Varieties of Capitalism

PETER A. HALL

Abstract

Scholarship on varieties of capitalism (VofC) explores the ways in which the institutions structuring the political economy affect patterns of economic performance or policy making and the distribution of well-being. Contesting the claim that there is one best route to superior economic performance, a number of schemas have been proposed to explain why countries have often been able to secure substantial rates of growth in different ways, often with relatively egalitarian distributions of income. Prominent among them is a VofC analysis focused on the developed democracies that distinguishes liberal and coordinated market economies according to the ways in which firms coordinate their endeavors. On the basis of institutional complementarities among subspheres of the political economy, it suggests that the institutional structure of the political economy confers comparative institutional advantages, notably for radical and incremental innovation, which explains why economies have not converged in the context of globalization. Although this framework is contested, it has inspired new research on many subjects, including the basis for innovation, the determinants of social policy, the grounds for international negotiation, and the character of institutional change. In this issue area, there is promising terrain for further research into the origins of varieties of capitalism, the factors that drive institutional change in the political economy, how institutional arrangements in the subspheres of the political economy interact with one another, the normative underlay for capitalism, and the effects of varieties of capitalism on multiple dimensions of well-being.

INTRODUCTION

Is there more than one route to efficient economic performance? What are the most consequential institutional differences across capitalist political economies? How enduring are these differences and what effects follow from them? These are the core issues taken up by analysts of varieties of capitalism (VofC). They bear on the distribution of well-being as well as what makes economies competitive. Many European economies have a more equal distribution of income than the Anglo-American economies and, on the basis of an efficiency-equity trade-off, some argue that this egalitarianism comes at the cost of economic growth. Others suggest that more egalitarian forms of capitalism can be just as efficient.

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Research on this subject was inspired by a turn in the social sciences to a "new institutionalism." Like states, markets are institutions that take a historically specific shape, and analysts of varieties of capitalism are interested in how their operation is affected by other institutions in the political economy, such as trade unions, firm networks, and policy regimes. Research on this topic speaks to a number of overarching issues in institutional analysis, such as how institutions in one sphere of the political economy affect the operation of those in other spheres. This work has also been revealing about the pacing and drivers of institutional change.

The research done on this topic carries many implications for policy making. VofC analyses have shown, for instance, that more generous social policies do not always reflect the triumph of labor over business. They have shown how the institutional shape of the political economy conditions the positions taken by national governments in international negotiations. Studies of institutional complementarities call into question the efficiency of piecemeal reforms to one sphere of the economy and the accuracy of estimations assessing the impact of such reforms that do not take such institutional interaction effects into account.

At the heart of these inquiries are questions, not only about how political economies differ but also why ensembles of institutions cohere. One of the defining features of this research is its inclination to treat political economies as coherent wholes with distinctive features grounded in national histories rather than as examples of a homogeneous market terrain onto which new institutions can be readily grafted without much concern for other institutions in the economy. Thus, this research draws on neoclassical economics and game theory, but questions some of the assumptions of neoclassical models.

FOUNDATIONAL RESEARCH

The contemporary study of comparative capitalism dates to pioneering research in the 1960s of Andrew Shonfield (1969), who compared the character of state intervention across political economies with a view to establishing how each was able to modernize. In early works, France and Japan were typically presented as success stories. When global attention shifted to the problem of "stagflation" during the 1970s, analysts began to emphasize instead how the structures of wage bargaining condition the economic success of countries. Their most prominent contention was that superior economic performance can be secured where wage bargaining is operated by relatively centralized trade unions and employers associations under what were usually termed "neocorporatist" arrangements. In this era, the small states of northern Europe emerged as major success stories

(Goldthorpe, 1984). The third strand of work influencing subsequent theories was by the French "regulation school" and scholars of firm-networks, which emphasized connections between how production is organized on the shop floor and supportive firm-networks, bargaining institutions or policy regimes at the regional level and in the macro-economy. This literature focused on the institutional underpinnings for "Fordist mass production" (after Henry Ford) or "diversified quality production" seen as an alternative to it (Boyer, 2005; Streeck, 1991).

