1. Varieties of Capitalism and the crisis

In spite of having originated more than a decade ago, the Varieties of Capitalism (VoC) paradigm, which Hall and Soskice had introduced in their seminal work published in 2001, remains influential in the analysis of the global political economy. Since its original publication the VoC approach has been referred to by many scholars as a useful framework to categorise economic divergences. The VoC approach nevertheless also received much critical attention. The more critical accounts concentrated on the fact that the VoC approach essentially differentiates between liberal and coordinated economies on the basis of the variations in the corporate governance and the production model of firms in these economies. The critics have rightly pointed their finger at the weaknesses of Hall and Soskice’s core argument, which is their relatively narrow emphasis on a corporate-based analysis. It considers companies as central actors in contemporary economies because of their role as ‘key agents of adjustment in the face of technological change or international competition’ (Hall and Soskice 2001: 6). Although the approach strongly emphasises the importance of the institutional background on which firms operate, it essentially neglects cultural aspects which are outside the ‘competitive advantage’ framework. The viability of companies is considered to be the main focus of economic policy-making. Policy-makers are hence reduced to the role of catalysts who have to find effective solutions on how to channel the pressures of globalisation in the right direction. Economic policy-making becomes a means to improve the economic performance of firms by ensuring that domestic institutions support the smooth interaction between economic actors. This follows a logic which assumes that facilitating business transactions and creating a peaceful industrial relations environment should be the principal aim of successful economic policy (Ibid.: 45).

The main contribution of the VoC approach to the globalisation debate at the beginning of the twenty-first century was to offer a new and broader perspective than the one that neoclassical economists put forward. The latter essentially considered it to be a force which inevitably leads to the radical liberalisation of national economies in response to pressure from market forces, such as capital flows. The neoliberal political paradigm of the 1980s and 1990s hence considered globalisation as a process in which economies
are orientated towards lowering transaction costs (Keohane 1984). From this perspective a best practice economic convergence model would emerge, whose competitive advantage lies in liberalisation and the openness towards foreign direct investment (FDI), labour market deregulation and the privatisation of public assets (Lane 2005; Sinn 2004a). Hans-Werner Sinn, the prominent German economist and President of the Munich based Institute for Economic Research (Institut für Wirtschaftsforschung, IFO) prominently introduced this notion into the public debate in Germany when he warned German policy-makers in 2004 that it was inevitable for the German economy to move towards the model of liberal market economies like the UK and Ireland. In this respect Sinn argued for a fully liberalised economic model with complete flexibility on prices, wages and ultimately also labour markets. From his perspective this would be ‘the condition for a successful reaction to globalisation’ (Sinn 2004b: 89).

Gill (1995) and others called this a process of ‘market civilisation’ where market forces manage to impose their priorities on global institutions and consequently increasingly also on national politics (Amin and Luckin 1996). The contribution of the VoC approach to the debate lies mainly in the rejection of the notion of a globalised convergence model and its emphasis on the importance of the differences in the institutional environment in which firms operate (Hall and Soskice 2001: 58). Hence the differentiation between a liberal and a coordinated institutional set-up.

The VoC approach nevertheless is a relatively cautious attempt to give the debate a new direction. It has not managed to offer a fundamental critique of the post-Cold War neoliberal status quo in the global economy. Neither has it identified the core weaknesses in economic policy-making which have led the global economy into its current crisis. On the contrary, VoC has supported that notion that politics would have to be subordinate to economic interests, albeit to different degrees, depending on the individual institutional framework. Hall and Soskice are quite thorough in outlining the differences in political organisation in liberal and coordinated models, which they mainly see in the different levels of centralisation. While the former tend to centralise power on the executive level, the latter show different levels of decentralisation amongst a variety of actors, such as business groups and trade unions, which are often independent from the state. This explains why policy-makers in these coordinated economies tend to avoid the implementation of policies which would threaten to undermine coordinative arrangements amongst economic actors, whilst liberal market economies tend to favour ‘market-incentive’ policies (Hall and Soskice 2001: 49). Overall the VoC approach clearly considers policy-makers in different institutional contexts to be adamant to avoid any policy changes which would ‘threaten the institutions most crucial to the compet-
itive advantage their firms enjoy’ (Ibid.: 52). This strong emphasis on the preservation of the competitive advantage of firms may not reflect the full complexity of the real motives behind economic policy-making. Yet it correctly identifies a predominant feature in setting economic policy priorities under the conditions of the post-war system of the Washington consensus. Political considerations such as working conditions, social equality and environmental sustainability were hence largely subordinate to the priority of reducing the regulatory burden for businesses. The European Union (EU) as an organisation has not been immune towards this trend. Instead of following its official rhetoric and adopting the role of a guardian of national welfare state cultures, it has predominantly taken on the role of an economic liberaliser (Hancké et al. 2007). From the national perspective the EU is hence perceived as a force which encourages institutional change towards market liberalisation and the relaxation of regulatory standards for businesses and financial services. At least up until the global financial crisis of 2008–2009, Brussels also principally opposed Keynesian policies like national subsidies and economic stimulus programmes. In the face of a deepening crisis in the eurozone this has changed to a certain degree. Ironically the EU Commission and the European Central Bank (ECB) are now advocating more interventionist policies than some of the leading member states, predominantly Germany and the UK, would like to see.

