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Thinking about Thinking about Comparative Political Economy: From Macro to Micro and Back

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Abstract

How and why did comparative political economy (CPE) lose sight of the sources of growing macroeconomic and political instability, a problem that encompassed a growing financial bubble and then a crash in the housing market, a period of sluggish growth that plausibly constitutes secular stagnation, and a crisis of political legitimacy manifesting itself in the rise of antisystem "populist" parties? A gradual shift in CPE's research agenda from macroeconomic to microeconomic concerns, and from demand-side to supply-side explanations, diminished its ability to analyze adequately the central economic and political problems of the past twenty years. This article traces CPE's evolution through successive "supermodels" that constituted its core research foci. To understand the current crisis, CPE needs to revisit and update its original roots in Keynes, macroeconomics, and the demand side. This shift is already happening at the margins, as CPE scholars struggle to understand the current crisis.

Keywords

comparative political economy, inflation, corporatism, developmental state, capitalism

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Scientific analysis is not simply a logically consistent process that starts with some primitive notions and then adds to the stock in some straight-line fashion. It is not simply progressive discovery of some objective reality—as is, for example, discovery in the basin of the Congo. Rather it is an incessant struggle with creations of our own and our predecessors' minds and it "progresses," if at all, in a criss-cross fashion, not as logic, but as the impact of new ideas or observations or needs, and also as the bents and temperaments of new men, dictate.

—Joseph Schumpeter[1]

How and why did comparative political economy (CPE) lose sight of the sources of the growing macroeconomic and political instability marking the past two decades, an instability that encompassed a growing financial bubble and then a crash in the housing market, sluggish growth that plausibly constitutes secular stagnation, and a crisis of political legitimacy manifesting itself in the rise of antisystem "populist" parties? We argue that CPE reflected and reacted to changes in the economy by generating a series of economic governance "supermodels"—stylized accounts of what CPE argued were the optimal institutional forms and policies for economic governance. Those models typically arose, like the owl of Minerva, just as their real-world referent reached the dusk of its optimal performance. The subsequent deterioration of a given supermodel's performance then set a series of critiques in motion. Thus, CPE as a body of knowledge traveled down a quasi-Kuhnian path, in which efforts to account for anomalies generated new research fields with scope conditions that excluded older knowledge. Over the past five decades, this loss of knowledge gradually diminished CPE's ability to analyze adequately the central economic and political problems that emerged during the past two decades.

First, CPE's core analytic models gradually shifted from a predominant focus on how macrosocial actors tamed the "violence of the market" to a focus on the emergence of stable institutional equilibria through the market.[2] Second, CPE lost sight of the role of emotion and legitimacy in politics, as its core point of entry shifted from the legitimacy of state policies that structured income distribution and the rate of growth and toward transaction-cost-based analyses of how actors efficiently coordinated exchanges. Finally, CPE's attention shifted from a predominantly macro-oriented, demand-side focus, which included a keen understanding of the fallacy of composition in the creation of demand, toward a predominantly supply-side focus largely ignoring the sources of demand. All these shifts were a matter of degree rather than absolute losses. Indeed, one point of stability was a continuing focus on manufacturing in CPE's core models even as other sectors became more important for value creation and capture in the economy. A second point of stability was a continued focus on national economies even as globalization, for lack of a better word, occurred, magnifying the fallacies of composition around disinflation and export success. But these shifts and their related loss of knowledge—which paralleled the economics discipline—gradually blinded CPE to macro-level mechanisms and legitimacy concerns. CPE's eventual focus on institutional stability blinded it to the broader instability arising from flagging demand, volatile and globally integrated housing finance markets, and declining social legitimacy. These evident failures—CPE's inability to produce timely advice about stabilizing the economy—have produced a return to some of the concerns Andrew Shonfield first raised at the dawn of modern CPE.

These three shifts occurred as both continuous and discrete processes. The discrete changes are best seen in the succession of national institutional configurations that CPE identified as ideal models or, as we will call them, supermodels, for economic governance. Here we focus on American Fordism, Swedish and German corporatism, Japanese developmental statism, and the two complementary worlds of liberal and coordinated market economies in varieties of capitalism (VoC). Each was briefly *the* fashionable institutional supermodel. Each displaced the prior model, albeit with some overlap, although the transition out of VoC remains unclear. Each supermodel linked specific institutional configurations to specific desirable economic outcomes. In that sense, each supermodel was both a normative ideal and an idealized model—a goal to be pursued and a stylized model for explaining how things worked, or did not work, in modern economies.

Why did CPE lose sight of growing macroeconomic and political instability? First, something like Kuhnian science occurred.[3] As the real world changed, political economists sought to explain anomalies in their understanding of that world. This process of addressing anomalies produced new knowledge. Yet, as Kuhn argues, all new approaches involve some loss of old knowledge. The analytic shift from legitimacy to transaction costs and from the demand side to the supply side drove the gradual loss of established knowledge about Keynes's fallacy of composition[4] and about the social purpose of the economy. The fallacy of composition and a sense of the social and moral underpinnings for the economy were critical components of CPE in the 1950s and 1960s. As S.M. Amadae has shown, one factor driving the shifts we identify stem from a shift in public funding toward approaches that shaped knowledge in directions that accelerated these losses.[5] Restoring lost components requires new models. CPE scholars confronting the current crisis are already generating some provisional shifts back toward the demand side and the macroeconomy.

Conceptually, none of these shifts qualifies as a full-fledged Kuhnian paradigm shift. A scholar of the sociology of science might correctly say that CPE by itself is the right level of abstraction at which to apply the paradigm label. Authoritative reviews of CPE treat it as a paradigm with three different analytic approaches.[6] On this view, the shifts between supermodels look like intraparadigmatic change. However, in the shift from one supermodel to the next, scholars converged on a set of questions, used shared assumptions to answer those questions, and then gradually shifted to a new set of questions, assumptions, and answers to deal with accumulating anomalies. In important respects, this pattern reflects the kind of social construction and evolution of knowledge that Kuhn analyzed, albeit at a lower level of abstraction. So we will use Kuhn metaphorically to capture the academic process in which the CPE community shifted from one supermodel to another.[7]

Second, in the nonacademic world, supermodels are part of larger debates informing political positions in struggles over public policy. Space limits prevent a full consideration of the degree to which these ideas generate endogenous sources of decay in that model.[8] Actors in the political economy strive to imitate whatever is the socially accepted best practice for policy and behavior. They do so by emulating the shared understanding of those policies and behaviors, which may well be only partially accurate explanations. In each supermodel's real-world referent, initial success rested on the presence of some abundant and therefore cheap material and social resources that powered growth; growth in turn created the illusion of stability; stability encouraged actors to continue exploiting those resources. Emulation of each given supermodel by other national actors created excess claims on the cheap resources powering that supermodel, exhausting them. Exhaustion could take the form of price shocks or deviant (from the point of view of the model) human behavior. This progression undoes the processes that made the original model a somewhat accurate representation of the world, just as they did in MacKenzie's canonical example of Black-Scholes option pricing.[9] As each successful real-world economy increasingly failed to cope with its changed environment, CPE reacted by updating what constituted its ideal model. In doing so, it lost sight of the utility of the fallacy of composition for understanding this generic process.[10]

This article thus analyzes the long-term shifts in CPE that eventually blinded it to the last two decades of economic and political turmoil. By examining the content of, and transitions between, five important CPE supermodels, it demonstrates the shift from a demand-side to a supply-side focus, the shift in imputed actor motivations from legitimacy issues to transaction costs, and the shift in baseline assumptions about the market from skepticism about stability based on the fallacy of composition to belief in efficient and stable equilibria. The first section defines and explains transitions between supermodels. Subsequent sections consider five major supermodels stretching from the 1960s to the 2000s. These sections show how changes in both independent and dependent variables in these supermodels led to the shifts noted above. The final section addresses the consequences of these shifts and losses, while noting that CPE's inability to adequately assess the current conjuncture is already inducing a movement back toward macrosocial and macroeconomic, demand-side, and legitimacy issues.

What Is a CPE Supermodel?

Over the past sixty years, the mainstream of CPE debates over economic governance has moved forward partly through a sequence and superposition of different economic supermodels. Supermodels are meta-analyses that causally link governance institutions to economic outcomes and thus serve as a focal point for analysis. Each model differs significantly with respect to what the model defines as the relevant policy problem confronting actors and which governance institutions matter for social action. Three things give supermodels a "meta" status relative to typical CPE analyses. First, supermodels generally claim that the institutional configuration of a specific country or small number of similar countries constitutes a best practice, indeed a universal solution to what is implicitly or explicitly seen as the most significant economic governance problem of the day.