Many current debates in the field revolve around an analytical framework presented in Hall and Soskice (2001) and the term "varieties of capitalism" is often used to refer to that framework. If a first wave of work focused on modernization and the second focused on stagflation, this third wave emphasizes the problems of the political economy in an era when international competition became more intense and factors of production more mobile. Many scholars argued that, in the face of this globalization, economies would "liberalize" to converge on something similar to an American model.

Hall and Soskice argued against this convergence thesis on the grounds that different types of political economies have distinctive comparative advantages they can exploit to prosper in an open global economy. As the English political economist David Ricardo once argued, the best way to survive intense competition is often not to imitate one's competitors but to capitalize on one's differences. The innovative element here was to suggest that national comparative advantages might be rooted in the institutional structures of the political economy.

Because it set many of the terms for contemporary debate, I summarize the core propositions of this "VofC" approach. In contrast to previous work that emphasized trade unions and rarely discussed firms, this is a firm-oriented perspective, which sees companies as central actors in the economy and organizations whose success turns on the quality of the relationships they form in key realms of endeavor, including industrial relations where wages are set, interfirm relations governing technology transfer, markets for corporate governance that supply finance, and intrafirm relations bearing on how products are made.

VofC analyses distinguish between two ways of managing these relationships: one based on competitive market relations and the other on the types of strategic coordination described by game theory. The approach a firm will adopt depends on the extent to which each is supported by the overarching institutions of the political economy, including relevant policy regimes, interfirm networks, and the structure of industrial relations. Thus, this approach distinguishes between types of economies according to how firms coordinate their endeavors. In one ideal type, known as liberal market economies

(LMEs), most firms coordinate many of their activities via market mechanisms, while, in the ideal type of coordinated market economy (CME), a typical firm's relations with other actors turn more heavily on strategic coordination.

In addition, Hall and Soskice (2001) allow for a number of subtypes reflecting, for instance, differences in the forms of strategic coordination found in East Asia and northern Europe and the "mixed market economies" of southern Europe where there is more strategic coordination in corporate governance than labor relations (Hall & Gingerich, 2009). Others argue for the distinctiveness of CMEs in the Nordic region, where social democratic dominance has given rise to distinctive industrial relations regimes and social policies. In western Europe, that schema yields four types of political economies—LMEs in Ireland and the United Kingdom; the mixed market economies of Portugal, Spain, and Greece; Nordic coordinated economies in Denmark, Sweden, Finland, and Norway; and continental CMEs in most of the rest.

The influence of this paradigm follows from the implications that can be derived from it. First, it posits "institutional complementarities" where the presence of a specific set of institutions in one sphere of the economy enhances the returns available from corresponding institutions in other spheres, often turning on whether market (or strategic) coordination is found in both spheres. The implication is that firms and workers may hesitate to change institutions in one sphere without corresponding reform in other spheres. For instance, Goyer (2011) finds that German firms were more reluctant than French firms to liberalize the market for corporate governance, lest an aggressive takeover regime interfere with the advantages they draw from strategically coordinated industrial relations not present in France.

Second, proponents of this approach build on the work of Swenson (2001) to emphasize the political importance of "cross-class coalitions" in which segments of labor and capital unite behind a policy position to defend a set of institutional structures from which both benefit. The implication is that cross-national variation in some kinds of institutions, such as the shape of an industrial relations system, is often explained by a politics in which the balance of class power is less important than cross-national variation in the interests of employers—a challenge to the "power resources" approach to such issues (cf. Korpi, 2006).