The original VoC approach of Hall and Soskice has undergone fundamental scrutiny from academic scholars across different disciplines. Its weaknesses but also its strengths in offering a framework of analysis for the changes in contemporary capitalist economies have been outlined in a number of critical publications (most prominently in Allen 2004; Hancké 2009; Hancké et al. 2007; Morgan et al. 2005; Streeck and Thelen 2005) but also by Hall and Soskice themselves in response to their critics (Hall and Soskice 2003).

Whilst taking into account the discussions which have taken place previously, in this book I want to apply the VoC approach in the light of unprecedented circumstances. In the past five years the foundations of the global economy were shaken to the core by the most fundamental crisis since the Great Depression of the 1930s. The crisis emerged primarily as a result of the instability in global financial markets, first in the US and subsequently as a ripple effect on the European continent. It has uncovered fundamental flaws in the regulatory practices of the banking industries and deepened the structural budgetary problems which had previously existed in many countries. The result is a vicious circle of low growth and rising unemployment in a number of eurozone countries. It is made worse by the need to impose noticeable cuts to public spending in the crisis economies, in particular in Southern Europe.
This unprecedented situation confronts scholars across disciplines with a profound challenge to adapt existing frameworks for the analysis of differences in national political economies. Modern capitalist economies have been in a process of constant development and are becoming ever more complex. This is the result of the increasing transparency of national borders in the era of globalisation and the advance of global communication technology which is especially important for business and financial transactions. Analysts of national political economies have therefore in recent years concentrated on examining if and under which conditions institutional change takes place. From the very influential historical institutionalist perspective, which advocates path-dependency, national elites tend to be socialised by their domestic institutional setting and are therefore reluctant to pursue a radical departure from its rules and procedures. The expectation that the continuation along the established national institutional path will lead to secure permanent successful outcomes (‘increasing returns’) is at the heart of this concept. If changes occur, they tend to be the result of substantial external pressures or ‘exogenous shocks’. These are based on the rational consideration of domestic elites that a continuation along the established path is no longer the best option to pursue (Pierson 2000: 266). This perspective is shared by the VoC approach, which has a strong institutionalist bias. VoC also shares the view of historical institutionalists that, in response to fundamental shocks, domestic actors will try to increase the efficiency of institutions and processes. The purpose of this is to enable them to deal with the challenge rather than to fundamentally alter the existing institutional framework. Radical policy adjustment is therefore more likely than fundamental institutional overhaul (Pierson 2000: 259). Key domestic actors, such as companies, stakeholders and policy-makers are likely to look towards finding new ways of efficient interaction within the existing institutional structures of their domestic economy (Hall and Soskice 2001: 63). This perspective has indeed turned out to be far more accurate than the notion of global economic convergence which many economists considered to be an inevitable result of the increasing interdependence of national economies. Before the recent global financial crisis the discussion on convergence vs continuing variety concentrated predominantly on the German model which VoC classified as the classic example of a coordinated economy (Morgan 2005: 6). The question for many scholars in this respect was if the institutional culture of the German economy with its emphasis on widespread consultation amongst a multiplicity of actors across different levels would be unable to withstand competition with liberal models without abandoning core elements of its established industrial relations system (collective bargaining, industry-wide general wage agreements and the principle of co-decision
and solidarity between employers and workers) (Streeck and Yamamura 2003). The substantial reforms of the German employment system introduced in 2003 in response to spiralling levels of unemployment, which are discussed in Chapter 5 in this book, led many to believe that they would be the first phase in an inevitable move towards the further liberalisation of the German economy. The impact of the reforms on the institutional core of Germany’s market economy continues to be subject of the German domestic political debate. After the introduction of the reforms public opinion in Germany started to become increasingly uneasy with the notion of imposing further institutional changes and prominently rejected the radical liberalisation programme the Christian Democrats (CDU) had proposed during the 2005 general election campaign. The majority of the mainstream political elite in Germany, with the exception of the neoliberal Free Democratic Party (FDP), has refrained from advocating further institutional change. The fact that the global financial crisis has unveiled the strong dependence of liberal models on financial markets as a substantial weakness and the surprisingly strong German economic performance during the crisis has furthered dampened calls for further institutional reforms in Germany. The core of the German employment model has certainly been liberalised as a result of the Hartz labour market reforms. They instilled the Anglo-Saxon principle of welfare-to-work into the German economy and therefore essentially abandoned the traditional post-war principle of life standard guarantee for the unemployed through high wage replacement rates (Kemmerling and Bruttel 2006). Equally the German economy has witnessed substantial changes in two other areas: first, the traditional link between companies and individual commercial ‘house’ banks has been weakened in favour of the greater reliance on stock market capitalisation and the introduction of the principle of ‘shareholder value’. Most analysts agree however that this change has taken place within the existing coordinative setting and consequently enhanced worker participation by enabling them to buy shares while also not having undermined the general consensual approach of German corporations (Deeg 2005; Hancké and Goyer 2005; Vitols 2003). Second, the increasing flexibilisation and decentralisation of wage-setting in Germany, mainly as a result of the creation of many jobs in the low-wage sector, has altered Germany’s formerly rigid system of collective bargaining (Bosch 2008). The cooperative climate in which employers and trade unions have negotiated consensual solutions on wage levels and shorter working hours during times of crisis nevertheless shows that the traditional industrial patterns in Germany continue to prevail (Funk 2007). The particularities of the German economy, which neoliberal sceptics had branded as hurdles towards global competitiveness, have turned out to be Germany’s competitive advantage. Its
consensus-orientated industrial relations system, the strong focus on high quality manufacturing export goods and a much lesser dependence on the financial markets than its liberal counterparts, have allowed Germany to evolve from the crisis relatively unscathed and ultimately once again as the leading economic force in Europe.

