The International Competitiveness Of the Small European State in the 1980s: Denmark, Ireland, Sweden, and Switzerland

by

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Submitted for the Ph.D. Degree
in the
Department of International Relations
at
The London School of Economics

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To my mother and father,
for having given so much

Abstract

This thesis tests the hypothesis that the degree of international competitiveness of the small European state in the 1980s resulted from its unique internal process of interaction derived from its industrial culture, developed from state priorities and societal values. Small European states, because of their position as international price takers, controlling relatively few product markets, were forced to rely on various forms of domestic intervention, such as monetary, labour market, and industrial policies, to stimulate international competitiveness. A systematised dialogue and communication process among internal economic actors due to geographic proximity and consequent actor familiarity was the small European state's competitive advantage necessary to compete for world markets against larger states possessing both natural and human resource advantages. The more systematised the internal interactive process was, however, the more flexible the internationally vulnerable small European state would be to respond to changing global political and economic conditions.

In cases such as Sweden and Switzerland, the small European state was able to fashion this process of interaction into a system, where peak associations were able to communicate effectively to preserve a flexible industrial environment and where the principal actor maintained a key role in directing the national economy. The economic success of Sweden throughout the 1980s was facilitated by the trade unions, while in Switzerland the economy was guided by its financial institutions. Because of these principal actors, both states were highly independent, having developed oligopolised, high technology oriented industrial structures that featured powerful multinational corporations.

However, during the 1980s, in small European states such as Denmark and Ireland, with weak industrial structures, high levels of international dependence on the European Community, and poor economic performances, confused consultation processes bred incoherent policy-making that resulted in low levels of international competitiveness. In both states, the State as the principal actor attempted to facilitate industrial adjustment, aspiring to modernise their relatively weak indigenous industrial structures.

The thesis examines actor relations and policy-making in three functional areas: finance-industry relations and monetary policies; trade union-industry relations and supportive labour market policies; and state-industry relations and industrial policies. Given the myriad of policies that small state policy-makers employed during the 1980s, the thesis argues and illustrates that small European state interventionism was both state-specific and necessary because of the pressures of the world market.

Acknowledgements

This thesis was completed under the guidance of Michael Hodges of the Department of International Relations at the London School of Economics. I would like to thank him not only for his active role as my thesis supervisor, but also for his patience and encouragement. I owe him a special debt of gratitude for having assumed the role of my supervisor two years into my research, for helping to focus my energies, and for providing meaningful intellectual support. I also wish to express my appreciation to Professor Emeritus Susan Strange, my supervisor during the first two years at the LSE, who retired in 1988; Gautam Sen, who was kind enough to read numerous drafts during the initial stages of my research and who was instrumental in helping unravel many difficult definitions and questions of interpretation; and Roger Tooze, who clarified many of the vital theoretical underpinnings of this thesis.

In order to gain a first-hand perspective of the economic, political, and social conditions of the four small European states examined in this thesis, over one hundred interviews were conducted in the major cities of these countries. I would like to express my appreciation to Mr. Albert Gallatin, who facilitated the interview process, as well as those persons listed at the end of the thesis.

I would also like to acknowledge a select few individuals who made the research and writing of the thesis much easier: Coy Bennett and Wayne Connaway, who provided significant graphics services; Albert Moncrieff, who helped track down some vital statistics and information; Barbara Moreland Gee, who helped edit the manuscript; and Steve Campbell and Bob Goodman, both of whom were kind enough to provide much appreciated office space. I owe a special debt of gratitude to Wanda Ruddick, whose unfailing administrative support and consistent willingness to help never went unnoticed or unappreciated.

Most importantly, this thesis would never have been completed without the understanding of my parents and sister, who supported and encouraged me with remarkable patience. In particular, I wish to express my gratitude to my father, Dr. Sanford R. Singer, for his support, counsel, and inspiration. He furnished every imaginable resource, provided assistance on the most tedious of tasks, and read every draft of each chapter with the trained eye of both businessman and scholar. During the course of writing the thesis he was always available, both as a colleague ready to act as a sounding board for ideas and as a sympathetic, understanding friend.

M.E.S.
November, 1989

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Acronyms

AIB	Allied Irish Banks
ASM	*Association Suisse des Machines et Metaux* (Employers' Association of the Swiss Engineering and Metalworking Industrialists)
ATP	*Allman Tillaggspension* (Swedish Supplementary Pension Programme)
BOI	Bank of Ireland
CAP	Common Agricultural Policy
CIF	Irish Construction Industry Federation
CII	Confederation of Irish Industries
CNG	*Christlich-Nationaler Gewerkschaftsbund der Schweiz* (Swiss National Federation of Christian Trade Unions)
CVP	*Christlichdemokratische Volkspartei* (Swiss Christian Democratic People's Party)
DA	*Dansk Arbejdsgiverforening* (Confederation of Danish Employers' Associations)
D.Kr.	Danish Kronor
EC	European Community
EKN	*Exportkreditnamnden* (Swedish State-supported export credit guarantee system)
EFTA	European Free Trade Association
EMS	European Monetary System
ERG	*Garantie Contre Les Risques a l'Exportation* (Swiss export credit guarantee system)
FDI	Foreign Direct Investment
FDP	*Freisinnig-demokratische Partei* (Swiss Radical Democratic party)
FTF	*Funktionaerernes og Tjenestemaendenes Faellesrad* (Danish Confederation of Salaried Workers)
FUE	Irish Federated Union of Employers
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GFSW	*Gesellschaft Zur Forderung der Schweizerischen Wirtschaft* (Society for the Development of the Swiss Economy)
GNP	Gross National Product
ICTU	Irish Confederation of Trade Unions
IDA	Industrial Development Authority of Ireland
IFSC	Irish International Financial Services Centre
IMF	International Monetary Fund
Ir.Pd.	Irish Pounds
LO	*Landsorganisation i Danmark, Landsorganisationen i Sverige* (Danish, Swedish Confederation of Trade Unions)
LMB	Swedish Labour Market Board (*Arbetsmarknadsstyrelsen*)

MNC	Multinational Corporation
NATO	North Atlantic Treaty Organisation
NESC	Irish National Economic and Social Council
NIC	Newly Industrialising Country
NU	Irish (wage) National Understanding
OECD	Organisation for Co-operation and Development
OMA	Orderly Marketing Arrangement
OSEC	*Office Suisse d'Expansion Commerciale* (Swiss Office for Commercial Expansion)
R&D	Research and Development
SACO/SR	*Centralorganisationen Sveriges Akedimekers Centralorganisationentatsjanstemannens Rifsforbundet* (Swedish Confederation of Professional Associations/Federation of Civil Servants)
SAF	*Svenska Arbetsgivarforeningen* (Swedish Employers' Confederation)
SAP	*Sveriges Socialdemokratiska Arbetarepartiet* (Swedish Social Democratic Party)
SAS	Scandinavian Airline Systems
SBA	Swiss Bankers Association
SBP	Scandinavian Banking Partners
SEK	*AB Svensk Exportkredit* (Swedish export credit private/public agency)
S.Fr.	Swiss Francs
SGB	*Schweizerischer Gewerkschaftsbund* (Swiss Federation of Trade Unions)
S.Kr.	Swedish Kronor
SNB	*Schweizerischer Nationalbank* (Swiss National Bank)
SSIC	Societe Suisse des Industries Chimiques (Swiss Society of Chemical Industries)
SSIH	*Societe Suisse Pour L'Industrie Horlogere* (Swiss Watch Corporation)
TCO	*Tjanstemannens Centralorganisation* (Swedish Central Organisation of Salaried Workers)
UN	United Nations
VER	Voluntary Export Restraint

Chapter One
The Small European State International Competitiveness Process

1.1 Introduction and Methodology

This thesis will examine the political-economic performance of Denmark, Ireland, Sweden, and Switzerland from 1980-1987, using a chapter-by-chapter comparative approach, as opposed to separate state studies. It will draw upon the lessons of the past literature of small states operating in foreign markets. The evidence used to compare the case studies includes primary documents and personal interviews in each of the four countries with representatives from important ministries, trade unions, employers' confederations, industrial associations, financial institutions, universities, and research institutions. (*See interview listings after Chapter Six.*)

As the basis for forming comparisons, the four selected small European states have some common points: each is relatively small, with a population of less than ten million; all are located on or near the continent of Europe; and all are heavily dependent on international commerce. However, there are differences. Three of the states - Ireland, Sweden, and Switzerland - are neutral, while Denmark is a member of the North Atlantic Treaty Organisation (NATO). While Denmark and Ireland are members of the European Community (EC), Sweden and Switzerland are members of the European Free Trade Association (EFTA).

The most important difference among the case states is that each has a distinct, state specific process of internal interaction among its influential economic actors; variations in these processes help to explain small European state economic performance. Using this approach based on the case studies, this thesis will argue and interpret why some small European states were more internationally competitive than others in the 1980s, as well as the prospects for these states to maintain or augment their levels of international competitiveness into the 1990s.

Most scholars have agreed that international competitiveness assumes that a state's economic problems, such as unemployment, inflation, and slow growth, can be overcome by substantial increases in productivity such that the state can increase its global market share by increasing exports and reducing imports.[1] A strong current account balance, a balanced fiscal budget, stable growth, and low levels of unemployment and inflation indicate that a state has achieved a high level of international competitiveness. In the 1980s Sweden and Switzerland enjoyed such relative economic success.

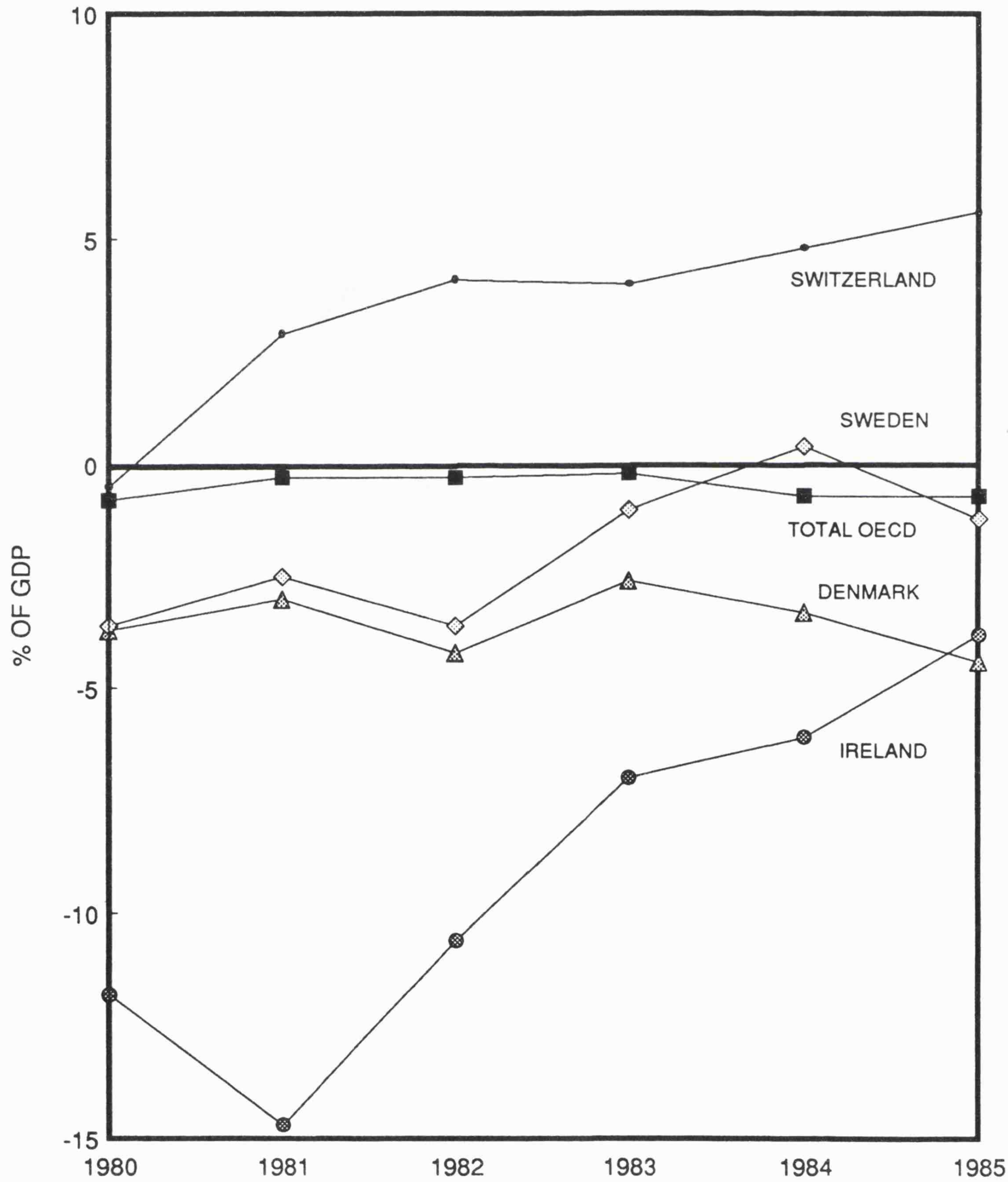
Conversely, a large deficit in a state's balance of payments[2] and a decline in relative purchasing power is indicative of declining international competitiveness. Throughout most of the 1980s Denmark and Ireland experienced high levels of foreign debt, wage-inspired inflation, mammoth levels of unemployment, and enduring current account deficits; these adverse economic indicators typify a deficient level of international competitiveness.

International competitiveness as used in this thesis denotes the degree to which a state's industries produce goods and services for markets abroad, both through trade and foreign direct investment, while expanding the incomes (and therefore the standard of living) of its citizens. The level of a state's international competitiveness is either fostered or inhibited as a result of the internal process of interaction among its important economic actors.

Quadrilateral relations between and among financial institutions, labour, the State[3], and industry lead to either a systematised or a confused process of communication and policy-making. Particular attention in this thesis will be on how state actors attempt to undertake policies that would enhance productivity and stimulate product desirability in foreign markets. Such state-specific interaction and policy-making determines a state's level of growth, employment, prices, current account balance, level of technological sophistication, direct investment abroad, and industrial structure - the prime indicators of a state's level of international competitiveness. (<u>See Figures 1.1 and 1.2.</u>)

Figure 1.1

CURRENT ACCOUNT BALANCE
WITH THE REST OF THE WORLD
1980 - 1985 FOR SELECTED COUNTRIES

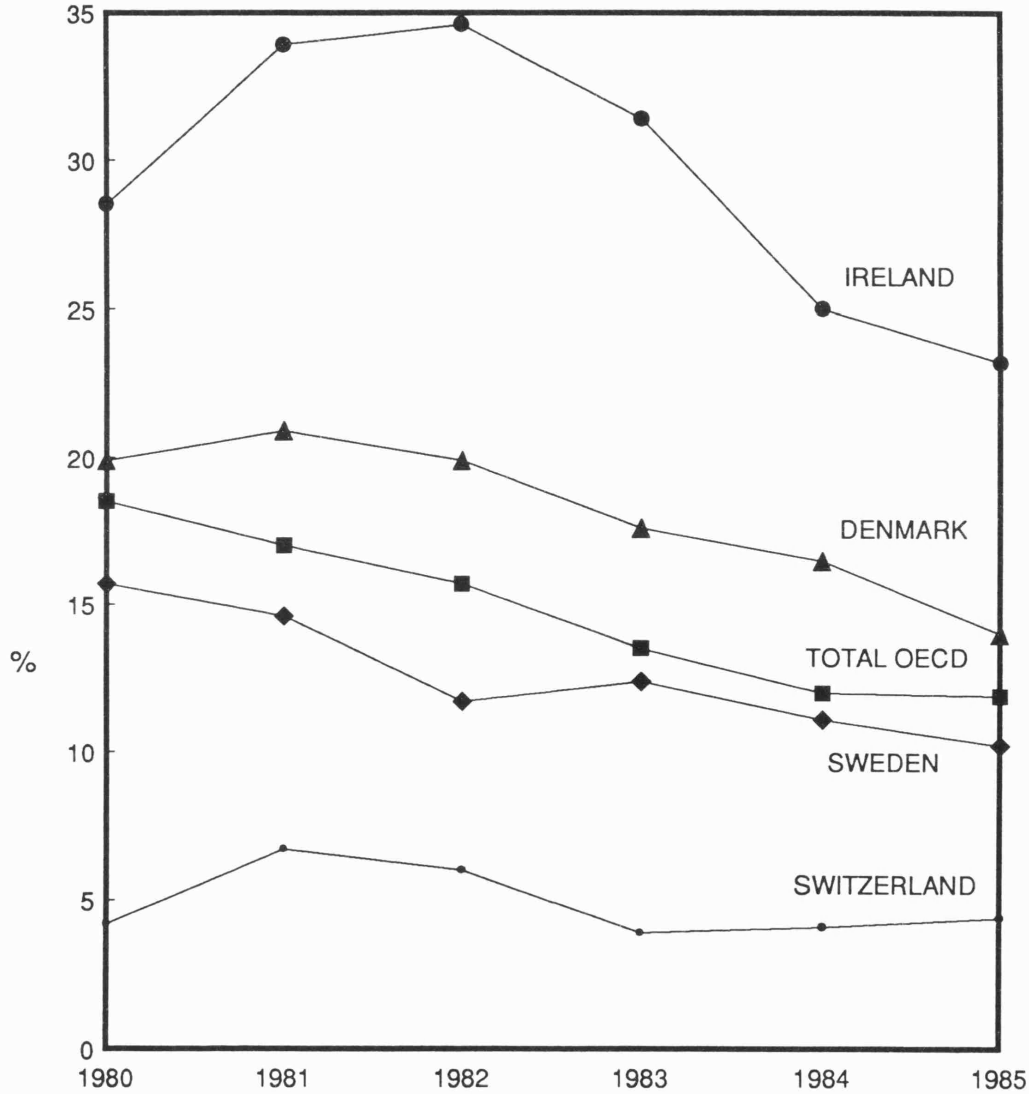


Source: OECD (1987)

Figure 1.2

MISERY INDEX*

1980 - 1985 FOR SELECTED COUNTRIES



Source: OECD (1987)

* Misery Index = inflation (% change over previous year) + unemployment (as % of workforce)

New and increasing global pressures tested the ability of the small European state to remain internationally competitive in the 1980s. The pressures of the decade included the proliferation of tariff and non-tariff barriers, the advent of competition from the newly industrialising countries (NICs), and changes in the relative economic position of the United States. By the mid-1980s the prospect of an internal market for the EC to be created by 1992 under the terms of the Single European Act was perhaps the most interesting development for the small European state.

While international competitiveness has been a popular term used by scholars to refer to the condition of economic vitality of larger states such as the United Kingdom and the United States, it takes on a whole new meaning and importance for the internationally vulnerable small state. Its sensitivity to global political and economic pressures tends to be greater than larger states because of its relatively greater dependence on international commerce. As a result of its modest domestic market, the trade to gross national product (GNP) ratio of the small European state is higher than those in larger states Moreover, as will be discussed later in the chapter, small state industries tend to be price takers as opposed to price makers.

1.2 The Economic Consequences of Being a Small State

A. Limited Political Power

In comparison to large industrialised states such as the Federal Republic of Germany, France, Japan, the United Kingdom, and the United States, small states[4] like Denmark, Ireland, Sweden, and Switzerland encounter a high degree of economic and political[5] vulnerability. The small European state tends to be similar to its larger Organisation for Co-operation and Development (OECD) counterparts in terms of overall standard of living, yet it remains more sensitive[6] to global political and economic pressures. This sensitivity exists because of its limited strategic and political power vis-a-vis larger powers and its high level of dependence on international commerce. In the political realm, David Vital correctly states that "a small state [in comparison to larger states] is more vulnerable to pressure, more likely to give way under stress, more limited in respect of the political options open to it and subject to a tighter connection between domestic and external affairs."[7]

As a result of its comparatively weak political position, the small state has generally attempted to avoid conflict of any kind (military, economic, etc.) with larger powers.[8] Unlike mini-, micro-, or client- states[9] such as Andorra, Monaco, or the Channel Islands, small states, operationally defined here and in much of the small state literature as industrialised states with population sizes of less than ten to fifteen million[10], have identity and autonomy - the "capacity to withstand opposition and stick to purposes thought commensurate with the national interest."[11] They are not "mere pawns" in the strategic relations between large powers, but can have some, though often slight, international or global impact, primarily as a result of their national political and economic autonomy and geo-political puissance in certain areas of the world.[12]

Nonetheless, much of the small state literature has equated "smallness" with "weakness."[13] The small state, though internationally more powerful than mini- or client-states as a result of greater political and economic autonomy, has a limited ability to "induce change in the structure of international relations;"[14] in addition, it "... needs to avoid being regarded as 'hostile'" by larger allies.[15] Small states toe a fine line between retaining the responsibility for their identity and autonomy, and at the same time avoiding conflict, both militarily[16] and economically, with larger powers.

Small European states such as Austria, Finland, Ireland, Sweden, and Switzerland have attempted to avoid international conflict through permanent neutrality. This policy has sent an "unequivocal message" to larger powers that these small European states will avoid all forms of conflict, hence minimising or perhaps averting large-scale politics and security matters, even during wartime.[17]

B. Limited Economic Power

Most important to this thesis, however, are those non-military forms of international pressure, those which imply "injury by deprivation" rather than through military might. Nonetheless, because the territorial-state system defines the parameters of the international economic system, the small state's vulnerable strategic and political position sets the framework for its ability to exert international economic power. Indeed, power in the international system supports the state's attempts at accumulating plenty. As Gautam Sen contends, "The real causes of international trade disputes hinge on the division of international power among competitive nation-states."[18] International economic relations are inherently political, and there is little that a small state can do from either a political or an economic standpoint to alter this situation.[19]

While large powers can either organise the international economic system (system makers) or mobilise their significant domestic resource base to garner a beneficial position in the international division of labour, small states have limited options due to their inferior resource base. In referring to Robinson's important work in 1960 on the *Economic Consequences of the Size of Nations*, S.N. Eisenstadt identifies that small states' internal markets are not sufficiently large nor diversified to produce all that the small state needs, nor does it have the ability to consume all that it produces. Therefore, the small state must seek external markets for both consumption and production purposes.[20]

What will be argued in the following section is that the high level of dependence of small states on foreign markets has fostered policy-makers in these states to pontificate about their commitment to openness and policies based on laissez-faire principles, when in fact these self-identified tenets are examples of "symbolic politics"[21] and fallacious self-characterisations. With their understanding of the politicisation of trade and with increasing international pressures, small states have used various forms of compromising rhetoric[22] towards their larger state counterparts, whose markets remain vital to the small state and whose international military, political, and economic power overrides their own. Moreover, with the international political and economic shield of larger state membership in the European Community, as well as the continuing political unity of the twelve member states, common external tariffs provide trade policy options for small member states not available to those small European states outside the EC.

Hence, unlike numerous scholars who have argued that small states are forced to develop programmes based on laissez-faire principles and openness as a result of a comparatively weak international political stature, it is argued here that small state interventionism, which consists of various labour market, monetary, and industrial policies, is indeed consistent with the pressures of the world market and necessary because small states are price takers.

1.3 The Small European State in the International Market

A. Price Dependency and Flexible Specialisation

Because small states have limited abilities to control product markets, they tend to be internationally dependent price takers.[23] This means that small state industries are vulnerable to world price fluctuations influenced in most cases by large state enterprises with greater market impact. Only in relatively few circumstances are small states able to take on the position of controlling product markets, or becoming price makers.[24] Subsequently, the small state must maintain a high degree of flexibility vis-a-vis those international markets on which it is dependent.

Being "peculiarly vulnerable to 'external shocks,'"[25] or even changes in the overall international economic climate, small state entrepreneurs must be able to compete against larger, more powerful competitors in the international marketplace. Various exogenous turbulences, such as an international recession or increasing prices of production inputs (e.g., oil price shocks), can have serious ramifications for the small state economy.

Moreover, as Conybeare correctly asserts, the small economy has more to gain from open trading relations as a result of its price taking status than larger states.

> The pure theory of trade suggests that most of the gains from trade will accrue to smaller countries, because the terms of trade are determined by domestic prices in the larger countries; hence, a small country will experience a large increase in the price of its export when trade begins, the large country perhaps none at all.[26]

Both flexibility and specialisation (i.e., "flexible specialisation"[27]) are vital to small state industry, which must carefully choose a relatively small range of products, often in *niche* markets, that highly correspond to global, as opposed to (a limited) domestic, demand. Due to natural and human resource disadvantages *vis-a-vis* large states, small state industries are precluded from developing a broad range of products for export.

As a result of its limited export product range, small state markets must adjust to global demand fluctuations by continually, indeed flexibly, replacing antiquated products with those in higher demand (i.e., the Schumpeterian notion of "creative destruction").[28] If a state tends to produce "sunrise" industry products, those in which global demand is expected to increase, such as telecommunications equipment, computers, and pharmaceutical products, then generally it has a better opportunity for future global market growth than it would by producing "sunset" industry goods, those in which global demand is decreasing. While this principle generally applies to all states, the small state, because of its price taking status and limited ability to produce a broad range of items relative to larger states, must be more flexibly specialised than the larger state. As S.N. Eisenstadt explains,

> ...the type of specialization open to small states and the nature of their dependency may change throughout history. One of the great problems of small states is that they may become so attuned to one type of international market that they collapse entirely if this market changes....Thus, a basic problem faced above all by the small state is the need for a high degree of flexibility vis-a-vis those international

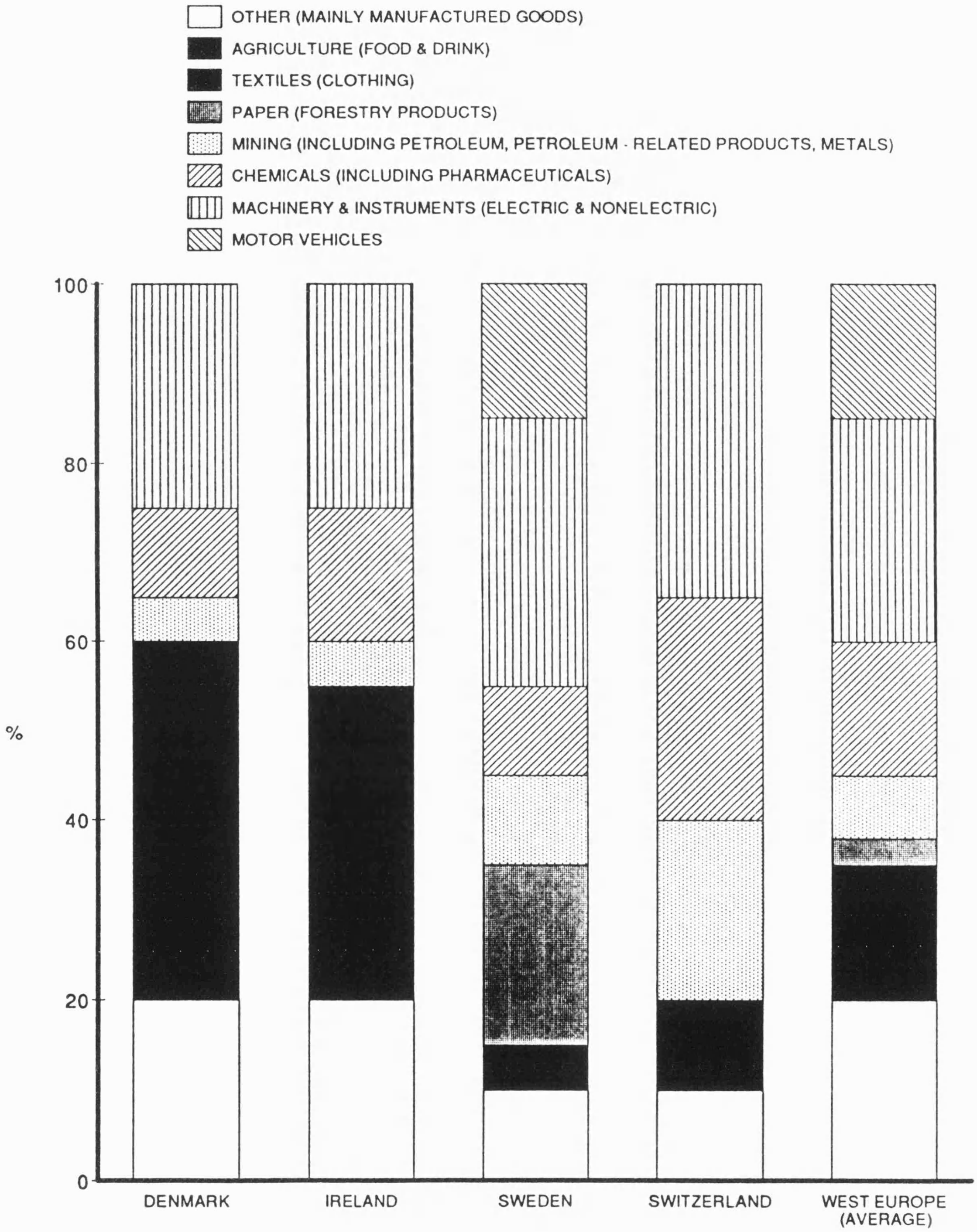
markets on which they are dependent.[29]

Having a sunrise product export orientation increases the likelihood that a small state, highly dependent on international trade, will be able to maintain its international competitiveness in the future. The Swedish and Swiss export orientations in the 1980s were geared towards high technology products. Indigenous Danish and Irish industries exported primarily in the agricultural field. (See Figure 1.3.) In both Sweden and Switzerland, for example, exports significantly increased in the telecommunications field, where OECD demand continued to grow. (See Figures 1.4 and 1.5.) In the decade the Irish and Danish economies were heavily dependent on the agriculture sector, even though global demand levelled. (See Figures 1.6 and 1.7.)

In addition to the export of goods, a few small European states were highly successful in exporting another specialised product: services. (See Figure 1.8.) The tertiary sector, particularly banking (and to a lesser extent tourism), in Switzerland, Belgium, Luxembourg, and the Netherlands enabled these states to maintain surpluses in their balance of services and was a major reason for the economic success of these countries.

Figure 1.3

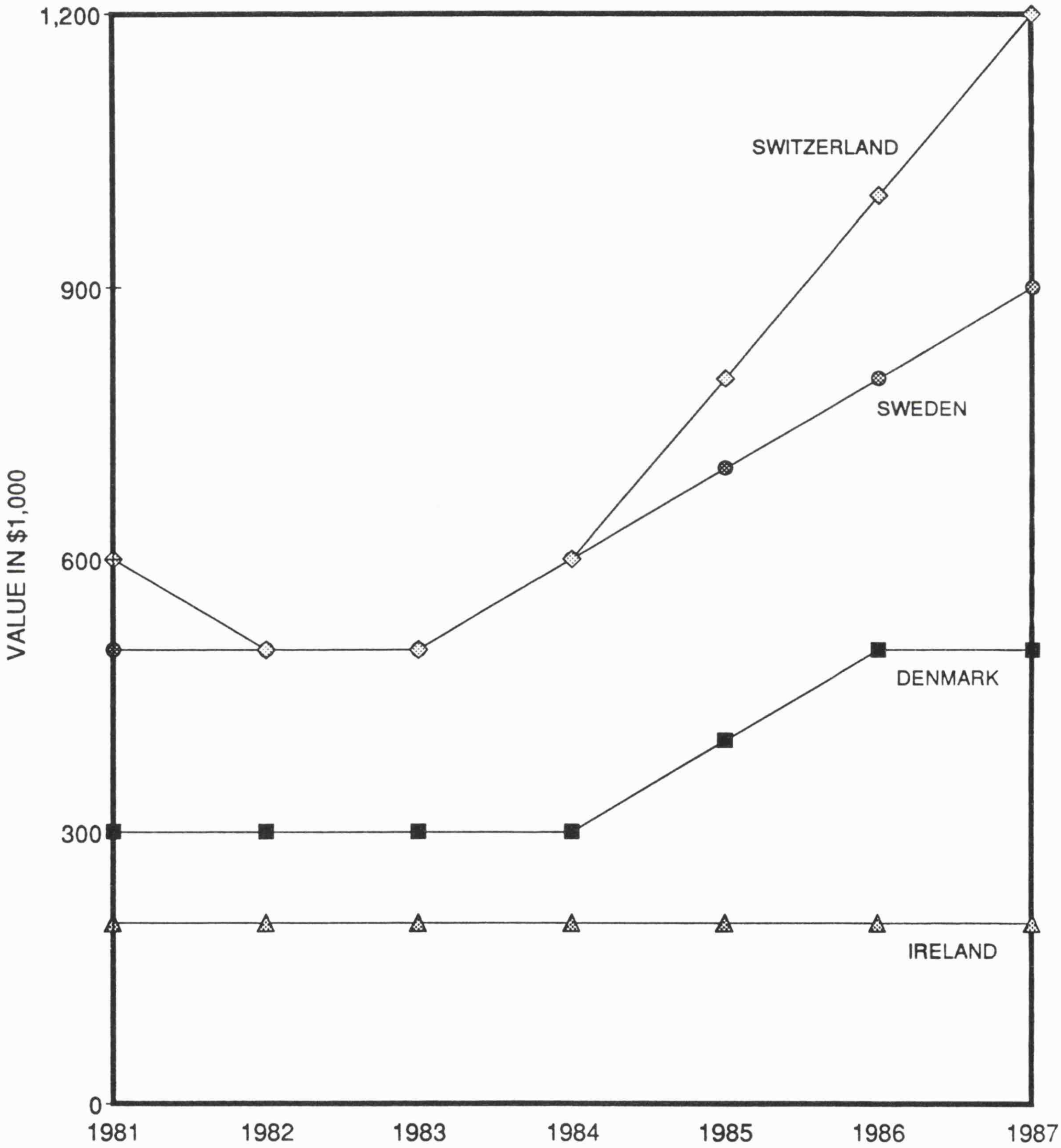
MAIN EXPORT COMPOSITION (%) FOR SELECTED COUNTRIES, 1987



Source: The Economist (1987) The World in Figures

Figure 1.4

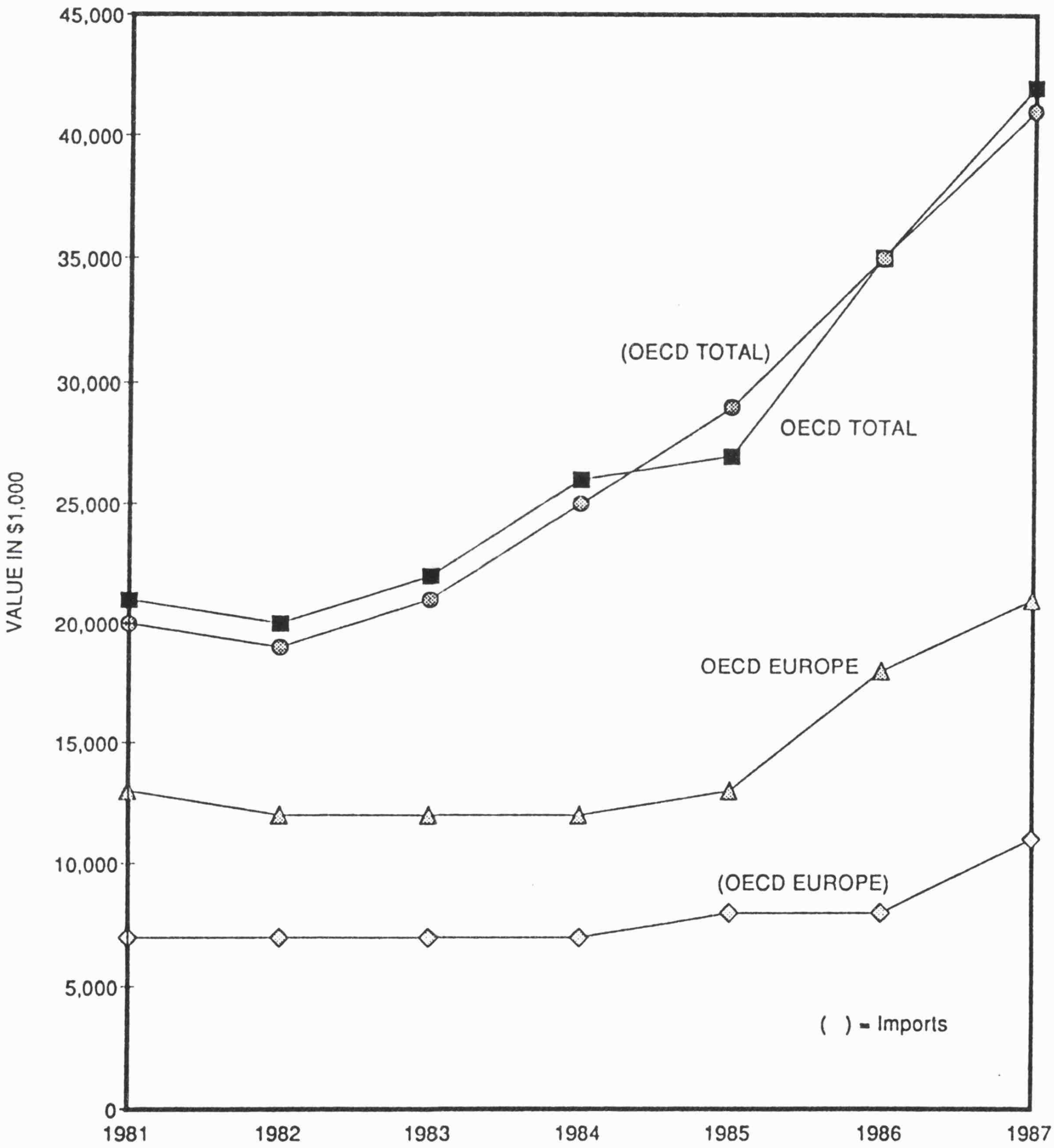
TELECOMMUNICATIONS AND SOUND RECORDING APPARATUS TRADE, VALUE IN $1,000



Source: OECD (1988) Foreign Trade By Commodities, Volume I.

Figure 1.5

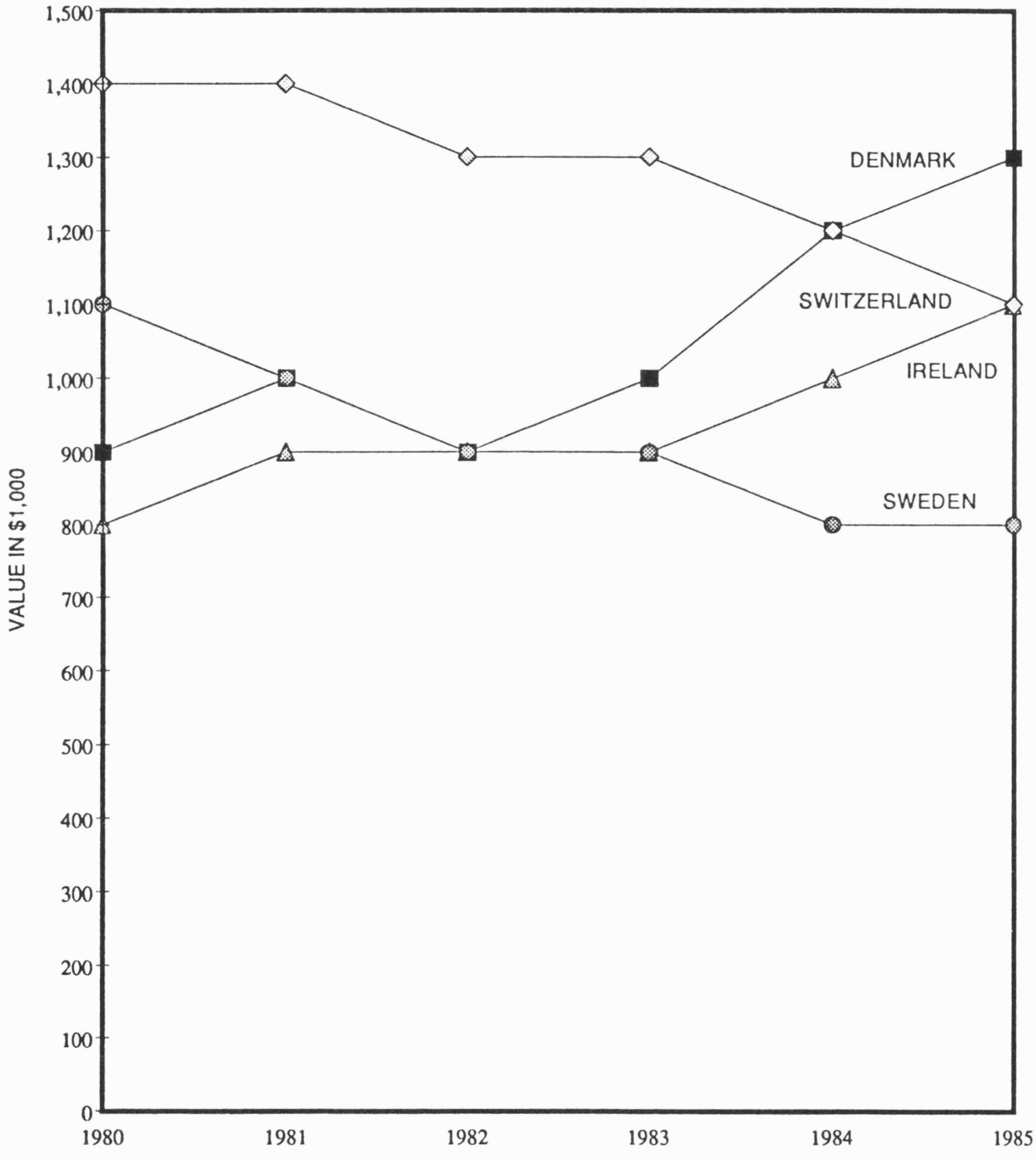
TELECOMMUNICATIONS AND SOUND RECORDING APPARATUS TRADE, VALUE IN $1,000



Source: OECD (1988) Foreign Trade By Commodities, Volumes I and II.

Figure 1.6

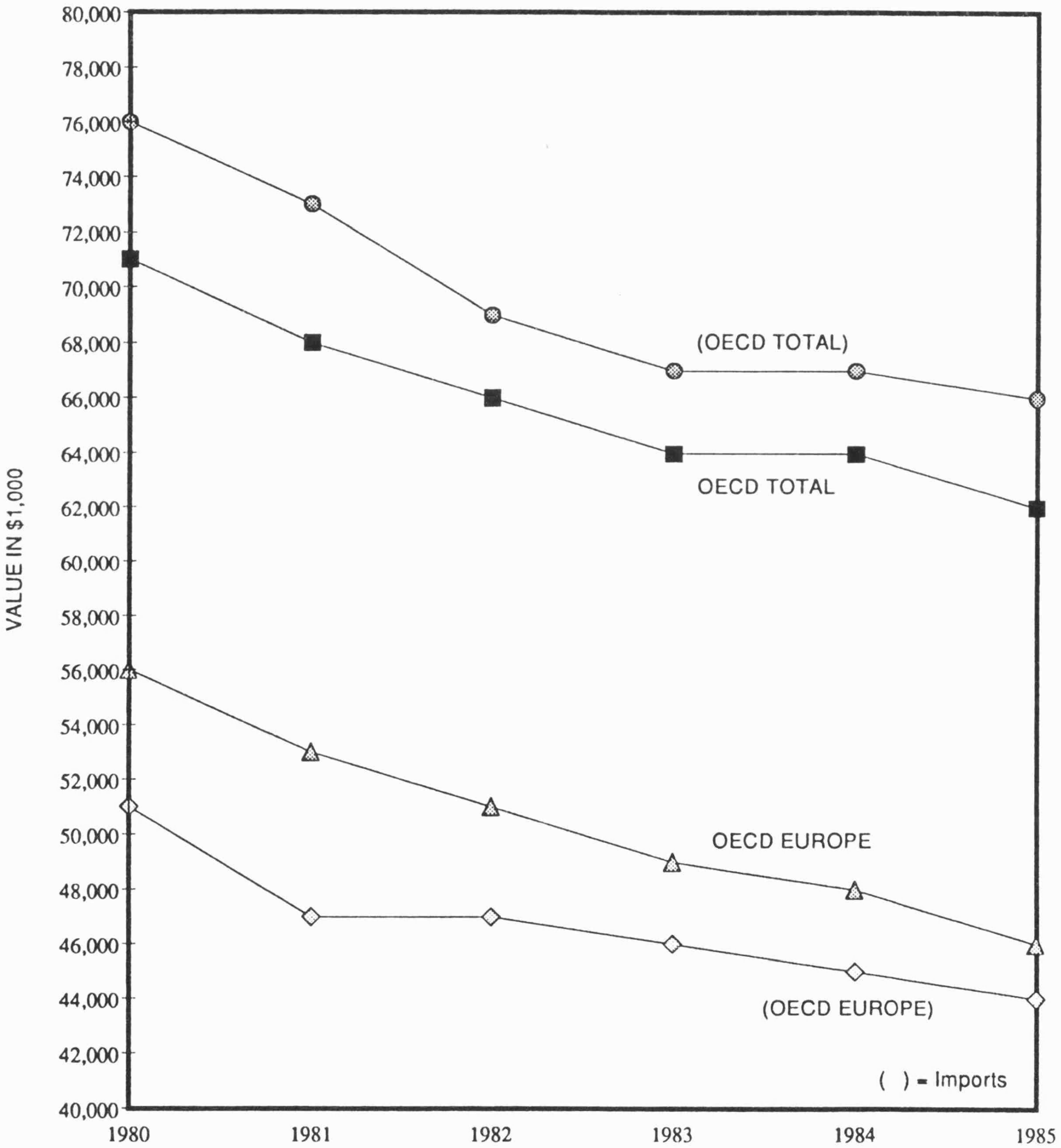
FOOD AND LIVE ANIMAL TRADE, 1980-1985 IN $1,000 - EXPORTS



Source: OECD (1988) Foreign Trade By Commodities, Volume I.

Figure 1.7

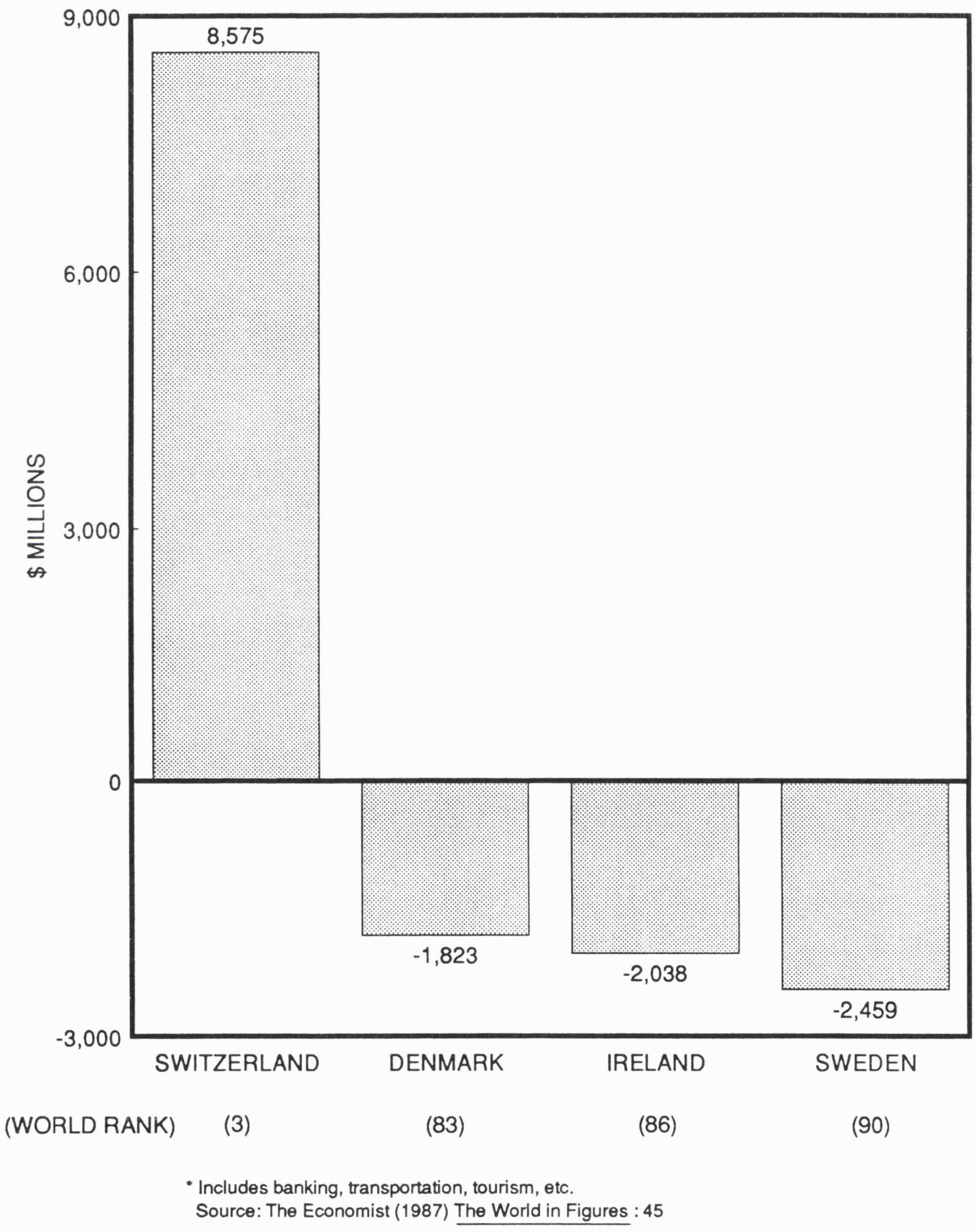
FOOD AND LIVE ANIMAL TRADE, 1980-1985
IN $1,000 - EXPORTS AND (IMPORTS)



Source: OECD (1988) Foreign Trade By Commodities, Volumes I and II.

Figure 1.8

BALANCE OF SERVICES, 1985*
($ MILLIONS)



* Includes banking, transportation, tourism, etc.
Source: The Economist (1987) The World in Figures : 45

These three profiles - sunrise industries, agriculture, and services - can be explained as (a) indicators of industrial development and (b) historical industrial preferences.

a) Industrial Development. Throughout the 1980s Ireland's level of industrial development, for example, was significantly lower than the Swiss or the Swedish level. This difference helps to explain why the Irish economy remained heavily dependent on its indigenous agricultural sector and inward foreign direct investment (FDI),[30] while the Swedish and Swiss economies depended on powerful international banks and giant multinationals in such high tech areas as sophisticated machinery equipment and pharmaceutical products.

b) Industrial Preferences. Though the agriculture sector is often cited as a low-growth sector, Danish agriculture, renowned for having highly mechanised productive techniques, has been a highly productive force in the economy.[31] In the same vein, as a result of the number of forests in Sweden, the forestry industry has remained a relatively large industry in the country. Certainly the large agriculture sector in Switzerland has been a manifestation of its historical presence in the dairy industry, particularly with regard to the production of cheese and chocolates.

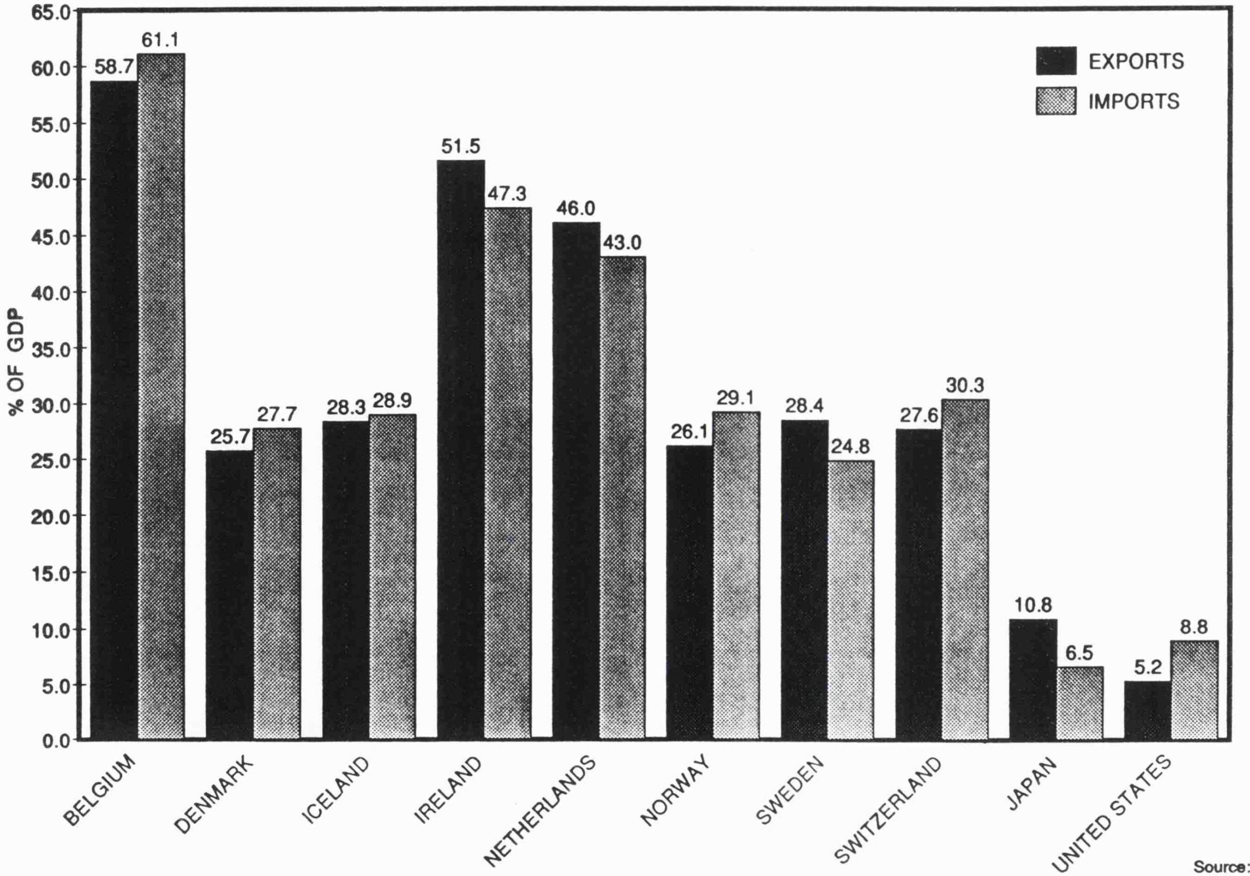
B. Reliance on Trade and Inward and Outward Foreign Direct Investment

No matter the level of industrial development, the degree of trade dependence of the small state tends to be much greater than the larger state. (See Figure 1.9.) In 1986 United States exports totalled 5.2% of its Gross Domestic Product (GDP), and Japan's exports amounted to 10.8% of its GDP. Imports totalled 8.8% and 6.5% of their respective GDPs. However, in small states like Belgium and the Netherlands, exports totalled 58.7% and 46.0% of their respective GDPs, while imports in these states amounted to 61.1% and 43.0%.[32]

While some small European states such as Ireland have welcomed inward FDI in order to spur its industrial development, in the 1980s such small European states as the Netherlands, Sweden, and Switzerland[33] were less accepting of inward FDI from foreign sources as evidenced by restrictive share-holding policies that obstruct foreign takeovers of indigenous industries. These states, whose investment success has also been a manifestation of their level of industrial development and historical industrial preferences, have gained much of their national wealth through profits from direct investment abroad that has been either repatriated, reinvested, or exported from the offshore site to other locations overseas. Multinational corporations (MNCs) have followed industrial organisation theories for growth based on both horizontal and vertical integration, the latter "where the production of outputs in one plant serves as inputs for other plants."[34]

Figure 1.9

FOREIGN TRADE AS PERCENT OF GDP (1986)
FOR SELECTED SMALL EUROPEAN STATES VS. JAPAN
AND UNITED STATES



Source: OECD (1988)

C. Small European State Trade Policy Options

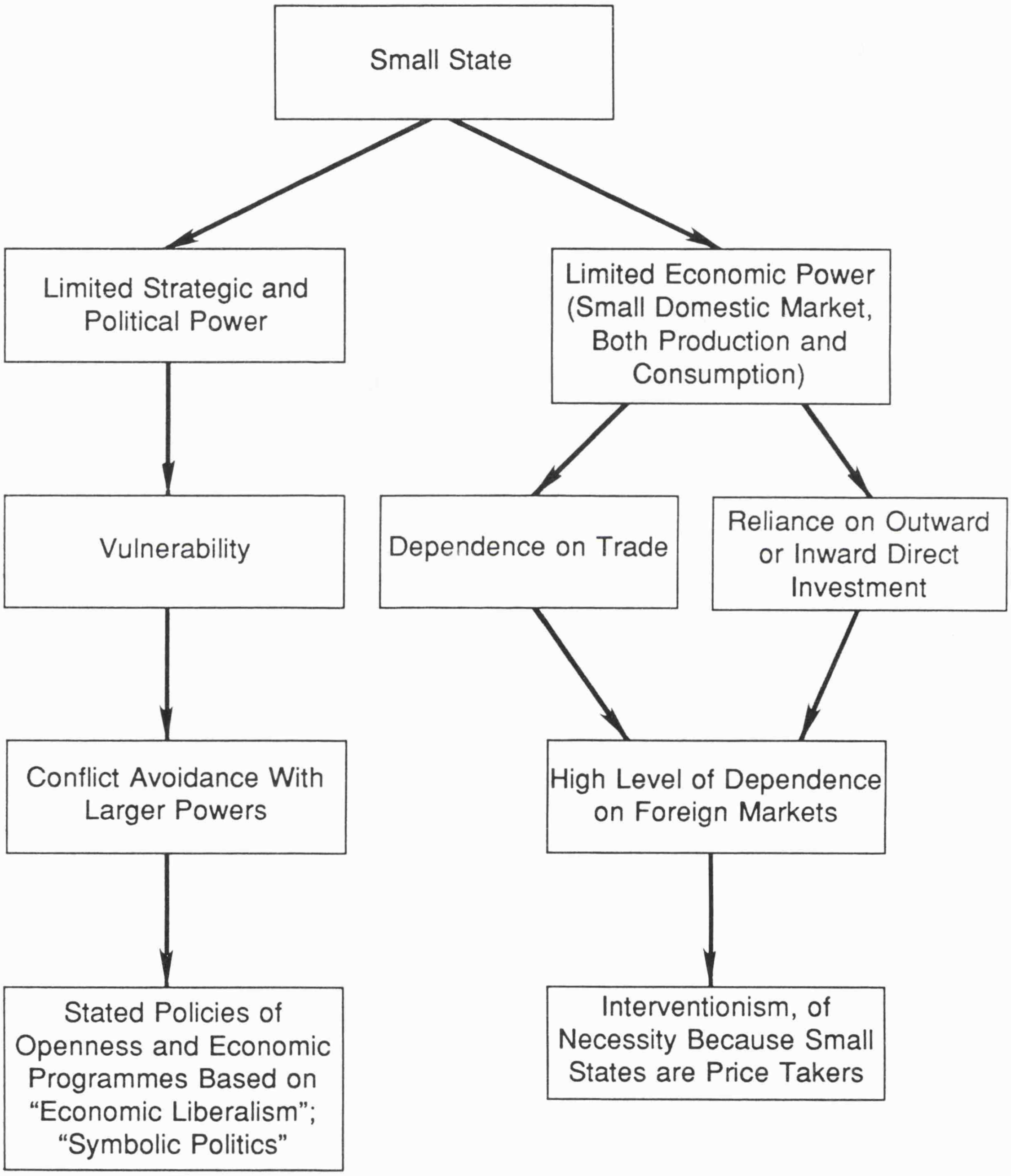
With such a high degree of dependence on world markets, coupled with the necessity to avoid costly trade conflict with large powers, a number of authors have asserted that the small state must opt for openness and economic programmes based on laissez-faire principles. Authors such as Peter J. Katzenstein assert that small state industrial and trade policies from the 1930s through the 1970s tended to be reactive, or defensive, while larger states with more international muscle, like Japan and France, were able to form a number of mercantilist or offensive programmes such as targeting, pick the winners, and administrative guidance that could directly influence the composition and location of industrial output. Moreover, it has been argued that because of their lack of international power and dependence on international commerce, small states cannot develop these offensive, seemingly protectionistic policies that could foster animosity from large states for fear that the consequent retaliation could result in the elimination or restriction of vital foreign markets.

According to many scholars writing about the small state in the past, negative sanctions, such as voluntary export restraints (VERs) and orderly marketing arrangements (OMAs), have been avoided by the small European state, not only because of the impracticality of such measures for small states dependent on export-led growth, but also as a result of their fear of larger state retaliation and the consequent loss of vital trading lanes. Instead, as David Yoffie asserts, long-run political strategies are developed to prevent crises in bilateral trade regimes with larger states, including the short-term acceptance of VERs and OMAs imposed by larger states to quell further, long-term antagonism.[35] In spite of some exceptions, negative sanctions, such as embargoes, boycotts, tariff increases, and blacklisting,[36] have generally been avoided by the small European state.

What should be apparent is that other instruments of intervention have been available in the small state's "economic statecraft" repertoire. It is argued here that small states have been able to develop and implement a number of programmes that directly influence the composition and location of industrial output as part of a strategic trade policy. (See Figure 1.10.) Indeed, the "small country assumption" accepts that, "In the case of a small country, even if its domestic policies cause its exports to increase or imports to decline, these effects are insignificant for all trading partners and, thus, they have no reason to react."[37] With inferior international political power, such frequently used terms by small European state policy-makers as "laissez-faire" and "openness" have helped induce large state acquiescence towards, or oversight of, acts of market intervention by the governments of small states.[38]

Figure 1.10

THE EFFECTS OF INTERNATIONAL PRESSURES ON SMALL STATES IN THE 1980s



Moreover, as Paul Krugman explains, the optimum form of intervention has not been trade intervention, but domestic intervention, such as loan guarantees, manpower programmes, and research and development policies.[39] A number of monetary, labour market, and industrial policies have been developed in small European states to maintain or increase their levels of international competitiveness. In many ways this is the other side of David Baldwin's "economic statecraft" coin. (<u>See Figure 1.11.</u>)

<u>Figure 1.11</u>
<u>Examples of Economic Statecraft: Positive Sanctions</u>

Trade	Capital
Tariff discrimination (favourable)	Providing aid
Granting 'most-favoured-nation treatment'	Investment guarantees
Tariff reduction	Encouragement of private capital exports or imports
Direct purchase	Taxation (favourable)
Subsidies to exports or imports	Promises of the above
Granting licenses (import or export)	
Promises of the above	

Source: David A. Baldwin (1985) *Economic Statecraft*: 42.

Nonetheless, the experience of the four small European states suggests that when particular sectors experienced stagnation because of changing international economic conditions, the State was forced to respond flexibly despite its price taking status making such aid to declining sectors futile economic statecraft. Sweden's giant shipbuilding industry eventually could not compete with Japanese and

Korean shipbuilders in the 1970s, yet the Swedish State continued to subsidise the industry even in a short and atypical period when the government was led by a centre-right coalition, rather than the historically powerful Social Democrats. Nonetheless, after some consideration and attempted priming, Swedish policy-makers allowed the industry to run its course.

In Denmark, the State continued to subsidise the declining shipbuilding industry, neglecting to understand its internationally vulnerable price taking status much as a consequence of increased competition from Asia. Likewise, the watch industry in Switzerland was subsidised in the 1970s as a result of increased competition primarily from Japan, yet unlike the Danish shipbuilding case, the Swiss watch industry recovered and became successful again as a result of innovation and product differentiation. These three cases - Swedish shipbuilding, Swiss watchmaking, and Danish shipbuilding are the most important, not to mention unique, examples of State subsidisation in the case states. As a result, these cases will be addressed in detail throughout the thesis, particularly in Chapter Five. Of course, the agriculture sector, particularly in Denmark and Ireland, has also been heavily subsidised.

The Irish and Danish cases underscore the importance of the EC for small states. With the international political and economic shield of larger state membership, as well as the continuing political unity of the twelve member states, common external tariffs and the common EC stance at the

General Agreement on Tariffs and Trade (GATT) have provided trade policy options not open to those small states outside the EC. For example, with Danish and Irish membership in the EC, along with West German, French, English, and Italian membership, small "European" state trade policy options have been less constrained than for those small European states that have not been members, such as Austria, Finland, Iceland, Norway, Sweden, and Switzerland.[40]

These latter states have been members of the European Free Trade Association (EFTA), and hence have received favourable terms of access for their manufactured goods (not agricultural ones) into the European Community market, the destination of three-fifths of EFTA's exports throughout the 1980s. However, their position outside the more economically and politically powerful Common Market has not afforded them the same trade policy options as those small states forming common policies and political ties with larger states in the EC. Certainly one of the greatest advantages for these states is that the EC has trade creation benefits resulting from the lack of internal tariffs.[41]

One can infer the following about the small European state's policy actions in terms of the limitations imposed upon it as a result of international pressures:

a) While both larger states and small states encounter many similar external pressures (e.g., oil shocks, international recession, etc.), the major difference between large state and small state pressures is that large state industries tend to be price makers, which means they have greater ability to control product markets than most smaller state industries, who have significantly less control on international markets as price takers.

b) As a result of international pressures, small European states have pursued strategic trade policies in some cases even more rigorously than larger states. Some authors have asserted that small state trade policies have tended to be only reactive, or defensive, while larger states with more international muscle have been able to form a number of mercantilist, offensive programmes that directly influence the composition and location of industrial output. An important point is that while larger states such as Japan and West Germany have developed interventionist policies, a key distinction is that their industries are price makers. Yet because of the small European state's price taking vulnerability, interventionism has been used to combat international economic pressures. The degree of intervention has ranged from the highly active Irish State to the moderately active Danish and Swedish States to the less active Swiss State.

c) Knowledge of the internal process, in which critical economic actors form important bargaining relationships that breed flexible specialisation, is the key to understanding how particular small European states remain internationally competitive. The degree of success of small European states in the international marketplace is significantly determined by internal conditions, which differ as a result of varying industrial cultures and consequent internal bargaining processes.

1.4 Efficient Collectivism as a Source of International Competitiveness

A. The Collectivist Literature

This thesis posits that all small European states are neither always similar nor uniformly economically successful, but rather that economic outcomes depend on the internal conditions of the state. Small states are, however, similar in that they often, though not always, face similar exogenous conditions. For instance, the economic vitality of Ireland and Switzerland are appreciably different despite both being small states. While small European states possess the commonality of size, they have reacted in different ways to changing external conditions. Indeed, a major reason for these varied reactions can be attributed to internal factors which, beyond a few works, have been "wholly neglected in the studies."[42]

Small states can create the necessary domestic conditions for their industries to remain globally competitive in order for the state itself to realise an advantage in the world trading system. John Zysman and Laura Tyson illustrate the importance of the ability of a state's actors to spur productivity levels, particularly in growth sectors, and to support high incomes. Most importantly, they affirm that "National and corporate competitiveness are analytically distinct but practically intertwined."[43] In a similar sense, Michael Porter explains that "a favorable competitive position in an industry [is] the fundamental arena in which competition occurs."[44]

Several political economists who are associated with the collectivist school, including Andrew Shonfield,[45] have examined the institutional relationships among trade unions, employers' confederations, industrial associations, financial institutions, and the State.[46] Ricardian trade theory assumes that the ability of any state to gain comparative advantages in international trade is a product of an "efficient state," and these interactive relations may "create" the necessary domestic conditions for (in particular) a *small* state to remain efficient.

Shonfield's *Modern Capitalism* is the original and most renowned of the collectivist literature, and it has spawned a number of works from such academics as Lehmbruch,[47] Lindberg,[48] Maier,[49] Schmitter, and Streeck.[50] Differentiated from mainstream economists and rational choice theorists who "conclude that politicians, bureaucrats, and lobbyists take collective action which neglect market incentives, debase allocative efficiency, and downgrade economic performance,"[51] the collectivists have studied the economic purpose of intergroup consensus and tripartite negotiation between the State, industry, and labour.

> [These authors] emphasize the interaction among economic agents and group interests and between them and the state. Patterns of economic production and consumption, the economic goals pursued and instruments chosen, and the ability of political authorities to adapt policies and implementation of strategies to changing political and economic conditions are largely

institutionally constrained or determined.[52]

This thesis, therefore, posits that in studying the international competitiveness of small states it is necessary to examine the structure of the relationship between the State and the market, in which domestic economic actors provide "resources and incentives that in an interactive process, reinforce governing."[53] At the heart of this institutional perspective is the dynamic process in which policy-making is developed and the collective and individual impact these policies eventually have on the ability of the small state to be internationally competitive. This process is extracted from political and institutional struggles that are based and arbitrated by a preestablished organisation of state power.[54]

B. The Small State Advantage and Democratic Corporatism

Many scholars have accepted that small states hold a distinct advantage over larger states simply because smallness tends to breed "economic efficiency" and "cultural productivity".[55] They argue that the small European state has been able to profit from frequent formal and informal discussion and bargaining between (and among) the State and peak associations,[56] the top-echelon centralised level of representation for each particular economic institution. With paradigms derived from the collectivist school of political economy, Peter J. Katzenstein, David Cameron,[57] Charles Maier and Mancur Olson,[58] for instance, have accepted institutionalised bargaining, coupled with political stability, as the root of economic success for such nations as Austria, Belgium, the Netherlands, Norway, Sweden, and Switzerland from the 1930s through the 1970s.

Katzenstein, for example, has labelled the consensus formation of small states as democratic corporatism, which is characterised by three traits:

> an ideology of social partnership expressed at the national level; a relatively centralized and concentrated system of interest groups; and voluntary and informal coordination of conflicting objectives through continuous political bargaining between interest groups, state bureaucracies, and political parties.[59]

He proposes that since the 1930s a number of small states have been forced to develop economic programmes based on laissez-faire principles in order to avoid policies that larger states might perceive as being protectionistic, thus causing possible large state retaliation with consequences that are extreme for small states dependent on foreign trade.[60] Subsequently, economic smallness typically translates into economic openness.

> This view is held because small states must achieve specialized niches in the world economy if they are to thrive and because productive specialization requires ample free trade both to obviate consumer shortages and to avert risks of crippling foreign tariff retaliations that might be provoked by protectionism.[61]

He proposes that if small states are forced to have open economies without the aid of offensive industrial policies, they remain economically strong by being flexible. The government rewards its citizens for the costs of being flexible (or "investment and employment instabilities"[62]) by compensating them through various manpower, incomes, and employment policies. He applauds the ability of several small European states who preserve their economic openness, manifested through both import dependence and export specialisation, by being capable of adjusting to international political and economic conditions.

The "flexible industrial adjustment" programme of the small European state, furthermore, does not include exporting the costs of change, an option open to larger states; rather, the small state tends to live with these conditions, responding to them as they come.

> The strategy of the small European state is flexible, reactive, and incremental. It does not counter adverse changes by shifting its costs to others abroad; it does not attempt to preempt change by ambitiously reordering the economy at home. Instead the small European states continually improvise in living with change.[63]

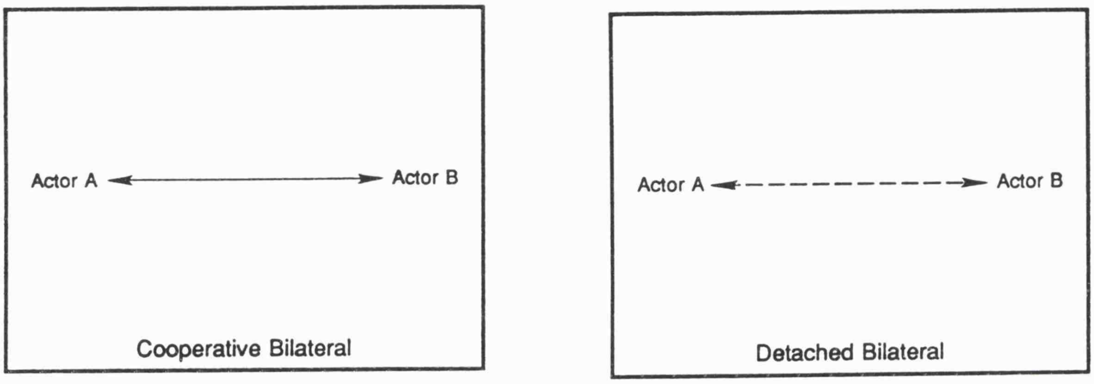
Katzenstein attributes democratic corporatism, in combination with a system of proportional representation[64], which leads to minority governments that "attempt to influence policy" as opposed to trying to "accumulate patronage," as the root from which the small European state attains flexible industrial adjustment. "Democratic corporatism, which creates a relatively dull and predictable kind of politics, manifests itself through an ideology of social partnership - centralised and concentrated interest groups that form an integral part of a comprehensive bargaining system - and through a system of voluntary and informal coordination between conflicting objectives."[65] Thus, he concludes that "these [small European state] traditions, institutions, and structures form a context and impose policies which bear no resemblance to those of the larger European countries."[66]

C. The Thesis Model of Actor Interaction

This thesis contends that each small European state has a distinctive process of internal interaction that cannot be generalised through imprecise nomenclature such as democratic corporatism. It is assumed here that the process of internal actor interaction is both dynamic and state-specific; as a result, generalisation and the use of vague terminology are less helpful than comparing each state individually. To frame a state-specific process of interaction in universal overtones undercuts the meaningful aspects of how each small European state attempts to maintain or augment its level of international competitiveness. Differences between the Katzenstein model and the approach used in this thesis are further enumerated in the final section of this chapter (Section 1.6).[67]

This thesis sets out a relatively straightforward framework to examine variances in the communication processes of small European states. There is no grand scheme or recipe for small European state political-economic success; rather, the model provides a useful method to analyze actor interaction within the small European state to determine the reasons for political-economic success *or failure*.

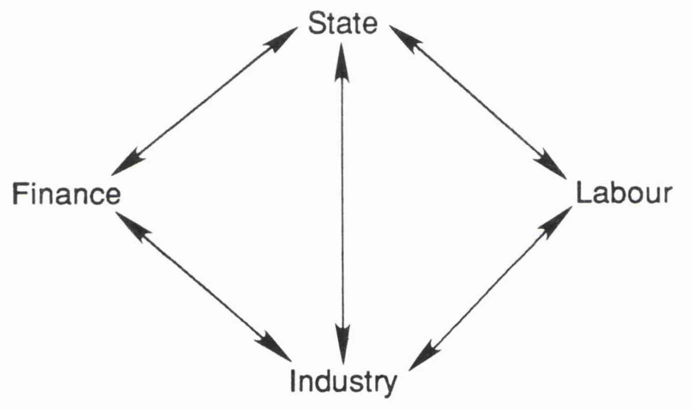
At its most basic level, communication within the small European state can be examined through dialogue between two actors, where relations can be characterised as either cooperative or detached.



Under cooperative bilateral relations, actor interaction is familiar, and consultation and exchange is frequent and orderly. Typically such ties breed high levels of cooperation necessary for the state to remain internationally competitive. If bilateral interaction involves the State itself, cooperative relations usually lead to policy progress. In contrast, detached bilateral relations occur when actor interaction is characterised by distant and infrequent communication, and where the lack of dialogue inhibits cooperation. Under detached bilateral relations involving the State, policy-making is usually unproductive and ineffective.

The level of international competitiveness of the small European state can be evaluated by assessing a subsequent level of actor interaction within the state between and among the fundamental market actors and the State. Therefore, the model of actor communication used in this thesis involves evaluation of the process of relations among the four major actors - financial institutions, labour, industry, and the State - that support and augment international competitiveness.

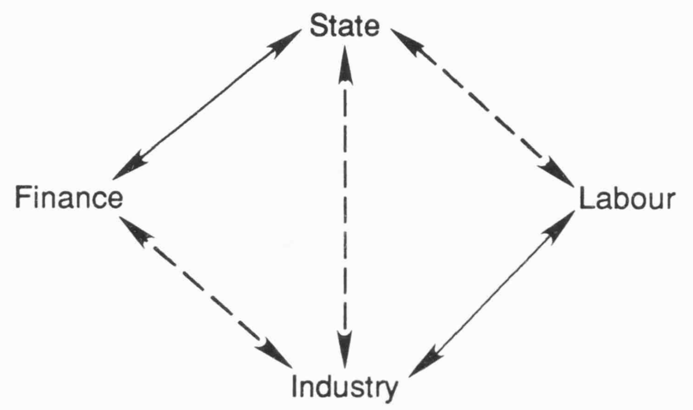
Under a best-case scenario of communication among these actors, where all relations are cooperative, communication within the state can be characterised as continuous quadrilateral.



Continuous Quadrilateral

Under continuous quadrilateral actor relations, the dialogue process is systematised and orderly. The State is able to form monetary, labour market, and industrial policies that act as necessary complements to cooperative bilateral interaction between finance and industry, labour and industry, and the State and industry. Continuous quadrilateral relations breed high levels of cooperation necessary for the state to achieve high levels of political-economic performance.

Under a scenario where some (or all) forms of communication are detached, the level of interaction within the state can be characterised as intermittent quadrilateral.



Intermittent Quadrilateral

Dialogue among actors can be detached, causing a less systematised process of interaction that can be characterised as intermittent quadrilateral. Further, the State is not always able to form monetary, labour market, and industrial policies. As a result of less efficient and effective policy-making and more distant actor relations, the state is less able to achieve a high level of international competitiveness.