Second, supermodels open up a research agenda; by definition this means they attract much attention and generate many citations and publications. Even when dissenters criticize the model, they honor it, increasing its salience in the literature. In this article, we bring forward only partial evidence for this attention or preeminence within CPE debates. Yet we think that there is some consensus around the salience of the five supermodels selected here. For example, as of July 2018 Google Scholar shows over 12,000 citations to Hall and Soskice's *Varieties of Capitalism* (published in 2001 by

Oxford University Press); 2,300 to Andrew Shonfield's *Modern Capitalism* (published in 1965, also by Oxford University Press); and 7,800 to Chalmers Johnson's *MITI and the Japanese Miracle* (published in 1982 by Stanford University Press).[11] These are extremely large numbers compared to the average publication, which is lucky to garner low double-digit citations over a decade, and very large compared to the lifetime citation figures for a typical American academic's entire oeuvre.

Finally, unlike much CPE writing, supermodels are picked up by journalists, think tanks, and public intellectuals and deployed in mainstream policy debates.[12] Precisely because they make claims about the best form of economic governance, supermodels attract attention from policy elites seeking solutions to problems and from public intellectuals searching for the next big thing. For example, Chalmers Johnson's arguments about the Japanese developmental state underlay efforts at an openly interventionist industrial policy by the so-called Atari Democrats of the 1980s and later by the Clinton administration's more covert industrial policy.[13]

Each supermodel identified a set of social or state institutions driving successful economic outcomes and, by implication, different or missing institutions driving unsuccessful ones. For example, CPE models have focused on the ideal structure for collective bargaining or capital-labor relations, for the relationship between the state and firms, for the relationship between the financial sector and nonfinancial firms, for relationships among nonfinancial firms, for gender relations and female employment (although often only implicitly), and ultimately for the causal mechanisms that produce the model's positive outcome(s). Supermodels generally combine many if not all of these features into one model, albeit while emphasizing one or two features.

Although all the supermodels attend to macroeconomic outcomes such as growth and employment in a general way, they differ in their assumptions about what makes economies work, which motivates them to examine differing causal mechanisms. For example, the supermodels as analytic constructs differ in their relative focus on demand-side and supply-side factors. A focus on demand is connected to macroeconomics for historical reasons. A demand-side focus does not assume that Say's law works, but rather takes the level of aggregate demand as an output of a political process, which, per Keynes, induces an expansion of supply. By contrast, a supply-side focus does not black box firms and labor supply, but rather asks what explains the kinds of goods or labor market a given institutional complex generates, what kinds of production processes firms utilize, and the level of efficiency in production. Efficiency concerns link the supply side and microeconomic approaches.

However, this concern with efficiency increasingly obscured the importance of what Keynes saw as a major fallacy of composition around the level of demand in the economy: increased efficiency without increased demand might simply lead to self-sustaining falling employment. Similarly, even as globalization made the question of the relationship between the supermodel's constitutive units (national economies) and the global economic system ever more important, all the supermodels from corporatism onward presented competitiveness, rather than balancing supply and demand, as the crucial economic issue. So a Keynesian fallacy of composition around demand reemerged at the international level: one state's export surplus and excess savings is another state's current account deficit and borrowing on international capital markets. Differing beliefs about the inherent stability of the market also parallel the methodological split between Keynesian macroeconomic and Chicago-school microfounded assumptions about stability. Finally, supermodels diverge in their theory of human nature: some emphasize actors' sense of justice and equity whereas others emphasize efficiency and coordination.[14]

Although the evolution of CPE had elements conforming to the standard model of scientific progress, successive supermodels were not formed and discarded solely on the basis of a one-directional relationship between real-world developments, scientific labor, and knowledge accumulation. Instead, new supermodel discourses emerged and became obsolete in a complex social process reflecting at least three distinct dynamics. The first is ecological or material, in two broad senses: it reflects what was going on in the real world, and it addresses the social and physical resources available for exploitation. Countries differ in their institutional capacity to use available cheap and abundant resources—docile semiskilled labor, "costless" dumping of pollutants, or cheap oil, for example. Countries also differ in their institutional capacity for handling whatever seems to be the most salient current economic problem—including unemployment, inflation, or export performance. Those that adapted best are typically lauded as model economies, producing social and market pressure to emulate them. We can see this in the steady stream of OECD publications urging conformity with some new best governance practice, or more strongly in the Marshall Plan–mediated but partial transfer of American consumption, production, and collective bargaining norms to Europe and Japan after 1948.[15]

Indeed, postwar CPE in some sense starts by "forgetting" that transfer and the related suppression or disappearance of the models of political, economic, and social order contending for dominance in the 1920s and 1930s. Those decades saw contestation among Catholic and other forms of corporatism, fascism, different flavors of social democracy, liberal capitalism, continued nineteenth-century imperialism, and communism, to name only the major options. In this sense, prewar "CPE" was more about the "P"—alternative models for political regimes—than about the "E." Purported 1930s supermodels varied more significantly on the political dimension than the economic, to the extent that they can be separated.

The war shrank this contestation into an essentially frozen one between US-style democratic capitalism and Soviet-style communism. Mirroring the "three worlds" in the real world, the emerging field of CPE divided into a comparative communism subdiscipline, the CPE examined here, and analyses of development. Among CPEs of advanced industrial countries, the US supermodel was the obvious choice for emulation, albeit tempered by substantial domestic pressure for social protection, on the one side, and American reengineering of their domestic politics via the Marshall Plan and electoral interference, on the other.[16] Forward-looking European automobile firms were already emulating US production and advertising practices before the war.[17] Postwar, US economic and military dominance made it the default model for capitalism. States pressured their firms—above all automobile manufacturers—to emulate US practices, while carrying over aspects of wartime economic planning.

This institutional isomorphism by nonsupermodel economies shifted them toward a greater use of the cheap and abundant social or material resources that powered whatever country got identified as the "right" solution to current economic problems and, thus, as the supermodel.[18] But the fallacy of composition matters here too. If all economies try to use those material and social cheap resources, they stop being cheap. Successful emulation of continuous-flow automobile production leads to oil shortages. Successful expansion of continuous-flow production can tighten labor markets and enable strikes driven by status issues.[19] Resource exhaustion in turn undermines the material and social basis for the current supermodel. Like the owl of Minerva, academic supermodels presenting a coherent understanding of institutional configurations typically fly off the press just as those configurations have exhausted their social and material basis.

Both Shonfield and Galbraith were already discussing the isomorphism problem in the 1960s, anticipating elements of the rational expectations model.[20] Shonfield, for example, argued that too much or too little understanding of a given economic policy model would nullify its utility. Too little knowledge, and actors lacking logics of appropriateness would be unable to orient their action around that model.[21] Too much knowledge, and actors would necessarily have doubts about the efficacy of their actions; logics of consequence would break down, via what we now label rational expectations, as overly knowledgeable actors began to game the system.

It is important to note here that the supermodels are only representations of reality and that we are not claiming below that any given supermodel is an accurate representation. Disjuncture between the representation and the actual object is a given. So any given supermodel might well misrepresent reality in ways that go beyond the usual simplification inherent in any analytic exercise. Indeed, each supermodel typically has a parallel dissident literature arguing that the institutional features lauded as that supermodel's strength were actually weaknesses. Thus, the "Japan as number one" supermodel provoked dissents from, among others, Friedman and Okimoto over the relative efficacy of state industrial targeting using subsidized capital and van Wolferen over whether a Japanese state actually existed.[22] These dissents often gathered as much attention (in terms of citation counts and publications) as the original supermodel publication. But they operated on the research terrain established by the supermodel.

Moreover, a whole body of Marxist and *marxisant* literature dissented from the entire mainstream of CPE discussed here. This literature grew out of the French "Regulation School" and its contemporaneous American cousin, the social structures of accumulation school.[23] Unlike the works surveyed here, these did attend to macroeconomic issues and particularly to the question of the quantity and stability of demand. That was particularly true of Piore and Sabel's *Second Industrial Divide*, the only regulationist-influenced study that managed to exert much influence on mainstream American CPE, perhaps because it contained within it a turn to the supply side.[24]

Piore and Sabel, like the Regulation School, focused precisely on the two fallacies of composition. First, a fully Fordist production regime was impossible, insofar as Fordism required general-purpose tools and skilled labor to make its special-purpose (asset-specific) machinery. Second, stabilizing and balancing supply and demand required national- or global-level institutional solutions and did not grow naturally out of the aggregation of micro-level actors (firms and individuals). Piore and Sabel argued that local and global demand-side management was failing, and thus someone had to buffer the supply side instead. They argued that flexible specialization would make supply less rigid and thus temper both inflation and unemployment. Yet Piore and Sabel's nascent flexible specialization supermodel gained little traction in either the real world or academia. Articles on central bank independence appeared at roughly ten times the rate of those on flexible specialization in eight top political science journals; and although many Marshallian industrial districts exist, Italian real per capita income in 2016 was the same as in 1999, which dampened enthusiasm for the Italian model.[25]