In this book I will concentrate on two aspects which I consider to be the main weaknesses in the traditional VoC approach that were revealed by the recent global financial crisis. First, as was outlined in a number of critical accounts, Hall and Soskice underestimated the role the state plays in sustaining economies during fundamental crisis periods. Second, the VoC approach is too focused on companies and therefore ignores the increasingly crucial and frequently destabilising role of financial markets.

I will now address each of these points individually. The financial crisis has substantially shifted the debate on economic policy-making. In recent years it was both intellectually and practically focused on minimising state intervention and advocating shareholder value as a principle which would eventually lead towards the increasing liberalisation of coordinated economies. Here critical accounts of the VoC approach have rightly emphasised its relatively narrow categorisation and its neglect of the variety of different state traditions. Amable (2003) made an attempt to fine-tune the dual typology of VoC by dividing the coordinated model into further groups. Her approach builds on a more fine-tuned categorisation of capitalist typologies like Esping-Andersen's classic welfare state 'regime clusters', which distinguishes between corporatist and social democratic clusters of welfare regime (Esping-Andersen 1989). Amable’s differentiation of the VoC coordinated model into continental European, Mediterranean and social democratic economies takes into account the different traditions of the state in these economies. The level of state intervention in the economy increases with each category. In the continental European model the state predominantly adopts the role of a supervisor of economic activity to ensure that established rules (for example collective bargaining in industrial relations) are adhered to by all actors. In the Mediterranean model the state plays a stronger role when it comes to regulating the labour market and industrial relations but is less involved in the provision of welfare, which was traditionally a dominion of the family and the church. The social democratic model, as it predominantly exists in Scandinavian countries, on the contrary accepts a strong role for the state as the guardian against market forces and the provider of strong quality services, high levels of welfare provision and public sector employment. The challenge for many scholars continues to be how to fit in the countries in Central and Eastern Europe (CEE), which were for some time simply subsumed under a transition model category. More detailed studies such as Lane and Myant
(2007) have shown that countries in this region have developed a variety of different economic and welfare cultures. Some have been transformed towards the liberal typology and others towards coordinated varieties.

