of state intervention, on the other, constitutes the set of constraints governments face in designing and implementing policy in different contexts. Let us discuss different analytical configurations in the quadrants of Figure 1.4 as ideal types of policy settings.

\begin{center}
\textbf{Figure 1.4.}
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Dimensionality and configurations of institutional constraints.

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\(^8\)As argued previously, we conceive of the investment-consumption dimension in terms of the relative weight of investment and consumption in the inherited, institutionalized allocation of public resources, that is, in terms of policy priorities rather than absolute levels of policy implementation. This implies that strong state intervention is not a precondition for a particular profile regarding investment or consumption. Incumbents in settings of both strong and weak state intervention are equally constrained by the legacy of policy priorities.
In an institutional setting as in the lower right-hand quadrant, public policy operates on a selective case-by-case base to compensate the losers of the process of market allocation. It has very little forward-looking capacity but responds to the immediate demands of particular social groups. Because intervention occurs case by case, chances are great that small, well-organized groups capture parts of the state and carve out preserves that cater to their interests. Both the fragmentary social policy as well as the selective regulation of industries and occupational groups illustrate this process of policy formation. We are dealing here with a situation of “state capture” in public policy and regulation, which was common at the beginning of democratic politics in most capitalist countries. New incumbents assuming office in these societies encounter medium to low levels of state intervention and capacity with a strong accent on consumption expenditures and regulatory insider protection.

Countries belonging to the lower left-hand quadrant in Figure 1.4 are characterized by stratifying and status-oriented patterns of state intervention. Welfare states are comprehensive, including a variety of consumption benefits and the codification of differential access to such benefits (pensions, health care, unemployment), but also systematic policies to regulate whole industries and organize their access to capital, their methods of skill formation, their certification of products, and their exposure to foreign competitors. We use the shortcut of policy making as awarding “status” to groups through a complex array of measures. Continental European countries such as France, Germany, or Austria correspond most typically to this type of policy legacy, as they combine an emphasis on consumption expenditure (cf. Figure 1.2) with high regulatory density that protects well-organized business and labor interests, but provides little for the poorest tier of the population and creates limited capabilities for innovation.

Investment-oriented polities involve a relatively higher public effort in education and skill formation, measures to stimulate research and development directly or indirectly through an
infrastructure of basic research and professional excellence, as well as investment into the logistical infrastructure of communication and transportation. Furthermore, investments in families (notably work-care conciliation policies) are investments in the future viability of postindustrial economies facing demographic transition. In settings where investment-oriented policies are combined with limited state intervention, it is likely that such policies fuel and intensify a competitive struggle for scarce resources and marketable assets. Actors compete for a relatively small pool of resources, and policies tend to concentrate resources on individuals and organizations whose marginal productivity promises to be very high. Hence, the outcomes of this policy pattern are likely to be highly unequal and driven by a competitive mode of resource allocation; that is why we refer to this quadrant as a “competitiveness”-oriented model. It is mostly the Anglo-Saxon countries, which combine an overall weak state effort (see Figure 1.2) with a relative accent on investment, which suggests a conscious policy choice. It is important to stress that this accent on investment is a relative one. Indeed, “status”-oriented polities may spend similar amounts on investment to competitiveness-oriented ones, but what counts here is that the relative weight of consumption expenditures, which constitute the bulk of past policy constraints for governments, will be much higher in the status-oriented polities.

Finally, in settings where investment-oriented policies are pursued within a framework of rather strong state intervention, new incumbents confront a different set of constraints. Previous policy distributed benefits across a broad spectrum of groups, and individuals receive the opportunity to improve their capacities to acquire economic resources (e.g. through early, universal, affordable, and high-quality schooling or generous work-care policies). Such a policy configuration is thus more likely to result in a more equal distribution of wealth than in a configuration where future oriented investments accrue only to relatively small groups. The equalizing effect is further enhanced by the long time horizon of investment policies, which
creates uncertainty about the ultimate beneficiaries of the policy. For these reasons, we refer to the combination of strong state intervention and investment orientation in policy making as “equality”-enhancing policies, with the Nordic countries being instances where policy legacies correspond most closely to this ideal type.

Our basic premise is that in any particular polity, not all conceivable policy options are available to the political actors to respond to challenges, given the nature of the political supply space, that is, the institutional policy legacies. These institutional legacies shape future policy dynamics through several feedback mechanisms: on the levels of state capacity over time; on the social structure, that is, on the relative weight of different social groups in a society (Oesch 2013); and on their political predispositions and preferences regarding alternative policy proposals. Through these channels, policy legacies endogenously prestructure power relations at a later point. However, the actual policy trajectories within the two-dimensional continuum opened up by the combination of weak or strong state intervention with more consumption or more investment oriented policy options reflect not only institutional legacies, but also the relative size and preferences of different groups of actors in a society, to which we turn now.

1.2.3. The Demand Side: Mapping Citizens’ Political Preferences on the Space of Political-Economic Policy Alternatives

In this section we focus on the preferences and electoral demands to incumbents and their connection with the political economy space (as in Figure 1.4). We do so by mapping the location of relevant socio-structural groups in the political preferences space. Moreover, we claim that
political-economically relevant parts of the citizens’ preference space directly map on the two-dimensional policy space we have outlined above.

Building on a large body of public opinion survey research, we characterize the structure of political preferences as two-dimensional. A first dimension refers to considerations of material gains. People are concerned about the amount and the security of resources that now or in the future accrue to them through markets and the state. They tend to opt for markets when their endowments and capabilities make them expect strong market revenues. They demand state intervention when their prospects and payoffs in the market are weaker.

The analytical characterization of the second dimension of political preferences has been more diverse in the literature. This second dimension combines concerns for sociopolitical governance (“libertarian” versus “authoritarian” positions, Kitschelt 1994) with concerns for group identity and diversity in an increasingly open, multicultural world (national demarcation vs. supranational integration, Kriesi et al. 2008). For our purposes, it is sufficient to settle on a single second dimension, orthogonal to the state-market dimension, that distinguishes preferences for a “universalistic” conception of social order9 in which all individuals enjoy and support a wide and equal discretion of personal freedoms to make choices over their personal lives, from preferences for a “particularistic” conception that sees the individual as embedded in a collective heritage and tradition that commands compliance, including a clear demarcation of boundaries between those who are members and those who are not (see Bornschier 2010, Häusermann and Kriesi and Kitschelt and Rehm, this volume). The polarity of universalism versus particularism, in our terminological use, thus has to do with the role of the individual, as the locus of rights and the origin of choices and with the basic equality of all individuals. It

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9 Bornschier (2010) characterizes this pole of the second dimension as “universalistic-egalitarian”.
therefore reflects a preference over the procedural treatment of all individuals as equal and endowed with personal autonomy to make decisions over their own lives and participate in collective decision making, regardless of their particular tastes, beliefs, and social affiliations.

The critical challenge now is how to theorize the link between these two preference dimensions and the two policy dimensions. In which regard can it be claimed that the preferences “map” on the policy alternatives? We establish this link by identifying the experiential anchors that explain people’s preferences over positions in the two-dimensional preference space. The determinants driving preference dynamics are developed in greater detail, both theoretically and empirically, in the chapters by Oesch and by Häusermann and Kriesi in this volume. For now, consider basic socio-demographic and political economic endowments and faculties shaping political preferences.

On the first policy dimension, scope of state intervention, the link between preferences and the policy space is straight-forward. Individuals try to maximize their flow of material benefits. Hence, capacities and endowments that command a high market income are likely to poise people to endorse a limited scope of economic intervention: capital ownership, high income and/or wealth, high education, self-employment, and managerial or professional occupational status in competitive private sector corporations come into play here. Because prevailing cultural norms thrust upon women the majority of care responsibilities, which often enough restrict their labor market opportunities, they tend to be more supportive of expansive policies to hedge labor market risks. Low skill, low education wage earners, more generally,
endorse broader state intervention with insurance and redistributive effects. Also highly educated socio-cultural professionals in social service professions, especially education, health and well-being, culture and personal counseling services tend to support broader scope of state intervention. Most importantly, such professionals tend to work in organizations insulated from hard budget constraints of bankruptcy, as they are funded by governments or run as non-profits. Even as profit-oriented enterprises, they typically are not competing beyond local or national frontiers and thus face less competition. Many of their salaries depend on a broad scope of the state, and strong tax extraction by the state does not endanger the competitiveness of their organizations in a global market. Moreover, such occupations are immersed in client-interactive service processes that may encourage a greater understanding of and sympathy with the less well-off and thus induce support for more state intervention in the market economy.

The second dimension of preference formation—universalism versus particularism—is, on the face of it, harder to associate with political-economic orientations towards investment or consumption, because many of the political issues around which this dimension crystallizes in actual party competition appear to be very weakly related to questions of political economy (cultural liberalism, multiculturalism, etc). However, we claim that there is a link between universalistic preferences and support for investment and a link between particularistic preferences and support for consumption. We establish this link via two mechanisms: through joint socio-structural determinants of these preferences, as well as – analytically – through the distributive effects of investment vs. consumption oriented policies.

So first, we note that the same socio-demographic capacities and endowments that predict (non-economic) universalistic versus particularistic preference orientations also by implication predict preferences over the second economic policy dimension, dividing policies with high ratios of investment to consumption at one extreme from those with low ratios. The
most clear-cut link between universalistic preferences and investment works through education. The most powerful predictor of universalism on questions of political governance and collective identity is education. But in political-economic terms, highly educated people also have more cognitive capacities and material resources to put a high value on policies of investment that yield a stream of income only in the more distant future. Most importantly, their own advantageous market location is a result of long-term investment policies in education. After all, pursuit of lengthy courses of general education or professional training is a long-term strategy to boost one’s labor market returns. Gender, as a second predictor of preferences over universalism and particularism, may also have a political-economic implication.: with the role of primary caregiver thrust upon them for long-term dependents, particularly children, and being themselves often more precariously inserted in labor markets than men, women tend to express a stronger emphasis for policies of investment than men.

Beyond these socio-demographic, experiential bridging mechanisms, universalistic orientation, as a belief in the procedural equality and autonomy of all individuals, may be epistemically linked to investment policies more directly. The magnitude and beneficiaries of investments, which pay off in the distant future, are more uncertain than the distributive effect of more immediate consumption policies. Their distributive consequences can less easily be targeted to specific groups and individuals in the here and now than current consumption expenditures. Because of this veil of ignorance over future distributions resulting from current investment policies, people with universalistic preferences are more likely to embrace investment strategies than advocates of particularistic preferences.

Having established the congruence of the political economy space and the political preference space, we are able to locate specific socio-structural groups in the respective quadrants of the two-dimensional space. The definition and location of these groups will allow us
to theorize coalitional potentials and dynamics. Conventional uni-dimensional political economy models usually distinguish among the poor, the middle, and the rich only. In the two-dimensional space, there is greater differentiation between the characteristics that affect the political preferences of social groups. For the purposes of our analytical framework, we define the relevant social groups with a special focus on occupational profiles. Occupational task structures are strong correlates of income, education, gender, and employment status (Oesch 2006; Goldthorpe and McKnight 2006). They are also independent causes of preferences through the work experience they generate for individuals, and, finally, occupational groups or classes form relevant socio-structural categories with distinct political preferences and voting behavior. We propose a stylized model with four main groups, based on the criteria of occupation and market situation, building on Oesch’s (2006) class scheme. The preference profiles of these groups can be located in the respective quadrants of the two-dimensional space. In this Introduction, we cannot elaborate fully on the mechanisms that link these occupational groups and their socio-structural correlates to political preference profiles. A large body of research on class politics has obviously done precisely that (Evans 1999; Knutsen 2004). More recent studies theorize the links between labor market experiences and preferences for a transformed, typically postindustrial structure of occupations. We build here on this growing body of literature to identify both the relevant groups and the determinants of their specific preference profiles (e.g., Kitschelt 1994; Kriesi 1998; Oesch 2006; Häusermann 2010; Schwander and Häusermann 2013; Häusermann et al. forthcoming; Kitschelt and Rehm 2014; and Häusermann and Kriesi, this volume):

- Business-finance professionals, technical experts and managers: Individuals with high education, high earnings, and capital assets in financial industries and at the peaks of managerial hierarchies or liberal professionals who assist people in these
positions (legal and business consultants) tend to prefer market-based resource allocation with a minimally invasive state, but, when pressed, prefer government investment to consumption expenses (services and transfers to groups with little market income). On the universalism-particularism dimension, they take more universalist positions given their high level of education.

- Sociocultural professionals: Individuals with high education in social and cultural services, typically working in nonprofit or public organizations with flat hierarchies and with extensive work autonomy and client interaction, are characterized by decisively universalistic positions but are somewhat conflicted on questions of economic distribution. Their high income and human capital make them somewhat more critical toward state intervention, but given their universalistic-egalitarian value profile, their often atypical employment biographies (many of them being women), and their reliance on (para-)public sector employment, they are in favor of strong state intervention.

- Petty bourgeoisie: Individuals with low education, but relatively high incomes and capital assets who are typically self-employed and run small enterprises, whether in agriculture, retail and general services, or custom crafts production, tend to be predisposed toward free markets, opposed to state intervention other than enterprise subsidies, and thoroughly rooted in a culture of political particularism, rejecting multi-culturalization of society and libertarian governance.