We focus on five major supermodels out of the full range of CPE supermodels over the past fifty to sixty years: the organized capitalism literature, the corporatism debate (which in turn divides into two phases), the developmental state literature, and the varieties of capitalism literature. We will use Andrew Shonfield's *Modern Capitalism*, articles in both Fred Hirsch and John Goldthorpe's edited volume *Political Economy of Inflation* and John Goldthorpe's edited volume *Order and Conflict in Contemporary Capitalism*, Fritz Scharpf's *Games Real Actors Play*, Chalmers Johnson's *MITI and the Japanese Miracle*, and Hall and Soskice's *Varieties of Capitalism* as representative highly influential examples, along with some works selected from their penumbra of related publications.[26]

Each of these supermodels reflected academic efforts to explicate solutions to the problems of a social order facing exhaustion at the end of the prior period. *Modern Capitalism* analyzed planned economies and collective bargaining as responses to the Great Depression, along with the US economy's slow growth relative to Europe during the 1950s and early 1960s. The corporatism literature addressed the evident problems in *Modern Capitalism* literally and metaphorically by looking at the collective bargaining strand. Planning and bargaining interacted to produce inflation at politically unacceptable levels: could inflation be controlled? We divide the answers into "carrot" and "stick" phases. Meanwhile, the mostly Asia-centered developmental state literature paralleling the Europe-centered corporatist literature captured the supply-side planning strands in *Modern Capitalism* and elevated them into a central feature of its hyperinterventionist Asian supermodels. *Varieties of Capitalism* sought to explain how different institutional combinations of planning and collective bargaining characterized a resurgent United States and Germany, providing a better theorized version of Michel Albert's distinction between liberal and Rhenish capitalisms.[27] Finally, some green shoots of a macroeconomic demand-side analysis have emerged in response to the post-2008 crises and to CPE's inability to put forward a compelling (and, it is to be hoped, accurate) explanation for those crises that enables steps toward a more stable economy. Table 1 helps orient the reader.

Andrew Shonfield and *Modern Capitalism*

Shonfield's *Modern Capitalism* presented a comprehensive institutional analysis of rich-country political economy in the postwar period. Shonfield effectively explained

Table 1. A Schematic View of Five Supermodels.

Attribute	Fordism[a]	Corporatism: Carrot Phase	Corporatism: Stick Phase	Developmental State	Varieties of Capitalism
Time period	1950s–1960s	1970s–1980s	1980s–1990s	1980s–1990	2000s
Paradigmatic authors	Shonfield	Hirsch, Goldthorpe	Hall and Franzese	Johnson	Hall and Soskice
Level of analysis	Demand- and supply-side management at a macro level	Demand-side management at a macro / meso level	Supply side via microeconomic reform and demand side via meso-level wage restraint	Supply-side management at a meso level	Supply side at a micro level
Ethos	Equitable distribution of growth	Restoration of stability	"Rules not discretion" to maximize disinflation	Mercantilist maximization of state power	Strategic coordination by micro-level actors
Main problems (policy focus)	Balancing demand with supply, legitimacy	Inflation as a problem of social order	Inflation framed as a competitiveness problem	Export performance	Coordination among firms, between firms and workers; asset-specific investment (or not)
Main actors	State planners plus unions, business organizations	Unions, employer associations, and finance ministries	Central banks, disciplining unions and employer associations	"Pilot" bureaucracies	Firms and their business associations
Main instruments/ mechanisms	Indicative planning to secure stable investment levels	State-supported coordinated bargaining	Coordinated bargaining under the threat of CB-instigated rate hikes	Industrial policy via credit allocation, picking winners	Policies to build institutional complementarities
Policy benchmarks	GDP growth, employment	Low inflation	Low inflation and central bank independence	Export surpluses	Cooperation around institutional solutions to coordination issues

Source: Authors' construction.
[a]"Fordism" as a label for Shonfield is a bit anachronistic but permits a connection to the essential problems of supply-demand management and organized capitalism characteristic of his era.

the first great moderation: the Keynesian taming of the violent business cycles that had racked pre-1940s economies. In doing so, he in effect started or restarted CPE as a field, by problematizing the institutional sources of growth and contrasting the growth problems of the older, US supermodel against the relatively better performance of the French and German economies. Shonfield thus partially departed from such earlier institutionalists as Thorstein Veblen and John R. Commons, who were primarily concerned with the forms that capitalist production took and the distributional consequences of those forms, while picking up the growth concerns of later institutionalists like Josef Steindl and, implicitly, Joseph Schumpeter.[28] Unlike his contemporary institutionalist J.K. Galbraith, he was explicitly comparative.[29]

Shonfield explained how organized capitalism generated economic stability as a general phenomenon in the Atlantic economies despite variation in the specific national macrosocial actors and institutions creating variation in stability, employment, and growth outcomes. Shonfield had a demand-side orientation, showing, as he put it, how high real wages could also be consistent with high investment levels. What linked them was "keep[ing] demand constantly at a very high level."[30] Finally, Shonfield saw maintaining the legitimacy of planning as the critical issue in state organized planning. This planning largely addressed manufacturing, which at that time was the heart of the economy.

Shonfield starts with Keynes's main concern, namely, "the problem of how to provide employment for more people using a given stock of productive assets."[31] But he adds a Schumpeterian concern for growth and technological development to this, as well as putting institutional flesh on Keynes's analytically austere skeleton. Coordination at the level of the whole economy produced good outcomes for two core macro-level dependent variables constituting the social purpose of the economy: aggregate growth and employment.

How did Shonfield explain growth and employment? The summary in chapter 4 highlights expanding international trade, desynchronized business cycles, and a global construction boom as necessary but not sufficient conditions for economic stability. Rather, says Shonfield, "economic planning is the most characteristic expression of the new capitalism," explaining the "success of the modern capitalist society in reversing the pressures for high consumption at the expense of investment."[32] And indeed, in some of the most successful cases, the postwar wage share of GDP was lower than in the prewar period, despite rapidly rising absolute wages. That is precisely why the "organized" part of organized capitalism also mattered. Planning required various social actors to cooperate with state planning, and cooperation could come only from organized actors. Centralized collective bargaining was prerequisite for delineating and enacting the plans that tamed the violence of the market. This planning had to be seen as just and legitimate, because it touched directly on distributional issues. Absent a sense that distribution was just, and that today's wage restraint meant higher wages tomorrow, planning would have collapsed.[33]

The comprehensive collective bargaining systems and far-reaching planning systems Shonfield elucidated determined the distribution of income between capital and labor and where new capital income would be invested. Explicit political bargains produced a predictable income distribution and thus produced more economic stability, validating planned investment. Reciprocally, stability led to more growth and employment by inducing more investment. Finally, in a nonfallacy of composition, stability at the level of individual economies produced stability among all rich economies, with the expansion of trade helping to produce full employment by opening up supply bottlenecks in the preglobalization world economy. Shonfield's major cases highlight the relative salience of legitimate planning and collective bargaining in allocating capital and stabilizing demand. Within these cases, France is the clear supermodel of *Modern Capitalism*, whose animus was "Why are the British unable to emulate the French?" and "How can the Germans plan without a visible state?"

Shonfield answers those questions by looking at how real-world, organized political actors operated within logics of appropriateness specific to each country. But these logics had to be built through negotiation, repeated interaction, and successful implementation. Shonfield does not single out a planning tradition in France as the source of this success; surprisingly, the French initially looked to Britain for ideas about planning as process and institutions. Rather, he highlights how French planners built consensus among key actors by bringing together handpicked representatives from capital, labor, and consumers to lay out a broad scheme for economic development.[34] Planning could never be a purely technical exercise, nor could it be successfully imposed from the top down, despite certain caricatures of France and Japan. Successful planning needed economic actors to grant legitimacy to both the means and ends of planning in order to secure compliance with planning. Shonfield's core actors were macrosocial organizations, like the French *commissions de modernization* and German employers' associations rather than abstract individual firms or workers. Shonfield's negative cases, the United States and Britain, similarly highlight the legal and cultural reasons why centralized and effective union federations and employer associations did not exist, and thus why planning agencies had little apparent power. Intellectually, Shonfield is thus to VoC as Chandler (*The Visible Hand*) is to Williamson (*Markets and Hierarchies*); real actors operating in different specific contexts versus abstract actors, production versus exchange; and throughput maximization versus transaction cost minimization.[35]

Shonfield's analysis of planning focused largely on demand, not just supply. Thus, French indicative planning mattered not because it increased output and then that increased physical output created its own demand through Say's law. Rather, planning mattered because businesses could count on reliable demand over the life of any given plan. In turn, they could then plan and execute their own investments, stimulating aggregate demand. Planning created its own demand in advance of supply, operating through demand-pull rather than supply-push.[36]

Shonfield was somewhat prescient about the limits to his modern capitalism. Although collective bargaining and planning had tamed the business cycle, Shonfield did not believe that these things worked automatically. Moreover, maximizing demand ran the risk of igniting inflation. Planning required political "skill and will."[37] The chapter on France, for example, lingered on planners' efforts to get cooperation and support from politicians. Shonfield thus repeatedly located modern capitalism's major vulnerability in a potential loss of political legitimacy and normative consensus over the utility of planning and the distributional outcomes it produced. The apparent illegitimacy of state intervention in the United States and Britain hindered public planning. Planning changed the distribution of income, as did inflation, and engineering a visible change in the distribution of income required a consensus on the outcome. Anticipating the subsequent corporatism literature, Shonfield noted that inflation could be controlled if

> each of the main groups, the wage earners and the owners of capital in various industries, agree in advance on how big a share of any increase they will expect to receive in wages and profits respectively. But of course such an "incomes policy" could not possibly work without a basic identity of view about the main objectives of economic and social policy and the methods to be used to attain them. . . . To run a successful "incomes policy" a society must not only be just; it must immediately be seen to be so.[38]

Simply aggregating individual firm and worker preferences via the market would not produce stability.