Building on this, VofC analysts develop an account of why employers have interests in social policy regimes (Estevez-Abe, Iversen, & Soskice, 2001; Iversen & Soskice, 2001; Mares, 2004). Instead of seeing business as an implacable opponent of social policy, these scholars argue that the generous unemployment benefits of many CMEs are supported by business as well as labor because they provide incentives for workers to invest in the industry-specific skills central to the production regimes of such economies. "Specific skills" are typically acquired through apprenticeship or experience and of value principally in one industry or firm, while "general skills" are portable across sectors and occupations. The observation that firms in CMEs tend to make extensive use of specific skills, while those in LMEs rely on general skills can be used to explain, not only cross-national variations in firm strategy but also national differences in educational systems, social policy regimes, and gender segmentation across occupations.

The most radical implications of this approach concern national economic performance. The contention is that aggregate economic performance, measured by rates of economic growth or productivity, can be as high in coordinated as LMEs, a point often supported by reference to Germany, Sweden, Denmark, and Norway. However, the VofC perspective also emphasizes that aggregate performance can be secured in different ways. The institutional structures of coordinated and LME are said to confer distinctive competitive advantages on firms that translate into national comparative advantages.

The most striking contention here is that by virtue of their fluid labor and capital markets, which make it easy for firms to begin new ventures knowing they can quickly be unwound, LMEs offer more support for radical innovation, understood as the development of entirely new products or technologies. By contrast, CMEs are said to be better at incremental innovation, involving quality control and continuous improvements to products or production processes, because strong trade unions and longer job tenures encourage firms to make long-term commitments to workers that elicit higher levels of cooperation and encourage investment in the high skill levels that make such innovation feasible. Thus, LMEs should produce radical innovations more successfully, while CMEs are better at quality control and incremental innovation.

This point carries implications for where firms locate their operations. Hall and Soskice (2001) argue that many firms will engage in "institutional arbitrage"—locating endeavors such as research and development that depend on radical innovation in LMEs, while high-value-added manufacturing is more often located in CMEs. Although other considerations also bear on location decisions and there are always exceptional cases, this theory provides a new perspective on globalization, which explains why globalization might not lead to convergence on the American economic model.

CUTTING-EDGE RESEARCH

The VofC framework elaborated by Hall and Soskice has inspired many theoretical critiques, efforts to test the approach, and to extend it. Some of this research asks whether countries cluster into the types of capitalism identified by this framework—a difficult task because the typology turns on forms of coordination that can rarely be measured directly. Hall and Gingerich (2009) construct a widely used but time-invariant index of (market-oriented vs strategic) coordination and find that Organisation for Economic Cooperation and Development (OECD) countries cluster on coordination in labor relations and corporate governance as suggested by the theory; but they also identify a group of southern European "mixed market economies" where corporate governance is more strategically coordinated than labor relations. Using time-variant measures, Schneider and Paunescu (2012) find country groupings and sector-specific comparative advantages predicted by the theory, but also recent movement, especially in the Nordic region, toward an LME model and Casey (2009) too finds support for these theories. Using a cluster analysis highly sensitive to the variables chosen as proxies, Geffen and Kenyon (2006) find a stable cluster corresponding only to LMEs, which raises questions about the theory.

In this context, it is important to note that several analysts have developed other classifications of capitalism, based on alternate principles. Some time ago, Whitley (1999) identified six types of business systems that vary according to the ways firms secure coordination and control, linked to the institutional context. Amable (2003) posits five forms of capitalism, characterized by distinctive institutional complementarities, in Scandinavia, Asia, southern Europe, the Anglo-American world, and continental Europe. More recently, Becker (2009) suggests four types of capitalism seen as loosely ordered and relatively open systems.

Another series of analyses assess the contention that LMEs provide more propitious institutional ground for radical innovation than CMEs. Taylor (2004) saw no evidence for this proposition; but Allen, Funk, and Tüselmann (2006) and Akkermans, Castaldi, and Los (2009) find that the revealed comparative advantage of sectors corresponds broadly to VofC predictions with some notable exceptions. Huo (2012) extends the theory to show why competition encourages radical innovation based on information effects, while cooperation does not. In a bold intervention, Acemoglu, Robinson, and Verdier (2012) find support for the proposition that radical innovation is more likely in LMEs, and use the point to contend that economic growth in the "cuddly capitalism" of CMEs is ultimately dependent on the technological innovations devised in the "ruthless capitalism" of LMEs. However, using different measures, Maliranta, Mättännen, and Vihriälä (2012) dispute this argument on the grounds that radical innovation can be found in the Nordic economies.