1.5 The Interactive Process and the Roles of the Major Economic Actors in the Small European State

Undeniably the paradox of the small state is that while it faces international political and economic vulnerability because of limited international power *vis-a-vis* large powers, its small size is also its greatest asset to maintain or augment its level of international competitiveness. Because of its geographic proximity that encourages actor familiarity, communication between and among actors can be facilitated. A major advantage the small state possesses over large states is the monocephalic nature of its society, one in which "all resource-holders within a territory tend to congregate within short distances of each other..."[68] In contrast, a polycephalic society is defined as one in which there is "a marked geographical dispersion of different types of arenas across a very wide area...."[69]

In general, small states hold the monocephalic advantage, with both governmental and industrial power located in the same location, while larger states like "Japan and West Germany ... have a clear-cut dissociation of the political from the economic centres."[70] In Denmark, Ireland, and Sweden, the governmental, financial, and industrial centres are located within the capitol city. Only in Switzerland are the governmental and financial/industrial centres in different locations, yet the distance is short between the three centres (Zurich, Basel, and Berne). Because the role of government in Switzerland is extremely limited, most interest representation occurs in Zurich, the powerful financial centre.

Because of this small state advantage, interest representation, particularly from industry and labour, is often centralised through confederations. One can readily think of the Manufacturer's Association of Israel (MAI) and Norway's *Industrirardet* as good examples of powerful small state employers' confederations. Among the case countries, the Swedish *Arbetsgivarforeningen* (SAF), the Swiss *Vorort*, and the Danish *Industrirardet* are excellent examples of strong employers' confederations; on the labour front, the Swedish *Landsorganisationen* (LO) and *Tjanstemannens Centralorganisation* (TCO), the Danish LO, and the Swiss *Gewerkschaftsbund* (SGB) are powerful labour confederations.

A number of small European states have been able to manipulate the relations among centralised bodies, often in conjunction with the State, into streamlined systems of communication and bargaining. Such forms of interest representation help to avoid societal conflict and to promote economic structures that stimulate a progressive and flexible dialogue, resulting in high levels of international competitiveness for the state. When communication fails, the small European state negates its monocephalic small state communication accessibility advantage over its larger competitors. Indeed, it is this assertion that will be discussed throughout the thesis.

A particular process of interaction between and among financial institutions, organised labour, the State, and industry develops as a result of the small state's industrial culture, which is composed of nationally specific institutional goals that guide the state and society, both knowingly and unknowingly, in either inhibiting or promoting industrial progress. This institutional framework "... mediate[s] the interests and capacities ... [within] the large-scale and historically evolving organisational structure of state and society."[71] An attitude or ideology, particularly towards the role of the State, becomes manifest through a state's industrial culture.

While its small size is an advantage over large state competitors, what is also important is that the role of a particular actor, coupled with an institutional framework that streamlines the process of interaction among the four key actors, can produce the necessary internal situation for increasing a small state's share in growing foreign markets, which in turn expands the incomes of its citizens. In the 1980s the State did not always act as the primary impetus within the small European state in attempting to preserve or increase its level of international competitiveness. What will be illustrated in this thesis is that depending upon each state's specific industrial culture, other actors such as financial institutions and labour assumed the role of the small European state's principal actor.

Therefore, while the small European state has the monocephalic advantage that lends itself to communication and dialogue accessibility, its industrial culture, which is composed of rules of behaviour, norms, roles, or "patterned habits of thought learned by individuals performing these roles,"[72] determines how the major economic actors in society bargain to attempt to foster the development of industry. The impact of the three major actors, financial institutions, labour, and the State on industry is discussed below.

A. The Interaction Between Financial Institutions, Industry, and the State

The nature of the tripartite finance-industry-State relationship can determine whether financial institutions in small states foster international competitiveness.[73] Where there are financial institution relationships in a credit-based system, in which much of the political economy literature has focused on the Japanese and West German systems, as opposed to a capital market-based system, such as in the U.K. and the U.S., these relations can facilitate the ability of industry to remain internationally competitive. As John Zysman explains,

> In capital market-based systems with elaborate secondary markets, entrance to and exit from different financial holdings are quite simple processes....In credit-based systems with fewer arrangements for an easy exit, financial institutions are obliged to remain loyal to their customers.[74]

Under a credit-based system, industry is able to maintain high levels of investment because of a high debt-equity ratio; the amount of equity employed in a company's financial structure is a combination of the actual cost of equity versus debt to the firm. In addition, having highly leveraged firms ensures strong financial institution-industry relations because of financial institutions controlling industries' debt.

However, it is impossible for a state's financial institutions to provide low rates of credit, even for their most valued customers when monetary authorities are unable to maintain low real interest rates as a result of inflationary problems. In addition, high real interest rates cause overvaluation vis-a-vis the currencies of the trading partners, which in turn causes the prices of the state's exports to be higher for the foreign consumer.

Throughout the 1980s, Switzerland was able to maintain lower real interest rates than its competitors and was able to maintain a relatively stable national currency. The relationship among monetary authorities, financial institutions, and industry produced a coordinated interest rate and exchange rate policy that was quite beneficial to Swiss industry. Moreover, in Sweden by the beginning of the 1980s active monetary policy-making primarily through devaluation led to increased industrial growth.

Consequently, because of the monocephalic nature of the small state, during the 1980s the proximity of financial institutions to industry could breed a strong working relationship between the two parties. Certainly in Sweden and Switzerland financial relationships were such that most corporations tended to seek financing with particular banks. In Switzerland in particular, financial institution-industry relations were similar to those in the Federal Republic of Germany; strong banking relationships produced lower real costs of capital for Swiss industries relative to that which its international competition paid, which allowed for strong industrial market development and research investment. However, in the cases of Denmark and Ireland under deleterious domestic monetary conditions, weak banking relationships existed. As a result both small states lost an advantage in competing against other states, both small and large.

B. The Interaction Between Labour, Industry and the State

With high levels of international economic vulnerability, small states can less afford to have inflated labour costs and/or needless periods of labour disruption when competing against larger states with greater natural and human resources. Labour unrest can paralyse a major export industry in any state, as evidenced by the effects of strike activity in Italy and the United Kingdom throughout the 1970s and into the 1980s. However, increasing labour costs and excessive strike activity can have a much more serious impact on a small, tightly concentrated, export-led economy than on a larger economy less dependent on foreign commerce and less sensitive to international prices. In the same vein, unsuccessful collective bargaining in a small state may not result in industrial action, but inflated wages damage industries' price competitiveness. For the small European state as an international price taker, these problems simply thwart international competitiveness.

For small states, the ability to possess strong bargaining structures between industry and labour is enhanced by the fact that the labour community can communicate with the advantage of monocephalic centralisation and a relatively small labour pool. With this internal bargaining advantage in comparison to larger states, small states could possibly avert the dual Achilles heels of many large states such as France, Italy, and the United Kingdom: rising labour costs due to mismanaged collective bargaining and periods of industrial unproductivity as a result of labour unrest.

As in all states, the process of interaction among labour, the State, and industry can have either: (1) little negative influence on international competitiveness by maintaining a social compact, but without significant programmes to help labour; (2) a positive influence, where low levels of unemployment and industrial action are complemented by active labour market policies; or (3) a negative influence, where the labour market system is inflexible or the structure is inadequate.

For a number of small European states, there has been the propensity to form social compacts between employers and trade unions in order to avoid needless periods of unproductivity in the face of industrial action. Switzerland, for instance, has been able to avoid labour disputes, and Sweden has also maintained active labour market programmes that act as mechanisms to complement low levels of industrial action. In the Swedish case the trade unions and the major political party, the Social Democrats, have been able to form a Solidaristic Wage Policy, or an "equal pay for equal work" system. In the 1980s active labour market and retraining programmes kept the population employed and trained due to the centralisation of trade union - employers' confederations - industry bargaining. In addition, due to high levels of labour productivity, real unit labour costs remained low.

However, in small states where the interactive process lies somewhere between centralisation and decentralisation, the labour market structure can actually impede international competitiveness, resulting in inflated wages or significant strike activity. Denmark and Ireland, for example, have faced these structural problems and have added to them by continuing to rely on significant benefits for the unemployed without serious reemployment incentives.

Because of its size, the small state would seem to have a collective bargaining advantage, both as a result of strong peak organisation centralisation and the proximity of important labour and industrial actors to one another. Whether the small state could take advantage of this in the 1980s, however, was another question.

C. The Interaction Between the State and Industry

One of the most important means of distinguishing differences in the ways states attempt to achieve higher levels of international competitiveness is the amount of State direct industrial intervention, or the degree to which the State plays a direct role in changing the composition and location of industrial output. The State can play a direct role by developing industrial policies,[75] most easily identified by the two defensive policy avenues of direct sectoral subsidy and nationalisation. However, the State can play other interventionist roles by stimulating industrial competitiveness, namely through targeting, credit mechanisms, taxation schemes, public procurement, regional policies, competition policies, mergers and acquisition policies, and perhaps most importantly, research and development (R & D) programmes. Of course, nearly all macroeconomic and microeconomic policies in some way or another influence the structure of industry. Policies that the government intends for other purposes can also inadvertently have an impact on industry.

Industrial policy weapons vary in name from state to state depending upon levels of economic development, changes in political circumstances, and industrial culture. As was explained earlier in the chapter, small state policy-makers have claimed that their economic programmes have been based on laissez-faire principles as a consequence of their international vulnerability. However, as Robert Ozaki explains,

> ...while specific names and designs may vary, practically all nations have practiced and continue to practice industrial policy of one kind or another. Laissez-faire, or a total absence of industrial policy, has never existed except in the realm of ideological imagination."[76]

For example, in attempting to maintain economic vitality in the face of increasing international pressures, small states have resorted to defensive subsidisation. The State has reacted to help injured industries, sectors, or regions, in most cases as a consequence of their price taker status and vulnerability to a changing international economic environment. Denmark, Ireland, Sweden, and Switzerland have all at one time subsidised injured or declining industries or sectors, and all have policies designed to aid depressed regions.

To varying degrees the State has employed industrial policies to stimulate industrial competitiveness. In Ireland the State has actively attempted to attract inward foreign direct investment, and there continues to be a substantial State enterprise sector. In Denmark, while the State has historically attempted to maintain a "persistently liberal"[77] approach to economic policy-making, the pressures from the world oil shocks and the decline of the Danish economy have forced the State to reconsider its policy options, focusing by the mid-1980s on the development of technology as a means to modernise its industrial structure.

Moreover, membership in the EC has created a very different environment for Denmark and Ireland, as opposed to Sweden and Switzerland, owing to 1) common external tariffs that protect their domestic markets with the powerful security and protection of the twelve EC members (that include such powerful large states as the Federal Republic of Germany, France, Italy, and the U.K.), 2) EC competition policy, and 3) the common EC stance at the GATT. Since Denmark and Ireland have also remained highly dependent on agriculture, the EC's Common Agriculture Policy (CAP) has allowed European interventionism in a major domestic sector in these countries, yet with the political protection of the

Common Market.

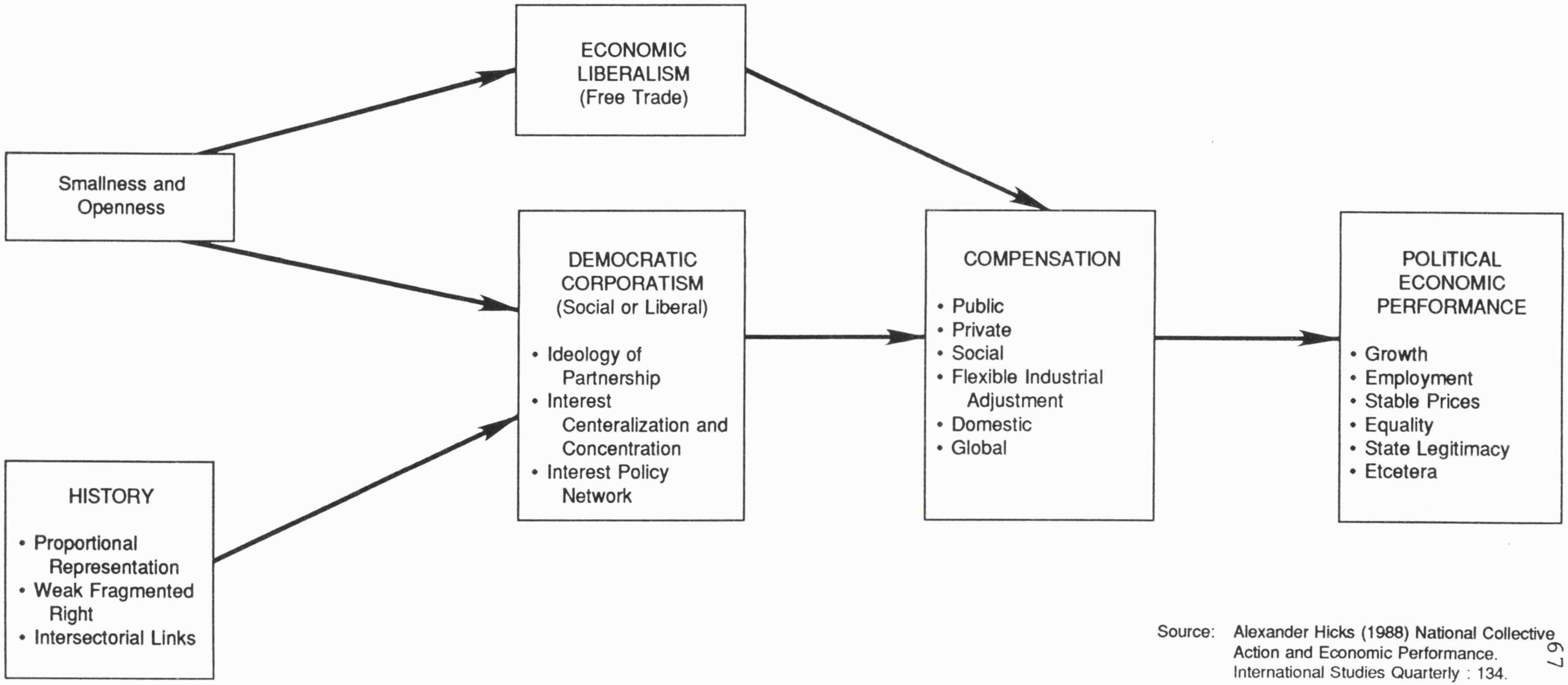
In the more developed and internationally powerful and recognised Swedish and Swiss economies, interventionism has been focused more on labour market policies and monetary policies. Nonetheless, the State has worked closely with each state's principal actor to form state-specific industrial policies that attempt to stimulate industrial competitiveness. Both states to different extents have utilised export credit guarantee programmes, export promotion schemes, and R & D policies. Notably in Sweden, with labour acting as the principal actor, active employment policies have been incorporated with industrial policies in declining regions as a result of shipbuilding closures.

1.6 A Revised Small European State Model

A number of scholars, such as Katzenstein, Cameron, Maier and Schmitter, have advanced the argument that the small European state attempts to achieve its competitive advantage by opting against protectionism and direct intervention; it instead utilises its small size to achieve fluid and effective lines of communication among peak associations, allowing a flexible response to global economic changes. This thesis, however, will take a step beyond this often accepted argument and develop a revised small European state model for international competitiveness during the 1980s. (See Figures 1.12 and 1.13.)

Figure 1.12

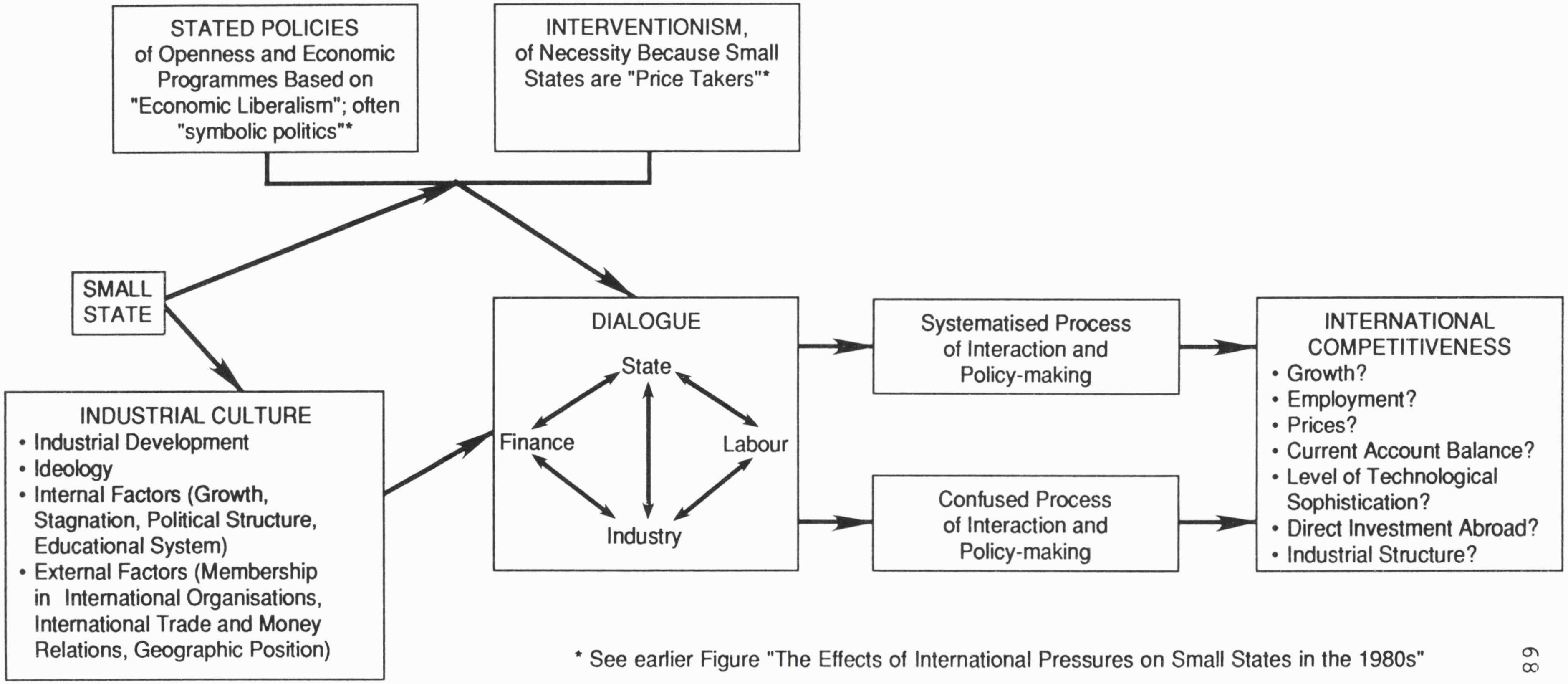
KATZENSTEIN'S SMALL STATE MODEL OF POLITICAL ECONOMIC PERFORMANCE



Source: Alexander Hicks (1988) National Collective Action and Economic Performance. International Studies Quarterly : 134.

Figure 1.13

SMALL EUROPEAN STATE MODEL FOR INTERNATIONAL COMPETITIVENESS IN THE 1980s



* See earlier Figure "The Effects of International Pressures on Small States in the 1980s"

The approach used in this thesis modifies the Katzenstein model in a number of ways, including six revisions.

1. *Symbolic politics and intervention.*

Understanding the politicisation of trade and with increasing international pressures, small state policy-makers during the 1980s directed various forms of compromising rhetoric towards their larger state counterparts, using such phrases as "openness," "economic programmes based on economic liberalism," and "laissez-faire." Such self-characterisations were forms of what Edelman has termed "symbolic politics" towards their larger state counterparts, whose markets remain vital to them and whose international military, political, and economic power overrode their own. With the international political and economic shield of larger state membership in the European Community (as well as the continuing political unity of the twelve member states), the small European state within the EC, unlike the non-EC small European states, was able to use common external tariffs to protect its domestic market. Unlike numerous scholars who have argued that small states are forced to develop programmes based on laissez-faire principles and openness as a result of a comparatively weak international political stature, it is argued here that small state interventionism in the 1980s was indeed consistent with the pressures of the world market and necessary because small state industries were usually price takers.

2. A bargaining process does not necessarily bring success.

There are those who assume that democratic corporatism is the competitive advantage answer to being able to respond flexibly to international economic changes,[78] but merely having a bargaining process did not necessarily breed international competitiveness for the small European state in the 1980s. Denmark faced stagnation, inflation, unemployment, terms of trade deficiencies, a current account deficit, and foreign debt. These economic difficulties, coupled with problems in the structure of both the labour market and its industry, caused Denmark to be less internationally competitive than its Scandinavian partner, Sweden. The question is, Why were countries like Denmark less able to respond to changing international economic conditions than countries like Sweden and Switzerland, who also maintained bargaining or corporatist processes of interaction?

3. Size alone does not bring success.

It is also not assumed in this thesis that all small European states during the 1980s were able to use their size to form corporatist structures. In Katzenstein's *Small States in World Markets*, the "economic success stories" of the small European "corporatist" states such as Austria, the Netherlands, and Sweden were compared. However, small European states like Greece, Iceland, and Ireland, though having populations less than ten million, have had relatively underdeveloped bargaining structures and inferior human (and natural) resources. Were these less industrialised small European states developing bargaining relationships found in more industrialised small states, such as Sweden and Switzerland, as part of the small state competitive advantage, thus producing policy progress that fostered higher levels of international competitiveness?

4. *Industrial culture is a key determining factor for international competitiveness.*

Through their own distinctive interactive systems, small European states could be either aided or bound by their industrial culture, those nationally specific economic, political, and social institutional priorities and values that guide the State and society, both explicitly and implicitly, in either inhibiting or promoting industrial progress. During the 1980s specific strengths or deficiencies in the ability of important actors to communicate with each other either promoted or hindered the small state flexibility necessary to respond to international economic changes. In Sweden and Switzerland the dialogue process ran fluidly and effectively between peak associations. The results for these countries in the 1980s was stable economic growth, low rates of inflation and unemployment, and high standards of living.

5. *Macroeconomic policies developed through interaction act as necessary complements to actor relations.*

The interaction among and the role of key dialogue players - financial institutions, trade unions, employers' confederations, industrial organisations, and government ministries - in the small European state in the 1980s led to the introduction, development, and implementation of a number of active macroeconomic policies geared to enhance productivity, state efficiency, and international competitiveness. To varying degrees of use and success, monetary, labour market, and industrial policies acted as necessary complements to working relations between financial institutions, trade unions, industrial organisations, and the State.

6. *Variances in the communication process influence degrees of success.*

Specific strengths or deficiencies in the communication process among the key actors can either aid or hinder the necessary flexibility of the small European state to respond to changing international economic conditions. In some cases, the small European state has been able to fashion this process of interaction, directed by the state's principal actor, into a system characterised by orderly and effective communication between peak associations and effective complementary policy-making. Unlike what has been argued in the past about the small state advantage of particular countries like Sweden and Switzerland, some small

European states in the 1980s, such as Denmark, have been unable to take advantage of their small size to enhance communication between actors; the dialogue process has not facilitated policy progress or coordination among economic actors. In cases like Ireland, while the State has attempted to develop industrial policies, an unsystematised consultation process has bred incoherent policy-making that has contributed to poor economic performance.

This thesis will therefore test the following hypothesis:

The degree of international competitiveness of the small European state in the 1980s resulted from its internal process of interaction, derived from its industrial culture, which framed national attitudes, goals, and policies that evolved through years of development. The more systematised this interactive process was among financial institutions, labour, the State, and industry, the more flexible the small European state would be to respond to changing global economic and political conditions. Without the capability for dialogue and communication, the internationally vulnerable small European state lost the small state competitive advantage necessary to compete for growing markets against larger states, which possess both natural and human resource advantages. Small state interventionism was not only nationally-specific but also consistent with the pressures of the world market necessary because in most cases small state industries were price takers.

Notes for Chapter One

1.This assumption is more tendentious rather than steadfast.

2.The balance of payments remains perhaps the most important indicator of a state's international competitiveness because it remains the most comprehensive system of recording a country's economic transactions with the rest of the world. The balance of payments also helps to evaluate and forecast the strength of a state's currency.

3.Although grammatical rules dictate otherwise, the term "state" is capitalised when referring to the supreme public power within a sovereign political entity. It is not capitalised when referring to the body politic.

4."Small state," as used in this thesis, reflects David Vital's guidepost for industrialised states with population sizes of less than 10-15 million. Opinions on the exact population size of small states do, however, differ. A study by Jalan on small developing countries placed the number at 15 million. Sutton defines a small state as a country with a population size of one million or less. See Vital (1980) *The Inequality of Nations: A Study of the Small Power in International Relations*: 8; Bimal Jalan (1982) "Classification of Economies By Size" in Jalan, ed. *Problems and Policies in Small Economies*: 39-45; Paul Sutton (1987) "Political Aspects" in Colin Clarke and Tony Payne, eds. *Security and Development in Small States*: 6.

5.This specifically implies the security of the small state.

6.Some have termed this vulnerability as "stress sensitivity:" "the degree to which societal structures are affected by changes in the external environment." See Niels Amstrup (1976) "The Perennial Problem of Small States: A Survey of Research Efforts." *Cooperation and Conflict*: 168.

7.Vital (1980) *op.cit.*: 3.

8.Though there are some notable exceptions, such as Iceland's Cod War against the UK.

9.One might use the following example categorisation of states for purposes of the thesis:

Mini-, micro-, or client- states	Small states
Andorra	Austria
Bahamas	Belgium
Bermuda	Denmark
Channel Islands	Finland
Cyprus	Greece
Faeroe Islands	Iceland
Jamaica	Ireland

Maldives	Israel
Mauritius	Luxembourg
Monaco	Netherlands
Puerto Rico	Norway
Sri Lanka	Portugal

10.See Note 2.

11.David Vital (1971) *The Survival of Small States: Studies in Small Power/Great Power Conflict*: 9; Vital (1980) *op.cit.*: 184.

12.Niels Amstrup (1976) *op.cit.*: 169. Robert O Keohane (1971) "The Big Influence of Small Allies." *Foreign Policy*: 162. As Keohane shows, the best example of this is the international power Israel has developed in its relationship with the U.S.

13.See, for instance, Jorn Levinsen and Peer Hull Kristensen (1983) *The Small Country Squeeze*: 62; Amstrup (1976) *op.cit.*: 167-169.

14.Vital (1971) *op.cit.*: 9-10. The "influence capability" of states is "the degree to which a state can affect or manipulate its external environment." See Amstrup (1976) *op.cit.*: 168.

15.Keohane (1971) *op.cit.*: 167.

16.Security pressures are mitigated through the decision to become neutral, as evidenced by countries such as Sweden and Switzerland, or through alliances with larger states. See Hans H. Indorf (1985) *Strategies for Small-State Survival*. A path-breaking book by Annette Baker Fox showed that alliance-seeking small states must form an association with a greater power as part of a larger strategy. An alliance of small states would certainly fail because the sum total of their aggregate influence was still weakness. See Fox (1959) *The Power of Small States: Diplomacy in World War II*.

17.See Efraim Karsh (1988) *Neutrality and Small States*: 196.

18.Gautam Sen (1984) *The Military Origins of Industrialisation and International Trade Rivalry*: 249.

19.See David Yoffie (1983) *Power and Protectionism: Strategies of the Newly Industrializing Countries*: 18.

20.S.N. Eisenstadt (1985) "Reflections on Centre-Periphery Relations and Small European States" in Alapuro, Risto et. al. *Small States in Comparative Perspective*: 44.

21.See Murray Edelman (1971) *Politics As Symbolic Action: Mass Arousal and Quiescence*. (See particularly Chapter 9.)

22.Katzenstein asserts that "Reliance on political rhetoric ... [is] politically costless." See Peter J. Katzenstein (1985) *Small States in World Markets: Industrial Policy in Europe*: 49.

23.See, for instance, Vittorio Corbo and Fernando Ossa (1985) "Small Open Economies: The Main Issues" in Vittorio Corbo, Anne O. Krueger, and Fernando Ossa, eds. *Export-Oriented Development Strategies: The Success of Five Newly Industrializing Countries*: 5-25.

24.For instance, one could contend that the Swiss pharmaceutical industries do have some price making abilities. See Chapter Two.

25.G.K. Helleiner (1982) "Balance of Payments Problems and Macro-economic Policymaking in Small Economies" in Bimal Jalan, ed. *Problems and Policies in Small Economies*: 166.

26.John C. Conybeare (1987) *Trade Wars: The Theory and Practice of International Commercial Rivalry*: 23.

27.See Michael J. Piore and Charles F. Sabel (1984) *The Second Industrial Divide: Possibilities for Prosperity.*

28.See Joseph A. Schumpeter (1939) *Business Cycles: A Theoretical, Historical, and Statistical Analysis of the Capitalist Process.*

29.Eistenstadt (1985) *op.cit.*: 45.

30.However, much of Irish inward FDI was for export.

31.In the same light, New Zealand is often mentioned in the same breath as Denmark as a result of its highly mechanized agricultural sector. See Sen (1984) *op.cit.*: 2.

32.OECD (1988) *Economic Surveys.*

33.Bhagwati points to two notable economists who have studied the export orientations of Swedish and Swiss multinationals respectively. See Magnus Blomstron (1986) *Swedish Multinationals Abroad* and Silvio Borner (1986) *Internationalization of Industry.*

34.Robert Gilpin (1987) *The Political Economy of International Relations*: 235.

35.See Yoffie (1983) *op.cit.*: 21-22.

36.David Baldwin (1985) *Economic Statecraft*: 41.

37.Klaus Stegemann (1989) "Policy Rivalry Among Industrial States: What We Can Learn from Models of Strategic Trade Policy." *International Organization*: 98.

38.See Murray Edelman (1988) *Constructing the Political Spectacle*: 98.

39.See Paul Krugman (1988) "New Thinking About Trade Policy" in Krugman, ed. *Strategic Trade Policy*: 1-22. Stegemann (1989) *op.cit.*: 86, 97.

40.However, articles 90-92 (EC) limit state aids to industry.

41.See R.C. Hine (1985) *The Political Economy of European Trade*: Chapters 4,5, and 8.

42.Amstrup (1976) *op.cit.*: 176.

43.Ibid.

44.See Michael E. Porter (1985) *Competitive Advantage: Creating and Sustaining Superior Performance*: 1.

45.Andrew Shonfield (1965) *Modern Capitalism: The Changing Balance of Public and Private Power.*

46.See Robert Gilpin (1981) *War and Change in World Politics*: 138-140.

47.Gerhard Lehmbruch (1985) "Neo-Corporatism in Western Europe: A Reassessment of the Concept in Cross-National Perspective." Paper presented to XIIIth International Political Science Congress.

48.Leon N. Lindberg (1984) "The Problems of Economic Theory in Explaining Economic Performance." *The Annals of the American Academy*: 14-27.

49.See Charles Maier (1985) "Inflation and Stagnation as Politics and History" in Leon N. Lindberg and Charles S. Maier, eds. *The Politics of Inflation and Economic Stagnation*: 3-24.

50.See Wolfgang Streeck and Philippe C. Schmitter, eds. (1985) *Private Interest Government: Beyond Market and State.*

51.Alexander Hicks (1988) "National Collective Action and Economic Performance." *International Studies Quarterly*: 132.

52.Lindberg (1984) *op.cit.*: 23.

53.Peter Gourevitch (1986) *Politics in Hard Times: Comparative Responses to International Economic Crises*: 30.

54.See Stephen Skowronek (1984) *Building a New American State: The Expansion of National Administrative Capacities, 1877-1920.*

55.Leopold Kohr (1986) *The Breakdown of Nations*: 69-75.

56.Robert A. Dahl (1982) *Dilemmas of Pluralist Democracy*: 74-80.

57.David R. Cameron (1984) "Social Democracy, Corporatism, and Labor Quiescence In Advanced Capitalist Societies" in John H. Goldthorpe, ed. *Order and Conflict in Contemporary Capitalism*: 143-178.

58.See Mancur Olson (1982) *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities.*

59.Katzenstein (1985) *op.cit.*: 32.

60.See Yoffie (1983) *op.cit.*

61.Hicks (1988) *op.cit.*: 133.

62.Katzenstein (1985) *op.cit.*: 48.

63.Ibid.:79.

64.As in Austria, Denmark, Finland, Norway, Sweden, and Switzerland.

65.Niels Chr. Sidenius (1986) "Comments and Reviews." *Scandinavian Political Studies*: 88.

66.Katzenstein (1985) *op.cit.*: 64.

67.It should be stressed that Katzenstein's two books on small European states, *Corporatism and Change* and *Small States in World Markets*, are referenced throughout the thesis. While there are significant differences between this thesis and the Katzenstein works, broad use is made of his extensive empirical work. Certainly the fundamantal point of agreement is that political economy and history are the most useful analytic tools to analyze the small European state.

68.Derek Unwin and Stein Rokkan (1983) *Economy, Territory, Identity*: 7.

69.Ibid.

70.Ibid.: 40.

71.G.John Ikenberry (1988) "An Institutional Approach to American Foreign Economic Policy." *International Organization*: 243.

72.William M. Dugger (1980) "Power: An Institutional Framework of Analysis." *Journal of Economic Issues*: 898.

73.See John Zysman (1983) *Governments, Markets and Growth: Financial Systems and the Politics of Industrial Change*; and, for a view of both the positive and negative aspects of a developed financial system, see Hyman P. Minsky (1986) "The

Evolution of Financial Institutions and the Performance of the Economy." *Journal of Economic Issues*: 345-353.

74.Zysman (1983) *op.cit.*: 57.

75.Definitions of "industrial policy" vary. Pinder, Hosomoi, and Diebold concisely define industrial policy as a policy that "aims directly to affect the structure of industry." See Pinder, Hosomi, and Diebold (1979) *Industrial Policy and the International Economy*: 67. Similarly, this thesis generally defines industrial policy as a policy imposed by the State that directly changes the composition and location of industrial output. See Chapter Five.

76.Robert Ozaki (1984) "How Japanese Industrial Policy Works" in Chalmers Johnson, ed. *The Industrial Policy Debate*: 49.

77.As discussed in Chapter Five.

78.See Katzenstein (1985) *op.cit.*: 211.

Chapter Two
External and Internal State Priorities, Societal Values, and Industrial Culture in the Small European State

2.1 Characterising Priorities, Values and Industrial Culture

One of the main theoretical challenges of this thesis is to integrate the individual case studies into a manageable framework of concepts; industrial culture is a means to compare underlying factors affecting the international competitiveness of small European states. This chapter will examine the role of industrial culture, which is developed as a result of internal and external factors and is based on state interests and societal values. State interests include measures necessary for a state to maintain or augment its level of international competitiveness, and societal values determine the means by which interests are achieved. This section outlines the way in which industrial culture will be discussed in the chapter.

1. *External and internal conditions affect industrial culture.*

Changing internal and external conditions can actually foster shifts in state interests and societal values.[1] As will be shown in this chapter, these factors tend to cause wide deviation in industrial culture among small states. Internal factors might include the current and historical levels of economic performance (such as growth, stagnation, income distribution, and unemployment) and the state's industrial structure (such as the size and orientation of a state's enterprises). External factors might include resource dependencies, foreign sources of capital, immigration, membership in international organisations, changes in the international economic climate, and international competition itself.

2. Industrial culture reveals societal priorities.

A state's industrial culture reveals its particular social, political, and economic priorities; these undercurrent beliefs or cultural qualities can either progress or hinder the economic vitality of states. As Ralf Dahrendorf succinctly explains, "'Economic performance and cultural values are linked.'"[2] These values may range from egalitarian or social policy-making, to religious influences, to the development of individual human potential. The purpose of examining the industrial culture of the small European state is that it provides an account of the impact of state interests and societal values on the practices of society and on the relationships that exist among its important political and economic actors. Duchene and Shepherd refer to these practices as the "idiosyncratic paths" of states.[3] Industrial culture helps to uncover those underlying elements that have specific effects on states' political-economic performance.

3. *Industrial culture defines actor roles and interaction, leading to state-specific policy preferences.*

Most importantly, a state's state interests and societal values affect the practices of its society by providing "patterned habits of thought learned by individuals performing these roles,"[4] creating,

> a bridge by which timeless values are connected to the surrounding reality .... It is the hymns a community sings to justify and make legitimate what it is doing...."[5]

Societal practices, which typically follow a standard pattern over time, are important to economic actors because they must continually justify their power, role, and behaviour through this set of beliefs or assumptions that constitute the source of their authority. Consequently, societal values define the role that various economic actors - government ministries, industrial organisations, financial institutions, trade unions, employers' confederations, and research institutions - will play in the development of a state's industry.

Due to the monocephalic nature of society in small European states, the interaction among, and the role of, key dialogue players in small European states lead to the introduction, development, and implementation of a number of active macroeconomic policies geared to enhance productivity, state efficiency, and international competitiveness. Policy preferences emerge from social interaction, and society chooses its "preferences as part of the process of constructing - building, modifying, rejecting

- their institutions."[6] For the State itself, the introduction of these policies is a means by which it can achieve the same desired ends for all States: to promote social cohesion and preserve security. Though the goal is the same from state to state, the industrial culture of a particular society determines the means to that end.

4. Industrial culture justifies the role of the principal actor.

When actors in the small European state work together to justify their power, role, and behaviour through a set of beliefs or assumptions that constitute the source of their authority - societal values - then typically a principal actor emerges to set the guidelines by which the state attempts to remain internationally competitive. Remaining the focal point of the economy, the principal actor's formal power is important, but its informal influence derived from community value support is essential in the monocephalic small European state. Hence, the principal actor sets priorities, develops programmes, and implements changes as a result of the power it has garnered through years of development and interaction with other actors.

Most often the State assumes this position, sometimes out of necessity as a result of poor economic performance, such as in Denmark, or a relatively low level of industrial development, such as in Ireland. However, under conditions of successful economic performance in which societal values and actor interaction are clearly enmeshed, the State does not necessarily have to be the principal actor. For example, labour often plays a leadership role in a society when its communitarian values are important, such as in Sweden. Or when a society has complete distaste for governmental intervention and a desire for personal entrepreneurialism, financial institutions play a principal role, as in Switzerland.

Therefore, by examining the industrial culture of the small European state, state interests and societal values can be linked to (a) the practices and interaction among important economic actors and the implementation of policy-making as a manifestation of the state's industrial culture; and (b) the development of the economy under the leadership of a principal actor, a role that evolves through years of interaction among major economic actors. The key points of discussion within this chapter are summarised in the following chart. (See Figure 2.1.)

Figure 2.1

INDUSTRIAL CULTURE: THE CASE STUDIES COMPARED

	DENMARK	IRELAND	SWEDEN	SWITZERLAND
Level of international independence	Moderate	Low	High	High
Number of indigenous industries acting as price makers in the world market	Hardly Any (Canned meat products)	None	Some (Forestry Products)	Some (Pharmaceutical products)
Strength and nature of industrial structure	Weak industrial structure; many niche enterprises, large agro-industrial complex	Weak industrial structure; many state owned enterprises, presence of foreign subsidiaries	Strong industrial structure; presence of several large MNCs	Strong industrial structure; presence of several large MNCs, banks
Level of economic performance in the 1980's (Major problems)	Poor (unemployment, inflation, current account deficit)	Poor (unemployment, inflation, foreign debt, current account deficit)	Excellent (some inflation)	Excellent (low rate of growth)
Political stability in the 1980s	Moderate	Moderate	High	Very high
Primary societal values	Communitarianism, societal equality	Mix between communitarianism and individualism	Communitarianism, societal equality	Individualism, personal entrepreneurialism
Historic attitude towards interventionism (welfare state; industry)	Very strong welfare state values; persistently liberal approach to industrial policy-making	Very strong welfare state values; intervention as a means for industrial development	Very strong welfare state values; intervention to support environment for industry	Preference for limited intervention in both facets

2.2 The Small European State Facing International Vulnerability: Independence vs. Dependence

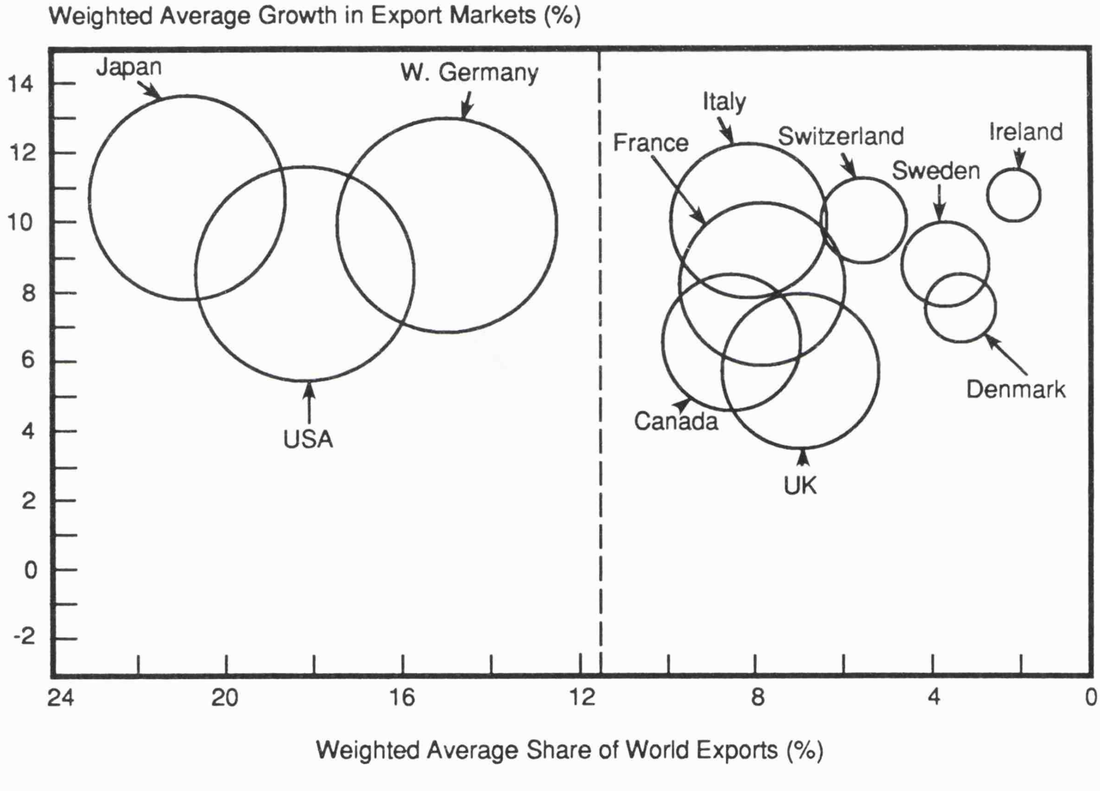
A. The Small European State as the Price Taker

As was discussed in the first chapter, during the 1980s small states were highly dependent on international trade and multinationalisation as a result of their limited producing and consuming markets. As Katzenstein asserts, "Vulnerability in relation to the international economy is an inescapable fact of life for all of the small countries in Europe."[7]

Small state industries tended to be price takers, while larger state industries, which had the ability to control product markets, were price makers. From 1982 to 1987 the Group of Seven Nations (Canada, the Federal Republic of Germany, France, Italy, Japan, the U.K., and the U.S) accounted for most of the world market share of exports. In contrast, small European states had relatively small shares of the world's export market; calculated by a weighted average market share in *The World Competitiveness Report*, Denmark, Ireland, Sweden, and Switzerland accounted for 3.1%, 1.8%, 3.5%, and 5.5%, respectively, of the world's export market.[8] (See Figure 2.2.)

Figure 2.2

THE EXPORT COMPETITIVENESS OF SELECTED INDUSTRIALISED STATES, 1982-1987



Circles proportional to total exports, 1982-1987

Source: IMEDE and World Economic Forum (1989), The World Competitiveness Report: 193.

In terms of particular sectors in the four case studies, throughout the 1980s only in a few circumstances did small state industries, producing either commodity or differentiated products, act as price makers. In both Denmark and Ireland, while having relatively large agricultural sectors that accounted for a significant proportion of their exports, neither had significant world markets shares. The one exception to this was Denmark's canned meat and poultry industry, which held around a twenty percent of world exports in these products.[9] Even with such renowned MNCs as Denmark's Carlsberg and Ireland's Guinness, beer production in Denmark and Ireland combined was less than one percent of the world production total.[10] While the Danish shipbuilding sector was the world's fifth largest in 1985, Denmark accounted for less than one percent of the world production of merchant vessels.[11] Indeed, the industrial structures of both Denmark and Ireland were composed primarily of small- and medium-sized enterprises; as a result, world price making by particular sectors in these states almost never occurred during the 1980s.

In Sweden, there were a few examples of particular sectors that acted as price makers. The backbone of Sweden's industrial portfolio, businesses based on forestry and steel products, accounted for significant world market shares; notably the pulp and paper sector maintained a fifteen percent share of the world's export market.[12] Moreover, several Swedish MNCs had significant shares in the specialised machinery sector. Though the home of the renowned automobile and commercial vehicle manufacturers Volvo and Saab-Scania, Sweden accounted for less than one percent of the world's production and less than five percent of the world's export market of passenger cars and commercial vehicles.[13]

Switzerland remained the best example of a small European state during the 1980s that was able to act as a price maker in particular industrial sectors. While the watch and clock industry was severely affected by international competition from the Far East, Switzerland maintained nearly a thirty percent world export market share in the industry due to its dominance in the high priced watch market.[14] Beyond watchmaking, Swiss industries maintained highly competitive in pharmaceutical products, specialised machinery, and chemicals; Switzerland maintained from ten to fifteen percent of the world's export market in these products.[15]

In sum, Swiss and Swedish industries were more competitive in the international marketplace than Irish and Danish industries, which were almost always price takers. Because of the international presence of Swiss and Swedish multinationals, both Switzerland and Sweden could remain more independently-minded than other small European states, such as Denmark and Ireland, which possessed weak industrial structures.

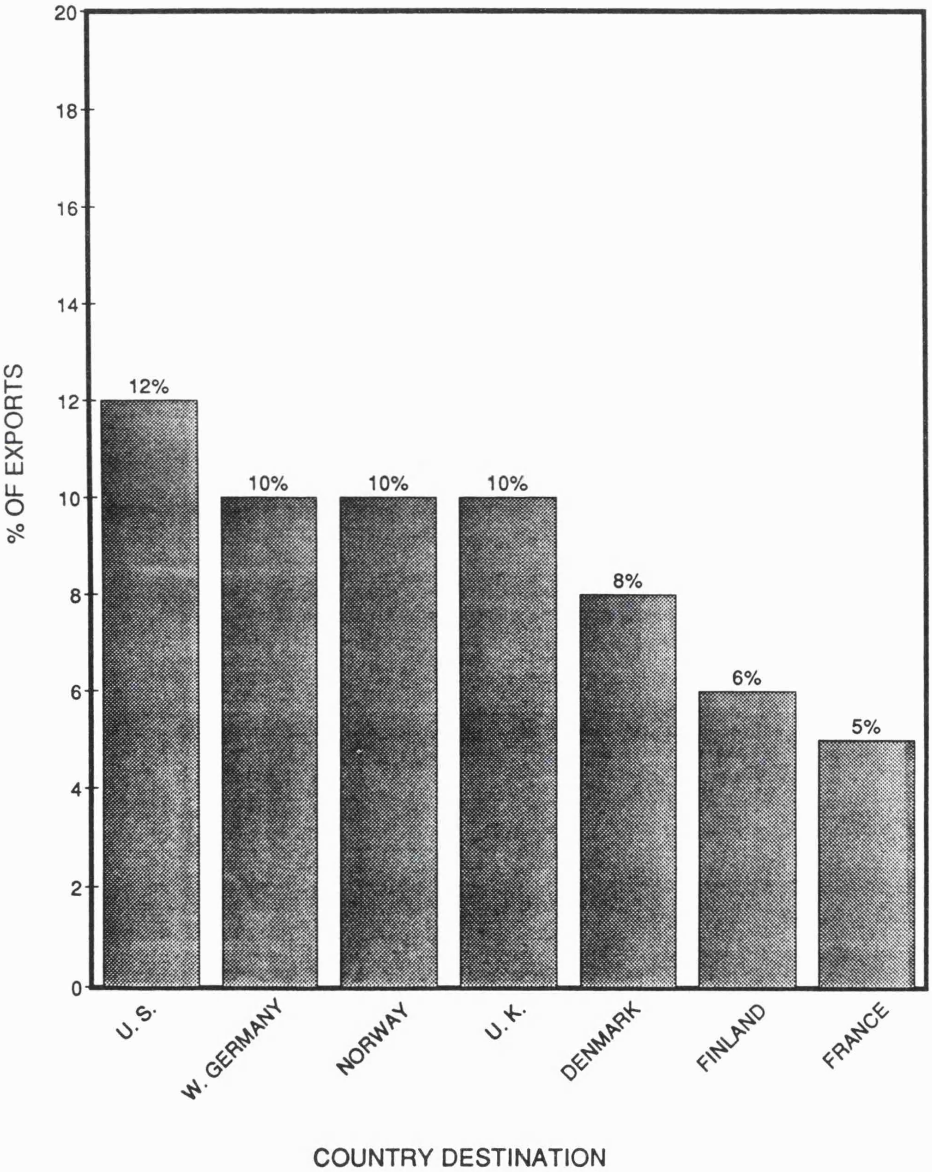
B. Independence vs. Dependence: Comparing the Case Studies

Throughout the 1980s the level of economic and political dependency of particular small European states on other states or international organisations varied. David Baldwin explains in simple terms that the "higher the opportunity cost of severing a relationship, the greater the dependency."[16] Certainly these opportunity costs differed among small European states during the decade.

In the 1980s the significant proportion of not only Danish and Irish, but also Swiss and Swedish, exports were destined for countries within the European market. Maintaining special trading relations with its Scandinavian partners through membership in EFTA and links with the EC, Sweden maintained strong trading links with a select few states. Switzerland remained highly dependent on the West German market. Danish industry exported most of its goods, primarily in the agricultural field, to one trading partner, West Germany. The Irish economy remained highly dependent on Britain as an export market, particularly for agricultural goods; throughout the 1980s over thirty percent of Irish exports were destined for Britain. (See Figures 2.3, 2.4, 2.5, and 2.6.)

Figure 2.3

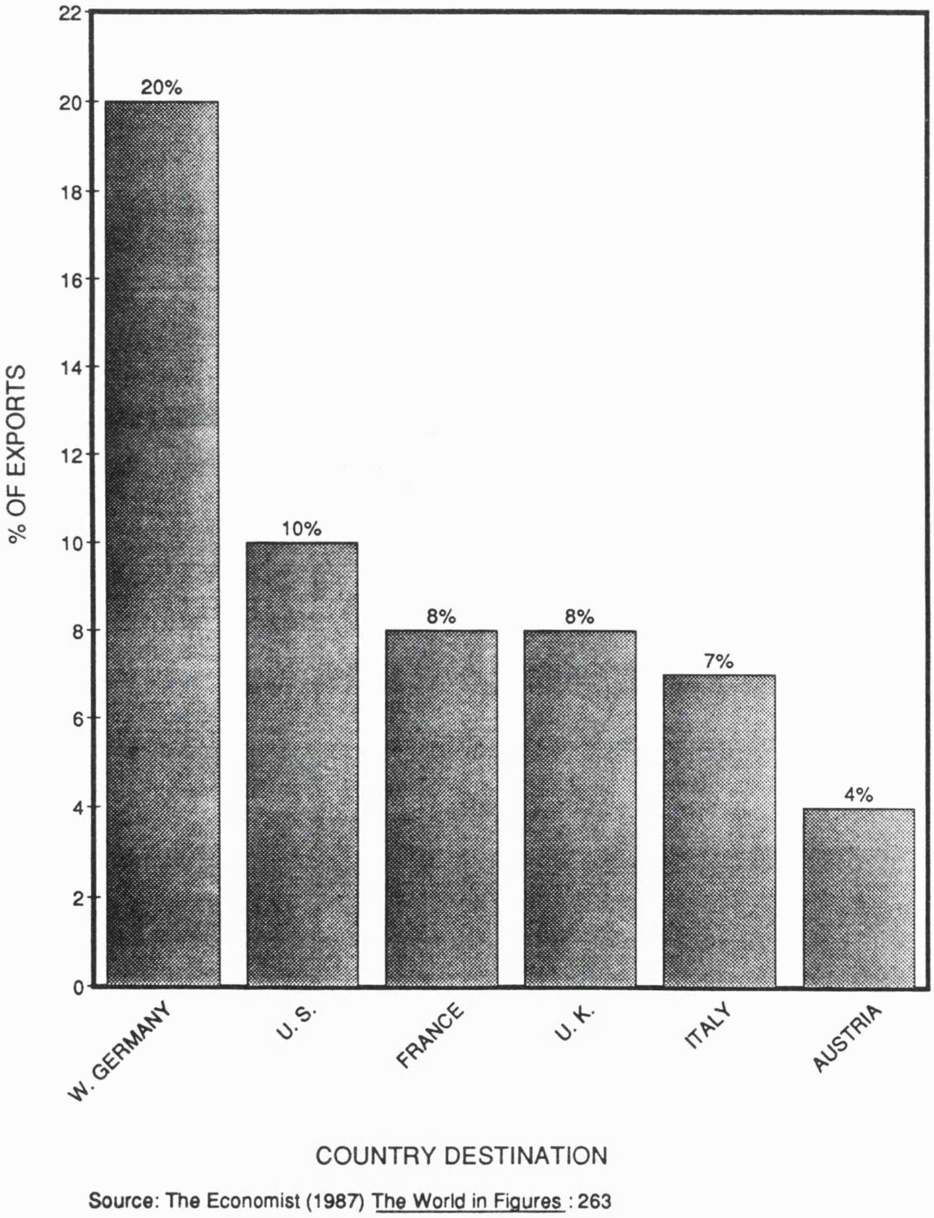
MAIN DESTINATIONS OF SWEDISH EXPORTS
1985



Source: The Economist (1987) The World in Figures : 261

Figure 2.4

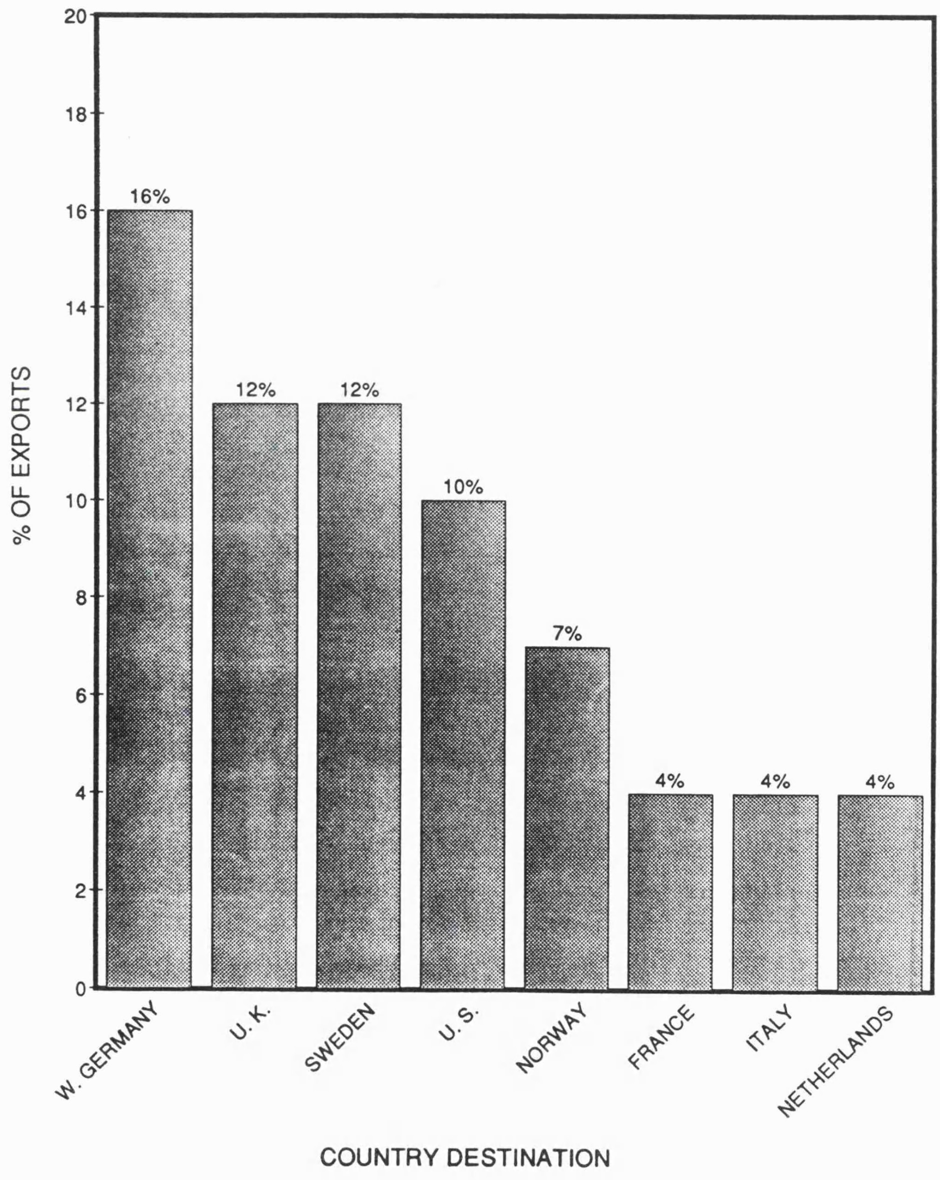
MAIN DESTINATIONS OF SWISS EXPORTS
1985



Source: The Economist (1987) The World in Figures : 263

Figure 2.5

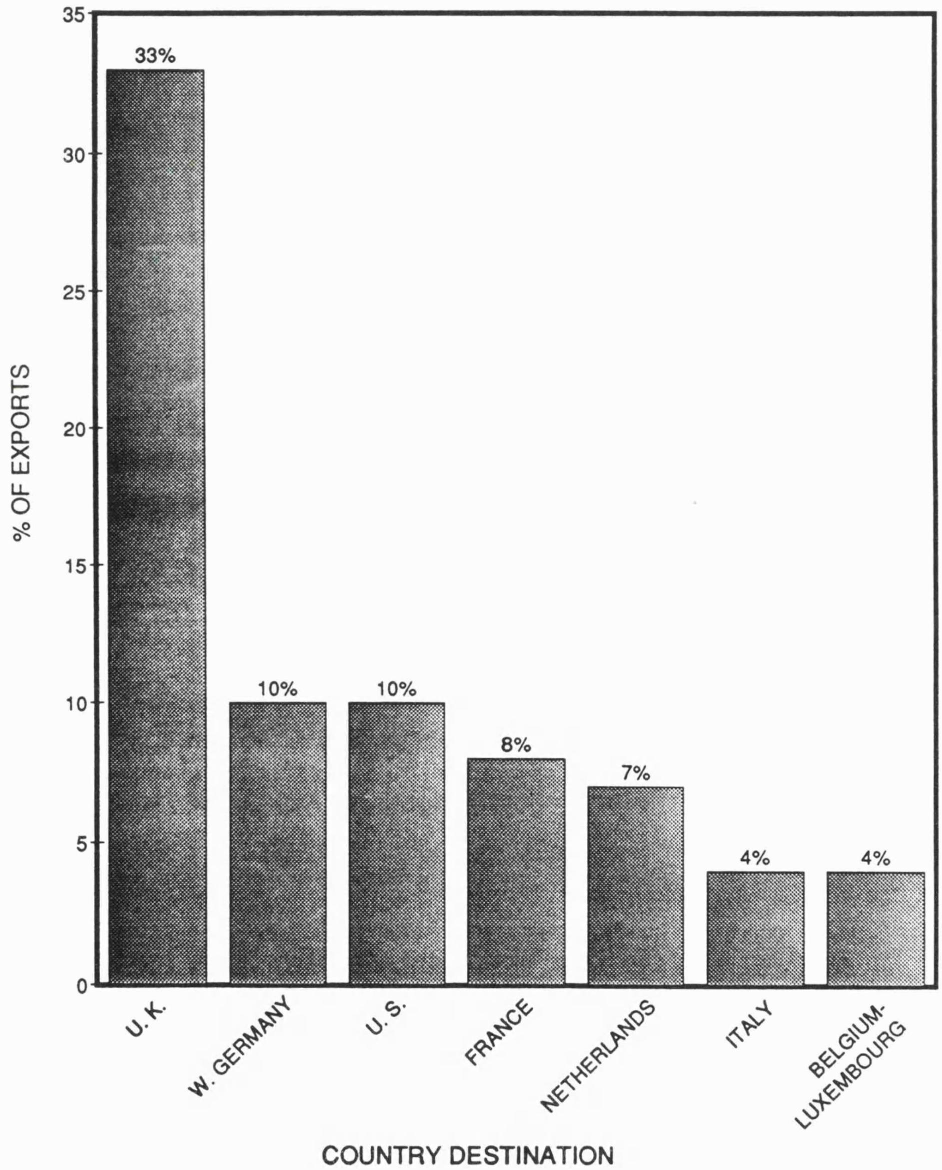
MAIN DESTINATIONS OF DANISH EXPORTS
1985



Source: The Economist (1987) The World in Figures : 220

Figure 2.6

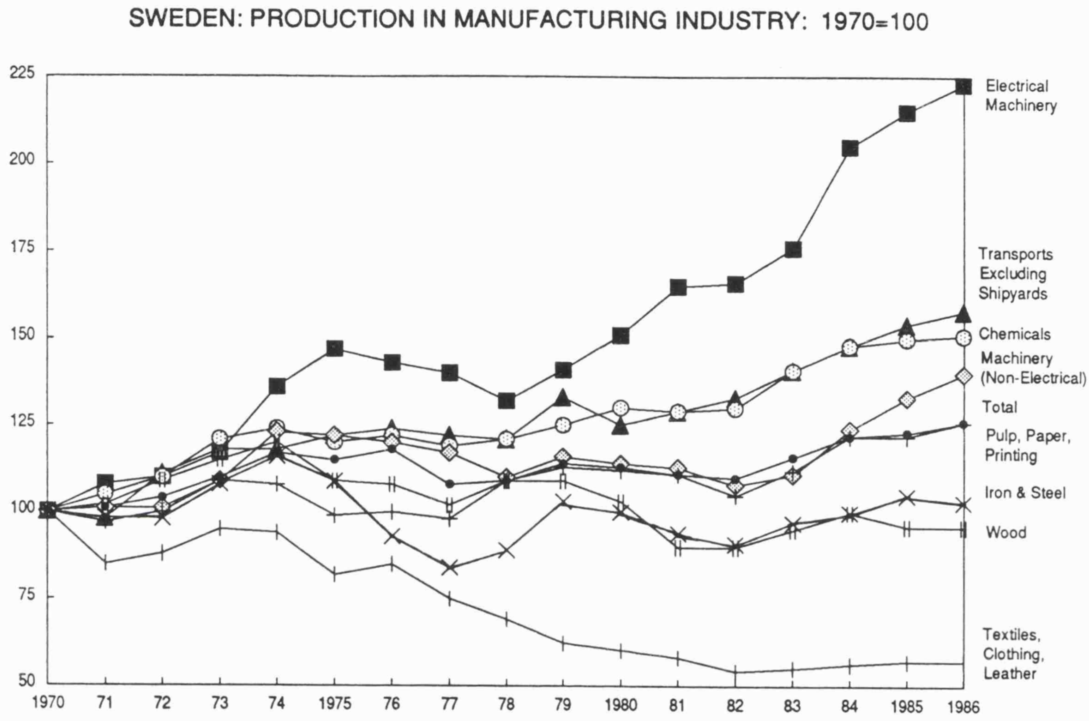
MAIN DESTINATIONS OF IRISH EXPORTS
1985



Source: The Economist (1987) The World in Figures : 237

However, while Sweden and Switzerland maintained trading dependencies, they remained independently minded, as evidenced by their reluctance to join the EC even though other small European states, like Denmark, Ireland, Belgium, and the Netherlands were recipients of financial benefits ranging from four to six percent of their GDPs in 1982.[17] Valuing their independence and autonomy, both the Swedes and the Swiss realised throughout the 1980s that through economic might, political dependency could be avoided. With the dual goals of wealth and peace, Sweden and Switzerland remained two of the world's most economically advanced states, both having powerful financial centres and a number of large multinationals that could compete on a global scale. Both Swedish and Swiss MNCs preferred to grow through foreign development sites, in which profitable subsidiary operations could move beyond national frontiers and where profits would not be limited by a small domestic market. The strategy of these sunrise industries was to sell and manufacture establishments abroad as part of a long-term strategy for maintaining or expanding market shares.[18] (See Figures 2.7 and 2.8.)

Figure 2.7



Source: Svenska Handelsbank (1986) Sweden in the World Economy.

Figure 2.8
Industrial Production in Switzerland, 1985-1986
(1980=100, %)

Sector	1985	1986	Change in %
Machinery	152	164	+ 7.9
Watches	84	94	+11.9
Textiles	119	122	+ 2.5
Foodstuffs	160	162	+ 1.3
Chemicals	304	310	+ 2.0
Metals	134	137	+ 2.2
Printing	190	201	+ 5.8
Total Avg.	164	171	+ 4.3

Source: Credit Suisse (1987) *Swiss Economic Data*.

During the 1980s multinationals excelled in Switzerland through exceptionally high retained earnings, a very sound capital base inspired by strong financial institution-industry relations (see Chapter Three), and far-flung international operations.[19] In Sweden, because of the Solidaristic Wage Policy, which will be discussed in detail in Chapter Four, firms were forced to pay previously agreed, industry specific wages based on centralised wage negotiations. Because of the necessity of firms to pay relatively high wages, the Swedish industrial structure was concentrated by a select number of large multinational enterprises operating in sunrise industries. (See Figure 2.9.)

Figure 2.9
Swedish Manufacturing Establishments By Size and Number of Employees, 1983 and 1985

Size By Employees	1983 A	1983 B	1985 A	1985 B
Under 10	17.2	1.5	24.2	2.3
10-49	56.7	15.5	52.4	15.7
50-99	12.4	11.1	10.5	10.1
100-199	7.5	13.5	6.3	12.5
200-499	4.8	19.5	3.9	17.0
500+	2.5	38.5	2.3	42.2
Total	9220	762,916	12,216	926,654

A= % establishments, B= % employees

Source: Guy Standing (1988) *Unemployment and Labour Market Flexibility*: 13.

In Switzerland, with an industrial structure composed of large, high technology oriented enterprises, a number of

MNCs such as Nestle, Ciba-Geigy, and Hoffman La Roche, not only acted as major employers in Switzerland, but also maintained a significant presence throughout the world. Moreover, Switzerland's large financial institutions, notably its big banks *Credit Suisse*, Swiss Bank Corporation, and Union Bank of Switzerland, were among Switzerland's most profitable companies. (See Figure 2.10.)

Figure 2.10
Top Profitable Swiss Companies (1987)
(In million S.Fr and %)

Company	1987 Net Profits	% Change from 1986
Nestle	1789	+ 2.2
Ciba-Geigy	1161	- 21.1
Swiss Life	781	+ 0.5
Union Bank of Switzerland	776	+ 12.1
Swiss Bank Corporation	674	+ 11.8
Credit Suisse	566	+ 11.6
PTT	554	+ 53.9
Sandoz	541	+ 2.3
Hoffmann-La Roche	416	- 7.9
Holderbank	239	+ 42.8
Migros	210	+ 20.7
Jacobs Suchard	191	+ 26.9
Winterthur Group	172	+ 21.7
Swiss Re	145	+ 20.8
Pirelli Group	141	+ 39.6
Zurich Insurance	141	+ 14.0
Coop Insurance	129	+ 18.3
Patria Insurance	128	+ 5.8
Swiss Volksbank	116	+ 15.0
Surveillance	112	+ 17.1
Brown Boveri	96	- 11.9

Source: "Top Profit Makers Throughout the Country" (1987) *Swiss Business*: 13.

Similarly, in Sweden the twenty largest MNCs accounted for almost half of the Swedish employment during the 1980s. Of the twenty, basic industry (the ten largest raw material companies) formed 20% of employment, while other major sunrise industries accounted for the bulk of the rest. Since 1982, sunrise industries, especially in electrical machinery and transportation flourished. The major sunrise MNCs included Volvo (transportation); Ericsson (electronics); Asea (energy); Saab (transportation); Pharmacea (pharmaceutical products); Atlas Copco (compressors and drilling equipment); Electrolux (vacuum cleaners and motor saws); SKF (ball bearings); Astra (pharmaceutical products); Sandvik (drills and cutting tools); AGA (tube gas); Swedish Match (matches and lighters); and Alfa Laval (dairy equipment).

Sweden's and Switzerland's small domestic markets meant that offensive, expansionary direct investment programmes remained the key to economic power. (See Figure 2.11.)

Figure 2.11
Swedish Direct Investments Abroad and Foreign Direct Investments in Sweden (Approximate) By Permits Granted
(In 1000 million S.Kr.)

Year	Swedish Direct Investments Abroad	FDI in Sweden
1976	3.80	.52
1977	4.50	.70
1978	3.20	.80
1979	3.80	.80
1980	4.00	1.20
1981	6.80	1.35
1982	9.50	1.60
1983	13.00	2.80
1984	16.00	3.00
1985	20.00	7.00

Source: Svenska Handelsbank (1986) *Sweden in the World Economy*: 14.

Much of Swiss FDI during the 1980s remained in the U.S., where overall direct investments by Swiss interests accrued up to $1.21 billion by the end of 1986.[20] FDI in West Germany, second only to the U.S., expanded significantly: in 1985 Swiss FDI totalled 537 million Deutschemarks (DM), in 1986 975 million DM, and in 1987 12,730 million DM.[21] Moreover, the overseas orientation of Swiss MNCs was evidenced by the record of the six largest (Nestle, Ciba Geigy, Hoffmann La Roche, Alusuisse, Asea-Brown Boveri, and Sandoz): all together they had seventy-one to ninety-five percent of their employees abroad and sales abroad accounted for sixty-three to ninety-six percent of their totals in 1986.[22] Foreign direct investment by Swiss companies totalled 41.0 billion S.Fr. in 1983, 46.0 in 1984, 50.5 in 1985, and 52.0 in 1986, as compared to 20.9 billion S.Fr. by foreign firms operating in Switzerland in 1985 and 22.0 in 1986. Moreover, in 1986 forty percent of all acquisitions in Switzerland involved the takeover of a foreign company by a Swiss concern.[23]

As a result of such powerful industrial structures, for Sweden and Switzerland, political and economic independence coupled with national autonomy, remained an overriding goal, as evidenced by their reluctance to consider joining the EC. Indeed, the EC offered trade policy options not available to those outside the Common Market, yet it continued to stand as a threat to its members (particularly small states with limited economic and political clout within the organisation) of compromising national autonomy and independence for these benefits.[24]

Because of their economic power extending beyond their geo-political influence, Sweden and Switzerland maintained relatively passive foreign policies based on neutrality. Both governments continued their commitments to the developing world and their roles as mediator for diplomatic negotiation among the world's most formidable powers.[25] For the most part, small during the 1980s European states preferred to rely on political deterrence as opposed to military defence, illustrated by most small European states[26] spending less than one-half the per capita expenditures of larger states on defence. As Katzenstein explains, "... interest in a reduction of international tensions stems from the awareness that security is best served by a general orientation towards war avoidance."[27] As a result, with some notable exceptions (such as Denmark), small European states such as Sweden and Switzerland maintained foreign policies based on neutrality.[28]

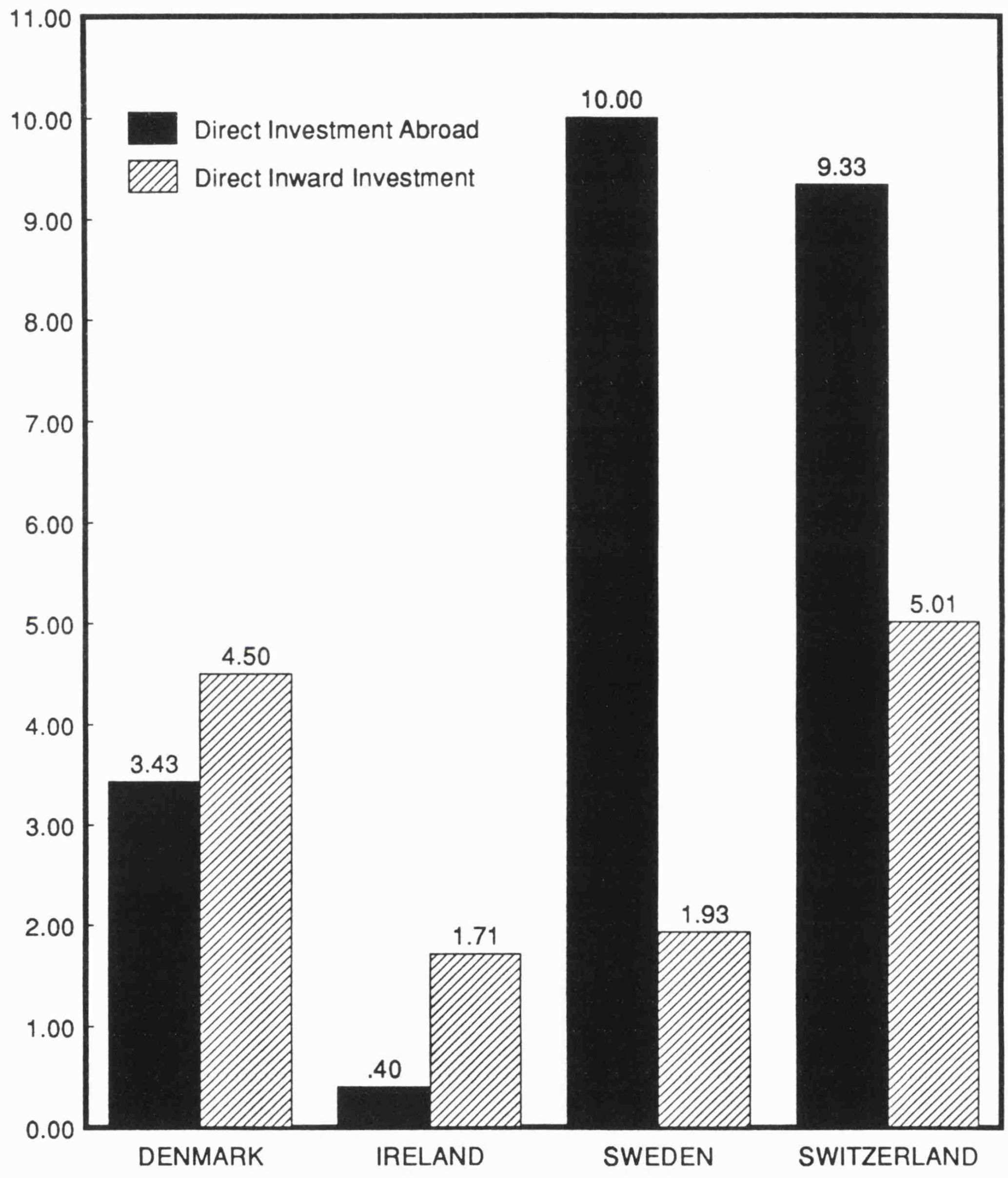
For other small European states such as Denmark and Ireland, dependency as a result of poor economic performance as well as weak industrial structures made them more reliant on outside sources of support, such as the EC. For Denmark, its agricultural sector significantly overshadowed the importance of industrial production; among twenty-two OECD countries, Denmark ranked fourth in 1986 in terms of agricultural production (value added per capita), first in terms of the growth in food production from 1984 to 1986, but last in terms of the importance of industrial production (as a percentage of GDP).[29]

As a result of Denmark's high dependence on agriculture, its industrial structure was composed primarily of small- and medium-sized enterprises. Among Denmark's twenty-five largest companies between 1984-1987, nearly half were involved in some form of agricultural activity. Denmark's largest enterprises included *Mejeriselskabet* (milk products), Carlsberg (beer), *Skandinavisk Holding* (agricultural conglomerate), *Dansk Landbrugs Grovvareselskab (processed sugar beets),* Tulip Slagterierne (slaughter-house), *Superfos* (fertilisers), and *Korn- og Foderstofkompagniet* (agricultural products). Outside of agriculture, Denmark's largest companies in the 1980s were involved in banking (e.g., *Den Danske bank*, *Privatbanken*), air-borne traffic (Scandinavian Airlines), and trading operating (East Asiatic Company).[30] However, in comparison to both Swedish and Swiss multinationals, even the largest Danish enterprises were significantly smaller; as a result, Danish outward FDI was also less substantial. From 1980 to 1987, while Denmark and Sweden had comparable standards of living, Denmark's level of FDI abroad was five times smaller than that of Sweden.[31] (See Figure 2.12.)

Moreover, Ireland's geographic semi-peripheral location and the necessity for Irish industry to participate in the global marketplace forced the State to move from an isolationist stance to an internationalist one in order to develop its economy.[32] With transatlantic cultural ties, the Irish summoned their New World families for assistance by appealing to U.S. industry to invest directly in Ireland.

Figure 2.12

DIRECT INVESTMENT ABROAD AND DIRECT INWARD INVESTMENT, 1985 - 1987 FOR SELECTED STATES (AS % OF GROSS FIXED CAPITAL FORMATION)



Source: IMEDE and The World Economic Forum (1989) The World Competitiveness Report: 154, 156; Department of Finance (1988) (Ireland) Economic Statistics, December.