- Low-skill clerical, service, and manufacturing wage earners: On the basis of their low human capital assets, this group tends to be committed to strong state intervention in the economy. Low-skilled workers have a propensity to embrace particularistic positions, and here both economic considerations as well as
education and cultural interpretations come into play as explanatory factors (see Dancygier and Walter, this volume). Lower-skill workers, particularly in manufacturing, tend to favor consumption expenditure over investment, as they share a strong preference for answering current needs. We want to point here to a differentiation between lower-skill workers in manufacturing and lower-skill service sector workers. These two groups differ strongly not only in their gender ratio (the group of service workers being mostly female and manufacturing workers predominantly male) and the type of employment relationship they are typically in (with service workers being frequently exposed to atypical and interrupted employment biographies and precarious employment), but also to some extent with regard to their preference for consumption versus investment. Because of their more fragile employment situation, lower-skilled service workers have a stronger interest in investment-oriented policies of activation and human capital development. The literature on insider-outsider divides and dualization theorizes precisely this divide within the working class (e.g., Rueda 2005; Häusermann 2010; Schwander and Häusermann 2013; Emmenegger et al. 2012). Lower-skilled service workers, however, have so far been only weakly mobilized politically in terms of turnout and representation; that is why they matter less as a group for the theorization of electoral coalitional dynamics.

Figure 1.6 projects these groups onto the two-dimensional political economy space. Note that the “middle class” is fragmented among sociocultural professionals, business-finance professionals and managers, and the petty bourgeoisie.¹⁰

¹⁰We are aware that our stylized simplification leaves out many considerations that most certainly impact on individuals’ political preferences, as well. Gender, as discussed earlier, overlaps with insertion in the occupational
The two-dimensional space suggests that politicians have considerable opportunities to devise electoral appeals that craft diverse coalitions for government majorities (Evans and De Graaf 2013). And such electoral coalitions are not entirely bound by structural or institutional constraints. Rather, they have opportunities to change the trajectory of a certain polity. Hence, our two-dimensional account of politics stresses the possibilities of change and the opportunities for political choice. In the postindustrial context, “coalitional flexibility” (Häusermann 2010: 87) is further enhanced by the ongoing process of electoral realignment and dealignment: On the one hand, the vote is still structured by societal experiences, but the relevant dimensions of these societal experiences are more complex than in industrial societies. Simple uni-dimensional class-based models like Erikson and Goldthorpe’s (1992) or those of Moene and Wallerstein (2001) fail to capture these essentials. On the other hand, the differentiation and diversification of life experiences also weaken the socioeconomic roots of political preferences and contribute to the growth of unaffiliated electorates and electoral volatility (Dalton 2004).

However, coalitional flexibility is not absolute and the opportunities for governments seeking to build majorities are constrained. First and foremost, they are constrained by the relative size of the groups displayed in Figure 1.6. None of the groups has a majority by itself. Low- and intermediate-skill wage earners together, for instance, account for between 30 and 40 structure, but gender roles sui generis leave an imprint on preferences that is not reflected in the political-economy scheme. Labor market outsiders’ interests cannot be exactly mapped onto the occupational groups. However, even though their integration in our analytical scheme is perfectly possible, they are not a powerful electoral group in contemporary capitalist democracies; that is why we do not fully conceptualize them in the context of demand side constraints governments face. The same applies to migrant minorities. Likewise, the nonworking do not appear here.
percent of the society when taking all advanced capitalist economies together (around 50 percent of the workforce, i.e., excluding pensioners). The relative size of the different groups is an important constraint on the reform strategies governments can pursue (what we will call the “feasibility set”). It is most relevant to notice that this relative size varies across countries, partly endogenously to the institutional legacies. Indeed, the production regimes and welfare states themselves have contributed to shaping the occupational structure and thereby have pre-structured the opportunities and limits of coalitional strategies in the postindustrial era. Hence, the particular configurations of policy legacies (as conceptualized in Figure 1.4) are also characterized by the relative size and importance of specific socio-structural groups and their political potentials. The equality model builds on a very strong public sector and massive investment in education and public services, which has generated not only a politicized, but also a particularly large category of sociocultural professionals as one of the core coalitional potentials in electoral dynamics. Similarly, status-oriented models have fostered the organized working class mostly in manufacturing as one of the key coalitional actors. The same goes for business-finance professionals and managers in the competitiveness-oriented model and for the petty bourgeoisie in those countries characterized by consumption-oriented policies and weak state capacity overall. Hence, every set of institutional legacies and constraints is also characterized by a core group, on whose support the traditional model relies politically. Just to illustrate this idea of long-term, endogenous institutional effects on the occupational structure and relative size of groups, consider that sociocultural professionals, for instance, represent almost 20 percent of the workforce in the Nordic countries, as opposed to about 15 percent in continental Europe, 10 percent in the United Kingdom, and only 7 percent in Southern Europe. Conversely, small business owners, that is, the petty bourgeoisie, represent almost 25 percent of

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11 These numbers reflect calculations based on ESS 2008 data.
the workforce in Southern Europe, as opposed to only around 10 to 15 percent in continental Europe and the United Kingdom and less then 10 percent in the Nordic countries on average. Such differences in the relative sizes of these groups are no coincidence. They reflect the institutional structure of capitalism, which in turn reflects the (historically accumulated) power resources of different societal interests. For this reason, past policy choices codefine the set of feasible coalitional strategies on which governments can build. Democratic politics is coalitional politics across preference divides.

1.2.3. Collective Mobilization through Parties and Elections as the Critical Democratic Link

What is the organizational link between preference distributions and political action? How do preferences get primed and mobilized in the political process to crystallize around collective actors that pursue policies corresponding to their constituencies’ preference profiles? We posit that for the foreseeable future the prime organizational vehicle to make the link between citizens and market participants, on one hand, and policy formation, on the other, is political parties and elections. Parties represent segments of the popular preference distribution. But there is no one-to-one relationship. Politicians have a limited freedom to carve out different profiles of support groups, contingent upon how they stage their appeals. They operate under different institutional rules that, at the margin will modify their strategies and capacities to reach voting blocs and craft coalitions among political parties. The “electoral turn” in political economy means for us that parties are not just treated as direct representation of producer (labor, business, etc.) or income groups, but that parties may form complex alignments of economic interests both within their own ranks as well as through inter-party coalitions, where
institutional rules make the formation of government executives and legislative majorities dependent on inter-party cooperation.

At first sight, it might appear that our account of transformation in the political economies of advanced capitalist democracies is devoid of economic producer interest groups, a core concern in much of the political economy literature over the past two generations, and instead puts all the emphasis on electoral competition. Let us offer here a few clarifications to dispel this inference. We are not arguing that economic producer groups are unimportant. Instead, we are arguing that producer group politics alone is insufficient to account for the politics of advanced capitalism, and that electoral politics has become increasingly important for the transformation in the political economies of advanced democracies. But we certainly do recognize that producers, particularly those with capital to threaten exit from a polity, have “outside options” to influence the policy-making process and further constrain the feasibility set of likely policy outcomes.

First of all, then, we would not deny that the degrees of business and labor organization, and the change of such organization over time, are important constraints affecting parties’ strategies of constructing electoral alignments, and parties’ degrees of freedom to modify the institutional and policy legacies with which they are working in each polity. However, the institutional setup of labor market relations and economic coordination is itself dependent on distributive politics and shifts along with the development of political coalitions (Beramendi and Rueda 2014).

Second, however, and demonstrated in the contributions to this volume by Hassel and, to a lesser extent, Jackson and Thelen, there has been at least a partial atrophy of the organizational capacity of labor, manifested in sometimes catastrophic membership decline of labor unions. This decline is most visible where labor has always been weak, particularly in the United States,
but it has extended to a rather large swath of countries with the partial exception of Scandinavia.
The decline of labor has given more prominence to electoral partisan competition. Ironically,
whereas the theorists of corporatism in the 1970s saw electoral politics only as a marginal
contributor to the choice of political-economic strategies, parties have become central mediators
of political-economic change now. Parties are not simply ratifying the balance of power among
economic interest groups. Taking off from the Jackson-Thelen chapter on industrial relations
change, this could be fleshed out for the calculations of German social democrats in 1998–2004
in accepting and promoting corporate governance reform, or of Danish conservatives in
transforming industrial relations systems.  

Third, while labor unions have declined in organizational capacity more so than business,
the electoral perspective, however, qualifies a seemingly plausible implication, namely, that with
the weakness of labor, it is business alone that prevails in policy making. While this appears to be
by and large true in the United States (cf. Hacker and Pierson 2010; Gilens 2012), for many
other contemporary capitalist democracies, one may find instances where politicians have the
incentives to pursue policies not favored by business, for reasons of their very own electoral
survival. Examples in this volume are supplied in the chapters by Gingrich and Ansell, and by
Huber and Stephens on social policy development.

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12 Recent electoral politics in Germany may also serve as an example: Schröder’s Agenda 2010 was a form of
“government by commission” (Czada 2005: 177), implemented by a social-democratic government that felt
abandoned and immobilized by status-preserving, progressively weaker labor unions. After all the attempts to reach
a consensus with the unions had failed, the only way out appeared to be a reform against instead of together with
the unions (Streeck 2005: 163). Even though this strategy backfired electorally and subsequent governments had to
reorient policies toward the demands of labor to some extent, key elements of the Agenda 2010 that were
implemented against the will of the trade unions have remained in place.

13 However, the autonomous weight of shifting public opinion and “second dimension” politics about
sociocultural governance should not be counted out (cf. McCarty et al. 2006; Kitschelt and Rehm 2013)
Fourth, finally, we should not forget that the economic interest group literature ignores large and electorally influential occupational groups that traditionally have weak associational mobilization, but that are nevertheless substantial electoral forces able to shape partisan strategies and policy choice. Across a broad range of countries, this applies especially to the growing numbers of sociocultural professionals who are not the main, traditional constituencies of labor unions, but who organize through specialized professional associations or even public interest groups, few of which have any direct national weight in policy making. We made the point that these socioeconomic groups are electorally important earlier; now let us emphasize, however, that particularly for these politically aware and interested citizens the mediation of their concerns through electoral partisan vehicles is absolutely crucial, as their associational vehicles are unsuitable to deliver much bargaining power over policy-making. In a similar vein, the petty bourgeois self-employed in crafts, retail, and increasingly social service sectors still constitute a vocal force in a number of advanced democracies, particularly in the Mediterranean countries, although they have never produced strong national interest associations. Lacking powerful associational articulation, petty bourgeois tend to mobilize above all in the form of electoral populist parties. Both sociocultural professionals and petty bourgeois together with their families may well account for 40 percent or more of national electorates in most democracies, but in different proportions (sociocultural professionals dominant in some, petty bourgeois in others). The traditional fixation in the political economy literature on big corporate capital and organized wage labor tends to ignore these large categories of citizens and the vital importance of electoral mediation for the pursuit of their interests.
1.3. Constrained Partisanship at Work: Feasibility Sets and Political Dynamics in Advanced Capitalism

We turn now to the final stage in our analytical account, which involves using the theoretical framework to analyze the likely politico economic dynamics in advanced capitalist societies. The presence of news shocks that actors have to work through and the two-dimensionality of the competitive policy space and options call for a dynamic analysis of coalition building, political choice, and change that does not (yet?) result in equilibria.

As the shocks of occupational change, demographics, and globalization put pressure on incumbents to devise new policies and find new budgetary resources, they face tough choices. Our framework predicts that governments – depending on the electoral coalition they are based on – have opportunities for innovation, but the range of options available to them is limited by both electoral and institutional constraints: there are paths of institutional reform and adjustment that are outside the feasibility set for newly elected leaders, whereas others are within the range of feasible strategies. More precisely, we argue that governments in different polities start out in a configuration of institutional legacies regarding both the profile of state intervention (consumption vs. investment) and its level, which puts certain policy strategies to the forefront. Moreover, they also start out in a political-electoral configuration of preferences and power relations that makes particular interests and groups pivotal politically.

Analytically, we consider three possible types of policy reform:
- **Marketization**: policy reforms that make access to or levels of either consumption or investment policies dependent on the individual’s situation in the labor market. The reduction of minimum, non-contributory unemployment benefits or pension benefits, or the privatization of education are examples of marketization in consumption and investment policies. In terms of expected outcomes, marketization leads to more inequality.

- **Segmentation**: policy reforms that stratify the access to consumption benefits or investment services across different groups of the population via regulation. Access to particular benefits, such as pension rights, health benefits, or educational opportunities by type of contract or other legal-regulatory markers are examples of segmentation. In terms of expected outcomes, segmentation also leads to more inegalitarian outcomes as it exacerbates divisions between different types of insiders and outsiders (core workers vs. marginal workers, natives vs. immigrants, etc.) with respect to consumption and investment policies.

- **Inclusion**: policy reforms undertaken to broaden the pool of beneficiaries in either investment or consumption policies. Removal of barriers to access to basic pensions between contributors and non-contributors, expansion of access to child-care to all, or removal of restrictions to access higher education for low income families are all policies that exemplify the idea of inclusion. Inclusion is in large part the antithesis of segmentation. At the extreme, universalist policies are the most inclusive of all.
From any given status quo ante the combination of reforms undertaken by incumbents shapes the transition towards possible alternative equilibria. Our analysis of the dynamics of advanced capitalism rests on three claims, to be substantiated below:

1. In addition to all the common challenges associated with postindustrialism, political conflict revolves around a number of issues that are specific to each pre-existing equilibrium. Policy legacies generate effects and constituencies of their own. Hence, a certain degree of specificity in the type of problems to be confronted is to be expected.