A third group of studies ask whether institutional complementarities operate as Hall and Soskice predict. In a wide-ranging debate, some critics contend that market-oriented institutions can be complementary to institutions supporting strategic coordination, while others argue that complementarities are rooted in institutional features more specific than the types of coordination they support. Höpner (2005) draws a useful distinction between complementarity, coherence, and compatibility. In addition to complementarities between the institutions supporting labor relations and corporate governance in France and Germany, Goyer (2011) finds patterns of international investment influenced by VofC, as investors seeking steady returns invest more heavily in CMEs, while those seeking more risk and larger returns favor LMEs. A number of studies ask whether multinational enterprises exploit institutional comparative advantages or undermine national institutional practices by adhering to the practices of their home country (Morgan & Kristensen, 2006).

It is hotly debated whether the varieties of capitalism identified in this literature are stable over time, converging, or otherwise dissolving. Everyone agrees that some liberalization has taken place in all economies but Hall and Gingerich find slower liberalization in CMEs than in LMEs and argue it preserves many of the main differences, while Streeck (2009) argues, on the basis of the German case, that coordinated capitalism is disappearing as the inexorable entrepreneurialism of capitalism erodes the normative order underpinning CMEs. Some analysts argue that declining trade union membership is destroying strategic coordination, while others contend that trade unions and employers associations retain strategic capacities, even in the face of the cleavages globalization opens up between more and less competitive firms (Baccaro & Howell, 2011; Thelen & van Wijnbergen, 2005).

The issue of how and why varieties of capitalism might be changing is bound up with debates about how they originate. Although Hall and Soskice (2001) explicitly specified that VofC were not explaining why countries develop different types of capitalism and Hall and Thelen (2009) argue that institutional reform is dependent on a coalitional politics in which distributive issues based on who benefits predominate, some analysts accuse them of taking an overly functionalist approach to such issues (Streeck, 2009). Others argue that the emphasis on cross-class coalitions understates the extent to which such processes are driven by fundamental conflicts between capital and labor (Coates, 2005; Korpi, 2006).

Thelen (2004) treats these issues empirically by charting the development of skill formation systems in four countries. She argues that early conflicts between skilled labor, artisans, and employers conditioned subsequent processes of coalition formation to drive each country along a distinctive trajectory, while Streeck and Yamamura (2002) ascribe the features of national capitalism to a multitude of historical developments. Iversen and Soskice (2009) take the view that the development of the economy is the driving force and explore how it relates to the development of political institutions (with an emphasis on electoral rules). They argue that early forms of coordination in regional economies, with preindustrial roots, conditioned the support employers and their political allies would later provide for proportional representation. However, these are still matters of lively debate (cf. Boix, 1991; Martin & Swank, 2012).

KEY ISSUES FOR FUTURE RESEARCH

There is ample room for further research on this topic and many important issues are signaled by contemporary debates. Preeminent among them is the question of why countries developed distinctive varieties of capitalism, a topic closely linked to broader issues in the study of institutional change. The central actors include firms, which must devise corporate strategies, and governments, whose regulatory regimes support particular strategies. However, each responds to different incentives, as firms seek to compete more effectively on domestic and international markets, while governments try to please their constituencies that may include electorates as well as producer groups. One of the overarching issues is how much influence producer groups have relative to electorates and over what kinds of policies. This topic is neglected in political science, which tends to divide into scholars of electoral politics and producer politics (but cf. Culpepper, 2010; Trumbull, 2012).