The importance of the state in determining the future of individual economic models is therefore undisputed. The VoC approach acknowledges the state as one element which makes up the institutional particularities of an economy but it tends to underestimate the importance of the state in stabilising and sustaining economic activity, particularly at times of crisis. The state is therefore more than just one of the actors in the coordinative arrangements of an economy. It has maintained far greater autonomy to determine the parameters of a national economy than followers of the functionalist paradigm (such as the VoC) had wanted to concede. The functionalist notion that ‘politics follows economics’ (Hancké et al. 2007: 23–24) remains valid to a certain degree when one analyses the recent developments in capitalist economies around the world, particularly in Europe. The perception that the separation between the public and economic interests would become increasingly blurred in the process of economic globalisation has nevertheless turned out to be flawed. It is certainly true that, as a result of the ongoing crisis symptoms in many economies in Europe, economic issues tend to dominate the political agenda to an increasing extent. A comprehensive analysis can however not ignore the fact that globalisation has not pushed different economic models towards a high level of convergence. It is now the established consensus that the globalisation convergence theory which assumed the emergence of a best practice liberal economic model was flawed. Instead many scholars have pointed out that each economic model has responded to the challenges of globalisation in a different way and on the basis of its particular institutional background (Crouch 2005; Hall and Gingerich 2009; Hay 2000). In this respect it is highlighted that even though the principle of ‘shareholder value’ has started to infiltrate coordinated economies, it has not necessarily lead to a complete shake-up of their institutional foundations. Instead, established corporate actors have managed to integrate the principle into their existing institutional practices. Even the reforms in national employment systems, like in the case of Germany, have not completely changed the coordinative institutional core of these economies (Hall and Thelen 2009).

It would also be wrong to assume that has managed to eradicate a political and social agenda which goes beyond facilitating market interaction and enhancing profit-orientated business opportunities for the purpose of stimulating growth. States remain responsible for the overall well-being of their citizens. The elected representatives of the state consequently have to look beyond the pure market interest. It consequently makes sense to consider the ‘state and the mode of business coordination as analytically inde-
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...ependent properties of any given model of capitalism’ (Hancké et al. 2007: 24). Hall and Soskice’s original approach fails to differentiate between the market and the wider societal interests. This weakness was highlighted by Bruff who argues that the VoC approach fails to adequately acknowledge the domestic social foundations of the national institutional VoC (Bruff 2008 and 2011). Hall and Soskice also tend to accept the predominant view of neoclassical economics that institutions in the national context are shaped by market interests (Crouch 2005: 80). Institutions which do not follow this logic are consequently supposed to be fundamentally altered or even replaced on the basis of a best practice selection of institutional success. These are usually those institutions which support economic competitiveness on the basis of reducing investment and transaction costs for businesses (Barro and Sala-i-Martin 1992; Parker 1998).

The globalisation convergence advocates however also acknowledging that a powerful external shock like a major economic crisis would most likely stall this process (Lane 2005: 105). This is where the importance of the recent global financial crisis comes in. I argue that the crisis has fundamentally shaken the established perception of the role of the state in modern capitalist economies. The globalisation debate failed to establish a consensus on determining to what extent state actors are able to maintain their independence under the conditions of global market interaction. The emerging trend in the field of political economy before the crisis was that active state intervention in the economy in the form of Keynesian demand management and the imposition of regulatory burdens on businesses and markets would be a thing of the past. Instead new concepts of the state as facilitator in the area of employment, welfare and education started to emerge, most prominently advocated by Giddens (1998) as the ‘Third Way’ economic philosophy to be positioned between the classic neoliberal and leftist Keynesian approaches. It was subsequently adopted by reformed centre-left parties in the 1990s, which branded themselves as modern Social Democrats, such as Bill Clinton’s New Democrats in the US and Tony Blair’s New Labour Party in the United Kingdom. The ‘Third Way’ argued for an economic approach without ideological bias, which could combine economic liberalism and social cohesion by limiting the role of the state to that of a facilitator of economic activity. The emphasis was hence on removing regulatory burdens for businesses and markets and making labour markets more flexible through the introduction of a welfare-to-work approach. The latter gives incentives to take up employment or at least education and training opportunities and penalises individuals who remain economically inactive. The ‘Third Way’ approach was actively promoted at the EU level, especially by the British New Labour government in the run-up to the 2005 revision of the Lisbon Strategy. The Third Way
became the basis for a reformed social model, which was to be grounded in a strategy of decentralisation and diversification. In this respect Giddens differentiated the European social model from the liberal model of the US economy by promoting the development of what he called the ‘social investment state’ (Giddens 2006: 32). In contrast to the US, the state would remain active but concentrate its activities more towards human capital by transferring risk from the welfare state towards the individual. Crucial for this was the promotion of education and learning and the pursuit of an overall strategy which is predominantly orientated towards stimulating economic growth and job creation. This led to the development of a ‘flexicurity’ strategy for the reform of labour markets which borrowed heavily from the active labour market policy approach in Scandinavian countries like Sweden. The principle combines labour market flexibility with a new form of security. It is aimed at reducing passive welfare support in favour of introducing targeted activation through education and training programmes for the unemployment with the overall purpose of ensuring that they get back into work and are equipped to find a new job quickly (Funk 2008: 357). ‘Flexicurity’ was the core principle of the labour market and welfare state reforms which the British New Labour government and the German Social Democrats introduced between 1997 and 2003 (Schweiger 2010). As is outlined in greater detail in Chapter 2 in this book, during the run-up to the revision of the Lisbon Strategy in 2005 the British government was very active in promoting this principle successfully against the background of successive years of record domestic levels of economic growth and employment. The result was the emphasis on economic growth and jobs as the new priorities for the revised Lisbon Strategy. Subsequently and even before the effects of the US financial crisis on European economies could really be felt, the debate in the EU switched towards a more critical approach to the Lisbon Strategy and the flexicurity principle.