2. What parties can do depends in turn on the feasibility set of policy reforms for each quadrant. Conceptually, this implies that there are policy reforms inside the feasibility set (i.e. available for different partisan coalitions to choose from) and paths of policy reform that are out for reach. The feasibility set depends upon state capacity, past policy legacies, and the electoral constraints they face by virtue of the composition of their coalition of support. Figure 1.7 maps out the feasibility sets for different politico-economic configurations in advanced capitalism.

3. While political coalitions can undertake horizontal and vertical movements toward adjacent cells, so to speak as “incremental” change of policy from respective status quo ante starting points, we consider distant diagonal moves across the entire policy space to lie beyond the policy feasibility set of any coalitions. Put simply, governments either lack political support or the institutional capacity to pursue them. An important caveat is in order: we are talking about policy reforms to be enacted within one electoral term. In the long run, governments can shift their policy regimes in any direction of the political space. Our argument simply states that direct transitions along the diagonal are unfeasible within the limits of one legislative term.
In what follows, we substantiate these claims on the basis of an in-depth analysis of the political dynamics in each of these quadrants. For each quadrant, we provide the same sequential analytical treatment: (1) status quo equilibrium (policy & supporting coalition); (2) challenges; (3) potential coaltional strategies and feasible paths; (4) illustration of actual policy moves on the basis of relevant country experiences. We conclude by bringing the core lessons from the analysis of each quadrant together.

1.3.1.- Equality Oriented Capitalism: Challenges and Evolution

Status Quo Equilibrium

Equality oriented political economies are characterized by encompassing welfare states, with a strong component of social services. These configurations reflect the long term dominance of Social-Democracy\(^\text{14}\) (Castles 1978; Stephens 1979) and rest upon three pillars: (1) a cross-class compromise by which strong unions (Hassel, this volume) facilitate wage compression at the top in exchange for generous consumption and investment policies and large levels of private

\(^{14}\) The dominant position of the Nordic Social Democrats can be explained by a combination of structural advantages: On the one hand, because of the absence of both a religious cleavage and a strong communist challenge, they did not face significant competition for the working-class vote (Przeworski and Sprague 1986); on the other hand, the traditional divisions on the Right (with a farmers’ party complicating the classic opposition between liberals and conservatives) weakened their main competitors.
investment; (2) an institutional system of coordination, both in the economic and the political arenas (Iversen and Soskice 2006, 2009), that allowed unions, employers and political coalitions to overcome commitment problems in the short run and develop long-term economic strategies; and (3) a rapid expansion of the public sector as a way to develop investment policies and absorb the employment surplus of deindustrialization. As a result, equality oriented welfare states have achieved both low social inequality and high investment ratios.

Over time, the expansion of the public sector altered the balance between different occupational groups, increasing the relative weight and socio-political importance of sociocultural professionals who have become the core electoral constituency in these countries (Esping-Andersen 1996; Oesch, this volume). The erstwhile dominant working-class organizations have transformed over time by nurturing an electoral constituency of sociocultural professionals that is partly supportive of their goals, but partly transcends their objectives. These (mostly state-affiliated) groups press for investment oriented social policies, particularly in the realms of education and family policies, and they clearly support overall strong state intervention. Hence, the dominant electoral coalition in these economies is one of sociocultural professionals and organized labor. The policy package that has held them together historically is a combination of generous universal social insurance with large-scale efforts devoted to innovation and human capital formation. Business in this model was de facto subsidized with relatively lower tax burdens and a highly trained labor force willing to undertake major skill investments.
By virtue of this particular solution to the democratic class struggle, these societies were typically characterized by a policy legacy of large budgetary commitments, a very inclusive set of both consumption and investment policies and, accordingly, very low levels of either labor market segmentation or marketization.

**Challenges**

Yet it is the very inclusiveness of the system, arguably one of its core strengths that came to be perceived by many political actors as a potential source of weakness. Three developments put the traditional policy strategies under pressure. First is a very high and growing fiscal burden is effectively narrowing the room to increase consumption taxes further or reduce the progressivity in income tax returns (Mares 2006; Beramendi and Rueda 2007). Second, at the same time some businesses and high wage earners, namely, those with a strong earnings potential in the international economy, may find tax levels and wage binding agreements too straight a jacket and start to mobilize against them.

These tensions have built up over a long period of time, as illustrated, for instance, by the Swedish experience. After its golden age in the fifties and sixties, the Swedish model ran into increasing difficulties as a result of the changing structure of the national economy (deindustrialization/tertiarization, technological change in industrial production, feminization of the workforce), which implied an increasingly heterogeneous risk profile in the workforce. This reflected in large part a changing international context (1973 oil crisis, deregulation and integration of financial markets, multinationalization of Swedish corporations) which made Swedish business less dependent on the national economy (Pontusson and Swenson 1996) and
undermined the financial instruments (national credit controls and devaluations of the national currency) that had traditionally been used to stabilize the Swedish model (Huber and Stephens 1998).

These developments threatened directly the stability of the cross-class coalition between low and high wage earners on the one hand and business on the other. In an effort to protect the relative position of low skilled workers, the LO turned to the Social Democrats to legislate a series of measures to democratize working life and to control investments by other means. The most radical element of this program was the wage earner funds, which were conceived “as a mechanism to socialize the economy and reverse the trend toward the concentration of economic power in private hands” (Steinmo 1988: 431). This move of the unions toward an accentuation of the equality model provoked a massive counteroffensive by the business community that not only led the Social Democrats to abandon the wage earner funds (1982), but eventually induced the Swedish employers’ association (SAF) to withdraw from the key institutions of the Swedish model of corporatism (1990) and, supported by the neoliberal ideas of allied think tanks and academic economists, to contest the legitimacy of the Swedish model altogether (Blyth 2001). The erosion of the Swedish industrial relations system went hand in hand with the Swedish Social Democrats’ loss of power in the 1991 elections. This example illustrates the extent to which fiscal sustainability exercises pressure to re-draw the coalitional map in equality oriented capitalism.

Third, the policy inclusiveness built in the model has in more recent years opened yet another political divide within the original coalition: a growing inflow of immigrants and their access to universal services and insurance policies has fed resentment throughout the labor
force. For low-wage earners, immigrants are competitors in access to transfers and services. Sociocultural professionals, business professionals, and managers, perceive immigrants as a lesser competitive threat and express more tolerance toward diversity, even though a proper integration of immigrants may increase their very significant fiscal burden. Immigration thus becomes a major political divide among workers not only in identity or cultural terms but also, critically, in purely distributive ones.

Coalitional Options

In the face of these challenges, what can office seeking parties do to succeed in building or preserving governing coalitions? Given the transformations in the structure of political demand outlined above, political parties articulate their platforms around two issues: calls for ensuring the fiscal viability of the state and, closely linked, demands for introducing some degree of segmentation in the labor market. Figure 1.8 displays the possible coalitional strategies available to parties.

The urgency to respond to the pressures posed by a growing fiscal burden and immigration triggers two possible coalitional realignments. The first one would involve an alliance between socio-cultural professionals, business and managerial professionals, and large employers. This strategy would open up opportunities for private supplementary insurance (pensions, health care) or defined contributions plans for high wage earners relieving them from redistributive burdens in the public social insurance pools. This policy would be carried by a coalition of all high-skilled professionals, moving the political status quo from equality towards competitiveness via marketization. In strategic terms, the existence of this opportunity for center-right parties may force Social-Democrats to adjust their preferences and offer, for the
sake of political survival, policy changes aimed to retain high wage earners as part of their core constituency.

A second, potentially concurrent, shift in the coalitional strategy would concentrate primarily at the lower end of the wage distribution. The idea is to respond to the challenges of immigration by increasing segmentation in the labor market. This would imply a move towards status via segmentation. The goal is to preserve the stability of the coalition between socio-cultural professionals and low wage earners by introducing a clearer distinction – or dualization – between those who are both contributors to and recipients from the system, and those, such as lower-skilled immigrants, whose labor market trajectories may put them in a position to extract net benefits. These reforms, fiercely advocated by new challengers, such as radical right populist parties, force incumbents to concede reforms in order to preempt massive political losses among core members of their coalition.

These two sets of reforms are gradually transforming the nature of equality-oriented capitalism. But none of them should be interpreted as a full scale-transition towards a different politico-economic model. Full dualization, for instance, would imply a model in which insiders enjoy high levels of protection via consumption policies and a sharp decline in investment levels via public services, both strongly opposed by sociocultural professionals, business, and parts of labor alike. Such a move is clearly off the political realm of feasible reforms, as is a nearly impossible transition to a regime built around the ability of organized interests to capture rents. In terms of political coalitions, this implies that the petit bourgeois cannot be the core building block of any feasible political coalition in equality oriented capitalism. Its unwillingness to contribute to the common pool of resources via taxes and its antagonistic approach to both consumption and investment policies alienate them from both business and organized workers.
Empirical Illustrations: Sweden and Denmark

Sweden and Denmark provide prominent examples of the type of coalitional moves our argument suggests. In 1992, Sweden, together with Finland, was hit by a dramatic financial and economic crisis – the deepest and most complicated crisis in its modern history. The fact that this crisis had hit when the center-Right was in power gave the Social Democrats the chance of a fast comeback. Constrained by the employers’ associations’ neoliberal positions and the fiscal consequences of the crisis, Social Democrats reconstructed the industrial relations system and reformed the Swedish social and economic policy. The reemerging industrial relations system was clearly a step in the direction of marketization. Central collective agreements became thinner, establishing a set of principles and procedures for predominantly local bargaining and wider discretion at the firm level (Baccaro and Howell 2011: 29). In addition, the new Social Democratic government consolidated a sharp reduction in income tax progressivity, taking another step in the direction of marketization (Bengston et al. 2012). These reforms provided a favorable context for export-oriented growth by combining a hard currency and price stability policy with a balanced budget (Benner and Vad 2000: 426ff.), which in turn fed back into growing tensions between high and low skilled workers, slowly eroding the Social Democratic coalition.15 These tensions exacerbated electoral trade-offs for center-left parties in Sweden. In their analysis of Swedish elections between 1994 and 2010, Lindvall and Rueda (2013) show

15 This reorientation was underpinned by the decision to join the EU, a move seen as a way to lock in these policy changes.
that if center-left parties emphasize the interest of insiders (as in the 1998 election)\textsuperscript{16}, low skilled, low wage, outsiders tend to either abandon politics altogether or switch towards radical right parties. By contrast, when center-left parties reform policy in a more inclusive way to retain outsiders (as in the 2006 and 2010 elections)\textsuperscript{17}, high wage earners shift their support in favor of center-right parties and their platform of pro marketization reforms. Eventually, the electoral success of the Swedish Social Democrats declined, too, reaching a historic low of only 30.7 percent in the 2010 elections. From 2006 to 2014, Sweden was governed by a center-Right coalition, as Denmark was from 2001 to 2011.

The strength of the challenges and their coalitional implications are even more extreme in the Danish case. In 1993, under the pressure of unemployment peaking at 10 percent, the incoming Social Democratic government, in cooperation with its social partners, introduced key labor-market policy reforms, including an emphasis on activation and a regionalization of the implementation of labor-market policy (tripartite regional boards that strengthened the role of the social partners). Subsequently, given their minority status after the 1994 elections, the Social Democrats had to make compromises with the support of various reform partners (Green-Pedersen \textsuperscript{2001}). Eventually, in 2001, they lost power and for the next ten years, a center-Right coalition stayed in power, supported by the radical populist Right Danish People’s Party (PF). Against the resistance of both the Left and the unions, and aided by the exogenous shock of the financial crisis of 2008, this cohesive government pushed through a series of far-reaching social reforms based on a program combining tax freezes (highly effective in limiting the growth of social expenditures), welfare chauvinism (segmentation through dualization, introducing

\textsuperscript{16} In this election, the incumbent Social Democrats put a low cap at the fees to be paid to access child-care services, a measure that clearly benefited high wage earners.

\textsuperscript{17} Social Democrats, Greens, and the Left party objected to tax cuts and reductions in benefits for the long-term unemployed, a core subgroup among outsiders.
targeted cuts for social assistance, immigrants, and young unemployed), and anti-unionism (exclusion of social partners from the implementation of labor-market policy and breakup of the Ghent system of administrating unemployment insurance) (Rathgeb 2013). Even if the amount of money spent on activation is still comparatively large in Denmark, these reforms turned the pre-existing “flexicurity” model into something very different – a “work-first” regime in which sanctions are at least as important as incentives (Jørgensen and Schulze 2012) and that excluded the unions from both legislation and implementation.