Realising the advantages that American industry could provide to the Irish economy, the State imposed a policy of openness coupled with investment incentives. However, as James Wickham properly explains, while Ireland began to industrialise after its protectionist period that ended in 1958, the introduction of foreign-owned firms into the Republic signalled "a clear example of dependent industrialisation."[33]

Indeed, throughout the 1980s Ireland's indigenous industrial structure was composed primarily of small- and medium-sized enterprises, mainly in the agricultural field. Among these, many of Ireland's largest companies were State-owned (e.g., ESB, *Telecom Eireann*, *Aer Lingus*, *Siuicre Eireann*). Even the size of its largest companies, such as Jefferson Smurfit Group, Dunnes Stores, Guinness Ireland, and Waterford Glass, were extremely modest by international standards.[34] With perhaps one exception (Jefferson Smurfit), none of Ireland's enterprises ranked among Europe's largest two hundred companies. Indeed, Ireland's GDP was the smallest in the OECD, one-fifth the size of Sweden and Switzerland and one-third the size of Denmark.[35]

Moreover, while Sweden and Switzerland enjoyed relative economic success during the 1970s and 1980s, the international recession at the beginning of the 1980s had dire consequences particularly for economy of Ireland, but also for Denmark, causing significant economic decline and reliance on outside sources of aid, most notably the EC.[36]

Since the inception of the EC in 1957 under the Treaty of Rome, Sweden and Switzerland have eschewed membership. While throughout the 1980s the Common Market offered unique trade policy options for member states, neither wished to risk their political autonomy (and neutrality) for these economic benefits, since both maintained stable economic and political systems without EC assistance. However in 1973 both Denmark and Ireland (along with Britain) joined the EC to a large degree because of both state's dependence on the British market. (See Figures 2.5 and 2.6.) Danish and Irish policy-makers understood, nonetheless, that membership could limit their future economic independence and political autonomy.[37]

Paradoxically, while Denmark hoped to capitalise on the apparent gains from EC status, including Common Agricultural Policy (CAP) benefits and foreign exchange stability as a member of the "snake,"[38] the sharp oil price increases in late 1973 caused a swift fifteen percent deterioration of Denmark's terms of trade. Competing in a larger market, Ireland's industry struggled economically from the increased competition, yet began to enjoy some of the same benefits of membership that Denmark was enjoying, such as agricultural subsidies granted through the CAP.[39] Moreover, joining the EC provided Ireland and Denmark with a means to attempt to reduce their unilateral dependence on their major trading partners, the UK and the Federal Republic of Germany respectively.

With Denmark and Ireland receiving such significant aid from the EC, and with little to contribute to other states within the Common Market, the Irish, and to a lesser extent the Danes, developed a role of being the *demandeur*.

> [This] strategy refers to the attempt to extract special concessions from the Community on the basis of Ireland's particular circumstances, namely the fact that it was poorer and economically less developed than other members of the EEC.[40]

To the average Irish and Danish farmer, the EC was a source of funds; they perceived themselves as being worthy recipients, but not patrons. As stated in an article in the *Irish Independent* on the "Eurogravytrain," "Mention the EC to the average punter and they will yawn ... unless you mention EC money."[41]

C. Summarising Differences in Small European State International Vulnerability: Independence vs. Dependence

In summary, the four case studies illustrate how small European states differed in the 1980s as to how they dealt with the vulnerability caused by their limited international political and economic influence. For Sweden and Switzerland, strong commitments to independence were preserved both through globally powerful multinational corporations and financial institutions that provided economic might, and relatively neutral foreign policies that avoided hostility from more economically and politically powerful states while at the same time preserving domestic political autonomy.

With unsatisfactory economic performance relative to Sweden and Switzerland, Denmark and Ireland remained highly dependent small European states, evidenced by both joining the European Community in 1973 and by their reliance on a single trading partner, namely Ireland with Britain and Denmark with West Germany. In Denmark, a relatively weak industrial structure and economic misfortune in the 1980s caused Danish policy-makers to view the EC as a means to overcome economic problems, illustrated by Danish dependence on the CAP. At the same time, unlike the other three states, which were relatively unburdened by defense issues and whose policy-makers focused primarily on economic performance, throughout the 1980s Denmark faced foreign policy pressures from western allies, as well as from within the Danish state, as to its defense posture and NATO commitment. In Ireland, a desire for economic development fostered an industrial structure that was dependent on both foreign-owned subsidiaries and the benefits accrued from EC membership.

2.3 Economic Performance: The Principal Internal Condition Affecting Industrial Culture

For the most part, the single most important internal condition affecting any industrialised state's industrial culture is its level of economic performance. The oil crises in 1973-1974 and 1978-1989 ushered in the new decade with extreme external turbulence that resulted in an international recession throughout all European states, small and large. (See Figure 2.13.)

Figure 2.13
Growth in Large European States and USA (% Change per Annum)

	1966-1970	1971-1975	1976-1980	1980	1981
FRG	4.5	2.2	3.6	2.1	-0.3
France	5.4	4.0	3.3	2.0	0.3
Italy	6.2	2.5	3.8	3.8	-0.2
Britain	2.5	2.1	1.3	-3.0	-2.2
USA	3.2	2.7	3.7	-0.1	2.0

Source: Stephen Wilks and Kenneth Dyson (1983) "The Character and Context of Industrial Crises." in Dyson and Wilks, eds. *Industrial Crisis*: 10.

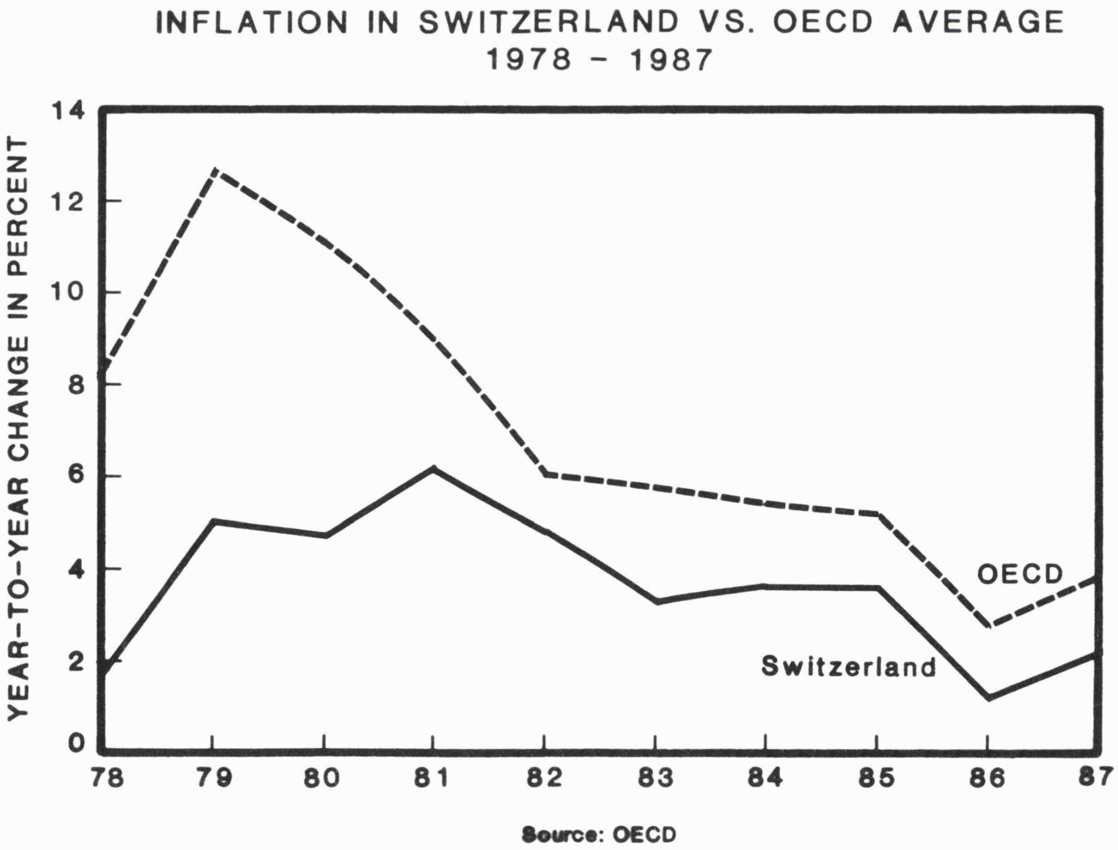
While some small European economies were less affected than others by the international shocks, the international economic instability at the beginning of the decade resulted in political upheaval and consequent regime change in most small European states. To varying degrees the four case study economies were negatively influenced by the international recession; when they did experience a significant decline in their level of international competitiveness, a regime change resulted.

The least affected of the four case studies from the international recession was the Swiss economy, which defied the Phillips Curve by avoiding unemployment problems in the 1980s due to both the high levels of industrialism and entrepreneurialism, as well as the cultural bias against personal laziness. Unemployment remained at the lowest relative levels in the OECD; in a work force of about 3.1 million, only some twenty to twenty five thousand persons per year were without jobs throughout the 1980s, due in part to migrant worker employment.[42] (See Figure 2.14.)

Figure 2.14

Moreover, as will be discussed later in this chapter, throughout the decade the inflation rate in Switzerland was the major priority of the Swiss State and was controlled through strict monetary means. (See Figure 2.15.) It has often been suggested that an increasing rate of inflation in Switzerland has an adverse effect on favourably passing governmental policies. Schneider, Pommerehne, and Frey determine in their article on "politico-economic independence in Switzerland" that " ... the Swiss government undertakes a restrictive policy in order to combat inflation when it considers the level of the electorate's support for it to be too low."[43] While Switzerland experienced relative economic and political stability throughout the decade, Sweden, Denmark, and Ireland were less economically, and therefore, politically stable. All three experienced government changes in the beginning of the 1980s, much as a result of internal economic problems.

Figure 2.15



Between 1976 and 1982 Sweden was governed for the first time in several decades by a government not from the Social Democratic party (SAP), the reasons for which are discussed in detail in this chapter and particularly in Chapter Five. However, much as a result of international economic pressures resulting from the oil shocks during this period, Swedish economic performance declined. The recessionary problems others in the OECD experienced also occurred in Sweden. (See Figure 2.16.) Sweden had one of the highest budget deficits in the OECD, lower manufacturing output than it had ten years perviously, and among the highest tax rates in the world; public disaffection with declining Swedish international competitiveness allowed the SAP to regain power in 1982.[44]

Figure 2.16
Changes in Economic Growth, Sweden/OECD 1976-1982

Year	OECD Annual Rate of Change, GDP	Sweden, Annual Rate of Change GDP/	Industrial Production/	Investment
1976	5.2	1.5/	-0.8/	0.2
1977	3.7	-2.4/	-5.4/	-17.1
1978	3.9	1.3/	-1.7/	-21.7
1979	3.2	4.3/	6.3/	3.4
1980	1.3	1.9/	0.4/	19.2
1981	1.4	-0.9/	3.6/	-8.6
1982	-0.3	-0.1/	-0.1/	-17.0

Source: Andrew Martin (1987) "Wages, Profit, and Investment in Sweden"in Leon N. Lindberg and Charles S. Maier, eds. *The Politics of Inflation and Economic Stagnation*: 430.

Throughout the rest of the decade, Sweden's economic performance was excellent, with growth remaining steady, unemployment at low levels, and the current account in surplus. Only inflation inspired by wage drift and increasing consumer spending, remained a threat to overall economic stability. (See Figure 2.17.)

Figure 2.17

Source: Medium Term Survey of the Swedish Economy, Ministry of Finance: 169; Global Analysis Systems, Country Risk Report - Sweden, October 1987

In Denmark and Ireland, however, economic performance was relatively poor. In 1981 inflation in Denmark hovered around ten percent, while in Ireland it remained around sixteen percent. In the same year, unemployment was eight to nine percent in Denmark; in Ireland it ran as high as twenty percent.[45] (See Figure 1.2.)

While the Danish standard of living remained relatively high, with its GDP per capita ($16,130) being greater than its Scandinavian neighbour Sweden, it continued to face a mammoth external debt. Since the mid-1970s Denmark's external debt climbed to forty percent of GDP (exactly as bad as Brazil's) and one-hundred and forty percent as a proportion of its exports.[46] In Ireland the standard of living remained significantly below the OECD average, and like Denmark, it too faced significant debt troubles. (See Figures 2.18 and 2.19.)

Figure 2.18
Denmark's External Balance, 1975-1985 (% of GDP)

Year	Trade Balance	Net Foreign Debt
1975	-8.3	12.4
1976	-4.9	16.1
1977	-4.0	20.5
1978	-2.0	21.0
1979	-3.1	24.7
1980	-1.1	26.7
1981	-1.7	30.5
1982	-1.4	33.0
1983	0.4	36.0
1984	-0.4	38.9
1985	-1.3	40.0

Source: The Institute for Future Studies (1987) *Growth Policies in Nordic Perspective*: 350.

Figure 2.19
National Debt in Ireland, 1973-1985 (as % of GDP)

Year	Total Debt	Foreign Debt	Debt Service
1973	60.0	6.2	5.6
1975	74.2	15.4	6.5
1979	88.5	20.9	8.4
1981	96.5	46.6	9.5
1983	120.1	65.9	12.5
1985	133.6	67.9	14.5

Source: Barry Brunt (1988) *The Republic of Ireland*: 8.

In both states, much as a result of declining levels of international competitiveness, regime changes occurred. In Denmark, a combination of factors, including the oft-debated EEC issue, the fragmentation of the political centre, the splitting of the old Left, and perhaps most important, weakened economic performance brought about a change of regime in 1982. The Social Democrats were removed by a coalition of conservatives in a distinctive system of proportional representation that meticulously divided party representation yet as a result brought extreme political fragmentation.[47] Nonetheless, during the period 1983-1985 Denmark experienced decreased levels of inflation and unemployment, lower interest rates, and growth. This period was followed by extreme wage increases that overcame the significant progress achieved during the previous years.

In Ireland, poor economic performance in the beginning of the 1980s contributed to the downfall of the *Fianna Fail* government and the formation of a national coalition government headed by the *Fine Gaels*.[48] Nonetheless, with

Ireland continuing to face declining levels of international competitiveness, the *Fianna Fails* garnered enough support under their *Programme for National Recovery*, an agreement that would attempt to spur Ireland's economy through wage moderation, budget spending cuts, and investment incentives, to reclaim enough power to lead a national coalition government.

In summary, this section has reviewed the level of economic performance in each of the four small European states. It has also illustrated the relationship that existed between national economic performance and regime change among small European states in the 1980s. In Switzerland, economic stability was coupled with political stability, even in the face of the international recession at the beginning of the decade. In Sweden, however, the oil shocks of the 1970s and their consequent deleterious effects on the Swedish economy allowed the SAP to remove the then-governing centre-right coalition in 1982. Throughout the remainder of the decade in Sweden, the economy flourished and the SAP maintained solid political support. In Denmark and Ireland, however, declining levels of international competitiveness at the beginning of the 1980s and throughout the decade spurred several elections and regime changes.

2.4 Societal Value Differences Among Small European States

While the former section examined state priorities, this section will analyze the effects of societal values on the industrial culture and subsequent policy development in the small European state during the 1980s. While values differ from the top industrialist down to the lowest paid worker in any society, pervasive community attitudes and values can either hinder or augment industrial development.

Because of the small state's limited international political and economic power relative to large states, as well as its high level of dependence on foreign markets, policy-makers in these countries during the 1980s expressed their favour of both openness and economic programmes based on laissez-faire principles. However, under extreme global economic pressures, such as the oil shocks of the 1970s and the consequent recession of the early part of the 1980s, the State in the four case countries reverted to defensive subsidies for declining industries. In addition, even with these self-characterisations of openness and economic liberalism, various government policies were introduced, developed, and implemented in each of the case countries. Interventionism, though different among small states, was a necessity because of international pressures, the state's position as a price taker, and the sustenance or revitalisation of the state's level of economic performance.

The study of cultural relativism, which presumes that differences in societal action can be explained from differences in culture, has fostered the growth of "industrial culture relativism," which presumes that State policies and programmes towards industry differ according to cultural values. For example, in assessing the attitudes of various societies in terms of State intervention, Dyson asserts that,

> The Americans are disposed to a radical equation of 'crisis intervention' with 'socialism', the British are inhibited by a deep cultural aversion to 'interference' with the firm. In continental Europe, the State assumes the responsibility for managing industrial crises, either by direct and detailed intervention or by a public regulation of private sector management of crises.[49]

As the Dyson quotation illustrates, size similarity among states does not necessitate societal value unanimity, either among large states or among small ones. One need only return to the numerous internal and external factors described earlier to understand such deviations. For example, even though Japan and the United States are large states, in the early 1980s attitudes towards governmental intervention in these countries differed significantly, while the government in power enjoyed relatively high degrees of popularity. The political stability of Japan, evidenced by the perpetuation of political power by the hegemonic Liberal Democratic Party (who were given much credit for the growing Japanese economy) during the 1980s, illustrated a positive public attitude towards the government's handling of economic programmes, which included a number of strait-jacket, highly interventionist industrial policies.[50] On the other hand, the popular Reaganomics doctrine glamorised decreased intervention (though not a retreat from policy-making itself).[51]

For the small European state, societal values can differ dramatically as well. For example, the "work ethic" of a society, which directly affects its productivity, is defined as "a value or belief (or a set of values or beliefs) concerning the place of work in one's life that (a) either serves as a conscious guide to conduct or (b) is simply implied in manifested attitudes and behavior."[52] When workers are victims of complacency or selfishness as a result of an attitude of dependency and ill-fatedness, a trait often considered a cause of the problems of Denmark and Ireland, economic stagnation can ensue.[53] On the other hand, when states actively seek to maintain autonomy and independence through economic might, as exemplified by the Swedish and Swiss cases, industrial productivity is often enhanced through labour diligence.

Beyond work ethic, other societal values and priorities in small European states might include "communitarianism" and the successful maintenance of a welfare state, such as in the Scandinavian countries; "individualism" and a cultural bias against welfare dependency and inter-generational poverty, such as in Switzerland; relatively liberal, non-restrictive social policies, particularly prevalent in the Netherlands and the Scandinavian countries; relatively restrictive social policies due to the significant influence of the church, such as in Belgium and Ireland; and relatively high levels of international independence, such as the reluctance of Sweden and Switzerland in joining the European Community. These values affect the way in which the State makes policy, the ability of finance and industry to work together, the method that labour employs to maintain a unified voice, and the emphasis private industry places on becoming more technologically advanced.

A. Societal Values and Priorities Among the Case Studies

Among the four case studies, Switzerland is the best example of a state determined to maintain independence despite an incomparable degree of national diversity, evidenced by four national languages - French, Italian, Romansh, and Swiss-German (*Schwyzertusch*); the two majority faiths, Protestantism and Catholicism, having roughly equal numbers; and significant cultural differences between those in the French, German, and Italian regions. Although the members of the confederation had little in common when Switzerland was originally formed, their determination to lead an independent life, aggressively averting the imposition of foreign laws and foreign taxes, overshadowed these differences. Even with linguistic, religious, and cultural differences, problems that have led to significant internal strife in other small European states such as Belgium and Ireland[54], such impediments to unity have been overlooked in the Swiss system of federalism, based on *foedus*, which means "treaty" under a confederation of territories. Internal unity among its cantons, driven by a socio-cultural aspiration to preserve an affluent and peaceful community, explains why some have justified the existence of the confederal structure as a marriage of convenience. Through Swiss confederalism, the power of the central government has remained limited.[55]

Throughout the 1980s Swiss industrial culture was based on the nationally pervasive attitude that through market competition and personal entrepreneurialism, a society of strong individuals would foster national economic wealth. National prosperity was translated though the affluence of individuals; society itself may become affluent, but only through individual, not community, industrialism. (A poignant reminder of the Swiss commitment to economic success was the rejection of a referendum proposal in the latter part of the 1970s to reduce the working week from forty-two to forty hours.[56])

The Swiss maintained that the State should have a limited role in both society and industry, having an almost passive position in aiding the welfare of both the individual and the enterprise. Because of the State's limited intervention in either providing welfare or industrial aid, "'old time religion' has dominated and still dominates Swiss fiscal policy: public accounts must be balanced, and public monies should not be squandered."[57]

With their intense belief in the individual and capitalism, during the 1980s the Swiss State provided limited aid to industry through direct intervention. The State only once provided significant defensive subsidies to an industry since the Second World War, notably the watch industry, and in comparison to the national power of the major banks and multinationals, it has a limited presence. As Danthine and Lambelet explain, the Swiss commitment to limited intervention is not enough "to show that nonintruding policies are necessary for performing economic structure ... [however] 'nothing succeeds like success.'"[58]

Moreover, the overall lack of welfare benefits and a welfare system based on elimination of and cultural shame against welfare dependency and inter-generational poverty highlighted the societal value of individualism, or the preference for personal, as opposed to community, responsibility. Consequently, throughout the decade Switzerland was hardly a welfare state. There was no national health service, with most of the population being covered by voluntary health insurance, and there was not a central programme to provide a minimum guaranteed income for all of the population as in Denmark and Sweden.[59]

With few natural resources, the Swiss economy evolved into one based on the tertiary sector, namely financial services and tourism. Through the influence of Switzerland's financial institutions, the Swiss economy continued to thrive on a highly successful, conservative course, in which annual growth remained unspectacular, but in which inflation, the capitalists' and financial institutions' greatest enemy, was avoided through strict monetary policy. As a result of the influence of successful monetary and financial policies and intimate finance-industry relations, financial institutions were the principal actor in Switzerland's achievement of high levels of international competitiveness. This is discussed in detail in Chapter Three.

Moreover, throughout most of the twentieth century in

Switzerland, the slow-moving political process mirrored the economic process. The Swiss application of gradualism reduced the strain on its institutions by preserving moderation in all facets of its political-economic life. (See Figure 2.20.) Even with the "tangled maze" of religious and cultural diversity, the "complex network of cross-cutting cleavages"[60] did not destroy its true sense of stability, which was confirmed by a lack of polarisation of hostile parties, such as was found in the neighbouring small state Austria.[61]

Figure 2.20
Average Yearly Sector Change in Switzerland (% Growth)

	Year (19--)								
	00/10	10/20	20/30	30/41	41/50	50/60	60/70	70/80	%Change
A	-0.4	-0.1	-0.5	0.1	-0.6	-0.5	-0.5	-0.1	-3.30
B	0.1	-0.1	0.1	-0.1	0.3	-0.3	-0.2	-0.6	-5.00
C	0.3	0.2	0.4	0.1	0.3	0.7	0.7	0.7	3.70
	0.0	0.0	0.0	0.0	0.0	-0.1	0.0	0.0	

A = Agriculture
B = Industry
C = Service

Source: David E. Bohn (1986) "The Failure of the Radical Left." *Comparative Political Studies*: 97.

According to *The World Competitiveness Report*, a major survey published by IMEDE and the World Economic Forum analyzing and ranking thirty-two countries through nearly three-hundred criteria based on findings in the 1980s, Switzerland ranked first out of twenty-two OECD countries in terms of socio-political stability.[62]

Voting for seats in the bicameral parliament was on a proportional representation (*proporz*) basis, with the coalition of the four largest political parties, the so-called "magic formula," remaining in power for thirty years. These four parties accounted for more than eighty-five percent of all parliamentary seats; only fifteen percent of the vote was not directly represented in the government. (See Figures 2.21 and 2.22.)

Figure 2.21
Nationalrat Party Representation(% By Size of Canton)[63]

Year (19__)	19	22	25	28	31	35	39	43	47	51	55	59	63	67	71	75	79	83	87
FDP	63	58	59	58	52	48	51	47	52	51	50	51	51	49	49	47	51	54	51
CVP	41	44	42	46	44	42	43	43	44	48	47	47	48	45	44	46	44	42	42
SPS	41	43	49	50	49	50	45	56	48	49	53	51	53	51	46	55	51	47	41
SVP	41	35	30	31	30	21	22	23	21	23	22	23	22	21	23	21	23	23	25
LDU	25	0	0	0	0	7	9	5	9	10	10	10	10	16	13	11	11	12	12
LPS	9	10	7	6	6	7	6	8	7	5	5	5	6	6	9	9	8	8	9

Figure 2.22
Staenderat Party Representation (Two Delegates per Canton)

Year (19__)	19	22	25	28	31	35	39	43	47	51	55	59	63	67	71	75	79	83	87
FDP	23	23	21	20	19	15	14	12	11	12	12	13	13	14	15	15	11	14	12
CVP	17	17	18	18	18	19	18	19	18	18	17	17	18	18	17	17	18	18	15
SPS	0	1	2	0	2	3	3	5	5	4	5	4	3	2	4	5	9	6	2
SVP	1	1	1	3	3	3	4	4	4	3	3	3	4	3	5	5	5	5	4
LDU	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	1	0	0	1
LPS	2	1	1	1	1	1	2	2	2	3	3	3	3	3	2	1	3	3	2

Source: *Gesellschaft Zur Forderung Der Schweizerischen Wirtschaft*, 1987.

Throughout the decade most political battles were fought through the referendum process, not through competition between political parties; referenda were required when the government and the parliament proposed a change in the constitution and were optional in the case of federal laws. While discrepancies among political parties were mediated through the direct democracy process, the ideologies of the major parties were generally similar.[64] The strength of Switzerland's direct democracy as a stabilising force was unmistakable. In 1983-1987, the Swiss population voted during thirteen weekends on thirty-five issues, and twenty-nine of the thirty-five submitted were supported. The government's referendum "success rate" was around eighty-three percent.[65]

Throughout the 1980s Switzerland subsequently assumed the political process with a prudent eye on economics. Analogous to countries such as Japan where trading power was more important than military power, economics and security were intimately linked in Switzerland.[66] In fashioning economic policies, informal puissance remained in many ways more meaningful than formal power. *Ad hoc tete-a-tete* and standard dialogue among peak industrial, banking, and labour associations relieved potential conflict, which uncovered the reasons for Swiss strike activity being the lowest in the industrialised world. In Switzerland, strike activity was so limited that annual strike statistics were counted in seconds per one thousand workers.[67]

In developing economic policies, the Swiss framework for consultation included the gathering of interests from all facets of economic life including a process known as *Konjunturfragen*, in which the Ministries of Foreign Trade and Labour/Industry advised on economic policy matters and provided detailed economic forecasts and proposals.[68] This was followed by *Vernehmlassung* (or *procedure de consultation*), meaning notification or promulgation, in which pluralistic peak association representation was framed into a "concerted"[69] package for interest articulation. The policy implementation aspect, referred to as *Verflechtungen* involved mixed administrative structures, "where a specialized sector of the state administration and the staff of a private association cooperate closely in order to tackle a specific economic or social problem."[70]As Katzenstein contends, this lengthy process "strengthen[ed] Switzerland's compulsion to compromise."[71]

Although the formal networking procedure was important for Switzerland to remain internationally competitive in the 1980s, the Swiss themselves perceived corporatism as over-formalising a naturally "Swiss" phenomenon. Much of this reticence can be attributed to corporatism's connotations in reference to Mussolini's symbolic interest articulation in fascist Italy. Others perceived corporatism as misrepresenting Switzerland's laissez-faire doctrine in all facets of its economic and political culture. But most Swiss concluded that manipulating the term corporatism on distinctly national characteristics was an example of assembly-line, quixotic, and circumlocutory terminology that misrepresented authentic Swiss industrial culture.[72] What is truly "Swiss" has been their admiration and deference for consociational politics;[73] the Swiss have truly believed that pluralistic compromise, not static uniformity, would lead to more competent and rational decision-making by integrating the contributions of all economic actors into the process. To frame this process in universal overtones may extract the meaningful, portentous, aspects of how Switzerland achieved its high level of international competitiveness during the 1980s.

In contrast to Switzerland, during the 1980s Sweden upheld a unified societal value of political and economic equality, marked by State programmes to assure "cradle to grave" benefits for society. Based on such communitarian principles, Swedish welfare state goals were achieved through programmes with "universalistic and comprehensive structures and criteria."[74] Swedish policy-makers assumed under communitarian principles that economic and social policy would be synchronised, causing a noticeable reduction of gross inequality and better quality of life for all. As Lindberg explains,

> [The Swedish welfare state values the] transformation of the social order through elimination of class/status distinctions and promotion of solidaristic ethic and promotion of social mobility."[75]

Sweden's industrial culture deviated rather dramatically from that of Switzerland in terms of national outlook. While Swiss prosperity was translated through the affluence of individuals in society, in Sweden it was the overall well-being of the community that remained the vital goal. The affluence of the community, however, was achieved in much the same way as that of the individual in Switzerland, where the State played a relatively minor direct role in shaping industry throughout most of the 1980s. The State targeted much of its attention, expertise, and money towards maintaining a strong welfare state, in which all members of society received social benefits.

While welfare and egalitarianism remained central precepts to the Swedish model of communitarianism, policy-makers, industrialists, trade unionists, and scholars in Sweden during the 1970s and 1980s agreed that the most effective way to promote industrial progress was through the combination of providing egalitarian social benefits while maintaining a limited interventionist outlook for industry.[76] Nonetheless, between 1976-1982 the centre-right coalition under extreme international economic pressures did impose significant subsidies to declining industries, most notably shipbuilding.

Upon the gradual improvement of the Swedish economy following the recessionary period and the return of the SAP to power in 1982, the Swedish State continued its rhetoric of maintaining its primary economic objectives of full employment, welfare benefits, and industrial progress. The Swedish State maintained its commitment to limited intervention by explaining that, "The government's industrial policy ... is to create favourable conditions and readiness instead of regulating development in a predetermined way."[77] Indeed, such rhetoric was more credible under positive international and domestic economic conditions.

Nonetheless, because full employment remained the central tenet to the Swedish communitarian ideology, the role of the Swedish trade union movement under a system of centralised bargaining and solidaristic wages, coupled with active labour market policies implemented by the State, remained the primary avenue through which Sweden remained internationally competitive during the 1980s. Consequently, labour was the principal actor in Sweden throughout the decade, and this is discussed in detail in Chapter Four. As Wilson strongly argues in terms of the power of labour, "To deny the Swedish ... unions a role in policy-making would be to invite severe trouble."[78] In Sweden social equality and strong economic performance were not mutually exclusive; rather, Sweden's communitarian ideology acted as an ideological concomitant to increasing levels of international competitiveness.

Political stability has also been a historical trademark of Sweden. From the 1930s through the 1980s (other than the period 1976-1982 known as the *bourgeois interregnum*) the SAP was in power and used its strong working relationship with the trade unions to maintain its political strength.[79] This relationship was indicative of Swedish policy-making, since the Swedish way was one of cautious but purposive policy-making involving a cultural bias towards communitarianism; the result was often effective, though not necessarily efficient (in terms of the amount of time it took legislation to pass through the process), policy implementation. As Heclo and Madsen assert,

> ... [Swedish] politics is kind of a therapeutic exercise. Its mission is the slow, careful eradication of disease and the establishment of a regimen of good health in society. It is always to be done with a patient's consent, but also with the recognition that some unpleasant medicine and restrictions may need to be accepted because they are good for the people. This approach permeates Swedish life.[80]

In a similar vein to Sweden, Denmark also attempted to maintain a welfare, or provident, state commitment throughout the 1980s. Grundwig, the great Danish statesman, philosopher, and theologian, is considered to be the father of social education (through his *folkehojskoler*, the first attempt at State-sponsored schooling). From his influence the Danes felt a special desire to preserve their welfare state based on egalitarian principles.

While Grundwig was the father of Danish communitarianism, Kierkegaard arose as the master of individualism. His direct and indirect influence in terms of the role of the State left an indelible mark on the country; throughout the 1980s Denmark's industrial preferences were similar to those in Sweden, where Danish policy-makers expressed a preference for industry to compete in the free marketplace with limited intervention of the State, illustrating what Sidenius has termed Denmark's "persistent liberalism".[81] Danish industry attempted to remain competitive with even less direct help from the State, particularly subsidies, than that in Sweden during the *bourgeois interregnum*, in which the centre-right government subsidised a number of ailing industries. Nonetheless, the Danish State did continue to subsidise its ailing shipbuilding industry, while the Swedish State discontinued shipbuilding subsidisation.

Danish industrial culture, however, deviated from Swedish industrial culture in terms of the distinct separation between social policy, influenced by the Grundwig doctrine, and its limited interventionist stand towards industry, based on the Kierkegaardian philosophy of individualism. While during the 1980s Denmark was plagued with the division, Sweden was better able to integrate its philosophies on society and industry. For instance, Sweden's primary social objective of full employment was used as a tool to aid industrial competitiveness through a number of active labour market programmes, including both retraining and mobility policies.

According to *The World Competitiveness Report*, Denmark was ranked first out of twenty-two OECD countries in terms of "the extent to which the state's health care facilities are adequate for the individual worker and his family."[82] However, Denmark was ranked last in terms of "the extent to which taxation and social security systems encourage the will to work."[83] Indeed, while Sweden ranked among the top half countries in terms of health care facilities, it also ranked among the top five in terms of encouraging the will to work.

Consequently, a dependent attitude pervaded throughout Danish society because social policies virtually alleviated incentives for reemployment. "More and more often the subject [of Danish State aid was] not a citizen with rights and duties, but a client, a recipient of aid and services waiting to be told what to do rather than doing what he wants...."[84] Unfortunately the Danish provident state was unable to integrate its social and economic philosophies into an overriding, comprehensive goal, as was the case in Sweden, much as a result of its poor economic performance since the mid-1970s.

With inflation, unemployment, and current account deficit problems, the Danish State imposed an austerity programme - the "Potato Diet" - in the early part of the 1980s as a "major crisis step."[85] The State levied a twenty percent tax on interest rate expenditures in an attempt to thwart borrowing for domestic consumption, promote savings, limit import consumption, and reduce the current account deficit.[86] Ironically, with personal taxes among the highest in the world to fund Denmark's social benefits schemes, the average Dane simply consumed by borrowing from the bank - but now even that was taxed.

While attempting to tackle its cross-current demands ranging from its giant welfare state commitment to maintaining a high standard of living (evidenced by the borrowing for personal consumption), as well as holding off inflation and import consumption, the Danish State had relatively few ideas as to how to increase industrial productivity. Denmark ranked last out of twenty-two OECD countries in the *World Competitiveness Report* in terms of "the importance of industrial production on its economy." [87] From the 1960s until the mid-1980s the lines between social and economic policy remained clearly delineated in Denmark, even though it began to face a number of international economic pressures. Nonetheless, policy-makers were unclear as to what role the State should play in terms of industrial development, though they were certain that "some action needed to be taken."[88] Most important, Denmark's industrial structure was composed principally of small- and medium-sized enterprises, most of which were operating in *niche* areas.

More out of practice than reason, Denmark chose its "persistently liberal"[89] path of limited intervention without attempting to respond flexibly to changing external conditions. While policy was clearly oriented towards the demand side, the supply side was neglected as a result of liberal economic ideology. Indeed, with international pressures and the increasing vulnerability of the Danish economy, its international competitiveness waned, with Denmark becoming increasingly dependent on the EC for economic sustenance throughout the 1980s. Nevertheless, by the middle of the decade, the Danish State realized that an industrial policy needed to be formulated, and it began to work closely with industry and research institutions to bolster is technological competitiveness. As a result of such action, the State in Denmark became the principal actor in helping to augment the state's level of international competitiveness, and this is discussed in detail in Chapter Five.

While facing economic instability throughout the 1970s and 1980s, Denmark faced political instability as well. Much of the reason for such economic policy fluctuation was the Danish approach to forming consensus politics. As in Sweden, Danish political was marked by constant negotiation[90] between the major trade union (the *Landsorganisationen- LO*); the major peak industrial association similar to the Swiss *Vorort*, the *Industrirardet;* and various ministries. Moreover, because of the proportional representation system of voting, most Danish governments were minority-led, meaning that "various positions [were] openly announced and speculated upon.

By the mid-1970s under a new system of proportional representation, the new parliament had a far greater number of diverging political parties, including a rightist tax refusal party, which garnered an amazing sixteen percent of the vote. (See Figure 2.23.)

Figure 2.23
Composition of Parliament (Folketing) by Party, 1988 Election

Party	Number of Seats
Social Democrats	55
Conservatives	35
People's Socialists	24
Liberals	22
Progressive Party	16
Social Liberals	10
Centre Democrats	9
Christian Democrats	4
Greenland and Faroe Islands	4
Total	179

Source: OECD (1988) *Denmark*: 7.

With these changes, significant political stalemates ensued, resulting in weak minority governments throughout the 1973-1980 period.[91]

> After 1973, the Folketing became extremely fragmented with ten or eleven parties....the 1970s brought an alienation from traditional politics and the arrival of new political forces expressing and articulating these sentiments.[92]

In short, there [was] a considerable degree of transparency in the whole process."[93] Similar to other negotiated political systems, like Sweden and Switzerland, Denmark's governmental process was characterised by "muddling through," which for Denmark has often led to static, stalemated policy-making.

With external shocks ushering in the 1980s, Ireland struggled with poor economic performances: the debt--to-GNP ratio remained around three times the average of European Community nations,[94] unemployment was near twenty percent, and growth was sluggish. Throughout the 1970s public expenditure grew rapidly; in 1974-1975 the coalition increased its deficit to attempt to revitalise the recession-struck economy, and the *Fianna Fail* government of 1977-1981 increased government spending as part of job creation programmes.[95] In addition, with seven different governments operating from 1970-1987,[96] policies were not developed out of long-term ideological consensus but rather out of an *ad hoc* and short-term necessity. As Hardiman maintains, "Irish parties ... tended to adopt a more *ad hoc* approach to policy-making and were constrained by other features of the political system from developing specific ideological profiles in sharper outline."[97]

After the Irish government had introduced a coherent economic philosophy based on protectionism twenty years earlier, industrialists and policy-makers in Ireland during the 1970s understood the necessity to spur economic growth by (1) linking with the larger unit of Europe, which Ireland did by joining the EC in 1972; (2) dismantling trade barriers, which Ireland began to accomplish through the Anglo-Irish Free Trade Agreement of 1966; and (3) spurring economic development by giving the State a larger role.[98]

However, with increased competition from abroad as a result of opened markets and membership in the EC, Irish indigenous industry suffered net losses in market shares at home without compensation from increases abroad.[99] Indigenous industry made little progress in developing R & D programmes to revitalise its stagnating industrial base, and the State introduced few policies to spur development of Irish industry. Instead, Ireland became dependent on the EC; it remained a net beneficiary from transfer payments totalling six times its contribution. Seventy-four percent of these transfers were as a result of the CAP, and the EC also granted substantial Community loans for development of Ireland's industrial base and infrastructure.[100]

This attitude of dependency in its external relations was also manifested internally through the Irish welfare state. With income tax rates comparable to those in Scandinavia to cover its comprehensive welfare state programmes, including a major social insurance scheme, throughout the 1980s the Irish State continued to grant such benefits even in the face of a major budget deficit. Similar to Denmark, Irish society developed an attitude of dependency in which social policies virtually alleviated incentives for reemployment.

For the Irish, an attitude that the State has a moral responsibility to support the population pervaded through society as a result of the strong influence of the church.[101] With a unique linkage between church and State in the Irish constitution, during the 1980s the Catholic Church remained the most powerful institution in Republican society. The church's role in state affairs, particularly social policy-making, remained so influential that, "The Catholic Church attempt[ed] to enforce an idea that Irish ethics is the same thing as Catholic doctrine."[102] Moreover, as Hogan contends,

> The Church rarely finds it necessary to intervene in political affairs because politicians have found that it is rarely electorally profitable to take on the Church. Moreover, the entire apparatus of public affairs is 'conditioned to articulate and legislate what the Church wants without the Church having to lobby for it.'"[103]

As a result of the influence of the church on the Irish, they remained staunchly conservative in their social views: abortion and divorce, for example, have been outlawed. Irish conservatism also pervaded into politics and economics. Edmund Burke, whose political writings on incrementalism and conservatism have greatly influenced political thinking, is one of the major figures in Ireland's most prestigious university, Trinity College, Dublin.

With the industrial revolution bypassing the country, except for the north in Belfast (particularly in shipbuilding and woolens),[104] Ireland maintained a predominantly rural economy. Moreover, its industrial structure was composed of only small- and medium-sized enterprises. Without a significant industrial base, Ireland remained highly dependent on the EC, most importantly the British economy, to support its infrastructural problems and semi-peripheral location. With radical political problems gnawing at Irish society, Ireland's rural-based and traditional society could not sustain economic growth throughout the 1970s into the 1980s. Unemployment and inflation both ensued.

Moreover, tensions between the Republic and Britain as a result of the Northern Ireland situation continued to be one of the most powerful reminders of deep-rooted historical conflicts with political and sectarian origins.[105] One must remember that "both the Republic of Ireland and Northern Ireland were created by a combination of military force and popular will."[106] Consequently, while there remained a virtual symbiotic economic relationship between Ireland and Britain (at least from the Irish perspective) throughout the 1980s, feelings of dislike, distrust, and frustration towards the English pervaded Irish society. Beyond national differences, the Northern Ireland situation also brought to light the differences between Catholic Ireland and Protestant Ulster. While violence continued throughout the 1980s, both Ireland and Britain remained in a stalemate over the issue.

With an ideological reluctance for dramatic action, Irish society began to develop an attitude of ill-fatedness and powerlessness as a result of declining international competitiveness, infrastructural problems, and internal violence. As Ivor Kenny explains,

> What we face now is a more generalised malaise defined as an economic crisis .... the symptoms of the disease are ... the human consequences of inflation (the destruction of wealth), of unemployment (the destruction of jobs), of a coarsening in the quality of Irish life, and of alienation .... we thrashed around laying blame: on the increase in oil prices, on the international recession, on the Northern Ireland conflict. We slowly learned that laying blame would not cure our ills, but we were not yet ready to face the consequences, to take the medicine ....[107]

Moreover, in a series of lectures by Ireland's most noted economic scholars, which were compiled in a single book, virtually all expressed the same tone:

> The problems which we face are now of such a magnitude....
>
> ....we are now faced with enormous problems which have no easy answers....
>
> ....how can then we plot an escape route from the morass?[108]

As a result of poor economic performance and a weak industrial structure, coupled with societal attitudes of powerlessness, the Irish State remained highly dependent on external sources for economic development and modernisation. Its external dependency on the United States and the EC, most importantly the United Kingdom, resulted in overall reluctance to form comprehensive state goals; instead, Irish industry remained dependent on American industry, Irish farmers became dependent on CAP funds, and Irish policy-makers attempted to combat declining levels of international competitiveness with little agreement as to how to solve their economic problems. Nevertheless, by the mid-1980s the State was able to attract foreign direct investment, continued to maintain a strong export orientation, and commenced a programme to limit wage increases. As a result, the State was the principal actor in Ireland's effort to augment is level of international competitiveness.

2.5. Summarising State Priorities and Societal Values in the Case Studies

By distinguishing state external priorities (e.g., international independence) and state internal priorities (e.g., political and economic stability, economic growth), as well as identifying differences in societal values, this chapter has presented the circumstances and conditions underlying differences in practice among important economic actors in the small European state and their consequent effects on each state's international competitiveness. Subsequent chapters will elaborate on these practices and actor interaction.

The following three chapters examine relations between the fundamental actors - financial institutions, labour, industry, and the State - that support and augment international competitiveness. Chapter Three analyzes the role of financial institutions in the small European state, specifically examining the small European state's monetary environment and the relations between financial institutions and industry. Chapter Four investigates the cooperative or detached nature of trade union-industry relations and the use (or lack of) labour market policies. And Chapter Five analyzes State-industry relations, examining the use of industrial policy-making in each of the four case studies.

Because of limited international economic power status as price takers, the four small states used various forms of intervention to sustain and/or increase their levels of international competitiveness during the 1980s. However, applications of intervention differed among the four case studies. While Sweden and Switzerland developed policy strategies cultivated as a result of their industrial cultures, confused objectives and conflicting beliefs in Denmark and Ireland hampered the development of policy strategies to combat declining levels of international competitiveness.

Throughout the 1980s in both Sweden and Switzerland, state priorities and societal values remained relatively coordinated within each country. In both states independence remained a major priority and was achieved through foreign policies based on neutrality, powerful industrial structures, and strong economic performances. Internally, however, Swedish society preferred mixed economy values, allowing an integration of its philosophies on society and industry. Because of the Swiss desire to maintain a prosperous community based on individual economic achievement, welfare state goals were overlooked and personal entrepreneurialism advocated.

In Denmark and Ireland, however, their industrial cultures were marked by external state dependence and internal State and societal confusion as to the way to engender higher levels of international competitiveness. For the Danes, the liberal path of non-intervention in industry, even in times when international pressures may have called for State action, produced attitudes that some action needed to be taken, though the State was unsure what should be done. Indeed, the choice of Danish policy-makers was to attack the demand side of the problem while neglecting the supply side. Paradoxically, while Danish society enjoyed a high standard of living comparable to that of Sweden and Switzerland, its industrial structure was significantly weaker. With poor economic performance throughout much of the 1980s, by the end of the decade Danish policy-making focused on efforts to make Danish enterprises more competitive in foreign markets.

During the 1980s Ireland's semi-peripheral location, infrastructural inadequacies, weak indigenous industrial structure, and domestic political tensions caused extreme divisiveness as to how to solve numerous political and economic problems. With a stated belief in the free marketplace and a high degree of dependence on the EC, Irish policy-making throughout much of the decade was characterised by inaction coupled with international dependency. Similar to Denmark, only by the end of the decade did policy-makers initiate attempts to promote Ireland's level of international competitiveness.

Understanding these background factors, this thesis will examine the practices of interaction between financial institutions, trade unions, and the State. The following three chapters will functionally compare the four small European states by analyzing these tripartite relations; this form of functional comparison will attempt to clearly illustrate why some small European states were more internationally competitive than others during the 1980s.

Notes for Chapter Two

1.George C. Lodge (1987) "Ideology and Country Analysis" in George C. Lodge, and Ezra F. Vogel, eds. *Ideology and National Competitiveness*: 15.

2.Martin J. Wiener (1985) *English Culture and the Decline of Industrial Spirit, 1850-1980*: 3.

3.See Francois Duchene and Geoffrey Shepherd (1987) "Western Europe: A Family of Contrasts" in Duchene and Shepherd, eds. *Managing Industrial Change in Western Europe*: 25.

4.William M. Dugger (1980) "Power: An Institutional Framework of Analysis." *Journal of Economic Issues*: 898.

5.Lodge (1987) *op.cit.*: 15.

6.Aaron Wildavsky (1986) "Industrial Policies in American Political Cultures" in Claude E. Barfield and William A. Schambra, eds. *The Politics of Industrial Policy*: 17 (15-32).

7.Peter J. Katzenstein (1985a) "Small Nations in an Open International Economy: The Converging Balance of State and Society in Switzerland and Austria" in Rueschemeyer, Evans, and Skocpol, eds. *Bringing the State Back In*: 227.

8.Yet in terms of export growth they did as well as the U.S., Japan, and the Federal Republic of Germany. IMEDE and World Economic Forum (1989) *The World Competitiveness Report*: 192-231.

9.Ibid.: 202, 203, 212, 213.

10.The Economist (1987) *The World in Figures*: 35.

11.Ibid.: 36.

12.Imede and World Economic Forum (1989) *op.cit.*: 222-223.

13.The Economist (1987) *op.cit.*: 36; IMEDE and World Economic Forum (1989) *op.cit.*: 223.

14.In terms of quantity, Switzerland lagged far behind Japanese watchmakers.

15.However, in certain pharmaceutical products, the share was significantly higher. IMEDE and World Economic Forum (1989) *op.cit.*: 224-225.

16.David A. Baldwin (1985) *Economic Statecraft*: 366.

17.Christopher Tugendhat (1986) *Making Sense of Europe*: 111.

18.Perhaps the best example of Swiss MNC flexible specialization implementation is that of the watch industry of the 1970s. By 1979 over one-third of Swiss watches were assembled abroad, and more than one-half of Swiss watches manufactured at home relied on parts and components that were produced abroad through the FDI process. Through the help of the banks and the restructuring process, the Swiss watch industry regained its particular *niche* market by flexibly specialising - by making their watches thinner and marketing craftsmanship over electronics. In the 1980s, the Swiss share of the world market for watches priced above $225 was eighty-five percent, and it continued to produce one-quarter of all quartz watches. See Peter J. Katzenstein (1982) *Corporatism and Change*: 220-226.

19.Nonetheless, during the 1980s Swiss MNCs employed various strategies. Some, like Nestle and *Alusuisse*, were vertically integrated, some took a horizontal integration perspective, like Brown Boveri, and still others became conglomerates like Buhrle, which was integrated by financial strategies that mixed profitability and risk dispersion. See Katzenstein (1984) *op.cit.*: 73.

20.At the same time, U.S. direct investments totalled around $15,800 m. in 1985 and $17,500 m. in 1986.

21.See "Have Money Will Travel." (1987) *Swiss Business*: 33.

22.Ibid.

23.Unfortunately the government does not publish estimated totals of FDI, much less by industry. However, private sources have made estimates. See Credit Suisse (1987) *Swiss Economic Data* and "Have Money Will Travel" (1987) *op.cit.*: 33.

24.Also some larger states within the Community have perceived such a threat. For example, Britain has opposed membership in the EMS.

25.On Sweden, see Marquis Childs (1980) *Sweden: The Middle Way on Trial*: Chapter 7.

26.One exception is Sweden, which though neutral spends more heavily on defence than most small European states. In the 1987-88 budget, 26,378 million S.Kr. were spent on defence. Swedish Ministry of Finance (1988) *The Swedish Budget*: 49.

27.Peter J. Katzenstein (1985) *Small States in World Markets: Industrial Policy In Europe*: 46.

28.Swiss, Swedish, and Irish foreign and defence policies during the 1980s were based on neutrality; Denmark's position was less clear, given its membership in NATO, and caused larger states like the United States and Britain to question Danish defence priorities. While Sweden, Switzerland, and Ireland remained neutral with defence issues taking a minor role in public debate, in Denmark defence issues spurred national controversy; various party manifestos in the 1987 election were based on the question of whether Denmark should remain a member of NATO, while elections in the same period in Ireland and Sweden were based on internal issues such as economic performance. See Karen De Young (1988) "Danish premier Resigns, But Will Seek to Form New Coalition." *The Washington Post* (May 12): A26 and "Denmark's Election: Fiddle, Fuddle" (1988) *The Economist.* (May 14): 57.

29.IMEDE and World Economic Forum (1989) *op.cit.*: 69, 132.

30.A listing of the top twenty-five companies (ranked by revenues) in Denmark from 1984-1987 was provided by Henning Hasle, *Privatbanken.* Information sent on 2 December 1988, letter ref. "Henning Hasle/sha."

31.Ibid.; Svenska Handelsbank *op.cit.*: 14.

32.See Barry Brunt (1988) *The Republic of Ireland*: 2-11.

33.James Wickham (1986) "Industrialisation, Work, and Unemployment" in Patrick Clancy, Sheelah Drudy et. al., eds. *Ireland: A Sociological Profile*: 74.

34.See Aspect: The Investor's Business Journal (1989) *Top 1,000 Companies and Who's Who in Ireland, 1989*: 52-85.

35.The size of the Irish economy is roughly comparable to that of Manchester, England. See Imede and World Economic Forum (1989) *op.cit.*: 64. (Tables 1.01, 1.02)

36. Certainly much of the reason for international dependency is due to a state's level of international development and can help explain why some states, most notably Third World countries, are underdeveloped. *Dependencia* theories in regard to the development of the Third World abound. See various writings by Amin, Caporaso, Evans, and Frank. No such propositions are made in this section, since its purpose is descriptive and attempts to frame each state's international position.

37.Accordingly, in the "Documents Concerning the Accession" of Denmark and Ireland each received ten delegates to the Assembly out of a possible 198. In the council, each received three votes out of a total 58. See European Community (1978) *Treaties Establishing the European Communities, Treaties Amending These Treaties, and Documents Concerning the Accession*: 1005, 1008-1009.

38.Snake membership in 1972 was particularly important since currency stability was seen as vital for maintaining a strong trading relationship with West Germany, Denmark's main trading partner.

39.The two greatest beneficiaries of the CAP have been the Danish and the Irish. See Stephen George (1985) *Politics and Policy in the European Community*: 126. For example, between 1972 and 1986 family farm income in Ireland increased from 284 million Ir.Pd. to 1,239 million Ir.Pd. See Department of Foreign Affairs (1987) *Ireland in Brief*: 9.

40.Paul Sharp (1987) "Small State Foreign Policy and International Regimes: The Case of Ireland the European Monetary System and the Common Fisheries Policy." *Millennium: Journal of International Studies*: 56.

41.Emer Hughes (1989) "Has Ireland Missed the Euro Gravytrain?" *Irish Independent*. (February 20): 6.

42.Margaret Studer (1988) "Spooked by Job Cutbacks, Swiss Shudder At Unemployment Specter That Barely Exists." *The Wall Street Journal*. (March 30): 2.

43.Friedrich Schneider, Werner W. Pommerehne, and Bruno S. Frey (1981) "Politico-Economic Interdependence in a Direct Democracy: The Case of Switzerland" in Douglas Hibbs et. al., eds. *Contemporary Political Economy: Studies on the Interdependence of Politics and Economics*: 247.

44.See Kjell Lundmark (1983) ""Welfare State and Employment Policy: Sweden" in Dyson and Wilks, eds. *Industrial Crisis: A Comparative Study of State and Industry*: 242-243.

45.OECD (1982-1983) *Economic Surveys: Denmark*: International Statistical Comparisons.

46.See The Institute for Future Studies (1987) *Growth Politics in a Nordic Perspective*: 350.

47.See Bo Sarlvik (1983) "Scandinavia" in Vernon Bogdanor and David Butler, eds. *Democracy and Elections: Electoral Systems and Their Political Consequences*: 122-148; and, Erik Damgaard (1989) "Crisis Politics in Denmark, 1974-1987" in E. Damgaard, P. Gerlich, and J.J. Richardson, eds. *The Politics of Economic Crisis*: 74-75.

48.See Paul McKee (1983) "The Republic of Ireland" in Bogdanor and Butler, eds. *op.cit.*: 185-188.

49.Kenneth Dyson (1983) "The Cultural, Ideological, and Structural Context" in Dyson and Wilks, eds. *op.cit.*: 34.

50.For varying outlooks on this subject, see: Richard J. Samuels (1987) *The Business of the Japanese State*; Robert S. Ozaki (1984) "How Japanese Industrial Policy Works" in Chalmers Johnson, ed. *The Industrial Policy Debate*: 47-70; Richard Boyd (1987) "Government-Industry Relations in Japan: Access, Communication, and Competitive Collaboration" in Wilks and Wright, eds. *Comparative Government-Industry Relations*: 61-90.

51.Perhaps so much so that the first incumbent vice-president was elected president in over one-hundred years. See William Niskanen (1988) *Reaganomics* and Martin Anderson (1988) *Revolution*.

52.Irving H. Siegel (1983) "Work Ethic and Productivity" in Industrial Relations Research Association Series. *The Work Ethic: A Critical Analysis*: 28.

53.As Perry Pascarella explains, "... when people are unwilling or unable to work effectively, they suffer the penalties for poor productivity in both economic and non-economic terms." See Pascarella (1984) *The New Achievers: Creating a Modern Work Ethic*: 6.

54.In Belgium the split between the Flemish and the Walloons has divided the country and has consistently affected Belgium's fragile political system. In Ireland, the differences between Protestant Ulster and the Catholic Republic continue to be manifested though internal strife and violence.

55.Hans J. Halbheer (1985) "An Attempt to Explain Switzerland to a Foreigner." *The World Today: Credit Suisse Bulletin*. (offprint).

56.Interview with Dr. Beat Moser, Head of the Economic Affairs Department, Swiss Society of Chemical Industries, Zurich, 12 November 1987.

57.Jean-Pierre Danthine and Jean Christian Lambelet (1987) "The Swiss Recipe: Conservative Policies Ain't Enough!" *Economic Policy: A Special Report - The Conservative Revolution*: 161.

58.Ibid.: 174.

59.See Ralph Segalman (1986) "Welfare and Dependency in Switzerland." *The Public Interest*: 106-117.

60.See David E. Bohn (1986) "The Failure of the Radical Left in Switzerland." *Comparative Political Studies*: 92-97.

61.States Peter J. Katzenstein: "The partisan penetration of Austria's nationalized industries and nationalized banks, as well as the institutional requirements of its industrial policy, illustrate how the political parties have neutralized state power." See Katzenstein (1985a) op.cit: 237.

62.IMEDE and World Economic Forum (1989) *op.cit.*: 19. Sweden ranked eighth, Denmark eleventh, and Ireland fourteenth.

63.The main parties include: *Christlichdemokratische Volkspartei* (CVP) - Christian Democratic Peoples party; *Freisinnig-demokratische Partei* (FDP) - Radical Democratic Party; *Sozialdemokratische Partei* (SPS) - Social Democratic

Party; *Schweizerische Volkspartei* (SVP) - Swiss People's Party. The main smaller parties include: *Landesring de Unabhangigen* (LDU) - Independent Party and *Liberale Partei* (LPS) - Liberal party. See J.M. Gabriel (1984) *How Switzerland is Governed*: 48.

64.See Schneider, Pommerehne and Frey (1981) *op.cit.*: 232-240.

65.Mario A. Corti (1987) "Are the Swiss Good At Managing Change?" Bank Baer Group Meeting, September 11.

66.Interview with Gerhard Schwarz, Economics Correspondent, *Neue Zurcher Zeitung*, Zurich, 11 November 1987.

67.See Katzenstein (1985a) *op.cit.* : 236.

68.Interview with Dr. Philippe Saurer, Ministry for Economic Affairs, Berne, 16 November 1987.

69.See Philippe C. Schmitter (1982) "Reflections on Where the Theory of Neo-Corporatism Has Gone and Where the Praxis of Neo-Corporatism May Be Going" in Lehmbruch and Schmitter, eds. *Patterns of Corporatist Policy-Making*: 259-280.

70.Leonardo Parri (1987) "Neo-Corporatist Arrangements, 'Konkordanz', and Direct Democracy: The Swiss Experience" in Ilja Scholten, ed. *Political Stability and Neo-Corporatism*: 78.

71.Peter J. Katzenstein (1980) "Capitalism in One Country: Switzerland in the International Economy." *International Organization*: 526.

72.This was vigorously stated in the Interview with Dr. Gerhard Schwarz. Interview with Schwarz, 11 November 1987.

73.As Katzenstein states in the preface: "Swiss readers in particular have often disagreed vigorously with my emphasis on the capitalist rather than the consociational feature of Swiss politics." See Katzenstein (1980) *op.cit.*: 507.

74.See Leon N. Lindberg (1987) "A Classification of Welfare States." Paper presented at the University of Wisconsin-Madison.

75.Ibid.

76.See Peter Gourevitch (1986) *Politics in Hard Times: Comparative Responses to International Economic Crises*. The mixed economy approach is discussed in terms of the Swedish paradox between collectivism and individualism in: Marquis Childs (1980) *Sweden: The Middle Way on Trial*: Chapters 3 and 4.

77.Ministry of Industry (1987) *Swedish Industry Facing the 90s.* Government Bill 1986/7:74: 16.

78.Graham K. Wilson (1985) *Business and Politics*: 113.

79.Pontusson contends that the power of the SAP has been "hegemonic." (He defines this as "the ability of the Swedish Social Democrats to dominate coalition politics, i.e., to strike alliances with other political forces (parties and interest groups) or preempt hostile alliances being formed, and to define the problems on the political agenda as well as the terms in which these problems have been debated by most, if not all, major political actors.") See Jonas Pontusson (1988) *Swedish Social Democracy and British Labour: Essays on the Nature and Conditions of Social Democratic Hegemony.* (See page 2 for quotation.)

80.Hugh Heclo and Henrik Madsen (1987) *Politics and Policy in Sweden: Principled Pragmatism*: 27.

81.See Niels Chr. Sidenius (1983) "Danish Industrial Policy: Persistent Liberalism." *Journal of Public Policy*, 3, 1: 49-62.

82.IMEDE and World Economic Forum (1989) *op.cit.*: 122 (Table 5.38). Switzerland ranked second, Sweden ninth, Ireland seventeenth.

83.Ibid.: 125 (Table 6.05). Sweden ranked fourth, Switzerland eighth, and Ireland seventeenth.

84.David Gress (1982) "Daily Life in the Danish welfare State." *The Public Interest.* Number 69, Fall: 41.

85.Interview with Henrik Fugmann, Head of Section, Ministry of Industry, Copenhagen, 9 September 1988.

86.Ibid.

87.IMEDE and World Economic Forum (1989) *op.cit.*: 69 (Table 1.15). The countries were ranked according to industrial production as a percentage contribution to GDP.

88.Interview with Jesper Kongstad, Ministry of Industry, Copenhagen, 9 September 1988.

89.See Sidenius (1983) *op.cit.*

90.See Klaus Nielsen and Ove Kai Pedersen (1988) "The Negotiated Economy: Ideal and History." *Scandinavian Political Studies*: 79-101.

91.See Hans Christian Johansen (1987) *The Danish Economy in the Twentieth Century*: 164-166. Also, Bo Sarlvik (1983) "Scandinavia" in Bogdanor and Butler, eds. *op.cit.*: 122-148.

92.John Fitzmaurice (1987) "The Politics of Belgium and Denmark: A Comparative Perspective." *Government and Opposition*: 40, 41 (33-48).

93.Ibid.: 45 (33-48).

94.See Jim O'Leary (1987) "The National Debt: Implications for Fiscal Policy." *Irish Banking Review*: 3-19.

95.Niamh Hardiman (1987) "'Consensual Politics?': Public Goods and Collective Action in Ireland" in Scholten, ed. *op.cit.*: 167-169.

96.See McKee (1983) *op.cit.*: 188.

97.Hardiman (1987) *op.cit.*: 169.

98.It should be mentioned that Ireland has the only constitution that states that private enterprise is the preferred economic model.

99.See Eoin O'Malley (1985) "The Problem of Late Industrialisation and the Experience of the Republic of Ireland." *Cambridge Journal of Economics*: 145-147.

100.See Desmond A. Gillmor (1985) *Economic Activities in the Republic of Ireland: A Geographical Perspective*: 19.

101.See Maire Nic Ghiolla Phadraig (1986) "Religious Practice and Secularisation" in Patrick Clancy et. al., eds. *Ireland: A Sociological Profile*: 137-154.

102."Two-Sided Trinity" (1988) *The Economist* (November 19): 66.

103.G.W. Hogan (1987) "Law and Religion: Church-State Relations in Ireland from Independence to the Present Day." *The American Journal of Comparative Law*: 95.

104.See Gillmore (1985) *op.cit.*: Chapter One.

105.For an interesting viewpoint, Marx and Engels took a great interest in the "liberation" of Ireland. See Karl Marx and Frederick Engels (1975) *Ireland and the Irish Question*.

106.Kevin Boylde and Tom Hadden (1984) "How to Read the New Ireland Forum Report." *The Political Quarterly*: 403-404.

107.Ivor Kenny (1984) *Government and Enterprise in Ireland*: 14.

108.Kieran A. Kennedy, ed. (1986) *Ireland in Transition: Economic and Social Change Since 1960*: 39, 78, 153.

Chapter Three
Finance-Industry Relations:
Monetary Policies and Financial Practices

3.1 The Relationship Between Monetary Policy-Making and Finance-Industry Relations

The focus of this chapter is on how particular small European state financial systems in the 1980s either encouraged or discouraged productive activities that helped the small European state remain internationally competitive. Most importantly, while there exists a vast literature in political economy in the area of corporatism and concertation between the community, market, and State as a means for states to achieve international competitiveness, there are significantly fewer works by political economists on finance-industry relations.[1] For example, Lindblom's path-breaking *Politics and Markets*, which analyzes the relationship between government and business, virtually excludes any mention of the role of financial intermediaries in augmenting business' "privileged position."[2] Other notable scholars of networks, policy concertation, and collective action have also excluded the role of financial institutions in their definition of corporatism, tacitly favouring the examination of tripartite negotiations between government, business, and labour.[3]

Moreover, while authors like Zysman have analyzed "financial systems and the politics of industrial change" and authors such as Katzenstein have examined "small state industrial policies," relatively few scholars have examined finance-industry relations in the small state and the effects of these relations on the state's level of international competitiveness. This form of collective action for the small European state has remained as important, perhaps even more so, than labour- or State-industry relations.

Monetary policy is a government's response to private sector requirements. Its purpose is to promote economic stability and enhance communication among three critical actors involved in promoting international competitiveness - the State, industry, and finance. This chapter will examine the effects of the international monetary and financial environment from the latter part of the 1970s through the 1980s on the consequent domestic environments of each of the four small European states. It will analyze the monetary and policy responses to that environment in each of the case states, demonstrating the importance of communication between the private sector actors. The key points of discussion within this chapter are summarised in the chart on the following page. (See Figure 3.1.)

Figure 3.1

FINANCE - INDUSTRY RELATIONS: THE CASE STUDIES COMPARED

	DENMARK	IRELAND	SWEDEN	SWITZERLAND
Monetary policy emphasis during the 1980s	Austerity policy to control wage-inspired inflation	Passive policy highly reliant on EMS	High growth through devaluation and low interest rates	Control of inflation through monetary aggregates
Monetary environment during the 1980s	Inflation, high real interest rates, debt, low savings rate, moderate growth	Inflation, high real interest rates, debt, low savings rate, low growth	High growth, moderate real interest rates, some inflation	Low level of inflation, low real interest rates, high savings rate, moderate growth
Role of the Central Bank in the 1980s	Active role in fighting inflation	Prudential role	Active role in stimulating growth	Highly active role in controlling inflation and interest rates (the principal policy-making authority in Switzerland)
Bank ownership of industry	Up to 20 - 25% bank ownership of firms	Negligible	Sphere structure ensures bank ownership of industry	Up to 20 - 25% bank ownership of industry
Board directorships between banks and industry	Some cross-directorships	Few cross-directorships	Many cross-directorships	Many cross-directorships
Relative level of indigenous industry debt-equity ratios	High	Low	Very high	High
Relations between banks and industry during the 1980s	Close relations, though hampered by poor monetary environment	Relatively distant in comparison to other small European states	Close relations	Very close principal bank relations
Size of financial sector	Moderate; three major domestic banks with moderate presence in Scandinavia	Small; presence of two major domestic banks	Moderately large; three major domestic banks with powerful presence in Scandinavia, moderate presence worldwide	Large; three major domestic banks with significant presence worldwide; large banking (and insurance) sector ensured Switzerland as an international financial centre
Cooperative or detached financial institution-industry relations	Relatively cooperative	Detached	Cooperative	Cooperative

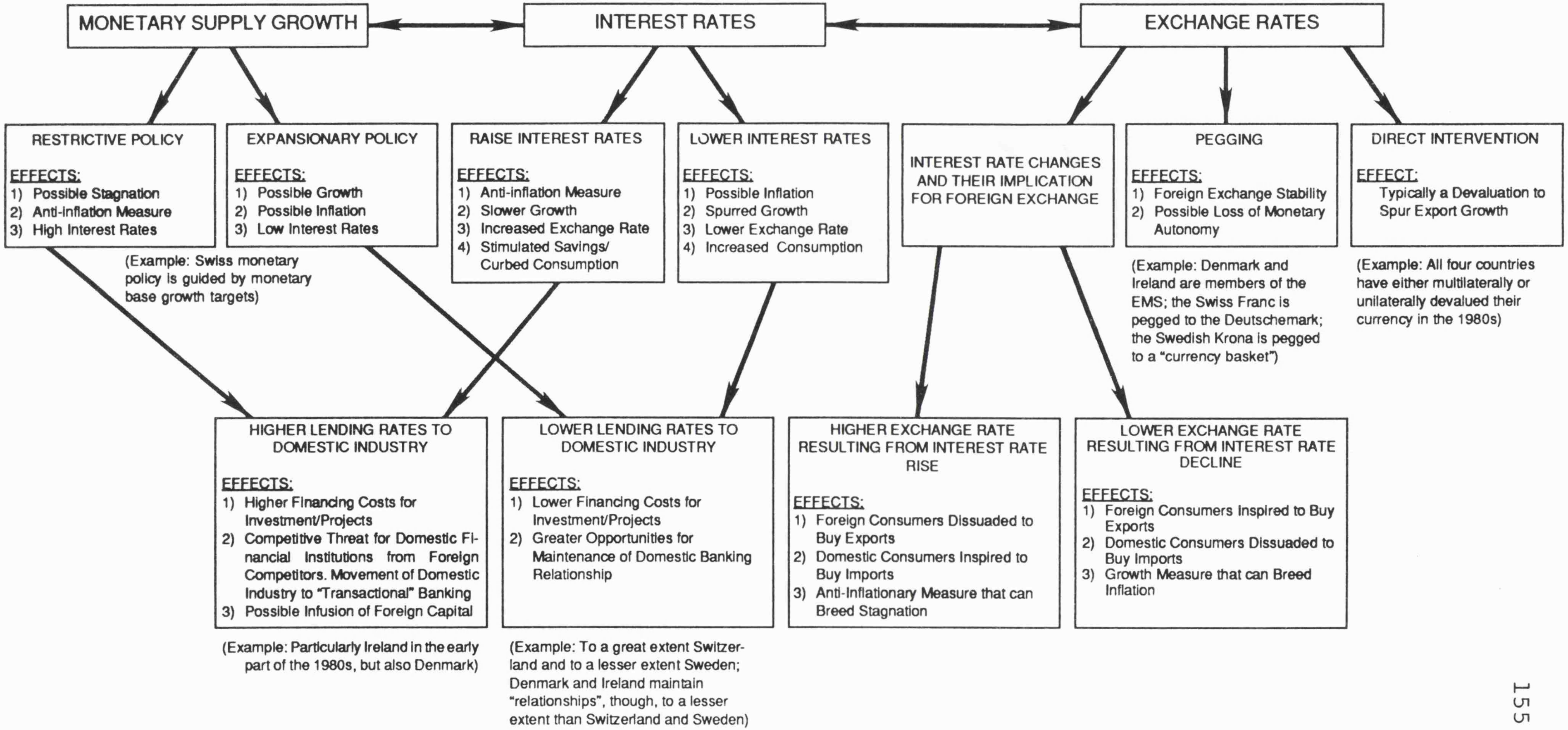
The first half of the chapter will concentrate on the role of central banks and regulators and their impact on the domestic monetary environment of the state, while the second half of the chapter will examine the role of private financial intermediaries, commercial banks, merchant banks, and insurance companies as sources of private finance. Public sources of financing as a form of industrial policy are touched upon in Chapter Five.

In terms of monetary policy, some small states have preferred to focus on interest rates, while others have focused on monetary aggregates to foster internal economic stability. Switzerland, for example, is a classic example of a small state able to control inflation by closely monitoring the growth of the money supply. With regard to the small European state's external stability, a stable foreign exchange rate is vital because of the small states significant dependence on foreign trade. Consequently, small European states attempted to maintain exchange rate stability by pegging their currencies to those of their main larger state trading partners.[4] (<u>See Figure 3.2.</u>)

In most small European states a few large players established the finance-industry communication environment of the 1980s. In Austria, Belgium, Denmark, Greece, Ireland, Luxembourg, Finland, the Netherlands, Norway, Portugal, Sweden, and Switzerland - one to three big banks controlled most of the credit markets within the country. In some cases, the monocephalic communication advantage afforded to the small European state engendered close

Figure 3.2

SMALL EUROPEAN STATE CENTRAL BANK MONETARY POLICY TRADE-OFFS AND THEIR POSSIBLE EFFECTS ON GROWTH



financial institution-industry relationships. In others, close finance-industry relations did not prevail throughout the 1980s.

When strong banking relationships in particular small European states produced lower real costs of capital for domestic industries relative to that which their international competition paid to their industries, a competitive advantage resulted. Augmented by close finance-industry affiliation through directorships and in some cases significant bank ownership of industry, some small European financial systems, notably the Swiss and the Swedish, were capable of providing the necessary funds for growth that allowed their industries to remain internationally competitive.

However, some relationships between financial institutions and industry, such as in Denmark and Ireland, were stifled in the 1980s. This stagnation came as a result of both relatively ineffective monetary policies, which increased real interest rates and adversely affected lending and exchange rates, as well as financial institution-industry relations that were less intimate than in other small European states. Under this scenario, the small European state lost the advantages against other states produced by its monocephalic concentration of industrial and financial institutions, a loss felt particularly in relation to large states such as the U.S. and the U.K.

In large states such as these, relations between banks and industry were based primarily on the capital markets and transactional banking. Defined by Yao-Su Hu as separatist systems, "government authorities, the managers of finance, and the managers of industry pursue their interests separately and go their separate ways....the relations between the three are of an arm's length, often adversarial nature."[5] For the small state in the 1980s, adversarialism in finance was a liability; monetary policies and financial practices needed to be coordinated to yield enough latitude for both public and private financial institutions to offer domestic industries a competitive cost of capital, a necessary staple to support economic growth and international competitiveness.

3.2 The International Monetary and Financial Environment

With American inflationary pressures spreading worldwide during the 1970s as a consequence of its "benign neglect" policy and the two oil price increases, inflation became a worldwide phenomenon affecting all the small European states. The Bretton Woods system of fixed exchange rates ended in 1973, and with the inception of floating rates, a new period of international financial and monetary turbulence ensued under a monetary system characterised by economic interdependence and hegemonic leadership by the U.S.

As a result of its significant export dependence, the small European state remained highly reliant on favourable and stable foreign exchange rates; however, the movement to flexible rates in 1973 resulted in worldwide monetary instability.[6] In 1978 the European Monetary System (EMS) was launched as a vehicle to strengthen the alignment of the European currencies.[7] This action was taken because of (a) European concern over the handling of the international monetary system by the U.S., (b) the polarisation of European currencies into the "strong" and "weak" according more to states' ability to control inflation rates than to their current account balances,[8] and (c) the desire to establish some degree of autonomy.[9]

The inflationary pressures of the 1970s, engendered for the most part by the oil shocks of 1973-1974 and 1979-1980, initiated a period of American deflationary policy-making. As the U.S. Federal Reserve increased interest rates, interest rates all over Europe concurrently escalated because of Europeans' fear of capital flight. Furthermore, with European interest rates rising, the effects on their exchange rates vis-a-vis the dollar were similar, making European exports to the U.S. less competitive.

By the beginning of the 1980s nearly all of the small European states experienced industrial decline and a deterioration in their terms of trade, yet they did not have the international monetary and economic power of large states to circumvent or overcome the situation. Despite trade and budget deficits under the Reagan Administration, the U.S. experienced significant economic growth through a strong dollar, a low inflation rate, and comparatively high real interest rates. Within this environment capital investment in the U.S. increased and business prospered.

However, many of the small European states faced difficulties in reflating their economies because their own depreciated currencies increased the prices for imported raw materials, which were for the most part factored in dollars.[10] As Robert Keohane explains,

> By 1973 and 1982, however, the terms of trade for these countries worsened by about twenty percent. This dramatic shift, caused largely by the huge oil price increases of that period, reflected the[ir] inability ... to force the costs of adjustment to higher oil prices on to others ....[11]

Accordingly, the option for the small European state was to adapt to the situation through flexible policy-making. For most small European states, reflation to overcome declining export competitiveness was through devaluation in 1981-1982; the best example of this tactic's use was the Swedish case.[12]

This unstable international monetary system of the 1980s was complicated by the volatile international financial system. With the U.S. experiencing an economic boom during the Reagan years (1980-1988), deregulation of financial markets accompanied the anti-inflationary high growth monetary programme. As a result of these deregulation effects, other domestic financial systems, including those in the small European states, followed the financial deregulation band-wagon, though to varying degrees and extents. Moreover, the continuing internationalisation of the financial markets began to outgrow the national systems. The advent of the Euromarkets and international syndicates of financial institutions providing securitisation for transnational industry became commonplace.[13]

In sum, with the international monetary and financial instability that ushered in and pervaded the 1980s, the internationally vulnerable small European state was forced to decide how to allocate the costs of adjustment between capital and labour and between inflation and unemployment. As a result of varying monetary and financial policy choices, the monetary and financial environments of each small European state differed.

3.3 The Monetary and Financial Environments in the Four Case Studies

A. Switzerland

Swiss monetary policy remained the pivotal point on which the economy rested during the 1980s, and the principal aim of Swiss monetary policy was achieving and maintaining a stable price level.[14] Consequently, throughout the decade the Swiss National Bank (SNB) acted as the tight-fisted national banker, autonomous from the government and maintaining virtual control over the money supply. It preserved a policy in which almost all restrictive financial regulations were eliminated, and its quantitative approach to monetary policy, trying not to influence directly the formation of interest rates or exchange rates, allowed Swiss banks to decide on the level of these rates.[15] As Georg Rich asserts,

The SNB has always regarded price stability as the

> ultimate objective of monetary policy. The SNB's focus on price stability reflects a firm political consensus in Switzerland as to the ultimate objectives of monetary policy.[16]

As a result of Switzerland's stable monetary policy, Swiss firms held a monetary advantage over their international competitors. Real interest rates were lower for Swiss firms working with Swiss banks, price stability assured that the domestic economy did not starve production or consumption, exchange rates remained stable (though relatively high), and a high savings rate assured liquidity in the system. As one banker stated, "The Swiss 'industrial policy' is made in part by the National Bank with its monetary policy."[17]

Perhaps the most striking aspect of Swiss monetary policy was that the SNB was the only central bank in the industrialised world during the 1980s that relied on the monetary base as a target variable and successfully achieved targeted rates.[18] (<u>See Figure 3.3.</u>) Further, the SNB's ability to maintain a tight linking between money supply and income expansion maintained price stability throughout the 1980s.[19] (<u>See Figure 3.4.</u>)

Figure 3.3
Target and Actual Growth Rates of M1
and Monetary Base in Switzerland, 1975-1986
(Target and Actual Change)

Year	Target Variable	Target Change %	Actual Change %
1975	M1	6	4.4
1976	M1	6	7.7
1977	M1	5	5.5
1978	M1	5	16.2
1979	Adjusted Monetary Base	-	-
1980	Adjusted Monetary Base	4	-0.6
1981	Adjusted Monetary Base	4	-0.5
1982	Adjusted Monetary Base	3	2.6
1983	Adjusted Monetary Base	3	3.6
1984	Adjusted Monetary Base	3	2.6
1985	Adjusted Monetary Base	3	2.2
1986	Adjusted Monetary Base	2	1.8

Sources: George Rich and Jean-Pierre Beguelin (1982) "Swiss Monetary Policy in the 1970s and 1980s"; Georg Rich (1984) "Is Swiss Monetary Policy Really Monetarist?" Lugano Monetary Conference; OECD (1987) *Economic Surveys: Switzerland*: 33.