This was the result of rising inequality and poverty levels even in countries such as the UK, Ireland and Germany) that had actively implemented the flexicurity principle through welfare cuts and increased pressure on individuals to take up work.

The crisis has created a situation where the centrality of the state for the survival of national economies suddenly resurfaced. Ironically it hit those countries in Europe hardest who had rolled back state influence the most. The emerging dramatic flaws in the British and Irish banking industries led to a previously unimaginable level of state interference in the sector in 2007–2008. The governments in London and Dublin invested record amounts of taxpayers’ money to stabilise failing banks and effectively nationalised or part-nationalised substantial sections of their banking industry in an attempt to avoid a complete meltdown of a crucial pillar of
their economies. The sudden emergence of the state as a safety net for a failing industry which for many years had provided the backbone for the good performance of the British and Irish economies raises doubts on the sustainability of the liberal model's foundations. An increasing number of critical accounts of the three former liberal role model economies of the US, the UK and Ireland have outlined the shaky foundations upon which their growth and jobs miracle was built in the 1990s and early 2000s (Gamble 2009; Hutton 2011; O'Toole 2010; Ross 2010; Stiglitz 2010). Most of all they highlight how a blind trust in markets and a profound scepticism towards government interference in the economy caused a situation where the financial sector was allowed to get away with reckless and unsubstantiated lending in the form of subprime mortgages. This was strengthened by an EU strategy which essentially amounted to negative integration: forcing national governments to gradually remove regulatory barriers to competition in more and more sectors of their economy and in particular encouraging them to look towards the liberalisation of the services and the financial industry. Although the EU Commission led by José Manuel Barroso frequently emphasised the differences between the reformed European social model and US-style capitalism, it is obvious that the Lisbon Strategy initiated developments which made it difficult for countries to maintain what Hutton defines as the essential feature of the distinctive European social model: the role of the state as a guardian of citizens against the excesses of market competition. For Hutton this amounts to the notion ‘that all citizens should have an equal right to participate in economic and social life, and that the state is more than a safety net of last resort: it is the fundamental vehicle for the delivery of this equality’ (Hutton 2002: 63).