This program catered to the preoccupations of a coalition composed of the business-financial professionals (clearly in favor of marketization) and a significant share of low skilled wage earners (clearly in favor of segmentation and dualization between them and the growing population of immigrant workers). The center-Right coalition succeeded in interpreting the coalitional implications of the changes in Danish society. As a consequence of immigration and individualization, Denmark is no longer the homogeneous society it used to be. Therefore, pressures for marketization at the upper end of the wage distribution and pressures for segmentation at the lower end of the wage distribution jointly undermined the traditional ideal of social partnership (Katzenstein 1985; Campbell and Hall 2009). This is particularly the case among the constituents of the “traditional Left”. In a powerful analysis, Sniderman et al. (2012) show that these voters long for the time when Denmark was a culturally homogeneous and religious country and feel marginalized in the contemporary world, which has lost “a feeling of community.” It is this group, which combines particularistic preferences with preferences for strong state intervention and is very sensitive to the sirens of the radical populist Right.

These two cases illustrate the scope of changes in equality oriented capitalism in the last two decades. As Thelen (2012, 2014) suggests, these societies have followed their own path of
liberalization – the path of “embedded flexibilization,” which involves a combination of lower levels of coordination, market-promoting labor market policies and still-egalitarian social programs designed to ease the adaptation of especially weaker segments of society to changes in the market. Marketization and segmentation have taken place but have not completely unraveled the core features of the pre-existing equilibrium (Schneider and Paunescu 2012). The emerging hybrid policy regimes reconciling equality (solidarity) and market efficiency continue to show considerable success (Emmenegger et al. 2012; Martin and Swank 2012; Häusermann and Palier 2008; Pontusson 2011), but it is too early to tell how much egalitarianism will change as the inherent tensions within the model continue to exacerbate.

1.3.2- Status Oriented Capitalism: Challenges and Evolution

Status Quo Equilibrium

The dominant equilibrium in these societies features encompassing, but status-preserving social insurance security nets with relatively limited redistributive capacity. Status-oriented polities are typically “premised on segregated risk pools” (Palier and Thelen 2010: 122). Coverage has become inclusive over time but has remained fragmented, stratified, and often indirect, especially for spouses and dependent family members. The core electoral constituency both social-democratic and moderate right-wing (often Christian-democratic) parties have been competing for in these party systems is labor, more specifically the core workforce of the main manufacturing industries. The pivotal electoral position of this class is one of the key reasons why status-oriented polities have been built around the consumption needs and demands of the industrial male breadwinner workers and their employers. Labor in these countries tends to be
organized in different political parties and in both sectorally and ideologically fragmented unions. Therefore, the cross-class policy compromises that have emerged from this structure of interest representation are segmented, as well.

The preeminence of the actuarial insurance principle brings together labor as the key socio-structural constituency favored by such strong, stratified, and consumption-oriented welfare states, with the petty bourgeoisie and business. By virtue of their design, these political economies generate a lower share of sociocultural professionals in the labor force than equality-oriented political economies. In contrast to equality oriented capitalism, the key characteristic of the allocation of rights and benefits in these countries is a tight link between employment and entitlements, which is reflected in the strong reliance on financing state activities through contribution payments, that is, payroll taxes. For instance, until the 1990s, social insurance contributions increased to more than 40 percent of total taxation in France and Germany (Manow 2010: 292). Unsurprisingly, these regimes have a much weaker redistributive impact. Insofar as these welfare states have supplied redistribution, it proceeds from families in the upper middle to the lower middle of the income distribution, rather than through highly progressive benefits targeted to the very poorest.

Challenges

Much like in the case of equality oriented capitalism, the structural transformations reshaping advanced capitalism since the early 1980s adopted the form of some specific challenges in these political economies. As the labor market surplus of deindustrialization required responses, governments decided to fight unemployment by shedding labor (through early retirement, the discouragement of female employment, or easier access to disability pensions), thus entering a seemingly vicious circle of declining state revenues, soaring
consumption social expenditures, and increasing contribution rates, which just discouraged employment performance further. By the late 1990s, status-oriented countries such as Germany and France were considered “frozen landscapes” (Esping-Andersen 1996: 24), suffering from the symptom of very high levels of consumption expenditures with an eroding tax basis. The growing gap between rapidly increasing budgetary demands and a shrinking revenue base was particularly intense in status oriented capitalism. These tensions are only exacerbated by increasing levels of immigration. Immigration matters for two reasons: it increases the budgetary burden, and it increases the within class heterogeneity, thus weakening the support for the defense of the status quo among wage earners, particularly at the lower end of the wage distribution (Shayo 2009). These trends in turn shape directly the evolution of coalitional politics in these political economies.

Coalitional Options

In terms of preferences, the risk of excessive generosity to consumption demands, particularly pension systems requiring high payroll taxes, jeopardizes the viability of export-oriented industries, and therefore higher income classes may support reforms oriented to more public sector efficiency. On the other hand, organized labor strives for the maintenance of the status quo in terms of protection and consumption, particularly in the case of low-wage earners in declining manufacturing sectors, while perceiving economic globalization and immigration as sources of the increasing threat to their labor market conditions.

Given this map of preferences and institutional legacies, what are the options in terms of coalition formation? Governments may form an alliance between organized labor and especially small and medium-sized business to further increase the levels of labor market segmentation, meaning that the core maintains the status quo, whereas the outer buffer becomes exposed to
tougher conditions, in terms of both salaries and social insurance packages. This allows business to secure fiscal solvency and a lesser tax burden, whereas organized insiders achieve what could be called welfare protectionism (Häusermann 2012: 117). The obvious losers of this strategy, labor market outsiders in weakly organized sectors, tend to be marginalized politically. This move would effectively imply an increase in the degree of budgetary capture by a more selected group of insiders, limiting consumption benefits to themselves, and the petit bourgeois, limiting their tax contributions to the common pool. Thus, figure 1.9 below depicts this movement towards capture through higher levels of segmentation (implying effects of marketization for the outsiders). The end point of this move is a large yet highly segmented welfare state, composed of a protected core of wage earners and a growing belt of lesser paid and more weakly protected workers. These marginal workers usually have only restricted levels of access to regular social insurance and are instead relegated to (more or less generous) means-tested social security programs.

Alternatively, incumbents (or challengers) may opt for a strategy more oriented toward sociocultural professionals, seeking an alliance between the latter and organized labor. This would be a move from Status towards Equality, as captured in 1.9, via higher levels of inclusion through the extension of consumption or investment policies. Such a move is more likely in status oriented political economies with more moderately organized labor and more flexible labor markets to begin with. The end point along this path is a flexicurity-oriented model of flexible labor markets, high rates of labor market participation, and inclusive social protection for atypical workers.

What seems politically unfeasible, however, when starting from a status quo of segmented, consumption-oriented social policy is a drastic move towards a de-regulated, market driven, competitive model of allocation of economic resources. The preferred option for top
managers and some businesses, this option meets the resistance of both organized labor and sociocultural professionals, and even the petit bourgeois. Given the relative size of these different groups, we regard such a transition as politically and electorally unfeasible in the short run.

Figure 1.9.

Coalitional Politics in Status Oriented Capitalism

Empirical Illustrations: France, Germany, and the Netherlands

In response to the challenges outlined above, French, German, and Dutch governments have, from the 1990s onwards, defied the picture of inertia and implemented a series of “ambitious” (Vail 2010: 83) and even “path-breaking” (Hemerijck 2013: 183) reforms aimed at fiscal balancing and employment creation. The politics of this attempted turn toward both activation as well as lowering the preponderance of consumption expenditures is highly revealing with regard to our analytical model, because it shows the range of feasible coalitional options governments have had in these countries. A brief discussion of the main reform strategies of different governments in France and Germany in the next paragraphs reveals that the manufacturing working class has remained a pivotal constituency in these status-oriented polities: The turn toward more investment-oriented strategies of activation and job creation generally did not occur at the expense of the formerly privileged core workers. Rather, governments to a large extent preserved the rights of the core workforce but pursued segmentation by liberalizing, activating, and retrenching at the margin, that is, among service sector employees, atypically employed workers, the young, and others. This strategy of segmentation and dualization (Emmenegger et al. 2012) exacerbates the fragmented and
stratified nature of these systems with the support of a coalition of the core workforce and industrial employers (Palier and Thelen 2010). In sharp contrast with these two experiences, the Dutch case, arguably a traditionally status-oriented polity, has successfully engaged in a more investment-oriented path of more egalitarian activation and universal welfare (inclusion through flexicurity).

French governments started in the late 1980s to move from labor shedding to encouraging employment growth by liberalizing and increasing nonstandard work, and in particular by expanding state-subsidized employment (Palier and Thelen 2010: 130). As far as this strategy of publicly subsidized job creation was supposed to generate stable and profitable employment in the longer run, it can be seen as an increase in investment-oriented expenditures. The accent of all French governments’ reforms since the late 1980s, however, was not on investment or (de)regulation, but on consumption welfare policies, that is, on reforming the distribution of social insurance benefits and their financing, to preserve the model of the French social insurance welfare state for the core workforce, while relegating the nonstandard employed to a separate area of tax-financed, means-tested welfare (Palier 2010). Such a dualizing strategy relied on the support of organized labor and (strongly subsidized) business but further exacerbated the segmented, particularistic, and inegalitarian aspects of the French welfare state. Left-wing governments, typically reliant on a coalition of labor and sociocultural professionals, have thus put stronger accents on the creation and reinforcement of rather generous universal minimum income schemes, which to date have managed to prevent the rise in income inequality that we observe in the other continental European countries.

Hence, while both left- and right-wing governments segmented the French labor market, broadening the gap between insiders and outsiders, Left governments expanded consumption benefits to prevent outsider poverty, starting most markedly with the introduction of the _revenu_
minimum d’insertion (RMI) in 1988 by the socialist Rocard government. The conservative governments in the 1990s then continued to encourage employers to expand part-time and fixed-term work by exempting these contracts from social contribution payments. On the expenditure side, the Juppé government famously failed to curtail pension and health benefits in the mid-1990s: These reform proposals were purely retrenchment-oriented, mobilizing a massive and unified labor protest against them in the streets (Häusermann 2010). The failure of the Juppé reforms showed that despite weak union density, the core workforce’s full opposition could not be circumvented.

The socialist Jospin government that took power in 1997 attempted a more fundamental redesign of the French labor market and welfare financing from consumption to investment (Levy 1999: 246–252), without, however, even touching the hot potatoes of pensions and health care. Regarding the labor market, the government introduced massive subsidization of employment for young labor market entrants, created a negative income tax for low-paid employment, attempted to distribute employment by reducing the regular work time and – most importantly –broadly increased the fiscalization of social security charges. The Jospin government increased the contribution social généralisée, a tax levied on all forms of income, from 3.4 to 7.5 percent, thus widening the tax base and alleviating wages. This tax reform managed to reduce the cost of labor, but it also served the goal of generating tax-financed revenues to finance the “noncontributory” benefits for social insurance outsiders. It thus deepened the “social protection dualism” (Palier 2010) of the reformed French welfare state, at the same time alleviating some of the exclusionary social policy consequences of labor market segmentation. The right-wing governments that assumed power after 2003 followed the path of expanding low-wage employment (e.g., the contrat première embauche by the Villepin government in 2005), while reinforcing the accent on negative activation and workfare by
transforming the RMI into a conditional benefit with higher benefits for in-work individuals. In addition, they retrenched pension levels significantly, watering down the cuts, however, for core workers with long employment careers (Häusermann 2010).

In sum, this brief overview shows that none of the French governments significantly lowered consumption benefits and rights of the core workforce. Rather, they differed in the extent to which they expanded specific benefits and services for the marginal workforce. For business, the model of dualizing both the labor market and the welfare state (Palier and Thelen 2010) was acceptable, because it provided employers with flexibility in terms of regulation and wages (Vail 2010: 91).

A similar story of segmentation by design, that is, preserving employment protection for the core workforce while liberalizing and expanding a low-wage sector of nonstandard work, applies to the German trajectory (Palier and Thelen 2010). Both the Conservative Kohl government in the 1990s and subsequently the Social-Democratic and Green Schröder government around 2000 lowered the restrictions on the use of agency workers and fixed-term employment and encouraged the spread of “marginal employment” exempt from social contributions (Vail 2010). In consequence, as in France, the distinction between social insurance and assistance was sharpened in Germany. Another similarity appears in the fact that the conservative Chancellor Kohl attempted radical retrenchment against labor in the mid-1990s with his 1996 pension reform and failed. The pension reform backfired at the polls and put the Left in power after sixteen years of Christian-Democratic rule. As with the failure of the Juppé reforms in France, this failure of retrenchment against organized labor demonstrates the pivotal role of organized labor in status-oriented polities.

The years of the red-green government, however, deviated from the more timid French reform trajectories by the ambition and scope of the reforms. The German red-green government
that lasted between 1998 and 2005 is the only government that seriously attempted to reallocate resources from consumption and insider privileges toward investment, activation, and flexicurity. In coalition terms, it is fair to say that the Schröder government tried to shift reform efforts from the consumption to the investment-oriented axis, attempting almost a diagonal move toward competitiveness, with the support of a coalition of business and sociocultural professionals. Indeed both groups worried about the financial unsustainability of the consumption-heavy profile of the German welfare state and were open to measures of financial consolidation. The Schröder agenda involved a mixture of competitiveness-oriented elements of tax cuts, retrenchment, and liberalization, with equality-oriented investment and some improvement through universal minimum protection. Most instructively, this attempt ultimately failed. Such a move would have required a strong alliance of sociocultural professionals, parts of business, and parts of labor. Against such an alliance worked the fact that precommitted consumption expenditures continued to impose strong constraints on the expansion of investment.