Chapter 10 and the two final chapters of *Modern Capitalism* dealt with the decreasing public accountability of insulated managers, bureaucracies, and economic interest organizations. Shonfield, an English liberal, worried that macrosocial institutions would circumscribe individual liberty, producing anomie and injustice.[39] He correctly understood and predicted the delegitimizing consequences of this insulation and the degree to which it would endogenously generate resistance. The late 1960s and 1970s saw explicit challenges from both left and right to centralization, bureaucratic control, and the standardization and routinization of life necessary for successful planning. In addition to the challenge posed by this loss of legitimacy, a purely material exhaustion also emerged endogenously as relatively successful planning everywhere put pressure on environmental and energy resources.

The owl of Minerva flies. *Modern Capitalism* was published in 1965, on the eve of a decade of intense strife between management and labor, particularly in the archetypically Fordist automobile industry. Fordist-era macroeconomic planning relied on three cheap resources: docile semiskilled male labor, docile female compliance with housewifery, and docile ex-colonial suppliers of cheap oil. Compliance with collective bargaining rested on a steady supply of cooperative—and increasingly immigrant—semiskilled workers coming into the core Fordist factories. Success in generating full employment elevated disputes over fair shares, the monotony of work, and the homogenization of the labor force into the great strike wave of the 1960s.[40] Successful automobilization increased global demand for oil. Strikes and oil-price shocks triggered the kind of inflation that Shonfield's more farsighted union leaders already feared in the early 1960s.[41] As Piore and Sabel argued retrospectively, rigid Fordist production systems could not cope with the volatile labor and raw-material markets they created through their own successful expansion.[42]

Unprecedented inflation thus became the focus for academic study, and a new literature focusing only on corporatist collective bargaining replaced Shonfield's modern capitalism; other potential pathways (e.g., flexible specialization) became byways. At the same time, the surprising strength of the Japanese economy, and particularly its rising share of international trade, generated a separate literature on planning, with the developmental state literature applied mostly to Japan and developing Asia. Shonfield's analysis thus split into two streams that matured simultaneously and later rejoined in the VoC literature. We consider the corporatism literature first, then the developmental state literature. Significantly, CPE did not pick up on the importance of women's revolt against economic exclusion until much later, and even then largely in analyses of the welfare state and, in a disguised, genderless fashion, arguments about the new service economy.

Corporatism

Modern Capitalism emerged organically from the Depression and war-economy experience; the corporatism supermodel emerged organically from modern capitalism's inflationary tendencies and the breakdown of legitimacy in the great strike waves of the 1960s. In the roughly ten years that passed between Shonfield's book and the emergence of the corporatism literature, inflation and labor strife signaled a return to volatile markets. People presumed that wage leapfrogging lay at the heart of accelerating inflation, so the supermodels in the corporatism literature proposed bilateral or trilateral negotiation or voluntary self-restraint as ways to tame inflation (i.e., militancy) in labor markets. In short, the corporatism literature took up the collective bargaining and legitimacy strands in Shonfield, emphasizing their operation in relatively low-inflation northern Europe. Shonfield addressed collective bargaining's role in securing an equitably distributed, sufficient and stable level of demand. The (neo)corporatist supermodels, by contrast, addressed the problem of stagflation. At an even deeper level they were concerned with the re-creation of a stable social order with docile labor after the consensus that Shonfield identified had broken down. Here, demand was not something to be maximized in pursuit of full employment but rather seen as tendentially inflationary.

The corporatism supermodel literature fell into two phases defined by the nature of the state-union link and the main policy objective. Both phases dealt with efforts to bargain within existing institutions or to change those institutions in order to reduce cost-push/wage-push inflation and restore shop-floor order. We call these the "carrot" and "stick" phases, depending on whether the state is using the carrot of expanded social spending or the stick of tight monetary policy to induce cooperation from unions.

Sweden of the Haga Accords was seen as the ideal case of a carrot relationship between unions and the state.[43] In this model, the state, via finance ministries largely controlled by left political parties, offered future welfare benefits and tax cuts in exchange for wage moderation now. Thus, the state tried to induce unions to moderate wage demands and to prevent wage leapfrogging by recentralizing collective bargaining. Here, the active parts of the state were the social welfare and fiscal side, offering rewards for good behavior.

Model Germany became the supermodel for the stick state in the second phase of the corporatism literature, reflecting the Bundesbank's extraordinary power. This model stressed direct state restraint of wage demands, with the state operating through the central bank and securing compliance using threats of higher unemployment. Here, the relevant part of the state was an independent central bank focused solely on reducing inflation through a coercive relationship with unions.

The corporatism supermodels' initial core concern was disorder. Schmitter's rescue of the term for analytical purposes revived concepts that emerged, tellingly, during the political disorder of the 1920s.[44] But inflation signified disorder rather than street fighting. Hirsch and Goldthorpe clearly state the problem:

> In the past decade, the problem of inflation has escalated from a continuing irritant to a blight on the stability and efficient performance of the leading economies and to a potential threat to the preservation of democratic societies. . . . Inflation of the kind now endemic in the noncommunist world is more than an economic problem. It pervades the political and social structure of society and may become embedded in those structures.[45]

Hirsch and Goldthorpe stressed that although economists were busy seeking a technical solution to the problem of inflation, only a political solution was possible; they thus preserved the legitimacy strand of Shonfield, but with a new problematic. This tension permeated the corporatism literature, which shifted from praising overtly political solutions for inflation via the carrot state to praising seemingly technical but covertly political solutions via the stick state. In the CPE literature, this can be seen in the shift from Katzenstein, who emphasizes a shared sense of social purpose, to the thinner institutionalism of Hall and Franzese, who reduce politics to signaling.[46] More generally, the carrot version of corporatism presumed that unions wanted to cooperate, whereas in the stick version they had to be coerced.

Inflation and rising concerns about export competitiveness were the surface manifestations for the question of whether the state could contain or reduce the power of the labor movement and thus generate an institutional solution to the inflation problem. Fifty years later this concern for union power might seem risible. But in the 1970s the wage share of GDP and strike activity peaked at historically high levels. As late as 1984, John Goldthorpe could still be writing about the degree to which organized labor posed a threat to social stability in capitalist societies; the title of his edited collection starts with *Order*. And tellingly, 1983 represents the absolute low point for the after-tax profit share in US GDP, at 3 percent of GDP.[47]

Academically, the corporatism literature sought to fix anomalies that did not fit Shonfield's analysis. Given the end of labor quiescence, the facts had changed, and analysts struggled to incorporate those changed facts within existing arguments. Using additional, newly relevant facts, such as the degree of union centralization and then the degree of central bank independence, this literature evolved increasingly detailed studies of the conditions producing social and macroeconomic stability. The corporatism literature picked up methodologically individualist and microeconomic arguments from Mancur Olson's *Logic of Collective Action* to answer the question of whether bargaining by organized interest groups could produce stable, positive macroeconomic outcomes.[48]

While the corporatism literature was not initially quantitative, it became increasingly so, borrowing statistical and formal modeling techniques from economics as well as economic theories of politics. The connection to Olson's microfounded arguments made this step easy. This systematic testing of hypotheses, albeit within the confines of an extremely limited set of cases and thus with enormous problems with statistical degrees of freedom,[49] set the stage for a shift of focus to "new facts" about central bank independence, displacing the older focus on unions and their internal organization.

The core assumptions in this research are intimately connected to movement away from Shonfield's macrosocial perspective. Calmfors and Driffill adapted Olson's microfounded argument to explain wage-push inflation.[50] They argued that differing levels of union centralization produced different levels of inflation, but in an inverse U-shaped rather than linear relationship. Standard economic theory argued that rising levels of unionization should cause wage-push inflation. Calmfors and Driffill agreed that disorganized labor markets should have no wage-push inflation, because wages should revert to marginal productivity for any given worker. In organized labor markets, unions, like any oligopoly, could use their control over the supply of labor to push wages above their market-clearing rate and pass these additional costs along to the more numerous disorganized workers and consumers. But above a certain level of centralization, unions pushing wage demands in excess of productivity growth would face either higher inflation that wiped out nominal wage gains or rising unemployment as exports were priced out of world markets. Calmfors and Driffill thus saw economies as falling into three groups, with inflation highest in the middle group. Although this formal insight did not emerge until the late 1980s, it explained the outcomes that motivated the choice of centralized Sweden as a supermodel in the 1970s and remains a central part of the later VoC literature.