Figure 3.4

GROWTH IN MONETARY BASE AND INFLATION RATE
IN SWITZERLAND, 1980-1984

(Percentage Change Over Preceding Year)

SOURCE: Georg Rich (1984) "Is Swiss Monetary Policy Really Monetarist." Lugano Monetary Conference; OECD (1985) Economic Surveys.

The SNB's quantitative approach to monetary policy attempted to avoid directly influencing the formation of nominal interest rates. Though industrial growth was slowed primarily because of relatively high exchange rates that adversely affected export growth, sustaining full employment in Switzerland required relatively less monetary stimulation than in other small European states as a result of Switzerland's greater economic strength. Nevertheless, real interest rates in Switzerland remained among the lowest in the OECD as a result of its anti-inflationary monetary policy, thus helping Swiss financial institutions provide low rates of lending to their industries. Accordingly, real lending rates in Switzerland ranged from two to three percent during the 1980s.[20] (See Figure 3.5.)

Figure 3.5
Long-Term Interest Rates in Switzerland and Other Countries
(Nominal and Real, %)

Nominal/{Real}

	1982	1983	1984	1985	1986
A	7.7{ 6.0}	7.2{5.4}	6.8{4.2}	6.7{5.3}	5.3{4.8}
B	4.2{-1.3}	4.2{2.1}	4.6{1.7}	4.4{1.2}	4.2{3.6}
C	7.8{ 3.2}	8.3{5.7}	7.0{5.0}	6.6{4.8}	5.6{6.0}
D	11.3{ 5.9}	10.4{5.0}	10.5{5.9}	10.5{4.8}	10.0{7.0}
E	11.8{ 8.0}	12.6{8.8}	12.1{8.2}	10.2{6.4}	8.9{7.1}

A= Japan, B= Switzerland, C= Federal Republic of Germany, D= U.K., E= U.S.A.

Source: OECD (1987) *Economic Surveys: Switzerland*: 37.

Beyond monetary targets to control inflation, a major aim of Swiss monetary policy throughout the decade was maintaining a strong, stable foreign exchange rate.

During the 1980s the SNB followed a "pragmatic" approach, in which it remained "prepared to deviate from - or even to give up temporarily -its money stock target if unexpected developments on the foreign exchange market call for such a course of action."[21] It, therefore, pegged the Swiss Franc to the German Mark, since the Federal Republic of Germany continued to be Switzerland's largest trading partner.

Throughout the 1980s the value of the Swiss France remained relatively high in comparison to the currencies of its major trading partners. As was asserted in a Lombard Odier and Cie publication, "Not a single currency has outperformed the Swiss Franc [in the] seventeen years since the Bretton Woods Agreement came to an end in 1971."[22] With a high relative value but slow, stable appreciation, the lack of volatility of the Swiss Franc helped to improve the state's terms of trade without damaging domestic commerce. (See Figure 3.6.)

Figure 3.6
Real Effective Exchange Rate Index, 1980-1987
Denmark, Ireland, Sweden, and Switzerland
(1980=100)

Year	Denmark	Ireland	Sweden	Switzerland
1980	100.0	100.0	100.0	100.0
1981	99.1	97.1	98.9	98.1
1982	98.4	100.3	93.2	102.7
1983	99.7	98.8	88.0	104.5
1984	99.1	97.3	95.3	101.3
1985	99.6	98.0	94.6	98.8
1986	101.7	103.4	94.8	107.5
1987	105.3	102.1	95.3	111.5

Source: International Monetary Fund (1988) *International Financial Statistics*: 111.

Moreover, with the financial services sector playing a vital role, the strong, stable Swiss Franc induced international investment in Switzerland throughout the 1980s. As Katzenstein contends,

> The role of the National Bank has been greatly enhanced by the system of floating exchange rates - to the point where its management of the Swiss Franc in international money markets is more important than any business cycle policy which the government might devise.[23]

Not only did the relatively high exchange rate induce investment in Switzerland, but the high savings rate in Switzerland, second only to Japan in the industrialised world, was a vital factor in the state's financial stability. (See Figures 3.7 and 3.8.)

Figure 3.7
Gross Savings Ratios of Selected Countries, 1980-1986

	A	B	C	D	E	F
1980	14.4	19.8	17.3	26.7	30.7	18.3
1981	12.3	22.3	16.0	28.7	31.9	18.9
1984	15.8	17.5	17.5	28.6	31.6	17.0
1985	14.9	16.3	17.8	30.0	31.4	16.5
1986	16.4	17.1	18.3	31.1	32.1	15.0

A= Denmark, B= Ireland, C= Sweden, D= Switzerland,
E= Japan, F= United States

Gross savings ratio = Gross national disposable income minus private and government consumption

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Source: OECD (1981-1987) Statistiques de Bases: Comparisons Internationales.

Figure 3.8
Total Official Reserves of Selected Countries, 1984-1986
(Ratio of Average Monthly Imports of Goods)

	A	B	C	D	E	F
1984	2.3	3.1	1.9	7.8	2.5	1.3
1985	3.3	3.3	1.5	7.7	2.3	1.4
1986	2.5	3.2	2.4	7.1	3.9	1.5
1987	2.5	2.9	3.0	7.3	3.4	1.5

A= Denmark, B= Ireland, C= Sweden, D= Switzerland, E= Japan, F= United States

Source: OECD (1981-1987) Statistiques de Base: Comparisons Internationales; IMF (1988) *International Financial Statistics*.

The Swiss propensity to save had a number of positive effects.

1. It helped dampen inflationary pressures as a result of Swiss investment over consumption.

2. It helped avoid current account imbalances.

3. It helped to avoid interest rate appreciation to overcome large capital supply reduction, which could result because of the low real interest rates in Switzerland.

4. It increased the opportunity for its financial institutions to accumulate liquid reserves for future investment capital.[24]

Furthermore, in terms of financial institution regulations, Switzerland remained one of the most financially deregulated countries in the world. During the 1980s Swiss banks were able to define their own range of operations because of the universal character of the banking system, and they were free to fix their own terms and conditions. For example there was no interest rate legislation except for a symbolic national maximum rate of eighteen percent. The securities markets were relatively free from regulation, and there was relative freedom of capital movement.[25] Capital requirements were weighted according to the risk associated with various assets, and consolidated balance sheets for capital requirements were introduced in 1980 for banks and subsidiaries. Banks were allowed to create hidden reserves, which remained a unique practise among small European states.[26]

In sum, despite relatively slow growth,[27] Switzerland's monetary environment remained highly secure, with an inflation rate remaining among the lowest in the OECD and exchange rates staying stable. Under strict monetary and deregulated financial conditions, coupled with such strong economic fundamentals as an extremely low level of unemployment, a steady current account balance, and socio-political stability, Switzerland maintained its position as an international financial centre. That strategy also paved the way for intimate financial institution-industry relations.

B. Sweden

While Switzerland favoured a strict monetary policy focused on fighting inflation, Sweden's commitment to full employment led to a monetary policy geared to economic growth. As a result, Sweden maintained a monetary environment in which relatively high inflation rates were overlooked so long as growth rates remained high.

Since 1977 the Swedish Krona has been weighted against an average of foreign currencies in a so-called currency-basket, which included the U.S. dollar and the Pound Sterling, several Scandinavian currencies, and most of the European currencies. As a result, Sweden maintained a relatively stable, pegged rate to all of its major trading partners;[28] from 1977-1986 Kronor deviations from the currency basket did not exceed two percent.[29]

From 1979-1983 with the explicit goal of improving its current account balance and government budget, the State imposed higher interest rates to inspire private capital inflow. At the same time, in 1981 and 1982, the Swedish *Riksbank* devalued the Swedish Kronor, which helped to increase profitability and counteract stagnation in the industrial sector. As a result, by 1984 production and investment had significantly increased. (See Figure 3.9.)

Figure 3.9
Gross Domestic Product Growth, 1980-1987
Denmark, Ireland, Sweden, and Switzerland

Year	Denmark	Ireland	Sweden	Switzerland
1980	-1%	3%	2%	5%
1981	-1	3	0	1
1982	3	3	1	0
1983	3	2	2	1
1984	4	-1	4	2
1985	4	4	2	4
1986	0	1	2	3
1987	-1	-1	3	2

*Calculated from constant 1980 prices of GDP.

Source: International Monetary Fund (1988) *International Financial Statistics*: 321, 429, 667, 671.

With near full employment and dramatic growth in production, the concern was that inflation would become a problem, and indeed it did become so because of wage increases, despite attempts by labour to control wage costs through a disinflation model.[30] With high consumption from the mid-1980s onwards as a result of the domestic economic boom, gross domestic savings as a percentage of GDP in Sweden fell in 1987 to just over seventeen percent, the fourth worst in the OECD (just ahead of the U.K., U.S., Denmark, and Greece).[31] With less liquidity in the system and higher inflation spurred on by increased consumption and wage drift, inflationary fears persisted, although less austere measures were taken in Sweden than in other countries such as Denmark.

As Sweden experienced significant growth after the 1981 and 1982 devaluations, the domestic monetary environment changed dramatically from that of the former interventionist decade. With a previous interest rate system, rates were regulated through a penalty system that put an upper limit on credit market interest rates such as treasury bills. This system was dismantled by 1983 into a central bank interest rate ladder, which "stepwise increased costs as borrowing grew."[32] Under this market-oriented monetary policy, both asset and liability management were determined on the basis of credit demand, funding costs, and interest rate developments. Moreover, the *Riksbank* removed foreign exchange controls,[33] recognising the reduced effectiveness of these restrictions in a world of MNCs and sophisticated international capital markets.[34]

In sum, the monetary and financial environment in Sweden was based on the principles of high growth and financial liberalisation. Different from Switzerland, Swedish authorities were less concerned about inflation (as well as savings) and more attentive to fostering growth. Such high growth was significantly augmented through the devaluations of 1981 and 1982, and the ensuing monetary environment became more market-oriented than in previous decades.

C. Denmark

Throughout the 1980s Denmark's current account deficit, financed through the most part by foreign borrowing,[35] hampered its level of international competitiveness, because not only were Danes consummate consumers but also because Danish industry lagged behind other European industrials in terms of export competitiveness. The persistent current account deficit and national debt implied a decrease in the monetary base that by the middle of the 1980s put upward pressure on the domestic interest rate. This pressure in turn stimulated private capital inflow, which caused the exchange rate to increase and precipitated a reduction of overall international competitiveness of its industry.

At the onset of the decade Denmark experienced extreme inflation and unemployment (both ranging from ten to fourteen percent), interest rates at twenty percent, and low productivity. After this period, the Danish economy did experience growth from 1983-1985, with inflation only around three to four percent as a result of relatively limited wage increases. Interest and mortgage rates were reduced under a system of fixed rates. Indeed, the *Nationalbank* faced a difficult situation in managing the monetary supply to control inflation; hence, a short-term "fixed" interest rate scheme was devised to help control inflation.[36]

As a member of the EMS since 1979, the Danish Kronor was kept within a constant average (i.e., the "snake") with its major trading partners, notably West Germany, but also many other countries within the EC. Unlike Sweden, whose currency was linked to the dollar as a result of its currency basket, Denmark's policy-makers preferred small, infrequent adjustments through short-term interest rate changes (as opposed to the strict use of monetary targets as in Switzerland) rather than exchange rate tinkering,[37] though in 1981-1982 Denmark followed Sweden in devaluing its currency. However, as Anders Moller Christensen of the Danish *Nationalbank* asserted, "In the early part of the eighties interest and mortgage rates were sky-high, but in 1982 after the devaluation and rates became fixed, interest rates declined steadily through 1986. And the Kronor was also stable ... kept within a constant average. What finally destroyed us in 1986 were rising wages."[38]

As will be discussed in Chapter Four, Denmark experienced significant wage drift that severely strained its ability to control inflation and interest rates. While attempting to maintain control, yet facing increasing wage demands, not only was inflation rising, but growth actually decreased by 0.7% in 1987, marking a period of economic stagflation in Denmark. Real lending rates rose to over eight percent by 1986,[39] and the Krona appreciated by 4.6% in 1986, and 3.0% in 1987. Manufacturing cost appreciation ensued, as Denmark's "cost competitiveness" deteriorated by eight percent in 1987.[40]

The Danish government attempted, using the Potato Diet, to reduce its debt obligations and the major current account deficit through a fiscal policy designed to dissuade consumption and promote savings; nonetheless, private sector savings throughout the 1980s remained low because of the high Danish standard of living coupled with the highest personal taxation system within the OECD leaving insufficient household funds for savings.[41] In 1987, Denmark ranked twentieth out of twenty-two OECD countries in terms of gross domestic savings as a percentage of GDP.[42] While Danish financial institutions had historically suffered from low levels of liquidity as a result of the Dane's propensity to consume rather than save, private sector savings worsened over the period, decreasing by over four percent in 1986 and remaining at relatively low levels thereafter.[43]

In its attempt to bolster the state's financial position, the Danish government introduced a number of measures to liberalise financial markets, which included the abolition of lending ceilings, price formation on bond markets, lending rate agreements, and many foreign exchange controls.[44] While both inward and outward transfers of capital and all borrowing and lending were subject to restrictive exchange controls, by 1983 the experience of Denmark illustrates the ability of monetary authorities to maintain a fixed exchange rate and thereby aid in aligning interest rates with those of its competitors.[45]

In sum, the Danish economy continued on a course to liberalise its financial markets and to impose austerity measures to eliminate the current account deficit. However, the ability to slow inflation and dampen consumer demand of imports was overshadowed by significant wage drift; the combination of a tight-fisted monetary policy coupled with wage-inspired inflation resulted in stagflation and high levels of unemployment by the mid-1980s.[46] (See Figure 3.9.) While foreign exchange reserves increased because of high exchange and interest rates that helped liquidity, the deficit in the current account prevented a loosening of monetary policy.[47] As Governor of the Danish Central Bank Erik Hoffmeyer stated in a speech, "It can be said that we are in a tight spot between a level of domestic costs which is too high and poor sales opportunities outside Denmark .... We need a lower level of interest rates ... created in future fiscal policy and cost trend decisions."[48]

D. Ireland

With significant economic problems thwarting Ireland's ability to foster industrial development, the monetary environment in the Irish Republic during the 1980s was less favourable than in the other three small European states for the promotion of finance-industry relations. During the decade, Ireland faced a large current account deficit in which the State maintained total foreign and central government debt burdens that were among the worst in the OECD; as a result, Ireland's credit rating was particularly poor.[49] With a high taxation rate as a result of a relatively demanding personal taxation system, Ireland also had a poor level of savings. (See Figure 3.7.) Along with such problems, during the 1980s it faced high levels of unemployment and inflation.[50]

With the international recession of the early part of the 1980s, Ireland stagflated longer than the other three countries not only because of the high domestic interest rates, which mirrored international rates, but also because of its lower level of development and the wage-price spiral that ensued and lasted through 1987.

As a member of the EMS since 1979, the Irish Pound was kept within a constant average with its major European trading partners through the "snake." However, unlike in Sweden, whose currency was linked to the Dollar and British Sterling as a result of its currency basket, in Ireland fluctuations in the Dollar and the Pound Sterling, both important trading partners outside the EMS, caused exchange and consequent interest rate problems for Irish policy-makers.[51].

Nonetheless, most of Irish monetary policy was based on a market-oriented approach to monetary control. Monetary targets were not used, and the primary influence on interest rates was the trend in international rates. As Tomas Cofaigh, Governor of the Central Bank of Ireland explained,

> [Irish monetary policy is] geared towards concentrating on the external value of the currency, seeking to keep it within a tolerable range .... As is widely appreciated, the dominant influence on Irish rates is the trend in international rates. In an economy as small and as open as ours, it would be unwise ... to pursue an interest-rate policy which did not have due regard to the level of external rates.[52]

As a consequence, international inflationary pressures and their deleterious effects on the Irish economy caused a significant tightening of domestic credit. At the same time, inflation was spurred through significant wage increases, the details of which are explained in Chapter Four.

With Ireland a member of the EMS in 1979, policy-makers in the government debated how to maintain its important agricultural sector, either by lowering inflation to EMS levels, or in the alternative, devaluing the currency. With the inflation rate not falling at the beginning of the 1980s and with policy-makers against devaluation, farmers faced a severe price-cost problem due to modest EC price increases coupled with inflationary Irish costs. Contends S.J. Sheehy:

> There is no doubt, therefore, that the greatest tragedy of EC membership to-date is the manner in which exchange rates operated to the detriment of Irish agriculture after joining the EMS. If Ireland's price experience had been that of the average, prices now would be twenty-six percent higher than they are [1988], and as a consequence farm income would be some fifty percent greater and agricultural exports would be worth some four hundred million pounds extra.[53]

As a result of this relatively passive monetary policy, between 1978-1986, real prices received by farmers fell two times over the average fall for the EC.[54]

Moreover, the Central Bank of Ireland maintained a relatively strong hold over financial institutions through an interest rate grid system that tightly regulated the ability of financial intermediaries to raise the prices of their products as well as the regulation of liquidity through strict ratios that ensured reserve adequacy.[55] Financial liberalisation began by the mid-to-latter part of the 1980s.[56]

Only as a result of bargaining during the mid-1980s between the so-called "social partners," including the minority *Fianna Fail* party, the Confederation of Irish Industries (CII), Federated Union of Employers (FUE), and the Irish Confederation of Trade Unions (ICTU), a *Programme for National Recovery* was developed in order to invigorate the listless Irish economy. While subsequent chapters will discuss the more major components of the *programme*, mot notably wage reductions and industrial policy changes, economic stagnation was viewed as a consequence of high nominal and real interest rates, which thwarted investment. Consequently, one major aspect of the *programme* was an emphasis on reducing Ireland's inflation rate, and "Monetary policy will be determined by the need to bring about the lowest possible interest rates..."[57]

In sum, throughout the 1980s Ireland was faced with wage drift, foreign debt, and current account deficits that adversely affected its domestic monetary environment. While small European states such as Denmark with similar problems actively pursued a policy of austerity, Ireland maintained a relatively passive monetary policy in which its primary goal was to maintain reserves adequacy and protect the exchange rate. Only by the end of the decade did Irish policy-makers attempt to spur growth through a monetary policy geared to reduced real interest rates which would consequently foster closer finance-industry relations.

3.4 Finance-Industry Relations in the Small European State

This section will examine what Lash and Urry refer to as "finance capital"[58] and what Yao-Su Hu alludes to as "industrial banking." In more concrete terms, finance capital or industrial banking can be characterised by:

> 1) the provision of long-term finance (long and medium-term debt, or such debt plus equity) to enterprises and entrepreneurs in the industrial and commercial sectors....
>
> 2) a sense of purpose, a perceived role or mission, an institutional culture or a set of attitudes, which is reflected in (a) a readiness to promote, encourage, and support industry, (b) a willingness to accept a measure of responsibility for the performance of industry..., and (c) an ability to understand the problems of industry due to close relations ....[59]

Finance-industry relations in the industrialised world have been patterned in one of two ways: a capital market based system, such as that in the United Kingdom and the United States; or, a credit based system, such as that in Japan and West Germany.[60] In the former case, resources are allocated through competitively established prices, and relations between government and industry are at an arm's length. In the latter case, prices can be administered by the government, which encourages State intervention in industrial affairs, or on the other hand, financial institutions in a country may be so powerful that they have a profound influence on industry. Yao-Su Hu refers to these financial systems as "integrationist." He explains that,

> ...governments in the U.K. and the U.S. from time to time exhort businessmen to export more, to invest more, to innovate more .... in the integrationist systems ... finance is channelled on a continuous basis on a sizable scale, with minimal fuss and fanfare, towards national priorities.[61]

In terms of credit-based financial systems, the role of the Bank of Japan (BOJ) serves as an illustration of the role government may play in monetary policy-making (providing a financial environment that can breed industrial growth without inflation) and in providing lending direction. The BOJ controls interest rates and rediscounts in order to provide private banks with adequate reserves; it also uses credit rationing and "window guidance" to "direct lending to favored uses."[62] The BOJ has been "guarantor of the system;" it has complete and detailed control over the "private banks".[63]

The other form of credit based financial system, referred to by Hu as "integrationist,"[64] is that where financial institutions do play a preeminent role in the economy, but the government does not intervene in credit allocation. In the Federal Republic of Germany, for example, banks not only have significant economic power, they also have the legal right to own a substantial amount of equity in German corporations, making them not only sources of financing but also "prefects" of management.[65] Known as *hausbanken*, the major German banks, such as *Deutschebank* and Dresdner, have particular corporations which they help finance as well as own a twenty-five to thirty percent equity share.[66] *Deutschebank*, for example, maintained 28.5% ownership of Daimler Benz in the 1980s.[67] (See Figure 3.10.)

Figure 3.10
Financial Systems and the Adjustment Process

Country	Financial System	Adjustment
France Japan	credit-based, price-administered	State-led
W. Germany	credit-based, institution dominated	Tripartite- negotiated
U.K. U.S.	capital market-based	unclear (U.K.) company-led (U.S.)

Source: John Zysman (1983) *Governments, Markets, and Growth: Financial Systems and the Politics of Industrial Change*: 94.

What makes the Japanese and German cases so special is that their financial systems are illustrative of the role financial institutions can play in helping to advance national industry. Both countries, for example, have been able to control inflation while maintaining relatively low interest rate levels. Therefore, while the average debt/equity ratio in the United Kingdom and the United States has been about 1:1.5, Japanese and German ratios have been as high as 4:1,[68] meaning Japanese and German industry maintain an advantage of holding greater debt over equity. These ratios suggest that industries prefer to utilise debt instruments through lending and bond issues, as opposed to equity instruments such as the issue of common stock, in their gross capital formation.[69]

With the recognition that finance could be a major tool for industrial growth, finance-industry relations in the small European state afforded industry the ability to maintain high levels of investment, which helped small state industries preserve their levels of development and competitiveness. Notably similar to the German financial system, banks remained preeminent among financial institutions to widely varying degrees in all of the four small European states analyzed in the thesis. In a similar vein to what Zysman contends in regard to the German financial system, "All routes to corporate external finance - loans, bonds, and equity - [led] back to the banks [in the 1980s]."[70] Hence, it is asserted in this thesis that in each of the four small European states, the financial systems were in the terminology of Yao-Su Hu "integrationist" and in the terminology of John Zysman, credit-based and, to different extents, institution-dominated throughout the 1980s.

For the small European state, the monocephalic communication advantage would suggest that in most small European states finance-industry relations would appear to be relatively close. Indeed, with only a few large players on both the financial and industrial fronts, intimate banking relations could augment a small European state's industries' international competitiveness. For example, throughout the 1980s Swiss firms such as Nestlé maintained close banking ties with the large Swiss bank *Credit Suisse*; Swedish companies such as Atlas Copco sought financing mainly from the largest Swedish bank, *Skandinaviska Enskilda Banken* (SE Banken); Danish firms such as Carlsberg banked with *Den Danske Bank*; and Irish companies such as Guinness maintained financial relations with the Bank of Ireland.

Similar to the German *hausbanken*, many small European financial institutions in the 1980s were not only involved in the financing of industry but also in ownership and management.[71] Such structures were prevalent in small European states such as Denmark, Finland, the Netherlands, Sweden, and Switzerland. Moreover, under such credit-based systems with companies being highly leveraged, small European state banks held significant power in particular industries because of their ability to control debt.

The following section will analyze and compare just how close finance-industry relationships were in each case country in the 1980s. In Switzerland in particular, but also in Sweden, finance-industry relations were characterised by close associations. With a seemingly competitive advantage as a result of the small European state's small size, economic pressures coupled with relatively distant finance-industry relations stifled economic progress and international competitiveness in Denmark and Ireland.

3.5 Finance-Industry Relations in the Case Studies

A. Switzerland

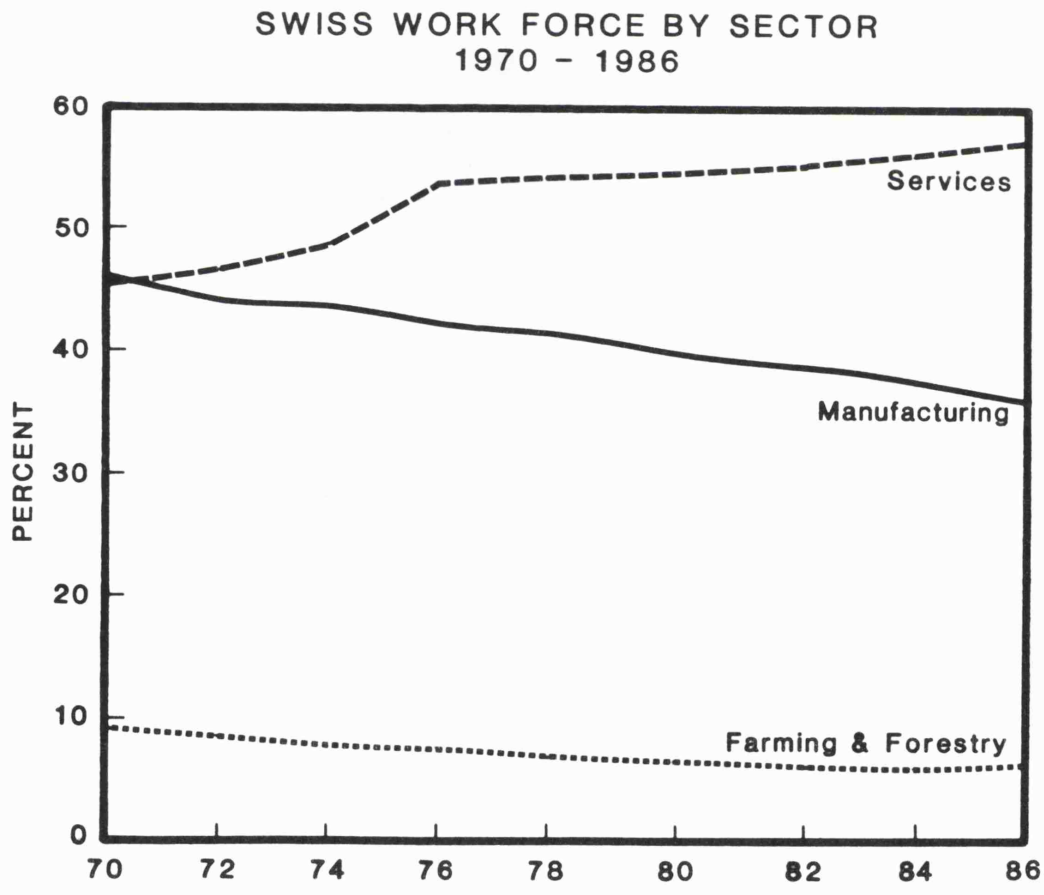
As a result of its low inflation rate, high savings rate, high degree of political and economic stability, and deregulated and non-restrictive banking regulations, financial institutions played the pivotal role in maintaining and augmenting Switzerland's relatively high level of international competitiveness in the 1980s. From an international perspective, throughout the decade Switzerland remained one of the five largest financial communities in the world (the other four being Japan, West Germany, the United Kingdom, and the United States). The importance of the tertiary sector (including finance) in Switzerland is evidenced by its employment throughout the 1980s. (See Figure 3.11) Asserts the OECD in a report on Switzerland,

> The financial system is among the most valuable assets of the Swiss economy. Its importance in world financial markets far exceeds the relative size of the country's economy; it affects her macroeconomic performance, through the direct contribution to GNP, the net exports of financial services, and its intermediation role between surplus and deficit units.[72]

As illustrated earlier by Switzerland's high rate of savings, Swiss financial institutions evolved from the Swiss propensity to save as opposed to spend, which provided these institutions high levels of liquidity for international and domestic lending as well as dampening consumption, which kept inflation levels low. With such liquidity in the system, banking became a Swiss priority in the eighteenth century, with Geneva private banks dominating the field and providing special services. Explains Nicholas Faith,

> So they were - and remain - partnerships dependent on a personal relationship for their business. They were discreet.... So the banks pioneered the methods that were to become routine in the Swiss banking community: letters from the banks to their clients were not posted in Switzerland .... and to this day Swiss bankers to not have 'banker' marked in their passports. Rather they are 'lawyers' or 'businessmen.'[73]

Figure 3.11



Source: Swiss Statistical Yearbook (1987).

From the 1800's onwards the Swiss banking system was comprised of both public and private banks, the public ones being cantonal banks and savings and loan associations that accounted for sixteen percent of the total assets of Swiss banks by the end of the 1970s.[74] By the 1980s banking was dominated by the three big banks, Union Bank of Switzerland. Credit Suisse, and Swiss Bank Corporation. (See Figures 3.12 and 3.13.)

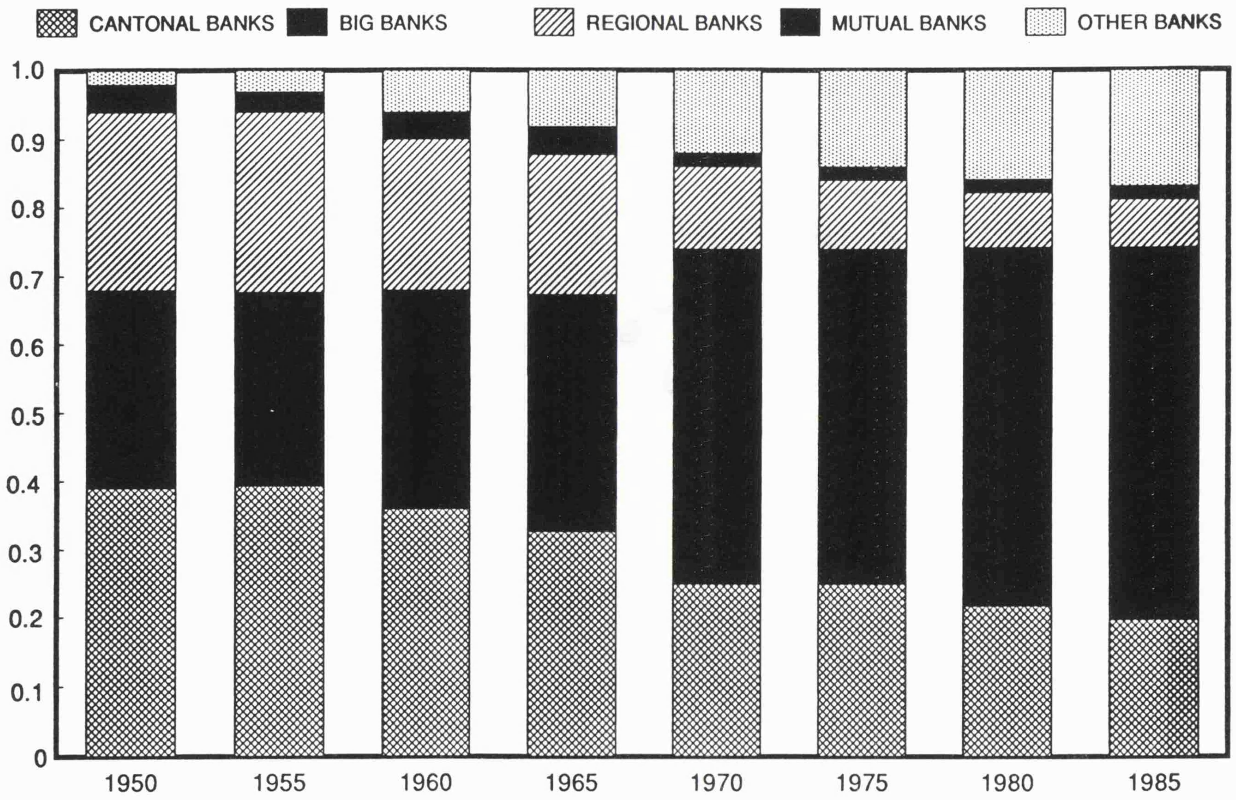
Figure 3.12[75]
Reported Net Profit, Credit Suisse 1978-1986
(Million S.Fr.)

Year	Net Profit
1980	281.0
1981	275.8
1982	303.0
1983	351.6
1984	417.4
1985	507.0
1986	566.3

Source: Credit Suisse (1987) *130th Annual Report*: 45.

Figure 3.13

MARKET SHARE IN THE SWISS BANKING SECTOR



Source: Swiss National Bank; OECD (1987) Economic Surveys : Switzerland : 62

The attractiveness of Swiss banking during the 1980s can be attributed to:

1) its "universal banking system" created the advantage over other countries where banking was more specialised (e.g. in Switzerland, there was no delineation between merchant and commercial banking);[76]

2) a stable political environment based on laissez-faire principles in which international investors were not subjected to various political risks;

3) a stable, strong Swiss Franc in which there was little exchange risk;

4) confidence in Switzerland's monetary policies, which engendered stable currency valuation, low interest rates, and low levels of inflation;

5) banking secrecy that was more protective in Switzerland than in any other country.[77]

With this monetary power, Swiss banks in the 1980s were able to exercise meaningful financial influence both through their power as a vital industrial sector, as illustrated above, and by aiding Swiss industry through relationships among the SNB, the Swiss Bankers' Association, and industry.

Throughout the 1980s the National Bank, which remained autonomous and kept a high degree of independence, reported to the Federal Council; the official link was through the Ministry of Finance.[78] The SBA, which represented the banks, also maintained a constant dialogue with the SNB. Indeed, there were also direct relations between industry and the central bank.[79] In 1977 the Chairman of Nestle took a seat on the Banking Council (*Bankrat*), which (at least nominally) supervised the National Bank. He was also appointed by the Federal Council as a member of the Swiss Commission for Foreign Trade Policy.[80] Moreover, the three major banks maintained a firm stance in favour of preserving low real interest rates partly to protect smaller banks (via "local conventions") that remained vital for the maintenance of the Swiss economy. Real interest rates were maintained at exceptionally low levels.

In addition, debt-equity ratios of Swiss indigenous industry were particularly high, which further reduced Swiss industries' cost of capital, increased return to equity, and therefore induced equity investments in the firms. Most importantly, with the real cost of funds being cheaper for Swiss firms, they could act more aggressively in the international marketplace against foreign competitors who were required to pay more for long-term development and growth. (See Figures 3.14 and 3.15.)

Figure 3.14
Debt-Equity Ratios, Non-Financial Enterprises
Switzerland and other Selected Countries
(Fixed Assets, Historic and Replacement Costs)

	Fixed Assets (Historic Cost)	Fixed Assets (Replacement Costs)
Switzerland	2.1	1.3
Germany	2.3	1.3
Japan	-	1.3
United Kingdom	1.1	0.6
United States	1.1	0.6

Source: OECD (1987) *Economic Surveys: Switzerland*: 58.

Figure 3.15
Debt-Equity Ratios: A Sampling of Swiss Enterprises
(Non-financial enterprises)

Sample size (total number of companies)	:	85
Average (mean) debt-equity ratio	:	1.50
Average (median) debt-equity ratio	:	1.18
Highest debt-equity ratio	:	5.46
Lowest debt-equity ratio	:	0.60

Debt-equity ratios of notable companies

Ciba Geigy	:	0.60
Jacobs Suchard	:	1.11
Nestle	:	1.37
Sandoz	:	0.61
Swissair	:	2.97

Source: Morgan Stanley (1989) *Capital International Perspective*. (October).

Throughout the decade industry was also at a prime advantage because of the principal bank structure,[81] even though the issue of shares and equity securities as a percentage of gross fixed capital formation averaged only 1.9% between 1983-1985, indicating Swiss industrials' preference for debt financing as opposed to owning capital.[82] Historically, bank-industry relations included those between the Swiss Bank Corporation with the chemical industry, mainly because both were based in the Basel area, and *Credit Suisse* with the machine tools industry (such as Brown Boveri). Also, each of the three big banks had members on the boards of directors of the major Swiss industrials.[83]

In Switzerland throughout the 1980s ownership of industry, like in Sweden, was very much based on family business. The Abbegg family owned fifty percent of Nestle, while Ciba-Geigy was five percent owned by the Phlanta, Geigy, and Iselin families. As Pierre Grou asserts,

> ... Switzerland is the one country in which the technocratic reorganisation of the dominant class does not yet seem to have led to changes in the capital structure of the multinational corporations. A family oligarchy reigns, through capital ownership, over the 'Swiss Empire'....[84]

Like the Swedish sphere structure, which will be discussed in the following section, the major Swiss MNCs such as Sandoz, Ciba-Geigy, Alusuisse, Nestle, Sulzer Brothers, and Brown Boveri were tied during the 1980s into families like the Iselins, Sulzers, Schmidheimys, Schwarzenbachs, and Haefners - all of whom were linked through capital ownership with the Big Three banks.

Although Switzerland's bank-industry relations were not quite as extensive as those in West Germany under the *hausbanken* structure, primarily because of the differences in bank ownership of industry is higher in Germany (twenty-five percent) than in Switzerland; however, the principal bank relationship did extend as far as twenty percent ownership of industry by a particular bank.[85]

The best historical example of this relationship occurred with the near demise of the watch industry and the intervention of the banks. The *Societe Suisse Pour L'Industrie Horlogere* (SSIH, or Swiss Watch Corporation), a holding company with twenty-seven subsidiaries including its two flagships Omega and Tissot, went bankrupt in 1980-1981 due to:

1) the problems associated with an undervalued franc

and an overvalued dollar;

2) Omega continuing to produce thicker watches than what the market called for, thus bringing a sharp drop in sales and rapidly increasing inventories; and

3) significant competition from electronic watch makers, particularly Japan.[86]

In 1980 the SSIH could not comply with the instruction of an industry-wide arbitration decision to pay cost of living bonuses to its workers totalling $3.6 million, and it was at this point that the banks intervened. In essence, they did the following:

1) stocks previously valued at $35 million were written down to $175,000, five percent of the previous value;
2) through converting $49 million of their credits to long-term capital, six banks increased the new capital base to $51 million;
3) the six banks agreed to write off credits totalling over $51 million;
4) the banks directed the merger of SSIH and ASUAG (another watchmaking company which had huge losses in 1982) and infused $300 million in new capital.[87]

This episode highlights the significant power that the big banks held in Switzerland throughout the 1980s and their ability to influence directly the economy - more than the State itself, which ironically approached the banks to coordinate the watch industry bailout.[88] Certainly the social and political consequences of such bank decisions in Switzerland were distinctly similar to those decisions States themselves usually make. As Katzenstein explains in regard to such strategies,

> One is a financial strategy intent on maximizing bank profits (or minimizing losses) irrespective of the consequences for employment, regional development, and the industry's long-term growth. The other is an industrial strategy that seeks to strengthen the technological and market strength of the company and takes a long-term attitude that includes industry-wide

> concern and, almost inevitably, further substantial infusion of capital.[89]

Throughout the 1980s credits to Swiss debtors accounted for thirty percent of the activity of Swiss big banks. In addition, the balance sheet of domestic banks (the cantonal banks, regional/savings banks, loan associations, and others), which accounted for one-third of the overall total in the banking industry, showed only seven percent of their business overseas. Moreover, Swiss banks had a much smaller part of their assets abroad (around fifty percent) as compared to foreign banks in Switzerland, who averaged around seventy percent. Thus, Swiss banks were prudent with their assets, infusing capital into Swiss industry (where they have significant control over the outcome) and limiting their credits mainly to OECD countries.

The SBA worked primarily with the three largest banks, maintaining a dialogue principally concerned with maintaining ethical standards, an issue that was complicated by Switzerland's famous secrecy laws.[90] The formal agreement among banks, and regulated by the SBA, included the prohibition against the active assistance of capital flight and tax evasion.[91] Perhaps most importantly, the SBA acted as an overall press agent to quell possible negative publicity about the banking sector, a necessary duty to preserve international confidence in its banking sector.

The economic record of Switzerland concomitantly with socio-political stability allayed investor fears of possible political risks, resulting in an inevitable inflow of financial resources from the rest of the world throughout the 1980s.[92] The factors listed earlier contributed to the international confidence necessary for Switzerland to maintain its strategy of being an international financial centre. They also explain why the Big Three banks remained among the most powerful financial institutions in the world. (See Figure 3.16.)

Figure 3.16
Europe's Ten Largest Banks, 1987
(By Proportion of Equity to Assets and Return on Assets)

Bank	Equity/Asset Percentage
Credit Suisse (Switzerland)	6.23%
Union Bank of Switzerland (Switzerland)	6.14
Swiss Bank Corporation (Switzerland)	6.06
Rabobank (Netherlands)	5.79
National Westminster (United Kingdom)	5.70
Midland (United Kingdom)	5.54
Lloyds (United Kingdom)	5.33
Paribas (France)	5.25
Barclays (United Kingdom)	4.98
Deutsche (Federal Republic of Germany)	4.22

Bank	Return on Asset Percentage
Credit Suisse (Switzerland)	.53%
Paribas (France)	.53
National Westminster (United Kingdom)	.52
Union Bank of Switzerland (Switzerland)	.49
Swiss Bank Corporation (Switzerland)	.49
Rabobank (Netherlands)	.49
Algemene (Netherlands)	.35
Amro (Netherlands)	.34
Societe Generale (France)	.34
BNP (France)	.32

Source: "Which Are Europe's Twenty-Five Top Banks?" (1989) *Euromoney*. (January): 32.

From 1975 to 1985 Switzerland's share in international banking covered a range of ten to fifteen percent of the world market.[93] While Swiss exports accounted for only 1.5% of total world exports from 1980 to 1985, Swiss banks held about seven percent of global foreign assets, putting them in third place after US and Japanese banks.[94] With a major presence in the north American market, new issues of securities, both shares and bonds, were typically sponsored by one of the major Swiss banks, which joined major underwriting syndicates with other large financial intermediaries, who were often Swiss as well. Throughout the decade the Big Three "banks perform[ed] all of the chief functions associated with securities issuance, from underwriting and distribution to the actual investing on behalf of clients, both fiduciary and retail."[95]

Much of the reason for their international success throughout much of the 1980s (at least up to the crash of 1987) was due to their ability of the Big Three banks to work together, posting similar changes in their profits and dividends and working within pre-arranged syndicates. "In no small part ... this dominant position has been achieved by their sticking together in an often cozy arrangement based on mutual benefit."[96] However, by the end of the decade, the three big banks began to formulate separate strategies as a result of post-crash international economic turbulences and stated anti-trust restrictions by the Swiss Cartel Commission to loosen price-fixing arrangements.[97]

Ironically, at least in terms of Swiss Franc public issues, such restrictive language imposed by the Cartel Commission remained only rhetoric. The Big Three Swiss banks remained in a permanent and exclusive syndicate with their smaller affiliates by forming an adjoining *ad hoc* syndicate; the entire syndicate would *only* participate in a public Swiss Franc offering if it was sponsored by a party within the syndicate, which would typically take twenty percent of the issue.[98]

In evaluating financial dynamism, *The World Competitiveness Report* weighted both "factual" statistical data and "perceived" survey analyses in categories ranging from interest and savings rates to the role of banks and finance; Switzerland ranked first among twenty-two OECD countries. In standard deviation values, Switzerland scored 0.90, compared with Japan's 0.87, Germany's 0.47, and the U.S.' 0.36.[99]

B. Sweden

While Switzerland was the best example of a small European state with strong bank-industry relations in the 1980s, Sweden also maintained a credit-based system of corporate finance.[100] Indeed, Sweden remains one of the best examples of a country whose financial institutions played a vital role in its industrialisation by providing banking capital for its developing industries from the 1890s onwards.[101] While the major Swedish commercial banks, *SE Banken*, *Svenska Handelsbank* and State-owned *PK Banken* have not been as globally oriented as the Big Three banks of

Switzerland, these banks have been important financing sources for Swedish industry during the decade.

In 1987 there were fourteen commercial banks, nearly one hundred and sixty savings banks and twelve cooperative banks; the commercial banks held sixty-six percent of total deposits. Throughout the 1970s the *Riksbank* (the Swedish central bank) and the Banking Inspection attempted to maintain a tight grip on domestic banking, the one major objective being to make financial institutions safe for depositors.[102] While the Banking Inspection verified private banks' capital adequacy requirements (since there is no institution in Sweden such as the FDIC in the U.S.), the *Riksbank* continued to impose a so-called "penalty rate," which placed an upper limit on other credit market interest rates such as treasury bills. Because of this policy, the *Riksbank* was able to keep the credit market tight enough to force banks to have positive amounts of borrowed reserves. Short-term interest rates were determined by the penalty rate, and the banks were not allowed to go any lower than this rate, because doing so could depreciate their borrowed reserves.[103]

In the 1980s, however, the *Riksbank* loosened its grip. While still firmly believing in "prudent banking," including major banking provisions against lending to the Third World, the *Riksbank* eased its control over banks in terms of capital adequacy requirements and interest rate controls. Moreover, while foreigners were not allowed to own shares in Swedish banks, in 1986 foreign banks were allowed to perform normal banking activities in Sweden. At the end of 1986 thirteen foreign banks had applied for licences to undertake banking activities in Sweden, the major players being the U.S. and French banks. There were no applications from either British or German banks.[104]

Fifty percent of Swedish bank lending was to the corporate sector.[105] The most influential of the Swedish banks was *SE Banken*, formed in 1972 in a merger headed by the powerful Wallenberg family. *SE Banken* was credited as being Sweden's first modern commercial bank, playing a vital role in Sweden's transformation from an agrarian to an industrial society. Building "spheres" from their wealth, the historical importance of the Wallenbergs can be traced back to their rescue of Ericsson and Swedish Match, and to their significant contribution to the creation of Scandinavian Airline Systems (SAS). Through key holdings held through investment companies and family trusts, the Wallenberg empire throughout the 1980s included most of the country's blue-chip companies: ASEA, Stora, Electrolux, Ericsson, Atlas Copco, Alfa Laval, Saab Scania, SKF, Esab, Incentive, and Astra.[106]

Throughout the decade the head of the Wallenberg empire, Peter, who started his career at Atlas Copco and in 1974 became Chairman of the Board, maintained his family influence through his seats on various boards, friendships with directors and executives of other Swedish companies, and through his (minority) investment influence in the Wallenberg Foundation corporate holdings. Such fund-management foundations, "allowed the old banking centre of Swedish industrial growth to be maintained...."[107] In the 1980s the Wallenberg Foundation had minority interests in the *Skandia Enskilda Bank*, the Providential Insurance, and in Investor.

Insofar as the foundation's relations with particular firms throughout the 1980s were concerned, Peter was not only the First Vice-Chairman of *SE Banken*, but also of ASEA, Electrolux, Telefon AB, Ericsson, and SKF.[108] Such ties between corporate and bank leaders in Sweden remained commonplace during the 1980s. For example, Volvo, Sweden's largest company, acquired a twenty percent stake in two of Wallenberg's holdings, Atlas Copco and Stora. The result was that Pehr Gyllenhammer, the Director of Volvo and board member of *SE Banken*,[109] was slated to take over SE Banken from the dying Marcus Wallenberg, Peter's father (the famous Raoul's cousin) and Chairman of the Bank. While Peter quickly stopped the Volvo investment in the two Wallenberg holdings by making a bargaining-chip investment of his own in Volvo that resulted in a coordinated disinvestment by both parties, neither of the two received the chairmanship. Instead, a compromise candidate Curt Olsson was selected,[110] and his ties to major Swedish industry through board memberships include: Esselte AB, the Stockholm Chamber of Commerce, Atlas Copco, and Svenska Dagbladets.[111]

The sphere structure provided Swedish industry with a dependable source of financing throughout the 1980s, since investment interests and management decisions were mixed between finance and industry. (See Figure 3.17.)

Figure 3.17
Selected Swedish Bank and Industry
Board Directorships, 1987

Board Membership	Name	Position
Banks		
SE Banken	Curt Nicolin	Chairman, Swedish Match
SE Banken	Gosta Bystedt	Dep. Chrmn., Electrolux
SE Banken	Ernst Herslow	Chairman, Euroc
SE Banken	Karl-Erik Sahlberg	Chairman, Perstorp
SE Banken	Pehr Gyllenhammer	Chairman, Volvo
Sv.Handelsbank	Sven Agrup	Chairman, Agrup
Sv.Handelsbank	Lars Hakanson	President, Skanska
Sv.Handelsbank	Tore Browoldh	Chairman, SCA Group
Industry		
Atlas Copco	Curt Olsson	Chairman, SE Banken
	Peter Wallenberg	Vice-Chmn., SE Banken
ASEA	Peter Wallenberg	Vice-Chmn., SE Banken
Nobel	Lars Thunholm	Fmr. Chmn., SE Banken
Perstorp	Alf Akerman	Fmr. CEO, SE Banken
Procordia	Bertil Danielson	President, PK Banken
SKF	Lennart Johansson	Vice-Chmn., SE Banken
	Peter Wallenberg	Vice-Chmn., SE Banken
Sv. Dagbladets	Curt Olsson	Chairman, SE Banken

Source: Annual reports (1987) from the following corporations: AGA, Atlas Copco, Electrolux, Euroc, Nobel Industries, Perstorp, Procordia, SCA, Skanska, SKF, Swedish Match, Volvo. Also, *International Who's Who* (1988): 1133, 1578.

With Swedish companies becoming increasingly large, the sphere structure was in danger as a result of Swedish investors like Peter Wallenberg being unable to maintain an equity linking. Nevertheless, throughout the 1980s Swedish banks continued to maintain much of the responsibility for corporate debt and were "able to call many of the shots"[112] in terms of management decisions because of relatively high debt-equity ratios.[113] As Pontusson explains,

> The big private banks have continued to exercise considerable leverage through the ownership of equity capital by their board members and retirement funds, and by investment companies closely linked to the banks. The supply of long-term credit has also remained an important source of influence. Though formally of limited duration, much of the business lending has been of a *de facto* long-term character. Furthermore, the commercial banks have come to mediate corporate access to other forms of long-term credit. Most notably, private corporations can only issue bonds through a bank.[114]

As illustrated below, debt-equity ratios of major Swedish industrial remained even higher than Swiss enterprises.[115] (See Figure 3.18.)

Figure 3.18
Debt-Equity Ratios: A Sampling of Swedish Enterprises
(Non-financial enterprises)

Sample size (total number of companies)	:	62
Average (mean) debt-equity ratio	:	2.25
Average (median) debt-equity ratio	:	1.77
Highest debt-equity ratio	:	6.54
Lowest debt-equity ratio	:	0.41

Debt-equity ratios of notable companies

Asea (Brown Boveri)	:	5.67
Electrolux	:	2.99
Ericsson	:	1.68
Saab-Scania	:	1.53
Volvo	:	1.61

Source: Morgan Stanley (1989) *Capital International Perspective*. (October).

Labour has played an important role in Swedish enterprises' collective capital formation. With a cradle-to-grave attitude among Swedes, Sweden's giant "supplementary-pension" (ATP) funds provided significant investment in Sweden's largest companies, providing between twelve and fifteen percent of the entire credit market in Sweden. Around twenty-five percent of net lending by the ATP funds was directed to the corporate sector between 1978-1983.[116] By the end of the bourgeois interregnum in 1982, the fourth ATP fund, which allowed for limited equity ownership, was the fourth largest single owner of shares listed on the Stockholm exchange, though it accounted for less than one percent of the total assets of the ATP funds.[117] Nonetheless, the influence was such that nearly ten percent of Volvo's assets were held by the pension funds throughout the 1980s.[118]

Moreover, in the 1980s the private financial sector in Sweden employed factoring as a vital means of financing, notably in the export area. Factoring was an important financial mechanism designed to eliminate payments risk in overseas sales (and to ensure that the seller received prompt settlement) as well as a system applied to the purchasing of invoices from businesses at a percentage discount. Factoring agreements improved the cash flow of the businesses concerned by enjoying a prompt release of cash, while the factor for a prescribed percentage charge took on, in effect, the function of collecting receivables. Hence, in Sweden with exports accounting for over thirty-five percent of GDP, international factoring remained a vital means to foster capital availability in Sweden's export sector and to stimulate its significant export orientation.[119]

Since the Swedish government in 1985 changed regulations and allowed foreign banks to establish operations in Sweden, the competitive environment for Swedish banks changed.[120] "In the 1970s all companies in the Wallenberg group only banked with *SE Banken* - period. Today it is completely different."[121] As one executive from competing *Svenska Handelsbank* stated, "There is a sphere relationship, particularly on the board level. The thing that changed between banks and industry is that of packaging of financing. Those who are the most helpful win. [In addition] relationship banking is becoming less and less of a phenomenon. Our [Sweden's] largest companies are becoming financial institutions in and of themselves."[122]

By the latter part of the 1980s, while relationship banking continued to be important in terms of new stock issues, takeovers, and corporate finance,[123] foreign banks were able to penetrate into the Swedish market through measures of financial liberalisation and deregulation,[124] though with much difficulty and with little success. Stated one official of a foreign bank entering the Swedish market, "'It is a difficult market and the picture is not that rosy, but we have good reasons to stay.'"[125] At the same time, with impressive levels of profitability, minimal Third World exposure, and a Moody's Investor Service top Rating of Aaa, Sweden's largest banks attempted in the latter part of the 1980s to attract foreign investors to acquire up to twenty percent of their stock and ten percent of their notes.[126] Sweden's largest bank *SE Banken* also teamed up with some of the other larger Scandinavian banks, such as *Privatbanken* of Denmark, to form Scandinavian Banking Partners (SBP), and thereby to creat a more visible presence in the international corporate finance arena.

In summary, evidence from *The World Competitiveness Report* corroborates some of the primary evidence furnished in this section on Sweden concerning the relationship between financial institutions and the banks. For example, in a survey sent to twelve thousand executives from thirty-two countries asking whether the banking sector gives "positive help to business enterprises," Sweden ranked first among twenty-two OECD countries.[127] Sweden also ranked second (behind Switzerland) in the "private sector borrowing category" in terms of "the extent to which the private sector is at an advantage vis-a-vis the public sector in tapping capital markets."[128] Finally, Sweden ranked second only behind the U.S. in terms of the availability of risk capital.[129]

C. Denmark

Perhaps the greatest impediment to finance-industry relations in Denmark during the 1980s was the domestic economic and monetary atmosphere in which they worked. Public debt remained high, GDP growth was sluggish, unemployment approached ten percent, the current account balance continued from past decades, and the savings rate to provide liquid funds to the financial institutions was among the worst in the industrialised world.[130] As a result of this situation, external investment in the Danish economy was slow, and Danish financial intermediaries were less able to provide capital investment to Danish industry and to remain competitive in the international services sector.

Similar to many other small European states during the 1980s, Danish financial institutions and enterprises were linked through share ownership. While banks were not allowed to own businesses, they were allowed to hold minor shares totalling twenty to twenty-five percent of equity and were not allowed to give industrial credits exceeding one-third of their own capital.[131] As a result, in *The World Competitiveness Report* Denmark ranked below the average ranking of a survey of twenty-two OECD countries in terms of the banking sector "providing positive help to business enterprise" and banks as a source of private credit.[132]

However, ties between financial institutions and industry did exist during the decade. For example, in 1987 Poul J. Svenholm was both chairman of *Den Danske Bank*, one of Denmark's three large banks (along with *Kobenhavens Handelsbank* and *Privatbanken*), and President of Carlsberg A/S, one of Denmark's ten largest industrials. Similarly, Fleming Count of Rosenborg, Chairman of the Danish industrial Calkas A/S, was Deputy Chairman of *Den Danske Bank*. Also in 1987, Hugo Schroeder was both chairman of *Privatbanken* and managing director of Skandinavisk Holding A/S, one of Denmark's twenty largest industrials.[133]

Moreover, throughout the decade particular banks continued to act as primary financial sourcing agents, sometimes to the extent of almost nominal *hausbanken*. Two of Denmark's more renowned industrials, Novo and FL Smith banked primarily with *Kobenhavens Handelsbank* and United Breweries banked primarily with *Den Danske Bank*. As Steen Parsholt, the director for Copenhagen's Citibank office explained,

> There is a very tight *hausbank*, principal bank, structure here. We [Citibank] will never fully succeed here because an atmosphere of hostility against foreign competition has been pervasive. While *hausbank* ownership relations are legally prohibited, the feeling is extremely strong and determined by groupings.[134]

Foreign banks entered the market in the 1970s, and by 1980 most were involved in such activities as providing letters of credit and short-term credit facilities. However, most of these banks not only avoided traditional banking, they also ran into credit problems because of strict capital adequacy ratios that propelled a feeling among foreign banks that the "lending control system discriminate[d] against banks without a retail deposit base .... [Moreover,] "corporate customers [were] fighting shy of foreign banks because of the tough line they ... [took] in bad debt negotiations."[135] In addition, new entrants to the Danish financial markets faced very high expatriate taxation that limited their staffing opportunities.[136] As a result of all of these factors, foreign financial institutions were relatively small players in the Danish financial markets, managing to garner less than five percent of the Danish market during the decade.

While throughout the 1980s Denmark maintained relatively strong working relations between Danish financial institutions and industry, the Swedish tradition of financial institution sphere ownership existed to a lesser extent in Denmark notably because Danish industry was significantly smaller than that in Sweden. As a result of Denmark's industrial structure, in which only twelve percent of the labour pool was used for industrial production in 1987 and the majority worked in the public sector,[137] financing through equity instruments was "not all that important"[138] and less significant than in other small European states. (See Figure 3.19)

Figure 3.19
Market Value of Equity Shares of Domestic Companies, December 1988

Exchange	Market Value US$ Millions
Amsterdam	103,643.9
Brussels	58,788.0
Copenhagen	26,878.1
Helsinki	30,549.2
Luxembourg	46,146.3
Stockholm	99,723.9
Zurich	140,359.0

Source: Shearson Lehman Hutton Public Finance (1989)

Instead of public equity securitisation being meaningful for Denmark's larger firms, Danish industrials preferred debt over equity instruments (and also because "the Dane is just not a natural private investor for the simple reason that he hardly saves.")[139] Ninety percent of *Den Danske Bank*'s and *Privatbanken*'s securities portfolios were composed of bonds, mostly the highly liquid and high yielding mortgage and government bonds,[140] while shares accounted for less than ten percent.[141] Under such conditions, debt-equity ratios in Denmark remained high.[142]

(See Figure 3.20.)

Figure 3.20
Debt-Equity Ratios: A Sampling of Danish Enterprises
(Non-financial enterprises)

Sample size (total number of companies)	:	19
Average (mean) debt-equity ratio	:	1.93
Average (median) debt-equity ratio	:	1.75
Extreme low	:	0.13
Extreme high	:	5.24

Debt-equity ratios of notable companies

Carlsberg	:	1.20
Novo	:	0.65
Royal Copenhagen	:	1.75

Source: Morgan Stanley (1989) *Capital International Perspective*. (October).

Denmark differed from Sweden and Switzerland not only in the scale of financial institutions but also in the nature of ownership in industry. In 1986, financial services in Denmark accounted for only four percent of GDP; the Danish financial services sector was, relatively, ten times smaller than that of the British sector.[143] While financial institutions had some ownership rights towards industry, industry remained relatively small with only ten to fifteen large industrials (with only three companies listed on the London Stock Exchange) and often cooperatively or family-owned.[144] For example, the electricity, food, and dairy industries were cooperatively owned. Well-known Danish industrials such as Carlsberg A/S was majority owned by a foundation, and AP Moller remained family-owned with a share structure designed to reduce the taxation burden yet maintain control through the family.[145] Despite the objections from family firms, the pension funds grew in importance in terms of industrial investment by providing by the latter part of the decade twenty-five percent ownership of many enterprises.[146] The pension funds also had equity investment in public financial institutions.[147]

Realising the necessity for Danish financial institutions to become larger to compete in the world markets, and realising that many previous corporate customers of Denmark's largest banks were turning to other avenues of financing (such as the Eurobond markets and domestic financial institutions such as the assurance companies) the majority of the Danish banks merged and attempted to spread across Europe. Most of the banks' international strategies rested on their activities in Luxembourg, though banks such as *Den Danske Bank* entered the West German market in order to gain a foothold in Europe in preparation for the (more) unified European market projected for 1992.[148] Towards the end of the decade Danish banks attempted to highlight their ability to be the Scandinavian outpost to the EC.

In addition, the Ministry of Industry maintained ties with financial institutions by appointing a representative to the boards of the country's largest banks.[149] This involvement was expanded in the latter part of the decade through a major conference between the State and the large banks to discuss improvements in the Danish economy, most importantly by expanding its relatively small industrial structure. As a consequence of its small size and limited number of large financial institutions, the State worked closely with the three major banks to form a financial institution consortium designed to provide venture capital to promote industry. As Jesper Kongstad of the Ministry of Industry explained,

> "This was not a traditional policy. It was done purely through consultations between the government, the Ministry of Industry, and three largest banks. It forced the three to work together ... and for our part, we said 'do this or we'll examine taxation issues with interest rate differentials.'"[150]

Throughout the latter part of the 1980s the consortium continued to advise the government on debt policy and, more generally, on the entire economy of Denmark.[151] Indeed, this cooperation remained a necessity in order to revamp an economic and monetary environment that was stinting industrial growth and thwarting the ability of domestic financial institutions to be, not only competitive themselves in the international services market, but also a help Danish industries secure important investment capital.

D. Ireland

In contrast to Switzerland and Sweden, and to a lesser extent Denmark, relations between financial institutions and industry were relatively deficient throughout the decade, much as a result of Ireland's weak industrial and financial structures. While throughout much of the 1980s Ireland experienced significant industrial growth that positively affected its export position, its service sector remained extremely small. It ranked last out of twenty-two OECD countries in terms of the value added in services as a percentage of GDP in 1986 and twentieth in terms of the number of banks among the world's top five-hundred; only two, the Bank of Ireland (BOI) and Allied Irish Banks (AIB), were included on the list.[152] (See Figure 3.21.) A further example of Ireland's small financial services sector is the fact that Britain's largest Building Society, Halifax Building Society, maintained an asset base fifty percent larger than the assets of Ireland's two largest banks and all the Irish building societies combined.[153]

Figure 3.21
Banks Doing Business in Ireland, 1987 (By Total Assets)

Rank	Financial Institution	Total Assets Irish Pounds
1	Allied Irish Banks	9,606.00
2	Bank of Ireland	8,838.00
3	Ulster bank	3,100.37
4	National Irish Bank	553.00
5	Industrial Credit Corpo.	543.62
6	Banque Nationale de Paris	511.18
7	Irish Intercontinental	446.00
8	Algemene Bank Nederland	445.11
9	Citibank	344.26
10	Bank of Nova Scotia	327.00
11	Hill Samuel Co.	232.21
12	Anglo Irish Bankcorp	215.08
13	Barclays Bank	211.00
14	Bank of America	142.37

Source: *Business and Finance, Ireland* (1989) January 26: 74-75.

Traditionally the Irish financial services sector was based on loyalty to the larger industrials through "key bankers,"[154] and as the above figure indicates the two largest banks in Ireland accounted for most of the large enterprise business. Much as a result of the influx of foreign multinationals, from 1980 onwards large bank-industry relationships weakened as new foreign banks accompanied this FDI into the Irish marketplace, "educating the old Irish establishment."[155] By 1987, thirteen foreign banks had a presence in the country in which banking relationships based from the home country were transferred to the host country (Ireland) mainly because of the tax advantages afforded to foreign industrial and financial enterprises. As a result, much of the relationship banking that did exist prior to the major influx of foreign multinationals became diluted through transactional banking typically involving the use of syndicates of domestic and foreign financial intermediaries.[156]

The Central Bank of Ireland maintained a relatively strong hold over financial institutions through an interest rate grid system that tightly regulated the ability of financial intermediaries to raise the prices of their products; the system also regulated liquidity through strict ratios.[157] However, certain advantages were afforded to Irish banks, such as their knowledge of the domestic market and their ability to lend in the local currency at cheaper rates than their foreign competitors could through Section 84 financing.[158] Through this tax-based lending system, interest paid on loans by Irish resident companies was treated as dividends and was therefore not taxed. This benefit to the lender was passed to the borrower, and only

Irish financial institutions were given the opportunity to provide Section 84 financing.[159] However, foreign financial intermediaries often provided these credit opportunities by working with an Irish bank.[160]

Unlike the other three financial systems examined in the thesis, Irish laws remained extremely prohibitive in terms of board directorship relations between financial institutions and industry, mainly because of "disclosure problems."[161] Indeed, with only one or two notable exceptions,[162] directorships in industry were held by other industrialists, while directorships in financial institutions were held by managers within the banks themselves and a small handful of industrialists. While AIB and BOI both maintained corporate relationships, the limitation by the Irish State to bank ownership of around five percent caused finance-industry links less extensive than those that existed during the 1980s in the other case countries and many other small European states.

(See Figure 3.22.)

Figure 3.22
Board of Directors Membership, 1987
Allied Irish Bank, Bank of Ireland
(Listed for those with Industrial Affiliation Only)

Bank	Director Name	Affiliation*	Company Ranking**
AIB	T. Cavanagh	Cavanaghs Fermoy	Not among top 1000
AIB	J. Culliton	Unidare	127
		Radio Telefis Eire	74
AIB	P. Fallon	Euromoney Public's	Not among top 1000
AIB	J. McGuckian	McGuckian Livestock	Not among top 1000
		Ulster Television	260
AIB	D. Murphy	St. Patrick Woollen	Not among top 1000
		Swansea Cork Ferries	Not among top 1000
		Securicor	418
BOI	J. Callaghan	Stokes, Kennedy	334
BOI	D. Carroll	Carroll Industries	30
BOI	D. Kennedy	Aer Lingus	10
BOI	T. Toner	Arnott Foods	147
		BWG Foods	86
		Irish Continental	220

*Either Chairman or CEO of company as denoted by either "Aspect" or by bank annual report.

**As ranked by Aspect.

Source: Aspect: The Investor's Business Journal (1989) *The Top 1,000 companies and Who's Who in Irish Industry 1989*; Bank of Ireland (1989) *Report and Accounts for the Year*: 21; Allied Irish Banks (1989) *Report and Accounts for the Year*: 24-25.

Indeed, the Irish financial system followed the British example, with detached finance-industry relations evidenced by the lack of cooperative board relationships between financial institutions and enterprises as well as inconsequential bank ownership of industry. While following the British decision to maintain a "separatist" system,[163] Irish industry did not require the financing through the capital markets necessary for giant American and British enterprises in the 1980s under similar financing relationships. As a result, the Irish financial system, different than the continental Europe example of intimate finance-industry relations based on lending and high debt-equity ratios, remained a major competitive disadvantage for Ireland. Indeed, during the 1980s, debt-equity ratios of Irish enterprises remained around .75 (.75 : 1.0).[164]

By using its key resources such as its educated public, its ties with UK, membership in the EC, and proximity to the rest of the world, and by providing various incentives to entice foreign financial institutions into the Irish market, the Irish State put significant hopes on invigorating its relatively weak and ineffective financial structure.[165] By the 1980s the Industrial Development Authority (IDA), whose relations with the banks remained relatively intimate throughout the decade in arranging financing for projects administered by the Agency, was provided an innovative mechanism to bolster Ireland's financial services position in the global market. A plan for an International Financial Services Centre (IFSC) located at the docks in Dublin was devised primarily by the IDA to house financial institutions to deal with various financing operations, including dealing and brokerage operations, insurance, and fund management.

Even with such attempts for the future, the Irish case of the 1980s provides a vivid example of a small European state unable to take advantage of proximate finance-industry relations to propel investment and financing for projects. Most importantly, the Irish economy was faced with a number of problems that detracted from monetary stability: a major debt problem that sapped the country's credit rating; low levels of savings and reserves that thwarted the necessary liquidity to provide loans; and inflation that discouraged investment because of the high levels of real interest rates. Financial institutions remained technologically deficient in comparison to their West European counterparts and domestic financial institutions maintained a traditional attitude that resulted in their declining competitiveness in the open Irish financial markets against foreign financial institutions.

While the international monetary system shifted during the decade to the use of securitisation through the capital markets, Irish industry was so small that there was little need for it. As a consequence, Irish financial institutions became less sophisticated in their methods of financing for Irish domestic industry and less competitive, remaining relatively insignificant global financial players.

3.6 The Monetary Environment and Finance-industry Relations in the Small European State in the 1980s: Lessons from the Case Countries

During the 1980s small European state monetary policies and financial practices varied in how they facilitated industrial financing. By 1980 all small European states were experiencing low growth and inflation as a result of the international recession spurred by the oil shocks of the 1970s. Some small European states such as Switzerland and Sweden were better able to adapt to these adverse conditions, flexibly responding through monetary policies that curtailed inflation and promoted growth. It was under these monetary conditions that strong finance-industry relations propelled industrial investment, economic growth, and international competitiveness. In Denmark and Ireland, relatively poor domestic economic and monetary conditions inhibited finance-industry relations.

In Switzerland, the monetary policy was based on four principles: 1) monetary aggregates that realised their targets and kept inflation under control; 2) a high savings rate that kept the necessary liquidity for financial institutions to maintain vital reserves; 3) external stability through a strong, steady Swiss Franc; and 4) relatively low real interest rates. These factors, coupled with socio-political stability and a deregulated, universal banking system, provided the necessary environment for Switzerland to maintain its strategy of being an international financial centre and to reinforce strong finance-industry relations. Higly cooperative bilateral Principal bank relations supported industrial financing arrangements both through bank ownership of industry and directorships that mixed board memberships between financial institutions and industries.

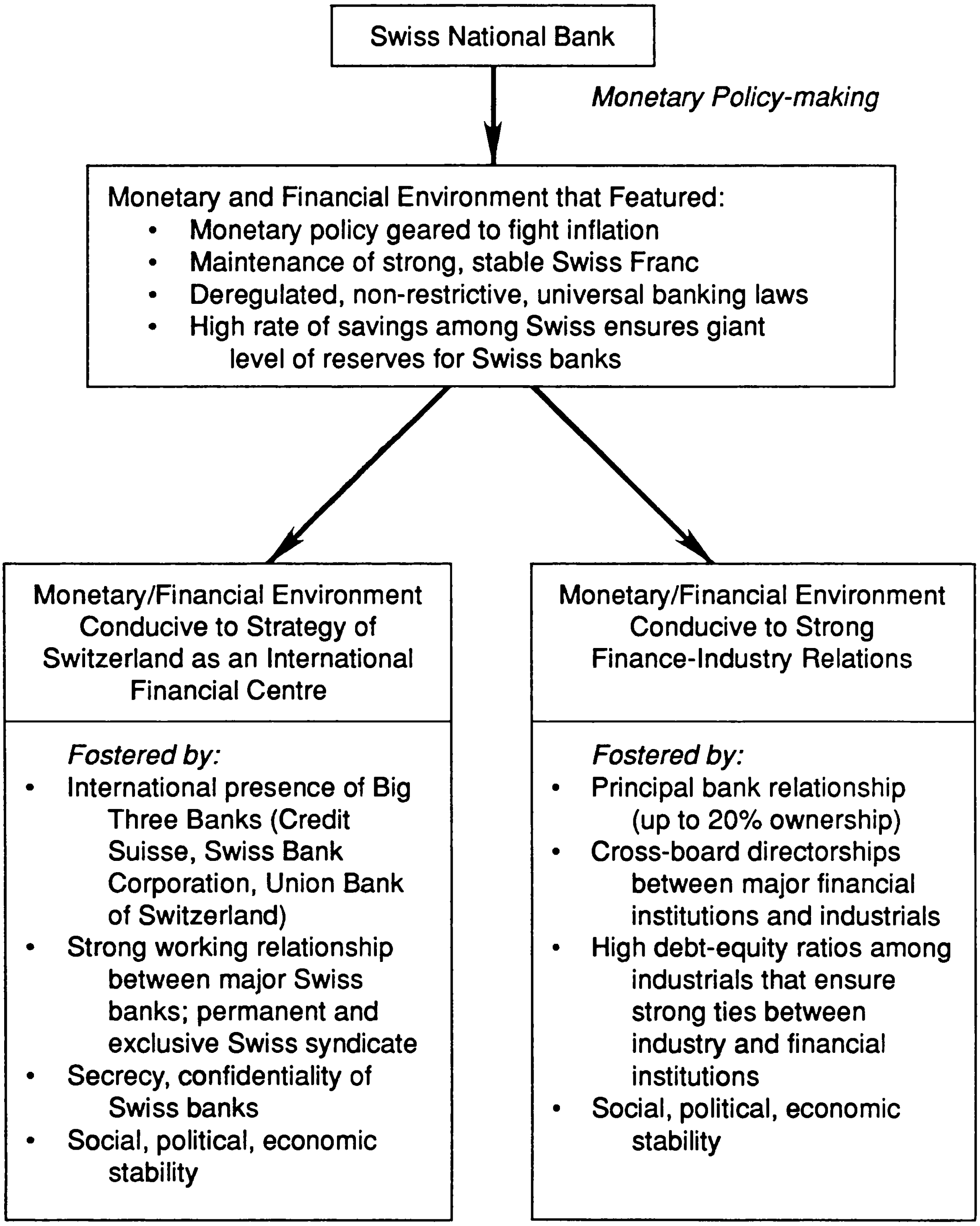
Within Switzerland, the Big Three banks possessed a significant amount of authority because of Swiss industries' preference for high debt-equity ratios. As a result of industries' highly leveraged positions, the Swiss big banks maintained significant control of Switzerland's industry. With the real cost of funds being cheaper for Swiss firms, they could act more aggressively in the international marketplace against foreign competitors who were required to pay more for long-term development and growth. Moreover, externally the Big Three banks of Switzerland remained internationally powerful, often participating in transnational financing syndicates, particularly in North America.

Consequently, throughout the 1980s effective monetary policy-making by the SNB effectuated an environment that both remained conducive to strong finance-industry relations and helped to foster Switzerland's important financial sector. While the SNB guided the Swiss economy by maintaining monetary stability, private financial institutions worked alongside industry as both capital and management sources. It is for these reasons that financial institutions were the principal actor in maintaining Switzerland's high level of international competitiveness during the 1980s. (See Figure 3.23.)

With the international recession severely affecting the Swedish economy at the beginning of the 1980s, Swedish policy-makers actively pursued a monetary policy intended to spur growth. As a result of the devaluations of 1981 and 1982, Sweden experienced significant economic and industrial growth throughout most of the 1980s. Under monetary circumstances conditioned for growth, finance-industry interaction could be characterised as cooperative bilateral, where familiar relations existed between Sweden's largest banks and industrials primarily through financial spheres.

Figure 3.23

MONETARY POLICY-MAKING AND FINANCE-INDUSTRY RELATIONS IN SWITZERLAND, 1980-1987: THE PRINCIPAL ROLE OF FINANCIAL INSTITUTIONS



Similar to Switzerland, the powerful Swedish industrial structure remained highly leveraged because overall business factors were favourable; such leverage reduced cost of capital, increased return to equity, induced equity investments in the firm, and allowed Sweden to act more aggressively in the international marketplace.

However, both Denmark and Ireland were faced with wage drift, foreign debt, and current account deficits that adversely affected their domestic monetary environments. While Denmark actively pursued a policy of austerity, Ireland maintained a relatively passive monetary policy in which its primary goal was to maintain reserves adequacy and protect the exchange rate. By doing so, it pursued a passive interest-rate policy that mirrored the level of external rates. As explained earlier, by Irish policy-makers refusing to devalue at the beginning of the decade, both vital agricultural output and incomes significantly diminished.

Given these poor monetary and economic conditions, neither Denmark nor Ireland could fully achieve intimate finance-industry relations. While Denmark maintained relatively cooperative bilateral relations between the two as a result of bank ownership of industry and mixed board directorships, austerity measures to halt inflation and reduce its current account deficit alienated these relations and caused domestic financial institutions to be unable to offer significant investment capital. In Ireland, poor economic and monetary conditions certainly did not contribute to stronger working relations between financial institutions and industry; only by 1987 under the *Programme for National Recovery* did Ireland attempt to spur growth by controlling wage-inspired inflation while at the same time reducing real interest rates. Nonetheless, Ireland's financial practices throughout the decade did not help the situation either. Following the Anglo tradition of separatist systems, Irish banks and industry tended to work less intimately than their continental neighbours; as a result, this detached bilateral relationship did not benefit from the state's monocephalic, proximity communication advantage.

In sum, small European state monetary interventionism was nationally specific. In each of the four cases, though external stability was couched through monetary pegging arrangements, different strategies were followed. In Switzerland, monetary stability, even at the price of high growth, was an economic necessity. In Sweden, growth through devaluation, even at the price of inflation, was stressed in order to stimulate industrial productivity. In Denmark, austerity characterised monetary policy-making, which resulted in inflation and economic stagnation. In Ireland, policy-makers maintained a relatively passive monetary policy, following world fluctuations in interest rates and consequent exchange rates. Therefore, during the 1980s monetary interventionism in Switzerland and Sweden - a necessity to respond flexibly to international monetary pressures - fostered favourable domestic monetary conditions for economic growth and high levels of international competitiveness, but in Denmark and Ireland ineffective or delayed interventionism frustrated finance-industry relations.

Notes for Chapter Three

1.Notable exceptions to the rule include a number of works on Japan and West Germany by Katzenstein, Samuels and Zysman. One of the reasons for the scarcity of works is explained by Michael Moran, who attributes "the politics of money and banking" as being "a politics of complexity.... (i.e., "making sense of slippery financial statistics ... [and] even more slippery financial institutions...." See Michael Moran (1984) *The Politics of Banking: The Strange Case of Competition and Credit Control*: 5-8, 75.