The idea that the state should guarantee social citizenship is connected to the notion of the existence of a public space which is protected from the realm of market competition. Rather than being pushed to the sidelines the state has a crucial role to play as a provider of public services. In addition the state is called on as an established mediator in industrial relations who ensures the adequate protection of workers through regulations such as co-decision, working time directives, a minimum wage and the provision of benefits in case of unemployment. This amounts to economic citizenship (Teague 1999: 12). Through its emphasis on market competition and deregulation the EU strategies therefore encouraged European economies with a pronounced state culture to transform themselves towards the liberal model. Combined with the budgetary restraints which were supposed to be introduced under the Stability and Growth Pact (SGP) for eurozone members, the EU hence was set on course to ‘mute into little more than a charter of economic liberalization and marketization’ (Hay 2000: 528).
The VoC approach has uncritically accompanied this trend by following a logic which portrays liberal economies as better equipped for the challenges of a globalised economy because of their orientation towards the services sector and their openness towards transnational capital flows. This is because coordinated economies tend to display what Hall and Soskice consider to be an ‘adjustment problem’ (Hall and Soskice 2001: 65) in failing to respond swiftly to new internal and external challenges. While Hall and Soskice acknowledge that ‘markets do not necessarily generate superior outcome’ (Ibid.: 65), it is clear that they consider the VoC in more market-orientated liberal models to be advantageous. Crouch goes as far as to argue that Hall and Soskice follow the logic of neoclassical economics which considers any non-market institution as potentially not viable for the long term under the conditions of globalisation (Crouch 2009: 80). I would argue that VoC does not offer a fine-tuned analysis on the differences in state cultures across Europe, which are subsumed under the firm-based liberal-coordinated dichotomy. This is a profound weakness of the approach which fortunately has in the meantime been addressed by a number of scholars. It is especially problematic when one applies the VoC approach to the analysis of the political economy of the EU. In order to understand the internal divisions between member states it is essential to refer back to the differences in national state cultures. Siedentop (2000) outlined this in his seminal work on the foundation of democracy in Europe. He argues that the EU supranational institutional framework was essentially built on the tradition of the French state which favours centralisation with little transparency and check and balances. From Siedentop’s perspective this explains why other member states with a more restrained state culture, especially the UK, have been struggling to integrate into what is essentially a French institutionalised design (Siedentop 2000: 105–107). The financial crisis and the subsequent sovereign debt crisis have once again re-emphasised the importance of differences in national state cultures in Europe. The eurozone crisis has opened up an obvious divide between those countries who favour austerity, monetary stability and central bank independence and others who are reluctant to abandon the notion of the role of the state as a generous provider of public employment and welfare benefits. At the same time we are witnessing a divide between member states who call for a move towards deeper political and economic integration and others who are profoundly sceptical of further integration and want to set a clear end point to further integration and are even calling for the renationalisation of powers. The advocates of deeper integration are countries which have experience with the division powers between the centre and periphery in a federal system. Examples for this are Germany, Italy, Austria, Spain and to a certain extent also Luxembourg.
with its system of consensual multi-party government. On the other side of the divide are countries with more unitary political systems that put great emphasis on preserving their national sovereignty over key strategic policies. In the latter category the United Kingdom and the Czech Republic are currently the most ardent defenders of their national sovereignty. These differences in state tradition are crucial to understand how the global financial crisis has affected the VoC in Europe. They also provide the background to the dynamics between national and supranational policy responses to the crisis. The crisis in the eurozone illustrates once again that it was a mistake for Hall and Soskice to neglect the differences in national state traditions, particularly when it comes to introducing a more fine-tuned differentiation between different state cultures within the coordinated typology. Lallement (2011) emphasises this point in his study which attempts to identify the effects on labour markets in different economies in Europe. He emphasises the need to go beyond Hall and Soskice’s positioning of a group of predominantly Southern European economies (France, Italy, Spain, Portugal, Greece and Turkey) somewhere between the liberal and the coordinated dichotomy and argues that they should instead clearly be determined as a Mediterranean model. This model has the following characteristics: a key role is assigned to the state, the level of social protection is substantially higher than in coordinated economies, even than in Scandinavian countries, but is not predominantly provided by the state. Education and training systems are weak, levels of labour market participation low, particularly amongst young people. The banking sector plays a key role as a lender to companies and individuals. Lallement identifies the reinforcement of inequalities as the most characteristic effect of the crisis on these economies (Lallement 2011: 637–638).

The crisis has accentuated the differences between the Mediterranean and the coordinated group. This is most prominently represented by the clash over policy solutions between Germany and Greece but to a certain extent also between Germany and France over the introduction of eurobonds and the role of the ECB, especially since the election of the Socialist French President François Hollande in 2012.

This leads us directly to the second essential weakness of the VoC approach. The second and probably most devastating global economic crisis in the history of the advanced modern economy had its origins in the financial sector. As the crisis deepens at the regional level in Europe it becomes obvious that national economies are increasingly at the mercy of market forces. Policy-makers have for decades pursued deregulatory policies towards the financial industry on the national as well as the supranational regional and global level. This was part of a neoliberal ‘financialisation’ strategy which was aimed at promoting the radical overhaul of economic
activity towards financial speculation and large-scale borrowing for businesses and consumers (Gamble 2009: 78). Hall and Soskice concentrate predominantly on the manufacturing industry and consequently underestimate the importance of the financial sector’s growing influence in what can be classified as an era of financial deregulation. They see the danger that ‘financial deregulation could be the string that unravels coordinated market economies’ (Hall and Soskice 2001: 64) but offer no critical perspective on the tendency towards the deregulation of the financial sector in liberal economic models. The financial crisis has made obvious that financial markets have acquired substantial powers in the globalised economy. This turned out to be the root of the problems which led to the 2008–2009 global financial crisis. The crisis illustrated to what extent both companies and governments have become increasingly dependent on financial markets as a source for funding. Financial markets have therefore moved into a position where their rating of a company’s or even a whole economy’s viability has profound implications for their long-term stability. As a result of a growing number of companies across the globe depending on financial markets, the latter are able to force companies to become more profit and budget-orientated and to pursue a shareholder-value strategy (Amable 2003: 28). In addition, they have also strengthened their position in the domestic process of determining economic policy strategies (Hancké et al. 2007: 28).