Sweden's more or less encompassing trade union federations, LO and TCO, enabled bargains with the state over the rate of wage growth. LO represented half of Sweden's workforce in the 1970s, so it could not externalize wage increases above productivity growth. Unions could exchange wage growth today for promises of an increased social wage in the future and policies to sustain full employment today. But could these unions then bind their members, preventing leapfrogging and inertial inflation? Legitimacy issues thus began giving way to issues of credibility. Only the state could credibly commit to a carrot by codifying a future stream of payments in legislation. Although business faced no such constraint on its future behavior, Sweden's tax system encouraged continued investment, and LO's strategy in the 1970s aimed at gaining some measure of control over investment.[51] Strong unions could thus confidently enter into these bargains. Business, meanwhile, appeared as a passive price taker in world markets. As with Shonfield's modern capitalism, the first phase of the corporatism literature captured real behaviors based on what turned out to be an exhaustible resource: unions' and business organizations' centralization and control over their members. Rank-and-file compliance with wage restraint and the erosion of wage relativities and firms' tolerance for loss of autonomy over wage levels proved hard to sustain over time even in the paradigmatic Nordic economies.[52]

The stick half of the early corporatism literature thus began in the mid- to late 1980s, as more economies began shifting toward Calmfors and Driffill's middle position. Here, direct state efforts to contain wage demands operated through the central bank and used the stick of threats of higher interest rates and increased unemployment to secure union compliance. Fiscal and social policy tools receded. A new version of Model Germany—the old one emphasized production and export excellence—centered on inflation performance and exchange-rate strength gradually emerged as the clear supermodel for this phase, paralleling the emergence of the Maastricht criteria in the European Union.

In a series of sophisticated analyses, Fritz Scharpf provided both the intellectual bridge between the carrot and stick state literatures and also to the VoC literature.[53] Scharpf contrasted the dramatic differences in inflation and employment performance during the turbulent 1970s among Britain, Germany, Sweden, and Austria. He argued that steering between the Charybdis of punitive austerity and tight money and the Scylla of cost-push inflation required wage moderation plus coordination across key policy areas. When inflation was cost-push, and unemployment was partly a result of insufficient demand, wage moderation could open up room for demand stimulation by curbing cost-push effects and boosting productivity and investment. For Scharpf, Austria's relative success rested on trust that the social partners would deliver on their commitments to wage moderation and investment.[54] By contrast, no British actor could commit, and the German Bundesbank actively distrusted unions and, less so, business. Scharpf dismissed the former Swedish Haga supermodel because neither the state nor central bank disciplined the Swedish labor movement. But he also dismissed Modell Deutschland, because he saw German unions in exactly the opposite position of the Swedish ones, "compelled by their own organizational logic to pursue strategies that they considered macroeconomically rational, [and] no longer able to extract a political price for their de facto collaboration."[55] Scharpf's analysis rested on a tripod built out of Shonfield's focus on legitimacy, the corporatist literature's focus on organizational capacity, and the emerging stick state focus on productivity and central bank autonomy.

Scharpf's critical stance on Modell Deutschland was lost as the economics literature and then the corporatism literature on central banks increasingly focused on inflation targeting regardless of its employment and growth consequences. Kydland and Prescott's elegant but data-free dismissal of discretionary planning in favor of rigid rules provided an intellectual basis for freeing central banks from overt political control and for incorporating fixed rules or targets into deals like the Maastricht Treaty.[56] This completed the shift from Shonfield's real actors to abstract ones. Subsequently, leading political economists like Peter Hall merged the corporatism literature with the growing literature using the degree of central bank autonomy as its only independent variable. Hall argued that the interaction between central bank independence and the wage-determination system generated inflation outcomes. A later quantitative article with Robert Franzese argued that in the presence of coordinated bargaining, central banks could avoid imposing higher unemployment simply through an effective signaling process.[57] Sticks needed merely to be shown if social actors could work together.

All of these corporatism approaches retained a lingering if limited concern with demand and employment, in contrast to the Chicago school–inspired conventional wisdom that the only proper macro task for government was stabilizing inflation at low levels and that the best way for an independent central bank to achieve any given inflation target was inflation targeting monetary policy. The disinflationary experience of the second "great moderation" in the 1990s reinforced the apparent validity of the Chicago approach. Yet it too was founded on exhaustible resources, namely, political patience with rising unemployment and subsequently worsening fiscal deficits. Put simply, in much of Europe, squeezing the inflation side of the economic balloon caused the unemployment and fiscal cost side to bulge outward.

Ironically, the return of mass unemployment brought the corporatist literature back to its carrot roots with a third flavor of corporatist supermodel in the 1990s. The explicitly supply-side formula of *flexicurity* blended inflation and employment concerns. Denmark and the Netherlands had a brief moment in the sun, because they appeared to attain American employment levels without the harshness of American labor market norms.[58] With unions retreating but with unemployment imposing great fiscal stress, the state could shift back to employment issues. The flexicurity literature argued that robust social welfare systems and residual corporatist institutions could combine to allow labor market flexibilities that produced full(er) employment. But all the action in flexicurity occurred in the interplay between the state's labor market policies and its welfare state institutions, with unions playing a much-diminished role.

Here, the shift from a concern with cost-push inflation to the unwillingness of firms to hire in rigid labor markets reflected a continuing shift from the macro to the micro level and from unions to firms.[59] In this respect, the flexicurity model foreshadowed VoC's emphasis on firms. The entire EU-Lisbon jobs strategy was premised on the generalization of the flexicurity model to non-Nordic Europe. In the flexicurity supermodel, welfare was not a side payment for wage moderation and quiescence but rather a means to reduce risks both for individual employees and employers and thus make labor markets less rigid. As an argument, flexicurity was supply-side and microeconomically oriented. The flexicurity model thus exhibited a fallacy of composition in that it depended on sources of demand external to either the labor market or its small European economies to attain full employment. Indeed, although we pick up this thread later when we discuss VoC, the demand created by housing booms and privatized Keynesianism seems to have had more to do with employment success than did supply-side reforms.[60] But before we turn to VoC, we need to examine how the planning strand in Shonfield turned into a pure supply-side, micro-level argument, equally blind to the fallacy of composition.

The Developmental State Supermodel

The corporatism literature evolved from Shonfield's arguments dealing with fair shares, collective bargaining, and the state's ability to manage class conflict. In both its carrot and stick phases, this literature searched for the optimal institutional structure to control inflation without damaging employment. The corporatism literature thus analyzed national structures as quasi- or fully independent units. In this sense, it implicitly endorsed at least part of Shonfield's simple, Keynesian, demand-side view of the world even as the corporatism literature became increasingly supply-side oriented and thus began losing sight of Keynes's fallacy of composition arguments about savings and demand.

By contrast, the developmental state literature picked up the planning and supply-side strands in Shonfield. This literature identified first Japan and then follow-on Asian states as consummate planners, while also crediting France with significant planning ability. It decisively shifted away from Shonfield in two limiting ways. First, it dropped Shonfield's closed-economy assumption. Exports mattered for Shonfield, but they mattered because imports allowed a rapidly growing economy to overcome temporary bottlenecks, or because exports allowed a slowing economy to keep traction. In the developmental state literature, global market share and current account surpluses became if not *the* metric for success, certainly one equal with Shonfield's growth and employment metrics. The developmental state literature thus rested on a massive fallacy of composition even as it adjusted to ongoing globalization. It assumed demand could always be found somewhere out in the global economy, reflecting a shift to an economic environment in which countries did not necessarily have to take responsibility for keeping their internal demand growth in line with their own productivity growth.

Thus, second, the developmental state literature decisively shifted toward a supply-side orientation. For Shonfield, the whole purpose of planning was to anticipate and increase output from bottleneck industries or services where future demand might exceed supply.[61] Demand came first. By contrast, the developmental state literature explained the origins of internationally competitive export industries. This literature thus stands midway between Shonfield's concern for growth and VoC's concern for the effective coordination of production. It reflects a shift from quantity (the aggregate economy) to quality (the merits of specific sectors), and a partial shift from control over finance to inter- and intrafirm relations. These macro- to meso-level shifts helped open the door to the subsequent VoC literature, which transformed the developmental state literature's concern with exports into the issue of distinct export profiles.