2.See Charles E. Lindblom (1977) *Politics and Markets: The World's Political-Economic Systems*: 170-188.

3.For example, see Charles Maier (1984) "Preconditions for Corporatism" in John Goldthorpe, ed. *Order and Conflict in Contemporary Capitalism: Studies in the Political Economy of West European Nations*: 39-59; Philippe C. Schmitter (1981) "Interest Intermediation and Regime Governability in Contemporary Western Europe and North America" in Suzanne Berger, ed. *Organizing Interests in Western Europe: Pluralism, Corporatism, and the Transformation of Politics*: 285-327.

4.See Pieter Korteweg (1982) "Exchange Rate and Monetary Policy in A World of Real Exchange Rate Variability" in Roy A. Batchelor and Geoffrey E. Wood, eds. *Exchange Rate Policy*: 135-160.

5.Yao-Su Hu (1984) *Industrial Banking and Special Credit Institutions*: 1.

6.See Robert Gilpin (1987) *The Political Economy of International Relations*: 142-151.

7.See Stephen George (1985) *Politics and Policy in the European Community*: 136-141.

8.See Susan Strange (1988) *States and Markets*: 104.

9.This extended to as far back as 1969 with the inception of the economic and monetary union (EMU). See Loukas Tsoukalis (1978) *The Politics and Economics of European Monetary Integration*.

10.David Calleo (1987) *Beyond American Hegemony: The Future of the Western Alliance*: 101.

11.See Robert O. Keohane (1984) "The World Political Economy and the Crisis of Embedded Liberalism" in Goldthorpe, ed. *op.cit.*: 30.

12.International Monetary Fund (1988) *International Financial Statistics*: 110-111. Also, see Figure 3.5.

13.See Susan Strange (1986) *Casino Capitalism.*

14.See OECD (1987) *Economic Surveys: Switzerland*: 32.

15.See Pierre Languetin (1987) "The Role of the Swiss National Bank" in Swiss Bankers' Association. *International Financial Centres*: 81.

16.See Georg Rich (1985) "Monetary Control: The Swiss Experience." Paper presented at CATO Institute Policy Conference. Also, see Banque Nationale Suisse (1987) *79er Rapport de Gestion*: 7; Banque Nationale Suisse (1986) *Functions, Instruments, Organisation*: 5.

17.Interview with Dr. Hilde Phan-Huy, Vice-President, Economics Division, *Credit Suisse*, Zurich, 17 November 1987.

18.Georg Rich (1987) "Swiss and United States Monetary Policy: Has Monetarism Failed?" Paper presented at Swiss Friends of U.S. (March 5).

19.See Ulrich Kohli (1985) "La Demande de Monnaie en Suisse: Aspects Divers" in Banque Nationale Suisse (1985) *Monnaie et Conjonctore* (Bulletin Trimestriel): 150-164.

20.For example, in 1984 Switzerland's real lending rates, calculated by subtracting its nominal lending rate by inflation, was 1.09%. In 1985 it was 2.33%. See IMF (1988) *International Financial Statistics*: 671; OECD (1987, 1988) *Etudes Economiques: Suisse*: Statistiques comparisons internationales.

21.Georg Rich (1984) "Is Swiss Monetary Policy Really Monetarist?" Paper presented at Lugano Monetary Conference.

22.Lombard Odier & Cie (1988) *The Swiss Paradox*: A13.

23.See Peter J. Katzenstein (1980) "Capitalism in One Country: Switzerland in the International Economy." *International Organization*: 522.

24.Continual reference is made in the book by Carrington and Edwards on the effect of savings and investment positions of households, industry and government on economic prosperity in the industrialised world. See John C. Carrington and George T. Edwards (1981) *Reversing Economic Decline: Government, Social and Economic Choices in the Use of Saving.*

25.International Monetary Fund (1988) *Exchange Agreements and Exchange Restrictions*: 461-462.

26.See Benedicte Vibe Christensen (1986) *Switzerland's Role As an International Financial Center*: 8-11.

27.However, the growth rate is somewhat misleading since throughout the 1980s Swiss industry pursued a strategy of manufacturing from abroad as opposed to exporting directly from Switzerland.

28.Anders Vredin (1986) *Capital Flows and Monetary Policy in Sweden*: 5.

29.Lars Horngren and Anders Vredin (1986) *The Foreign Exchange Risk Premium: A Review and Some Evidence From A Currency Basket System*: 38.

30.This was the so-called EFO Model, which is discussed in detail in the following chapter.

31.IMEDE and World Economic Forum (1989) *The World Competitiveness Report*: 101. (Table 4.07)

32.See Olle Lindgren (1988) "Stockholm Scraps Its Arsenal." Bayerische Landesbank. *Global Investment Management*: 91-94.

33.Interview with Nils Bjartun, Exchange Control Office, Riksbank, Stockholm, 3 September 1987.

34.Barry P. Bosworth and Robert Z. Lawrence (1987) "Economic Goals and the Policy Mix." *The Swedish Economy*: 105-107.

35.Out of twenty-two countries, Denmark ranked sixteenth in terms of central government foreign debt in 1987. It also ranked sixteenth in terms of country credit rating in 1987 assessed by *Institutional Investor* magazine. See IMEDE and World Economic Forum (1989) *op.cit.*: 99, 101. (Tables 4.02, 4.06)

36.See Dan Knudsen (1988) "Causes and Effects of Development in Money Supply." *Danmarks Nationalbank, Monetary Review.* (February): 8-11.

37.Interview with Henrik Fugmann, Head of Section, Ministry of Economy (Denmark), Copenhagen, 9 September 1988.

38.Interview with Anders Moller Christensen, Head of Research Unit, *Danmarks Nationalbank*, Copenhagen, 6 September 1988.

39.In 1986 the Danish real lending rate was 8.30%. Calculated from IMF (1988) *op.cit.*: 321; OECD (1988) *Economic Surveys: Denmark*: International Statistical Comparisons.

40.See Ministry of Finance, Department of Budget (1987) *Economic Prospects and Policies in Denmark, 1988-1992.* (December).

41.Denmark's personal income tax as a percentage of GDP on profits, income, and capital gains totalled 28.41% in 1986. In contrast, in Switzerland it was 13.38%, Ireland 14.30%, and

Sweden 22.90%. See IMEDE and World Economic Forum (1989) *op.cit.*: 127. (Table 6.12)

42.Ibid.: 101. (Table 4.07)

43.Ibid.

44.Palle Simonsen (1988) "The Dane Purse." *Bayerische Landesbank, op.cit.*: 73-78.

45.See Niels Thygesen (1985) "The Phasing Out of Exchange Controls." *Skandinaviska Enskilda Banken Quarterly Review.* Number 3: 59-65.

46.See Brian V. Mullaney (1988) "Denmark: Turning the Corner, But Austerity Continues." *Morgan Stanley Investment Perspectives - U.K. and Europe.* (August 30).

47.Jesper Jespersen (1988) "Monetary Policy in 1987." *Danmarks Nationalbank, Monthly Review 1987.* (May): 6-9.

48.Erik Hoffmeyer (1988) "Extract from a Speech at the Annual Meeting of the Danish Bankers Association." *Danmarks Nationalbank Monetary Review* (February): 14. In an interview, Christensen commented that "Most Danes consider him [Hoffmeyer] a pragmatist - he has received a reputation as being for austerity ... a tighter policy compared to most central banks..." See Interview with Christensen, 6 September 1988.

49.Ireland ranked last in terms of central government foreign debt in 1987 among twenty-two OECD countries, and nineteenth in terms of central government total debt in 1987. It also ranked nineteenth in its country credit rating. See IMEDE and World Economic Forum (1989) *op.cit.*: 99, 101. (Tables 4.02, 4.03, 4.06)

50.Ireland ranked last in terms of employment growth between 1980-1986 and second to last among twenty-two OECD countries in terms of overall unemployment in 1988, and sixteenth in terms of change in inflation from 1981-1987. Ibid: 100, 113, 114. (Tables 5.12, 5.14, 4.05).

51.See Padraic O'Connor (1987) "Exchange Rate Volatility and Consequences for Irish Interest Rates." *The Irish Banking Review.* (Spring): 3-13.

52.Tomas F. O'Cofaigh (1985) "Implementing Monetary Policy." *Central Bank of Ireland, Quarterly Bulletin.* (2): 61.

53.S.J. Sheehy (1988) "Irish Agriculture Into the Nineties." *The Irish Banking Review.* (Autumn): 23.

54.Ibid.

55.See Kevin Barry (1984) "The Central Bank's Management of the Aggregate Liquidity of Licensed Banks" in Bank of Ireland, *Annual Report 1983*: 104-116.

56.See Thomas O'Connell (1988) "The Central Bank: Monetary Policy and Financial Regulation." *Central Bank of Ireland, Quarterly Bulletin* (Summer): 72-86.

57.Government of Ireland (1987) *Programme for National Recovery*: 9.

58.See Scott Lash and John Urry (1987) *The End of Organized Capitalism*: 207.

59.Hu (1984) *op.cit.*: 17-18.

60.See Zysman (1983) *op.cit.*

61.Hu (1984) *op.cit.*: 2.

62.Thomas A. Pugel (1984) "Japan's Industrial Policy: Instruments, Trends, and Effects." *Journal of Comparative Economics*. Volume 8: 424.

63.Chalmers Johnson (1982) *MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925-1975*: 203.

64.Hu (1984) *op.cit.*: 2.

65.As coined by Shonfield. See Andrew Shonfield (1980) *Modern Capitalism: The Changing Balance of Public and Private Power*: 246-264.

66.See Terence Roth (1987) "Money Power: Critics Attack Role of W.German Banks in Politics, Industry - 'A Kind of Fourth Estate'." *The Wall Street Journal - Europe*. (September 28): 1.

67.Pierre Grou (1985) *The Financial Structure of Multinational Capitalism*: 150.

68.See Charles R. Geisst (1982) *A Guide to the Financial Markets*: 11.

69.As one OECD report contends, "...indications exist that business investment is more responsive to the level of current profits when debt-equity ratios are high ...." See OECD (1987): 59.

70.Zysman (1983) *op.cit.*: 261.

71.A good example is *Societe Generale de Belgique*. It has accounted for approximately one-third of all Belgian business and is ten percent owned by the nation's largest bank, *Generale de Banque*.

72.OECD (1987) *op.cit.*: 46.

73.Nicholas Faith (1982) *Safety in Numbers: The Mysterious World of Swiss Banking*: 22-23.

74.For a complete description of the Swiss banking structure, see Hans J. Bar (1975) *The Banking System of Switzerland*: 10-36.

75.Throughout most of the 1980s, the big three banks posted similar changes in their profits and dividends. These figures under-represent actual figures because of hidden reserves that reduced reported profits.

76.In the Swiss banking law of 1934, the government set the principle of "universality." At the same time, the U.S. imposed a restrictive banking act. See Christensen (1986) *op.cit.*: 10.

77.See Bar (1975) *op.cit.*: 56-60. The Swiss Banking Commission, which is independent of the government, supposedly supervises the Swiss banks, particularly in matters regarding secrecy. Nonetheless, it has been known as "ineffective" in supervising Switzerland's six-hundred banks. Much of this is due to a scandal in 1977 involving *Credit Suisse* and the closing of *Banque Leclerc*.

78.See Swiss National Bank (1986) "Functions, Instruments, and Organisation:" Part V.

79.Since 1977 there was a Due Diligence Convention between the Central Bank and the Swiss Bankers' Association concerning the rules of conduct for banks regarding (principally) the control of identity of their clients. See Francis Pahud (1987) "The Structure of the Swiss Banking System." Swiss Bankers' Association, *op.cit.*: 59.

80.See Katzenstein (1980) *op.cit.*: 521.

81.Interview with Martin Witschi, Director, *Credit-Suisse-*Berne, Berne, 13 November 1987.

82.Percentages particularly in the U.S. and the France were higher, while relatively the same in Germany and Japan. See OECD (1987) *op.cit.*: 59.

83.Interview with Hans J. Halbheer, Senior Vice-President, Public Affairs, *Credit Suisse*, Zurich, 12 November 1987.

84.Grou (1985) *op.cit.*: 167.

85.Interview with Daniel Witschi, Economics Division, Swiss Bank Corporation, Basel, 11 November 1987.

86.See Peter J. Katzenstein (1982) *Corporatism and Change*: 230.

87.Ibid: 230-232.

88.Interview with Phan-Huy, 9 November 1987.

89.Katzenstein (1982) *op.cit.*: 232.

90.Interview with Christoph Winzeler, Legal Department, Swiss Bankers' Association, 11 November 1987.

91.Swiss bankers' Association (1987) "Agreement on the Swiss Banks' Code of Conduct With Regard to the Exercise of Due Diligence (CDB)."

92.See Carrington and Edwards (1981) *op.cit.*: 56.

93.OECD (1987) *op.cit.*: 54.

94.Pahud (1987) *op.cit.*: 57-58.

95.Geisst (1982) *op.cit.*: 35.

96.David Frank (1989) "Three Ways to Win, or Lose." *Global Finance*. (August): 49.

97.Nonetheless, with large reserves, by 1989 Swiss banks still maintained a strong international position. Big three bank strategies, however, on remaining internationally competitive in the global financial markets differed. Ibid.: 49-53.

98.Under this structure, most often one of the Big Three Banks would sponsor the Swiss Franc issue. Included in the syndicate were the major German banks, *Deutsche*, *Dresdner*, and *Kommerz*.

99.Sweden was ninth (0.13), Denmark twelfth (0.07), and Ireland twentieth (-0.66). IMEDE and the World Economic Forum (1989) *op.cit.*: 23, 33, 34, 36.

100.For example, commercial banks provided between thirty-seven and fifty percent of short-term and long-term lending to industry between 1966-1980. See Jonas Pontusson (1986) *Labor Reformism and the Politics of Capital Formation in Sweden*: 426, 465.

101.As Lash and Urry explain, "Centrally important in this development [of Swedish industry] were the financial institutions, whose influence really began on a major scale in the 1890s. By the 1950s Sweden boasted the highest levels of concentration of any major western country. A central role in this process of concentration was played by the Swedish banks who had rapidly become major shareholders in leading industrial companies." See Lash and Urry (1987) *op.cit.*: 29-35, 302-303.

102.Interview with Jorgen Setterberg, Executive Vice-President, *Svenska Handelsbank*, Stockholm, 4 September 1987.

103.Anders Vredin (1986) *Capital Flows and Monetary Policy in Sweden*: 25.

104.T.E. Cooke (1988) *Financial Reporting in Sweden*: 31.

105.Ibid.

106.See "Keeping the Blue Chips in the Family." (1988) *Financial Times*. (November 21): 52.

107.Grou (1985) *op.cit.*: 151.

108.*International Who's Who* (1988): 1578.

109.Ibid.: 593.

110."Keeping the Blue Chips in the Family." *op.cit.*: 52.

111.*International Who's Who* (1988) *op.cit.*: 1133.

112.Interview with Sten Westerberg, *Skandinaviska Enskilda Fondkommission*, (Former Undersecretary of Foreign Affairs), Stockholm, 3 September 1987.

113.See Ministry of Industry (1985) *Swedish Industry and Industrial Policy*: 78-79.

114.Pontusson (1986) *op.cit.*: 428.

115.A notable reason for Swedish enterprises' carrying such high ratios is due to taxation reasons. According to sources from Morgan Guaranty, debt-equity ratios in Sweden remain around 2:1.

116.However, yields from the ATP funds were restricted from direct commercial investment. See Henry Milner (1989) *Sweden: Social Democracy in Practice*: 197. The wage-earner funds as well as the "renewal" funds also contributed investment capital in the 1980s, though to lesser extents. Unlike the fourth ATP fund introduced in 1974, the first three ATP funds were not equity investment instruments and allocated seventy-five percent of their lending to the purchase of prioritised bonds. "Retroverse loans" an important financing scheme throughout the 1970s that were designed for corporate sector pension fee re-borrowing, was severely curtailed by government restrictions imposed in 1979. Nonetheless, as Pontusson states, "Retroverse lending ... served to reinforce the autonomous power of the big banks." Pontusson (1986) *op.cit.*: 439, 460.

117.The government in 1979 limited the fund's scope to ten percent equity in any one company. Ibid.: 574-667.

118.See Grou (1985) *op.cit.*: 123.

119.According to the *World Competitiveness Report*, Sweden ranked fourth, Denmark eighth, Switzerland fifteenth, and Ireland seventeenth in terms of international factoring as a percentage of merchandise exports. The Netherlands, Finland, and Norway ranked first, second, and third respectively. IMEDE and World Economic Forum (1989) *op.cit.*: 105. (Table 4.19)

120.See Cooke (1988) *op.cit.*: 31.

121.Interview with Westerberg, 3 September 1987.

122.Interview with Setterberg, 4 September 1987.

123.Interview with Goran Mauritzen, Manager, Capital Markets, *PK Banken*, Stockholm, 3 September 1987.

124.Olle Lindgren (1988) "Stockholm Scraps Its Arsenal" in *Global Investment Management*: 91-94.

125."Foreign Banks Find Sweden Tough to Crack." (1987) *International Herald Tribune*. (July 16): 11.

126."Two Swedish Banks to Seek Foreign Listings." (1989) *International Herald Tribune*. (February 17): 18.

127.Switzerland ranked second, Ireland thirteenth, Denmark fourteenth. See IMEDE and World Economic Forum (1989) *op.cit.*: 103. (Table 4.13)

128.Denmark ranked ninth, Ireland twelfth. Ibid.: 104. (Table 4.15)

129.Switzerland ranked twelfth, Denmark sixth, Ireland ninth. Ibid. (Table 4.18)

130.Denmark's country credit rating was ranked sixteenth out of twenty-two OECD countries. Denmark ranked second to last in terms of gross domestic savings as a percentage of GDP in 1987. Ibid.: 101. (Tables 4.06 and 4.07)

131.Interview with Kai Lindberg, *Den Danske Bank*, Copenhagen, 7 September 1988.

132.IMEDE and World Economic Forum (1989) *op.cit.*: 103. (Tables 4.13 and 4.14.)

133.See Den Danske Bank (1988) *Annual Report*; Privatbanken (1988) *Reports and Accounts*. According to a listing provided by *Privatbanken*'s corporate banking department in terms of Denmark's largest companies ranked according to revenue in 1987, Carlsberg was rated ninth, *Kobenhavens Handelsbank* seventh, *Den Danske Bank* fifth, *Privatbanken* twelfth, and *Skandinavisk Holding* sixteenth.

134.Interview with Steen Parsholt, Country Corporate Officer, Citibank N.A., Copenhagen, 9 September 1988.

135.David Fairlamb (1983) "Transformed Outlook for Danish Bank." *The Banker.* (September): 128.

136.Edi Cohen (1987) "Denmark's Controlled Bang." *The Banker.* (May): 73. (61-73)

137.OECD (1989) *op.cit.*: 90.

138.Interview with Henning Hasle, *Privatbanken A/S*, Copenhagen, 14 September 1988.

139.Cohen (1987) *op.cit.*: 69.

140.See Hasse H. Nilsson (1988) "Denmark: Little Big Bang." Bayerische Landesbank, *op.cit.*: 63-68.

141.See Privatbanken (1988) *op.cit.*: 45; Den Danske Bank (1988) *op.cit.*: 24.

142.A notable reason for Danish enterprises' carrying such high ratios is due to taxation reasons. According to sources from Morgan Guaranty, debt-equity ratios in Denmark remain around 2.5 : 1.

143.Interview with Lindberg, 7 September 1988.

144.Grou (1985) *op.cit.*: 167.

145.Interview with Ole Jess Olsen, Institute for Economics and Planning, Roskilde University, Copenhagen, 9 September 1988.

146.Interview Bo Bogeskov, Institute for Economics and Planning, Roskilde University, Roskilde, 13 September 1988; Interview with Olsen, *op.cit.*

147.For example, in 1987 the Danish Labour Market Supplementary Pensions Scheme (ATP) and the Employees' Capital Pension Fund (LD) held over ten percent of *Privatbanken*'s share capital. A large number of other institutional investors accounted for another twenty-five percent of the bank's share capital. See Privatbanken (1988) *op.cit.*: 52.

148.Michael Metcalfe (1989) "Banks Set Sights on Expansion Into European Financial Services." *The International Herald Tribune*. (March 1): 10.

149.See for example Privatbanken (1988) *op.cit.*: 53.

150.Interview with Jesper Kongstad, Head of Section, Ministry of Industry, Copenhagen, 9 September 1988.

151.Interview with Hasle, 14 September 1988.

152.IMEDE and World Economic Forum (1989) *op.cit.*: 72, 103. (Tables 1.24 and 4.12.)

153.Michael Walsh (1988) "Perspectives on the Irish Financial Markets." *The Irish Banking Review*. (Spring): 24.

154.Interview with Jim O'Farrell, Country Corporate Officer, Citibank N.A., Dublin, 14 February 1989.

155.Interview with Richard Butler, Managing Director, Bank of Ireland Corporate Services, Ltd., Dublin, 21 February 1989.

156.Interview with W.E. O'Reilly, General Manager, Corporate Banking, Allied Irish Bank, Dublin, 14 February 1989.

157.See Barry (1984) *op.cit.*: 104-116.

158.Interview with G.A. O'Mahony, General Manager, International Banking, Allied Irish Bank, Dublin, 14 February 1989.

159.See Craig Gardner/Price Waterhouse (1986) *Tax and Business Decisions and Planning for Tax Incentives and Reliefs in the Republic of Ireland*: 36.

160.Interview with John Robinson, Manager, Corporate Banking, Barclay's Bank PLC, Dublin, 15 February 1989.

161.Interview with Butler, 21 February 1989.

162.For example, T.P. Hardiman, the Chairman of the Investment Bank of Ireland maintained board directorships on two of Ireland's major companies, Carroll Industries and IBM Ireland. See Aspect: The Investor's Business Journal (1989) *The Top 1,000 companies and Who's Who in Irish Industry 1989*: 24.

163.Hu (1984) *op.cit.*: 3.

164.Cited by Morgan Guaranty.

165.Incentives included: only ten percent corporation tax on profits; use of double tax agreements to shield double taxation; lack of capital gains tax; lack of stamp tax; no exchange control; services not liable to VAT; no repatriation requirements. See IDA (1989) *An International Financial Services Centre*.

Chapter Four
Trade Union-Industry Relations and Supportive Labour Market Policies

4.1 Labour-Industry Bargaining and the Influence of Coordinated Labour Market Policies on the Small European State

This chapter will argue that with high levels of international economic vulnerability, small states can less afford to have inflated labour costs and needless periods of industrial inactivity than larger states, which have greater natural and human resources.[1] While it is not assumed that larger states do not face labour unrest and wage drift, nor that their effects are not deleterious to their economies, increasing labour costs and excessive strike activity can more seriously affect a smaller, more concentrated, economy than a larger economy less dependent on foreign commerce and less sensitive to international prices.[2] Significant wage increases tend to undermine small state industries, which are usually price takers, to a greater extent than larger states industries, which tend to be price makers.

As was explained in Chapter One, in examining the four case studies, it is not assumed that these states possess corporatist wage-negotiation structures nor that corporatism is a useful mechanism to examine the role of labour in the small European state. As Claus Offe explains, "In spite of its apparent virtues as a solution to some systematic problems of the political economy, [corporatism] turns out to be a mixed blessing, which may not only heal major institutional defects but also generate new patterns of political conflict."[3] For example, each of the Benelux countries has had centralised wage setting, yet their unemployment rates were all in the double figures during at least a part of the 1980s. With corporatist Scandinavian brethren and supposedly a corporatist structure itself, Denmark has had significant wage inspired inflation along with unemployment. (See Figure 4.1.)

Figure 4.1
Unemployment Rates, Third Quarter 1986

Small European states	%	Larger states	%
Austria	3.4	France	10.1
Belgium	12.0	Italy	10.7
Denmark	8.0	Japan	2.9
Ireland	19.8	Spain	21.0
Netherlands	12.2	UK	13.1
Sweden	2.6	USA	10.1
Switzerland	0.8	West Germany	8.2

Source: *Financial Times* (1987) February 12: 25; *The Economist* (1987).

As illustrated above, while many larger European states such as France, Italy, and the United Kingdom have faced the dual problems of unemployment and labour unrest, small European states, though holding the monocephalic advantage, have not necessarily avoided the same problems. The position taken in this chapter is that while small states do possess a wage bargaining advantage over larger states as a result of their size, the process of bargaining between labour and industry and the role of the State in developing concomitant labour market programmes is a result of each small state's internal situation. Essential differences in trade union-industry relations obviate the utility of such terminology as corporatism as evidenced by the widely diverging levels of unionisation in the four small European states. While in Sweden and Denmark union membership as a percentage of the labour force approached ninety percent during the 1980s, in Ireland union membership was only around fifty percent and Swiss union membership less than forty percent.[4]

Relations between labour, industry, and the State can have a positive influence on the international competitiveness of the small European state, where low levels of unemployment and labour unrest are complemented by active labour market policies, such as in Sweden; little negative influence by maintaining a social compact, but without significant programmes to help labour, such as in Switzerland; or a negative influence, when the labour market system is inflexible or the structure is inadequate, such as in Denmark and Ireland.

Among those who have argued that the corporatist system in small European states provides a notable mechanism for labour and industry to bargain collectively, many point to the success of Sweden, which incorporated a Solidaristic Wage Policy with active labour market programmes during the 1980s. While this thesis will not examine the role of labour in Sweden in such terms as corporatism, there is the assumption that a significant degree of bargaining occurred between trade unions, the State, and industry in Sweden throughout the decade. Much as a result of its communitarian ideology, discussed in detail in Chapter Two, the two major Swedish trade unions were able to exact a significant amount of power in developing and coordinating labour market policies with the SAP. As will be shown in this chapter, unlike the other three countries, labour remained the principal actor in Sweden; it set priorities, developed programmes, and implemented change as a result of the power it garnered through years of development and interaction with other actors. Consequently, much of the focus in this chapter will be on the Swedish case.

In Switzerland, wage bargaining between trade unions and industry was decentralised in the 1980s; however, the Swiss Peace of Work agreement, along with a binding arbitration system, solidified the social compact between labour and industry. Though the Swiss State restricted immigration in times of recession, it developed few programmes to help the unemployed, much as a result of the ingratiated, culturally strong work ethic. While Sweden was able to use its small state advantage to centralise wage bargaining, Switzerland's size augmented a decentralised process of wage bargaining.

Finally, from 1980-1987 both Ireland and Denmark struggled to control wage costs. After attempts at combatting an inflationary price-wage spiral, unemployment and wage drift became such impediments to Ireland's international competitiveness that industry and labour leaders in 1987 worked together to form a *Programme for National Recovery*, a plan to hold down wage increases. In

Denmark the labour market structure, which was mixed between centralisation and decentralisation in the 1980s, was never capable of controlling increasing unit labour costs. As Newell and Symons explain in their monograph *Corporatism, Laissez-Faire, and the Rise in Unemployment*, those countries that have strongly established traditions of collective bargaining, yet also have independent unionisation, "appear to get the worst of all worlds, with a high underlying rate of unemployment whatever happens to inflation."[5] Unlike Sweden, which was able to incorporate its communitarian ideology with active labour market policies, the Danish State and trade unions provided significant unemployment benefits without incentives for reemployment.

This chapter will, therefore, examine the four case studies by comparing relations between trade unions and industry and the use of labour market policies. The key points of discussion are summarised in the following chart. (See Figure 4.2.) Thereafter, short narratives introduce the nature of each state's labour-industry relations during the 1980s.

Figure 4.2

TRADE UNION-INDUSTRY RELATIONS AND SUPPORTIVE LABOUR MARKET POLICIES: THE CASE STUDIES COMPARED

	DENMARK	IRELAND	SWEDEN	SWITZERLAND
Level of labour unionisation	Very high (85%)	Moderate (50%)	Very high (85%)	Low (35%)
Degree of wage bargaining centralisation during the 1980s	Mixed between centralisation and decentralisation	Mixed between centralisation and decentralisation	Highly centralised	Highly decentralised
Relative real unit labour costs in the 1980s	Very high	High before 1987, then moderate	Low	Low
Level of wage drift in the 1980s	High	High before 1987, then relatively low	Moderate	Low
Level of unemployment in the 1980s	High	Very high	Low	Low
Degree of labour unrest	Moderately high	High	Moderate	Very low
Unemployment insurance benefits	Very generous (30 months)	Very generous (15 months)	Limited	Extremely limited
Migration policies	Somewhat restrictive towards immigration	Ineffective policies to thwart massive level of emigration of educated youth	Somewhat restrictive towards immigration	Very restrictive towards immigration
Extent and nature of labour market policies	Few retraining and mobility programmes; emphasis on university education	Limited number of retraining and mobility programmes; significant emphasis on university education	Extensive retraining and mobility programmes; sophisticated university programmes	Few retraining and mobility programmes; extensive apprenticeship system
The effects of wage bargaining and supportive labour market policies on the international competitiveness of the State in the 1980s	Decreasing levels of international competitiveness as a result of ineffective wage baragining that inspired wage increases and the lack of labour market policies (with generous unemployment benefits)	Decreasing levels of international competitiveness as a result of wage-inspired inflation, unemployment, emigration, and the lack of labour market policies (with generous unemployment benefits)	Increasing levels of international competitiveness as a result of a highly productive workforce inspired by the solidaristic wage policy and complemented by active labour market policies	Increasing levels of international competitiveness as a result of a highly productive workforce and effective decentralised wage bargaining
Cooperative or detached trade union-industry relations	Detached	Detached before 1987, then cooperative	Cooperative	Cooperative

Sweden. With its Solidaristic Wage Policy and active labour market policies to counteract unemployment, labour-industry-State relations in Sweden were centralised in the 1980s. Labour played a principal role as a result of the Swedish communitarian ideology. The main vehicles through which labour exerted its influence over the Swedish economy in the 1980s were the combination of 1) centralised wage agreements based on a social compact between labour and industry and a strict solidaristic wage guideline; 2) reduction of inflation through the EFO Model; and 3) active labour market policies and proper education of youth aimed at maintaining full employment, absorbing labour slack, and promoting structural adjustment.

Switzerland. In the 1980s, a social compact was maintained in a decentralised wage bargaining process. In Switzerland a combination of factors allowed for cooperative labour relations, thus contributing to Switzerland's economic success. These measures included 1) the Peace of Work agreement; 2) the binding arbitration system; 3) relatively low unemployment benefits coupled with a nationally pervasive work ethic; 4) the lack of youth unemployment as a result of the apprenticeship system; and 5) significant immigration policies.

Ireland. While wages continued to grow from 1980-1986 as a result of decentralised wage negotiations, the *Programme for National Recovery* was developed and implemented to minimise wage increases as a result of interaction between the central trade union, the employers' confederation, and the State. This chapter will examine how the new government attempted to combat the public sector problem as well as a number of other labour problems from 1980-1987. Those problems included 1) severe unemployment and the lack of job creation programmes; 2) significant wage drift; 3) a relatively high level of labour unrest; and 4) a high rate of emigration.

Denmark. The interactive wage bargaining process remained mixed between centralisation and decentralisation, with the trade unions being able to increase wages significantly at the cost of international competitiveness of the state's industries. This chapter will examine Danish labour-industry relations from 1980-1987 by analyzing its two major problems: (1) wage drift as a result of an antiquated, inflexible system and (2) unemployment, the lack of job creation programmes, and significant unemployment benefits. Unlike Ireland from 1986-1987, where the social partners were able to suppress wage growth, during that period in Denmark labour negotiations became decentralised and wages dramatically increased.

4.2 Collective Bargaining, Wages, and Strikes In the Case Studies

A. Sweden

Since the 1961 report entitled *Trade Unions and Full Employment*, Swedish trade unionists and policy-makers have recognised, and acted upon, the implicit causal relationship between wage moderation, full employment, and international competitiveness. The LO, the premier trade union with membership around ninety percent of the blue-collar workforce, maintained in the report that strong fiscal and monetary policies would prevent excess demand in those regions and sectors with the tightest labour and goods markets, thus checking inflationary tendencies. The notion was to avoid formal price control machinery through a balanced aggregate demand policy; the unions, moreover, would bargain with industry to avoid both significant wage increases and industrial disputes.

This pervasive understanding of the necessity for labour restraint resulted from the LO realising that Swedish industrial competitiveness would ensure employment opportunities. As Richard Rosecrance indicates,

> [in the post World War II period, the] trade unions sought to 'boost quality in the interest of export promotion' while restraining wage increases.[6]

In keeping with the Swedish value of communitarianism, trade union appreciation of the need for wage moderation resulted in virtual "restraint of greedy appropriations of special products by special interests."[7]

However, during the 1970s Swedish international competitiveness faded as a result of the oil shocks and the consequent international recession.[8] Many of Sweden's economic problems persisted because of the inability of the State and trade unions to depress wage rate growth while prices continued to rise.[9] Costs skyrocketed and wages increased forty-four percent from 1976 to 1978.[10] The general real wage level should have been quickly adjusted to changes in productivity given the exogenous shock of the international recession; instead, the centre-right parties were unable to control the powerful LO, and wages continued to spiral despite decreasing industrial productivity. Relative unit labour costs rose by eleven percent per annum in Sweden from 1975-1982.[11]

Moreover, there were significant battles over pay increases during this period, mainly because the unions wanted to regain the purchasing power they had lost to inflation. However, the government wanted public sector employees to absorb the costs of maintaining a tight fiscal policy by minimising spending. The result was Sweden's first large strike in over forty years. As Peter Gourevitch asserts,

> Among other things, the strike seemed to affirm the SAP's claim that it could manage relations with unions better than the bourgeois coalition, overcoming some of the political disadvantage that the party suffered from general anti-union sentiment.[12]

Perhaps the most notable discussion concerning industrial adjustment from the mid-1970s into the 1980s occurred when the Swedish government attempted to influence the productivity of its industries through a policy on wage earner funds. Under the Meidner Model, named after the economist Rudolf Meidner, a portion of pre-tax profits were to be transferred to wage-earner funds administered by the unions. This new equity capital, which remained tax-exempt, would accrue to union funds instead of to private shareholders.[13] These wage earner funds were intended both to bolster the level of savings and investment without a drastic polarised redistribution of wealth and to supply the corporate sector with equity capital. At the same time, labour would maintain a significant management influence. Although the wage-earner fund issue illustrated labour's recognition of the need for equity capital for industrial adjustment, as well as the dramatic influence the Swedish trade unions sought to play in terms of industrial investment, some such as Pontusson have argued that it illustrates labour's failure to wield significant industrial adjustment influence during this period.[14]

Although the issue of labour's management role under the wage-earner fund scheme was debated many times over, the original Meidner model was never implemented, since it was viewed by employers as a "Leninist policy of collective ownership, which challenged the capitalist system."[15] As Henry Milner states, "When the LO called for the establishment of the Wage Earner Funds in 1976, it was, for many employers, the final straw; a line had been crossed."[16]

Because of the uproar the wage earner fund debate had caused, combined with the economic difficulties the state had confronted in the 1970s, the SAP began to work closely with the labour movement when it regained power in 1982. Eighty-five percent of the wage earners in Sweden were affiliated with one of the three major trade unions: the LO; the TCO, the white-collar union for workers without university degrees; and, the SACO/SR, the union for employees with university degrees. Even with the failure of the Meidner model, Sweden's communitarian and egalitarian values did not diminish from 1980-1987. The trade unions maintained their significant power, working alongside the Social Democrats in augmenting Sweden's level of international competitiveness.

After the Meidner debacle, the LO recognised the need for continued investment as evidenced by the ongoing debate over wage earner funds. In 1983 the Edin Proposal (named after the LO's former research director Per-Olof Edin) changed the tone of the wage-earner fund debate by altering any Marxist (or "worker control") overtones. Instead, the notion was to augment industrial productivity, as well as to avoid costly wage increases, by increasing the supply of risk capital through regional funds that locally based fund managers could invest in any company's shares. In contrast to the Meidner model, under this plan the unions could only have up to one-half the voting power attached to any fund shares; workers were not given the power to manage these companies. The Edin proposal offered a mutually beneficial circumstance for both worker and employer. Wage costs would be restrained because the capital originally used for wage increases would now be invested back into the company, and the worker would now have greater incentive to increase his workplace efficiency. Although public reception to this plan was cool (55% against), legislation based on the plan passed through the *Riksdag* in August, when many Swedes had left on holiday.[17]

The ability to pass such legislation with negative public reaction indicates the power of the "two branches of the Swedish labour movement, the ... SAP and LO."[18] As Gourevitch alleges,

> The strength of Swedish labour is intimately linked to its organizational forms, in particular the centralization of Swedish trade-union organization and its links to the Swedish Social Democrats; participating in the government provides resources and incentives that then, in an interactive process, reinforce governing.[19]

Indeed, from 1982-1987 the LO created what many labelled a "closed shop" in dealing with the SAP and industry. While the threat of increased wage demands from the LO persisted from 1980-1987, the popular Finance Minister Kjell-Olof Feldt and the head of the LO, Stig Malm, emerged from annual meetings during this period with wages low enough to avoid adversely affecting the country's international competitiveness. At the root of these centralised negotiations steadfastly remained a social compact between labour and industry, coupled with the Solidaristic Wage Policy.

While it received some criticism concerning efficiency being compromised for egalitarianism,[20] the Solidaristic Wage Policy remained virtually the same through 1987 as it was when introduced in the 1960s, maintaining its emphasis on "equal pay for equal work." The policy was originally developed under the principles of wage fairness and equality; however, it also affected the structural adjustment of Swedish industry because only efficient firms were able to pay the industrially specified wages.

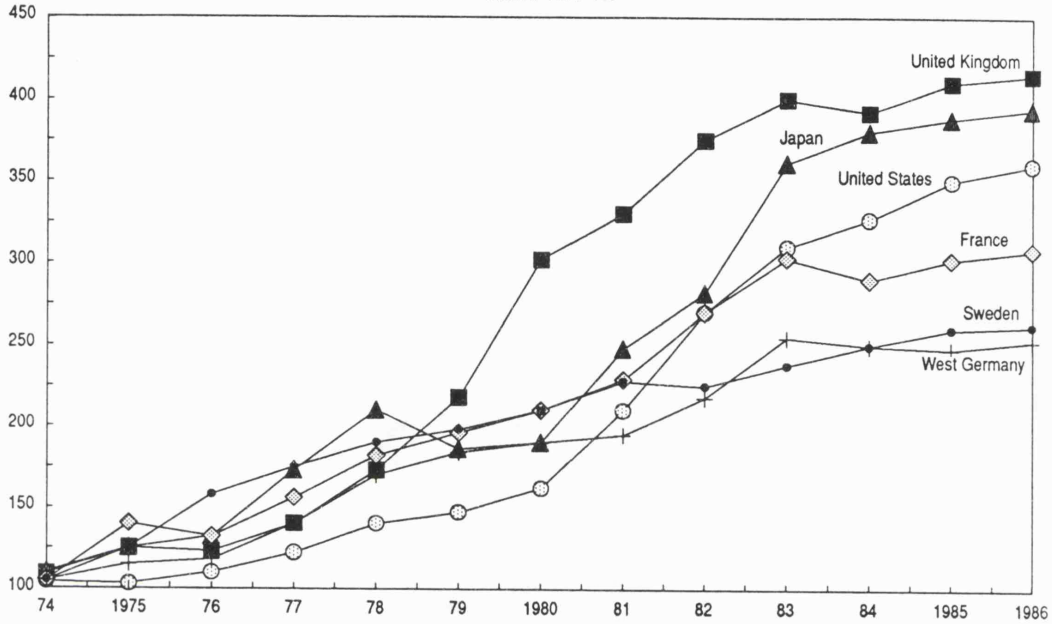
Moreover, inflation previously strained by industrial growth was stabilised[21] through the so-called EFO Model, named after three economists from the LO who produced the collaborative study on the model. It divided the economy into competitive ("C") sectors, based on export competitiveness, and sheltered ("S") sectors, those sectors in which the produced goods are not traded internationally. The essence of the EFO model was to provide a guideline by which wage rates could grow, or a calculation of the "'room' for increases in wages, salaries and profits."[22] Since Sweden maintained an economy significantly based on export-led growth,[23] the C-sector became the basis by which wage rates could increase. The unions could squeeze firms for high wages up to the point at which they would not exceed productivity and which investment would not be negatively affected. It was then up to the C-sector to provide wage guidelines that the S-sector could follow. Although the model was sometimes unreliable and proved difficult for practical use, it highlighted the importance of the trade unions' understanding the need for export competitiveness. Explains Andrew Martin, "At this point, the EFO Model's importance is that it testifies to the concern for external equilibrium shared by the LO with other actors."[24]

Therefore, from 1982-1987 a "bilateral monopoly" existed between the LO, which set wages, and the SAF, which adjusted employment and work hours.[25] Despite some wage bargaining at the local level, which resulted in wage drift,[26] wage negotiations were concluded in a centralised process "through which distributive conflict among the affiliates and their rank-and-file members [could] be effectively managed"[27] and which wage-inspired inflation was controlled through the EFO model. While the SAF "tightly controlled power over its affiliates" in the collective bargaining process, the LO was able to use a "leap frog" strategy to gain more wages from year to year.[28] In general, once wages were determined by the centralised collective bargaining system in trade union negotiations, chiefly for blue collar workers in the LO, firms unilaterally adjusted for employment and work hours.[29]

The ability of the LO to secure desired wages has given ample reason for some Swedish labour market scholars such as Anders Bjorklund to argue rightfully that the trade unions held the upper hand over enterprises in terms of wage negotiations during the 1980s.[30] Indeed, Sweden was ranked third behind Switzerland and West Germany in terms of hourly labour costs, including social security and paid leave.[31] Nonetheless, it is argued here that while Sweden did maintain a relatively high wage level, industrial productivity followed and surpassed wage growth through increasing profits and investment. Consequently, the cost of labour in real terms involved in making each unit of output (i.e., unit labour costs) was lower in Sweden than in competing states. For Swedish employers, high wages were associated with high productivity, which translated into a lower unit labour costs than in countries with lower wages and lower productivity. (See Figure 4.3.)

Figure 4.3

UNIT LABOUR COSTS IN MANUFACTURING INDUSTRY
INDEX: 1973=100



Source: Svenska Handelsbank, "Sweden in the World Economy:" 21; Svensk Industri Och Industripolitik, Industridepartmentet, 1987

While some have argued that the Solidaristic Wage Policy became an outdated, inefficient mechanism to ensure wage equality,[32] there was little question that labour was able to rationalise a programme that augmented international competitiveness. As Heclo and Madsen maintain,

> The wage equality principle imbued the labour movement's position with a programmatic commitment for the future... this development epitomized a distinctly Swedish approach to policy: the ability to rationalize policy moves initiated ostensibly for other purposes and to forge subsequent policy initiatives to fit an overall framework."[33]

In 1985, the difference between the average wage level for branches of industry above the general wage level and those below that level had been narrowed to 13%, compared to 30% in 1960.[34] Despite the powerful unions being able to exact high wages and short work weeks, Swedish industrial productivity grew; the high wage level did not diminish productivity but rather promoted profits and investments that enhanced growth in the manufacturing sector.[35]

In sum, on the basis of a labour-demand equation and real-wage equation, a study of eighteen different labour markets on how they responded to the exogenous shocks of the early 1980s concluded that the Swedish labour market was the most flexible.[36] In addition, according to a *World Competitiveness Report* survey, Sweden ranked second out of twenty-two OECD countries in terms of "the role of organised labour positively affecting the running of companies."[37] Nonetheless, the Swedish collective bargaining system had an essential concomitant ingredient: significant retraining and manpower programmes for workers unemployed as a result of the structural adjustment effects of the Solidaristic Wage Policy. These programmes will be discussed in the following section.

B. Switzerland

In the 1980s negotiations between labour and industry in Switzerland, unlike Sweden, were decentralised. Despite only around forty percent of workers in Switzerland being members of unions, union membership was heavily concentrated among Swiss male workers, even though major industries' labour forces had a large number of marginal or foreign workers, which were not easily organised.

Throughout the 1980s Switzerland's two main trade unions, the SGB and the CNG (*Christlich-Nationaler Gewerkschaftsbund der Schweiz*, the Swiss National Federation of Christian Trade Unions), primarily voiced unified labour opinions on national issues. However, a number of unions under these two umbrella unions conducted independent wage negotiations. Indeed, from the 1970s through the 1980s unions were fragmented as a result of the existence of various denominational unions, the separation between blue and white collar unions, and a split between craft and industrial unions. Much of the reason for these divisions was due to Switzerland's specialised labour force and highly differentiated product lines.

Moreover, unlike in Sweden, labour in Switzerland occupied "a subordinate position" as a result of 1) the decentralised nature of the trade unions and their differences in wage militancy, 2) the implicit threat of foreign direct investment by Swiss companies (i.e, the export of capital) and 3) the lack of coordination between the trade unions and the Swiss Social Democratic Party (*Sozialdemokratische Partei*).[38]

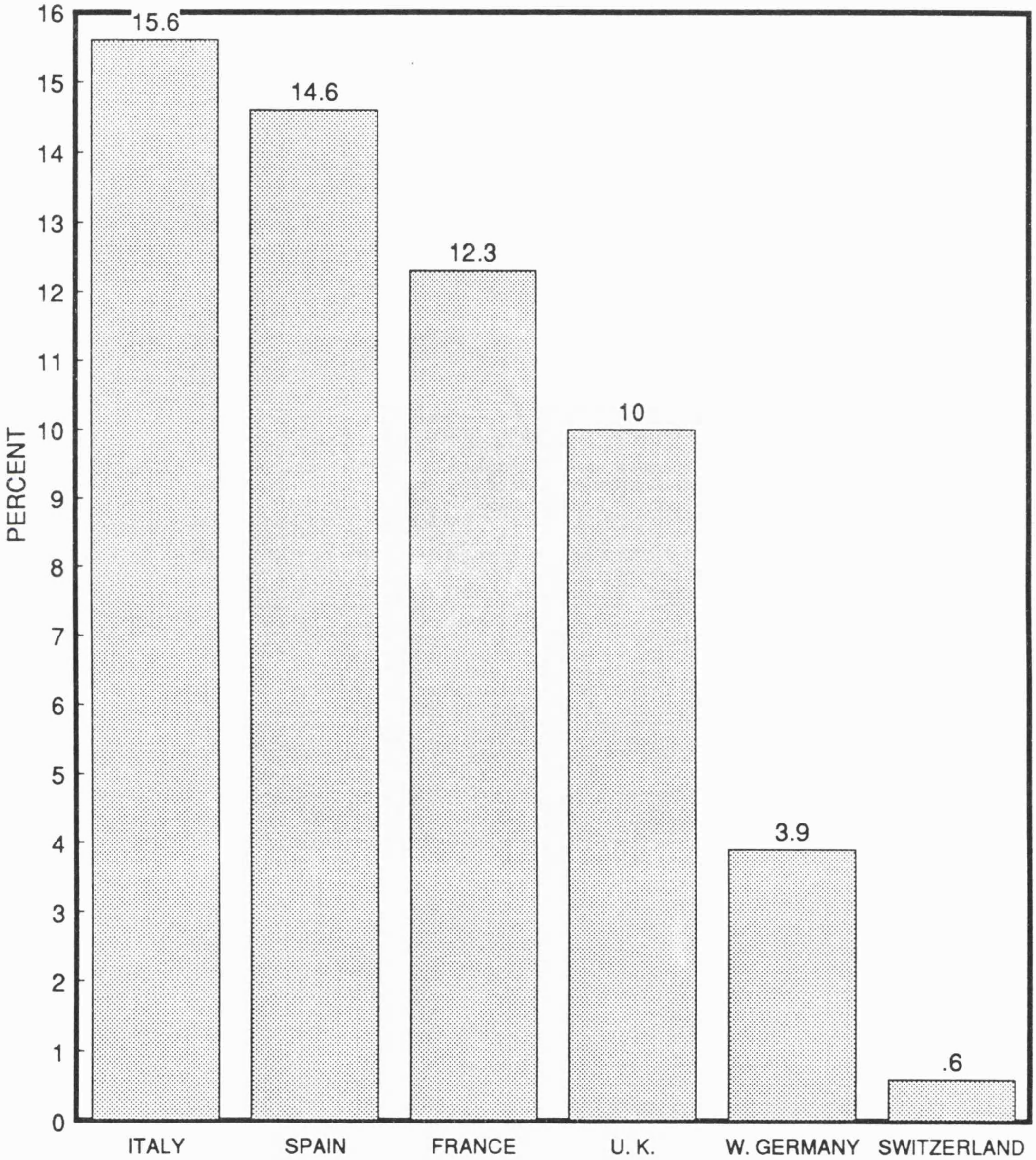
While in most European countries relations between the Social Democratic Party and labour remained strong, in Switzerland differences remained far greater. Throughout the 1980s the unions preserved a private sector strategy for industrial growth, while the party's preference was for greater public activity. Even pension plans stirred significant controversy; the Social Democrats wanted a national plan similar to that in Sweden, while the unions wanted a union pension fund. In fact, in a late 1970s survey, less than one-half of Social Democratic party and union leaders expressed satisfaction with party-union relations.[39]

With Swiss trade unions being relatively weak but also understanding the need for Swiss export competitiveness, decentralised wage negotiations in Switzerland remained highly cooperative. As many as eight-hundred to a thousand collective work agreements, settled through local collective agreements or between each firm and its work council, were bargained each year in the 1980s. This decentralised, yet cooperative, structure allowed for relative wage flexibility between sectors of the economy, in which real wage growth remained relatively low in comparison to competing states.[40] (See Figure 4.4.)

Moreover, the Swiss process of collective bargaining tended to take into account the interests of both labour and industry. This dual awareness explains why Swiss firms used partial unemployment techniques during the 1981-1983 recession, in which firms reduced working hours yet avoided lay-offs.[41] Other states such as Denmark facing recession during this period were more inclined simply to lay off workers, substantially increasing unemployment levels.

Figure 4.4

WAGES (EARNINGS) GROWTH PER YEAR, 1980-1985 SWITZERLAND VS. LARGER EUROPEAN STATES (%)



Source: The Economist (1987) The World in Figures : 225, 230, 241, 259. 263, 268.

Hence, the institutional process of labour-industry bargaining, as a result of "Switzerland's well-known tradition of political and economic decentralization," was developed "by a succession of grand measures: first, wage and profit moderation; second, shorter hours [see Figure 4.5]; and in the last resort, layoffs affecting primarily outsiders, i.e., the foreign workers."[42]

Figure 4.5
Average Hours Per Work Week, Switzerland

Year	Hours	Year	Hours
1919	50	1979	43
1957	47	1983	42
1958	46	1986	41
1960	45	1988	40
1963	44		

Source: Kurt Humbel (1987) *En Toute Bonne Foi: Genese et Evolution De La Convention Du Travail Dans L'Industrie Suisse Des Machines et Des Metaux*: 97.

Given the extraordinary success of the social compact between labour and industry in Switzerland, the binding arbitration mechanism helped ensure that industrial conflicts were both quickly and justly resolved. Even with the exogenous shocks in the 1970s, an agreement by the unions to limit strikes coupled with the binding arbitration system was an important means by which Switzerland was able to deal with difficult circumstances. As Katzenstein explains,

> Despite massive layoffs, collective bargaining proceeded through the late 1970s without strikes and in an orderly fashion. Controversies were resolved by arbitration, and since union officials agreed with the employers on the essential strategy for the industry,

> relations between employers and union officials remained 'excellent'.[43]

Moreover, the procedure to settle wage conflicts under a three-tiered system of arbitration proved particularly valuable throughout the 1970s and 1980s. At the highest level (the third echelon) the arbitral tribunal maintained the final, binding voice between the differing parties, but differences were rarely settled here. In most of the cases conflicts were resolved at the first echelon - at the enterprise echelon - in negotiations between the labour commission of the enterprise and the management. If the conflict could not be supplanted at that level, then it moved to the association echelon (the second echelon). For instance, for the Machinery Manufacturers, labour relations at the association level were between the Association for Machinery Manufacturers (VSM) and its sister organisation on the labour side, the Swiss Association of Machine and Industrial Manufacturers (ASM). (Its parent is the Union of All Employers' Associations, or DSAO, whose industrial counterpart is the *Vorort*.)[44]

During the 1980s if no resolution was reached at the association level, then the conflict moved to the arbitral tribunal. The two parties would designate together the mutual president and a representative from each side. The tribunal of the three members then would elaborate a proposition of conciliation. If this was refused by either party, the tribunal resolved the conflict in the last instance. Its sentence remained mandatory for the two parties.[45]

In addition to the binding arbitration mechanism, the trade unions also agreed to a "peace agreement" formed in 1937 with industry. The arguments in favour of the convention for the trade unions at the time were:

a) the trade unions and employers would be equal partners;
b) the trade unions would be able to demonstrate their respect for the general interest of industry; and
c) negotiations are always sweeter than strikes.

The arguments in favour of the convention for employers were:

a) salaries would be regulated at the level of the enterprise;
b) a peace of work agreement would assure the continuation of production.

And the advantages for both included:

a) an autonomous arbitrage procedure;
b) the peace agreement would help the internal unity of the country;
c) it would reenforce democratic principles;
d) the understanding that strikes are costly for everyone;
e) the belief that a voluntary entente is in the best interests of each, since it augments the prestige of each.[46]

Since its inception, the peace agreement has been extraordinarily strong and is well accepted by the Swiss public at large, illustrated by the level of strike activity in Switzerland being the lowest in the industrialised world. (See Figure 4.6.) According to a *World Competitiveness Report* survey, Switzerland ranked first out of twenty-two OECD countries in terms of "the extent to which unions are conducive to labour peace."[47]

Figure 4.6
The Swiss Peace of Work Advantage,
Days Lost Per 1,000 Workers

Country	Days
Italy	1276
Spain	729
U.K.	529
U.S.A.	269
France	166
West Germany	51
Switzerland	2

Source: Kurt Humbel (1987) *En Toute Bonne Foi: Genese et Evolution De La Convention Du Travail Dans L'Industrie Suisse Des Machines et Des Metaux*: 97.

Because the peace agreement prohibited strikes and lockouts throughout the 1980s, the trade unions and employers' confederations maintained close bargaining contacts. Every five years the peace agreement has been renewed, and work hours and vacations have been revised.

Perhaps most importantly, under favourable labour market conditions and with labour scarcity during the 1970s and 1980s, Swiss trade unions did not sacrifice free collective bargaining to constrain inflation. The trade unions, as social partners to business (*Sozialpartner*) also included in their collective bargains a number of issues beyond conditions of work, including social welfare measures.[48] Indeed, with highly favourable economic conditions within Switzerland in the 1980s, it ranked first among the industrialised countries of the world in terms of hourly labour costs that included social security and paid leave. Moreover, as Katzenstein affirms, "Because the Swiss union movement [would] not trade a stronger position in labor markets for a weaker position in politics, it has adamantly opposed any curtailing of free collective bargaining. As a result, Switzerland has no incomes policy."[49]

C. Ireland

From the 1970s through the early part of the 1980s collective bargaining between trade unions and industry in Ireland was centralised, yet the economic climate of the 1980s proved to be quite different from that of the preceding decade. With the oil crisis and the international economic recession ushering in the 1980s, the second National Understanding (NU) was followed by decentralised "rounds," which continued to prevail to 1987.

Throughout the 1970s tripartite negotiations between the government (the public sector), the ICTU, and the FUE evolved into norm-setting, in which centralised agreements brought about tiered increases in wages each year from 1970-1981. Two wage provisions, "productivity" and "unsustainable inequity," were abused and overused at the same time that the oil shocks, accompanied by the international recession, promoted inflation.[50] As the Economic and Social Research Institute of Dublin has documented, between 1970 and 1980 in Ireland real income grew fifteen percent more rapidly than productivity, while the differential in West Germany during this period was only around two percent.[51]

A political debate dividing those who supported free, decentralised bargaining and those who favoured centralised wage negotiations ensued, and though the *Fine Gael* government tried to buttress waning support for centralised collective bargaining by attempting to forge a peace agreement, the FUE opted against agreeing to centralised wage negotiations much as a result of imported inflation.[52] Hence, the centralised bargaining that prevailed throughout the 1970s collapsed because "norms" were set too high and the two aforementioned provisions abused.

With labour negotiations decentralised after 1981, the role of the ICTU diminished. Although it did issue guidelines to its affiliates in terms of pay guidelines, the ICTU had no centralised authority. "There was no collective mechanism of any sort to ensure equity in pay developments or protection of the interests of the low-paid, less still of the unemployed."[53]

No longer having direct ties with the government, and reduced ties with the Labour Party, the role of the ICTU became overtly criticised. As Hardiman indicates,

> The fragmentation of trade union interests due to decentralised bargaining became increasingly to be criticised.....A shared feeling began to become apparent that unless it could effect internal changes the trade union movement would lose any sense of collective purpose and would increasingly find itself unable to exert effective influence over public policy debates.[54]

Moreover, local bargaining procedures caused significant problems as a result of the large State and semi-State sector. With the State being the country's largest employer, bargaining agreements aroused lengthy phases of negotiation. These agreements became "front-" and "back-" loaded; the result was that the Irish State had the highest debt to GNP service ratio in the OECD, two-and-a-half times that which was tolerable by OECD standards. With the International Monetary Fund (IMF) about to intercede to help the Irish State in 1987, the new minority government led by the *Fianna Fails* had to develop a programme to slim the public payroll.[55]

Because of the international recession and inflation in Ireland topping twenty percent in 1981,[56] wage drift became a major problem in the 1980s. While real after-tax earnings declined by around fifteen percent between 1979 and 1985, the estimated average real cost of employing an industrial worker increased by between five and ten percent.[57] As price inflation increased on an annual basis, wage increases followed a similar pattern, with wage-price inspired inflation becoming a circular dilemma that resulted in some of the worst wage drift in Europe. (See Figure 4.7.)

Figure 4.7
Index of Hourly Earnings in Manufacturing
(In national currency terms, 1980=100)

	1980	1981	1982	1983	1984	1985	1986	1987
US	100	110	117	121	126	131	134	136
Japan	100	106	110	114	118	122	124	126
UK	100	113	126	137	149	163	175	190
France	100	115	132	147	158	167	174	180
FRG	100	105	110	114	117	122	127	132
Nthlnds	100	103	110	113	114	120	122	124
Denmark	100	109	120	128	134	141	148	162
Ireland	100	116	134	149	165	179	193	204

Source: Ministry of Finance (1989) *Economic Statistics*: 35.

Furthermore, significant wage expansion was experienced in traditional industry, which accounted for approximately three-fifths of manufacturing from 1980 to 1987. (See Figures 4.8 and 4.9.) While modern industry almost tripled its output and wage increases were kept to a minimum, traditional industry production output did not significantly change over the period; relative unit wage costs in these particular sectors significantly increased (particularly in 1981 and 1982) relative to other EMS currencies.[58]

Figure 4.8
Industrial Production in Ireland, 1984

Industry Group (000s)	Net Output*	Numbers Engaged
Modern	2273.6	39,400
Traditional	3031.5	156,800
Total Manufacturing	5305.1	196,150

----
*in Million Irish Pounds

Modern - Pharmaceuticals, Machinery, Electrical Engineering, Instrument Engineering, "Other Foods"

Traditional - Non-metallic Minerals, Rest of Chemicals, Rest of Metals, Rest of Food, Drink and Tobacco, Textiles, Clothing, Footwear, Leather, Timber, Wood, Furniture, paper, Printing, Misc. Industries

Source: T.J. Baker (1988) "Industrial Output and Wage Costs, 1980-1987." *ESCRI Quarterly Economic Commentary*: 34, 35.

Figure 4.9
Unit Wage Costs, 1980-1987 (Index 1980=100)

Indstry Group	1981	1982	1983	1984	1985	1986	1987
Modern	98.7	116.7	104.4	99.4	100.7	107.3	91.7
Traditional	112.6	123.9	128.4	132.6	132.5	141.4	142.5
Total Manuf'ing	107.8	118.9	115.0	113.6	112.3	116.4	108.1

Source: T.J. Baker (1988) *op.cit.*: 38.

In addition, the Irish system of conflict resolution remained non-binding for the private sector and binding for the public sector. In the private sector the non-binding arbitration system became inadequate for solving labour disputes, while in the public sector the binding arbitration mechanism remained too rigid for the government, which remained in a fiscal deficit. The examples below help illustrate these two points.

a) In 1982 the trade unions won an important victory over the FUE by amending the 1906 Trade Disputes Act, which in the past had excluded workers from the protection against tort action companies received from the act. Nonetheless, with case law in Ireland, different from many other European countries, the Trade Disputes Act had "implicity given workers the right to strike if they felt they were being injured, even with the changes."[59] Under the non-binding arbitration system the Labour Court, an independent body of six members (three nominated from the FUE, three from the ICTU), was established in 1946 to encourage the "voluntary resolution of industrial disputes."[60] While the court set the standard for arbitration, its non-binding status for private industry was inadequate for difficult labour disputes during the 1980s.[61]

With an adversarial relationship between the ICTU and the FUE, one trade union official asserted, "We do not have a cosy relationship. We do have a relationship based on respect, and we do have to do business, yet because of our legal system, and the ramifications of the trade disputes act, trade unions must at times exert their right to strike."[62]

b) In the public sector, where the court maintained a binding arbitration mechanism, the government as an employer was bound by extremely high wage figures even when the international recession severely affected the fiscal budget. In a dispute between the government and the ICTU's Public Services Committee in 1985, the binding arbitration decision was overturned by a *Dail* vote to negate special pay increases for teachers. It was the first time since 1953 that the government had overturned a public service pay recommendation, and the result was a giant teachers' union strike.

Moreover, strike activity continued to be a problem in Ireland throughout the 1980s. (See Figure 4.10.)

Figure 4.10
Strike Statistics (Official and Unofficial)
Ireland, 1980-1987

Year	No. of Strikes	Days Lost Per 1,000 Workers
1980	132	404
1981	117	436
1982	131	437
1983	151	311
1984	191	364
1985	116	412
1986	100	316
1987	76	260

Source: Department of Labour Estimates (1989)

With the unions being less able to take on a militant stance as a result of the recession and consequent unemployment, there was less industrial action between 1980 and 1987 than in the previous decade, even though the "free-for-all often produced many strikes that might not have occurred under centralised bargaining."[63] Even with these downward trends, strike activity remained a problem for Ireland during this period, especially when compared with the striking activity of such countries as Switzerland. (Also see Figure 4.6.)

As a result of the major problems Ireland faced in the early to mid-1980s, such as unemployment, wage drift, relatively high interest rates, inflation, and high levels of national debt, the CII began a massive campaign to educate the public about the increasing labour costs as a result of rising inflation. As Dr. Con Power, Director of Economic Policy at the CII, asserted,

> We jumped in where angels would fear to tread. We knew that no politician was willing to go to the public and say 'I have misled you; we have been pledging the taxpayers money on credit.'[64]

Moreover, public sector wage demands continued to undermine the national budget and increase national debt. While the National Economic and Social Council (NESC) led a specific campaign to reduce the budget deficit through lower energy, transport, telecommunication, and postal costs, the CII, the FUE, the CIF (Construction Industry Federation) and the ICTU - the so-called "social partners" - began to deal with the management of wage costs.

In the autumn of 1986 discussion commenced between the social partners and the middle-of-the-road opposition party *Fianna Fail*, which subsequently produced the party's election manifesto entitled *The Programme for National Recovery*.[65] With the election of the *Fianna Fail*s in 1987, negotiations began between the Prime Minister's Department (the *Taoiseach*), the ICTU, FUE, and CII. The *Fianna Fail* government entered into office with an attitude of attempting to defuse, rather than oppose, industrial conflict. At the same time, the new Prime Minister, Charles Haughey, openly declared that spending cuts needed to be made to reduce the national debt.

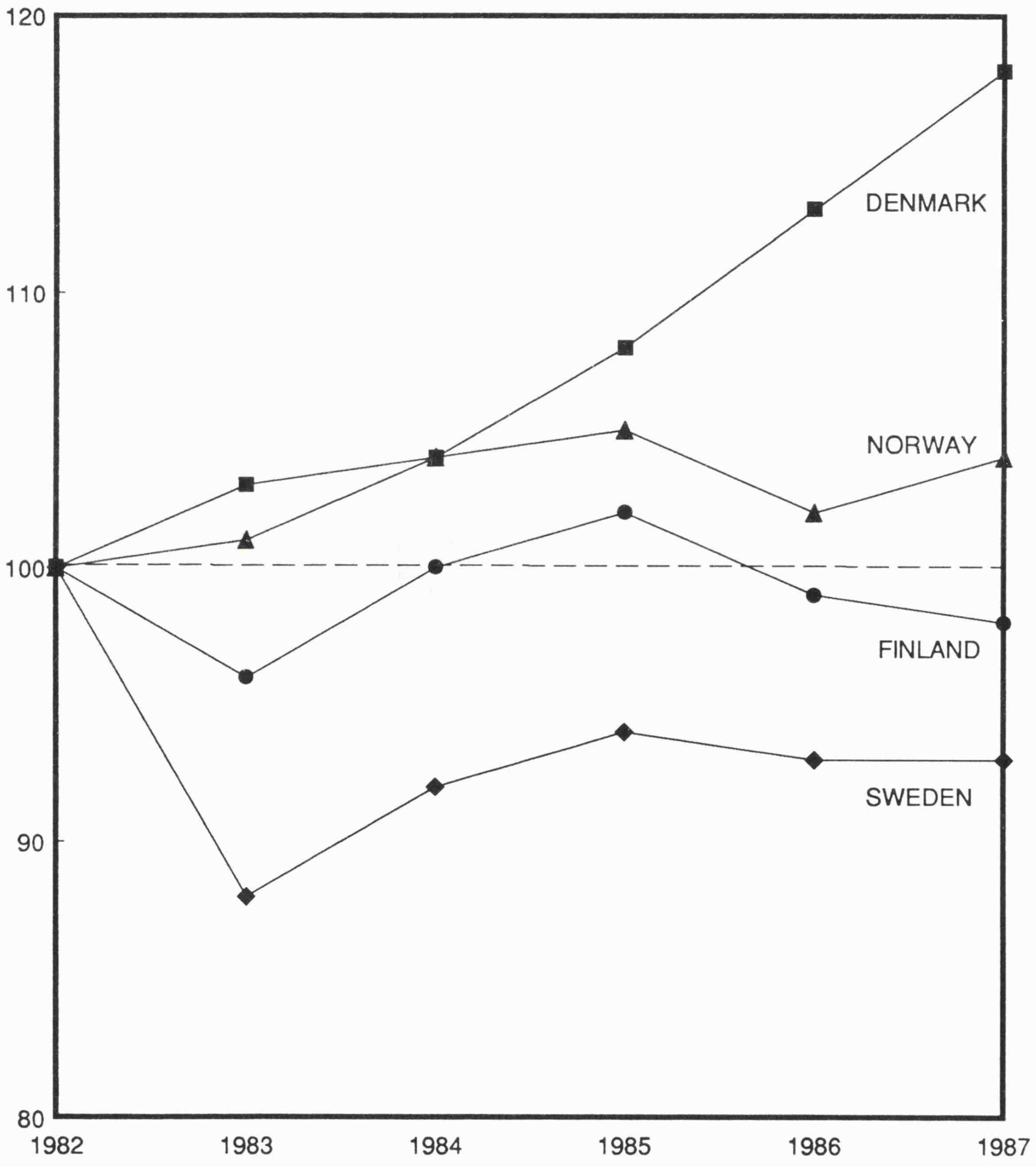
Consequently, the *Programme for National Recovery* was an attempt by the social partners to cut back on the public sector's payroll and at the same time suppress inflating wage costs on the private side. Based on the ICTU's policy document entitled "Confronting the Jobs' Crisis," along with negotiations between the FUE and the ICTU, *Programme* guidelines for annual wage increases would average 2.7% per annum from 1987-1989, with a working week of forty hours.[66] With centralised negotiations between the social partners on wages, the problem of wage drift was substantially alleviated, as was industrial action. Other policies of the national *Programme* attempted to regenerate the economy through tax reform and debt reduction policies.[67] Moreover, many of the problems associated with the decentralised nature of those agencies involved in job creation were being amalgamated into a single organisation known as FAS, the Central Training and Employment Authority, whose goal was to rationalise the three agencies' seventeen different programmes.

D. Denmark

From 1980-1987 Denmark was plagued by wage drift difficulties. Hourly labour costs in industry remained among the highest in the EC throughout much of the 1980s.[68] These problems persisted not only as a result of the international recession and oil shocks, but also because of Denmark's antiquated and inflexible labour market structure. From 1983 through 1987 labour costs per unit of output increased twenty percent faster than they did (on average) in other industrialised countries; wages rose faster than abroad, and productivity increased more slowly.[89] While comparisons are often formed among Scandinavian countries as a result of supposedly corporatist wage bargaining processes, in the 1980s there were significant differences between Denmark, Finland, Norway, and Sweden in their relative unit labour costs in manufacturing. (See Figure 4.11.)

Figure 4.11

RELATIVE UNIT LABOUR COSTS
IN MANUFACTURING,
DENMARK, NORWAY, FINLAND AND SWEDEN
(1982 = 100)



Source: OECD (1988)

Guided by the two umbrella or peak labour market organisations, the LO and the Confederation of Danish Employer's Associations (known as the DA), wages and conditions of work were negotiated on both centralised and decentralised bases in the 1980s.[70] As shown below, the system of collective bargaining between the trade unions and the employers' confederations changed from year to year from 1980 to 1987.

> In 1980/1981 bargaining was decentralised (the LO and the DA left it to the individual unions to negotiate all claims, both generally and special, directly with their employers);
>
> in 1982/1983 a combination of centralised and decentralised bargaining was applied. At first an attempt was made at decentralised bargaining, and, when this did not prove successful, LO and DA took over negotiations;
>
> in 1984/85 LO decided that collective bargaining should be divided into general and special claims .... special claims should be negotiated directly between the individual unions and their employers' organisations. After that the general issues on working hours should be negotiated directly between the negotiating committees of LO and DA .... negotiations were referred to arbitration, yet the mediator's proposal was rejected by the DA;
>
> in 1986 .... the individual unions came to a quick agreement with their respective employers regarding pay increases and a reduction in working hours from thirty-nine to thirty-seven hours; and
>
> in 1987 decentralised wage negotiations took place between individual trade unions and their employers' organisation - wage costs jumped by ten percent.[71]

While the international recession and domestic inflation inspired some small states into a course of dramatic action to forestall further wage increases, in Denmark the process of interaction between the trade unions and industry was unsuccessful in easing wage drift pressures. In Ireland in 1987 a social partnership between trade unions, the State, and industry developed into a national programme to suppress wage increases, yet in Denmark during the same period wage increases actually doubled under a decentralised process of collective bargaining.

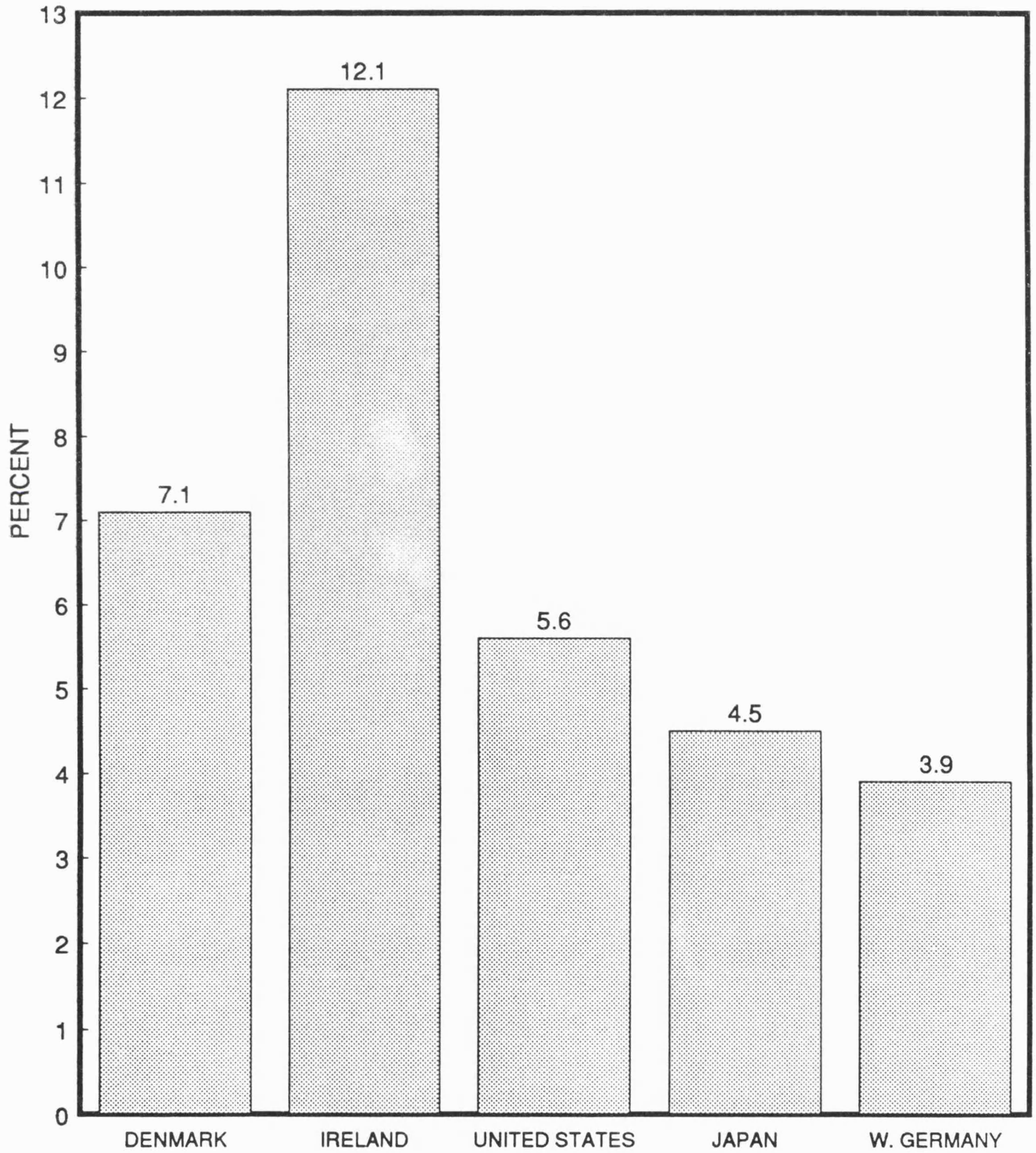
While wage reduction did occur from 1983 through 1987 under biannual voluntary agreements initiated primarily by the LO, in 1985 negotiations failed. There are three interesting points about this particular period of negotiations. First, the LO proposed a wage negotiation scheme mixed between centralisation and decentralisation, in which special claims would be negotiated at the shop level, while general claims would be negotiated at the central level. Second, because negotiations between the LO and the DA failed, binding arbitration ensued. While the Industrial Court's decisions were "final and must be respected by both parties,"[72] the mediator's proposal was rejected by the DA. While maintaining an "Obligation of Peace" agreement, in 1985 major strike action occurred as a result of failed wage negotiations.[73] While the government intervened in 1985 by imposing a legislated two percent wage increase, in 1986, much as a result of political pressures to avoid industrial disputes and declining support, the State opted against wage intervention. In 1987 wages increased ten percent due to the reduction of working hours to thirty-seven with full compensation. Wage negotiations became decentralised and hourly wages increased five percent more than the five percent annual average weighted increase.[74]

Moreover, Denmark became plagued by labour unrest; according to the *World Competitiveness Report*, between 1984-1987 nearly 132 days were lost per one-thousand inhabitants due to industrial disputes ranking Denmark number eighteen out of twenty-two OECD countries. Comparably, Switzerland lost less than one day per one-thousand inhabitants during the same period.[75]

With bargaining primarily at the shop level, the metalworkers, the largest manufacturing sector, had agreed in 1985 to no increases in minimum wages for two years; however, in 1987 they concluded an agreement that gave substantial increases in the minimum wage and a reduction of working hours. After the metalworkers had been successful, these pay increases fed into other sectors, most notably the construction workers and public sector workers. While minimum wages had been settled for the metalworkers, normal wages dramatically escalated. As one LO official explained, "They wanted to catch up to the minimum wage system, so they compensated even though they were already getting paid an annual five percent increase."[76] Similar to the minimum wage scenario, other sectors followed the metalworkers wage gains, causing overall wage drift to increase by ten percent. From 1986 to 1987, therefore, the background of the statutory incomes policy was not accepted by the unions - large pay increases ensued. (See Figure 4.12.)

Figure 4.12

WAGES (EARNINGS) GROWTH PER YEAR, 1980-1985 DENMARK, IRELAND AND SELECTED COUNTRIES (%)



Source: The Economist (1987) The World in Figures : 155, 179, 220, 230, 237.