In terms of retrenchment, the 2001 pension reform was probably the most significant project. The reform lowered regular pension replacement rates substantially, while introducing a new voluntary pillar of private, capitalized pension saving. At the same time, minimum pensions for people with discontinuous employment careers were improved and major financial incentives were introduced for low-income workers to take up supplementary insurance. This mixture of retrenchment, privatization for the higher-income classes, and subsidization for the outsiders proved successful politically, but it was possible only against labor, that is, in direct confrontation with the trade unions (Häusermann 2010). This split between German Social Democrats and trade unions intensified around the Hartz labor market reforms. While the unions had supported the early reforms of the government in favor of youth employment (JUMP
reform 1998) and activation and retraining (Job AQTIV law 2002), the Hartz reforms of 2002–2005 drove a deep split between the government and organized labor. The most consequential reform was the Hartz IV legislation, which merged long-term unemployment benefits (after twelve months) and social assistance into a new, tax-financed unemployment benefit II (which could also be paid as an in-work benefit), combined with stronger activation requirements. The distributive consequences of the reform are somewhat controversial (Palier and Thelen 2010: 138), but it clearly and most drastically cut the benefits for well-insured labor market insiders, while it actually provided a boost for an estimated one-third of those who were previously in the lowest tier of the old social assistance system, such as single mothers. However, as the unemployment benefit II was set very low and regular employment protection remained intact, the reform still negatively affected large parts of low-wage earners. Finally, regarding activation and investment, the Schröder government reinforced training and retraining programs, supported a large-scale reorientation of the higher education system toward more competitiveness, and initiated a profound reorientation of family policy toward child care and the encouragement of parental employment (Häusermann 2006; Bleses and Seeleib-Kaiser 2004).

Ultimately, the reforms of the Schröder government, tried to circumvent the core working class as the key electoral constituency, a strategy that backfired. The government lost its majority in 2005, and a new radical left-wing party (“die Linke”) entered the party system with a program emphasizing traditional consumption demands of the working class. During the following years of the grand coalition of CDU-CSU and SPD between 2005 and 2009, the government basically pursued the competitiveness- and investment-oriented agenda of the social-democratic government (e.g., by increasing the age of retirement to sixty-seven, lowering options for early retirement, and expanding child care options for middle-class women), while the radical Left
continuously grew in strength. In reaction, both SPD and CDU/CSU reoriented their electoral and programmatic focus to some extent back to the interests of labor. Unemployment benefit regulations were, for example, upgraded for elderly unemployed adults and family policy was reoriented toward more conservative male breadwinner concerns under the CDU/FDP coalition. Overall, the reform trajectory initiated by the SPD/Green government was an experiment appealing to an alliance of professionals of all stripes (socio-cultural and business-finance), but given the strong pivotal electoral and organizational position of labor in this country, the strategy was not viable politically. Agenda 2010 was an attempt to override labor, but by the mid-2000s, both Social-Democrats and Christian Democrats had realized the limits of such a coalitional strategy in a polity marked by a status-oriented institutional and electoral legacy.

The one country that arguably has managed a turnaround from a status-oriented model to an investment- and activation-oriented polity, that is a significant shift along the vertical axis in 1.9, is the Netherlands (see also Figure 1.2). It must be noted, however, that the Dutch welfare state had also traditionally deviated from the social insurance model by providing a basic public pension and tax-financed minimum assistance. Also, the Dutch unions decided in the 1980s already to support the activation strategy by the then-conservative CDA/VVD government (Levy 1999: 259), which may have been the pivotal point for the feasibility of a long-term strategy of equalization and inclusion in terms of combining a flexibilized labor market with social security.

When Labor entered a coalition with the conservatives in 1989, they asked for a stronger accent on equalization in the competitiveness-oriented activation strategy of the Lubbers government (Hemerijck 2013: 182). The deal was to make consumption expenditures conditional on activation: Full indexation of minimum wage and social benefits was conditional on a certain threshold of the ratio between the active and inactive population. From 1994 onward, successive social-democratic-led governments massively expanded (female) employment in the service
sector, introduced targeted tax breaks for low-income workers, made consumption exit options such as disability pensions more costly for employers, and improved employment conditions for atypical workers (Visser and Hemerijck 1997). A “flexicurity agreement” with the social partners in 2000 granted part-time workers explicit right to equal treatment in all areas of social security and equal wages. Hence, Dutch employers hire part-time workers as a means of organizational flexibility, not as a means of evading taxes and benefits paid to regular workers (Levy 1999: 262). Combined with efforts in the field of child care to support female employment, this long-term activation strategy resulted in the inclusion of nonstandard work. This reform was possible only because Dutch organized labor supported a transformative shift toward encompassing and investment-oriented interest representation already in the 1980s. Over time, the support base of the new policy strategy increased with the transformation of the occupational structure itself.

These three cases illustrate the evolution of status oriented capitalism over the last two decades. Attempts to transition towards competitiveness via a combination of marketization and investment have backfired because of the continuing pivotal position of organized labor. The dominant response by governments has been an increase in the levels of segmentation at the expense of outsiders. Only in the case of the Netherlands, there is systematic evidence of a transition towards an investment oriented strategy around flexicurity. That this is the case where the institutional legacies of status oriented polities were least present illustrates the long shadow of organized labor in coalitional politics within this subset of political economies.

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18 Hemerijck refers to this process as “labor market desegmentation” (2013: 183).
1.3.3.- Competitiveness Oriented Capitalism: Challenges and Evolution

*Status Quo Equilibrium*

The status quo in competitiveness oriented capitalism is a selective welfare state, with highly redistributive programs targeted to the very poorest, thereby implying a very high level of marketization from the start. Traditional partisan alignments pit mildly redistributive reformist parties against often militantly conservative free-market parties have geared public policy toward only restrained market intervention without a strong commitment to either large-scale consumption or investment policies, thus limiting the level of state intervention overall. Political coalitions collect and use revenues less than at full capacity, and therefore provide less extensive safety nets and public services.

Given the weaker level of public services generally, the growth of professional occupations in the interpersonal social service sector, particularly those serving the poorer tiers of the population, is more limited in this configuration. Rather, the centerpiece of governments’ support coalition has typically been big business and professionals, particularly in financial industries. The fragmented and uncoordinated nature of the labor movement, along with the dominant position of financial capitalists and business organizations renders the transition to any form of full-grown state led investment or consumption regime a political chimera.

Traditionally the conservative partisan coalition has been supplemented with support from small business and intermediate level wage earners, whereas reformist parties have drawn on organized labor and a wide range of intermediate occupational groups, as long as they walked a fine line not to antagonize business. More recently, with the erosion of small business and of low-skill wage earners in the voting population, both sides have vied for the support of the
growing segment of sociocultural professionals. As we discuss below in detail, failure to win majorities in this group spells defeat for the moderate Left.

Challenges

The major challenge of efficiency-oriented capitalism lies in the increasing polarization of income and wealth resulting from the shocks of technology. By rewarding those with very high and adaptable education, and globalization, and further penalizing citizens with low occupational skills and general education, efficiency oriented capitalism nurtures an extremely skewed distribution of fortunes. At the other end of the one percent, there emerges a tier of very low-income, low-education immigrants, most starkly articulated in—and already politically consequential—in the United States (cf. McCarty et al. 2006; Picketty 2014: 291-303). Even with relatively strong aggregate investment policies, the distribution of beneficiaries, for example in the education system, is so skewed to the well-off that major groups of the population are left behind, whether these are low skilled citizens in the dominant ethnic group or the much larger proportion of low-skilled individuals among minorities and immigrants. Here more so than in other capitalisms, the middle-income tier is hollowed out by the increasing restriction of economic opportunities at the upper tier of the income distribution.

Among the key challenges of efficiency-oriented capitalism is the incorporation of a growing proportion of practically illiterate young labor market entrants, unfit to compete for jobs in a postindustrial economy that could deliver a working wage. At the same time, there is also growing poverty and destitution among the elderly, now increasingly also affecting the retirement prospects of the ethnically indigenous majority. This is setting up a deep divide between those who want to invest more and broaden the scope of education and training (enabling young labor market entrants of diverse backgrounds to enjoy a more promising
occupational career) and those who prioritize improving the lot of older low-skilled wage earners and the self-employed (either by more defensive social insurance schemes or by lower income and payroll taxes).

**Coalitional Options**

This polarization of fortunes has direct implications for the prospects of political coalition formation, as captured in figure 1.10. Conflicts tend to center around extensions of the level of public investments on the horizontal dimension (a leftward horizontal move towards equality via inclusion) and tolerance towards the ability of organized interests and lobbyists to shape policy (a downward vertical move towards capture via an increasingly unequal access of lobbies, resulting in enhanced segmentation).

**Figure 1.10.**

*Coalitional Politics in Competitiveness Oriented Capitalism*

Parties and/or governments oriented towards the support of a coalition of professionals both in sociocultural services and in the large-scale corporate business and finance sectors in these polities would aim for a business- and employment-friendly coalition in favor of equality of opportunity-enhancing investments. This will be the dominant strategy by left wing forces in this type of political economies. By contrast, a coalition of predominantly large-scale corporate business and finance, together with small business in consumer and service economies, would support lower levels of state intervention and regulation and strive to maintain their policy influence through lobbying, seeking special interest group rents. This will be the dominant strategy among conservative parties and coalitions.
Sharp inequality compels conservative parties that favor only minimal social insurance or redistribution to attract support from portions of downwardly mobile low-skilled wage earners of the dominant ethnic group (cf. McCarty et al. 2006; Kitschelt and Rehm 2013), for example by appeals to oppose immigration and by emphasizing national identity (Shayo 2009). This creates the possibility of an electoral coalition of low-skilled wage earners and petty bourgeois, both belonging to the dominant indigenous ethnic group and confronting an alliance of professionals and ethnic minorities and immigrants at the other pole of the political spectrum. The former coalition converges on support for narrowly circumscribed and segmented social benefits and minimal overall scope of state intervention, undercutting public social investments, particularly in education. The latter emphasize public investment policy, but, given the realities of policy constraints and make-up of the coalition, has little momentum to mobilize a grand push for more equalization.

_Empirical Illustrations: the UK and the USA_

In Britain, the transition towards efficiency oriented capitalism took place under the Conservative governments of Thatcher and Major (1979–1997). The cabinets pushed systematically pro-market, anti-redistributive policies with little additional investment in education or health care. In their political-economic strategies, as well as with their positions on questions of sociocultural particularism, Thatcher and Major captured the petty bourgeois strata, intermediate groups, at least initially business, as well as even unorganized elements of labor, but clearly antagonized organized lower-skill wage earners, particularly with a brutal retrenchment of the unemployment insurance and especially of the earnings-related component
of the pension system, as a consequence of which Britain faces the prospect of massive old-age poverty in future decades (see Pierson 1996; Galasso 2008: 160–163; Seeleib-Kaiser et al. 2012: 162). In terms of investment policies, the Conservative governments added little to the existing mix. True, enrollment in higher education was broadened, particularly to the upper middle class, but at the price of steeply declining quality, as no new public spending was forthcoming (Ansell 2010: 198–200). Thatcher’s Conservatives disliked the British National Health Service but were politically unable to touch it, with the exception of creating more options for choice by higher income users. Overall, in terms of our two-dimensional scheme, the Thatcher-Major governments stayed close to, or sharply accentuated, political legacy features, that is, limited redistribution paired with restraint on investments, implementing an ideologically conservative program (Huber and Stephens 2001).

Against this background, Tony Blair’s subsequent Labour government provides a good example of a successful coalition between business and socio-cultural professionals towards higher levels of equality via public investments. Blair’s government reversed the redistribution toward the wealthy that had taken place under the Conservatives, and increased significantly investments in education and health care. Most importantly, Blair once again reformed the pension system in order to boost minimum pensions, achieved through a sharper redistributive design of the program benefits that provides relatively more for those with the lowest benefit levels. Nevertheless, public pension benefits for the less well-off remain very low and further deteriorated as the new century wears on (Galasso 2008: 171).

Blair’s government doubled spending on the National Health Service but sustained efforts to create more quasi-market competition among providers and personal choice among users in the spirit of market liberalization (Gingrich 2011b). British education spending, finally, increased by a quarter between 2000 and 2009, that of tertiary education alone by 30 percent (OECD 2012: 162).
244), although the Labour government did not reverse the Conservatives’ tuition policy.\footnote{They actually extended it to make the affluent pay more for their children’s higher education (Galasso 2008: 166).}

Overall, the Labour administration moved to a new course toward slightly more redistribution and a great deal more social investment. This thrust was particularly designed to attract sociocultural professionals who had been antagonized by the party in previous decades to Labour’s electoral coalition, while still providing a business friendly environment (especially among the City’s financial centers).