Japan was the developmental state literature's alpha supermodel. *Modern Capitalism* ignored Japan; Shonfield thought it sui generis. Although Ezra Vogel's *Japan as Number 1* made the first claim for Japan's supermodel status, Chalmers Johnson's analytically richer *MITI and the Japanese Miracle* became the touchstone for later analysts, whether or not they agreed with his argument.[62] *MITI*'s title signals the macro to micro shift, as it linked a handful of state agencies, particularly MITI and the Ministry of Finance, to a handful of critical manufacturing industries. Similarly, Johnson's dependent variable was Japan's industrial modernization and export success rather than growth per se. Johnson's book was part of a broader contemporaneous wave of books on industrial policy, that is, targeted efforts to develop competitive industries in a narrow set of sectors.[63] These sector studies had a much smaller ambit than Shonfield's macroeconomy or corporatism's macroeconomic aggregates. Inflation, the core concern of the corporatism literature, disappeared. Indeed, Japanese inflation rates generally exceeded the OECD average until the 1980s. Likewise, employment was a secondary outcome of trade success.

In another narrowing of Shonfield's field of vision, Johnson's independent variable was the shared social purpose of a handful of actors in a single bureaucracy. *MITI and the Japanese Miracle* is a genealogy of that ethos in relation to the targeted use of finance for developmental purposes. Johnson's emphasis on state-directed finance contrasted plan-rational economies with market-rational economies, creating a Pacific version of the later Atlantic *Varieties of Capitalism* dichotomy. The critical difference distinguishing Johnson's two types was their ethos, more than any actual organizational or legal differences. But as with conventional understandings of Shonfield, Katzenstein, and Scharpf, much of the subsequent literature fastened on only one aspect of the larger argument: the organizational aspects of planning and in particular control over financial flows.[64] For example, two subsequent books focused on the Korean state's use of discretionary and contingent financial subsidies to firms in order to induce world market competitive export production.[65]

Thus, the normative or ethical (in the sense of worldview) side of Shonfield's argument and indeed Johnson's argument was lost in debates about whether planning actually worked and which specific organizational technique mattered most.[66] For example, one of Johnson's strongest, albeit friendly, critics, David Friedman, argued that the outcomes Johnson credited to MITI's planning, cartels, and incentives were actually generated from the bottom up and in opposition to MITI's vision of a consolidated, large-firm, Fordist economy (which was MITI's goal and partially informed by the academic literature).[67] Friedman argued that Japanese firms succeeded through competitive strategies that aimed at breaking up mass markets into smaller specialized segments through continuous product modification and new product development by small and medium-size enterprises—an Asian version of Streeck's contemporaneous diversified quality production argument. All of this is antithetical to the enterprise consolidation that Shonfield and Johnson thought necessary for planning. Similarly, Daniel Okimoto raised the concept of reciprocal consent to capture the interaction of state and business elites, expanding the question of ethos from the state to firms.[68] Peter Evans's notion of "embedded autonomy" anchored reciprocal consent—which after all could simply be about corrupt bargains—back in the seemingly objective dichotomy between Weberian and predatory bureaucracies.[69]

But embedded autonomy left three critical conceptual issues from Shonfield hanging. First, as Weber himself said, the state is ethically neutral. Specific historical circumstances shaped MITI's ethos. Second, state-financed expansion and consolidation of industry was inherently inflationary—the issue motivating the corporatism literature. So the developmental state literature retained a subterranean link to the corporatism debate. By bringing more and more labor into assembly-line factories, and by supplying more and more credit to expanding firms, the state expanded the potential for inflation. Large, overindebted firms could not be left to go bankrupt for fear of negative employment and output consequences. As Loriaux argued, this locked the state into even more lending and thus expansion of the money supply.[70] Simultaneously, a few militant workers could bring production to a halt. This motivated the inflationary wage developments in 1970s Europe. But Japan, unlike much of western Europe, had labor markets segmented not only between core and peripheral workers but also between workers in different core firms. It had already attained the golden land of locally strong but nationally weak labor that the "stick" corporatism literature identified. Those unions effectively could not bargain for wage increases greater than productivity growth at their own firm, limiting wage-push inflation. The subterranean link to the corporatism literature hints at one of the limits to the developmental state supermodel.

In the real world, the developmental state supermodel exhausted its initially abundant resources, just like all the others. Developmental states' success in generating excessive streams of exports—"excessive" meaning politically unacceptable in North America and western Europe—provoked decisive changes in the domestic and international environment that undermined the developmental state. Domestically, export success gave rise to financial deregulation as firms accumulated reserves. This limited the state's ability to use credit markets to control firms. Internationally, export success led to market closure and pressure for more financial deregulation. So, developmental success eroded the model from within and without.

The counterpart to Japan's export surplus was US trade deficits. These deficits motivated two Republican presidents, Nixon and Reagan, to devalue the dollar, liberalize exchange rates, and partially deregulate finance. In turn, floating exchange rates revealed the fallacy of composition aspects of French and Japanese export success. As Loriaux argues, floating rates forced France to dismantle the entire system of financial controls at the heart of indicative planning.[71] In Japan, deregulation proceeded more slowly, but financial deregulation permitted firms to divert investment funds into land and stock market speculation. Successful planning and export drives gave firms the capacity to self-finance out of retained earnings, rather than relying on the state's offer of contingent finance. Facing limited export growth, they turned to speculation rather than reinvestment for growth. Both signaled the end of the supermodel, even as a second generation of popular books errantly heralded the Japanese century.[72]

Second, the fallacy of composition around demand reemerged at the global level. Emulation of the Japanese model eroded Japan's supremacy from below and from above by exhausting global demand. Developmental states in Korea and Taiwan competed with Japanese firms in commodity lines of business, while US firms shifted into more innovation-intensive product lines. Although discretionary control over finance gave MITI a mighty lever to extract compliance from mass-production firms seeking to move to the technology frontier, it was a less supple tool for moving the technology frontier outward. Meanwhile, in industries based on mass production and assembly lines, US firms assimilated enough of the "Toyota model" to retain or regain market share.[73] This pressured Japanese manufacturing firms. Slower global demand growth in the context of lifetime employment systems implied gradually rising overstaffing as productivity growth exceeded market growth.

The final source of breakdown in the developmental state supermodel came on the moral or normative side of the bureaucracy. Critics argued that Johnson's masterful bureaucracy had degenerated into turf wars, political gridlock, and an uncompetitive convoy capitalism.[74] Loriaux similarly noted the breakdown of the École nationale d'administration–derived moral orientation behind French indicative planning as private sector pathologies over pay, pointless expansion by firms, and real conflicts over market share infected ex-bureaucrats parachuted into the private sector.[75] Successful firms began hiring bureaucrats to influence the bureaucracy, reversing the flow of influence that *amakudari* and *pantouflage* generated.

The Japanese economy remained a manufacturing and exporting powerhouse but stagnated after 1990. Its share of global GDP inexorably shrank, and its firms increasingly moved production overseas. From 1991 to 2016, Japan's share of global GDP fell by 50 percent, while gross fixed capital formation fell roughly 12 percent in real terms.[76] Meanwhile, the United States enjoyed a second fifteen minutes of fame as a supermodel in the late 1990s. This provoked a new polarity already foreshadowed by Michel Albert's *Capitalisme contre Capitalisme*.[77] Although we cannot delve into the first round of this polarity, which pitted the American "jobs machine" against European "flexicurity," we turn to the full formalization of this polarity in the VoC literature.

Varieties of Capitalism

Varieties of capitalism (VoC) completed CPE's journey from macro to micro and from demand- to supply-side sources of growth. VoC formalized and grounded Albert's counterpoised Anglo-American and Rhenish economies. VoC asked how two different (and stylized) political economies overcame coordination problems in the extended division of labor characterizing contemporary economies. It thus moved away from Shonfield's focus on management of the macroeconomy, corporatism's focus on containment of inflation, and the developmental state's focus on state-organized export-led growth, to the management of individual people and firms, as in standard microeconomics. And as in standard microeconomics, it built up to the macro from micro-level actors, namely, firms and workers, rather than having a more Keynesian view of macro.

By emphasizing variety, VoC pushed back against mindless globalization arguments suggesting convergence around a single, market-based model. VoC thus carried over flexicurity arguments that a corporatist path was possible and that some welfare state programs enhanced competitiveness. But VoC did so using principal-agent theories anchored in microeconomics. VoC explicitly moved firms to center stage, displacing unions' role in the early corporatism analyses.[78] This reflected the real shift in social and labor market power toward firms and capital in the 1990s. The use of the new economics of organization in principle should not have limited VoC to two models. Masahiko Aoki, for example, used the same tools to develop multiple models.[79] But despite this potential for variety, VoC carried the original markets versus hierarchies dichotomy in Williamson over into its argument, positing two ideal typical and internally coherent models.[80]

VoC built off the central problem formalized by Williamson and Aoki: If markets were so efficient, why did we have firms? Actors obviously could coordinate via arm's-length transaction in markets. Why do so through other mechanisms? Transaction costs around writing and enforcing contracts in general (Coase) and especially around contracts involving specific assets (Williamson) led entrepreneurs to seek control over those assets (and workers) rather than simply purchasing them in the market.[81] VoC translated this dichotomy into a world of arm's-length, market-based interaction and a world of strategic coordination (not hierarchy) at the meso level. Different combinations of arm's length and strategic interaction produced different divisions of labor and thus different pathways to growth and employment outcomes. In particular, motivating individuals to invest in firm-specific human capital assets, and firms to invest in other specific assets, required strategic coordination outside the market.