Furthermore, most Danish scholars have agreed that during the 1980s the Danish labour structure was outdated because of the segmentation[77] of the unions' and employers' confederations' organisations, which included numerous small organisations. For example, in Denmark trade union membership remained high, with the ratio of unionisation around 82%. LO membership consisted of nearly 1.5 million wage earners, nearly sixty percent of the labour force. Within the LO were thirty-two member unions, 140 joint organisations, and approximately 1,400 branches. These numbers were strikingly large for a small state.[78] Consequently, the "antiquated labour market structure became an obstacle; clear-cut borders between various local trade unions ... became unclear."[79] Moreover, the LO and the FTF, the second largest union, became, as Tonboe explains, increasingly "municipalised". "They [the municipal unions] attract and stimulate local activity at the cost of centrally coordinated activity....this restructuring weakens the unions...."[80]

Perhaps the greatest achievement of the Danish trade unions during the 1980s was the pension schemes, which were introduced to stimulate household savings and industrial investment, as well as initiating an attempt at subduing wage drift.[81] By 1987 over one-third of the labour market was involved in the pension scheme, which reduced the wage costs for Danish enterprises much as a result of the Real Interest Tax System, in which a tax advantage was granted to those individuals who invested in equity capital. As one LO official indicated, "This programme helps our enterprises become more internationally competitive; the pension funds spur investment so that eventually if we want higher wages, our enterprises will be able to pay them."[82] Nonetheless, while the pension fund scheme became an innovative mechanism to spur industrial investment, it was relatively ineffective in combatting the wage drift problem.

By the end of the 1980s, however, Prime Minister Poul Schluter attempted to form a deal with Danish wage earners; by cutting their wages by ten percent, they would be given tax reductions. While the offer received a forty-nine percent approval rating from Denmark's wage-earners, "The very thought of reducing wages [was] galling for the unions."[83]

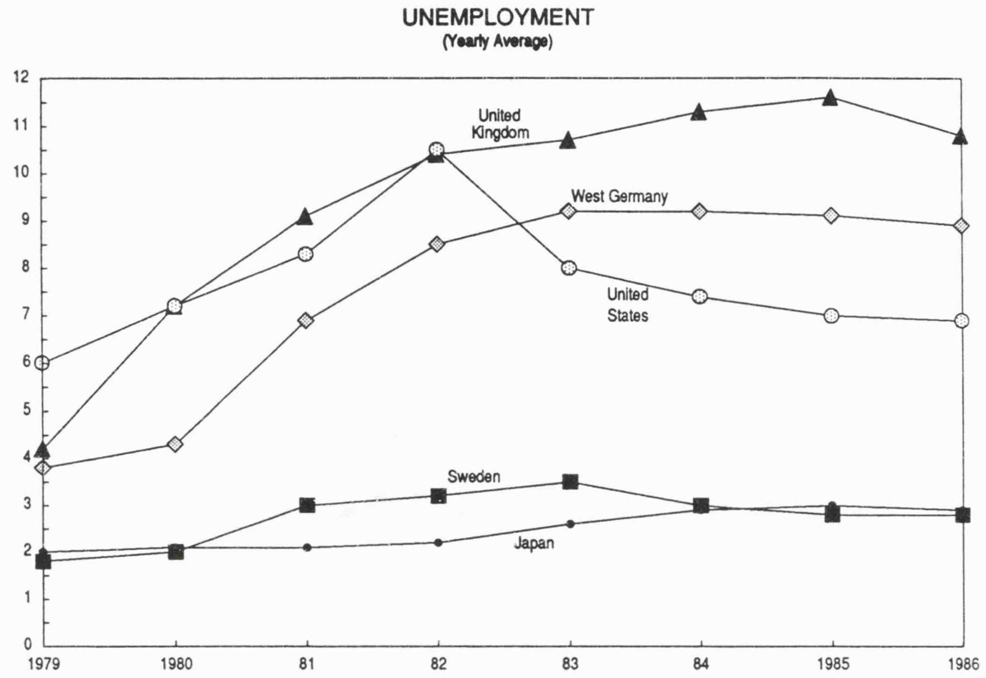
4.3 Combatting Unemployment and Training the Workforce

A. Sweden

Much, if not all, of the restructuring of industry in Sweden during the past twenty-five years can be attributed to the combination of centralised wage bargaining and labour-intensified, market-oriented policies. This section will examine what important trade unionists such as Meidner and Rehn developed as corollary programmes for growth and full employment to its successful centralised collective bargaining system.

Throughout the 1980s Sweden maintained comparatively low unemployment rates. (See Figure 4.13.)

Figure 4.13



Source: Svenska Handelsbank, "Sweden in the World Economy:" 22; Svensk Industri Och Industripolitik, Industridepartmentet, 1987

As a result of Swedish society valuing such communitarian goals as full employment and social welfare, the trade unions along with the State attempted to coordinate labour market programmes that would positively influence industry while maintaining their own egalitarian goals. In the 1960s the relationship between the LO and the government brought about compromise plans between neo-classical economists and trade unionists through the Rehn Plan, the original blueprint for the Solidaristic Wage Policy, which seemed to be a powerful vehicle towards forming a stronger industrial structure. The notion was to give unions the power to form wage agreements and make the State responsible for overall economic stability, including programmes to keep Swedish society employed.[84] For the most part the Rehn Plan achieved its primary goal: it eliminated the defensiveness of the powerful labour unions, maintained the rationalisation necessary for the industrial sector to move forward, and kept workers employed.[85]

Centred on the notion that the State would act as the facilitator in an active labour market policy, the main element of the plan was to starve those firms that were inefficient by making all firms provide discretionary reserve funds, or "wage equalisation pools." The desired effect of the model, which was implemented in 1960, was to promote only efficient, innovative firms that could survive the strict wage guidelines.[86]

Throughout the 1980s this Solidaristic Wage Policy was combined with a policy of labour mobility and retraining, in which the government played an active role in finding, transporting, and training labour for work. These manpower policies were necessary because the wage equalisation policy tended to create unemployment in weak industries; the labour mobility and retraining policies helped workers move to other industries that were flourishing. In the words of Ira Magaziner and Mark Patinkin, Swedish active labour market policies were based on the simple strategy of "retraining for yesterday's workers."[87] Others such as Peter Swenson have argued that government intervention was necessary under the Swedish centralised system of wage bargaining to resolve the "trilemma" between fair wage differentials, higher wages, and full employment.[88]

When the SAP regained power in 1982 and throughout the rest of the 1980s, workers who had been laid off had a number of options. Mobility grants covered travelling costs to prospective employers, and if hired in another region, the State paid moving costs plus a separate amount as a pre-stimulus move. In 1984 this amounted to 15,000 S.Kr.[89] The retraining programme, run by Labour Market Training Centres, maintained a notable participation rate of around four to five percent of the labour force per year. In general, applicants who were unemployed or ran the risk of being unemployed were retrained in growth industries. Employers also had two major responsibilities to their employees (or prospective employees). In case an employee was to be fired, all firms were required to give one month's notice; if any major lay-offs occurred at a particular firm, the Employment Exchange Office was notified in advance so that the office could begin a search process for employment of laid-off workers. Firms were also required to give notice of job openings.[90]

In addition, programmes were developed for disabled, young, aged, and female workers. For example, from 1982 throughout the rest of the 1980s there was a major policy shift towards educational measures to help youth employment, and the results were noticeable.[91] (See Figure 4.14.) Through Youth Cooperative Enterprises (YCEs), in which local governments and trade unions organised study courses which eventually turned into cooperative enterprises, the youth labour market became more productive and increasingly skilled. This mechanism became an increasingly important tool to supplement labour training programmes.[92]

Figure 4.14
Unemployment As % of Labour Force of Each Group (A)
Unemployment As % of Each Group (B)

	A				B			
Year	16	17	18	19	16	17	18	19
80	9.9	9.0	7.6	5.5	3.3	4.3	5.2	4.1
81	11.6	10.1	10.0	7.5	2.9	4.2	6.2	5.6
82	9.1	11.2	11.9	9.6	2.3	4.2	7.4	7.0
83	7.2	8.3	13.1	10.2	1.7	2.9	7.6	7.3
84	4.8	6.5	5.2	3.9	1.1	2.1	3.0	2.6
85	4.0	5.6	5.5	3.5	0.9	1.9	3.1	1.6

Source: Eskil Wadensjo (1987) "The Youth Labour Market in Sweden: Changes in the 1980s." *Economia and Lavoro*: 99.

Moreover, the Swedish educational system produced one of the most educated populations in the world, which helped breed high levels of worker productivity. With the State spending roughly eight percent of its GDP on education throughout the 1980s, compared with America's seven percent, Japan's six and one-half percent, and Britain's five percent, over ninety percent of Swedish students continued in school for two years past age sixteen.

Most importantly, with an educational system unlike that in Switzerland, which featured an apprenticeship approach, Swedish students spent more time in the classroom than most of their European counterparts and then afterwards spent two years at the vocational gymnasium. With such training, particularly in engineering, it is not surprising that Sweden's most internationally competitive firms, such as Asea-Brown Boveri, Alfa-Laval, Ericsson, Saab-Scania, and Volvo, have been in the high tech, engineering fields.

The interactive process between the trade unions and the government was fundamental in Sweden's active labour market policy. This policy was mainly administered by the Swedish Labour Market Board (LMB), whose role throughout the 1980s was to move unemployed workers to places where jobs remained available, create jobs, and retrain and rehabilitate unemployed workers. As will be discussed in Chapter Five, after 1982 when the State ended subsidisation to particular declining industries, most notably shipbuilding, the LMB helped these depressed regions attract new industries by offering training incentives.

Of central importance is the fact that the active labour market policy acted as a complement to the Solidaristic Wage Policy by 1) moving workers from enterprises expelled from the market because they were unable to remain competitive by not being able to pay the solidaristic wages and 2) retraining workers to those areas where they could be gainfully employed. Moreover, the Swedish State provided an educational system that comprehensively trained young people, particularly in the sciences, a necessity for Swedish industry to remain internationally competitive in the future. In essence, the government in the 1980s helped to provide incentives for people to work, as opposed to simply paying cash to the unemployed, such as was the case in both Denmark and Ireland.[93] Hence, centralised wage negotiations were reenforced as a result of labour mobility and retraining.[94]

B. Switzerland

As was discussed in Chapter Two, in Switzerland during the 1980s there were relatively few welfare state benefits; the State had an extremely limited unemployment insurance programme and restricted labour mobility programmes. With few State labour market policies, much as a result of a relatively small tax revenue base from which to establish them, and a nationally pervasive strict working ethic, the onus was placed on the individual to find work and on the firm to train workers.

Throughout the 1980s the Ministry of Economic Policy facilitated meetings between industry and research organisations to deliberate over projects for further training courses that would be managed and run by the employers' associations. Such plans called for the government to cover the costs of the training and for firms to cover the loss of income during the training period - in essence, the private sector would internalise the benefits of these further training costs.[95]

Training (or "impulse") programmes attempted to improve the knowledge of skilled employees and to "increase the diffusion of new knowledge," yet such programmes were relatively underdeveloped and a low priority of the State. With courses generally lasting from one day to one month, covering such subjects as software engineering and energy saving, the amount spent on these programmes declined from sixteen million S.Fr. in 1980 to 8.2 million S.Fr. in 1984.[96] In addition, the government sponsored retraining courses of other orientations, such as language skills classes. Geographic mobility aid, primarily in the form of grants, was also extended to a select number of persons who were retrained and moved to other parts of Switzerland, though the programme was not nearly as extensive as that in Sweden.[97]

Aside from Zurich with its 354,000 inhabitants, during the 1980s most of the population lived in villages and towns, where the social distance was minimal and the *Ruf*, or reputation, of a family in the community was extremely important. "If a child should begin to falter in such preparation [vocational training] for adult self-sufficiency, it is the concern of the whole community, not just school personnel."[98] The compulsory military service also played an important role in steering youth "the right way - ready and willing to work, rising early and working late." Every male was required to attend basic training for four months followed by an annual service, and employers were required to fund the wages of employees while they were on military duty "and usually glad to do so because military contacts are often helpful and 'good for business.'"[99]

Throughout the 1980s around eighty percent of young people attended the Vocational Training System, which was comprised of a two- to four-year apprenticeship with post graduate developing facilities in most professions. Vocational training incorporated "on the job" training, consisting of three-and-a-half days per week of professional instruction with one-and-a-half days of theoretical schooling in order to gain a *formation professionelle.*[100] Training began at age fifteen and lasted for four years, which helps to explain why Switzerland maintained an unparalleled low level of youth unemployment. This form of occasional training allowed firms to internalise the costs during the four years of instruction, moulding young employees, and facilitating integration to the firm.[101] The hazard was training young minds without allowing them to broaden their horizons.

In Swiss business there was a clear priority to practice and experience during the 1980s; young people were required to prove they could manage day-to-day problems before they were awared broader responsibilities. As a result of this business priority, only twenty percent of youths went to high schools and universities. In 1987 forty percent of industry felt they had a problem of lack of qualified workers, while seventy-five percent of the banking and insurance sectors expressed similar sentiments.[102] In general, while the student quota was well below the OECD average, vocational training in Switzerland (with a ninety-seven percent success rate for males, ninety-one percent for females) was well above the OECD average.[103]

Maintaining a workforce capable of handling the demands of the high-tech orientation of Swiss industry was primarily controlled through the immigration of foreign engineers and scientists. Around one-quarter of the working population in

Switzerland was foreign throughout most of the 1980s, and in general, immigration policies were geared to fill gaps between long-term labour market demand and supply. Those undesirable tasks that immigrants handled became less a part of the work composition of foreign labour, mainly because of their rising qualifications. From the beginning of the 1980s through 1986, foreigners as entrepreneurs, scientists, and inventors comprised nearly two-thirds of the yearly federal quota for new annual permits.[104]

Nonetheless, throughout the 1970s and 1980s foreign workers in Switzerland were tightly regulated, mainly because of their numbers - one million foreign people lived in Switzerland, or around one-sixth of the population. Permits, either on a frontier or seasonal basis, were granted by the Ministry for Industry and Work, yet they were not granted without significant speculation in regard to their effect on the "equilibrium of the labour market."[105] As Segalman alleges,

> ...the Swiss policy on immigrants operates almost as if it were controlled by a calibrated spigot which is opened only when labour shortages exist and is quickly shut when Swiss natives begin to draw excessively on unemployment compensation.[106]

Consequently, during periods of recession Switzerland exported its unemployment, while in times of recovery and economic growth, workers were allowed entry into the country.[107] (See Figure 4.15.)

Figure 4.15
Changes in the Swiss Labour Force

Change In:	1974-76 Recession 000's	%	1976-81 Recovery 000's	%	1981-83 Recession 000's	%
Employment	-330	-10.7	+125	+4.0	-65	-2.1
Labour Supply						
Swiss	-60	-1.9	+5	+0.2	-20	-0.7
Foreign	-245	-7.9	+100	+3.2	-20	-0.7
Unemployment	+25	+0.8	-20	-0.6	+25	+0.8

*As of total labour force.
Source: R. Lewin (1983) "Niveau und Struktur der Arbeitslosigkeit in der Schweiz 1979-1983." *Monnaie et Conjoncture*, Bulletin Trimestriel No. 5, Banque Nationale Suisse from Danthine and Lambelet (1987) "The Swiss Recipe." *Economic Policy*: 163.

With only around one-sixth of the working population being covered by unemployment insurance,[108] and despite significant labour market policies, Switzerland avoided significant unemployment problems. With favourable economic conditions during most of the 1980s, Switzerland's Vocational Training System, as well as immigration policies, added to its effective decentralised collective bargaining system.

C. Ireland

With unemployment in the 1980s consistently hovering around fifteen to twenty percent, and with forty-five percent of those unemployed between 1980 and 1987 remaining unemployed for over a year,[109] Ireland was faced with severe problems as to how to create employment. With the international recession affecting the Irish economy in the beginning of the decade, along with a giant national debt, the government imposed stringent measures against increasing public spending, opting against developing significant job creation programmes.

After 1981 when negotiations between the ICTU and the FUE became decentralised and when the ICTU no longer had centralised authority, the *Dail* decided to cut spending on already limited job creation programmes to help diminish a significant budget deficit even in the face of twenty percent unemployment. While the ICTU lobbied for job creation programmes, the results were ineffective. In one report, the ICTU exclaimed, "Trade unions insist that the causes of unemployment are political, that the responses, or lack of them, are also political and that governments are not powerless to deal with the crisis."[110] The result was deteriorating relations with its main political ally, the Labour Party.

Without a sufficient degree of central coordination by the government in forming manpower policies, two respected economists, Dennis Conniffe and Kieran Kennedy, writing on Ireland's employment policy (or lack thereof) indicated that, "A reasonable degree of harmony is difficult to maintain in the absence of a coherent overall set of policies providing the framework within which the various agencies can work."[111] With the Department of Labour playing virtually no role at all in the formulation of job creation programmes, three agencies (ANCO, the National Training Authority; the National Manpower Service; and the Youth Employment Agency) provided a total of seventeen different programmes in training and employment schemes, most of them only short-term solutions to difficult long-term structural unemployment problems.[112] Understanding the need to rationalise with overlapping programmes, Conniffe and Kennedy asserted that,

> There is an urgent need for central coordination of all the agencies operating in the [manpower] sphere because, currently, responsibility is fragmented, accountability is difficult to enforce, inter-agency friction occurs and agencies are left to form policy which is properly the prerogative of Government ministers and their departments.[113]

Similar in nature to the unemployment insurance programme offered in Denmark, unemployed individuals could remain unemployed and receive insurance benefits for up to 156 days (15 months).[114] With virtually an open-ended unemployment insurance scheme, the Irish State provided few incentives for those unemployed to seek jobs. Under the unemployment assistance programme, 5.6% of Ireland's GDP in 1987 was spent on this programme and the decentralised manpower programmes, the highest in the OECD.[115]

Furthermore, in the 1980s emigration, considered a major cause for economic decline in Ireland, rose to levels not seen since the 1950s. (See Figure 4.16.) While emigration helped to offset some of the unemployment problems in the country, much of the reason that emigration occurred at such a substantial rate was obviously because of better job prospects abroad.[116]

Figure 4.16
Migration Statistics, Ireland 1980-1987

Year	Mid-April Population Estimate (000)	Estimated Net Migration in the year to mid-April (- = Outflow, 000s)
1980	3,401	-8
1981	3,443	2
1982	3,480	-1
1983	3,504	-14
1984	3,529	-9
1985	3,540	-20
1986	3,541	-28
1987	3,543	-27

Source: Central Statistics Office (1989)

In terms of youthful human capital, the results were impressive: between 1985 and 1986, 33% of university engineering graduates emigrated; in electronic engineering, 40% emigrated; and in computer science, 26% emigrated.[117] Persons with third level qualifications who gained employment in Ireland fell from 84% in 1980 to 64% in 1986; in 1985 and 1986, 14.5% and 17.1% of these persons emigrated to find work.

Consequently, while in earlier periods such as the 1950s, the majority of the emigrants were from underdeveloped areas with limited educational opportunities, in the 1980s the group contained "an inordinately high proportion of qualified workers."[118] According to *The World Competitiveness Report*, Ireland ranked first out of twenty-two OECD countries in terms of "the extent to which institutions adequately prepared executives for the needs of the business" (categorised in the report as "education and training"). It also ranked first in both quantity *and* quality of available skilled labour. However, Ireland ranked last among those same countries in terms of "the extent to which a 'brain drain' of well-educated people occurs due to better job opportunities abroad."[119]

Therefore, both the *Fine Gael* and the *Fianna Fail* (coalition) governments of the 1980s attempted to combat unemployment by reinvigorating the economy, specifically through economic programmes that included major tax incentives; however, job creation programmes as necessary concomitants to these programmes lacked departmental centralisation, remained unreliable, and in need of extreme rationalisation. The unemployment insurance programme provided few reemployment benefits and remained a drain on the fiscal budget. At the same time, perhaps Ireland's greatest asset, its well-educated and youthful population, emigrated.

D. Denmark

From 1980-1987 Denmark was not only plagued by wage drift problems, but also unemployment difficulties. Unemployment as a percentage of the working population in Denmark between 1980 and 1984 averaged 9.2%.[120] This problem persisted not only as a result of the international recession and oil shocks, but also because of its antiquated and inflexible labour market structure along with the limited presence of labour market policies.

According to most economists, the unemployment problem in Denmark affected those on long-term assistance, social assistance clients, and early retired workers; these three groups grew from 9.9% of the Danish population in 1972-1973 to 21.1% in 1982.[121] The largest group of those who remained unemployed were the unskilled workers, a situation primarily caused by the Danish unemployment insurance scheme. The inequality of the unemployment burden was evidenced by those insured being the highest number of unemployed workers in Denmark. Denmark ranked amongst the worst in the OECD for having a significant proportion of the workforce being unemployed for over an extended period of time.[122] (See Figure 4.17.) Moreover, Danish legislation with respect to job security was among the most liberal in Europe, providing little employment protection against individual and collective dismissals.[123]

Figure 4.17
Risk of Unemployment in the Danish Workforce, 1987

	A	B	C	D
Unskilled, Insured	54.0	33.6	18.9	657,269
Clericals	27.5	36.6	10.1	290,764
Construction	48.5	16.6	8.1	91,358
Metalworkers	36.3	20.1	7.3	111,244
Rest	18.0	33.3	6.0	1,322,365
Total*	28.6	30.7	8.8	2,473,000

*Average in A, B, C; added total in D
A = Risk of being unemployed after one year
B = Average share of year unemployed per unemployed worker
C = Aggregate unemployment ratio
D = Total unemployed

Source: Det Okonomiske Rad (1988) *Dansk Okonomi*. (June): 86.

Throughout the 1980s the basic system of unemployment insurance offered unemployed unskilled workers (at a minimum) ninety percent of their previous wage, fifty percent for skilled workers. No matter the level of skill, the worker could receive these benefits for thirty months (two-and-a-half years). As a consequence there was little incentive for unskilled workers to accept a job at a lower wage, and even the benefits for the skilled worker were more generous than most other European unemployment programmes.[124]

Furthermore, not only were retraining programmes scarce in Denmark, but there were also only a limited number of mobility programmes. With a limited regional problem primarily in the south of Zealand, the Danish State did almost nothing in terms of labour mobility. Only a few very specific mobility programmes were offered to revitalise problem areas in the country.[125]

Although by the 1950s the Danish State had discovered that labour mobility remained a problem, there was greater focus in terms of improvement of coordination of wages and socio-economic necessities than actual State incentives to change locations to gain work.[126] While in the 1970s and 1980s negotiations did take place to reorganise labour market mobility and training, the State, remaining in a deficit through much of the 1980s, opted against direct mobility programmes such as grants. Instead, State money was pumped into the generous unemployment insurance scheme.

Much of the reason for the failure of the Danish State to initiate labour market programmes was due to ineffective, fragmented consultation between governmental bureaucracies. From the 1970s through the 1980s, the Ministry of Labour handled the retraining of skilled workers, while the Ministry of Education handled the training of unskilled workers. Yet the Minister for Labour in the 1980s was a conservative, while the education minister was a Social Democrat. Neither could agree on a suitable integration of these federations, and a stalemate ensued. While the LO and the DA could reasonably accept any policies, the institutionalisation stalemated the retraining process. As Nielsen and Pedersen maintained in an interview,

> We are not saying this is an inflexible system. There are long-standing traditions for negotiation, yet the problem is how do you use the flexibility of the system to break up the allocational inflexibilities. That is the contradiction.[127]

Consequently, while unemployment remained a problem, the Danish provident state granted generous unemployment insurance programmes with few incentives to work. At the same time few retraining and mobility programmes, such as those found in Denmark's neighbouring state Sweden, were generated to create employment opportunities.

4.4 Comparing Labour Market Systems: Swedish and Swiss Success and the Need for Change in Ireland and Denmark

With continual bargaining among labour, the State, and industry, Swedish trade unionists, policy-makers, and industrialists formed an innovative system in the 1980s whereby those unable to work were cared for by the State while those who were able to contribute in the workforce were mobilised, thus reducing and equalising the costs of a welfare state.

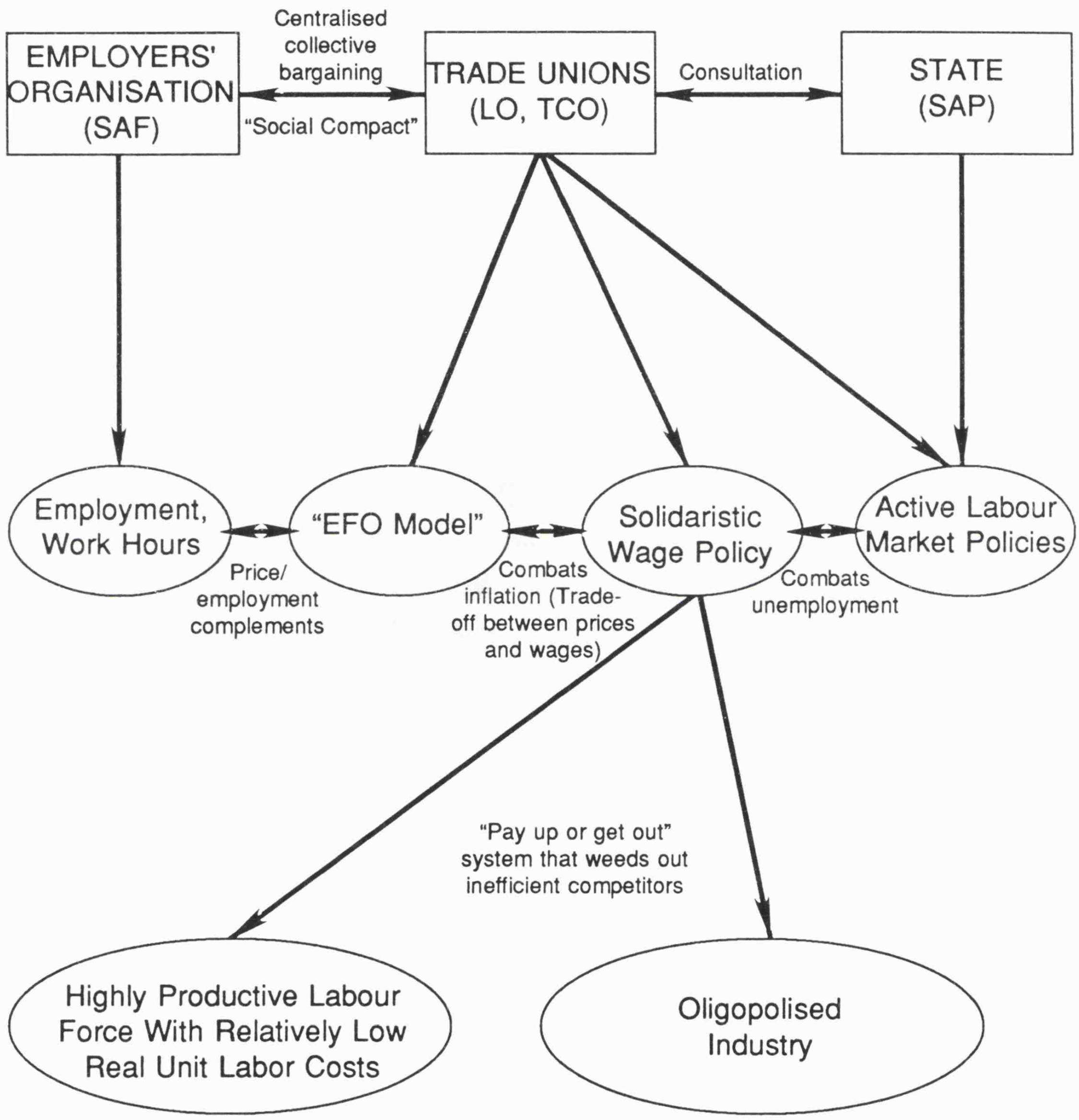
Swedish active labour market policy has been based on the principle that training and education provide an incentive for able-bodied workers. At the same time, the State must provide social welfare benefits for those who cannot work. As Gosta Rehn explains,

> The offer of economic incentives is designed to stimulate those who are willing and able to undertake adjustments in the labour market voluntarily instead of laying most of the burden of adjustment on the weaker groups, making 'social cases' of those who are most vulnerable to unemployment and least adaptable for new jobs....[128]

In Sweden during the 1980s there remained an effective social compact between labour and industry; relations between the two could be characterised as cooperative bilateral. Wage growth was restrained enough for firms to remain competitive, yet high enough to motivate workers and to avert significant labour disruption. While wage levels were relatively high, workers remained extremely productive. As a consequence, real unit labour costs in Sweden during the 1980s were relatively lower than most, if not all, of its competitors. In addition, as a result of the Solidaristic Wage Policy, firms unable to pay the bargained wages were forced out of the marketplace. Indeed, this "pay up or get out system" is precisely why in the 1980s Sweden maintained a relatively oligopolistic structure of multinationals, with twenty of the largest companies forming the backbone of the Swedish industrial base and providing over half of all employment in Sweden. (See Figure 4.18.)

Figure 4.18

THE ROLE OF LABOUR IN SWEDEN, 1982 - 1987: TRADE UNION - INDUSTRY RELATIONS AND SUPPORTIVE LABOUR MARKET POLICIES



The influence of Sweden's trade unions and the process of The interaction between the LO, the SAF, and the State was the primary vehicle for Sweden's industrial success; as illustrated through this process explained in this chapter, labour was the principal actor in Sweden's attempt at remaining internationally competitive in the 1980s.

In the 1980s negotiations between labour and industry in Switzerland, unlike Sweden, were decentralised. Wage issues were settled through local collective agreements or between each firm and its work council. This decentralised structure allowed for relative wage flexibility between sectors of the economy and integrated the interests of both labour and industry. As a result, relations between trade unions and industry could be characterised as cooperative bilateral. The Peace of Work agreement fosted labour cooperation, and when the odd industrial dispute did arise, it was resolved quickly through a binding arbitration mechanism. With few State programmes, much as a result of a relatively small tax revenue base from which to establish and a nationally pervasive strict working ethic, the onus was placed on the individual to find work and the firm to train the workers; however, the Swiss education system placed significant emphasis on apprenticeship training. In order to overcome a shortage of highly skilled workers during favourable economic periods, immigration policies attempted to attract highly skilled workers. However, during less favourable economic periods, strict immigration policies precluded an influx of less skilled workers.

Hence, Switzerland exported its unemployment during periods of recession, while in times of recovery and economic growth, workers were allowed entry into the country.

Under the *Programme for National Recovery*, Ireland was able to halt the growth of wage costs experienced under detached bilateral relations between trade unions and employers. At the same time the State began to undertake policies to reduce the national debt and unemployment. Unlike the Danish case, the Irish case (from 1987) provides a striking example of a small state struggling to tackle its problems, taking advantage of its size for negotiation and bargaining. Particular economic actors - the central trade union, the central employers' confederation, and the government - worked together in a monocephalic environment as so-called "social partners" to induce necessary changes. While the national consensus achieved in Ireland might not have taken place without the long, erratic period of the 1970s and early to mid-1980s, and although enormous labour problems persisted thereafter, the *Programme* did provide the necessary steps to suppress wage growth, a significant accomplishment for a state that was burdened with high wage costs and excessive unemployment throughout most of the 1980s.

As scholars such as Lars Calmfors and Newell and Symons have illustrated in their works, the most efficient forms of collective bargaining occur under very high levels of centralisation, such as the Swedish case, or under very low levels of centralisation, such as the Swiss case. However, between the two extremes during the 1980s was the Danish case; according to one Danish economist, over one-half of wage increases in the 1980s were due to the inefficient, mixed labour market structur. Hence, during the 1980s relations between trade unions and industry in Denmark could be characterised as detached bilateral.[129] There is also evidence that this relatively inefficient means of wage bargaining will produce further wage drift and possible strikes into the 1990s.[130]

In relating this chapter back to the original thesis, interaction between labour and industry varied during the 1980s among small European states. In the two cases of Sweden and Switzerland, positive interaction augmented the state's international competitiveness. Moreover, labour market interventionism, particularly in Sweden with its labour market policies and in Switzerland with its immigration policies, acted as active State policy concomitants to their impressive wage bargaining systems. In cases where active labour market policies were not implemented in the face of declining international competitiveness in the small European state, such as in Denmark and Ireland, the state faced significant wage drift, high levels of unemployment, high levels of labour unrest, and (in the case of Ireland) significant emigration of its trained youthful population. Only by the end of the 1980s had policy-makers in Ireland mapped a course of action, and in Denmark little was done at all during the decade to resolve its major labour market problems. Consequently, during the 1980s not all small European states were able to take advantage of their monocephalic communication advantage, and in cases where labour-industry interaction was successful, State interventionism was employed through complementary labour market policies.

Notes for Chapter Four

1.Among those who have attempted to define or characterise "international competitiveness," most economists have operationalised its definition as relative unit labour costs.

2.See Chapter One.

3.Claus Offe (1985) *Disorganized Capitalism*: 242.

4.See Hugh Heclo and Henrik Madsen (1987) *Policy and Politics in Sweden*: 19-21; European Trade Union Institute (1987) *The Trade Union Movement in Denmark*: 14; Niamh Hardiman *Pay, Politics, and Economic Performance in Ireland*: 221; and Ron Bean (1985) *Comparative Industrial Relations*: 39.

5.See Andrew Newell and James Symons (1986) *Corporatism, the Laissez-Faire, and the Rise in Unemployment*. Samuel Brittan (1987) "Corporatism Rides Again, But None Too Securely." *Financial Times*. February 12: 25.

6.Richard Rosecrance (1986) *The Rise of the Trading State: Commerce and Conquest in the Modern World*: 175.

7.Ibid.

8.See Gunnel Gustafsson (1989) "Challenges Confronting Swedish Decision-Makers: Political and Policy Responses 1974-1987" in Damgaard, Erlich, and Richardson, eds. *The Politics of Economic Crisis*: 164.

9.See Barry P. Bosworth and Robert Z. Lawrence (1987) "Economic Goals and the Policy Mix" in Bosworth and Rivlin, eds. *The Swedish Economy*: 112.

10.J.K. Johansson (1984) "Developing an Industrial Policy: The Swedish Experience." *Journal of Contemporary Business*: 84.

11.See Gosta Rehn (1987) "State, Economic Policy, and Industrial Relations in the 1980s: Problems and Trends." *Economic and Industrial Democracy*: 72-77.

12.Peter Gourevitch (1986) *Politics in Hard Times: Comparative Responses to International Economic Crises*: 203.

13.Andrew Martin (1985) "Wages, Profits, and Investment in Sweden" in Leon N. Lindberg and Charles S. Maier, eds. *The Politics of Inflation and Economic Stagnation*: 449.

14.See Jonas Pontusson (1986) *Labor Reformism and the Politics of Capital Formation*. Ph.D. Dissertation, University of California-Berkeley: Chapter 8.

15.Interview with Lars Heikensten, Head of Long-Term Planning, Ministry of Finance, Stockholm, 8 September 1987.

16.Henry Milner (1989) *Sweden: Social Democracy in Practice*: 129-130. In addition, as Pontusson explains, the wage earner fund debate tested "the limits of social democratic hegemony." While the wage-earner fund debate received an approval rating of 61% from socialist voters, it only received a 2% approval rating from bourgeois voters. See Jonas Pontusson (1988) *Swedish Social Democracy and British labour: Essays on the Nature and Conditions of Social Democratic Hegemony*: Chapter Three, 19.

17.Heclo and Madsen (1987) *op.cit.*: 282-284; Interview with Heikensten, 8 September 1987.

18.See C.H. Siven (1983) "The Political Economy of Sweden in the 1970s." *The Annual of the Institute of Economics*: 236; also, Heclo and Madsen refer to their power as "hegemonic."

19.Gourevitch (1986) *op.cit.*: 30.

20.Many scholars who have studied the Swedish economy point to the down side of the policy, noting that a price of efficiency for egalitarianism may be paid. This thesis will not attempt to assess the future allocational costs of the Solidaristic Wage Policy. See Robert J. Flanagan (1987) "Efficiency and Equality in Swedish Labor Markets" in Bosworth and Rivlin, eds. *The Swedish Economy*: 149-153.

21.Sweden has had notoriously an inflation problem, but inflation stabilised and progressively became lower from 1982-1987.

22.Flanagan (1987) *op.cit.*: 160.

23.Interview with Dr. Harry Flam, Institute for International Economics, Stockholm University, Stockholm, 1 September 1987.

24.Martin (1985) *op.cit.*: 415.

25.See Guy Standing (1988) *Unemployment and Labor Market Flexibility: Sweden*: 47.

26.See Stephen Turner (1987) "The Swedish Model: What Went Wrong." *The Economics of Institutions and Markets*: 81-82.

27.Martin (1985) *op.cit.*: 464-465.

28.See Bean (1985) *op.cit.*: 83-84.

29.See Bertil Holmlund and John Pencavel (1987) *The Determination of Wages, Employment, and Work Hours in an Economy with Centralized Wage-Setting, 1950-1983*: 17.

30.The Solidaristic Wage Policy was discussed in detail in the interview with Anders Bjorklund, Industrial Institute for Economic and Social Research, Stockholm University, Stockholm, 9 September 1987.

31.*The Economist* (1988) 23 April: 91.

32.For example, Swenson argues that in Sweden (and West Germany) a "wage policy trilemma" - a trade-off between fair wage differentials, higher wages, and full employment exists because typically only two out of the three can be addressed under centralised wage bargaining. Hence, government market intervention becomes necessary to resolve the trilemma. See Peter Swenson (1989) *Fair Shares: Unions, Pay, and Politics in Sweden and West Germany*: 129-176.

33.Heclo and Madsen (1987) *op.cit.*: 117.

34.Gosta Rehn (1984) "The Wages of Success." *Daedalus*: 141.

35.According to the *World Competitiveness Report*, in 1988 Sweden ranked second among twelve OECD countries in terms of real unit labour costs in manufacturing (based on 1977=100). See Imede and World Economic Forum (1989) *The World Competitiveness Report*: 78. (Table 2.08)

36.See C.R. Bean, P.R.G. Layard, and S.J. Nickell (1985) *The Rise in Unemployment: A Multi-Country Study*, Discussion Paper No.239. Moreover, in Sweden there has been evidence that nominal wages are more flexible than prices. If prices are not flexible, then wages must be. See Bengt Assarsson (1986) *Price Flexibility in the Swedish Manufacturing Industry: A Transaction Cost Approach*. Price Flexibility is explained by the transaction costs of firms.

37.IMEDE and World Economic Forum (1989) *op.cit.*: 183. (Table 10.11.) Switzerland ranked number three.

38.See Peter J. Katzenstein (1984) *Corporatism and Change: Austria, Switzerland, and the Politics of Change*: 114, 101-102.

39.See Peter J. Katzenstein (1980) "Capitalism in One Country? Switzerland in the International Economy." *International Organization*: 524-525. Also, Katzenstein (1984) *op.cit.*: 114, 101-102.

40.See Seppo Honkapohja (1987) "'Discussion' of 'The Swiss Recipe: Conservative Policies Ain't Enough.'" *Economic Policy*: 176.

41.Jean-Pierre Danthine and Jean-Christian Lambelet (1987) "The Swiss Recipe: Conservative Policies Ain't Enough." *Economic Policy*: 168-169.

42.Ibid.

43.Katzenstein (1984) *op.cit.*: 228.

44.Interview with Peter Eberhard, Director, Information Department, Swiss Association of Machinery Manufacturers, Zurich, 10 November 1987.

45.See Kurt Humbel (1987) *En Toute Bonne Foi: Genese et Evolution De La Convention Du Travail Dans L'Industrie Suisse Des Machines et Des Metaux*: 52.

46.Ibid.: 8.

47.See IMEDE and World Economic Forum (1989) *op.cit.*: 183. (Table 10.10)

48.Katzenstein (1984) *op.cit.*: 129, 144-145.

49.*The Economist* (1988) *op.cit.*: 91.

50.Interview with Dr. James O'Brien, Federated Union of Employers, Dublin, 21 February 1989.

51.Peter Bacon, Joe Durkan, Jim O'Leary (1982) *The Irish Economy: Policy and Performance 1972-1981*: 102-104.

52.Interview with Patricia O'Donovan, Deputy Secretary-General, Irish Confederation of Trade Unions, Dublin, 16 February 1989.

53.Niamh Hardiman (1988) *Pay, Politics, and Economic Performance in Ireland*: 224.

54.Ibid.: 226.

55.Interview with O'Brien, 21 February 1989.

56.Irish Department of Finance (1988) *Economic Statistics*: 49.

57.Hardiman (1988) *op.cit.*: 224.

58.See T.J. Baker (1988) "Industrial Output and Wage Costs, 1987." *Quarterly Economic Commentary*: 33-43.

59.Interview with O'Donovan, 16 February 1989.

60.Federated Union of Employers (1989) *Directory of Services*: 19.

61.Interview O'Donovan, 16 February 1989.

62.Ibid.

63.Interview with Brian Leonard, Department of Labour, Dublin, 22 February 1989. Moreover, much as a result of the recession and unemployment, trade union membership peaked at the end of the 1970s and reached fifty percent of the workforce in 1984.

64.Interview with Dr. Con Power, Director of Economic Policy, Confederation of Irish Industries, Dublin, 20 February 1989.

65.See Fianna Fail (1986) *The Programme for National Recovery*.

66.See "Draft Agreement on Pay in the Public Service" (1987); "Framework Agreement on Hours of Work (1987); and "Proposals for An Agreement Between the ICTU, the FUE, and the CIF."

67.See *Programme for National Recovery* (1987) *op.cit.*: 5.

68.Eurostat (1985) *Basic Statistics of the European Community*: 120, 146.

69.See "Denmark: The Smug Debtor" (1988) *The Economist*. September 3: 74-76.

70.See Klaus Nielsen and Ove K. Pedersen (1988) "The Negotiated Economy: Ideal and History." *Scandinavian Political Studies*: 79-101.

71.European Trade Union Institute (1987) *op.cit.*: 46-47; and "Denmark: The Smug Debtor" (1987) *op.cit.*: 75.

72.European Trade Union Institute (1987) *op.cit.*: 49.

73.Two major strikes in Denmark, one in 1973 and the other in 1985, were notable.

74.Interview with Henrik Fugmann, Head of Section, Ministry of Economy, Copenhagen, 9 September 1988.

75.See IMEDE and World Economic Forum (1989) *op.cit.*: 183 (Table 10.09 in the report.) Switzerland ranked number one, Ireland number fourteen, and Sweden number eleven.

76.Interview with Henrik Bjerre-Nielsen, Head of Section, Economics Department, LO, Copenhagen, 14 September 1988.

77.Boje (1986): 171-178.

78.European Trade Union Institute (1987): 14.

79.Interview with Nielsen and Pedersen, 13 September 1988.

80.Jens Chr. Tonboe (1986) "On the Political Importance of Space: The Socio-Spatial Relations of Trade Unions, Gender, and the Decentralized Danish Welfare State." *Acta Sociologica*: 21-22.

81.Interview with Ole Jess Olsen, Institute of Economics and Planning, Roskilde University, Roskilde, 9 September 1988.

82.Interview with Henrik Bjerre-Nielsen, 14 September 1988.

83."Denmark - Country Update" (1989) *Corporate Location Europe*. (March-April): 58.

84.Gosta Rehn (1985) "Swedish Active Labor Market Policy: Retrospect and Prospect." *Industrial Relations*: 62-79.

85.Nonetheless, there were unanticipated results from the plan. There was a backlash of centralization, as evidenced by the increased support of the Farmer's Party. There were also increases in personal distress factors, such as violent crimes, alcoholism, and drug abuse. And finally, the LO began to lose members, while the TCO, the white-collar union, gained members. See Rehn (1984) *op.cit.*: 151-154. Also, see interview with Villy Bergstrom, Director, Trade Union Institute for Economic Research, Stockholm, 9 September 1987.

86.This model served as the basis for the Solidaristic Wage Policy that is still in effect. Interview with Gosta Rehn, Stockholm University, 9 September 1987.

87.Ira C. Magaziner and Mark Patinkin (1989) *The Silent War: Inside the Global Business Battles Shaping America's Future*: 154.

88.See Swenson (1989) *op.cit.*: 111-176.

89.There was also another benefit to worker mobility: having maintained a "geographically mobile reserve army of labour," wage acceleration in specific areas of the country would be avoided.

90.See Anders Bjorklund (1986) *Policies for Labor Market Adjustment*: 7-14.

91.Interview with Eskil Wadensjo, Director, Industrial Institute for Economic and Social Research, Stockholm University, Stockholm, 9 September 1987.

92.Kjell Sehlstedt and Lena Schroder (1987) *Local Job Creation Programs for Youth in Sweden*: 13.

93.See Rehn (1984) *op.cit.*: 149.

94.See Turner (1987) *op.cit.*: 81-82.

95.Interview with Dr. Philippe Saurer, Ministry for Economic Policy, Berne, 16 November 1987.

96.European Free Trade Association and European Community (1986) *Government Aids to Industry In Switzerland*: 3.

97.Interview with Roger Piccand, Ministry of Industry, Small and Medium-Sized Enterprises, and Work, Berne, 17 November 1987.

98.Ralph Segalman (1986) "Welfare and Dependency in Switzerland." *The Public Interest*: 107-108.

99.Ibid: 116.

100.Interview Piccand, 16 November 1987.

101.Interview with Saurer, 16 November 1987.

102.Interview with Piccand, 16 November 1987.

103.Ibid.

104.See Volker Kind (1987) "Human Resources - A Shortage in Switzerland." Keynote Address by the Deputy Director, Federal Office for Industry and Labour at the IIR Conference on Employment Strategies.

105.Interview with Piccand, *op.cit.*, 16 November 1987.

106.Segalman (1986) *op.cit.*: 108.

107.See Danthine and Lambelet (1987) *op.cit.*: 162-167.

108.Katzenstein (1984) *op.cit.*: 128.

109.Irish Department of Finance (1988) *op.cit.*: 49.

110.Irish Confederation of Trade Unions (1984) *Confronting the Jobs Crisis*: 2.

111.Dennis Conniffe and Kieran A Kennedy (1984) *Employment and Unemployment Policy for Ireland*: 249.

112.Interview with John McGrath, Policy and Planning Unit, FAS (Training and Employment Authority), Dublin, 21 February 1989.

113.Conniffe and Kennedy (1984) *op.cit.*: 249.

114.See Department of Social Welfare (1988) *Social Welfare Services Guide*: 38-40.

115.Interview with McGrath, 21 February 1989.

116.According to a *World Competitiveness Report* survey (Table 8.41), Ireland ranked first and Switzerland next to last in terms of immigration laws that are favourable to competitiveness. See IMEDE and World Economc Forum (1989) *op.cit.*: 159.

117.John Sheehan (1987) "Investment in People." *Irish Banking Review*: 52.

118.J.J. Sexton (1987) "Recent Changes in the Irish Population and in the Pattern of Emigration." *Irish Banking Review*: 36, 41.

119.Tables 5.26 and 5.19 respectively in the report. See IMEDE and World Economic Forum (1989) *op.cit.*: 118, 116, 115. (Tables 5.26, 5.21, 5.22, 5.19)

120.Eurostat (1985) *op.cit.*: 120, 146.

121.See Thomas P. Boje (1986) "Segmentation and Mobility: An Analysis of Labour Market Flows on the Danish Labour Market." *Acta Sociologica*: 176.

122.According to the *World Competitiveness Report* (Table 5.16), Denmark ranked nineteen out of twenty-two OECD countries that suffered from long duration unemployment. See IMEDE and World Economic Forum (1989) *op.cit.*: 114.

123.Det Okonomiske Rad (1988) *Dansk Okonomi*. (June): 145.

124.Interview with Jorgen Sondergaard, Council of Economic Advisers (Denmark), Copenhagen, 13 September 1988.

125.Interview with Bjerre-Nielsen, 14 September 1989.

126.See Klaus Nielsen and Ove K. Pedersen (1988) "Structural Policy: A Danish Strategy for Flexibilization." Paper presented at the conference "Strategies for Flexibilization:" 54, 56.

127.Interview with Klaus Nielsen and Ove K. Pedersen, Institute for Economics and Planning, Roskilde University, Roskilde, 13 September 1988.

128.Rehn (1978) *Towards A Society of Free Choice*: 124.

129.Interview with Sondergaard, 13 September 1988.

130."Wage Strikes Threaten in Denmark." (1989) *Financial Times*. February 9: 3.

Chapter Five
State-Industry Relations and Industrial Policy-Making

5.1 The Relationship Between the State and Industry: The Formation of Industrial Policies

This chapter will examine industrial policies, which are developed and implemented through State-industry interaction and intended to change the composition and/or location of industrial output.[1] Students of industrial policy have primarily examined large states such as France and Japan, where the use of credit mechanisms, targeting, public procurement, and research and development policy have been "aimed directly to affect the structure of industry"[2] and the decisions of enterprises. Yet as Katzenstein explains, "In all industrial states, be they small or large, one can find a substantial array of policies seeking to modify market conditions through such instruments as subsidies, tax policies, regional development, concentration, and national development."[3]

Because forms of State intervention differed throughout the 1980s among small European states depending upon their economic development, economic performance, and changes in political circumstances (to name but three factors), industrial policy weapons varied both in name and form from state to state. As was identified in the first chapter, nearly all macroeconomic and microeconomic policies explicitly or implicitly influenced the structure of industry in the small European state.[4] In the two previous chapters it was illustrated that labour market policies and monetary policies were necessary forms of State intervention to act in concert with labour-industry and financial institution-industry relations. This chapter will be concerned with various measures by the State to influence the investment decisions of enterprises in the 1980s, covering "not only the creation, expansion, and re-equipment of production capacity, but decisions about research and development facilities and product development."[5] Consequently, significant attention will be directed not only to such standard analyses of industrial policy as nationalisation of industry and direct sectoral subsidisation, but also such policy avenues as production subsidies, mainly in the form of R & D capital transfers.

Throughout the decade one of the most meaningful ways in which small state industries could remain competitive in world markets, despite being highly vulnerable international price takers, was through technological sophistication.[6] As a consequence of actor proximity in the small European state, national "systems of innovation"[7] involving interaction between key actors (such as the State, research institutions, and industry) could produce a competitive advantage. Yet during the 1980s, while the small European state had the advantage of actor proximity in developing this interaction, varying degrees of technological innovation influenced the industrial success of these states as a result of "idiosyncratic technological capabilities."[8] Much of the reason for these differences in the level of technological competitiveness depended upon the role of the State in supporting R & D projects and the state's industrial structure.[9]

Both Sweden and Switzerland maintained high levels of technological sophistication, while Ireland was significantly less successful in promoting research and development. In Denmark, policy-makers recognised their industries' technological deficiencies and developed policies to modernise their industrial structure. According to the *World Competitiveness Report*, in 1986 Sweden and Switzerland ranked first and second, respectively, among twenty-two OECD countries in terms of total expenditure on R & D as a percentage of GDP, while Denmark and Ireland ranked sixteenth and eighteenth.[10]

While it is nearly impossible to provide an exhaustive listing of industrial policy measures, this chapter will target the most meaningful industrial policy instruments according to how each of the four small European states introduced and developed state-specific industrial policies. Analysis of industrial policy-making in these states is grouped into two categories:

1) defensive measures, notably direct sectoral subsidisation and nationalisation of industry; and

2) policies that attempted to stimulate the state's industrial competitiveness through R & D measures, regional development, credit provisions, taxation incentives, export promotion, and FDI promotion.

The key points of discussion within this chapter are summarised in the chart on the following page. (See Figure 5.1.)

Figure 5.1

STATE - INDUSTRY RELATIONS AND INDUSTRIAL POLICY-MAKING: THE CASE STUDIES COMPARED

	DENMARK	IRELAND	SWEDEN	SWITZERLAND
Degree that indigenous industry remained nationalized during the 1980s	Almost none	A large number of enterprises	A few enterprises	Almost none
Direct defensive sectoral subsidation in the 1980s	Extensive subsidies almost exclusively to the shipbuilding Industry	Some, primarily to nationalised enterprises	Extensive shipbuilding subsidies prior to 1982; thereafter no subsidies to shipbuilding and limited use to other sectors	Negligible
Level of research and development funding (for industrial development) in the 1980s	Low until mid-1980s, then moderate	Low	Very high	Very high
Research and development funding orientation	Derived primarily from the public sector	Derived primarily from foreign subsidiaries, though relatively unsuccessfully	Derived from both the public and private sectors	Derived primarily from the private sector
Attitude towards inward foreign direct investment in the 1980s	Not actively sought or prevented	Actively sought	Actively prevented	Actively prevented
Overall industrial policy focus during the 1980s	"Persistently liberal" approach until mid-1980s, then focus on technology policy	Focus on attracting foreign MNCs into Ireland to boost employment and induce technology transfer	Focus on R & D and other measures to stimulate growth/ renewal	Some limited measures, such as export promotion and export credit guarantees
Power of ministry (or other authority) dealing with industrial policy matters (in comparison to other state ministries)	Minimal until mid-1980s, somewhat stronger thereafter (Ministry of Industry)	Very strong (Department of Industry and Commerce, IDA)	Moderate (Ministry of Industry)	No such authority In Switzerland
Nature of relationship between the state's industrial policy authority and industry	State's role was minimal before mid-1980s, thereafter close ties to foster industrial modernisation; increasingly close relationship	State actively pursues projects for industrial development; very close relationship	State acts to support environment necessary for large MNCs to prosper; moderately close relationship	State's role is minimal in industrial development; distant relationship
Cooperative or detached state-industry relations	Detached before mid-1980s, then relatively cooperative	Cooperative	Cooperative	Relatively detached

5.2 Industrial Policy-making in the Four Small European States: From the 1970s to the 1980s

During the 1980s the role of the State in developing industrial policies depended to a significant degree upon both national priorities (e.g., economic performance and level of economic development) and societal values (e.g., attitudes towards the role of the State) in the small European state.[11] As a consequence, among the four case studies particular industrial policies were developed and implemented to varying degrees, policies that directly influenced the composition and location of industrial output.

Because of its relatively poor infrastructure and semi-peripheral location, the Irish economy developed slowly in comparison to the three other case studies. Because of these two factors coupled with its relatively modern formation[12] (and hence "late industrialisation"[13]) and the lack of defence initiatives that would spur strategic sectors[14], Ireland became a state with an extremely weak indigenous industrial structure. For the most part the State had historically taken an actively interventionist role through subsidisation of its large State commercial enterprise sector and initiatives to attract inward FDI.

Throughout the 1970s and 1980s, because unemployment remained endemically high, the State attempted to use direct industrial policy measures as a means of spurring employment. Membership in the EC adversely affected a number of Irish companies because of increased competition, and this had obvious detrimental effects on employment in Ireland. Consequently, the State imposed measures to induce foreign-owned companies to locate their factories and plants on Irish soil. The hopeful expectation was that technology from these foreign sources would spin off to Irish indigenous industry, yet with the international recession ushering in the 1980s, and unemployment surpassing twenty percent, employment (not value-added) was the sole criterion for industrial policy success. On both measures, however, during the first half of the 1980s the State was relatively unsuccessful. Different from countries with large industrial sectors involved in such sunset industries as steel and shipbuilding, Ireland's problem was even more fundamental - it had yet to cultivate an industrial structure that was not dependent on highly mobile foreign industry, and its major export sector, agriculture, was dependent on EC and Irish State subsidisation.

By the mid-1980s, the State's industrial policy champion, the Industrial Development Authority of Ireland (IDA), initiated further steps to induce foreign-owned MNCs to locate in Ireland. Yet having learned from many of its failures from the past, it attempted to augment the state's indigenous industrial structure, which became the principal industrial policy focus. While certainly the revamped industrial policy was "an organic evolution from its predecessors,"[15] the emphasis away from employment creation to industrial value-added (i.e., wealth) creation was a positive step towards the restructuring of the Irish indigenous industrial structure.

In Denmark, despite a number of international economic pressures, from the 1970s through the 1980s the lines between social and economic policy remained clearly delineated. The State attempted to tackle its cross-current demands, ranging from its giant welfare state commitment to maintaining a high standard of living (evidenced by the borrowing for personal consumption). As inflation, unemployment, a current account deficit, and foreign debt sapped the economic vitality of the Danish economy into the 1980s, the Danish State had relatively few ideas as to how to increase productivity. Policy-makers were unclear as to what role the state should play in terms of industrial development, though they were certain that "some action needed to be taken."[16]

More out of practice than reason, Denmark chose its "persistently liberal"[17] path of limited intervention without attempting to respond flexibly to changing external conditions. As Niels Chr. Sidenius contended (in 1983),

> Ever since the beginning of industrial policy in Denmark in the 1920s, the policy-making process has been characterised more by consensus than conflict, more by continuity than by ruptures .... the result of this has been an emerging and persisting dominance of a liberalistic paradigm.[18]

By the beginning of the 1980s and under extreme economic pressures, Danish fiscal policy remained clearly oriented towards the demand side, while the supply side was neglected. With the increasing vulnerability of its economy, Denmark's international competitiveness waned.

Yet, as will be discussed later in this chapter, the State initiated steps to "modernise"[19] its industrial structure through revamped industrial policy objectives, primarily by introducing a programme designed to augment its relatively weak and technologically deficient industrial structure. Due to these adverse domestic economic conditions, by the mid-1980s "direct interplay," notably between the Federation of Danish Industries (*Industrirardet*), the Ministry of Finance, and the Ministry of Industry, "changed the aims and the instruments of Danish industrial policy."[20]

In Sweden, welfare and egalitarianism remained central precepts to the Swedish model of communitarianism. Nevertheless, policy-makers, industrialists, trade unionists, and scholars in the state agreed that the most effective way to promote industrial progress was through the free market. Sweden typified the mixed economy, where the State provided significant egalitarian social benefits while maintaining a relatively non-interventionist outlook for industry.[21]

However, the *bourgeois interregnum* (1976-1982), when the centre parties governed Sweden, was marked by a massive bail-out policy in a situation that can only be described as paradoxical given the liberal record of the bourgeois centre-right parties. States Heclo and Madsen,

> ...the new bourgeois coalition government elected in 1976 maintained the overall design of its predecessor's economic policy. While awaiting the recovery in the international business cycle, the non-socialist coalition accelerated industrial subsidies, other government spending, and deficits.[22]

From 1976 to 1982, the Swedish State helped its indigenous industry "weather the storm" until there was a suitable international economic climate.[23] While subsidisation measures exacerbated wage and budget deficit problems, the new Swedish SAP government of 1982 would be operating on a relatively clean slate. Sunset industries would no longer be the backbone of Sweden's industrial base and measures to "renew"[24] its industrial structure through such measures as R & D policies became Sweden's primary industrial policy objective.

The combination of high levels of economic development and societal disdain for direct governmental intervention curtailed the role of industrial policy-making in Switzerland. Throughout the 1980s Swiss industrial success was achieved through a highly progressive interactive process in which the State's role remained subordinate to that of industry and financial institutions. Even with the international economic pressures of the 1970s and 1980s, the State almost never forged industrial policies (with the one major exception of the watch industry bailout in the 1970s) mainly because it lacked control over investment capital, which is essential to meaningful State intervention.

Consequently, by the mid-1980s under positive economic conditions State policies had little direct impact on firm strategies; industrial rebuilding as a result of economic crisis in Switzerland was accomplished through private enterprise, not the State.[25] Switzerland's industrial policy was relatively modest, with some regional policies, export credits, and export promotion policies. According to *The World Competitiveness Report*, Switzerland ranked first among twenty-two OECD countries in terms of the lack of involvement by the State in influencing industry.[26]

5.3 Defensive Sectoral Subsidisation and Nationalisation

A. Ireland

Certainly the state with the largest public enterprise sector of the four case studies during the 1980s was Ireland. Illustrative of this is the fact that six of the top ten employers in 1985 were State-sponsored public enterprises that were not part of the civil service yet belonged to the public sector of the economy. (See Figure 5.2.) James D. O'Donnell defines them as "permanent, autonomous, public bodies whose staff is not drawn from the civil service, but to whose board or council the government or ministers in the government appoint directors or council members."[27]

The commercial semi-State sector consisted of numerous companies involved in energy (ESB, *Bord na Mona*, *Bord Gais*, INPC), industry (NET, Irish Steel, *Ceimici*, *Siucre Eireann*), transport (*Aer Lingus*, *Aer Rianta*, B + I, CIE), banking and insurance (Industrial Credit, Agricultural Credit, Irish Life), communications (*Bord Telecom*, An Post, RTE), and other miscellaneous enterprises (National Stud, Arramara, OIE). For the most part, these enterprises within the State commercial sector remained a vital source of employment in a country whose unemployment remained around twenty percent. The total number of employees in public enterprises in 1986 was nearly eighty thousand, and total turnover was 3,925 million Ir.Pd..[28]

Figure 5.2
Top Ten Employers in Ireland, 1985
(By Numbers Employed)

Company	Numbers Employed
Telecom Eireann*	17,260
CIE*	15,000
ESB*	12,454
Smurfit Group	12,000
An Post*	8,871
Roadstone	6,935
Waterford Glass	6,407
Aer Lingus*	5,900
Bord na Mona*	5,850
Guinness Irl.	4,700

*Public enterprise

Source: ICTU (1986) *Public Enterprise: Everybody's Business*: 7.

A survey of the Ministry of Industry and Commerce's budget between 1983 and 1987, excluding capital expenditure on the promotion of industrial development for the IDA, the Shannon Free Airport Development Co., the National Development Corp., and *Udaras na Gaeltachta*, shows around forty percent of the Ministry's budget was for the provision of assistance to its semi-State enterprises. Yet this figure discounts the particular sectoral aid which State agencies like the IDA provided to State commercial enterprises.[29]

Nonetheless, the performance of these State enterprises was relatively poor, not only because many enterprises' operations were in relatively declining industries, but also because of poor management. The trading results and financial positions of the State enterprise sector illustrate the sector's relatively poor performance: in 1987 industrial bodies in the commercial semi-State sector posted a seven percent net loss as a percentage of sales with net liabilities at twenty-eight million Ir.Pd.[30] Examples of floundering State enterprises included *Siucre Eireann*, one of Ireland's fifty largest enterprises, which was forced to close its troubled Thurles Plant, ultimately threatening the company's solvency. Ireland's semi-State airline, *Aer Lingus,* and the airport authority, *Aer Rianta*, were plagued by poor management and competitive conditions within the European market that resulted in poor company performance.[31]

The capital support for these industries was provided directly by the Ministry of Industry and Commerce, yet the IDA and *Foir Teoranta* were primarily responsible for the "industrial rescue"[32] of these as well as private enterprises. Throughout the 1980s the IDA and *Foir Teoranta* provided between eighty-five and ninety-two percent of their grants for building and other fixed assets directly to industries, while marketing and R & D project grants were less than ten percent combined.[33] Indeed, the IDA was the primary organisation involved in providing direct sectoral and enterprise subsidisation. (See Figure 5.3.)

Most important, significant subsidisation was provided for Ireland's vital agricultural sector, both by the State and by the EC under the CAP. Between 1980 and 1987, an average of eighty-four million Ir.Pd. was granted by the Ministry of Agriculture for sectoral economic investment.[34] Under the CAP's FEOGA grant scheme, the average grant was around ten times the amount the Irish State provided.[35] In 1987, FEOGA receipts surpassed Ireland's total contribution to the budget by over 625 million Irish pounds. As Sheehy explains, "...allowing for the multiplier effect on both FEOGA and trade gains, the Irish economy in 1987 would probably have been between ten and fifteen percent smaller in the absence of the CAP.[36]

Figure 5.3
IDA Fixed Asset Payments to Industry, 1983-1986
(Total & % of Total Payments to Industry by the Irish State)

	Million Irish Pounds	IDA %*
1983	120,757	60
1984	114,116	57
1985	114,055	53
1986	101,571	54

* Percent of total fixed asset payments by IDA to industry

Source: Department of Industry and Commerce (1986) *Review of Industrial Performance*: 85.

In sum, because of Ireland's weak private indigenous industrial structure, the State continued to provide significant sectoral subsidisation to its relatively numerous semi-State enterprises as well as to private companies. Agriculture, its most important sector, accounting for around forty percent of indigenous industry exports and nearly twenty percent of employment throughout the 1980s, was heavily subsidised by both the the CAP and the Irish State.

B. Denmark

Throughout the 1970s and 1980s the steel industry, the agro-industrial complex, and the shipbuilding industry encountered problems of increased international surplus capacity, and as a result the Danish government initiated defensive programmes primarily through sectorally specific subsidisation. While the State did impose limited nationalisation of particular steelworks[37] and iron ore mines, the steel industry received defensive subsidies throughout the 1980s. As Ole Jess Olsen stated in an interview, "The Danish government has not been eager to nationalise its industries; the steel example is a special case with only particular examples of nationalisation."[38] Furthermore, a Ministry of Industry publication stated that, "There are no state-owned enterprises and no tradition for offering public assistance to individual enterprises in difficulties."[39]

Nonetheless, with agriculture's share of employment and net value of production in Denmark around twenty percent during the 1980s, Denmark remained Europe's largest producer and exporter of farm produce, notably animal products, relative to its population. Denmark's giant agriculture sector furnished the most significant amount of foreign exchange for trade and industrial capital in order to import industrial raw materials and manufactured goods, and as a result "occupied a strategic position" in the Danish economy.[40] Consequently, in 1987 the agricultural sector received State subsidies that totalled thirty-six percent of the value added of the entire sector, and 62,334 D.Kr. were allotted by the State per employee. Comparably, the most subsidised sector, shipbuilding, received seventy percent of its value added in subsidies, and 252,472 D.Kr. were allotted per employee.[41] Of course the agricultural subsidy was coupled with the relatively large contribution by the EC's CAP. By the latter part of the 1980s the curbs on farm production imposed by the EC provoked the Danish government to provide more than one billion D.Kr. of State aid to the agricultural sector.[42]

Ironically, while the Danish State continued to subsidise the shipbuilding industry, documents produced by the Budget Office professed that "crisis" support was virtually nil between 1970 and 1983.[43] In another document by the Ministry of Industry, a primary table indicates that between 1982 and 1984 the State did not give any "aid to enterprises in difficulties," despite the fact that "sectoral measures" listed above referred specifically to targeted steel and shipbuilding subsidies.[44] Indeed, there is much evidence to support Europe's and Denmark's declining share of shipbuilding in the world. For example, while in 1950 West European countries maintained nearly eighty percent of the world market share in merchant shipbuilding (with Denmark having around four percent of the world total), in 1980 West Europe had just over twenty percent of the world market and Denmark only two percent.[45]

Despite the contraction of the shipbuilding industry in Europe, Denmark continued to subsidise its ailing shipbuilding industry throughout the 1970s and 1980s. In sharp contrast to Sweden, whose policy-makers realised that its shipbuilding industry would never be able to recover from significant world competition (and hence closed most of its shipyards by the mid-1980s), the Danish State continued to provide direct industrial subsidies to its ailing shipbuilding industry, mainly through export credits and leasing incentives.[46]

With the shipbuilding industry in stagnation, the government offered individual tax incentives to encourage ship leasing, and with the Danish marginal personal income tax being extremely high, the leasing of ships by groups of Danish citizens became a popular vehicle for individuals' tax deductions. As a result, the shipbuilding misfortune became the private investor's advantage; "Money put into a notoriously non-profitable industry which had been backed by the taxpayer for so long, suddenly, in effect, generated profits which were not ploughed back into productive investment."[47]

With shipbuilding being a "nationally-identifiable industry,"[48] yet one that was experiencing degeneration, throughout the 1970s and 1980s the subsidy scheme fluctuated with the electoral process; policy-making regarding the shipbuilding industry never gained coherence or direction and remained in a "slow-down - speed-up" position.[49] (See Figure 5.4.)

Figure 5.4
Shipbuilding Subsidies in Denmark, 1981-1988

Year	Million Krona	% of Industry Ministry Budget
1981	1,457	49.1
1982	1,706	50.0
1983	1,163	47.1
1984	752	35.2
1985	362	22.0
1986	171	61.6
1987	385	57.8
1988	2,200	59.4

Source: Ministry of Industry (1988), Ministry of Finance (1988) *Redegorelse Om Den Offentlige Sektor, 1988*: 178.

C. Sweden

As the world economy experienced the oil shocks and an international recession during the *bourgeois interregnum* (1976-1982) direct State intervention began to implant itself firmly in a defensive mode. What were once Sweden's strongest industries, such as shipbuilding, mining, and forest products, needed help from the government in order to survive. As a consequence, the bourgeois interregnum was marked by a massive bail-out policy in a situation that can only be described as paradoxical given the non-interventionist manifestos of the centre-right parties in the years preceding their control of government.

While awaiting the recovery of the international economic environment, the governing coalition "accelerated industrial subsidies, other government spending, and deficits."[50] (See Figure 5.5.)

Figure 5.5
Sectoral Distribution of State Aid to Industry, Sweden, F.R.G., France and U.K., 1970-1977

Declining Sectors	Sweden	F.R.G.	France	U.K.
Coal Mining	-	12%	17%	10%
Shipbuilding	51%	5	7	9
Steel	9	-	7	14
Textiles/Apparel	2	3	-	1
Forest Products	6	5	-	1
Others	5	2	-	2
Subtotal	73%	27%	32%	27%
Growth Sectors				
Nuclear Power	2%	14%	14%	5%
Aerospace	10	10	17	27
Electronics/ Computers	3	10	27	27
Mech. Engin./Autos	8	20	6	9
Chemicals	2	8	4	4
Subtotal	25	68	66	61
Others	2	5	2	2
	100%	100%	100%	100%

Source: Boston Consulting Group (1979) *Framework for Swedish Industrial Policy*: Exhibit 31.

Most notably, by the mid-1970s its large shipbuilding industry was financially strapped; the State bailed out the ailing companies in a nationalisation effort (e.g. through *Swedyards*) that did not subsequently help the wounded industry.[51] Measures of support by the Swedish State to its shipbuilding industry were more directly interventionist as a result of nationalisation efforts and direct production subsidies than the home credit and export credit subsidies used by the Danish State during the same period.[52]

The forest products and steel industries were other examples of the bourgeois government's nationalisation efforts. In the forest products case, the government bailed out the two major forest-products companies that remained more structurally vulnerable than the other forest products firms (given their lack of ownership of forests and power plants). In a similar vein, the steel industry faced a dire economic crisis of overcapacity during the same period, and though subsidy loans and loan guarantees were offered to ailing companies such as Uddeholdm Corp., there was a significant downturn in the industry. Again, the government acted by (a) supporting the proposed merger of the three largest companies, (b) proposing an industry effort to specialise in order to adjust to changing competitive forces, and (c) offer 1.2 billion S.Kr. to form the Swedish Steel, Ltd. (the merger of the three companies under a national parent).

In sum, the policies of the bourgeois parties continued and extended those of the pre-bourgeois years. (See Figure 5.6.) As Pontusson asserts,

> All told, the bourgeois parties nationalized more industry during their first three years in power than the Social Democrats had done in the previous forty-four years![53]

After 1982 industrial subsidies were severely cut, and Swedish industrial policy-making significantly changed course away from defensive sectoral subsidisation. Evidence of this is found in the Swedish steel sector, where employment in the steel industry by the end of the 1980s was one-half that ten years earlier.

Figure 5.6
Industrial Policy Expenditures in Sweden Disaggregated by Type of Policy Measure, 1970-1980 Fiscal Year
(In Billion S.Kr. at 1980 Prices)

Year	A	B	C	D	E	F
70/71	0.8	1.6	1.4	0.4	1.0	0.3
71/72	1.1	1.6	1.4	0.4	1.4	3.9
72/73	0.8	1.5	1.1	0.5	2.3	0.5
73/74	1.2	2.0	1.0	0.5	1.2	0.5
74/75	1.5	1.8	1.5	1.2	1.9	0.9
75/76	1.1	2.0	1.9	1.2	2.1	1.9
76/77	1.1	2.4	1.4	1.3	2.2	5.1
77/78	1.1	2.5	2.6	1.4	2.2	5.0
78/79	0.8	3.1	1.5	1.4	1.1	8.8
79/80	1.1	2.7	1.3	2.1	1.6	8.1

A= regional aid, B= aid to small businesses, C= sectoral programmes, D= research and development support, E= export credits, F= extraordinary aid

Source: Jonas Pontusson (1986) *Labour Reforms and the Politics of Capital Formation in Sweden*: 559; SOU 1981: 53.

Moreover, by 1986 such major Swedish shipyards as Cityvarvet Arendal, Eriksberg, Kockums, Oresundsvarvet, and Uddevallavarvet, which in 1975 had employed over twenty-five thousand workers, were closed, under closure, or significantly decreased; what was once one of Sweden's most powerful industries barely existed by the end of the decade.

Those sunset industries that still existed in Sweden by the mid-1980s remained nationalised. The one notable exception of a non-sunset nationalised industy was Procordia, Sweden's successful tobacco, hotel, and restaurant conglomerate.[54] In total, the government operated seven public enterprises and a number of wholly or partly owned enterprises in which public sector operations amounted to 168 billion S.Kr. and employed 310,000 workers. Nonetheless, about 87% of Swedish industry was in private hands, with 8% government-owned and the rest held by cooperatives. Unlike other European left-of-centre parties, the SAP spared nationalisation efforts (...actually going towards greater privatisation) and moved towards a policy of growth and renewal. (See Figure 5.7.)

Figure 5.7
Key Data for Major State-Owned Swedish Companies, 1987

Name	Result (m.S.Kr)	Turnover	Employees
Procordia	389	12,788	25,499
Svenska Varv (Shipbuilding)	418	8,987	16,634
LKAB (Iron Mining)	121	5,453	4,752
SSAB (Steel)	-16	11,634	14,865
ASSI (Forest Industries)	21	6,202	7,688
NCB (Forest Industries)	9	2,792	3,848

Source: Ministry of Finance (1987) *The Swedish Budget, 1987/88*: 124.

D. Switzerland

While other European countries in the 1960s and early 1970s were adopting policies to expand employment by increasing governmental spending during periods of unfavourable economic conditions, Switzerland maintained a firm posture to preserve a limited interventionist position. Swiss policy-makers felt that the country's political stability coupled with its strong export orientation could sustain Swiss economic prosperity without significant direct aid to industry.[55] Certainly the trade balance was supported by an undervalued Swiss Franc, a significant influx of foreign workers, and union restraint.

The 1970s, however, witnessed an unusual overvaluation of the Swiss Franc that compelled adaptation by those sectors dependant on domestic production and export competitiveness.[56] The industries most affected were textiles and watches, and while the government practically avoided textiles industry assistance, the banks and government rescued the watch industry because of Switzerland's prestigious history of watchmaking. Omega Watches, for example, was "completely mismanaged,"[57] so the federal government approached the banks to aid the industry through a debt-handling, credit-offering programme. While the entire watch industry was supported by the State and the banks for a number of years, the industry has since rebounded with strong results. Moreover, the watch industry is the only example in modern Swiss history in which the State has acted directly to save an ailing industrial sector. One can witness the textiles example as a case-in-point in which Switzerland did not assist a declining industry; for the most part, the State relied more on market *Gesundschrumpfen* ("building up") than on State rescue operations.[58]

Since the mid-1960s the reduction of direct subsidies in Switzerland has been such that no outright governmental aid has been granted to any industrial firms or sectors.[59] Only the "embryonic" *Strukturpolitik*, which refers primarily to regional policy, comes close to any form of direct intervention. It is thus not surprising that some have termed Swiss industrial policy "passive."[60]

Furthermore, the State held virtually no industrial shares. The only important block of shares held by the government - ASUAG/SMH - (around six million Swiss Francs) was cut to ten percent in 1983 when the company was restructured.[61] In this instance the State acted as a "supervisory body" in which "they have nothing to do with an active industrial policy."[62] Direct subsidies to industry represent eight percent of the total, and they are designed not to "assign the total amount of a subsidy to units of output"[63] but as small-scale measures to promote industries that should become profitable without state aid in the near future.

5.4 Policies that Attempted to Stimulate the State's Industrial Competitiveness

A. Ireland

In Ireland the IDA had remained a permanent industrial policy fixture since the late 1940s, but its true influence did not develop until the 1960s, when it was determined that the IDA would help to induce inward FDI as well as develop small manufacturing businesses.[64] By the end of the 1970s the IDA had undertaken a strategy of developing "high flyers,"[65] industries with turnover of over twenty million Ir.Pd. These major multinational companies were being lured by the IDA through a number of enticements, the most prominent being fiscal incentives and capital grants.

Under IDA schemes a firm could expect a low tax on its manufacturing profits (only around ten percent[66]) and other advantages through leasing or special Section Eighty-Four loans (which are discussed in Chapter Three). Other incentives included non-repayable fixed asset grants that could be as high as sixty percent of total fixed asset expenditure, rent reductions, factory accommodation, training grants, and technology acquisition grants.[67] The IDA also stressed the highly trained Irish workforce and relatively large amount of unused land.

As a result of such actions, by the beginning of the 1980s a number of sunrise industries were operating in Ireland due to the significant influx of foreign multinationals. Over ninety percent of employment in the electronics industry and sixty-five percent of the chemicals industry was due to the presence of foreign companies operating on Irish soil.[68] By 1982, foreign MNCs accounted for nearly one-third of all manufacturing employment and seventy percent of manufactured exports.[69] (See Figure 5.8)

Figure 5.8
Manufacturing Employment in New Foreign Industry and the Rest of Industry in Ireland, 1960-1980 (Thousands)

	1960	1966	1973	1980
New foreign industry	3	10	36	61
Rest of Industry	169	188	186	182
Total	172	198	222	243

Source: Eion O'Malley (1985) "The Problem of Late Industrialisation and the Experience of the Republic of Ireland." *Cambridge Journal of Economics*: 145.

With external shocks ushering in the 1980s, Ireland struggled with poor economic performance: the debt-to-GNP ratio remained around three times the average of European Community nations,[70] unemployment was near twenty percent, and growth was sluggish. Ireland's industrial structure became dichotomised between strong economic performance by foreign subsidiaries in sunrise industries and sluggish performance by Ireland's indigenous enterprises.[71]

Nonetheless, Irish industrial policy continued on its course of inward FDI attraction through investment incentives, following a focus on creating the right environment. While foreign subsidiaries did employ Irish workers, this inward FDI was simply not enough to revitalise Ireland's sagging infrastructural difficulties and long-term unemployment problems. While the *Fine Gael* coalition began an austerity programme upon its election in 1982, little progress was made on Ireland's national debt, which doubled in a period of four years. Labour costs, as a manifestation of high inflation and high personal tax rates, also deterred Irish industry from becoming more internationally competitive. While many have claimed that Irish society has been marked by both ethnic and "confessional" homogeneity that "would appear to facilitate the development of a bargained consensual approach to economic policy,"[72] the beginning of the 1980s was marked by little agreement as to how policy-making could offset declining levels of international competitiveness.