Policy-makers in the EU are consequently facing a profound struggle to reimpose political control over a largely market-driven economic agenda. Instead they tend to be trapped in a constant process of attempting to reinstit the trust of financial market operators in the viability of individual economies (currently especially Cyprus, Greece, Italy, Portugal and Spain) and the single European currency in general. The ongoing market speculation against the euro and individual countries on the government bond and the credit default swap markets has not only put the membership of the crisis countries but even the future viability of the whole of the eurozone in jeopardy. This unprecedented situation where ‘the financial system was rescued by state intervention, only to turn and bite its rescuer’ (Lapavitsas et al. 2011: 58) is to a large extent the result of the hesitation of political leaders to fundamentally shake up the regulatory foundations of the global economy. In spite of the profound flaws which were uncovered by the financial crisis the global economy continues to be based on the twentieth century ideology of market dominance and small government (Stiglitz 2010: 207). Under these conditions a firm-centred approach such as the one promoted by the VoC is no longer sufficient to explain the new complexity of economic policy-making in Europe. The argument that companies are essentially the central actors in modern economies has been made superfluous by the new crisis conditions. The focus of economic
policy-making is consequently moving on from the agenda of the 1990s and early 2000s, when its predominant focus had been the creation of a business-friendly environment. The budgetary crisis in many economies and the resulting nervous market reactions, have led to the imposition of profound austerity programmes. Political elites seem to be driven by the fear that without these policies the long-term prospects for economic and particularly fiscal recovery may be severely undermined by adverse market speculation. They are therefore determined to pursue the austerity strategy against fierce domestic opposition and in spite of the risk it poses for the fabric of societies in Europe.

As political elites in the EU and particularly in the eurozone realise that their national competitive advantage is strongly interlinked with the overall success of the Single Market and the eurozone, they are also focusing more on the implementation of effective supranational policy solutions. This is especially obvious when one considers the emerging EU policy mechanisms in response to the crisis. In the third chapter of this book I therefore argue that the new policy mechanisms are the result of a new wave of functionalist spillover where the external crisis conditions force governments to transfer more of their national authority in the area of economic policy-making to the supranational level than they would be willing to concede under normal circumstances. The crisis is hence leading to the emergence of new set of multiple layers of policies which go substantially beyond the coordinative mechanisms of the open method of coordination (OMC). The OMC had been the EU’s preferred mechanism for more than a decade before the crisis. Examples for this are the annual European Semester policy mechanism under the Europe 2020 Strategy, the Euro Summit, the newly established European Stability Mechanism (ESM) and to a certain extent even the European System of Financial Supervision (ESFS). The details of the regulatory response to the crisis are discussed in Chapter 2 in this book. Chapter 3 deals with the political implications of the emergence of an increasingly complex set of functionalist policy initiatives which essentially divide the EU into multiple core groups with different levels of integration. The emerging division of the EU membership is essentially based on the horizontal division between eurozone insiders and outsiders and the deepening of vertical integration in the eurozone core with the potential aim of moving towards a political union. The countries outside the eurozone are hence either semi-detached or only very loosely connected to the euro core through the Europe 2020 annual cycle of policy coordination, which applies to all 28 member states.

In spite of its limitations I use the VoC approach as a basic framework for the analysis of the changes in European economies under unprecedented crisis conditions, which is presented in this book. As outlined
earlier, I argue that VoC puts too much emphasis on the role of companies and neglects the political dimension of economies. At the same time it pursues essentially an institutionalist perspective. Hall and Soskice correctly assume that change in response to new challenges is most likely to be dependent on the culture within the established institutional coordinative framework. This allows for more radical innovation in liberal market economies and rather incremental and modest change in coordinated economies (Hall and Soskice 2001: 38–39). The perspective that the national institutional setting of an economy determines its competitive advantage and consequently profoundly shapes the behaviour of domestic actors remains crucial to the understanding of the dynamics of institutional and policy development in the EU. This is even more so the case under the new set of circumstances European governments currently face. The crisis has shown us that even in the face of the most adverse external circumstances institutional particularities of individual economies tend to persist. I therefore follow the basic VoC hypothesis that ‘the distinctions central to the varieties of capitalism perspective are likely to be of continuing value’ (Hall and Gingerich 2009: 169). Since the emergence of the financial crisis the national and EU level discussions on the reform of policies and institutions have been characterised by a diversity of perspectives. All of these are nevertheless deeply rooted in the national institutional cultures of member states. A more active role for the ECB in supporting economies with budgetary problems, the introduction of a national or an EU-wide financial transaction tax, the reform of the eurozone SGP and more recent proposals from the five largest member states (Germany, France, Italy, Spain and Poland) and others for deeper political integration, including integrated financial, budgetary and economic policies (Future of Europe Group 2012) therefore continue to be hotly debated. It is therefore necessary to adapt the VoC approach to the current crisis conditions. They are likely to substantially change the direction of economic and political integration in the EU and will leave a lasting imprint on the national VoC in Europe.