This approach produced two model economies, a transaction-based liberal market economy (LME) and an organized coordinated market economy (CME), which in turn mapped onto stylized understandings of the United States and Germany. Each had different ways of overcoming five central coordination problems around production, namely, vocational training, corporate governance, interfirm relations, firms' relations with their own employees, and industrial relations. But in essence these are five supply-side issues: the production of labor inputs, the provision (but not production) of investment capital, the provision (but not production) of nonlabor inputs and standards, management of production and potential conflicts around production inside the firm, and the management of the relationship between productivity and wages (and thus class conflict) at the macroeconomic level. VoC thus did not completely abandon the macroeconomic concerns that animated Shonfield and the neocorporatists. But the bulk of its concerns arise from microeconomics and especially from principal-agent dilemmas that deter asset-specific investment.[82] VoC sees institutions through the lens of game theory and thus has a methodologically individualistic theoretical perspective. Despite this focus, VoC carries over from the first round of corporatist literature a concern for shared understanding, à la Katzenstein.[83] Strategic interactions among actors produce not just outcomes but durable understandings of the social meaning of those outcomes. This is what produces the (thin?) legitimacy of the institutions VoC studies.

VoC privileges neither LMEs nor CMEs but rather argues that their degree of success rests on the degree of internal complementarity among their various institutions. A hire-fire regime will not be conducive to the production of diversified high-quality goods; a system of gradually rising wages in the context of lifetime employment at one firm will not be conducive to radical innovation. Equally, banks interested in the recovery of capital via interest payments made possible by an ongoing firm's sales in product markets will not thrive in an open securities market, while venture capital firms interested in the recovery and multiplication of capital via initial public offerings will find such IPOs difficult where firms and banks prefer organic growth. Mismatches produce unemployment, slow growth, or inflation.[84]

Despite much creative work in the paradigm, VoC is anchored in an analysis of manufacturing firms. Indeed, the very point of view adopted is that of a manufacturing firm dealing with suppliers, borrowing in markets, and upgrading (or not) its workforce. Without forcing things too much, one could say that the paradigmatic VoC analysis shows how employers and employees cooperate to create and maintain a skilled male manufacturing labor force using jointly controlled educational and social welfare institutions. In this supply-side story, welfare exists to induce and preserve skills, not to stabilize aggregate income or provide dignity. This is a microinstitutional, microfounded story, in which meso- and microcorporatist organizations are the actors. Growth comes from an aggregation of actor behaviors that produces complementary institutions. And it is a manufacturing story, with cultural production, formal intellectual property rights, and household labor largely offstage.

As with the earlier supermodels, VoC's premises blinded it to the contradictions emerging from the economic system it was trying to explain. Institutional complementarity undoubtedly accounted for successful economic specialization and perhaps for some economic growth in VoC's iconic cases. But demand-side growth impulses at the level of the global economy dominated VoC's era. The United States' growth in the 1990s and 2000s was predicated on cheap oil, cheap Chinese wages, and cheap mortgage credit in the United States; the era of rising German trade surpluses was premised on US and Chinese economic synergy.[85] Without roughly $3.8 trillion of home equity withdrawal by, and $8 trillion in home-equity-generated wealth effects for, American homeowners from 2000 to 2006, would China have made so many physical exports to the United States using machinery made in Germany? And while VoC is alert to the symbiotic relationship among different sorts of production systems for different sorts of goods,[86] it commits the fallacy of composition in thinking that, for example, German export specialization in differentiated quality production could exist in the absence of US financialization, income inequality, and debt-fueled consumption.

Given its premises, VoC could at most conceive of a financial crisis as something that might affect LMEs on account of their arm's-length financial systems. As with economics, which wrote both finance and housing out of its microfounded dynamic stochastic general equilibrium models, VoC only sees finance as being material in relation to manufacturing and has nothing to say about housing or consumption more generally. VoC simply cannot explain why the German Landesbanks or for that matter banks like Deutschebank were busy speculating in the US subprime mortgage asset market or southern European housing markets rather than providing patient capital to the *mittelstand*. Nor can VoC really explain why housing markets were the focal point for (misconceived) credit creation.

VoC similarly has difficulty dealing with China's emergence as an über-developmental state, whose export surpluses on average rivaled those of Japan as a percentage of global GDP and exceeded them by a comfortable margin at their height. Japan aside, CPE's focus on developed economies makes it rather Eurocentric. Although VoC explicitly sets out only to explain developed economies,[87] one of its core implications is that complementarity exists not only within economies but also across them. VoC explains the origins of comparative advantage, of why economies specialize in the export of specific kinds of goods. But China does not fit VoC's dichotomous categories and is not complementary in global markets. Its exports range from labor-intensive garments to technology-intensive telecommunications and high-speed trains. This fact seems problematic, given that China on open market exchange rates is larger than the five biggest EU economies and thus a candidate for supermodel status and perhaps for global hegemon. VoC has trouble explaining what institutional complementarities make China's ambitious strategic plan "Made in China 2025" a threat to Germany's Industrie 4.0 ambitions.[88]

VoC's various blindnesses emerge from its supply-side and tradables foci, from its loss of sight of the fallacy of composition around exports. VoC's supply-side focus explained how different national subsystems brought different goods to market, not how those goods found sufficient monetary demand on the other side of the transaction. And while VoC plausibly sees the global complementarity between CME exports and LME imports of high-quality goods, it cannot specify the actual sources of demand for those goods. VoC's focus on complementary national subsystems, and complementarity of supply, blinds it to the way in which Chinese and German recycling of American trade deficits flowed into US and southern European housing markets and thus generated additional demand at the level of the global economy.[89] In short, losing sight of the fallacy of composition around demand creation puts phenomena like the cash out of American home equity outside the circle of light cast by VoC's manufacturing-oriented lamppost.

These weaknesses matter. The strikes Shonfield failed to predict emerged endogenously from collective bargaining systems that accommodated planners' needs more than the day-to-day needs of people as workers. VoC as an analytic paradigm emerged just as financialization became the dominant phenomenon in global economic growth and just as (mostly American) housing finance became one of the major sources of new demand in the world economy. The 2008 financial crash emerged from a deepening global division of labor in which a politically generated balancing of supply and demand inside national economies had given way to VoC's complementary production systems that balanced supply and demand at neither the national nor global level.

Today's functional equivalent of Shonfield's strikes is the rise of mass antisystem parties everywhere. This rise is deeply rooted in identity issues that make emotional reactions to the disappearance of a preferred social order the basis for voting choices. But antisystem parties arise equally from the massive outsourcing to low-wage economies by firms in both LMEs and CMEs over the past three decades. Outsourcing by price-sensitive LMEs fits comfortably within VoC's explanatory framework. That is not the case for firms in CMEs, which by definition are not competing over price. VoC has no ability to see the demand side of the economy, the workings of the global macroeconomy, or common patterns that cross over its two types.

Conclusions

CPE had a double cognitive failure in the 2000s. It missed the dynamics leading to the 2008 global financial crises and the subsequent secular stagnation because its analytic strategies steadily shifted from a macroeconomic and macro-actor orientation to a microeconomic, micro-actor orientation. Its explanandum shifted from the demand side to the supply side and from more sociological models of legitimacy to more instrumental bargaining models. A succession of ideal models for economic governance—supermodels—instantiated this shift. This analytic shift was not fundamentally flawed. It yielded interesting and useful insights about the inner dynamics of firms and complexes of firms. Yet the transition from macro to micro meant that CPE was unable to see how these better-understood discrete pieces fit together into a whole, in effect pushing the fallacy of composition away from the lamppost of research. Every research paradigm brings some set of phenomena to the foreground by pushing others into darkness.

Each step from Shonfield toward VoC shed part of earlier authors' macro and demand-side perspectives. The corporatism literature moved from Shonfield's concern with the generation of demand through organized collective bargaining to the limitation of demand through wage restraint by delving into union organization and central banking. The developmental state literature moved from planning as a social enterprise to planning as a technical enterprise by delving into planning ministries and specific control mechanisms. The microeconomic perspective that came to fruition in VoC highlighted individual (and firm) decisions around asset-specific investments and thus explained national differences in the supply of factors, and thence differences in the supply of goods from different countries.

VoC thus reunified the planning and bargaining strands emerging from Shonfield's original analysis, albeit at a microeconomic level rather than a macroeconomic one.

By reuniting them at a microeconomic level, VoC lost sight of the fallacy of composition around the sources of demand in the markets that its supply-side actors provisioned. In this movement, VoC followed trends in mainstream economics; the Hall and Soskice volume has only two references to Keynes. Moreover, VoC missed the sources of the populist political movement that had been building before 2008 but exploded thereafter. VoC's focus on Pareto-optimal equilibria took for granted stability in employment and demand, only to be surprised when the large parts of the population revolted against stable equilibria that disadvantaged them.