The parallel problem for contemporary capitalism is one of understanding how changes occur in the institutional infrastructure of varieties of capitalism. Here, the challenge is to go beyond studies adducing large-scale determinants such as "globalization" or "the balance of class power" toward work that provides an analytical account of the processes whereby such changes take place. Comparative case studies of specific instances of policy making, in which regulations pertaining to employment relations or corporate governance change, provide one of the best routes into such issues, although their findings must also be integrated into a more general understanding of what drives such processes along distinctive paths.

Here, one of the principal tasks is to develop models of how reform coalitions form that are sensitive to the ways in which existing institutions condition interests. This problem mirrors the more general dilemma facing contemporary political science of how to integrate accounts ascribing causal importance to coalitions of socioeconomic groups with accounts of how institutions structure politics. There is widespread agreement that both types of factors drive political outcomes but few works look explicitly at how institutions condition coalitions. Here, a more intensive dialog between game-theoretic analysis and historically grounded enquiry would be useful; and Swenson (2001) provides a template with an argument that institutional arrangements in one sphere of the political economy (industrial relations) condition the interests of employers in proposals for institutional reform in other spheres (such as social policy).

We also need to know more than we do about the precise nature of the institutional structures that underpin types of capitalism and how they relate to one another. Prevailing accounts of these structures emphasize regulatory regimes, formal organizational rules, and conventional firm practices. However, many practices may depend, to some extent, on normative orders, embodying beliefs about what is appropriate or just, that are also features of the political economy. In other words, we might build on work in economic sociology to ask whether a normative underlay is crucial to the persistence of some types of capitalism and, if so, what factors might change it. These are issues yet to receive much attention from political scientists (cf. Wueest, 2010).

There is also merit in enquiring further into the ways in which the subspheres of the political economy relate to one another and how these relationships are changing in the current conjuncture. For example, some accounts identify complementary relationships between a production regime, industrial relations regime, international regime, and policy regime specific both to varieties of capitalism and to particular historical epochs (Hall, 2013). We should ask whether these categories adequately define the principal institutional realms of a political economy and whether recent developments have altered the relationships between them in important ways. Does the growth of the financial sector, for instance, mean that it deserves a more central role in such analyses?

Closely related are questions about the extent to which the basic character of capitalism has changed over time. Some contend that changes in how capitalism operates, visible between the interwar years, the years of post-war growth, and the period since 1980 are so large that they dwarf cross-sectional variation in how varieties of capitalism work. While there is as yet no systematic empirical support for this contention, it is worth asking whether we are in a new era—perhaps of "finance capitalism"—and whether that has altered the basic character of political economies.

In the same vein, we do not as yet know nearly enough about how changes in electoral politics impinge on the operation of the political economy. Iversen and Soskice (2006) have argued forcefully that electoral systems based on proportional representation enhance the operation of CMEs, but there is scope for asking how variations in voting behavior across space or time might affect the support governments provide for the types of institutional arrangements central to varieties of capitalism. Do policies affect the *distribution* of economic returns, for instance, without much effect on the overall operation of the economy or do electoral shifts contribute to the transformation of national varieties of capitalism?

Attention is also turning toward questions about whether specific types of capitalism tend to require or promote distinctive growth strategies, understood as combinations of macroeconomic and supply-side policies. If so, are the growth strategies of the past still feasible in the economic conditions of the present? Some analysts argue that the efficient operation of particular types of political economies requires complementary macroeconomic policies (Carlin & Soskice, 2009) or that some kinds of "growth strategies" are viable only in certain types of political economies (Hall, 2012). We need to know more about what range of growth strategies is feasible in particular varieties of capitalism, such as the mixed market economies of southern Europe. Neoclassical economists have long tried to identify viable growth strategies, but they rarely deploy models that that are attentive to the institutional structures of the political economy. There is scope for research that integrates their insights into analyses of varieties of capitalism.