Relative to the UK, the USA illustrates better a move from efficiency to capture by the increasing role of specialized interest and lobbying over the last three decades. While partisan differences remain prominent, significantly more so than in Britain, the large number of institutional veto points have traditionally given business a lopsided advantage in Washington. Since the 1980s, the U.S. Republicans built a powerful backward-looking, if not nostalgic coalition of white (and male) America, configured around small business, parts of big business, and broad strands of the white working-class antagonized by the Democrats’ efforts to reach out to sociocultural professionals, women, and especially ethno-cultural minorities of many strands.\footnote{These efforts date back at least to McGovern’s 1972 presidential bid.}

In the spirit of this coalition, Republican congressional majorities and presidents worked to enact cutbacks in means-tested welfare support and health care benefits for the poor (Medicaid). A major watershed was the 1996 welfare reform in which a Democratic president relented and made substantial concessions in the face of a Republican onslaught.
Subsequent efforts by Republicans’ to engineer an erosion of social security programs by converting parts of them into defined contributions private savings accounts, however, failed, in part because it divided their own coalition. The U.S. social security system hence remained mildly redistributive toward the worse off (cf. Galasso 2008: 187–189). The 2002 Bush Medicare drug benefit expanded social policy along the consumption dimension by bestowing a new benefit on pensioners, a core group of the Republican support coalition, albeit with the greatest windfall being reaped by the pharmaceutical industry. The Republican coalition opposed higher public investments other than through research and development funneled through military defense. Nevertheless, a bipartisan majority passed the No Child Left Behind education act of 2002, which added a great deal of standardized testing, as well as substantial public educational funding (cf. OECD 2012: 232). This majority pushing the educational investment agenda and was supported by corporate business, on the moderate Republican side, and by socio-cultural professionals, as well as the African-American minority, aligning with moderate Democrats. It was primarily opposed by a radical populist wing of the Republican party whose members even wish to abolish the U.S. Department of Education and whose mass following is particularly strong among white low-skilled men and the self-employed. A similar coalition under the Bush administration (2001–2009) also passed tax legislation with Democratic Senate supporters and budgets that were designed to shift the income distribution in favor of the wealthy and to move policy tasks out of the public realm into the market.

Against this legacy, President Obama was elected by a coalition of sociocultural professionals, minorities of all sorts of occupational backgrounds, and considerable white working-class support, all shocked by the financial crisis of 2008 and the large loss of manufacturing jobs it caused. He has developed since several policy initiatives along to expand
inclusive investments in an egalitarian direction. The Affordable Health Care Act of 2010, as a strategy of inclusion, has prospectively shifted the benefits in a redistributive direction, benefiting uninsured younger citizens most. At the same time, the Democratic president did not tire of advocating more educational effort, but could not back up this claim in the face of a hostile legislature and the financial crisis.\footnote{Federal educational effort made much more progress under Obama’s Democratic predecessor Clinton and even some under Bush.} Overall, with divided government and powerful business interests, activist, interventionist Democratic governments made more headway building policy coalitions around investment-oriented polices than redistributive consumption policies. Even the Affordable Health Care Act fits this bill, as it focuses on children and working-age adults without health insurance who can be productive economic contributors, not retirees. Investment-oriented reforms not only are supported by large sectors of the Democratic coalition (sociocultural professionals, minorities, women), but also are negotiable with large sectors of large corporations that rely on qualified labor, that is, the core constituency of the competitiveness-oriented model. Redistributive-consumption policies, by contrast, fail to rally a winning coalition altogether, when it comes to expanding existing benefits, with the glaring exception of the 2002 Medicare drug benefit act. Conversely, it has been all but impossible to turn back the clock on universal benefits once enacted, such as basic Social Security and Medicare programs for the elderly (cf. Pierson 1996).}

In sum, partisan politics has moved policy making in different directions in both the United Kingdom and the United States. In terms of our analytical scheme, conservatives in both countries opted for an accentuation of the competitiveness model through a withdrawal from market intervention and disinvestment as well as retrenchment of consumption expenditure. By
contrast, center-Left governments, while trying to restore a modicum of redistribution, particularly in health care and sometimes pension systems, focused their strategy on expanding social investments, particularly in education and training. Around the latter, Left governments managed to rally a broad coalition of parts of low-skilled wage labor (albeit divided by ethnic loyalties) and parts of big business, most of the sociocultural professionals, and in the United States, ethnic minorities regardless of occupational and market experiences. Policy, by and large, has remained sensitive to partisan alternatives.

These alternatives are crystallized primarily in the area of investment. While they may pass narrow, focused targeted redistribution to the very poor in brief moments of political-economic crisis, our analysis suggests that the feasible coalitional options preclude them from instituting broad-ranged, encompassing policies with strong insurance and redistributive objectives. Hence, the remains of organized labor, low wage earners, linger outside the space of feasible winning coalitions.

1.3.4.- Capture Oriented Capitalism: Challenges and Evolution

Status Quo Equilibrium

The status quo equilibrium in capture oriented capitalism carries a heavy legacy from late industrialization and late democratization. Late industrialization implies typically a reliance on import substitution strategy. As cogently argued by Rueda, Wibbels, and Altamirano (this volume), state led import substitution industrialization processes generated a core of well-organized manufacturing workers who enjoyed the state’s insurance and protection even prior to democratization. With the arrival of the new regimes, these organized sectors of the labor
force were in a privileged position to protect their interests and became a central constituency for political parties, particularly those on the left of the political spectrum. On the other hand, small business owners, the chief beneficiaries of the spread of economic informality, became a natural focus of attention for conservative parties. The legacy of autocratic forms of social paternalism implies an insurance system tailored to the interests of insiders: Large, expensive, and quasi-regressive pension and unemployment insurance systems eat up most of the welfare budget. As a result, welfare states are deeply segmented and stratified, and effectively regressive in their distributive incidence. There is little to no redistributive solidarity towards the poor. And while public spending on consumption may be sizable, it is directed to relatively narrow sets of interests.

In terms of coalitional potential, sociocultural occupations have remained a marginal part of the workforce. Instead, the pivotal position belongs to two groups: small businesses and organized insiders (Rueda 2007). The former resist any sort of systematic expansion of state involvement in the economy that would require the increase of governments’ capacity to tax. The latter push for consumption policies tailored to their interest, whereas the upper end of the wage distribution rather supports the expansion of public services (investment). With few exceptions, such as health care in Spain or Italy, public services are generally low in quality and transfers benefit mostly a core of well-organized insiders. In such contexts, the lack of effective fiscal capacity finds its correlate in practices of organized patronage and even vote buying at national and local levels (Ferrera 1993, 1996).²² With services provided in small scope and quality, the

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²² As recently assessed by Hemerijck (2013: 197), “The combination of extended households, high rates of self-employment, large informal economies, tax evasion, and an institutionally weak administrative apparatus has created infertile grounds for the modernization of social safety nets based on criteria of quasi-universal coverage.”
family becomes a functional alternative for the purposes of income maintenance and provision of services and care.

Challenges

Capture oriented polities confront the challenges of deindustrialization and international economic integration from the worst possible footing. Their relatively weaker revenue collection capacity magnifies the political trade-offs associated with the push for austerity. Given the highly segmented nature of both labor markets and welfare states, the tensions between the insider core and the outsider's ring are bound to exacerbate and expand to a conflict between different political generations (the excluded young vs. the protected elderly).

These tensions breed a second, more political challenge, directly linked to the push for austerity. Low administrative capacities and the regressive nature of the welfare state (Beramendi and Rehm 2014) translate into fewer differences across political ideologies, further shrinking the realm of programmatic politics. The lack of effective fiscal capacity reduces the scope for political contentions between parties over the scope of the state intervention in the economy. In times of austerity, incumbents of both left and right are forced to pursue reductions in both consumption and investment policies, with direct consequences on the evolution of potential coalitions.

23 In most instances this limitation of the policy space reflects the constraints imposed by the Eurozone. The common currency constraints monetary policy directly, through the ECB, and fiscal policy indirectly, by imposing macro-economic thresholds in terms of public deficits that need to be observed at all costs.
Coalitional Politics

Figure 1.11 outlines the coalitional space in capture-oriented capitalism. Historically, left-oriented parties sought a coalition between organized labor and the emerging socio-cultural professionals around the expansion of services (health, education) and at the expense of the consumption options of those at the lower end of the wage distribution. Such was, for instance, the coalitional strategy of Gonzalez’s Socialist Government in Spain (Boix 1998, Maravall 1996). Right-wing parties, by contrast, sought a very different alliance: one between the petit bourgeois, business owners, and liberal professionals. This coalition would rest on the reduction of consumption benefits for workers, the regulatory protection of organized interests (in particular small business), and the purposeful limitation of the state’s tax capacity.

Over time, the legacy of limited state capacity in an era of austerity undermined the feasibility of both these strategies. The sustainability of a coalition between socio-cultural professionals and organized labor over the expansion of public services requires resources that are simply not available to incumbents. As a result, the left must choose between alienating the socio-cultural professionals by limiting investments or alienating labor by limiting (regressive) consumption. Against a backdrop of weak state capacity, governments will hardly be able to implement policies that deliver more inclusive redistribution or forward-looking investment oriented policies. Hence, the core supporters of large-scale investment fall out of any of the feasible policy coalitions. While a short-term move in the direction of inclusion is theoretically possible, it requires significant tax increases and a reallocation of benefits at the expense of more privileged constituencies. Accordingly, the lack of support by core groups renders these reforms unfeasible. With increasing economic strain, these countries operate under the imperative to reduce fiscal debt and deficits at the peril of declaring bankruptcy. A direct move towards equality via inclusion is out of the short term feasibility set.
This leaves incumbents and challenging parties with a very limited set of alternatives in the era of austerity. At first, conservative parties can ride the wave of austerity and orchestrate a pro-marketization coalition between the petit-bourgeois and large businesses. This alliance rests on the reduction of taxes and, importantly, the reduction of labor market protection and consumption transfers towards insiders. The political feasibility of such an approach has its limits though: pro-austerity wage policies (internal devaluations) and welfare cuts progressively alienate a large share of wage earners, putting pro-austerity incumbents at risk of electoral overhaul.

These dynamics should open up an opportunity for established left parties. Yet the latter are in an odd position to profit from it, for three reasons. First, the push for austerity caught many of them in office and with no room to resist (due to the weak fiscal capacity in their state). Second, any attempt to regain organized labor via enhancing consumption policies favoring insiders would alienate outsiders, high-wage earners, and socio-cultural professionals. And they lack enough government resources to craft a stable coalition across these subgroups. Finally, building those resources through tax increases in the short run is not an option because the medium term-gains will not overcome the short-term costs across employers and high wage earners to make the proposition electorally feasible. Therefore, the shift from capture to status via increased levels of consumption towards insider is within the feasibility set, but remains unlikely to provide a successful, stable coalitional strategy in these societies. As a consequence, partisan conflict over distributive issues becomes blurred.

Figure 1.11.
Coalitional Politics in Capture oriented Capitalism
Empirical Illustrations: Italy and Spain

The fate of major attempts at policy reform in Italy and Spain from the early 1990s until today illustrates the political dynamics of capture-oriented economies. Particularly illustrative are the failures of conscious political attempts to develop a move towards equality via expansions of investment policies in both countries.

Pushed by the EMU and the Maastricht requirements, successive Italian governments faced the challenge of correcting the skyrocketing fiscal burden, mostly driven by pensions directly paid by the Treasury (Jessoula and Alti 2010). Ideological differences among incumbents made them embrace the new context differently. During the early 1990s Berlusconi’s failure to impose a comprehensive program of reform (including reductions in seniority pensions and revisions in reference earnings and indexation mechanisms) contributed to his cabinet’s fall in December 1994. The opposition of insiders and current pensioners, articulated around a massive general strike, blocked the reform. Since the need to meet the Maastricht criteria did not end, Dini’s cabinet tried a more moderate strategy: He successfully managed to disconnect pensions from previous earnings and link them to contributions actually paid, and, via tax incentives, to complementary pension funds. Informed by Berlusconi’s experience, Dini only managed to get these reforms through by introducing a significant time lag for their actual implementation: The reforms would only apply to workers entering the system after 1996, thus sheltering current insiders from any negative implications. The fate of the Italian pension reform is illustrative of the veto power of insiders. However, from the standpoint of our predictions about the dynamics of different forms of capitalism, the (failed) attempts to pursue an investment-oriented strategy by left-leaning governments (Prodi most prominently) are even more revealing.
By the end of the 1990s, scholars and practitioners alike were aware of the unbalanced nature of the Italian welfare state: it overprotected old age and privileged labor market insiders at the expense of outsiders (Ferrera and Hemerijck 2003; Ferrera and Gualmini 2004). To correct these imbalances, left-leaning cabinets pushed forward a series of reforms to reduce the transfer dependency in labor market policy and boost the size and scope of active labor market policies. These included a tighter targeting of antipoverty benefits, the elimination of the public monopoly of placement services, and an expansion of services dedicated to ease labor market transition. The logic, very much inspired by the anti-exclusion and activation focus emerging from the European Employment Strategy, consisted in combining deregulation, activation, and a combination of universal services (in the realm of family policies, for instance) with noncontributory means tested transfers, such as the minimum insertion income. Seen in the light of our theoretical framework, the driving motive behind these policy packages implies a shift from consumption to investment. As Jessoula and Alti (2010: 172) point out, “If fully accomplished, [the reform plan] could have led the Italian welfare state and labor market clearly beyond Bismarck” – except that the program was never fully implemented. The political weakness of Left cabinets vis-à-vis organized interests and insiders, the inability of governments to overcome the budgetary pressures around the convergence criteria, and the eventual return of more conservative cabinets targeting the core basis of insiders stalled the experiment. The net outcome is one of stasis amid budgetary pressures. The elements of the reform pursuing budgetary stabilization remained in place, but by and large the fundamental parameters of a capture-oriented welfare state did not change. Dualization remains largely unchanged, as does the system of unemployment insurance, in an illustrative failure to overcome labor market segmentation. Deregulation stopped and so did the efforts to shift the balance between active and passive labor market policies. During the first half of the 2000s, Berlusconi drastically cut
social policy spending, closed the minimum insertion income, and restored a traditional family based welfare state articulated around community networks (Hemerijck 2013). The latter operated as an important device in his success as a political entrepreneur of the politics of capture. The eventual return of the Left to office for two years did not allow enough time to reattempt a feasible shift toward investment policies before the constraining impact of the Great Recession contributed to reducing observable differences across the parties in Italy's political spectrum.