More generally, the flow from Shonfield to VoC reflected a globalization-driven shift in thinking about employment and growth away from a "we're all in this together" mentality toward a competitiveness frame. Capital and foreign exchange controls allowed Shonfield's desynchronized economies to help each other balance supply and demand. Financial globalization has synchronized economies and facilitated the growing trade and thus debt imbalances beneath the recent financial crises. Keynes had already tried to preempt this problem at Bretton Woods by proposing the International Clearing Union as a mechanism for bringing global demand and supply into balance.

These intellectual shifts are not irreversible, and indeed, CPE was responsive to phenomena that thrust themselves into the circle of light cast by each of its supermodel lampposts. The decade of slow growth following the 2008 crash has ignited a new debate about secular stagnation.[90] Secular stagnation is, by definition, a demand-side problem, and we would expect attention to return to macroeconomic demand-side considerations and to how the distribution of income affects demand. The green shoots of such an orientation are already visible in the stony landscape of the otherwise microeconomically oriented CPE field. Peter Hall provides a literally paradigmatic example, insofar as his entire life cycle of work stretches from Shonfield to secular stagnation, with station stops at corporatism, central banking, and VoC. Hall's earliest work in essence grappled with the ideological, ideational, and legitimacy components of Shonfield's *Modern Capitalism*. Hall's recent work returns to the themes present in Shonfield, asking about the political bases for adequate economic governance and the importance of finding new sources of demand in a world with increasingly unequal incomes.[91]

Two other promising shoots are parts of the financialization literature and the rediscovery of Michał Kalecki and to a lesser extent Keynes. These literatures are explicitly macroeconomic. The best of the financialization literature elucidates problems of modern capitalism on all three levels of analysis—individuals, firms, and the macroeconomy—without falling into methodological individualism or a supply-side orientation.[92] These analyses help us understand how the transfer of risk to individuals, the rise of value-extracting rather than value-generating forms of corporate governance, and debt-fueled growth models led to slower growth. Similarly, Baccaro and Pontusson, among others, have revived Kalecki's juxtaposition of wage-led and profit-led growth models.[93] Wage-led models are of course a demand-side approach, and income inequality is a prime cause of weakening political legitimacy in the rich economies. Indeed, Baccaro and Pontusson forthrightly call for a rethink of CPE's main model:

> In contrast to the [VoC] approach, our approach emphasizes the demand-side of the economy and focuses on trajectories of change in the post-Fordist era. We identify different "growth models" based on the relative importance of household consumption and exports and the dynamic relationship(s) between these components of aggregate demand.[94]

These analyses argue that wage-led growth models probably deliver superior economic growth as well as better outcomes in terms of income equality. Even so, these arguments understate the importance of global demand for generating growth in what are still seen as national economies. The problem is one of the global and not just the national distribution of income.

Alas, although these new ways of approaching current economic problems return to older, more political ways of thinking about the problem, we lack an empirical supermodel, precisely because no one has sorted out institutional solutions to the problems of inequality and unbalanced global demand. CPE, as always, is a follower, not a leader, in understanding the reorganization of the economy. But Shonfield's concerns about the need to boost wages and investment simultaneously in a politically legitimate way remain as valid as ever. So, what is lacking is not ideas but rather a politics that can create a more stable modern capitalism based on rising wages and aggregate demand.

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Notes

1. Joseph Schumpeter, *History of Economic Analysis* (London: Allen & Unwin, 1954), 4.
2. Andrew Shonfield, *Modern Capitalism* (New York: Oxford University Press, 1965), 66.
3. Thomas Kuhn, *The Structure of Scientific Revolutions* (Chicago: University of Chicago Press, 1962).

4. John Maynard Keynes, *General Theory of Employment, Interest and Money* (London: Macmillan, 1936). Most generally, the fallacy of composition is the assumption that something that is true for part of a whole, characterizes, or is true for, the entire whole. Keynes's fallacy of composition states that individually rational economic behavior (like excessive savings) can produce collectively irrational outcomes (inadequate demand leading to economic downturns that destroy those savings). Similarly, not all countries can run export surpluses.
5. Sonja Amadae, *Rationalizing Capitalist Democracy: The Cold War Origins of Rational Choice Liberalism* (Chicago: University of Chicago Press, 2003).
6. See, e.g., Mark Blyth, "Political Economy," in Mark Lichbach and Alan Zuckerman, eds., *Comparative Politics: Rationality, Culture, and Structure* (Cambridge: Cambridge University Press, 2009).
7. Wolfgang Streeck, in "Varieties of Varieties: 'VoC' and the Growth Models," *Politics & Society* 44, no. 2 (2016): 243–47, also suggests a Kuhnian approach to understanding the internal evolution of the varieties of capitalism approach.
8. This endogenous decay is one kind of Barnesian performativity; Donald MacKenzie, *An Engine, Not a Camera: How Financial Models Shape Markets* (Cambridge, MA: MIT Press, 2008).
9. Ibid.
10. These processes also underlie the dynamics identified in Hyman Minsky, "The Financial Instability Hypothesis," Levy Institute Working Paper no. 74 (Annandale on Hudson, NY: Bard College, 1992); George Soros, *The Alchemy of Finance* (New York: Wiley, 2003).
11. Data from Google Scholar, July 1, 2018, with some nonstandard citations aggregated into the main count. Note that Shonfield's numbers are deflated by publication well before the internet era as well as the process of forgetting described here. David Samuels, in "Book Citations Count," *PS: Political Science & Politics* 46, no. 4 (2013): 785–90, claims that roughly 90 percent of cited political science articles get fewer than twenty lifetime citations.
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13. Fred Block and Matthew Keller, eds., *State of Innovation: The US Government's Role in Technology Development* (London: Routledge, 2015).
14. See, e.g., Blyth, "Political Economy."
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18. Paul DiMaggio and Walter Powell, "'The Iron Cage Revisited': Institutional Isomorphism and Collective Rationality in Organizational Fields," *American Sociological Review* 48, no. 2 (1983): 147–60.

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21. James March and Johan Olsen, *Rediscovering Institutions* (New York: Free Press, 1989).
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23. Exemplary works are Michel Aglietta, *A Theory of Capitalist Regulation: The US Experience* (London: NLB, 1979); Samuel Bowles, David Gordon, and Thomas Weisskopf, "Power and Profits: The Social Structure of Accumulation and the Profitability of the Postwar US Economy," *Review of Radical Political Economics* 18, nos. 1–2 (1986): 132–67; David Kotz, Terrence McDonough, and Michael Reich, eds., *Social Structures of Accumulation: The Political Economy of Growth and Crisis* (New York: Cambridge University Press, 1994). There were also other European cousins in Amsterdam—e.g., van der Pijl, *The Making of an Atlantic Ruling Class*—and Scandinavia—e.g., Lars Mjøset, ed., *Norden Dagen Derpå* (Oslo: Universitetsforlaget, 1986).
24. Michael Piore and Charles Sabel, *Second Industrial Divide* (New York: Basic Books, 1984).
25. A data draw on JSTOR.org, February 13, 2018, on the terms "flexible specialization" and "independent central bank" in the *American Political Science Review, International Organization, World Politics*, the *Journal of Politics*, the *American Journal of Political Science, Comparative Politics, Perspectives on Politics*, and the *British Journal of Political Science* from 1980 to the relevant JSTOR border (typically 2014) brought up 135 articles for the former and 1,732 articles for the latter. "Fordis*" showed up in even fewer articles—106. "Developmental state" showed up in 1,200 articles. "Corporatis*" showed up in 1,242 articles. The journals were chosen on the basis of their presence among the top twenty journals in Google Scholar metrics and their general focus (which excludes, e.g., the *Journal of Common Market Studies*). *Comparative Political Studies* and *Politics & Society* are not in JSTOR.
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27. Michel Albert, *Capitalism vs. Capitalism*, trans. Paul Haviland (New York: Four Walls Eight Windows, 1993).
28. Thorstein Veblen, *The Theory of Business Enterprise* (New York: Scribner's, 1904); John R. Commons, *Legal Foundations of Capitalism* (New York: Macmillan, 1923); Josef Steindl, *Maturity and Stagnation in American Capitalism* (New York: NYU Press, 1952); Joseph Schumpeter, *Capitalism, Socialism, and Democracy* (New York: Harper & Brothers, 1942). Commons and Veblen are in some ways closer to *Varieties* in terms of their explanandum.
29. Galbraith, *New Industrial State*.

30. Shonfield, *Modern Capitalism*, 64.
31. Ibid., 64.
32. Ibid., 6, 121.
33. Ibid., 225; Barry Eichengreen, in *The European Economy since 1945: Coordinated Capitalism and Beyond* (Princeton, NJ: Princeton University Press, 2008), provides a formal model for this.
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