The scope of this book is to offer an analysis of the emerging post-crisis VoC in Europe. It is certainly problematic to speak of a post-crisis situation when the economic and budgetary situation in a number of countries in the EU continues to be fundamentally grave. Given the volatility of events, it is likely that at this stage it is only possible to offer a snapshot of the full extent of the changes which national economies and the EU Single Market as a whole are still likely to be subjected to. Due to the profound nature of the changes that occur it is nevertheless essential to offer a new perspective on the existing categorisation of national capitalisms in Europe. Here the analysis needs to concentrate on the extent to which national institutional cultures continue to determine the preferences of policy-makers and
stakeholders and how these in turn influence the shape of supranational EU policies. The particularities of national institutional infrastructures and economic cultures continue and have not been eradicated by the external pressures of globalisation (Hall and Soskice 2001: 57). Even the severity of the pressures following the financial crisis has not pushed economies towards uniform transformation. Instead we witness a process where domestic elites are adamant to defend what they perceive as their national competitive economic advantage. Even in economies where the crisis has revealed that the existing institutional status quo is detrimental to economic recovery, the domestic resistance against change remains substantial.

On the EU level itself we are witnessing a surprisingly strong resistance towards finding common solutions to the crisis. It is therefore obvious that the EU remains based on a strong intergovernmentalist fundament. In practice this means that beyond the official rhetoric member state governments are adamant to remain in control of strategic policy-making (Pollack et al. 2010: 487) and are especially defensive over policy issues which are contentious with voters (Hix and Hoyland 2011: 335). This clashes with the realisation that the creation of a single European currency demands deeper integration of national economic policies beyond the harmonisation of interest rates. This essentially follows the functionalist logic that economic integration will inevitably be followed by deeper political integration. The persisting differences in national economic cultures make it hard for political elites to agree to the further transfer of national sovereignty towards the EU institutional level without the risk of losing the support of their electorate. To argue that the effective resolution of the crisis demands more and not less European integration is currently not very popular with citizens across Europe. The public debate tends to associate proposals to deepen integration with the creation of a transfer union and the sharing of risk in the eurozone. The latest Eurobarometer poll on the effects of the crisis shows that only 22 per cent of citizens across the EU-27 considered the EU to be best placed to ‘take effective actions against the effects of the financial and economic crisis’ (European Commission 2013: 27). The rest favoured either national governments (21 per cent) or other global organisations such as the G20 (13 per cent), the International Monetary Fund (IMF) (13 per cent) and even the US government (8 per cent). Overall trust in the EU has also fallen sharply recently with only 31 per cent of citizens across the EU-27 expressing the view that they have trust in the EU and its institutions (Ibid.: 27).

Large varieties between citizens in different member states persist when it comes to the level of acceptance of EU institutions and the proposals to deepen integration. It may therefore be inevitable that the EU becomes divided into a core eurozone group of countries who move towards full
political and economic union, while a smaller group of countries deliberately decide to stay on the sidelines and may even decide to repatriate core powers to the national level. This current division remains highly volatile and is likely to change in the future. This will not only be the result of further countries joining the eurozone. The opposition against the German plans to push the eurozone towards deeper political integration on the basis of a rigid system of monitoring of national macroeconomic and budgetary policies is already substantial. These concerns are likely to grow further once national governments realise the full impact of the proposals for deeper political union for the autonomy of their national policies. It is hence a realistic possibility that more countries both inside and outside the eurozone will decide to opt out of future treaty changes, which are designed to deepen integration.

The emerging vertical and horizontal divisions in the EU in the aftermath of the global financial crisis support the VoC notion that countries concentrate on developing strategies to defend their national competitive economic advantage and that these strategies are fundamentally shaped by their domestic institutional setting. VoC therefore remains prominent in the debate on the future of political and economic integration. The crisis has however also shown that even against the background of a persistence of national interests in the EU, the neofunctionalist concept which assumes that economic integration inevitably leads towards deeper political integration, essentially remains valid. The initial refusal of member states to accompany monetary integration with deeper political integration to ensure the effective coordination of fiscal and macroeconomic policies has turned out to be the fundamental flaw in the design of the eurozone. The deepening of political integration is now emerging as a bitter but arguably inevitable pill which eurozone countries will have to swallow to ensure that the single currency has a long-term future. This is the background upon which the EU institutional and policy changes under crisis conditions are discussed in the second and third chapters in this book.

REFERENCES