These considerations also raise questions about the relationship between national varieties of capitalism and international regimes. Eichengreen (1996) argued that post-war growth in Europe was made possible by the interactions between particular sets of domestic institutions and international regimes. Fioretos (2011) has explored how domestic structures condition the positions governments take within such regimes. But we know less about whether the viability of particular types of capitalism or corresponding growth strategies depends on supportive international regimes in trade and monetary affairs. The Euro crisis raised this issue in stark terms: Can all the varieties of capitalism prosper inside a monetary union or are some better served by a floating exchange-rate regime?

Much of the research into such topics concentrates on the developed economies. Hence, we should ask whether the principles behind this research can be used to understand the operation of political economies in the developing world. In many cases, new principles may have to be devised for that purpose. Schneider (2009) has found some parallel variation across Latin American economies, with the addition of a new category, and Feldmann (2007) uses a VofC analysis to compare Slovenia and Estonia. However, it is apparent that much of the relevant variation in transition economies and the developing world not well captured by standard VofC models, partly because some of these countries exhibit state-led forms of coordination that are rare in the developed democracies, are highly dependent on foreign direct investment, or lack trade unions strong enough to support strategic coordination in industrial relations (Bohle & Greskovits, 2012; Nölke & Vliegenthart, 2009). There is room for creative thought about the most consequential institutional differences between developing political economies in which large foreign or state-led sectors sit beside large informal economies and numerous small indigenous firms (Witt, 2010).

Finally, we need a better understanding of the contribution VofC make to the distribution of well-being. The foundational analyses in this field associate CMEs with a more egalitarian distribution of income. As globalization and the growth of service sector employment alter the basis for growth, however, this is again an open question. In an important intervention, Thelen (2014) argues that all capitalist economies are changing in terms that can be appreciated only by decoupling the concept of egalitarian capitalism from the VofC schema. She finds divergent trajectories in CMEs, as some such as Sweden and the Netherlands remain egalitarian, while others like Germany where dual labor markets have promoted inequality do not. Thelen attributes much of this divergence to a politics based on the size of the manufacturing sector, but other factors may be at work. We should enquire further into the relationship between varieties of capitalism and various forms of income inequality.

However, there is also a relationship between varieties of capitalism and other types of inequality such as inequalities in health, which deserve more attention (McLeod, Hall, Siddiqi, & Hertzman, 2012). A person's health is affected by sets of working conditions and social policies that vary systematically across types of capitalism, because the latter promote certain kinds of managerial structures, employment practices, and policy regimes. There is scope for seeing each variety of capitalism as a distinctive structure of economic relations that distributes health and other aspects of well-being in particular ways by virtue of how it distributes various kinds of economic and social resources that extend well beyond income. Studies of such phenomena could enrich our understanding of the determinants of cross-national variations in health and well-being and move the field of population health beyond its emphasis on income inequality.

In sum, there are still many open questions to be investigated about varieties of capitalism. Precisely which schemas will best describe the principal differences among the political economies of the world in the coming years is an issue that remains to be determined, but the contention that variations in the institutional structure of the political economy shape what firms and governments do, as well as the ensuing distribution of well-being, will be a keystone for many kinds of fruitful research.

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PETER A. HALL SHORT BIOGRAPHY

Peter A. Hall is Krupp Foundation Professor of European Studies in the Department of Government at Harvard University, a Faculty Associate at the Minda de Gunzburg Center for European Studies and Co-director of the Successful Societies Program for the Canadian Institute for Advanced Research. His publications include *Governing the Economy* (1986), *The Political Power of Economic Ideas* (1989), *Developments in French Politics I and II* (1990, 2001), *Varieties of Capitalism* (2001), *Changing France* (2005), *Successful Societies* (2009), *Social Resilience in the Neo-Liberal Era* and more than a 100 articles on comparative political economy and politics in the developed democracies. He has written widely about comparative institutional analysis, varieties of capitalism, economic policy-making, the role of ideas in politics, and methods of political analysis. His current research focuses on the development of the European political economies, issues in institutional change and the social basis for variations in population health across nations.

http://www.gov.harvard.edu/people/faculty/peter-hall
http://www.people.fas.harvard.edu/~phall/
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