The evolution of the welfare state in Spain presents a similar picture. The big push toward universalism in education and health during the 1980s, with significant success in health care provision, helped bridge the gap with other European economies by the early 1990s (Maravall 1996). The push was far less forceful in terms of social security transfers, which were only boosted after the general strike in 1988. Social effort as a percentage of GDP peaked at 23 percent right before the economic recession of 1993. Overall, total revenue collection and welfare effort have consistently remained below those of more advanced welfare states. The push to close the investment gap in education did not translate either to social security or to labor market regulations. As extensively analyzed by the specialized literature (Rueda 2007; Guillén 2010) the system was in part an achievement of organized insiders that made the most of its design. Several labor market reforms (1984, 1994, 1996) allegedly designed to increase flexibility in the labor market have only increased the levels of dualization in terms of economic opportunities between insiders and outsiders (Espina 2007). In recent years, conservative administrations have made an effort to reduce the level of regular employment protection, as partially reflected in Figure 1.3, whereas the level of protection of temporary workers has
remained stable.\textsuperscript{24} Along the way, the decentralization of health, education, and social assistance has created a complex institutional environment where reform has become harder to implement (Moreno 1997; Beramendi 2012). The need to fulfill the Euro convergence criteria allowed the Conservative cabinets (1996–2004) to justify austerity and freeze the expansion of social provision relative to needs, while pushing for flexibilization without investment.

It is against this background that Zapatero’s attempt to develop, even if partially, a move towards equality through inclusive investment took place. The two pillars of his strategy were a reinforcement in the scope of research and development and the introduction of a publicly funded comprehensive program of social services for dependent relatives (\textit{Ley de Dependencia}), along with regulatory changes to ease the conciliation between work and family for women (Moreno 2007). In Spain, families and especially women remain the main service providers in case of need, preventing an effective incorporation of the latter into the labor market. The ultimate goal was to rebalance the sectoral weights of the economy in favor of skill intensive sectors and erase some of the constraints imposed by the family-oriented welfare regime that had developed since the transition to democracy. But Zapatero proved unable to modify labor markets to reduce dualization and introduce measures of positive activation for outsiders. The reforms stalled for a number of reasons. Before the crisis, Zapatero lacked the political and institutional capacity to fund and implement them. By virtue of the decentralization process he had to rely on the regions as the executors of the legislation. He did so, \textit{yet without increasing their resources to meet the cost}. He lacked the resources to reform fiscal federal arrangements in a way that would allow the regions to implement this legislation effectively. Unsurprisingly, this

\textsuperscript{24}More recently, the conservative government in Spain has enacted a major reduction in the level of employment protection of regular workers, in a clear move toward the creation of a deregulated labor market. It is too early to evaluate the substantive implications of these reforms at this stage.
created an implementation deadlock that only became exacerbated after 2007–2008. The crisis also forced him to resort first to short-term transfer packages for the benefits of insiders (reelection took place in mid-2008) that depleted his fiscal buffer, effectively doing away with the possibility of implementing an investment strategy.

As was the case in Italy, after 2010 the two main parties became hardly distinguishable in terms of economic policy platforms. Zapatero first, in a remarkable change of course in May 2010 imposed from Brussels, and Rajoy later become champions of austerity. State weakness erased differences between the Left and the Right in terms of economic policy. Before the crisis, both countries saw attempts to eliminate labor market dualization blocked or distorted by organized insiders and governments without the budgetary clout to alter the balance between negative and positive activation in labor markets. Finally, post-crisis reforms appear primarily oriented toward the protection of patronage driven politics, creating a political deadlock on needed institutional reform. Unsurprisingly, this poor institutional and economic performance fed large increases in political disaffection and historic “high(s)” in levels of distrust of programmatic politics, ultimately casting a shadow on the actual functioning of democracy across these political economies.

These two experiences illustrate the difficulties of programmatic politics in capture oriented capitalism. The deadlock of programmatic politics paves the way for alternative political organizations to undertake the mobilization of those groups left out by the politics of austerity. A common strategy across these neo-populist (both left and right) forces is to portray a conflict between “the people” and the political class (or casta, or elite, according to various formulations). The left wing version of this strategy proposes a generalization of consumption benefits to both, insiders and outsiders, an expansion of investment, and a significant increase in taxation, along with a refusal to underwrite most of the current national debt. The right version
also endorses a expansion of consumption towards status but with a clear anti-immigrant message and a lesser emphasis on investment. Our argument suggests that, however appealing, these message contain policy paths of limited feasibility in the short run. Whether their initial appeal translates into a stable realignment of political coalitions and what the implications are for political stability in these societies remains to be seen.

1.3.5. Summary: The Political Space in Advanced Capitalism

Our analysis of the dynamics of policy-making in advanced capitalism suggests that the space for partisan politics over the last three decades across political economies has been at least two-dimensional, making possible multiple options for political alignments. It also suggests that the way the strategies of successful reform coalitions have shifted depends largely on past policy legacies, as captured by the four corners in figure 1.12., constraining policy shifts along two dimensions: the scope of the state’s intervention in the economy and the inherited balance in terms of investment and consumption policies. These two parameters shape the relative size of different social groups and their core policy claims, thus giving birth a new set of feasible vs. unfeasible political alliances. Figure 1.12 maps out the set of feasible coalitions across social groups emerging from our analysis. The political viability of these coalitions depends on the status quo equilibrium, as explained in detail above. Also, these coalitions may be mobilized by different partisan actors, depending on the patterns of party competition in different countries. A thorough analysis of the parties mobilizing these coalitions is, however, beyond the scope of this chapter (see, however, the chapters by Kitschelt and Rehm and by Häusermann and Kriesi in this volume).
1.- *Socio-cultural professionals and organized labor* (wage earners) remain, together, the core political coalition leading to outcome equality. Both groups agree on strong and redistributive state intervention, but they must compromise on investment and consumption. To some extent, labor must accept the socio-cultural professional’s emphasis on investments, whereas the socio-cultural professionals have to compromise with labor’s preference for status-segmented consumption. If these compromises become untenable, the pro-equality coalition unravels.

2.- A second coalition involves *socio-cultural professionals and business-finance professionals*: in this coalition, both parties agree on the emphasis on investment but must compromise with regard to the size and the redistributive scope of the state. Our analysis suggests that this coalition is likely to be pursued by left-wing parties in market oriented societies.

**Figure 1.12.**

*Coalitional Configurations in the Political Space of Advanced Capitalism*

3.- The third potential coalition is that between small and large businesses, between the *petit bourgeois and the business and finance professionals*. In this coalition, both agree on limiting state intervention in markets that benefits primarily organized labor. In turn, they must compromise on investment, necessary for industry development but disliked the self employed. If the tax burden associated with investment becomes too contentious, this typically conservative coalition will unravel, opening opportunities for the left.
4.- Finally, the fourth potential coalition highlighted by our analysis includes elements of organized labor (wage earners) and the petit bourgeois. Both sides agree on prioritizing consumption over investment, but must compromise on the scope of taxation and state intervention/regulation. This alliance of strange bedfellows emerges particularly in contexts, where both groups develop a strong anti-immigrant sentiment, and is most likely to be pursued by right-wing populist partisan forces.

Figure 1.12 places each of these coalitions around the coordinates of our theoretical framework. Critically, our analysis also rules out as implausible in advanced capitalism two other alliances:

a. An alliance between the socio-cultural professionals and the petit bourgeois: they disagree both on the scope of state policy (taxation and social benefits schemes) as well as on priorities over inter-temporal resource allocation (investment/consumption). Taxes and equality and on the policy priorities.

b. An alliance between business and organized labor (wage earners, and in particular, low wage earners): This suggests that such cross-class coalitions around which post-World War II capitalism was configured, particularly in what are today the status-oriented political economies, are hardly feasible anymore. Put simply, unions representing low wage earners want an emphasis on consumption that creates too high an opportunity cost in terms of investment and competitiveness for business and socio-cultural professionals. The alternative alliance with socio-cultural professionals in favor of investments (2 above) at the expense of consumption is a more attractive option for business, even in PR systems (Iversen and Soskice, forthcoming).
1.4. Relationship to the Existing Literature

In a stylized fashion, we see at least two approaches at variance with the proposal we have drawn up in this introduction. The first essentially posits a convergence of advanced capitalist politics and policy-making across all political units, and it is clearly far from our diagnosis. The second sees a path-dependent evolution of different varieties of capitalism and is closer to our analysis.

The convergence perspective that was also in the crosshairs of criticisms in this volume's predecessor (Kitschelt et al. 1999), has received a strong second wind through the financial crisis followed by the Great Recession. It essentially argues for convergence in at least two ways: (1) All incarnations of advanced capitalism develop in the same direction: convergence Mark I, parallel development; and (2) where there were differences across polities and regions, these “varieties” are being whittled away to a common political economic practice of “just capitalism” without adjectives (cf. Streeck (2009; 2011; 2014a and b): convergence Mark II, homogenization around a common "best" practice. This strong conception of inequality convergence, combining Mark I and Mark II, is also consistent with Piketty’s (2014) purely economic analysis of long-term patterns of inequality: the West’s reductions of inequality in the aftermath of World War I, the Great Depression, and especially World War II were idiosyncratic exceptions, induced by exogenous shocks of war and economic dislocation, that tempered inequality differentially and temporarily. Capitalism, to put in its crudest terms, is now returning to its steady state.
We have no doubt that there are powerful tendencies that increase inequality in contemporary capitalism (convergence Mark I). But we challenge that these forces evidence tendencies to effectively generate the homogenization of capitalism (convergence Mark II). The cursory evidence displayed in this introduction, as well as the more detailed evidence provided by the many contributions to this volume overwhelmingly speak against this hypothesis.

Moreover, we tend to disagree on the mechanisms of convergence. Whereas in the evolutionary political (Streeck) and economic (Piketty) approaches it is purely (global) markets that drive these changes, our approach highlights the continuing importance of politics as a source of diversity.25 In the convergence theory, it is the power of footloose capital, alone, that compels politicians and ultimately voters to accept the fate of convergence Mark II.

We beg to differ on a number of counts. On the one hand, we disagree with the analysis of mechanisms. Globalization is a force that constrains politics, but it is technology, mediated by the changes in occupational structures, that has far more influence on the movement of relative prices of capital and different skill and task profiles of labor. European and North American peasants and miners, printers and longshoremen, bank tellers and telephone switching operators did not lose their livelihood because their jobs went abroad or were taken away by immigrants. They vanished, supplanted by machines and increasingly “code.” About half of all jobs are highly likely to fall victim to “code” in the remainder of the twenty-first century (Frey and Osborne 2013). Also demographics, together with changes in family structure that, themselves, are intertwined with occupational and technological changes calling for new techniques of socialization and skilling young people, are powerful forces that have no room in the convergence narrative. We see no compelling reason why family structures and occupational

25 To be fair, Piketty (2014: part IV) agrees that democratic politics may modify outcomes, but that is not part of his analysis.
clusters should become uniform across space, even though they respond to similar fundamental technological challenges.

More importantly, however, the convergence perspective entirely discounts politics. Piketty says as much and delegates the task to explore the modifying role of politics to other researchers. Streeck’s analysis is a return to the models of late-capitalist state theories that saw state functionaries—out of their own interests to survive and thrive, not by taking direct orders from capitalist bosses—enact the imperatives of capital accumulation (cf. Offe 1972; 1985; Poulantzas 1973). Relying on Peter Mair’s theory of cartel parties and party systems, Streeck sees a “hollowing out” of politics (Mair 2006) in which democratic accountability to electoral interests and preferences vanishes either by politicians of all parties colluding to ignore them or by politicians (and the mass media) manipulating citizens so that popular preferences are no longer exogenous to the strategies of capital and party politicians seeking to secure their survival in political office. Politics becomes a handmaiden to international capital markets instead of responsive to genuine popular interests.

We document in this book that substantial evidence contradicts this general perspective. Parties remain differentiated in their electoral appeals, do represent constituency groups, and act on their electoral alignments in public policy-making. And if politicians do not implement the kind of redistribution contemporary Marxians would postulate for the working class to demand, it is not because they defy the preferences of large publics, but because these publics express more complicated, differentiated preference schedules. These observations contradicting structuralist neo-Marxism do not, of course, prevent or preempt that business has rather substantial leverage over policy formation outside the circuit of electoral partisan accountability. We are the last to deny that there are other ingredients to policy formation than electoral
politics. Nevertheless, understanding the operation of electoral democracy is constitutive in order to account for variance over time and across space in policies and quality of life outcomes delivered by postindustrial democracies.