By the mid-1980s the State began to examine the issue of industrial policy revitalisation, beginning with the Telesis Report of 1982. The report stated that while Ireland was able to induce foreign subsidiaries into the country, it was unable to develop its own indigenous industrial base because of lack of spin-off effects. It was recommended that there be "a more systematic programme for developing linkages between indigenous and foreign-owned firms."[73]

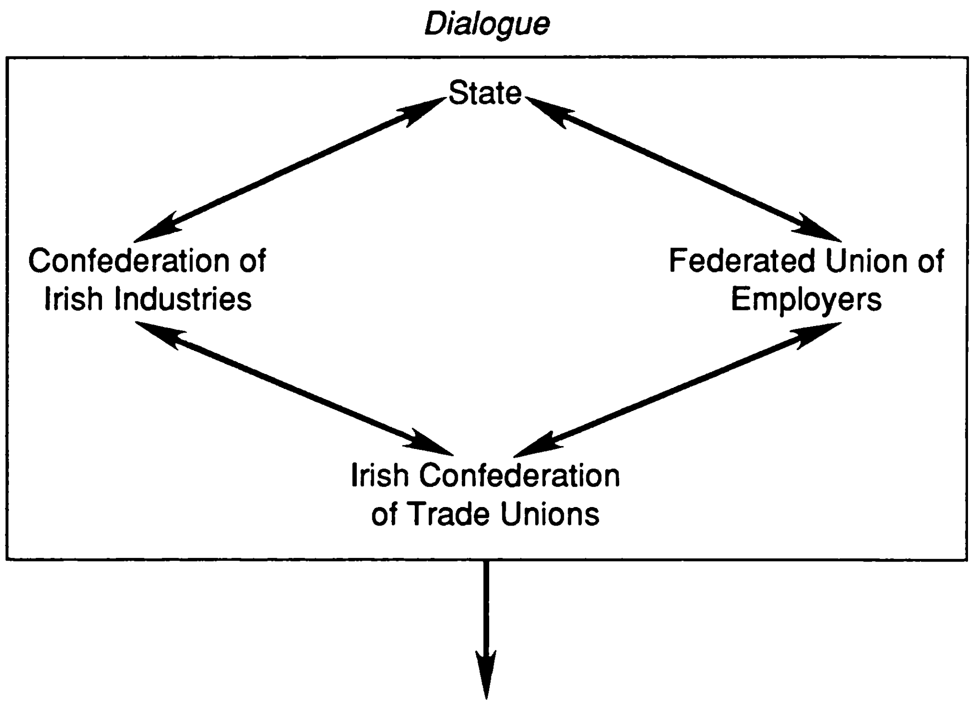
As a consequence of this report, as well as a subsequent report by the government entitled *A White Paper on Industrial Policy*, the new industrial policy focus was on strengthening Ireland's industrial structure, as opposed to previous efforts to control unemployment by virtual acceptance of any foreign MNC that could provide employment opportunities regardless of their impact on Ireland's industrial structure or long-term employment consequences. (See Figure 5.9.) As J.P. O'Carroll explains,

> The result was a major shift in industrialisation. Whereas previous policies emphasised the direct employment potential of industrial projects, their total impact on the economy would be the main consideration in the future.[74]

The industrial policy strategy the State pursued by the mid-1980s was based on the government's *White Paper*, which suggested a "'hands-on' approach by the State agencies...in a selective number of projects aimed at developing competencies within firms themselves."[75] The *Programme for National Recovery* of 1987, which was also designed to suppress wage growth, outlined industrial policy changes by focusing on programmes to develop specific Irish industries

Figure 5.9

THE ROLE OF THE STATE IN IRELAND, 1987: THE FORMATION OF *THE PROGRAMME FOR NATIONAL RECOVERY*



Policy Development: *Programme for National Recovery*

Industrial Policy Focus:	*Labour and Monetary Focus:*
• Strengthening of indigenous manufacturing sector • Technological development of indigenous manufacturing sector through expansion and growth of selected Irish companies • Emphasis on State aid to upgrade marketing, product development, R & D as opposed to support of fixed asset investment • Sector by sector development strategy • Continuation of State incentives for inward FDI	• Wage growth for 1988, 1989, 1990 set at 2.5% per year • Increased training grant expenditures to provide unemployment benefits and increase marketing, management, technological skills • Monetary policy to be determined by the "need to bring about the lowest possible interest rates. . . to promote investor confidence" • Lower level of inflation as a consequence of wage growth reduction

that would help modernise its weak, low tech indigenous industrial structure. As a result, the Ministry for Industry and Commerce began to work with the IDA "on a daily basis"[76] to stimulate particular high growth, sunrise industries such as electronics and pharmaceuticals. Both agencies began a strategy of creating "high flyers" as well as medium-sized enterprises (annual sales in excess of five million Ir.Pd.). The IDA became increasingly cognisant of attracting only those foreign subsidiaries that would add long-term benefits in line with this strategy and "provide guarantees" that factories would be more than simple assembly plants.[77]

At the same time, the State advocated close cooperation between the IDA, foreign firms operating in Ireland, and Irish indigenous industry. In particular, the IDA would oversee and administer prospective projects; indeed, the IDA under the supervision of only two directors in its history had maintained a philosophy based on the principle that "the only way to attract suitable foreign investment is if the IDA has the right people - the 'best and the brightest' if you will."[78]

Along with this sectoral strategy of attracting projects to augment its relatively weak industrial structure was an emphasis on export development and promotion and technology development.[79] A higher proportion of Ireland's GDP was placed in export promotion than in any other industrialised country.[80] (See Figure 5.10.)

Figure 5.10
Trade Promotion for Selected European States, 1986
(% State Budget)

Ireland	0.250%
Denmark	0.231
Sweden	0.093
Switzerland	0.011

Source: Verein Schweizerischer Maschinen-Industrieller (1987) "Bulletin: *ExportFoerderung Im Europaeischen Vergleich." (3 July)*: 2.

Perhaps most significant, Ireland suffered from relatively low levels of indigenous industrial technological development, not only because of the State's unwillingness and inability to pursue R & D projects as a result of its fiscal deficit problems, but also because of industries' size and orientation. The Irish industrial structure was composed of small- and medium-sized enterprises, and indigenous industry tended to be less technology driven than most other small European states.

Throughout the 1970s and most of the 1980s "technological development was overlooked" by both Irish industry and the Irish State.[81] While important economic actors such as the CII recognised the necessity for significant increases in R & D investment "with State support,"[82] they also appreciated that labour and other input costs needed to be reduced and that the government's fiscal budget deficit would hamper attempts to stimulate industrial innovation programmes. Reviews of industrial performance by the OECD[83] and the government's industrial

White Paper during the period illustrated the necessity for Irish industry to develop technology programmes, though in the latter case remarkably few recommendations were proposed.[84]

Ironically, throughout the 1980s Ireland maintained the highest share among EC countries of high tech products in its total exports, yet as McAleese explains, "This does not, of course, reflect any substantial strength in depth in these products."[85] The reasons for this paradox are that Irish indigenous industry maintained a relatively weak R & D capacity, and foreign multinationals lured by incentives to produce their products on Irish soil had few linkages with Irish industry. Consequently, while the IDA consciously attempted to attract high-value foreign manufacturing industry that could be applied for technological development of Irish industry,[86] R & D spin-off was not assured.[87]

At the same time, because Ireland's indigenous industries produced commodity and intermediate goods as opposed to capital goods, capital investment in R & D was risky for small and medium-sized enterprises; a cautious, low risk policy became necessary for indigenous industry.[88] At the same time, the State maintained a passive position, employing only minor R & D projects to "raise people's awareness" that technological development was a necessity in order for Irish industry to become more internationally competitive.[89] In 1985, fifty-three percent of gross public expenditure on industry was in the form of payments (or grants), of which only 6.1% was distributed to industry for

R & D purposes.[90]

Again, it was not until the Haughey Government in 1987 under the *Programme for National Recovery* that the State pursued an R & D policy, yet the administration of such programmes were not seriously funded or manned, nor were they earnestly organised to develop industrial technology. Perhaps most importantly, because of the budget deficit and high rate of foreign debt, R & D programmes received less funding and less personnel support than that given to other State programmes designed to change the composition of industrial output. In 1980 there was hardly any funding for technological development, and in 1987 only eight to nine million Ir.Pd. were secured for R & D. Also, in 1987 the Office of Science and Technology in the Department of Commerce and Industry maintained an executive staff of only five persons.

Other organisations devoted to technological development such as the Irish Science and Technology Agency (EOLAS) (until 1987 the National Board for Science and Technology) worked with universities; in addition, some informal contacts were made with industry, notably through the IDA for prospective projects from foreign firms.[91] Ireland did profit to a limited extent from several notable EC technology programmes. Such programmes as EPRIT (the most promising strategy for R & D in information technologies), EURONET (the first major European network for the long-distance transmission of computerised information), and TEDIS (a programme designed to promote the electronic transfer of data for commercial use) continued to gain increasing funding throughout the 1980s.[92]

In sum, Ireland's industrial policy objectives changed more in orientation than in actual funding. The majority of aid to industry was placed through two avenues: State commercial enterprises and the IDA. It should be noted, moreover, that Ireland faced a significant fiscal deficit and as a result placed its money almost equally between its sectoral (industry, agriculture, fisheries), productive (transport, roads, sanitation), and social (housing, education, hospitals) infrastructures. (See Figure 5.11)

Figure 5.11
Ireland's Public Capital Programme, 1980-1988
(% Volume Change)

Fisheries	-69%
Agriculture	-62
Industry	-45
Education	-34
Energy	-33
Housing	-29
Telecommunications	-21
Hospitals	-19
Government Construction, etc.	+97
Forestry	+55
Tourism	+43
Roads and Sanitary Services etc.	+41

Source: Ministry for Finance (1988) *Budget, 1988*: 140.

One of the more important means for industrial development in Ireland was through infrastructural development, which was firmly supported by the CII and consequently received significant attention from the State. Asserts Con Power, Director of Economic Policy for the CII, "The greatest single problem which still remains is the extraordinary high cost of inland freight transport, particularly road transport."[93]

Moreover, while the Irish State remained committed to developing its industrial structure, Irish technological development remained stagnant throughout the 1980s as a result of negative economic conditions coupled with an industrial structure unable to handle the investment requirements of technological development. At the same time, Ireland's hopes for technology transfer through inward FDI incentives managed by the IDA never came to fruition; foreign parent companies either avoided technology transfer or were working on a single stage of production (often component parts) which was unbefitting or unsuitable for replication by Irish industry. As a result, Irish indigenous industry was unable to absorb innovative productive techniques from foreign competition, and the Irish State, straddled with a budget deficit, could garner neither the funding nor the support from the business community to develop R & D programmes.

Nonetheless, Irish industrial policy became positively influenced through a coordinated understanding between the IDA, the Ministry of Commerce and Industry, and the CII. These three groups became convinced that Irish industrial policy needed to evolve into one based on the development of Ireland's indigenous industry much as a result of the pressures of the Single European Act. By 1987 the State initiated the most important steps to revitalise Irish industry by acting as the consensus maker in developing the *National Programme for Recovery*, which slowed wage-inspired inflation. At the same time, the IDA took on definitive supply-side measures to modernise its industrial structure; by the State working through these two positive goals, it was the Principal Actor in Ireland's quest for a higher level of international competitiveness.

B. Denmark

By the mid-1980s Denmark's industrial policy orientation was significantly modified to make technological competitiveness a major State priority. This action was taken to augment Denmark's relatively weak industrial structure. Unlike Sweden and Switzerland, Denmark had hardly any large, high technology oriented MNCs, nor did it have the ability to spin off high tech goods from a military sector; the problem was manifested by an impressively small proportion of high tech products being exported from the 1970s into the 1980s.[94]

Moreover, evidence provided from *The World Competitiveness Report* confirms that the role of the State in Denmark during much of the 1980s did not remain conducive to industrial growth. In fact, according to a survey within the report, Denmark ranked twenty-first out of twenty-two OECD countries in terms of "government economic priorities being directed towards investment and growth." Denmark also ranked eighteenth, twentieth, and twenty-second in three different surveys in terms of its fiscal policy orientation: (a) "favouring renewal of its infrastructure," (b) "stimulating investment," and (c) "encouraging entrepreneurial activity".[95]

Since the early 1960s the Danish industrial structure has been dominated by small- and medium-sized enterprises, with only a smattering of large corporations, all of which paled in size beside the major Swedish and Swiss corporations. Danish industrialists felt that by being small they could be flexible and adaptable to world market changes, and that there was no need for governmental policy to be adaptive when small enterprises "could act more quickly".[96] Throughout the 1980s Denmark's products were developed too slowly; the level of Danish FDI was significantly less than that in other small European states with similar levels of GDP per capita, such as Sweden and Switzerland, and exports were not as oriented towards high growth. For example, in 1985 total R & D personnel in Danish manufacturing industries totalled 8,659 persons, with the largest proportion being in the chemicals industry with 1,947 persons in 1985.[97] Two years earlier in Switzerland, there were 23,109 persons classified as R & D personnel, and in the chemicals industry, there were 7,695 R & D persons; in short, Swiss industry had nearly three times as many R & D personnel and virtually the same number of R & D persons working in the chemicals industry as all of Danish R & D personnel industry-wide.[98]

Without the same industrial structure impetus for technological innovation as in states such as Sweden and Switzerland, as well as the State's past disregard for R & D policy-making, Danish industry was technologically deficient.[99] (See Figure 5.12.) Hence, Danish small- and medium-sized enterprises relied to a significant extent on technology diffusion from other countries.[100]

Figure 5.12
A Comparison of Business R & D Intensity in Selected States 1985
(R & D Expenditure as Percent of GDP)

State	Business Enterprise R & D Expenditure (%)
Denmark	0.69
Ireland	0.41
Sweden	1.98
Switzerland	1.69
Belgium	1.12
Netherlands	1.18
Norway	1.01
Japan	1.88
United States	1.98
Germany	1.92

Source: OECD (1988) *Denmark: Reviews of National Science and Technology Policy*: 13.

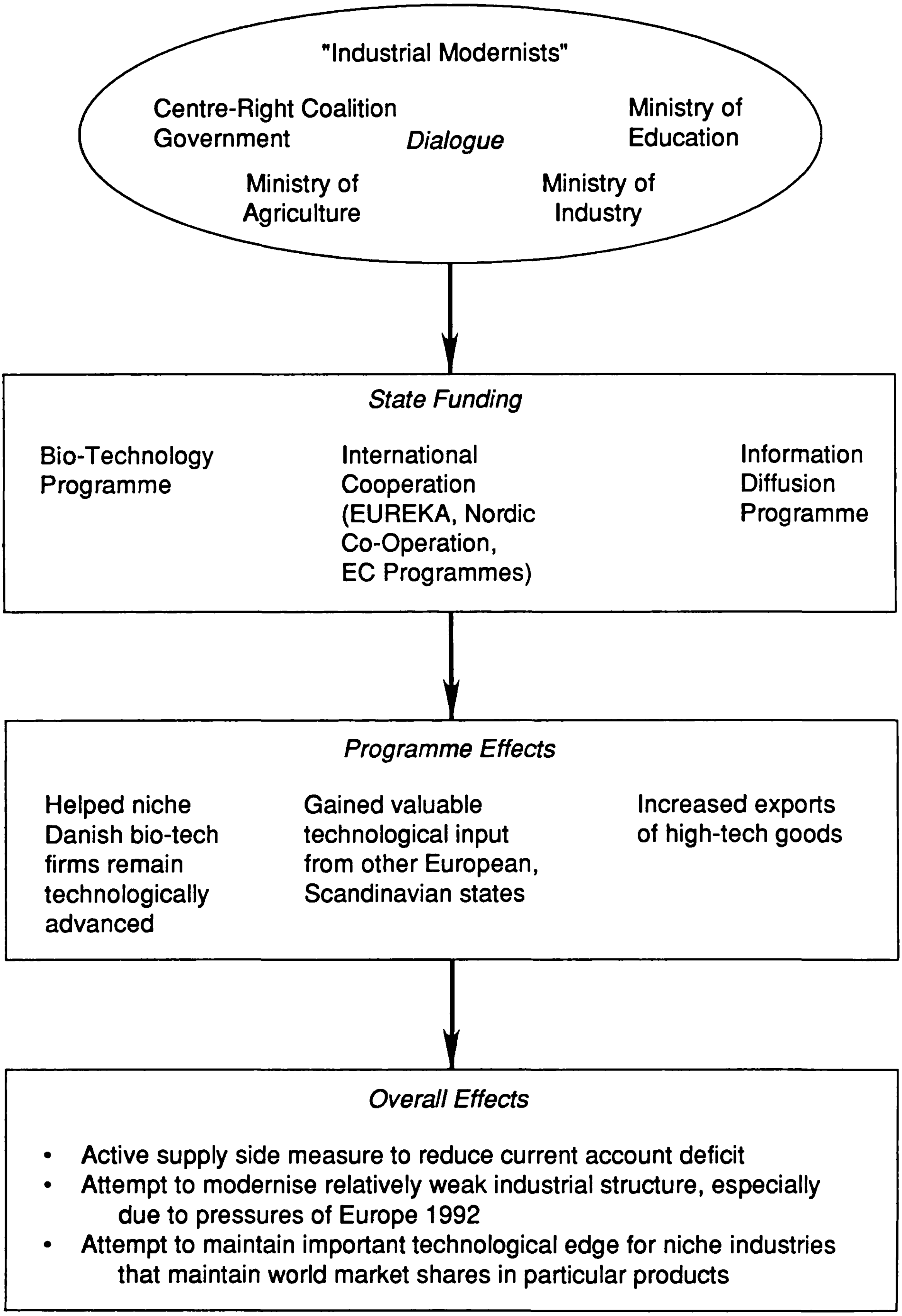
While Danish policy-making through much of the 1980s focused primarily on the supply side through such measures as the Potato Diet, Danish policy-makers began to realise that progress was necessary on the demand side. Danish policy-makers and industrialists had historically frowned upon industrial policy measures with the exception of aid for particular sectors, notably shipbuilding. Following the inception of the Ministry of Industry just three years earlier, in 1982 the minority coalition of the right developed as its main industrial policy ingredient a coordinated R & D programme, which was complemented by two other policy areas: regional development and export promotion. While regional development policy was not stressed throughout the 1980s, export promotion, primarily through grants that covered forty percent of projects, became an increasingly important industrial policy vehicle.[101] (<u>See Figure 5.10.</u>)

For the new centre-right coalition the main industrial policy component (its technology programme) was a relatively safe policy avenue "that did not stir societal anxiety about having an interventionist industrial policy...".[102] Nonetheless, while the various ministries and political parties discussed possible industrial policies, dialogue among a small number of industrialists and scientists, a group which Jan Annerstedt refers to as the "industrial modernists,"[103] was the primary impetus to the State's eventually developing technology policies. (<u>See Figure 5.13.</u>) In an interview he stated,

> The rhetoric after 1982 was about innovation, structure, and where procurement is coupled with technology push programmes. This was not done by the leftist parties, but by the Conservative party. Yet the Ministry of industry was in a stalemate until they were stimulated by the directors of companies to get a new direction. That was followed by eight to ten people who crystallised their ideas into technology policies.[104]

Figure 5.13

THE ROLE OF THE STATE IN DENMARK, 1982-1987: THE ADVENT OF TECHNOLOGY POLICY-MAKING



Following the industrial modernists' lead by realising that the Danish industrial structure was too small to yield effective technological results, the Danish State began to take on a principal role by elevating R & D as a "top priority policy area"[105] to restore the level of international competitiveness of Danish industry. (See Figure 5.14.) Nonetheless, until 1986 technology policy was not "guided by an overall plan" and there was "no significant saliency devoted to the analysis and planning of technology."[106]

Figure 5.14
State Support Schemes, Denmark 1982-1987
(As % and Million Danish Krona)

(%)	1981	1982	1983	1984	1985	1986	1987
A	14.2	15.0	21.6	26.3	40.9	58.1	52.7
B	5.1	5.9	4.2	6.1	6.6	0.7	0.6
C	6.3	6.3	9.3	12.8	17.3	18.7	17.5
D	20.6	19.0	12.4	14.2	3.8	0.0	0.0
E	49.1	50.0	46.8	34.6	22.0	11.6	19.7
F	4.7	3.8	5.7	6.0	9.4	10.9	9.5
	100.0	100.0	100.0	100.0	100.0	100.0	100.0

(Million Danish Kronor)							
A	422	516	537	571	673	859	1,032
B	152	201	104	133	109	10	12
C	186	215	231	277	285	277	343
D	612	649	307	308	21	0	0
E	1,457	1,706	1,163	752	362	171	385
F	138	128	143	131	29	162	185
	2,967	3,415	2,485	2,172	1,644	1,479	1,957

A= Technology Policies, B= Regional Policies, C= Export Promotion, D= Export Finance, E= Shipbuilding Subsidies, F= Other

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Source: Ministry of Industry (1988) "Subsidies and Structural Adjustment: The Danish Reply to Questionnaire IND(87)5:" *Tabel 5, Bilag 7.*

Yet in 1986 the government contended in its *Statement on Industrial Policy*:

> The jump in the technological development that is taking place these years means that even fairly large Danish enterprises are too small individually to be sufficiently offensive with regard to the development of technology. Therefore, the enterprises have to be encouraged to increase their efforts considerably as regards research and development.[107]

Much as a result of the *Industrirardet* objecting to direct sectoral intervention (e.g, "not promoting particular interests from member industries") yet favouring measures to adjust industry structurally through targeted R & D policies, consultation between the State and the *Industrirardet* eventually generated two technology programmes, one in information technology and the other in bio-technology.[108] Before 1986 the major technology programme was in information technology diffusion in which the State spent 1.5 bn. D.Kr. to spread existing technology throughout industry; indeed, this first technology programme was fostered by a significant degree of backing from the *Industrirardet*. Much as a consequence of Denmark's technological diffusion programme, particularly in electronics, engineering, and pharmaceutical products, it achieved a "remarkable" trade balance in high technology goods, in which its export/import ratio improved from 76.3% in 1970 to 97.0% in 1985.[109]

In addition, as a result of its significant agro-industrial sector, the State was interested in bio-technology innovation, despite the previous lack of cooperation among bio-tech firms in developing coordinated research programmes.[110] The Ministry of Education assumed much of the responsibility for bio-tech research, and due to the harmonisation efforts of the Ministries of Education, Agriculture, and Industry, the State appropriated five hundred million D.Kr. for a five year bio-tech programme that would establish twelve new centres for bio-technology research as well as arrange for joint public/ private programmes.[111] As a consequence, Denmark's *niche* high bio-technology firms such as NOVO, with major breakthroughs in enzymes,[112] and *Nordisk Gentrofte*, a world leader in insulin production, gained valuable public support from the State's bio-technology programme initiated in 1986.[113]

By 1987 the State had increased its commitments through its "Action Plan," adding an extra two hundred million D.Kr. to an R & D programme that totalled 1,420 million D.kr. for the years 1986-1990.[114] Not only were funds directed to information diffusion and bio-technological development, but funds were also directed to firm participation in international R & D programmes such as EUREKA, a scheme encompassing nineteen European countries to promote the technological development of non-military industrial activity.

In sum, the State became the principal actor in attempting to restore Denmark's level of international competitiveness. Although Denmark's current account deficit forced Danish fiscal policy to remain restrictive, a major policy priority of the Danish State after 1982 was to augment its level of industrial productivity through R & D programmes, which was a major change from its past policy preferences of sectoral-specific intervention. Although Denmark had the same (if not higher) standard of living of many of its European counterparts, its major competitive disadvantage was its industrial structure, which unlike those in Sweden and Switzerland, did not have the dual advantages of being both large and high tech oriented. Consequently the State acted as an impetus to modernise its industrial structure; the State understood the importance of technological innovation for its *niche* industries, encouraging them through technological policies to "increase their efforts considerably as regards research and development."[115] Having taken an active policy approach, by the end of the decade the State helped Danish industry achieve a strong trade balance in high technology goods through its diffusion programme and bolstered important technology funding for its agro-industrial *niche* enterprises. At the same time, it began a long-term supply-side strategy to defeat its enduring current account deficit, and the State actively attempted to formulate a modernisation programme to prepare Danish enterprises for increased competition in the European market driven by the Single European Act of 1992.

C. Sweden

Sweden's improved economic performance at the beginning of the decade was encouraged by the devaluations of 1981 and 1982, and at the same time Swedish industrial policy-making changed from the "money-oriented aid" (of the centre-right parties through sectoral subsidisation) to "service-oriented aid."[116] The emphasis of Swedish industrial policy shifted in the direction of regional development policies and programmes to "encourage industrial evolution by providing incentives for the diffusion of flexible manufacturing and other forms of advanced technology."[117] (See Figure 5.15.)

Figure 5.15
State Support to Swedish Industry, 1975/1976 - 1983/1984
(% According to Restructuring vs. Growth)[118]

		Restructuring/Reduction	Growth/Renewal
75/76	SAP	17%	83%
76/77	CR	73	27
77/78	CR	81	19
78/79	CR	79	21
79/80	CR	81	19
80/81	CR	70	30
81/82	CR	77	23
82/83	CR	73	27
83/84	SAP	45	55
84/85	SAP	39	61
85/86	SAP	20	70
86/87	SAP	20	70
87/88	SAP	22	68

Rest./Reduction = temporary support + sectoral support
Growth/Renewal = R & D support + Regional Policy support + Export Support + Small Business Support
SAP = Social Democratic Party in power, CR = Coalition Govt

Source: Ministry of Industry (1985) *Swedish Industry and Industrial Policy*: 15; Ministry of Finance (1987) *The Swedish Budget, 1987-1988*.

From 1982 onwards, the Minister of Finance, Kjell-Olof Feldt remained a most influential political personality, in many ways surpassing Prime Minister Ingvar Carlsson[119] in his abilities in the latter part of the 1980s to form policies. Feldt, in particular, remained a staunch advocate of a declining role of the Ministry of Industry in terms of budget support for direct intervention.[120] Consequently, by 1987 the role of the Ministry of Industry in terms of funding was relatively small (less than 2% of the ministry budget and 1.5% of the entire budget) in comparison to other ministries. (See Figure 5.16.)

Figure 5.16
Profile of the Swedish Budget, 1987-1988
(In Million Swedish Kronor, % Ministry Budget)

Expenditure by Ministry	Amount (m.S.Kr.)	% Ministry Budget
Health and Social Affairs	91,262	33.63%
Education and Cultural Affairs	43,169	15.91
Defence	26,378	9.72
Labour	21,250	7.83
Finance	20,690	7.63
Housing and Physical Planning	15,763	5.81
Foreign Affairs	11,631	4.29
Transport and Communications	11,532	4.25
Justice	10,330	3.81
Agriculture	6,191	2.28
Industry	5,081	1.87
Environment and Energy	4,889	1.80
Public Administration	3,168	1.17
Total Ministry Expenditure	271,334	100.00%
Total Swedish Budget	338,847	
% Ministry Expenditure to Total Budget		80.08%

Source: Ministry of Finance (1987) *The Swedish Budget, 1987/88*: 49.

After 1982 the Swedish Ministry of Industry began to view industrial policy in terms of structural changes in the market; significant funding by the ministry was directed to regional development policy. New factories were encouraged to relocate near distressed regions where former shipyards and steel mines were once located. With State incentives for firms to move, firms that welcomed the State scheme were allowed to pay their taxes into reserve funds, which they could subsequently recapture.[121] As a complementary policy, the State helped to train workers in these distressed areas. Consequently, over 40% of the Ministry of Industry budget was directed to the regional development fund by 1987.[122] (See Figure 5.17.)

Figure 5.17
Ministry of Industry Budget in Sweden, 1987
(In m.S.Kr., % Budget)

Policy	1986/7	1987/8	% 87/8 Bdgt	Diff.86/7-87/8
Regional Devlpmnt	1604	2025	40%	+421
Industry	1436	1135	22	-301
Technical Devlpmnt	1200	1151	22	- 49
State-Owned Companies	582	593	12	+ 11
Minerals Policy	123	127	3	+ 4
Miscell.	64	50	1	- 14
Total	5009	5081	100%	+ 72

Source: Ministry of Finance (1987) *The Swedish Budget, 1987/88*: 120.

Industrial policy-making, particularly with regard to these regional policy schemes, was funded through central State authorities (e.g., the Ministry of Industry) yet often enacted by regional authorities. States Jon Pierre of Gothenburg University, the Ministry of Industry adopted a strategy whereby,

> [It] provided subsidies for R & D projects, local restructuring initiatives, and infrastructural development, leaving the allocation of the capital to consortiums of public and private actors at the local and regional levels in order to encourage local resource mobilization....[123]

Moreover, the Ministry of Industry engaged in a serious effort to bolster technical research through its research and development programme. Six percent of the value of the country's industrial output was spent on research and development, making Sweden second only to the U.S. and well above most of its industrial competitors. Moreover, through the period 1987-1989, 2.5 billion S.Kr. was put forward to the National Board for Technical Development as finance grants.[124] Through the use of collaborative research institutes, the major universities attempted to use "greenhouses" where new enterprise ideas "germinated"[125] and also to promote university interest in technology-based "T"-Line degrees.[126]

In Sweden, R & D spending remained highly concentrated in large firms; ninety-five percent of R & D spending occurred in those with more 500 employees, with the ten largest firms accounting for two-thirds of all R & D.[127] From the end of the *bourgeois interregnum* in 1982 to 1988, the Swedish State spent four percent of its public money on commercial R & D, a higher percentage than in any other country in the world; most States spent only two to three percent, including the amount disbursed for defence.[128] Because of such R & D intensity, in 1983 Sweden had 2.00

robots per 1000 employees in manufacturing, while Japan had 1.46, the Federal Republic of Germany 0.63, the U.S. 0.43, Italy 0.38, France 0.32, and the U.K. 0.32.[129] Consequently, Sweden ranked first in a survey among OECD countries in terms of the level of automation in industry.[130]

In addition, other measures, such as Sweden's corporate taxation system and the furnishing of export credits, inspired industrial growth and investment. Throughout the 1980s the Swedish corporate taxation system allowed firms to pay lower taxes as long as profits were reinvested back into the firm. For multinationals operating abroad, the Swedish territorial tax system was far more lenient than in states such as the U.S. in exempting or deferring their home country tax.[131] As one business executive stated, "Sweden does not believe in rich people, but we do believe in rich companies."[132] Consequently, while the nominal corporate tax rate was 52%, with various tax breaks, the use of reserve funds, and the lenient territorial tax system, the corporate taxation burden was relatively modest. For example, while Sweden had the highest corporate income tax rate among OECD countries during the 1980s, Sweden ranked among the top five OECD countries in terms of corporate income after tax between 1984 and 1986.[133] As Magaziner and Patinkin contend, "The effective tax rate for most Swedish companies is close to zero....It is a very effective system, which encourages investment in the economy, enhances public purpose, yet gives Swedish companies a competitive advantage *vis-a-vis* foreign competitors that are taxed."[134]

Moreover, the Swedish State provided effective export financing through *AB Svensk Exportkredit* (SEK), a joint venture of the Swedish government and Swedish commercial banks; the Kingdom of Sweden owned fifty percent of SEK and the major commercial banks owned the other half.[135] Working with the *Exportkreditnamnden* (EKN), a government institution acting independently (though a part of the Ministry of Foreign Affairs), these two institutions provided three major programmes: funding, insurance, and mixed credits.[136] Under the joint system, a sales contract would be negotiated between the buyer and seller, a bank would then provide a long-term loan at the market rate plus fees, the SEK would provide an interest made agreement to the bank, and the EKN would insure against buyer default.[137] In the funding area, the SEK provided financing under a market rate and state support system. The market rate system provided export financing for Swedish firms at the market rate of interest and was fixed at a quarter of a percent above the cost of borrowed funds. The State support system provided loans for exports below market rates and remained "extremely flexible"[138] for Swedish exporters who face various political risks. Unlike the Swiss export credit guarantee programme that was scaled down during the 1980s in favour of private financing, SEK total assets, operating profit, and return on equity grew during the decade.[139]

Unlike in Ireland, where the State actively pursued inward FDI as a result of its weak indigenous industrial structure, in Sweden the State's approach was much more restrictive given its powerful, high tech indigenous industrial structure. In cases when mergers or acquisitions were proposed between a Swedish enterprise and a foreign company, the Ministry of Industry prepared a report based on discussions with the LO, the SAF, the authority for economic affairs, and the authority for technical development. The report, which would take three to four weeks to prepare, was a synthesis of the various viewpoints examining the global risks involved. After the government was briefed, a final cabinet decision was made by a vote of all the Ministries, not just the Ministry of Industry. Indeed, the government took these steps in regard to Sweden's biggest international merger during the 1980s - that between Asea and Switzerland's BBC Brown Boveri. Following the example of this merger, the position of the Ministry of Industry was, in the words of one bureaucrat in the Large-Scale Enterprise Section of the ministry, "an almost benign policing authority."[140]

Consequently, the Ministry of Industry adopted an industrial policy philosophy based on R & D subsidisation, regional and infrastructural development, and the provision of export credits. National and regional coordination became necessary because the allocation of industrial policy capital was typically given to consortiums mixed between public and private actors primarily at the local and regional levels.

D. Switzerland

In Switzerland, throughout the 1980s industry was represented primarily through the *Vorort*, Switzerland's peak business association, which was able to convey to the government in an organised sense the needs of industry and financial institutions.[141] The *Vorort* worked "intensely"[142] in a consultative way with the parliament, government, and the Ministry of Industry and Work (the *Gewerbeverbamt*); it aggregated the views of its associations, the major industrial associations being the Machinery and Chemicals Associations,[143] through standing committees on particular issues.[144] Despite diversified interests within the *Vorort* and with a high degree of regionalism, particular industrial interests never changed the overall market philosophy of the *Vorort*, which "strongly oppose[d] any sustained interference."[145] Consequently, problems of economic adjustment were viewed by the Swiss as a problem for the firm, not the State; this perspective explains why Rudolf Walser, Secretary of the *Vorort* asserted that, "Switzerland does not have an 'industrial' or 'structural' policy."[146]

A poignant example of this non-interventionist outlook occurred in 1985 when the three major Swiss banks (Union Bank of Switzerland, Swiss Bank Corporation, and Credit Suisse) examined the possibility of providing capital assistance for young Swiss firms that were unable to establish themselves in the face of international competition. Under the scheme, the federal government would offer guarantees to new companies as a risk premium which would essentially cover possible losses. While the scheme passed parliament, the *Vorort* successfully thwarted the proposal through a public referendum,[147] which overrode the parliament's earlier decision."[148]

Moreover, although Switzerland continued to advocate applied research in locations such as universities, R & D development occurred at the enterprise level.[149] The chemicals industry accounted for 52.9% of R & D spending by industry, while the machinery industry accounted for 42.2%; in sum, industry spent 3597 million S.Fr. on R & D, or 740 S.Fr. per each head in Switzerland.[150] (See Figures 5.18, 5.19, and 5.20.)

Figure 5.18
Research and Development Expenditures
For Selected Countries, 1986
(As % of Internal Production)

Country	Private Financed	State Financed	Others	Part of R & D In Production
Switzerland	75%	25%	0%	2.3%
Japan	62	27	11	2.4
FRG	58	41	1	2.6
Sweden	57	40	3	2.2
USA	49	49	2	2.7
Italy	49	49	2	1.1
Netherlands	46	48	6	1.9
Canada	42	50	8	1.4
France	42	58	0	2.1
Britain	41	50	9	2.4

Figure 5.19
Amount Spent on R & D in Switzerland Per Sector, 1986
(Millions Swiss Francs and % per sector)

Sector	m.S.Fr.	%
Machines, Electrotechnics, Metals	1517.1	42.2
Chemicals	1901.6	52.9
Watchmaking	68.9	1.9
Textiles	27.3	0.8
Clothing Industry	36.0	1.0
Paper and Plastic	14.2	0.4
Construction	32.1	0.9
	3597.2	100.0

Figure 5.20
R & D Spending in Switzerland by Size of Enterprise, 1986

No. of Employees	In m.S.Fr.	% of R & D Spending
Less than 10	10.1	0.3
10-49	134.6	3.7
50-99	196.0	5.4
100-499	723.8	20.1
500-999	405.3	11.3
100-4999	2127.4	59.1

Source: Union Suisse Du Commerce et De L'Industrie (1987) *La Recherche et Le Developpement Dans L'Economie Privee En Suisse*: 17, 23, 40.

Such societal values, strong economic conditions that did not necessitate intervention, and relatively passive fiscal policy-making in general,[151] resulted in government aid to industry in Switzerland being relatively small throughout the 1980s. (See Figure 5.21.)

Figure 5.21
Government Aid to Industry in Switzerland, 1981-1986
(In Million S.Fr.)

Aid	1981	1982	1983	1984	1985	1986
General Aids						
- Grants	-	-	-	-	0.68	0.67
- Loans	-	-	-	-	0.18	0.10
Regional Aid						
- Grants	0.38	2.34	3.60	2.85	0.59	1.01
- Loans	-	-	-	-	-	-
- Grntees	28.40	37.10	60.80	86.60	2.36	3.69
R & D						
- Grants	9.20	11.20	11.80	15.80	15.33	16.33
Emplymnt Aid						
- Grants	-	0.78	-	1.90	0.07	0.08
Sectoral Aids	-	-	-	-	-	-
Strct'l Sppt and Rscue						
- Grants	14.40	15.40	7.80	8.20	6.22	6.97
Small Firm Dvlpmnt						
- Guarantees	0.55	0.61	0.74	0.36	1.70	1.87
Firm Specific Subsidies	-	-	-	-	-	-
Export Promo						
-Grants	7.10	7.10	6.30	6.30	9.53	9.45
Total	49.93	63.53	70.04	105.01	41.88	46.31

Source: EFTA/EC, Annex VI, 11/86, "Government Aids to Industry in Switzerland: 7; Bundesamt fur Aussenwirtschaft (1987) "Government Aids to Industry in Switzerland, October 14.

Nevertheless, a substantial portion of support for industry was derived at the cantonal (or state) level; Switzerland ranked first among twenty-two OECD countries in terms of "the independence of regional authorities for central government in financing and decision-making."[152] Out of twenty-six cantons, thirteen provided their industries with direct aid (grants, lower interest rates, security losses). Areas that were particularly affected by the recession of the 1970s - namely the watch cantons (Group A) of Soluthurn, Jura, Berne, Basle country, Neuchatel, and Vaud - received cantonal aid, mainly in the form of guarantees and interest rate subsidies. Cantonal aid was also awarded to the mountain cantons (Group B) and the Midland cantons (Group C). (See Figure 5.22.)

Figure 5.22
Cantonal Support to Industry in Switzerland, 1981-1985
(Net Cost Expenditures in Millions S.Fr.)

Canton	1981	1982	1983	1984	1985
Group A	2.1	5.4	12.0	7.1	9.4
Group B	1.5	0.8	1.0	1.1	1.3
Group C	0.1	0.3	0.4	0.5	0.5
	3.7	6.5	13.4	8.7	11.2

Source: EFTA/EC, Annex VI, 11/86, "Government Aids to Industry in Switzerland: 8.

This minimal amount of State aid, even through the cantons, illustrates that the crisis of the latter 1970s was insufficient to prompt the Swiss State to use large-scale measures of intervention. Notably in 1978, under the regional programme that focused on the watch cantons in the Jura, the State began to grant only limited subsidisation and loan guarantees for private investment projects that were considered promising. Stated one government official, "In principal, if there were any problems within any industry other than the watch industry, the government would not step in."[153]

Moreover, completely opposite to both the Irish industrial structure and the Irish industrial policy orientation, Switzerland's indigenous industrial structure was filled with large multinational corporations that remained relatively closed to foreign companies seeking FDI through acquisition. During the 1980s Switzerland's commercial code had few limits on the way in which companies wrote their statutes, and directors could refuse to register a shareholder for nearly any reason. Stated one British newspaper, "The Swiss legal system allows Swiss companies to be virtually bid-proof, while the UK, along with the US, is probably the most open market in the world."[154] As Urs W. Benz explains,

> There are instances where restrictions on the free transfer of shares are in the interest of corporations and/or their shareholders. Most often one finds transfer restrictions in the charters of so-called closed corporations or family corporations. Such transfer restrictions are designed to maintain the original balance of control, avoiding the sale of shares to outside persons, or to ensure that shares can be held only by members of one of a few families.[155]

As a consequence, Swiss MNCs preferred to protect their large MNCs' to preserve their national character, avoid dependence on foreign competitors, and maintain government contacts in some cases where only domestic producers would be considered. Hence, Swiss MNCs usually maintained one of the following restrictions with regard to ownership:

1) only Swiss citizens may be registered as shareholders;
2) foreigners and foreign companies may not be registered as shareholders. Swiss companies that are controlled by foreigners are regarded as foreign companies;
3) only Swiss citizens and foreigners who are domiciled in Switzerland may be registered shareholders;
4) the board of directors may refuse a new shareholder without stating a reason;
5) the board of directors may refuse a new

shareholder 'on important grounds';
6) the board of directors may refuse a new shareholder if one of certain enumerated grounds applies; and
7) a foreigner may not acquire more than a certain number or percentage of nominal shares.[156]

In the 1980s all of the following companies had such restrictions: Alusuisse, Bank Leu, Ciba Geigy, Hasler Holding, *Kolderbank*, Nestle,[157] Oerlikon-Buhrle Holding, *Schweiz Bankverein*, *Schweiz Ruckversicherung*, Sibra Holding, Sulzer, Swissair, and Winterthur.[158]

Moreover, the State granted Swiss multinationals an extreme amount of independence in which Swiss firms were able to build up hidden assets (*Stille Reserven*). The reasons for the secrecy was the fear that if the size of assets were to become public, this would spur government taxation and further recognition from international competitors. As a consequence, corporate reporting was extremely lax in Switzerland. During the 1980s a number of corporations did not publish consolidated reports because there were no formal balance sheet schemes required[159]. As Pauchard explains,

> ...no precise scheme of regulations exists for the composition of the balance sheet and the profit and loss account, and the reporting of companies with a broad shareholder base is, at best, as good as in other continental European countries, where accounting standards have probably not affected the economy negatively.[160]

Moreover, in the 1960s, 1970s, and 1980s Swiss taxes were by far the lowest of all the small European states, hovering just above Japanese rates. Swiss revenue loss remained around 2.85% of GDP, which was much higher than in other OECD countries.[161] In general, it should be remembered that the Swiss themselves directly voted on how much they should tax themselves and their corporations (indeed, a unique, if not startling, circumstance). The proportion of federal, cantonal, and local taxes to GDP per capita was just over thirty percent.[162] Tax reliefs included those for "interesting" firms, which consisted of partial or total tax exemption for a period of up to ten years or additional possibilities for depreciation.[163]

In taking an active role in stimulating Swiss industrial competitiveness, the State did attempt to positively affect industry through two notable policies: export risk guarantees and export promotion. The Export Risk Guarantees (ERG), operated by the *Office Suisse d'Expansion Commerciale*, provided risk guarantees for depreciation of foreign currency, difficulties for transfer, insolvability or the refusal to pay, extraordinary measures taken by foreign states or political events, and problems of transportation to foreign recipient.[164] By the mid-1980s, new guarantee issues were reduced; in 1985 these totalled two million S.Fr., which represented a decrease of twenty percent from the preceding year of 2.5 million S.Fr. ERG coverage was phased down because of the suspension of guarantees against monetary risk after April 1985, the decision to use the private sector to shoulder more of the coverage burden, and the general reticence to accord guarantees for projects in countries with high political risks.[165] (See Figures 5.23 and 5.24.)

Figure 5.23
Guarantees Provided by the GRE in Switzerland, 1974-1985
(Total Numbers)

Year	No. of Guarantees	New Guarantees	Total Engagements
1974	6,456	3,406.0	6,921.3
1975	7,492	3,067.6	8,465.5
1976	8,718	6,216.7	12,663.9
1977	10,703	6,310.4	16,166.0
1978	14,325	8,877.3	22,957.5
1979	14,593	6,332.3	25,470.8
1980	15,596	6,959.4	25,282.6
1981	11,469	4,481.5	22,280.5
1982	9,315	2,345.3	19,694.4
1983	8,787	4,184.5	17,989.4
1984	7,961	2,513.5	15,837.7
1985	7,613	2,007.5	14,123.2

Source: Office de Gestion De La Garantie Contre Les Risques a L'Exportation (1986) "Rapport Sur L'Exercice de la Garantie Contre Les Risques a L'Exportation:" 11.

Figure 5.24
Total Engagements for All Branches, 1985

Sector	m.S.Fr.	Part in %	Part +/- 1984
Machines	11319	80.15	-5.6
Chemicals	969	6.86	-40.2
Watches	59	0.42	-67.0
Textiles/ Clothing	131	0.93	-33.6
Construction	990	7.00	-12.6
Permits	7	0.05	-31.0
Engineering	549	3.88	-11.9
Miscellaneous	99	0.71	-12.6

Source: Office de Gestion De La Garantie Contre Les Risques a L'Exportation (1986) "Rapport Sur L'Exercice de la Garantie Contre Les Risques a L'Exportation:" 13.

Second, export promotion was one of the most important aspects of Swiss industrial policy and was run by the 2,500 member *Office Suisse d'Expansion Commerciale* (OSEC) [the

Swiss Office for Commercial Expansion]. Throughout the 1980s the Federal Department of Public Economy contributed one-third of its budget for export promotion, and it accomplished its tasks in a consultative procedure among the *Vorort*, foreign chambers of commerce, and Swiss embassies around the world. In general, the Swiss Export Promotion Programme attempted to gather and distribute information on foreign markets in favour of Swiss companies; gather and distribute information on Swiss goods and services;[166] organise, manage, and assist in finding business partners abroad; and organise trade fairs and special conferences.[167] In general, it remained an effective policy avenue because of the highly organised system of interaction among the State, foreign Swiss Chambers of Commerce, embassies and consulates, foreign representations, and OSEC.

In sum, Switzerland devoted a relatively small proportion of its fiscal budget towards industrial policy measures because of societal disaffection for fiscal intervention as well as the lack of necessity for industrial policy-making given the performance of the Swiss economy. Nonetheless, the State did have a minimal form of industrial policy that was implemented primarily at the cantonal level. Because of its oligopolised industrial structure, State R & D policies were less notable than technology development from within its major industrial firms.

5.5 The Role of the State in Developing Industrial Policies: Lessons from the Case Studies

This chapter has examined the role of the State in developing and implementing industrial policies in each of the four case studies. To different degrees each of the four small European states used various forms of industrial policy-making during the 1980s.

In Ireland, from the 1970s through the beginning of the 1980s industrial policy-making had historically emphasised the funding of a large State enterprise sector, along with promoting inward FDI. Agriculture, the state's most important sector, remained heavily subsidised from both the EC and the Irish State. By 1984 the State began to assess ways in which its industrial policy could be improved, specifically by examining the overall effects on Ireland's weak industrial structure as opposed to the effects on unemployment.

As the primary administrator of Ireland's industrial policy, the IDA became increasingly cognisant of attracting only those foreign subsidiaries that would add long-term benefits, benefits which could be achieved by carefully scrutinising foreign subsidiaries' industrial projects. In so doing, the IDA would preclude the historical problems of foreign subsidiary short-term employment and attracting only assembly plants where technology transfer to Irish indigenous industry could not take place. Needless to say, Ireland's indigenous industry remained small and without a significant technological base; as a result the new focus on industrial policy was not only one of encouraging improved direct foreign investment, but also of funding targeted sunrise sectors, such as the chemicals and electronics industry.

Consequently, under the *Programme for National Recovery*, the Irish State initiated a major transformation of its industrial policy, in which the new emphasis was placed on value for money defined in terms of wealth creation (as opposed to employment). At the same time, appreciating that its international competitiveness was being sapped by wage-inspired inflation, the State also worked with the ICTU and the FUE to suppress wage growth. (See Chapter Four). Through cooperative bilateral relations between the State and industry, by 1987 the State developed new industrial policy initiatives that stressed assistance to only high technology, sunrise industries. By initiating this programme as well as bringing about major wage reductions in 1987, the State established itself as the principal actor in attempting to elevate Ireland's level of international competitiveness.

In a similar vein, Denmark's industrial structure was composed of small- and medium-sized enterprises, operating primarily in the agricultural field. While Denmark's agricultural sector was also heavily subsidised by the CAP, its industrial policy had historically been one of non-intervention; a Ministry of Industry was formed only by the latter part of the 1970s and there were few if any nationalised industries.

Nonetheless, the international recession at the beginning of the 1980s negatively affected some of Denmark's most important industries, the most notable of which was shipbuilding. As a result, despite the State's rhetoric of avoiding subsidisation into "declining" sectors, the State disbursed a significant amount of its budget into various credit and leasing programmes to subsidise the ailing industry. Unlike Sweden, Denmark continued on a relatively inflexible course, pumping in public funding to the shipbuilding industry with varying annual amounts dependent upon the political winds. (See Figure 5.4.)

By the mid-1980s bilateral relations between the State and industry began to shift from detached to cooperative bilateral as Denmark's industrialists and policy-makers reassessed their industrial policy objectives. In particular, they evaluated Denmark's relatively weak, low technology oriented industrial structure. Due to the efforts of the "industrial modernists" in an interactive process involving several governmental ministries and industries, Danish industrial policy was transformed into a nationwide effort to modernise their industrial structure through comprehensive technology programmes. In particular, the State initiated a technology diffusion programme that resulted in increased levels of high technology good exports, and because of Denmark's large agro-industrial complex, it spearheaded a bio-technology programme. Despite the State's inability to control other negative economic factors (e.g., unemployment, inflation, current account deficit, foreign debt) through other fiscal policies, it provided the important impetus in recognising a primary state deficiency - its industrial structure. As a consequence, the State was the principal actor in Denmark in attempting to restore its level of international competitiveness.

The Swedish case of the 1980s provides a stimulating parallel. In 1976, the centre-right parties, which overtook the Social Democrats, provided significant subsidisation to the ailing shipbuilding sector, including nationalisation efforts of particular shipyards. In 1982, however, under Social Democratic leadership, shipbuilding subsidies were cut off, and what was once one of Sweden's largest industries no longer existed by the middle of the 1980s. From 1982 onwards the SAP changed Sweden's past industrial policy orientation away from restructuring and reduction to growth and renewal. The Swedish Ministry of Industry also attempted to spur its already oligopolised, high technology oriented industrial structure by spending on R & D programmes.

Because of Sweden's Solidaristic Wage Policy that forced companies to pay agreed-upon wages, only the strongest and largest could survive; as a result, unlike states such as Denmark and Ireland that had weak industrial structures, Sweden was filled with large MNCs. (See Chapter Four) With the State pumping money into the economy for reemployment, evidenced through regional policies that were complemented by active labour market polices in areas most affected by the shipbuilding closures, Swedish multinationals were highly productive, maintained low real unit labour costs, and were able to contribute vast sums of money for technological development. Through cooperative bilateral relations between the State and industry, the Swedish State complemented corporate R & D investment, providing the highest per capita amount of any state in the world.

With excellent economic performance and cultural aversion against interventionism, Switzerland had relatively minor industrial policies. With the Swiss industrial structure composed primarily of internationally powerful MNCs, the Swiss orientation towards inward FDI differed dramatically from the Irish industrial policy of enticing foreign companies to locate on domestic soil. With an already powerful industrial structure, Swiss laws remained compliant with indigenous industries' desire to prevent foreign ownership of Swiss MNCs through restrictive share ownership. Indeed, while Ireland ranked first in a survey of twenty-two OECD countries in terms of "the extent to which foreign investment is welcome at home," Switzerland ranked twentieth.[168]

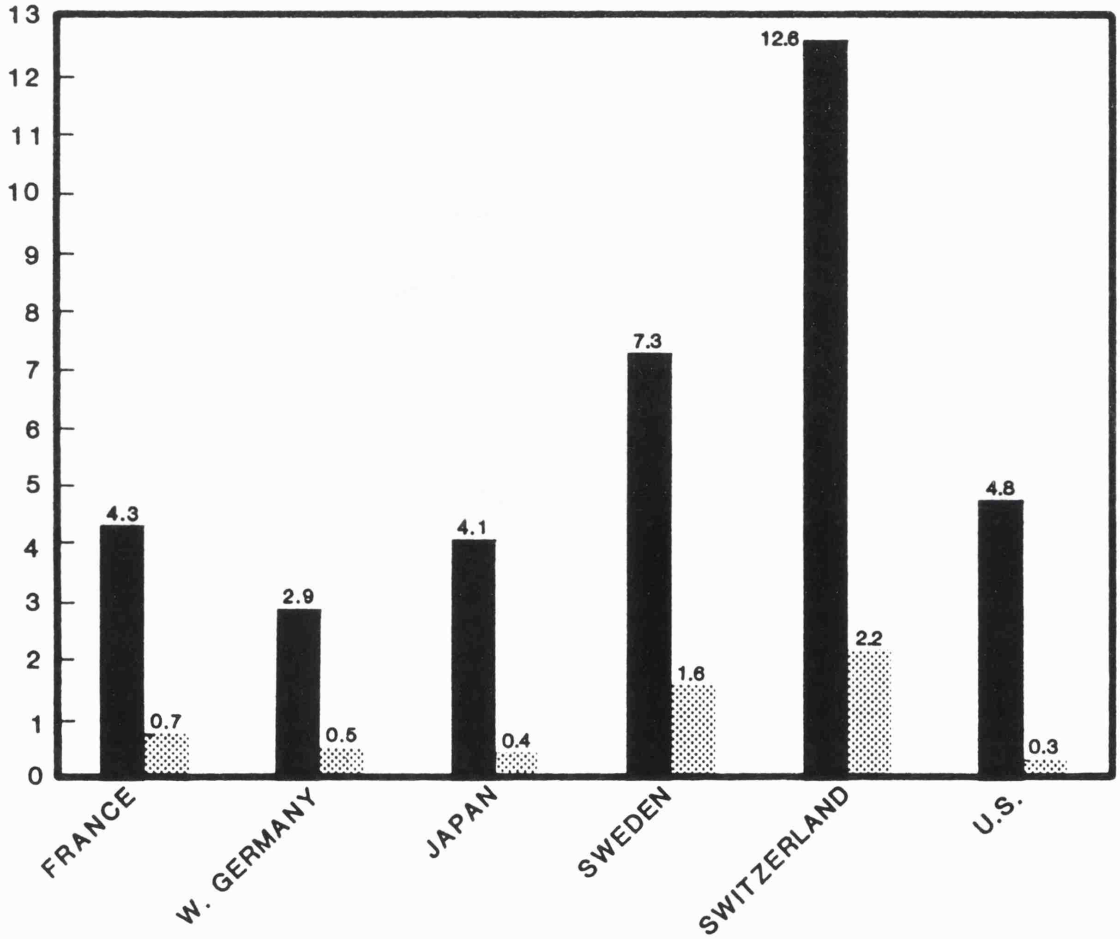
For the most part Swiss industrial policies that attempted to stimulate the state's industrial competitiveness were implemented at the cantonal level, though its export credit guarantee and export promotion programmes remained excellent examples of successful federal programme development and implementation. Similar in industrial structure to Sweden, Switzerland maintained an industrial structure filled with large, high technology oriented MNCs that were backed by Switzerland's powerful financial institutions. (See Chapter Three.) In Switzerland, however, the State played only a relatively minor role in granting R & D assistance.

Nonetheless, for both Switzerland and Sweden the record on patents provides a poignant illustration of just how effective technological development was for both states during the 1980s. Switzerland and Sweden ranked first and fourth, respectively, among twenty-two OECD countries in terms of the average annual number of patents granted to residents per 100,000 inhabitants between 1984-1986. (See Figure 5.25.) At the same time, both states successfully secured patent rights from abroad; they were ranked first and second, respectively, by the number of patents in the rest of the world per one-hundred thousand inhabitants. Moreover, both states' industrials protected their patent rights and secured them for their own use; Switzerland and Sweden ranked eighteenth and nineteenth among twenty-two OECD countries in terms of patents granted to foreign competitors.[169]

With such impressive R & D results in these two states, the evidence provided in this chapter with regard to Denmark and Ireland illustrate the level of importance that both states placed on technological development. While Sweden and Switzerland maintained powerful industrial structures that could afford to invest in technological development,

Figure 5.25

NUMBER OF PATENTS PER THOUSAND INHABITANTS IN 1985



Source: World Industrial Property Organization (1987). Industrial Property Statistics

much as a consequence of the impetus provided by each state's principal actor, neither Denmark nor Ireland possessed the industrial structure for this important form of investment. Consequently, in both states the State assumed the responsiblity for modernising its industrial structure, acting as the catalyst to foster industrial technological development. In Denmark, industrial policy and technology policy were terms that could be used interchangeably by the middle of the 1980s. In Ireland, the State's realisation that its industrial policy was not effective in transforming foreign subsidiary technology to its indigenous industry caused a major reformation of industrial policy focus.

Notes for Chapter Five

1.The multitude of definitions of industrial policy vary from author to author, though there is the pervasive notion that industrial policy affects the structure of industry and the decision-making of enterprises. For various characterisations and definitions of industrial policy, see F. Gerard Adams and Lawrence Klein, eds. (1983) *Industrial Policies for Growth and Competitiveness*: 14-19; Claude E. Barfield and William A. Schambra, eds. *The Politics of Industrial Policy*: 17, 33, 63; Chalmers Johnson (1984) "The Idea of Industrial Policy" in Johnson, ed. *The Industrial Policy Debate*: 7-9; David Vogel (1987) "Government-Industry Relations in the United States" in Wilks and Wright, eds. *Comparative Government-Industry Relations*: 91-103; Stephen S. Cohen and John Zysman (1987) *Manufacturing Matters: The Myth of the Post-Industrial Economy*: 218-219; Laura Tyson and John Zysman (1983) "American Industry in International Competition" in Zysman and Tyson, eds. *American Industry in International Competition*: 19-22.

2.See John Pinder, Takashi Hosomi, and William Diebold (1979) *Industrial Policy and the International Economy*: 67.

3.Peter J. Katzenstein (1985) *Small States in World Markets: Industrial Policy in Europe*: 26-27.

4.See Wyn Grant (1983) "The Political Economy of Industrial Policy" in R.J. Barry Jones, ed. *Perspectives on Political Economy*: 118.

5.Grant (1983) *op.cit.*: 118.

6.See Bengt-Ake Lundvall (1983) "Technology, Competitiveness, and Small Countries."

7.See Bjorn Johnson and Bengt-Ake Lundvall (1988) "Institutional Learning and National Systems of Innovation." Paper presented at the conference on "Strategies of Flexibilisation in Western Europe," Roskilde Universitetscenter (April 6-10).

8.Ibid.

9.See Bengt-Ake Lundvall (1988) "Innovation as an Interactive Process: For User-Producer Interaction to the National System of Innovation" in Giovanni Dosi et. al., eds. *Technical Change and Economic Theory*: 360.

10.IMEDE and World Economic Forum (1989) *The World Competitiveness Report*: 163. (Table 9.05)

11.See Chapter Two.

12.The Republic of Ireland was officially formed in 1922.

13.See Eoin O'Malley (1985) "The Problem of Late Industrialisation and the Experience of the Republic of Ireland." *Cambridge Journal of Economics*: 141-154.

14.See Gautam Sen (1984) *The Military Origins of Industrialisation and International Trade Rivalry*: 76-89.

15.J.P. O'Carroll (1987) "Ireland: The Political Dominance of Business" in M.P.C.P.M. Van Schendelen and R.J. Jackson, eds. *The Politicisation of Business in Western Europe*: 95.

16.Interview with Jesper Kongstad, Ministry of Industry, Copenhagen, Denmark, 9 September 1988.

17.See Niels Chr. Sidenius (1983) "Danish Industrial Policy: Persistent Liberalism." *Journal of Public Policy*: 49-61.

18.Niels Chr. Sidenius (1983) "Who Defines Industrial Strategies: The Danish Case." Paper prepared for the group "Who Defines Industrial Strategies?" at the 6th EGOS Colloquium, Florence (November 3-5): 14-15.

19.However, some detractors such as Damgaard have contended that such terminology was only an example of the government's use of "symbolic politics." See Erik Damgaard (1989) "Crisis Politics in Denmark, 1974-1987" in Damgaard, Peter Gerlich, and J.J. Richardson, eds. *The Politics of Economic Crisis: Lessons from Western Europe*: 83.

20.Interview with Niels Chr. Sidenius, Institute of Political Science, Aarhus University, Aarhus, 12 September 1988.

21.The mixed economy approach is discussed in terms of the Swedish paradox between collectivism and individualism in: Marquis Childs (1980) *Sweden: The Middle Way on Trial*: Chapters 3 and 4.

22.Hugh Heclo and Henrik Madsen (1987) *Policy and Politics in Sweden*: 60.

23.Lennart Erixon (1982) "Why Did Swedish Industry Perform so Poorly in the Crisis?" *Skandinaviska Enskilda Banken Quarterly Review*: 126.

24.Interview with Dr. Arne M. Andersson, Department of Economics, Gothenburg University, Gothenburg, 7 September 1987.

25.For instance, Japan has built up particular industrial sectors through its MITI-MOF laser-beam strategy and France's *planning indicative* national champion strategy is well-documented. See Patrick Messerlin (1987) "France: The Ambitious State" in Duchene and Shepherd, eds. *Managing Industrial Change in Western Europe*: 90-92.

26.This was an aggregate ranking from twenty-two categorisations. See IMEDE and World Economic Forum (1989) *op.cit.*: 25, 123-129.

27.James D. O'Donnell (1979) *How Ireland is Governed*: 73.

28.ICTU (1986) *Public Enterprise: Everybody's Business*: 36-37.

29.Government of Ireland (1988) *Budget, 1988*: 144-151. For example, the IDA provided over forty million Irish pounds to *Siucre Eireann* for project development. See "Sugar Report Paves Way for Goodman Takeover." (1989) *Aspect: The Investor's Business Journal*. (February): 7.

30.Government of Ireland (1988) *op.cit.*: 197.

31.See "Cash Crisis Looms at Aer Lingus." (1988) *Aspect: The Investors' Business Journal*. (March): 10-14 and "Rough Landing Ahead for Aer Rianta." *Aspect: The Investors' Business Journal*. (May): 1989.

32.Government of Ireland (1984) *White Paper on Industrial Policy*: 106.

33.See Department of Industry and Commerce (1986) *Review of Industrial Performance*: 34.

34.Ibid.: 141.

35.Ibid.: 99.

36.S.J. Sheehy (1988) "Irish Agriculture into the Nineties." *The Irish Banking Review*. (Autumn): 27.

37.By 1987 State ownership in a large steelwork in the northern region of Denmark was around ten to fifteen percent.

38.Interview with Ole Jess Olsen, Institute for Economics and Planning, Roskilde University, Roskilde (Copenhagen - interview location), 9 September 1988.

39.Ministry of Industry (1988) "Subsidies and Structural Adjustment: The Danish Reply to Questionnaire IND(87)5:" 7. (16 June, Reference JN/BKPS)

40.See Heine Andersen (1980) "Organizations, Classes, and the Growth of State Interventionism in Denmark." *Acta Sociologica*. Volume 23, Nos. 2-3: 123-126.

41.Interview with Kongstad, 9 September 1988. Figures taken from "*Volbetalt erversstolte i Kr. per best ajegekte og i pct of BFI og FSKpark.*"

42.Christopher Follett (1989) "Farmers Facing Multilevel Crisis." (Special Section: "Denmark: Signs of Strain.") *International Herald Tribune*. (March 1): 11.

43.See Braendgaard (1984) *op.cit.*: 14-15.

44.Ministry of Industry (1988) *op.cit.*: 3.

45.Peter Mottershead (1983) "Shipbuilding: Adjustment-Led Intervention or Intervention-Led Adjustment" in Geoffrey Shepherd, Francois Duchene, and Christopher Saunders, eds. *Europe's Industries: Public and Private Strategies for Change*: 90.

46.See Bo Strath (1987) *The Politics of De-Industrialisation: The Contraction of the West European Shipbuilding Industry*: 194-198.

47.Ibid.: 195.

48.Interview with Jesper Kongstad, Head of Section, Ministry of Industry, Copenhagen, 9 September 1988.

49.Interview with Dr. Esben Sloth Andersen, Institute of Production, Aalborg University, Aalborg, 12 September 1988.

50.Ibid.: 60.

51.In particular, competition from markets with lower labour costs, like South Korea and Japan, could produce ships at a far lower cost. See C.H. Siven (1983) "The Political Economy of Sweden in the 1970s." *The Annual Institute of Economic Research*, Chuo University, No. 14: 215-246.

52.See Mottershead (1983) *op.cit.*: 100-101.

53.Jonas Pontusson (1986) *Labor Reforms and the Politics of Capital Formation in Sweden*. Ph.D. Dissertation, University of California-Berkeley: 527.

54.There has been much talk of privatisation of Procordia, which has been highly profitable. The government has issued stocks amounting to less than 10% of the total, a rather small chunk, but it is a first step. The government plans to use the capital markets to finance investments in it.

55.Interview with Dr. Hilde Phan-Huy, Assistant Vice-President, Economics Department, Credit Suisse, Zurich, 9 November 1987.

56.This adjustment was consequential since the Swiss Franc had traditionally been undervalued.

57.Interview with Dr. Franz Halbheer, Senior Vice-President, Public Affairs, Credit Suisse, Zurich, 12 November 1987.

58.Among those with the most significant influence on the debate on textiles was the Swiss bank, *Credit Suisse*, who opposed awarding special credit assistance to the troubled industry (ies). The bank asserted that clothing production from the Far East was too competitive because of lower labour costs. Moreover, unlike the watch industry, textiles did not hold the national interest. Hence, the Swiss textiles industry never received aid.

59.Indicative of the lack of interest in industrial policy is that the government survey of different aspects of Swiss economic policy lacks a chapter on industrial policy.

60.See Katzenstein (1985) *op.cit.*: 70.

61.As of this writing there are plans to sell the remaining shares.

62.EFTA/EC (1986) "Government Aids to Industry." (November).

63.Ibid.

64.Interview with Eamonn Sheehy, Project Manager, Industrial Development Authority of Ireland, Dublin, 13 February 1989.

65.Interview with Peter Coyle, Manager, Technology Enterprises Department, Industrial Development Authority of Ireland, Dublin, 22 February 1989.

66.Under the 1980 Finance Act Ireland installed the ten percent maximum corporate tax, which is given in respect of the profits from the sales of manufactured goods. For details, see Industrial Development Authority (1988) *Guide to Taxes and Tax Reliefs in Ireland.*

67.See Dermot McAleese (1987) "Industrial Policy and Performance in Ireland" in P.R. Beije, J. Groenewegen, I. Koustoulas, J. Paelinck, and C. Van Paridon, eds. *A Competitive Future for Europe? Towards A New European Industrial Policy*: 162.

68.Ibid.: 152.

69.O'Malley (1985) *op.cit.*: 149.

70.See Jim O'Leary (1987) "The National Debt: Implications for Fiscal Policy." *Irish Banking Review*: 3-19.

71.O'Malley (1985) *op.cit.*: 149-153.

72.Niamh Hardiman (1987) "'Consensual Politics?' Public Goods and Collective Action in Ireland" in Ilja Scholten, ed. *Political Stability and Neo-Corporatism*: 154.

73.Government of Ireland (1984) *op.cit.*: 12.

74.O'Carroll (1987) *op.cit.*: 94.

75.Government of Ireland (1984) *op.cit.*: 11.

76.Interview with Ronald Long, Principal Officer, Office of Science and Technology, Department of Industry and Commerce, Dublin, 16 February 1989.

77.Interview with Sheehy, 13 February 1989; Interview with Sean Ward, Assistant Principal Officer, Planning Division, Department of Commerce and Industry, Dublin, 16 February 1989. Department of Industry and Commerce (1989) *Strategy for the Irish-Owned Electronics Industry.*

78.Interview with Coyle, 22 February 1989.

79.See Frances Ruane (1984) "The White Paper on Industrial Policy." *The Irish Banking Review.* (September): 35-45.

80.Verein Schweizerischer Maschinen-Industrieller (1987) "Bulletin: *ExportFoerderung Im Europaeischen Vergleich." (3 July)*: 2.

81.Interview with Dermot O'Doherty, Science and Technology Policy Unit, Irish Science and Technology Agency (EOLAS), Dublin, 22 February 1989.

82.Confederation of Irish Industry (1988) *Annual Report, 1987*: 18.

83.OECD (1985) *Innovation Policy in Ireland.*

84.See Government of Ireland (1984) *op.cit.*: 33, 106.

85.McAleese (1987) *op.cit.*: 147.

86.Interview with Paul Toal, Manager, New Product Development, Industrial Development Authority of Ireland, Dublin, 13 February 1989. Grants for research and development projects by foreign firms (up to 50% of the approved cost of a project) totalled 12.88 million Ir.Pd. in 1987 (706 projects), while IDA R & D expenditure totalled 28.49 million Ir.Pd.

87.See Brendan O'Sullivan (1987) "Technology and Innovation in the Regeneration of Established Firms" in Dermot O'Doherty, ed. *Managing Technology and Innovation Successfully.* Technology and Industrial Development Conference Proceedings: 33-45.

88.Ibid.: 36-41.

89.Interview with Ned Costello, Office of Science and Technology, Department of Commerce and Industry, Dublin, 22 February 1989.

90.See Paul Turpin (1987) "Implications for Industrial Policy" in O'Doherty, ed. *op.cit.*: 49.

91.Interview with Toal, 13 February 1989.

92.See Commission of the European Communities (1987) *Eurotec.* (October); Commission of the European Communities (1985) *Completing the Internal Market*: 30-32; Commission of the European Communities (1982) *The European Community's Internal Strategy*: 49-54.

93.Con Power (1988) "Business and Government." Press release extract from a talk to the certificate course of the Public Relations Institute of Ireland (28 November): 3.

94.In 1983 the high technology products share of industrial exports was 9.1%. The average for most other European countries ranged from twelve to nineteen percent. See Ministry of Finance (1986) *Debatoplaeg om Vaekst og Omstilling*. (May): 30.

95.Imede and World Economic Forum (1989) *op.cit.*: 129, 126 (Tables 6.21, 6.07, 6.08, 6.09).

96.Interview with Asger Braendgaard, Institute for Production, Aalborg University, Aalborg, 12 September 1988.

97.Forskningssekretariatet (1987) *Ehrverslivets Forskning Og Udviklingsarbejde, 1985*: 30-31. Of the total, the greatest percentage (22%) was from the chemicals industry.

98.Union Suisse du Commerce de L'Industrie (1987) *La Recherche et Le Developpement Dans L'Economie Privee En Suisse*: 35.

99.Some notable exceptions were NOVO, whose R & D budget remained around 450 m. D.Kr.; *Chr. Hansens Laboratorium*, the food additives enterprise with a R & D budget of 50 m. D.kr.; Carlsberg, with a 200 m. D.Kr.R & D budget for plant breeding activities; and the Sugar Factories, with a R & D budget of 200 m. D.Kr. Interview with Jorgen Lindgaard Pedersen, Lecturer, Institute of Social Sciences Technical University of Denmark, Lyngby (Denmark), 7 September 1988.

100.See Jesper Kongstad and Ole Jess Olsen (1987) "Danish Industrial Policy: Continuity or Change?" in P.R. Beije et. al., eds. *op.cit.*: 128-130.

101.However, in 1986 the government stated that there would be "a considerable tightening up of the industrial promotion system..." *Ministry of Industry (1986) The Danish Government's Statement on Industrial Policy, 1986*: 6.

102.Interview with Braendgaad, 12 September 1988. As he further stated, "After all, the chances for major strikes over technology policy were not that high."

103.See Jan Annerstedt (1988) "Industrial Modernists and 'National Programs' for High Technology." Paper for the Special Session on "State Policies on Techno-Industrial Innovation and Unintended Consequences," International Political Science Association, Washington, D.C.

104.Interview with Jan Annerstedt, Institute for Economics and Planning, Roskilde University, Roskilde (Denmark), 13 September 1988.

105.OECD (1988) *Reviews of National Science and Technology Policy*: 11.

106.Peter Munk Christiansen (1988) *Teknologi Mellem Stat Og Marked*: 330, 332.

107.Ministry of Industry (1986) *op.cit.*: 4.

108.Interview with Sigurd Nis Schmidt, Head of Section, Federation of Danish Industries, Copenhagen, 5 September 1988. Also, see Niels Chr. Sidenius (1987) "Denmark: Business as Part of Politics" in Van Schendelen and Jackson, eds. *op.cit.*: 54.

109.OECD (1988) *op.cit.*: 91.

110.Jorgen Lindgaard Pedersen and Inger-Marie Wiegman (1987) *Biotechnology in Denmark*.

111.Interview with Martin Korst, Head of Science Policy Division, Danish Research Administration, Copenhagen, 6 September 1988.

112.See Alfred S. Pedersen (1988) "The Great Lipase Chase." *Scanorama*. (September): 107-112.

113.Interview with Pedersen (Jorgen Lindgaard), 7 September 1988.

114.OECD (1988) *op.cit.*: 54.

115.Ministry of Industry (1986) *op.cit.*: 4.

116.A discussion of this can be found in Roger Henning (1985) "Politics and Business in Sweden, 1974-1985." Paper presented for the ECPR workshop "Politics and Business in Western Democracies, (March 25-30).

117.Robert Z. Lawrence and Barry P. Bosworth (1987) "Adjusting to Slower Economic Growth: The External Sector" in Barry P. Bosworth and Alice M. Rivlin, eds. *The Swedish Economy*: 85.

118.The scale of this graph is somewhat misleading because it only takes percentages into account, not the monetary amount. The Ministry of Industry Budget was several times smaller in 1975/1976 than in 1983/1984.

119.Because of Olaf Palme's assassination, Ingvar Carlsson became prime minister in 1986. While Palme was outspoken and particularly popular among Swedes, Carlsson has been far more reserved and less popular.

120.Interview with Lars Heikensten, Head of Long-Term Planning, Ministry of Finance, Stockholm, 8 September 1987.

121.See Ira C. Magaziner and Mark Patinkin (1989) *The Silent War: Inside the Global Business Battles Shaping America's Future*: 165, 353.

122.In terms of regional policy, the government was able to use effectively five policies: (1) regional development support through location grants, investment grants, and conditional support; (2) employment grants, which were essentially a fixed sum paid annually for up to seven years; (3) special measures for sparsely populated areas such as rural communities; (4) transport support for northern area companies; and (5) reduced payroll taxes. The Swedish Institute (1986) *Swedish Regional Policy*.

123.Jon Pierre (1988) "Central State, Local Government, and the Market: A Comparative Analysis of Industrial Policy in Structural Change in Japan and Sweden." Paper presented at the XIVth World Congress of the International Political Science Association (August 28-September 1).

124.There are also conditional loans for company research/development projects. Such loans are split 50-50 between the State and the company, and if the project is successful, the company must pay the State back its 50%. If it fails, the State writes it off.

125.Bengt-Arne Vedin (1985) "Links Between Swedish Industry and the Higher Education System." *Social Change in Sweden*.

126.Bengt-Arne Vedin (1982) "Knowledge - The Basis for Industrial Success" in Bengt Ryden and Villy Bergstrom, eds. *Sweden: Choices for Economic and Social Policy in the 1980s*: 99-103.

127.See Ministry of Industry (1985) *Swedish Industry and Industrial Policy* and Lawrence and Bosworth (1987) *op.cit.*: 77.

128.Magaziner and Patinkin (1989) *op.cit.*: 165, 353.

129.Guy Standing (1988) *Unemployment and Labor Market Flexibility*: 89.

130.IMEDE and World Economic Forum (1989) *op.cit.*: 82. (Table 2.17)

131.See Arthur Young and Company (1988) *The Competitive Burden: Tax Treatment of U.S. Multinationals*.

132.Interview with Hans-Dietr Weise, Senior Manager, Business Coordination, Project Finance, Ericsson, Stockholm, 8 September 1987.

133.IMEDE and World Economic Forum (1989) *op.cit.*: 86. (Tables 2.27, 2.28)

134.Magaziner and Patinkin (1989) *op.cit.*: 353.

135.*Se Banken* owned eighteen percent, *PK Banken* ten percent, *Svenska Handelsbank* ten percent, and other Swedish banks twelve percent. Interview with Leon Odnevall, Senior Adviser to the Management of the Central International Department, *Svenska Handelsbank*, Member of Board, *AB Svensk Exportkredit*, Stockholm, 2 September 1987.

136.Interview with Birgitta Nygren, Swedish National Debt Office, Ministry of Foreign Affairs, Member of Board, *AB Svensk Exportkredit*, Stockholm, 2 September 1987.

137.Interview with Carl Karlmark, Assistant Treasurer, *AB Svensk Exportkredit*, Stockholm, 1 September 1987.

138.Interview with Ms. Stena Kreps, Market Group, *AB Svensk Exportkredit*, Stockholm, 1 September 1987.

139.SEK total assets were over 40,000 million S.Kr. in 1986, operating profit was 400 million S.Kr., and return on equity was over twenty percent. See AB Svensk Exportkredit (1986) *Annual Report*: 3.