Compared to structuralist neo-marxism, our perspective is much closer to the varieties-of-capitalism (VoC) literature that goes back at least as far as Shonfield (1965), then the corporatism literature (e.g. Cameron 1984; Katzenstein 1985; Lange and Garrett 1985), and finally what has then explicitly called itself “varieties of capitalism” (VoC) approach (see Soskice 1999; Hall and Soskice 2001; Iversen 2005; Iversen and Stephens 2008; Iversen and Soskice 2009). Let us first sketch how our approach is steeped in the VoC literature before we specify where we depart from its postulates.

We align with VoC in accounting for the development of political-economic institutions (e.g., industrial relations regimes, corporate governance), actors (producers, political parties) and endowments (technology, skills) as a path-dependent process in which starting points matter and the options for change follow from distinctive constraints and capacities encountered in the choice process. Both VoC and the constrained partisanship framework observe that actors’ basic political preference schedules are largely exogenous to the game of party competition, rooted in political-economic, occupational, and social experiences. Democracy does operate as an accountability mechanism in which competing party politicians must pick up on (some of) their constituencies preferences in order to achieve and stay in office. While globalization of products/services, labor and capital imposes restrictions on polities’ domestic domain of maneuver, it remains quite large, as can be traced in the differential responses of party governments to similar exogenous technological and demographic shocks (cf. Hall and Thelen 2009).
Our endeavor, however, also parts company with VoC in some regards. First of all, in the distinction of variety types, as clusters of institutional and political attributes (mainly corporate governance, industrial relations, skill formation and research and development on the production side, profiles of redistribution and risk hedging in social policy on the welfare state side), we think it to be less useful for most explanatory purposes to operate with two main types—coordinated and competitive market economies (CME and LME)—and then many “mixed” types and “sub” types than straight-forwardly with four types introduced above that crystallized in the post-World War II decades in today’s advanced capitalist democracies. The welfare state literature always had to operate with a minimum of three rather than two types that required a distinction based on partisan politics alone (Esping-Andersen 1990; van Kersbergen 1995; Kitschelt et al. 1999). Cross-class Christian Democratic parties whose unique role could not be characterized in terms of production systems were introduced to account for major differences in social policy formation and inequality outcomes that broke the CME/LME conceptual dualism. A further limitation of VoC’s conceptual dualism was its treatment of the Mediterranean countries by either excluding them from analysis or relegating them to the “mixed” types hard to accommodate with the existing conceptual strategy.

Second, we accord a different theoretical status to political-economic types than the VoC theorists might suggest. For us, types are shorthand for empirical clusters of the scores on continuous variables that appear historically and bring about different effects, depending on circumstances. For VoC, by contrast, the empirical approximation of types activates specific “complementarities” of institutions and policies that yield particularly desirable macro-economic performance. Clusters of traits reinforce each other both in the production system (Hall and Soskice 2001) as well as between production and social policy (Estevez-Abe et al. 2001; Iversen 2005; Iversen and Soskice 2009) according to the economic interests of all producers—both
capital and labor—and make them particularly efficient and competitive compared to “mixed” types in macro-economic terms (Hall and Gingerich 2009). Moreover, complementary institutions are equilibria that make it costly for any single actor to diverge from them.

Empirical research has shown that the association of polities with particular types of production systems has been in flux for some time (Schneider and Paunescu 2012). We challenge that at least currently, under the impact of the technological, demographic and globalization “shocks,” it is possible for theory to identify efficient equilibria of political-economic “packages” of policies and institutions that deliver superior performance. Likewise, political actors, such as party (coalitions), grounded in different political-economic interest alignments, experiment into an open horizon, often driven by myopic conceptions of group interests, without anyone being able to predict today whether the path pursued will actually pay off in the longer run either for (1) for the political actors and their constituencies advancing the reforms right now and/or (2) for the macro-economic performance of the polities (or regions) in which these reforms prevail.

We have not investigated here whether the past record of political-economic development since World War II ever produced time windows in which empirical clusters of political-economic institutions and polices became complementarities that were particularly high performing. In recent decades, however, under the impact of the new shocks—technology-induced occupational change, demographics, and globalization—partisan governments and coalitions appear to have adopted policy and institutional experimentation that move them away from the complementarity and equilibrium conditions even in the historical cases that once came closest to the two CME/LME types of capitalist varieties (Ahlquist and Breunig 2012; Schneider and Paunescu 2012; Thelen 2014; in this volume: see especially Jackson and Thelen, as well as Hassel).
Beyond pure description, all that is currently possible in political-economic explanation is to delineate feasibility sets of policy options that are reachable from certain status quo institutions and policies and trace the partisan coalitions that dominate the political agenda within this feasibility set. Because of high uncertainty about economic consequences and efficiencies of alternative policy pathways, however, such partisan alignments express pure politics, unfettered by clear economic signals of “best” and “inferior” policy practices, and it remains uncertain whether the emerging partisan and policy coalition strategies may enact lasting equilibria, let alone equilibria with collectively beneficial positive-sum outcomes.

Recent work by key proponents of VoC comes close to this very perspective (Iversen and Soskice, forthcoming). For CMEs, they see the technological conditions that fuelled the superior performance of CME institutions as now unraveling the producer coalition that built the CME consensus. Technology undercuts the coordination between different components of the working class, broadly conceived as consisting of an ascending ladder of skills, with an increasingly narrow band of high-skilled workers in CMEs still supporting the continued coordination with business that once market this type, but increasingly separated from low-skilled wage earners. How policy-making treats the mass of less-skilled labor, then, is a matter of pure partisan politics in the Iversen-Soskice analysis, just as it would be within the framework of “constrained partisanship.” According to them, where cross-class parties prevail in systems of proportional representation, the pathway of policy reform will be different, and less favorable, for the worst-off, than where pure bourgeois parties with strong liberalization agendas make it more likely that center-left and left parties rally in coalitions protecting even the poorest against the onslaught of market liberalization promoted by parties of business and professionals.
We need not examine the substance of the empirical claims in Iversen and Soskice’s interesting paper here,\(^{26}\) but point out the theoretical moves made against the backdrop of VoC and relate them to our approach. As in our case, there is no economic explanation for the difference in party systems, the grounding of which has to be sought in politics itself, and pure politics yields policies with different distributive results.\(^{27}\) We would add: And the actors (and scholarly observers!) do not know whether or not they contribute to an ensemble of strategies ultimately generating a set of policies and institutions that might again deserve to be labeled “types” in political-economic analysis, because they persist over time and may yield superior economic performance. It is this supremacy of electoral partisan politics, acting into an uncertain future of reform, but constrained by the existing institutions, state capacities, and party system configurations, that should drive explanatory accounts of policy choice in political economy right now and that deserves the label of “constrained partisanship” approach.

This leaves one feature to be highlighted on which VoC and the constrained partisanship approach sketched here may or may not agree: the need for a two-dimensional characterization of the space of political controversy that builds on citizens’ diverging economic interests. Economic actors disagree not only about the allocation of resources and capabilities at any given point in time, but also about the inter-temporal distribution of chances to acquire resources and capabilities: some want to discount the future more than others. In the constrained partisanship approach the wager is that (1) preference disagreements over the level of state intervention are orthogonal to (2) the targeting of more policy resources to current consumers (however these

\(^{26}\) For example, Iversen/Soskice do not focus on social policies—particularly pension reform—where party systems with pure market-liberal parties have prompted even center-left coalitions to embrace stronger market liberalization than governments produced by cross-class parties, e.g. through defined-contributions components within the public pension system or raising the criteria of eligibility for full pension benefits.

\(^{27}\) Note that it is not electoral systems, and economic producer interests standing behind the choice of electoral systems, that explain the difference of party systems with or without cross-class parties.
resources may be distributed among claimants) or more heavily to future consumers, by making investment efforts right now that pay off for the chances of future citizens to earn a good income.

Our insistence on the two-dimensional nature of the policy space is intimately associated with the different characterization of relevant economic occupational groups highlighted in the “constrained partisanship” approach, when contrasted to VoC. Whereas VoC—all the way to Iversen and Soskice’s recent paper—makes do with what is essentially a uni-dimensional characterization of social structure, rising from unskilled, via high-specifically skilled to very high/generally skilled professional/business operatives (or from low to middle to high incomes), we propose a two-dimensional field of occupational groups, market locations, and economic interests as the “raw material” for politicians’ creative efforts to craft winning electoral coalitions and novel public policies.

1.5. Organization of the book

This chapter has outlined the fundamental elements of our re-interpretation of the politics of advanced capitalism. In the rest of the volume contributors take on the task of analyzing in detail specific preconditions, dynamics and consequences of the general process described in this introduction. The volume is organized in four sections.

We begin by situating our cases of interest in space and time and by analyzing the key structural transformations putting pressure on advanced industrial democracies and delimiting the context in which the dynamics of our model of constrained partisanship play out. The determinants and constraints on productivity and prosperity are such key factors shaping the
larger macroeconomic context. Carles Boix offers a long-dureé perspective on the relationship between sector composition and economic growth and contextualizes current developments in advanced democracies within these long-run processes of structural transformations in the composition of economic sectors. Rueda, Wibbels and Altamirano complement this view on structural determinant with a focus on institutions. They argue that differences in the timing and type of industrialization between a “core” of advanced capitalist democracies and the “periphery” have led to very different institutional configurations of labor market regulation, resulting in the patterns of dualization we observe today, especially in the countries of Southern Europe and Latin America. These two chapters situate advanced capitalism in a broader context and help calibrate the scope of our conclusions.

Thereafter, the volume turns to three major sources of social structural change: the occupational structure (Oesch), changing household patterns and gender roles (Esping-Andersen), and international pressures, with a particular focus on the pressure migration puts on the working class (Dancygier and Walter). Oesch argues that technological change has eroded lower-skill occupations in advanced capitalist democracies and reduced social and occupational mobility, because of stronger educational stratification. The chapter by Esping-Andersen then shows that these occupational trends are reinforced by changing household patterns, in particular increasing socio-structural homogamy, a trend that also increases stratification and reduces social mobility. Moreover, as Dancygier and Walter show, globalization and migration flows further threaten the jobs and social status of the lower skill classes in society, thereby changing the political preference space governments are confronted with.

In second step, we go on to analyze the impact of these structural changes on politics. Kitschelt and Rehm start with a defense of realignment theory, showing that in most advanced capitalist democracies, political parties still present voters with alternative programmatic
choices and represent their constituencies rather well. Häusermann and Kriesi then analyze these constituencies in more detail. They investigate the preference profile of party electorates, as well as the socio-structural determinants of these preferences with regard to the state-market and universalism-particularism dimension. The upshot is that the class profile of left- and right-wing parties has profoundly changed: while the left has largely become the representative of a universalist-statist middle class, working class and low-income voter increasingly vote for particularistic parties. These changes clearly transform the coalitional opportunities for constrained governments even further, especially on the state-market dimension. Furthermore, the chapter by Hassel shows that the left is losing the working class not only in terms of its parties, but also in terms of organized labor: union density is not only declining, but highly unequal in all but the “universalist” Nordic countries. Despite relatively stable levels of institutional coordination, this erosion of organized labor further complicates the coalitional choices constrained governments have in terms of their policy choices.

The first two sections lay the foundations for the analyses of the political and institutional responses to transformed supply- and demand-side constraints. The third section on policies then analyzes coalitional dynamics and government choices with regard to particular key distributive policy areas. In line with our analytical framework, we focus on consumption (Huber and Stephens), investment (Gingrich and Ansell), as well as the evolution of labor market regulation and corporate governance, two policy areas for which our focus on electoral dynamics needs to be complemented by a close analysis of producer group politics and its interaction with partisan strategies (Jackson and Thelen). Both chapters on consumption and investment show that partisanship continues to matter within altered structural and institutional constraints. All three chapters account for a growing hybridization of the institutional policy set-up of advanced capitalist countries, and for complex coalitional dynamics governments engage in.
Finally, we turn to analyzing the outcomes of the constrained partisanship politics of advanced capitalism, broadly understood. We focus first on economic and distributive outcomes of different sets of constraints (Beramendi), to then analyze the determinants of self-reported happiness across political economies (Anderson and Hecht). The conclusion by the editors summarizes our key results and discusses the impact of the economic crisis on politics and policies.
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Figures


Figure 1.1: Public expenditure on public consumption and investment as a percentage of GDP over time
Figure 1.2: Total expenditures for consumption and investment in the mid 2000s and the weight of spending on investment in total expenditure (2003-2007, OECD data)

Figure 1.3: Employment protection of regular and temporary employment contracts in the mid 1980s and mid 2000s
Figure 1.4: *Dimensionality and configurations of institutional constraints*
Figure 1.5: *Dimensions of the preferences space*
Figure 1.6: Electoral constraints: socio-economic groups in the political economy space
Figure 1.7. Political Contention and Feasible Reform Paths in Advanced Capitalism
Figure 1.8. Coalitional Politics in Equality Oriented Capitalism
Figure 1.9. Coalitional Politics in Status Oriented Capitalism
Figure 1.10. *Coalitional Politics in Competitiveness Oriented Capitalism*
Figure 1.11. *Coalitional Politics in Capture oriented Capitalism*
Figure 1.12. *Coalitional Configurations in the Political Space of Advanced Capitalism*