140.Interview with Peter Sanden, Head of Section, Large-Scale Enterprises, Ministry of Industry, Stockholm, 8 September 1987.

141.In a 1986 study by Zurich University that attempted to quantify the political weight of peak associations in Switzerland, it was determined that the *Vorort* was considered to have the most influence on moulding fiscal policies. Interview with Rudolf Walser, *Sekretar des Vororts des Schweizerischen Industrie*, Zurich, 10 November 1987.

142.Interview with Roger Piccand, Ministry of Industry, Small and Medium-Sized Enterprises, and Work, Berne.

143.In the Machinery Manufacturers Association, for example, membership is by "contribution" of 0.055% of the tax-deductible payroll for each company. Interview with Mr. Peter Eberhard, Director, Information Services, Swiss Association of Machinery Manufacturers, Zurich.

144.It was rare for particular enterprises to approach the State directly, since for the most part these associations agreed with the *Vorort*'s declared position of opposing state intervention. Interview with Christoph Gysin, Economic Affairs Department, Swiss Society of Chemical Industries, Zurich.

145.Peter J. Katzenstein (1984) *Corporatism and Change*: 170.

146.Interview with Walser, *op.cit.*, 10 November 1987.

147.Because of Switzerland's direct democracy, the *Gesellschaft Zur Forderung Der Schweizerischen Wirtschaft* (GFSW) (Society for the Development of the Swiss Economy), created in 1942, provided a pivotal role in informing society on both economic and political issues. Not surprisingly, stated one official at the GFSW, "We help to assure that politics helps the economy, and we take a full laissez-faire stance." Interview with Theo Zidjenbos, Society for the Development of the Swiss Economy, Zurich, 9 November 1987. Stated one economist, "While their impact is indirect, they are extremely powerful. Their influence is through knowledge; their documentation is filled with marvellous graphs that makes economics interesting to the average person on the street." Interview with Phan-Huy, 9 November 1987.

148.Interview with Dr. Philippe Saurer, *Bundesamt fur Aussenwirtschaft*, Berne, 16 November 1987.

149.For instance, while in the 1950s the Swiss watch industry maintained a relatively large world market share, this dominance propelled neglect of technological innovation that pulled the industry to stagnation by the following decades. Thus, while in 1962 the watch industry spent over $7 million on R & D, it was spending over $60 million by the beginning of the 1980s. This example is illustrative of Swiss industries' predilection for sizable private R & D investment.

150.Union Suisse Du Commerce et De L'Industrie (1987) *La Recherche et Le Developpement Dans L'Economie Privee En Suisse*: 8.

151.As the OECD stated, "the Swiss authorities do not consider fiscal policy a suitable instrument for cyclical stabilization." See OECD (1986/1987) *Economic Surveys: Switzerland*: 38.

152.IMEDE and World Economic Forum (1989) *op.cit.*: 128. (Table 6.14)

153.Interview with Piccand, 17 November 1987.

154.Melvyn Marckus (1988) "Swiss Embarrassment." *The Observer*. (May 8).

155.Urs W. Benz (1985) "The Foreign Investor and the Swiss Equity Market: Legal and Fiscal Aspects" in Henri B. Meier, ed. *The Swiss Equity Market*: 108.

156.Ibid.: 109.

157.Though Nestle did revise its articles of association in 1988 to makes them less restrictive. See the following chapter for details.

158.Ibid.

159.Except listed companies, banks, insurance companies, and railways.

160.A. Pauchard (1985) "Corporate Financial Reporting in Switzerland and Accounting Principles" in Meier, ed. *op.cit.*: 119.

161.OECD (1980-1986) *Public Expenditure Trends.*

162.Ibid.

163.Interview with Saurer, 16 November 1987.

164."*Loi Federale Sur La Garantie Contre Les Risques a L'Exportation,*" (1958) 26 Septembre, 946: 11.

165.Office de Gestion de La Garantie Contre Les Risques a L'Exportation (1986) "*Rapport Sur L'Exercice de La Garantie Contre Les Risques a L'Exportation.*" (May). Also, interview with Philippe Nell, Ministry for Foreign Trade, Berne, 16 November 1987.

166.See Office Suisse D'Expansion Commerciale (1988) "*Programme d'Activites, OSEC*".

167.Interview with Thomas Pletscher, Secretary-General, Swiss Office for the Development of Trade, Zurich, 11 November 1987.

168.IMEDE and World Economic Forum (1989) *op.cit.*: 156. (Table 8.35)

169.Ibid.: 173-174. (Tables 9.25, 9.28, 9.31)

Chapter Six
Explaining Differences in Small European State International Competitiveness in the 1980s and Looking Towards the 1990s

6.1 The Small European State As an International Price Taker: Domestic Interventionism as a Necessity in the 1980s

This thesis has argued that because small European state industries are usually international price takers, during the 1980s small European states were forced to use various forms of intervention - such as monetary, labour market, and industrial policies - that acted as necessary complements to interaction between industry, financial institutions, and labour. However, because small European states remained dependent on international trade as a result of their limited producing and consuming markets, small state policy-makers also favoured in their public statements multilateralism in order to guarantee unobstructed trade.

One can conclude from this paradox that small states inherently followed an 'embedded liberalist' path, one where "... multilateralism and domestic stability were coupled and even conditioned by one another...."[1] Yet at the same time through various forms of intervention, the State actively supported state priorities and societal values in an attempt to provide such state benefits as full employment, a higher standard of living, a social welfare system based on equality, and higher levels of international competitiveness for industry.

For scholars of international political economy, the

1 does small
state matter?

2

lessons of the four case studies provide a source for analysis and investigation in studying the nature of the international economic system in the 1980s. In particular, given the various state-specific policy programmes discussed throughout the thesis, the small European state example questions whether the international economic system was 'liberal' during the decade.

Two significant questions with regard to the nature of the international economic system must be addressed. First, one must consider whether small European state domestic interventionism was indicative of the policy-making efforts of *all* states in the 1980s as a means to remain internationally competitive. In this respect, small European states may not have been distinctive. Small European states had only limited political and economic power, yet evidence from the thesis suggests that these states were able to use various forms of policy-making to attempt to maintain international competitiveness. One must question whether the small state example suggests that large states could, or did, use similar state-specific policy programmes during the 1980s without recrimination from their trading partners. Given the small European state's limited political and economic power, perhaps their interventionism was simply overlooked by large states? Or, maybe one could surmise that small European state policy-maker rhetoric worked.

Second, serious consideration must be given to the question of whether all states, small or large, required domestic interventionism to sustain international competitiveness. If indeed state-specific policy-making remained a necessity for states to remain internationally competitive, analysis of the international economic system by political economists will be guided less by such unqualified terms as free trade and protectionism. Such stark distinctions become obsolete in a world where all states have forms of domestic policy programmes - from strategic trade policies[2] to industrial policies - to stimulate political-economic performance as well as to augment their industries' competitiveness in world markets.[3]

For example, as John Zysman contends, any State has as many as four policy orientation alternatives through which it can help industry remain internationally competitive. First, the State can abide by the outcomes of market competition, avoiding any form of policy interference. Second, the State can attempt to influence industry through aggregate macroeconomic measures that affect all sectors equally, such as taxes or monetary policies. Third, the State can grant support to particular industries or sectors. Finally, the State can protect domestic firms, either by external protection or defensive subsidy.[4]

Of the four options, only the first option of economic liberalism was not employed in the case studies because of the small European state's international economic vulnerability. Contrary to those who have suggested that small European states are forced to employ 'laissez-faire,' 'liberal,' 'open,' or 'free trade' practices because of their international vulnerability, during the 1980s small European states used various state-specific policy programmes, which often included labour market policies, monetary policies, R & D policies, policies that provided capital transfers to troubled industries, or policies that promoted export expansion. (See Figures 1.12 and 1.13.)

At the same time, because of the small European state's high level of dependence on foreign markets, during the 1980s small European state policy-makers developed public images for their states of commitments to both openness and economic programmes based on laissez-faire principles. These policy-makers developed particular patterned habits of expression - ways they desired larger states to perceive their policy-making. As Peter Gourevitch explains,

> The growth of neo-liberalism [has been] in rhetoric and to a lesser degree in reality. In the early 1970s the challenge to consensus came largely from the left in demands for more democratization of the economy: workers' control, co-management, union investment funds, equality of income. A decade later the focus has shifted to themes of productivity, renewal, job creation, rationalization, and restoring competitiveness.[5]

6.2 From Rhetoric to Reality: Examining Interventionism in Denmark, Ireland, Sweden, and Switzerland during the 1980s

Of the four case studies, Switzerland was the best example of a small European state that limited its use of State policies to stimulate international competitiveness. Despite having subsidised the watchmaking industry in earlier years, during the 1980s direct defensive subsidies were hardly used; instead, its limited direct forms of industrial intervention were conducted primarily through regional policies implemented by the cantons. Even so, Switzerland did not follow a truly "liberal" approach; Switzerland did have various forms of policy-making, and the Swiss market was not particularly open.

For the most part, the State attempted to influence industry through aggregate measures that affected all sectors equally, notably monetary policies and favourable corporate tax rates. Switzerland's societal disdain for inflation resulted in a distinctly Swiss form of State intervention: active monetary policies that attempted to (a) suppress inflation through monetary aggregates, (b) maintain exchange rate stability, and (c) keep real interest rates low for strong finance-industry relations. Under this strategy, Switzerland was able to maintain its status as an international financial centre.

At the same time, while not employing significant resources on labour market policy, Swiss policy-making included highly restrictive immigration laws. In times of recession the State quickly adjusted by closing off its borders, and in times of economic growth, it allowed foreigners to enter the country.

In terms of inward FDI, Switzerland was highly protected by Swiss multinationals who restricted share ownership in order to prevent foreign takeovers.
Giant Swiss firms such as Nestle were protected by Swiss laws on equity ownership, which allowed Swiss companies to differentiate between bearer and registered shares, the

latter of which could only be owned by Swiss citizens.[6] As explained in one British newspaper, "The Swiss legal system allows Swiss companies to be virtually bid-proof."[7]

Moreover, under Swiss law, a company that was more than thirty percent owned by a non-Swiss company did not have the right to acquire real estate in Switzerland. Hence, foreign MNCs could not buy land for the purposes of development; this legal restriction remained another barrier to foreign companies' freedom of operations in Switzerland.

In Sweden the beginning of the 1980s was marked, most notably, by the State continuing to subsidise the ailing shipbuilding industry. Only by the end of the *bourgeois interregnum* in 1982 did direct subsidies to industry end. With the return of the SAP to power, the State pledged to reverse its old policies of defensive subsidisation and nationalisation, "creating favourable conditions" and avoidance of "regulating development in a predetermined way."[8] Such circumlocution translated into other forms of intervention, including various monetary, labour market, and industrial policies. The coordinated effect of these policies was a solid level of growth and a high degree of international competitiveness for Swedish MNCs.

Towards the end of the *bourgeois interregnum* the government attempted to stimulate growth through the two devaluations of 1981 and 1982. Different from Swiss monetary policy, which emphasised retarding inflation, Sweden's monetary policy was geared towards economic stimulation. With the return of the SAP and enhanced economic performance primarily because of the devaluations, the government imposed several labour market and industrial policies. In particular, retraining and mobility programmes provided employment opportunities in those areas where former shipyards were located. The combination of active labour market policies with industrial policies, which provided financial and tax incentives for companies to locate in formerly distressed areas, increased employment and growth in these previously unproductive areas.[9]

During the 1980s the Swedish government attempted to stimulate its enterprises' technological competitiveness by providing significant State R & D funds. On a percentage basis the Swedish State used more of its budget for industrial technological development than any other State in the world. Moreover, as was discussed in Chapter Five, while Sweden and Switzerland were rated first and second in gaining patents abroad per 100,000 inhabitants, they were also third and fourth in restricting non-residents from securing patents.[10]

In addition, similar to Swiss MNCs, Swedish MNCs also had both restricted and free shares. Swedish companies owning property in Sweden were allowed to issue free shares up to forty percent of the share capital or twenty percent of the votes, and purchase of free shares by foreigners required the permission of the Swedish Exchange Control. As T.E. Cooke explains, "This unusual distinction between restricted and free shares has protectionist overtones ... the limitation on foreign purchases of shares in Sweden effectively prevents a hostile takeover by a foreigner."[11] Around three-fifths of the Stockholm bourse's capitalization remained in firm hands, the majority of which was controlled by the Wallenberg family. Only about a fifth of the stock market took the form of unrestricted shares, which foreigners could own but have few or no voting rights.[12]

In a completely different vein from both Sweden and Switzerland, because of Ireland's relatively underdeveloped economy and weak industrial structure, the Irish state remained quite open. While maintaining an industrial policy that featured various tax and capital enticements for foreign MNCs to locate on Irish soil, the State also heavily subsidised a large commercial State sector, although exact figures on subsidisation to particular State commercial enterprises are difficult, if not impossible, to uncover in the literature provided by the government, the Ministry of Industry, or the IDA.[13]

State interventionism in Ireland was directed primarily through the IDA's inward FDI incentives schemes, while monetary and labour market policies were de-emphasised. Because of wage-inspired inflation, Ireland's monetary policies throughout most of the 1980s were based on measures to slow inflation, primarily through high real interest rates. Unlike Sweden, which used labour market policies as a means to suppress unemployment, Ireland had relatively few manpower programmes; instead, the State offered generous unemployment insurance benefits that discouraged unemployed workers from seeking jobs.

Only by the end of the decade under *The Programme for National Recovery* did interventionism become an integral part of the State's effort to improve economic performance and modernise its industrial structure. The *programme* featured a monetary policy to suppress real interest rates, labour market policies to retrain yesterday's unemployed workers for tomorrow's employment opportunities, and an active industrial policy geared to building sunrise sectors through more selectively targeted inward FDI promotion.

Throughout the 1980s in Denmark, the State continued to subsidise the ailing shipbuilding industry, providing significant funding to a sunset industry. Despite these defensive subsidies, the Danish State insisted that it was not granting "crisis" support or "aid to enterprises in difficulties;" it instead was providing "sectoral measures."[14] While the State provided these defensive subsidies, national subsidy limits imposed by international and EC rules were not surpassed. Indeed, the Danish State spent a significant proportion of its budget on its welfare state, yet there were few policies that integrated these social policies with other forms of policies to spur employment opportunities, as in Sweden.

Unlike the other three case studies, the Danish State was relatively passive in developing any form of policy-making. Monetary policies to inhibit inflation were ineffective primarily because of wage drift (in contrast to the experience of states such as Switzerland); as a result, Danish monetary policy throughout much of the 1980s was restrictive, while in nearby Sweden monetary policy-making stimulated growth. Moreover, even with high levels of unemployment, the Danish State had relatively few labour market programmes designed to create employment, as did the Swedish State. Instead, a generous unemployment insurance programme decreased incentives for Danish labour to work. Finally, even with a relatively weak industrial structure, Danish industrial policy-making was centred on defensive subsidisation to the shipbuilding industry. Beyond this subsidisation, the State had few industrial policies to stimulate growth and renewal of Danish industry; certainly the first half of the decade could be characterised by "persistently liberal" industrial policy-making in Denmark.[15]

Only in the mid-1980s did the Danish State introduce an industrial policy aimed at stimulating Danish industries' technological competitiveness. Yet these policy measures were an example of "too little, too late." Other forms of interventionism were still not actively employed; monetary policies still stifled growth, and there were few if any labour market programmes designed to stimulate employment. The result of such inadequate interventionism was weaker economic performance - unemployment, inflation, a current account deficit, a continuing weak industrial structure, and greater reliance on the EC.

Moreover, unlike small European states with weak industrial structures, such as Ireland, the Danish State had few incentives for foreign MNCs to locate on Danish soil.

According to *The World Competitiveness Report*, out of twenty-two OECD countries Denmark ranked sixteenth in terms of "the extent to which inbound foreign investment is welcome;" Ireland ranked first, Switzerland second to last, and Sweden fourteenth.[16] To a great extent, the high taxation rate in Denmark inhibited inward FDI into the country.

In sum, during the 1980s despite being vulnerable to international political pressures, to varying degrees small states implemented forms of intervention to maintain or augment their levels of international competitiveness. In cases such as Sweden and Switzerland policy-makers publicly stressed their support for openness, but restrictive practices in terms of patents, land ownership, and immigration, as well as strict corporate laws regarding foreign share ownership were less than subtle forms of protectionism. Because Ireland and Denmark had relatively weak industrial structures, different strategies of intervention were followed. While the Irish State provided significant capital and taxation incentives to entice foreign subsidiaries onto Irish soil, the Danish State's relatively high taxation system and lack of incentives failed to bring inward FDI into Denmark.

According to *The World Competitiveness Report*, Ireland ranked last out of twenty-two OECD countries in terms of "the extent to which inward trade is hampered by protectionist policies," while Switzerland, Denmark, and Sweden ranked fourth, fifth, and sixth, respectively.[17] At the same time, small state rhetoric seemed to be paying off. In terms of "the extent to which the [domestic] business community suffers from protectionism abroad," graded from least to worst, Sweden, Ireland, and Switzerland ranked third, fourth, and eighth, respectively. Only the Danish business community seemed to be suffering from foreign protectionism - Denmark ranked seventeenth.[18]

Notably Switzerland and Sweden had state-specific forms of interventionism that during the 1980s engendered successful economic performance and strong industrial structures. In Ireland, only by the end of the decade did interventionism take on a favourable light through *The Programme for National Recovery*. In Denmark, however, the State exercised relatively ineffective policy-making in all three areas examined in the thesis - monetary, labour market, and industrial policies. Only by the end of the decade did Danish policy-makers wisely begin to move away from its past "persistently liberal" industrial policy.

In all cases small state policy-making to stimulate industrial competitiveness was based on augmenting the state's social infrastructure of financing, labour skills, education, and technology, which allowed for favourable, flexible market change. Despite rhetoric claiming that industrial policy-making was not used, that the State followed a "liberal" form of economic policy-making, or that small states were forced to remain open because of their fear of large state retaliation, during the 1980s the successful employment of the various forms of interventionism discussed in previous chapters was a necessity for the small European state. As John Hall and G. John Ikenberry contend in their book on *The State*,

> ...small countries in modern capitalist societies have no choice but to develop State capacity in order to respond flexibly to the market by internal change; they do not have the option of larger states, better insulated from international economic shocks to seek to change the rules of international economic life. However, ... State power depends, at least in part, upon the intelligence, nimbleness, and skill of political actors; if social actors are given particular cards much depends upon the way they play them.[19]

If policy-making was constructively employed, it acted as a necessary complement to working relations between industry, financial institutions, and labour. If intervention was not used effectively, decreasing levels of international competitiveness resulted.

6.3 Small European State International Competitiveness: A Product of the State's Internal Interactive Process

A. Lessons in Studying the Small European State's Internal Interactive Process

This thesis has taken a step beyond the concepts introduced by Peter J. Katzenstein in his book *Small States in World Markets*. Katzenstein has advanced the argument that the small European state attempts to achieve its competitive advantage against larger states by opting against protectionism and direct intervention. The small European state utilises its small size to achieve fluid and effective lines of communication among peak associations, allowing for a flexible response to global economic changes.

This thesis argues that the Katzenstein model ineffectively evaluates small European state political-economic performance by over-generalising at the expense of state-specific analysis. The quadrilateral model developed in this thesis provides a framework that accounts for both the dynamic and the individual nature of states. At the same time, the model does not assume that (1) small European states develop economic programmes based on economic liberalism, (2) they have effective bargaining processes, (3) their small size breeds effective political-economic performance, or (4) all small European states have high levels of international competitiveness. This thesis offers a framework by which these states can be analyzed and their bargaining processes differentiated. Divergences from the Katzenstein model are discussed below.

Interventionism. Previous chapters and former sections of this chapter argued that the small European state did indeed use state-specific policy programmes in the 1980s to stimulate political-economic performance. While several scholars have argued in the political economy literature that small states are forced to develop economic programmes based on laissez-faire principles and openness as a result of comparatively weak international political and economic statures, it has been argued in this thesis that the small state interventionism in the 1980s was consistent with the pressures of the world market and necessary because in most cases small state industries were price takers. At the same time, the impact of such state intervention was not large enough to provoke retaliation.

Corporatism. Many scholars have accepted that corporatism is the competitive advantage necessary for the small European state to remain internationally competitive. However, small European states did not necessarily have "an ideology of social partnership, shared by both business and expressed in national politics," nor was there necessarily "a voluntary and informal coordination of conflicting objectives."[20] Both of these are central tenets to Katzenstein's democratic corporatism. As was shown in previous chapters, during the 1980s the economic performance of Denmark was relatively poor despite most Danish scholars agreeing that domestic interaction in Denmark should be characterised by 'negotiation.'[21] Perhaps most detrimental to the Danish economy was the inability of its actors, particularly its trade unions and industry, to solve difficult economic problems.

Size. This thesis has not accepted that the size of states necessarily brings political-economic success. While the competitive advantage of the small European state is its geographic proximity that breeds actor familiarity, not all small European states were able to use their monocephalic communication advantage to bring high levels of international competitiveness. For example, in both Denmark and Ireland the inability of trade unions and industry to effectively minimise wage drift induced significant wage-inspired inflation. As a result, during most of the 1980s both states were forced to employ austerity policies that hindered economic growth.

State-specific analysis. This thesis contends that the best method of studying small European state political-economic performance is to study each state individually, examining state-specific internal interaction during a particular time period. The internal interactive processes of states are not only dynamic, but each state has different state priorities and societal values. State priorities include such factors as the state's level of economic performance, the strength of the state's industrial structure, and the state's ability to maintain independence and autonomy. Societal values affect the way in which these priorities are pursued - through various state-specific policy preferences and through the role of state actors in facilitating these means. Referred to in this thesis as industrial culture, the unique history and current political, social, and economic positions of states pave the individual path that the state will follow in attempting to maintain or augment international competitiveness.

The communication process. The communication process of actors in each small European state remains unique, though variances in the ability of actors to effectively communicate influence the relative success of political-economic performance. As was expressed in Chapter Two, each state's industrial culture either nurtures or inhibits a general domestic environment under which values and priorities should be convergent for high levels of political-economic performance. Under cooperative relations, interaction between actors is familiar, consultation and exchange is both frequent and orderly, and the policy-making process is typically efficient and effective. However, under detached relations, actor exchange is distant and infrequent; policy-making is usually unproductive and ineffective. Depending upon the level of cooperation or detachment of relations among actors, the small European state fashions a state-specific process of interaction that either breeds or obstructs international competitiveness.

The continuity of relations. The ability of the small European state's major economic actors - industry, financial institutions, labour, and the State - to interact under a system of cooperative relations leads to economic success. Under continuous quadrilateral relations, the small European state is able to fashion a process of interaction characterised by orderly and relatively uninterrupted communication among the state's four major economic actors. A principal actor sets priorities, develops programmes, and implements changes as a result of the power it has garnered through years of development and interaction with other actors. This systematised process is complemented by effective domestic intervention. However, when relations between two or more actors becomes detached, relations become intermittent. Under intermittent quadrilateral relations, the small European state's level of international competitiveness depends on the degree of detachment between and among actors and the effects of this on actor coordination and policy progress.

B. Using the Small European State Interactive Framework: The Case Studies Compared

This thesis has argued and interpreted why some small European states were more internationally competitive than others during the 1980s. In all cases, state-specific interaction was complemented by various forms of domestic interventionism, necessary because of the small state's international vulnerability and its role generally as a price taker. As evidenced by the Swiss and Swedish cases, the degree of international competitiveness of the small European state resulted from its systematised process of internal interaction, derived from its industrial culture, which is composed of both state priorities and societal values. However, as evidenced by the Irish and Danish cases, without the capability for dialogue and communication, and without effective complementary policy-making, the small European state lost the small state competitive advantage necessary to compete for growing markets against larger states.

This section will analyse the interactive processes of each of the four small European states. Following narratives on each of the states will be diagrams that summarise the main points of discussion within the body of the thesis. While Switzerland and Sweden had relatively continuous quadrilateral processes of interaction among important economic actors, in Ireland and Denmark intermittent quadrilateral relations thwarted higher levels of international competitiveness. (See Figure 6.1.)

Figure 6.1

THE NATURE OF RELATIONS AMONG FINANCIAL INSTITUTIONS, TRADE UNIONS, INDUSTRY, AND THE STATE: THE CASE STUDIES COMPARED

	DENMARK	IRELAND	SWEDEN	SWITZERLAND
Financial institution-industry relations, 1980-1987	Relatively cooperative	Detached	Cooperative	Highly cooperative
Trade union-industry relations, 1980-1987	Detached	Detached	Cooperative	Cooperative
State-industry relations, 1980-1987	Detached	Relatively cooperative	Cooperative	Relatively detached
Quadrilateral relations (financial institutions, trade unions, industry, State), 1980-1987	Intermittent	Intermittent	Continuous	Relatively continuous
Quadrilateral relations: forecasting from 1987 into the 1990s	More of the same	More Continuous	Less continuous	Somewhat less continuous

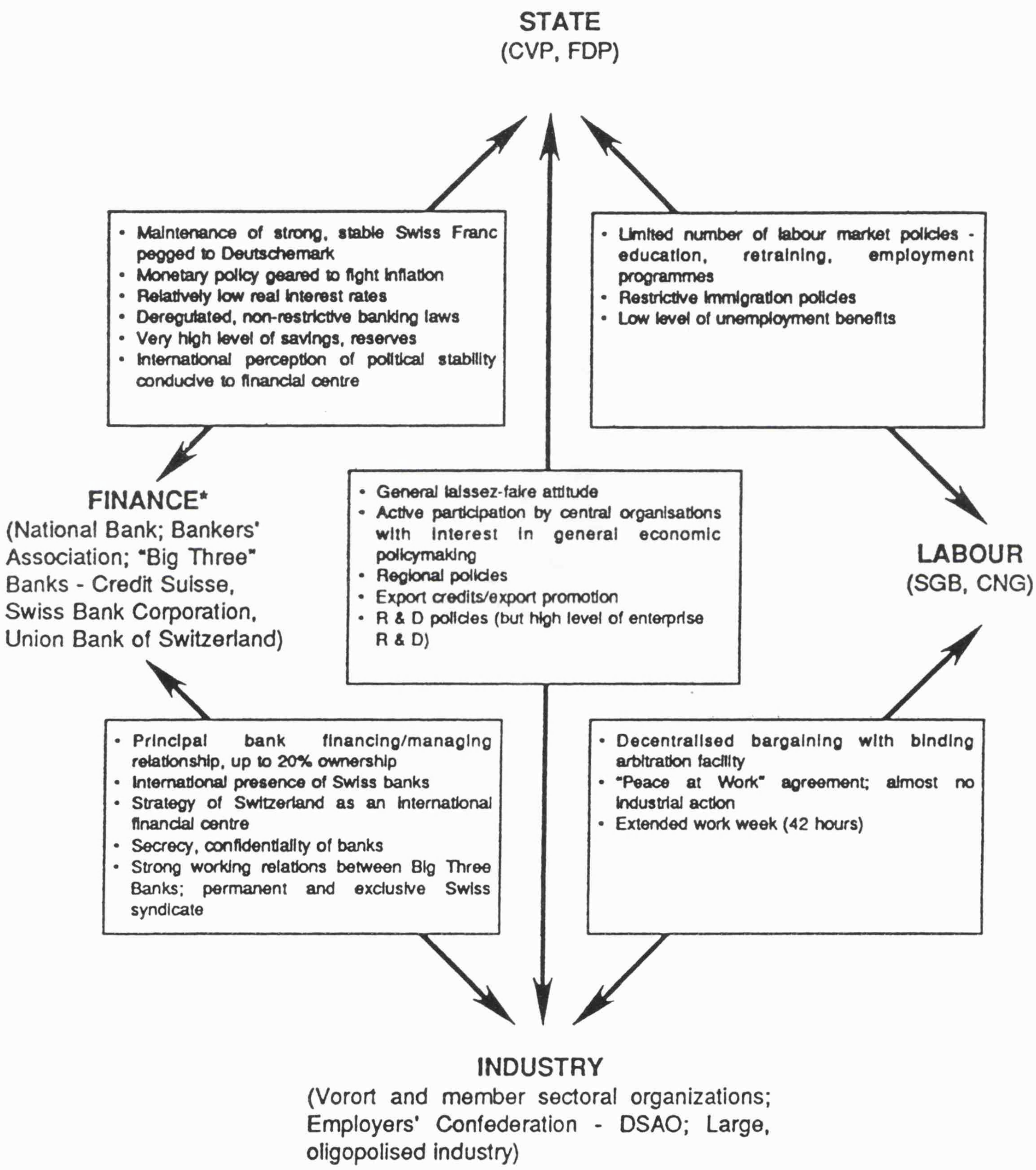
Switzerland. During the 1980s, strong economic performance and socio-political stability bred high levels of international competitiveness in Switzerland. Relations between industry, labour, financial institutions, and the State were marked by a highly systematised interactive process. While the State maintained relatively few labour market policies and limited unemployment benefits, decentralised wage bargaining between labour and industry in Switzerland led to low levels of labour unrest. Wages, though relatively high, grew slowly, and impressive labour productivity as a result of the Swiss work ethic resulted in comparably low real unit labour costs.

Because of the SNB's ability to provide monetary stability through a policy geared to fight inflation yet maintaining relatively low real interest rates, private financial institutions, notably the Big Three Banks, not only continued their strong international presence but were also capable of furnishing necessary industrial investment capital. Ties between Swiss MNCs and financial institutions were reinforced by principal bank financing and managing relationships as well as by the maintenance of high debt-equity ratios by Swiss MNCs. These ratios reduced costs of capital, increased return to equity, induced equity investments in firms, and allowed Swiss MNCS to act more aggressively in the international marketplace. Moreover, such highly leveraged industries ensured financial institution participation in corporate investment decisions. With the Big Banks being able to provide significant capital for industrial investment, large high tech Swiss MNCs such as Ciba Geigy and Hoffman La Roche were able to maintain world market shares through significant capital investment in R & D. At the same time, large Swiss banks such as *Credit Suisse*, Swiss Bank Corporation, and Union Bank of Switzerland, maintaining strong working relations through a permanent and exclusive Swiss syndicate, fostered a strategy for preserving Switzerland's impressive international financial centre. Hence, the commanding ability of the SNB to affect economic policy-making in such a way that monetary policies remained the preferred mechanism for ensuring domestic economic stability was strategically combined with the domestic and international presence of Swiss private banks. This financial institution coalition stimulated high levels of economic performance and helped Swiss industry remain highly competitive in world markets.

In sum, relations among important economic actors within Switzerland from 1980 to 1987 were typically cooperative; the process of interaction among financial institutions, industry, labour, and the State could for the most part be characterised as continuous quadrilateral. Nonetheless, as will be discussed in the following section, by the end of the decade Switzerland faced increasing political, social, and economic obstacles which would test its ability to maintain the very high standards it had set in previous years. (See Figure 6.2.)

Figure 6.2

THE SWISS INTERACTIVE PROCESS (1980 - 1987)



* Denotes Principal Actor

Sweden. After the *bourgeois interregnum* ended in 1982, Sweden also maintained a solid level of economic performance coupled with socio-political stability. The Swedish interactive process remained highly systematised, in which industry, financial institutions, and labour actively worked together to induce higher levels of international competitiveness.

With a monetary policy geared to stimulate growth primarily through devaluation, relations between financial institutions and industry in Sweden were encouraged. The sphere structure of industry ownership by financial institutions provided strong links between the two; for example, Sweden's largest bank, *SE Banken,* and largest company, Volvo, maintained close ties as a result of this structure. Cross board directorships between banks and industry and highly leveraged Swedish MNCs also ensured strong finance-industry relations. Under such conditions, Sweden's largest banks, *Se Banken*, *Svenska Handelsbank*, and *PK Banken*, were capable of furnishing capital to large high tech Swedish MNCs, such as Alfa Laval, Atlas Copco, Electrolux, and Ericsson, for important R & D financing.

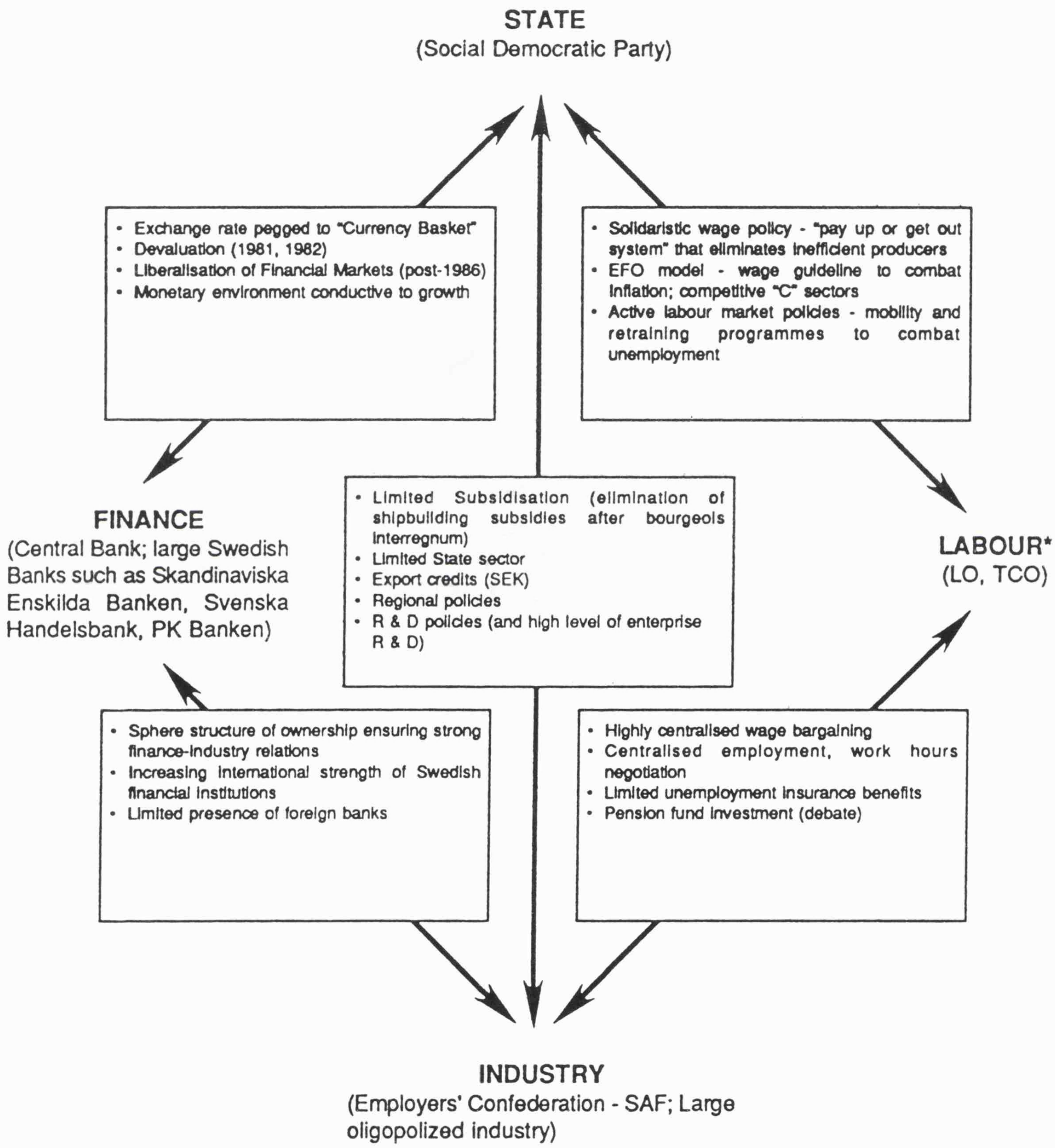
As a consequence of Sweden's communitarian ideology, the essential catalyst of the Swedish economy was labour, notably the LO. Under the Solidaristic Wage Policy, which attempted to maintain wage equality, previously agreed to and sector-specific wages forced firms to pay particular wages. The Solidaristic Wage Policy had three effects. First, it resulted in a highly concentrated industrial structure, in which only large and efficient enterprises survived these wage pressures. Second, it forced Swedish industry to possess an exceedingly productive workforce in which Swedish real unit labour costs remained relatively low. And third, it forced firms to be innovative in order to be able to pay these relatively high wages and at the same time maintain competitiveness in world markets.

The Solidaristic Wage Policy was necessarily complemented by the most comprehensive labour market programme in the OECD. Retraining and mobility schemes acted as obligatory concomitants to the competitive pressures induced by the Solidaristic Wage Policy. During the 1980s these corresponding policies strengthened Sweden's level of international competitiveness; the Swedish State continued to provide significant welfare state measures, the Swedish standard of living continued to be impressive, unemployment was scarce, and growth was vigorous. Moreover, Sweden's large, high tech MNCs continued to remain highly competitive in the world market.

In sum, relations among important economic actors in Sweden from 1980 to 1987 were typically cooperative; the process of interaction among financial institutions, industry, labour, and the State could for the most part be characterised as continuous quadrilateral. (See Figure 6.3.) However, as will be discussed in the following section, by the end of the decade bilateral relations, particularly between labour and industry, became increasingly detached, resulting in a major wage-price spiral.

Figure 6.3

THE SWEDISH INTERACTIVE PROCESS (1982 - 1987)



* Denotes Principal Actor

Ireland. Different from both Sweden and Switzerland, Ireland's economic performance was mediocre during the 1980s, having been plagued with unemployment approaching twenty percent, high amounts of inflation, a current account deficit, and large amounts of foreign debt. Certainly Ireland's lower level of industrialisation, semi-peripheral location, and weak infrastructure could explain much of the reason for its domestic employment problems and the lack of international competitiveness of its indigenous industry. However, throughout most of the 1980s the Irish interactive process involving industry, financial institutions, labour, and the State did not effectively stimulate an environment conducive to generating higher levels of economic performance.

From 1980 to 1987 decentralised wage negotiations engendered increasing levels of labour unrest and wage drift. Inflation continued to be a problem through 1987 as a result of a wage-price spiral. Unlike small European states such as Switzerland, which utilised a binding arbitration mechanism, wage differences between labour and the private sector were handled under a non-binding system.

Wage inflation was also accompanied by high levels of unemployment and emigration. In contrast to small European states such as Sweden, which emphasised retraining and mobility programmes, the Irish State provided significant unemployment insurance benefits without incentives to work, while limiting its manpower programmes. Even though

Ireland's educational system was highly effective in training its large population of youth, emigration from Ireland was extremely high. As a consequence, "brain drain" sapped Ireland of perhaps its greatest resource - its well educated, abundant supply of youthful workers.

Irish financial institution-industry relations also remained relatively weak. Despite a monetary policy geared to fight inflation in which real interest rates remained high, some of the larger Irish enterprises did maintain some banking relationships with the largest Irish banks, notably the Bank of Ireland and the Allied Irish Banks. Yet for the most part relations between Irish industry and financial institutions was patterned in the British and American "separatist" style of banking; board directorships were not mixed between banks and industry but were rather strictly divided. Irish industry was not afforded the same financing and managing benefits that its counterparts in Switzerland and Sweden were in their principal bank and sphere relationships.

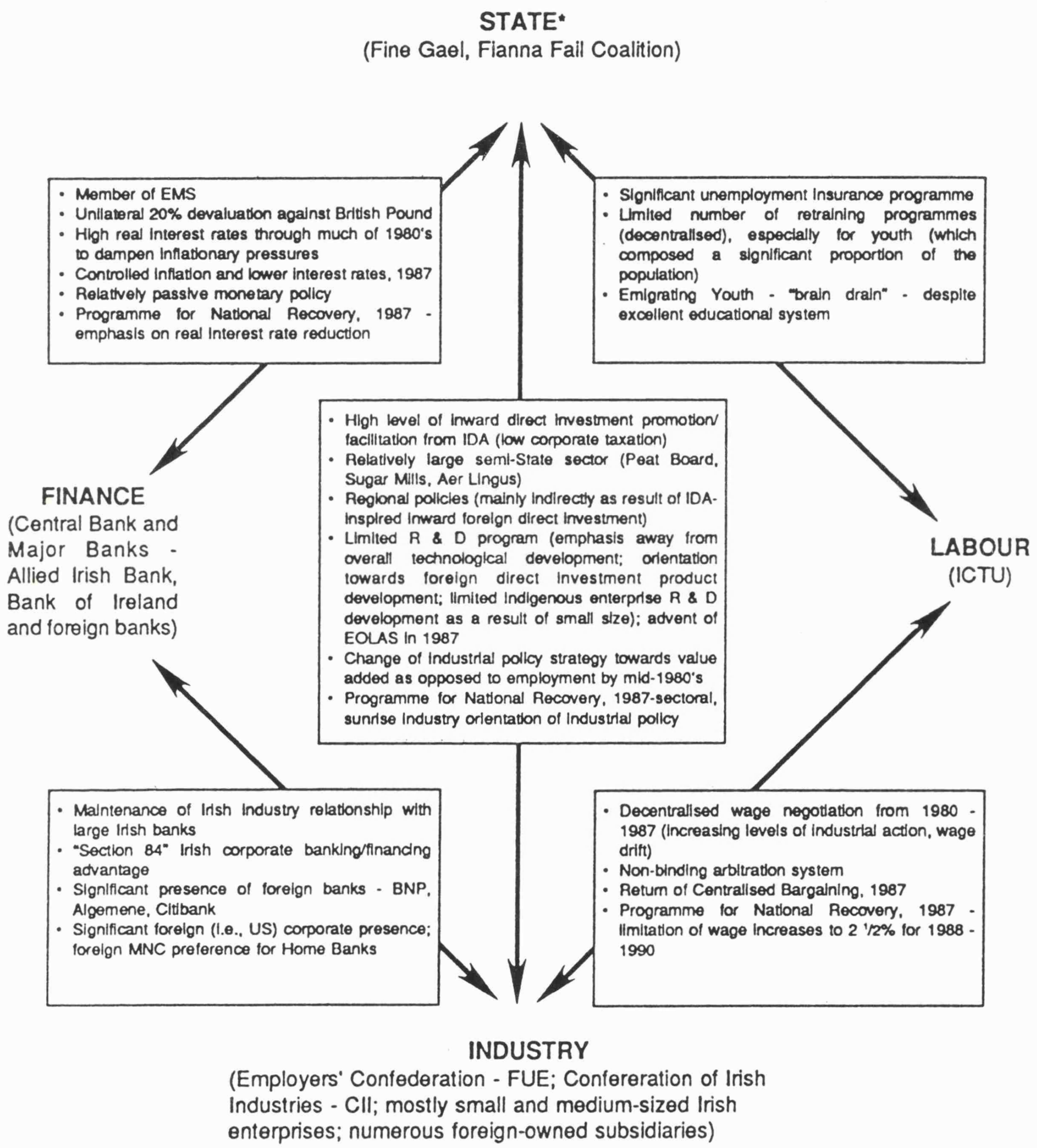
Given Ireland's weak industrial structure, the State acted as the principal actor in attempting to revitalise its sagging economic performance and enhance its industrial structure. Because of programmes designed to entice inward FDI onto Irish soil, foreign subsidiaries tended to locate inside the country. However, Irish indigenous industry was not capturing the technological benefits from the sunrise industry plants operating in ireland. Moreover, while the IDA attracted various high tech industries to Ireland, operations were either ephemeral or a single, unrelated step in a company's vast operations.

By the mid-1980s, however, the opposition *Fianna Fail* party along with the CII, ICTU, and FUE - the so-called "social partners" - devised a plan to attempt to rejuvenate the languid Irish economy. Through the State's *Programme for National Recovery* under *Fianna Fail* leadership, from 1987 to 1990 the ICTU agreed to limit wage increases to two and one-half percent per year. The Irish policy would stress control of inflation while reducing real interest rates (a possibility now that wage growth was limited) in order to inspire capital investment and improve relations between financial institutions and industry. Finally, the State's industrial policy strategy changed towards value added rather than employment. Focus would be on elevating specific sunrise sectors by carefully scrutinising the technology transfer effects of inward FDI projects.

Thus, from 1980-1986 while the Irish State attempted to modernise its industrial structure by inducing foreign subsidiaries, the lack of technological knock-off effects did not result in an improved indigenous industrial structure. Moreover, with significant levels of labour unrest, wage drift, emigration, and unemployment, economic performance did not improve. However, with coordination and consultation among the "social partners" by the mid-1980s, Ireland began a constructive course of action, one which intended to stimulate economic performance and strengthen its industrial structure.

In sum, relations among important economic actors in Ireland from 1980 to 1987 were often detached, particularly between industry and labour. The process of interaction among financial institutions, industry, labour, and the State could for the most part be characterised as intermittent quadrilateral. (See Figure 6.4.) However, as will be discussed in the following section, by the end of the decade relations among these actors, particularly between labour and industry, became increasingly cooperative. Under the *Programme for National Recovery*, the historical wage-price spiral was controlled under a collective agreement to dampen wage growth.

Figure 6.4
THE IRISH INTERACTIVE PROCESS (1980 - 1987)



* Denotes Principal Actor

Denmark. Despite maintaining a high standard of living, Denmark's economic performance was relatively poor during the 1980s, and its industrial structure continued to be significantly weaker than that in Switzerland and Sweden. Much of the reason for Denmark's declining levels of international competitiveness during the decade can be attributed to a confused interactive process among industry, financial institutions, labour, and the State.

Because Denmark's monetary policy was geared to fight its current account deficit and inflation throughout most of the 1980s, the domestic monetary environment in Denmark thwarted close financial institution-industry relations. Nonetheless, industry did maintain links with financial institutions through principal bank relations between particular banks and enterprises, and similar to Swedish and Swiss MNCs, Danish businesses remained highly leveraged, which facilitated close bank-industry association. However, in contrast to both Sweden and Switzerland, because Denmark had a domestic monetary environment detrimental to growth, in which real interest rates remained high, these relations were severely stifled throughout much of the decade.

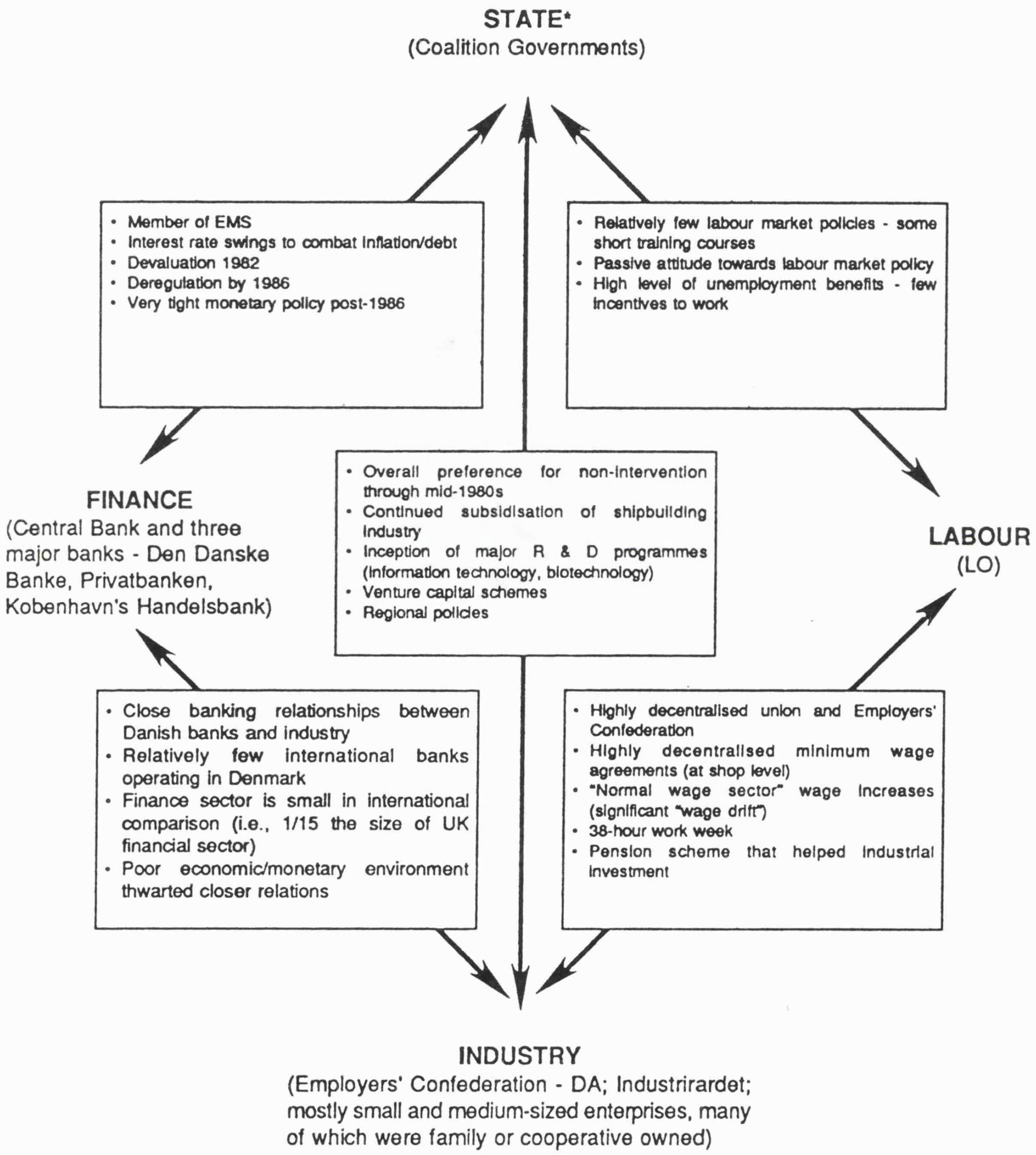
Under a system of wage negotiation mixed between centralisation and decentralisation, wage drift continued to be a problem in Denmark. While Denmark experienced a wage-price spiral, it also faced major unemployment problems; however, different from Sweden, Denmark had few labour market policies, opting instead for an unemployment insurance programme that provided significant benefits for the unemployed worker with little motivation to return to the workplace. Having emphasised its welfare state, Denmark was unable to devise a formula that could balance its communitarian principles with economic efficiency. Neighbouring Sweden, which had similar societal values, did equate egalitarianism with equality, using a solidaristic wage "equal pay for equal work" scheme with complementary labour market programmes that provided employment opportunities made necessary by the competitive pressures of the wage policy.

Moreover, the Danish State's relatively passive attitude towards monetary and labour market policy-making pervaded into industrial policy-making; even with a relatively weak industrial structure, Denmark had few industrial policies. While holding the advantage over other European states of not having big sunset sectors, such as the coal and steel industries, the Danish State industrial policy, nevertheless, was primarily composed of subsidisation to its sunset shipbuilding industry.

While maintaining an overall preference of non-intervention, by the middle of the 1980s a group of Danish policy-makers and industrialists - the so called "industrial modernists" - began to realise that the state's industrial structure, composed primarily of small- and medium-sized enterprises, was technologically deficient. Perceiving that Denmark's greatest competitive disadvantage was its weak industrial structure, the State acted as the catalyst - the principal actor - in fostering programmes, notably in bio-technology and information technology, designed to stimulate technological advancement in industries.

Despite the State's initiating these constructive steps by the mid-1980s, significant economic problems continued to inhibit Denmark's economic performance. The trade unions and industry continued to lack the ability to bargain effectively, resulting in wage-inspired inflation and labour unrest. Still maintaining significant levels of unemployment and inflation, a current account deficit, and high levels of debt, the State attempted to maintain its welfare state commitment through substantial personal and corporate taxation as well as high real interest rates. Under such deleterious conditions during the decade, and with generally detached relations among industry, financial institutions, labour, and the State to combat these problems, such highly intermittent quadrilateral relations resulted in deteriorating economic performance. (See Figure 6.5.)

Figure 6.5
THE DANISH INTERACTIVE PROCESS (1980 - 1987)



* Denotes Principal Actor

6.4 The Small European State In the 1990s

A. The International Pressures of the 1990s: Increasing International Competition and Europe "1992"

This section will briefly examine the prospects for maintaining or augmenting small European state international competitiveness in the 1990s. The international marketplace of the 1980s was characterised by increasing competition primarily from Asia. The presence of such NICs as South Korea, Hong Kong, Taiwan, Singapore, Malaysia, and Thailand will further press industries in small European states for world market shares.[22]

Perhaps the single most important pressure that the small European state will face during the 1990s will be the continuing cooperation of European states within the Common Market. Under the Single European Act, the twelve EC member states will attempt to bridge state policies and practices to create a single market by the end of 1992. While arguments vary as to how European unity might affect particular member states, there is little doubt that the primary effect on the small European state will be on its ability to maintain political autonomy and economic independence. While the EC will offer meaningful benefits to member small European states, it will test the ability of each State to develop and implement state-specific policies to maintain or augment its level of international competitiveness.

By the latter part of the 1980s industrialists in

Europe and around the world formed strategies as a result of this European unification process. Under a possible scenario in which product specifications and government regulations become standardised, the Europe of the 1980s characterised by fragmented markets could be transformed into one that would be increasingly consolidated and concentrated. Indications already existed by the latter part of the 1980s that consolidation through merger and acquisition was occurring[23] in such industries as pharmaceutical products, financial services,[24] and telecommunications.[25] Moreover, merger and acquisition activity by non-EC MNCs in the European market increased dramatically as a result of the fear of a closed European market;[26] in 1988, mergers and acquisitions jumped by twenty-five percent from the preceding year.[27]

For the small European state whose industries tend to be price takers, a more concentrated and consolidated European market will bring further challenges for their industries to remain competitive in world markets in the 1990s. Uncertainty over a possibly barrier-free Common Market and its consequences provoked policy-makers and industrialists in non-member small European states, such as Sweden and Switzerland, to reconsider their industrial strategies. By 1987 large Swiss and Swedish MNCs were gaining footholds in the European market through vast acquisitions. For other small European states with membership in the EC but with weaker industrial structures, such as Denmark and Ireland, industrial strategies for the future will differ; these states' policy-makers and industrialists will stress gaining *niche* market shares and enticing foreign subsidiaries into their state markets through their affiliation with the EC. Because of differences in industrial structure, out of fifteen European countries, Switzerland ranked fourth, Sweden sixth, Denmark eighth, and Ireland eleventh in a survey that asked industrialists and state policy-makers to rate states by their preparation for Europe 1992.[28]

Hence, during the 1990s the small European state will face expanding competition, not only from the U.S. and Japan, but notably from Asia's NICs and from the pressures of the increasingly unified Europe. Small European states will be increasingly challenged to avoid penetration of those foreign markets in which their industries have gained shares. Increasing competition from such rising economic powers as South Korea, Singapore, Hong Kong, and Taiwan, and possible dilution of their economic power from an increasingly concentrated and consolidated European market, will further test the ability of small European state industries to remain internationally competitive. How small European states will react to these competitive pressures to maintain a prosperous economic environment coupled with political stability, and how the small European state's industries will respond to these international pressures, are briefly discussed below.

B. Into the 1990s: The Case Studies Examined

Switzerland. Of the four case studies, Switzerland was the best example of a small European state during the 1980s that was able to integrate successfully state priorities with societal values. Despite some international pressures to change its financial practices and anxiety with regard to EC membership, there is little indication that the political-economic stability of Switzerland in the 1980s will degenerate in the following decade.

With financial institutions historically acting as the catalyst for Switzerland's high level of international competitiveness, perhaps the most significant question will be whether its financial institutions will be able to hold the same amount of authority and influence in the Switzerland of the 1990s as they did in the previous decade. By the end of the 1980s Switzerland experienced inflationary pressures because of an uncharacteristically lax SNB monetary policy; under conditions of high growth, the Swiss Franc remained unusually low, which despite helping Swiss exporters, tarnished Switzerland's matchless reputation as a safe haven for foreign investors to deposit their money.[29] Switzerland's historically distinct and successful financial practices will also be challenged in the 1990s. Secrecy, a trademark of Swiss banking, was significantly strained not only from external pressures as a consequence of the Iran-Contra affair, but also under the so-called "Koppgate" affair, which involved a Swiss bank, the Minister of

Justice, and money derived from drug trafficking.[30] Indeed, the lack of inflation, a strong and stable Swiss Franc, and banking secrecy remained the roots of Switzerland's international financial success in the 1980s but may require some adjustments in the 1990s.

Moreover, during the 1990s Switzerland will no longer be virtually alone among financial communities with universal, deregulated financial systems as it was during most of the 1980s; a giant worldwide deregulation process transpired by the mid-1980s, and this process should continue throughout the 1990s. Several states that achieved increasing economic strength during the 1980s will also compete with Switzerland as alternative international financial centres, not only other small European states such as Luxembourg, Belgium, and the Netherlands, but also such Asian NICs as Singapore, Hong Kong, and Taiwan.

As the EC continues to work towards greater economic, monetary, and financial union, there will be greater financial market competition within Europe; Switzerland's financial system and practices will be forced to be modified to ensure that Switzerland's own legislative framework does not impede Swiss banks to integrate into the European financial system.[31] The Cartel Commission has initiated steps to investigate the permanent and exclusive Swiss syndicate in the Swiss capital markets, much as result of Switzerland's fear of potential obstacles to access in the financial markets of EC states. Steps for reciprocal access to insurance markets between the EC and Switzerland were initiated by the end of the 1980s.

Moreover, while during the 1970s and much of the 1980s Swiss industries had followed internalisation strategies for growth, fear of fortress Europe has caused Swiss firms to recast past industrial strategies, stepping up investment in industries within the Common Market. For example, from 1987 through 1989, Swiss MNC acquisitions of European firms included Nestle's purchase of Britain's Rowntree and Italy's (and France's) Buitoni, Jacobs Suchard's of Belgium's *Cote d'Or* and Greece's Pavlides Chocolates, and Brown Boveri's of Italy's Sadelmi.[32] At the same time, Swiss financial institutions have sought to become larger in the European market: acquisitions included Swiss Reinsurance's purchase of Italy's Lloyd Adriatic, Zurich Insurance's of Spain's Union Iberoamericana, and Swiss Bank Corporation's of Britain's Savory Miln.[33]

All of these changes - from Switzerland's reformed financial system to altering industrial growth strategies - seem to underscore changes in Switzerland's historical ability for almost complete independence and autonomy. As further evidence, Swiss MNCs' less than subtle historical form of protectionism by restricting share ownership has begun to change; Switzerland's most celebrated company, Nestle, has awarded equal registered share rights to Swiss citizens and foreigners.[34] Moreover, by the end of the 1980s its acclaimed socio-political stability was challenged. High levels of drug addiction, evidenced by Zurich's *Platzpromenade* (a park where drug use has been legalised), has highlighted Switzerland's continued integration into the world's darker side, and on a per capita basis, Switzerland has the highest level of AIDS in the world.[35] Despite all of these diversions, if the 1980s were any indication of how flexible a state's actors can be to conform to changing international economic conditions, Switzerland will successfully adjust.

Sweden. While also enjoying a relatively high level of political and economic success in the 1980s, Sweden will be pressed to maintain the same degree of international competitiveness in the 1990s. Sweden's biggest problem in the latter part of the 1980s, and one that will most likely continue into the 1990s, is the ability of its powerful unions to gain higher wages. Under conditions of high growth in the 1980s, by the end of the decade high levels of personal consumption inspired significant inflation; with factories running at full capacity and a continuing strong demand for labour, a wage-price spiral was generated.[36]

During the 1980s the trade unions remained the catalyst of the Swedish economy through a complementary wage - labour market policy that engendered high levels of labour productivity and an innovative and concentrated industrial structure. As a result of this labour market scheme and the EFO model that attempted to gauge wage growth with inflation, while real wages were comparably high, high levels of productivity produced relatively low real unit labour costs. Yet by the end of the decade levels of working time decreased, labour absenteeism increased, and most importantly, unions demanded higher wages. As a response to wage pressures, by the latter part of the 1980s Swedish monetary policy-makers dampened growth by increasing real interest rates.

Consequently, by the 1990s the Swedish trade unions will be forced to exercise wage moderation or face decreasing levels of growth similar to their Scandinavian neighbour Denmark. Much of this will depend on a possible overhaul of the Swedish tax system, which in the past had boosted inflation and depressed incentives to work, yet remained a necessity to pay for its welfare state. However, signals from the 1980s indicate that the Swedish taxation system might be modified; tax revenues will not decrease, but personal taxation rates will be reduced while former tax loopholes will be removed.[37]

In terms of financial institutions, the powerful financial sphere structure of the 1980s will be meaningfully reduced in the 1990s as a result of the increasing securitisation of the Swedish financial markets. By the middle of the 1980s, Swedish monetary authorities began to ease restrictions on foreign share purchases and other forms of deregulation, such as the lifting of foreign exchange controls.[38] Similar to Switzerland, the Sweden of the 1990s will be forced to be more open, to enact legislation in line with that of EC countries.

Most important, Swedish industries have already responded to the market pressures engendered by Europe 1992. During the 1980s Sweden's powerful MNCs had grown through internal development, rarely acquiring foreign enterprises. Yet by the end of the decade, Sweden's fear of a protected European market initiated a Swedish MNC European buying spree similar to that of Switzerland's largest enterprises. In order to gain a foothold in the European market, Swedish MNCs were involved in a number of mergers and acquisitions: Volvo's purchase of Britain's Leyland Bus Group, *Svenska Cellulosa*'s of France's *Peaudouce*, Iggesund's of Thames Board of Britain, and *Euroc*'s of Britain's Castle Cement.[39] The most prominent merger occurred between Sweden's ASEA and Switzerland's Brown Boveri - the combination of these already large MNCs was a means to create a pan-European electrical machinery company.[40] Even within Sweden a further concentration of Swedish industry occurred by the end of the 1980s; sectors such as forestry and building were consolidated into blocks, "an interesting example of a change in attitude of the tightly knit web of Swedish industry."[41]

Consequently, similar to Switzerland, Sweden has strengthened its industries' already powerful position in the European market through a significant acquisition spree. Such moves illustrate how disproportionately powerful Swedish multinationals have been in comparison to its country size. Yet the problem of the 1990s at this time appears to be whether Sweden's principal actor of the 1980s, labour, will continue to be as productive in the 1990s. Indications from the latter part of the decade point to mounting labour costs with decreased levels of productivity, the combination of which would not only incite a tightening of monetary supply, but even further inflation and reduction of growth.

If economic performance deteriorates in Sweden, or in Switzerland, and with fear of possible economic isolation, policy-makers in these states will have little choice but to consider membership in the European Community.[42] Different from Austria, which submitted its application for EC membership in 1989, during the 1980s Sweden and Switzerland maintained solid economic performances coupled with powerful industrial structures that bred economic independence. Only under conditions where Swedish or Swiss international competitiveness degenerated, or European integration progressed to the point where Swedish and Swiss participation was excluded in the European market, would either state seek membership in the EC.

Ireland. Throughout much of the 1980s Ireland struggled with a number of economic problems, notably unemployment, inflation, a significant foreign debt, and a high degree of emigration. Yet in 1987 the Irish State initiated constructive steps through *The Programme for National Recovery*, which suppressed wage growth and set new industrial policy priorities. While it is too early to evaluate Ireland's industrial policy changes from the *programme*, wage-inspired inflation has decreased. In addition, under the *Taoiseach* Charles Haughey, the *Fianna Fail* government initiated an austerity programme to bring the economy under control and halt the outflow of capital, which by the end of the decade seemed to be paying off. In 1987 and 1988 exports surged by fourteen percent and eight percent, respectively, unemployment decreased to seventeen percent (the first fall in unemployment in almost a decade), GDP growth remained at around four percent in 1989, and most important, inflation stabilised to just over three percent.[43] Yet while the *Fianna Fail* government seemed to be enjoying significant popularity, by the end of the 1980s an election by Haughey to gain a majority in the *Dail* failed.[44] An unprecedented coalition government has since ensued. As a consequence, by the beginning of the 1990s Ireland will face difficult, unexpected political pressures.

Irish industrial policy, which changed courses (at least in rhetoric) by targeting specific sunrise industries and ensuring that carefully scrutinised inward FDI would effectuate industrial technology transfer, will be faced with mounting pressures from the increasingly harmonised European market. While there is little question that a unified Europe can lead to more efficient European industry through rationalisation and concentration, smaller and less developed economies within the market, such as Ireland, if not backed by the Community through structural funds, face increasing economic vulnerability.[45] Such concerns have been recognised by Irish policy-makers because of Ireland's already weak industrial structure, inferior infrastructure, and semi-peripheral location in comparison to the rest of Europe.[46]

Hence, the 1990s will pose continued economic challenges to Ireland; it should continue on the course the State initiated in 1987 to overcome major economic problems, notably its foreign debt and unemployment. The 1987 *Programme for National Recovery* was an excellent example of valuable State intervention that resulted in improved economic performance. The 1990s will further test whether the "social partners" - the State, ICTU, FUE, and CII - will be able to continue this progress, suppressing wage-inspired inflation, limiting real interest rates, and pinpointing State industrial priorities in sunrise sectors. The State will also have to improve on some primary weaknesses, enhancing its infrastructure and preventing the emigration of its highly educated youth. Most importantly, Ireland will face its most serious challenge from a more unified European market; its already fragile economic independence as well as its political autonomy will be tested in an increasingly competitive and concentrated European market.

Denmark. Throughout the 1980s Denmark was plagued by significant wage drift, and without the ability of the LO and the DA to negotiate effectively lower wages in the 1990s, there will be little hope for improved economic performance. Moreover, from 1988 to 1990 only New Zealand ranked worse than Denmark among OECD states in terms of employment change; Denmark's employment actually decreased by 2.6%, while all other OECD countries (with the exception of New Zealand) experienced employment growth.[47] The dual problems of inflation and unemployment continued throughout the 1980s without significant constructive government intervention. There were not any labour market policies to combat unemployment, as in Sweden, and the government did not intervene in wage negotiations, as in Ireland. According to a poll taken in 1989, a vast majority of Danes would support government intervention to reduce wage increases; this included forty-four percent of the *workers* questioned.[48]

The Danish State's inability to use various forms of intervention throughout nearly all of the 1980s inhibited improvement in economic performance. Indications from the end of the 1980s point to increasing State intervention, notably through industrial policies to stimulate technological competitiveness. Yet such steps must be coupled with interventionism that would slow inflation and generate employment. Hence, two forms of intervention seem felicitous: government involvement to suppress wage-inspired inflation and labour market policies to promote employment (as opposed to simply furnishing significant unemployment insurance benefits).

At the same time, Denmark's relatively weak industrial structure will need to be strengthened. While non-EC small European states such as Sweden and Switzerland strengthened their industrial presences in the Common Market through merger and acquisition, Denmark's relatively weak industrial presence obviates the need for such actions. Different from both the Swedish and Swiss industrial strategies for the 1990s, by the end of the 1980s Danish industrial strategies appeared to be oriented towards market expansion in *niche* products by using its technology programmes to remain competitive in distinctive areas, such as bio-engineered products like enzymes produced by such Danish firms as NOVO. Moreover, being the only Scandinavian country in the EC, by the end of the 1980s Danish industries and financial institutions began to emphasise Danish links with the EC to its Nordic neighbours in order to entice Scandinavian inward FDI into Denmark.[49]

Consequently, Denmark will face two significant challenges in the 1990s. First, it must overcome domestic economic problems, most notably wage drift, in order to generate higher levels of growth and productivity and overcome its ageless current account deficit and foreign debt. Second, Danish enterprises must devise constructive industrial strategies conducive to strengthening Denmark's relatively weak industrial structure. While being a member of the EC, Denmark's economic problems will not be overcome simply through EC membership; as an example, the significant benefits Denmark historically accrued from the CAP began to change by the end of the 1980s as a consequence of CAP reforms, and there is little indication that the EC will further provide extraordinary assistance to the Danish agricultural sector relative to other EC states during the 1990s.[50]

The increasing harmonisation of Europe will also pose new problems not only for Danish industries attempting to attain *niche* markets, but also in the Danish State's ability to enhance domestic economic conditions for improved industrial activity. For example, Denmark has had among the highest tax rates in the EC; EC tax harmonisation would most certainly necessitate a lowering of Danish taxes, severely straining the Danish State's ability to finance its expensive welfare state. Yet such a measure may be the necessary challenge for Denmark to adjust to the pressures of the 1990s - being forced to better equate its societal value of egalitarianism with higher levels of efficiency.

C. Lessons From the 1980s: The Small European State in the International System In the 1990s

Despite limited political power, economic necessity dictated that during the 1980s the small European state had little choice but to employ state-specific forms of interventionism to remain internationally competitive. Small European state interventionism and state-specific actor interaction materialised in various forms throughout the 1980s, including monetary policies, labour market policies, industrial policies, trade policies, and even overtly protectionist practices to impede inward foreign direct investment. In the 1990s small states will be continue to be compelled to use domestic interventionism to stimulate economic and industrial performance.

By the end of the 1980s the principal focus of policy-makers, industrialists, and academics concerned with the future of the European economy was on the unification of the Common Market projected for 1992. However, the lessons of the 1980s indicate how vital *state-specific* actor interaction and domestic interventionism was to remain internationally competitive in the international marketplace. It should not be construed that a state-specific process of interaction is an advantage for small European states to remain internationally competitive, since an implicit assumption in this thesis is that all states have state-specific means to attempt to achieve high levels of political-economic performance. Rather, a vital message in this thesis is that in *studying* small European states, rules cannot be made for every state. The lessons of the 1980s demonstrate that, if utilised successfully, the small European state's competitive advantage against larger states with greater natural and human resources was its geographic proximity that generated actor familiarity; intimate relations among industry, financial institutions, labour, and the State; the guidance of the economy by the state's principal actor; and state-specific policy-making.

This message from the 1980s illuminates the necessity of the small European state to attempt to maintain its economic independence, utilising its size to facilitate a systematised process of interaction coupled with constructive policy-making. The examples of Switzerland and Sweden illustrate how successful small European state interaction and interventionism could promote high levels of international competitiveness and consequent economic independence and political autonomy. The Danish and Irish examples, however, demonstrate that misdirected policy-making and a confused process of interaction in the small

European state could generate a lower degree of economic independence.

In sum, the 1990s will test small European state industries - usually price takers - to remain competitive not only in a world market characterised by aggressive competition from Asia,[51] but also in a more consolidated and concentrated European market. Such pressures will test the ability of small European states to use their state-specific processes of interaction and intervention to maintain or augment their foreign market shares, both within and outside Europe.

While the European market of the 1980s was characterised by segmentation, during the 1990s a more integrated European market under conditions of increased internal competition will foster the potential for increasing consolidation and concentration of production and distribution structures. Having been able to use state-specific forms of intervention in the 1980s, small European states will be challenged to continue to use state-specific intervention under a more active and intervening European Community. In this respect, the small European state will be challenged to maintain economic independence and political autonomy in an increasingly unified Europe.

Notes for Chapter Six

1.John Gerard Ruggie (1983) "International Regimes, Transaction, and Change: Embedded Liberalism in the Postwar Economic Order" in Stephen D. Krasner, ed. *International Regimes*: 214.

2.See Paul Krugman (1988) "New Thinking About Trade Policy" in Krugman, ed. *Strategic Trade Policy*: 1-22.

3.Evidence from the four case studies suggests that the State promoted what David Baldwin terms "positive sanctions," such as subsidies to exports, providing capital aid, investment guarantees, favourable taxation, and encouragement of private capital exports. David A. Baldwin (1985) *Economic Statecraft*: 42.

4.See Zysman for more description on these policy choices. John Zysman (1983) *Governments, Markets, and Growth*: 274.

5.Peter Gourevitch (1986) *Politics in Hard Times: Comparative Responses to International Economic Crises*: 184.

6.See Floyd Norris (1988) "Nestle's Foreign Investors Learn How Sweet It Isn't." *International Herald Tribune*. (November 29): 11.

7.See Melvyn Marckus (1988) "Swiss Embarrassment." *The Observer*. (8 May): 57.

8.Ministry of Industry (Sweden) (1987) *Swedish Industry Facing the 90s*. Government Bill 1986/7:74: 16.

9.The most poignant example was the location of a major Volvo plant at Uddevalla, the site of a former shipyard. See Jonathan Kapstein (1989) "Volvo's Radical New Plant: 'The Death of the Assembly Line.'?" *Business Week*. (August 28): 92-93.

10.IMEDE and World Economic Forum (1989) *The World Competitiveness Report*: 174-175. (Tables 9.28, 9.31)

11.T.E. Cooke (1988) *Financial Reporting in Sweden*: 18. As Cooke explains, during the 1980s foreign firms remained relatively uninterested in Swedish MNCs because of obligation of management to employees, rights of employees, the wage bargaining process, the obligation for audit, the obligation to have reserves, the scope of the Swedish accounting act, role of employee investment funds, and the level of taxation and extent of allowances.

12.See "Taking Stock Home." (1988) *The Economist*. (May 28): 102.

13.For example, in various government publications data was given on the amounts the State gave to the IDA, yet there is no further break-down of the IDA's exact contribution. See Government of Ireland (1988) *Budget, 1988*: 144-151; Department of Industry and Commerce (1986) *Review of Industrial Performance*; ICTU (1986) *Public Enterprise: Everybody's Business*.

14.See Ministry of Industry (1988) "Subsidies and Structural Adjustment: The Danish Reply to Questionnaire IND(87)5:" 7.

15.See Niels Chr. Sidenius (1983) "Danish Industrial Policy: Persistent Liberalism." *Journal of Public Policy*: 49-61.

16.IMEDE and World Economic Forum (1989) *op.cit.*: 156. (Table 8.35)

17.Ironically other small states such as Belgium, Luxembourg and the Netherlands were ahead of the three listed above.

18.Ibid.: 149. (Tables 8.18, 8.19) One can assume that Denmark's position can be partly explained due to the importance of agriculture - and agriculture subsidies - to its economy.

19.John Hall and G. John Ikenberry (1989) *The State*: 14.

20.Peter J. Katzenstein (1985) *Small States in World Markets: Industrial Policy in Europe*: 87-88, 91.

21.See Klaus Nielsen and Ove K. Pedersen (1988) "The Negotiated Economy: Ideal and History." *Scandinavian Political Studies*: 79-101.

22.Much of the recent literature on small states has focused on the East Asian small states, illustrating how the "four dragons" used state-specific forms of state intervention to attain high levels of political-economic performance. See Yun Han-chu (1989) "State Structure and Economic Adjustment: East Asia." *International Organization*: 647-672; Brian Kelly and Mark London (1989) *The Four Little Dragons*.

23.See Barnaby J. Feder (1988) "Investors Look to Europe 1992." *The New York Times*. (August 26): B1.

24.From 1987 to 1988, there were seven mergers or joint ventures between major EC banks.

25.Deutsche Bank (1988) "The Single Market: Europe Looks to the Future." *Deutsche Bank Bulletin*. (June): 6-15.

26.Jack Stewart Clark (1988) *Europe After 1992: Establishing a New Economic Community*; Kleinwort Benson (1989) *Countdown to 1992: Growth Opportunities in Europe for US Corporations*.

27.Mark M. Nelson and Julie Wolf (1989) "EC Notebook: Are Subsidies Running Amuck? Merger Madness Snowballs." *The Wall Street Journal*. (August 1): A8.

28.IMEDE and World Economic Forum (1989) *op.cit.*: 150. (Table 8.21)

29.See Richard E. Smith (1989) "Inflation Fears, Political Worries Cause Twinge in Durable Swiss Franc." *The International Herald Tribune*. (April 11): 13.

30.See William Dullforce (1989) "How to Cope with Koppgate." *Financial Times Survey*. (April 25): II.

31.See Ernest Kilgus (1989) "The Swiss Financial Centre and The Challenges of 1992." *Credit Suisse - The Global Asset Manager*. (Summer): 38-40.

32.See Diana Federman and Margaret Studer (1988) "Swiss Go on A European Shopping Spree: Expanding Firms Seek to Avert EC Protectionism." *The Wall Street Journal*. (August 31): 16; Diana Federman and Margaret Studer (1989) "Swiss Firms Prepare For 1992 By Embarking on Acquisition Spree." *The Wall Street Journal - Europe*. (August 31): 1, 8.

33.Ibid.

34.However, by April 1989 only one other Swiss company, Rieter, had followed Nestle's example in opening up registered share ownership to foreigners. See William Dullforce (1989) Switzerland: Old Habits That Must Change." *Financial Times Survey* (April 25): I. See "Swiss Businesses: Opening the Chocolate Box." (1988) *The Economist*. (November 26): 104, 109; Mark Edmiston (1989) "Feature Investment Focus - Nestle." *Swiss Investment Strategy Highlights*. (June/July): 13-14.

35.See Craig Forman (1989) "Idyllic Switzerland Discovers its Idyll Is Turning Prosaic." *The Wall Street Journal*. (July 25): A1, A12.

36.Juris Kaza (1989) "Inflation Fears Dampen Boom." *International Herald Tribune*. Special New Report: Sweden, Walking Softly." (June 16): 9.

37."Sweden: Mensheviksson." *The Economist*. (April 1): 58, 60; "Feldt's Flip." *The Economist*. (May 13): 66.

38.See Marcus W. Brauchli (1987) "Sweden Eases Restriction of Foreign Share Purchases." *The Wall Street Journal - Europe*. (August 4): 22.

39."Swedish Takeovers: A European Smorgasbord." *The Economist*. (April 9): 68, 72.

40."Asea-Brown Boveri: Power Play." *The Economist*. (May 28): 21-24.

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50.For example, in 1989 the EC curbed farm production primarily in cereals, oil-seeds, and vegetables, costing the Danish agricultural sector one billion D.Kr.

51.One should note the increasingly international presence of the East Asian NICs, many of which successfully used various forms of intervention to achieve high levels of economic development. See Note 22 in this chapter.

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