

# The politics of growth models

Lucio Baccaro

Director, Max Planck Institute for the Study of Societies, Cologne, Germany

Jonas Pontusson

Professor of Comparative Politics, University of Geneva, Switzerland

*This article develops a framework for studying the politics of growth models. These, the authors posit, are sustained by ‘growth coalitions’ based in key sectors. Their members are first and foremost firms and employer associations, but fractions of labor are also included, if their interests do not impair the model’s functionality. There is no guarantee that a growth coalition and a winning electoral coalition coincide. In normal times, a growth coalition effectively insulates itself from political competition, and mainstream political parties converge on key growth model policies. In moments of crisis, however, the coalition shrinks, favoring the emergence of challengers that fundamentally contest the status quo. The way governing parties respond to electoral pressures can also play an important role in the recalibration of growth models. The authors illustrate the argument by examining the politics of ‘export-led growth’ in Germany, ‘construction-led growth’ in Spain, and ‘balanced growth’ in Sweden.*

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## 1 INTRODUCTION

Conceived as a follow-up to our previous work, this article articulates a framework for thinking about the politics of growth models. We argue that stable growth models are sustained by a coalition of organized interests that enjoy privileged access to the policy-making sphere and ensure that government policies, especially macroeconomic policies, reflect its interests and the functional requirements of the growth model. Growth coalitions operate outside the domain of electoral politics, but electoral politics constrain the politics of policy choice, and occasionally generate paradigmatic policy changes that transform the growth model. In the second half of the article, we illustrate some of the analytic leverage provided by this framework through stylized case studies of export-led growth in Germany, construction-led growth Spain, and ‘balanced growth’ in Sweden.<sup>1</sup>

Our approach builds on the literature on producer coalitions in Comparative and International Political Economy (Gourevitch 1986; Swenson 1991; Frieden and Rogowski 1996, Thelen 2014) while addressing its apparent neglect of electoral politics.

1. The ideas presented in this article draw on the introduction to a forthcoming volume, co-authored with Mark Blyth (Baccaro et al. 2022), as well as our previous work (Baccaro and Pontusson 2016; 2019). The case studies on Germany, Spain, and Sweden are syntheses of chapters co-authored with Martin Höpner (Baccaro and Höpner 2022), Fabio Bulfone (Baccaro and Bulfone 2022), and Lennart Erixon (Erixon and Pontusson 2022), respectively. We thank our co-authors for their many direct and indirect contributions.

We conceive a growth coalition as being based in one or more key sectors (for example, export-oriented manufacturing or the nexus of construction and mortgage finance). The members of a growth coalition are first and foremost firms and business associations, but fractions of labor are also included, albeit in a subordinate position, if their interests are in tune with the sectoral profile of the growth model and can be accommodated without impairing the latter's functionality.

Growth coalitions seek to project sectoral interests as coincident with the 'national interest' and to shape public perceptions of 'how the economy works,' but the success of such efforts is by no means a foregone conclusion. Relatedly, growth coalitions and electoral majorities do not necessarily coincide. In normal times, dominant growth coalitions typically succeed in insulating themselves from the electoral arena as mainstream political parties converge on key growth model policies (Hopkin and Voss 2022; Hübscher and Sattler 2022). However, growth coalitions shrink in numerical terms and the ranks of losers swell during economic crises and sustained periods of economic stagnation, favoring the emergence of new parties – or factions within mainstream parties – that challenge existing policy paradigms (Hopkin 2020). Under these conditions, the growth model itself may become politically contested and 'up for grabs.' As illustrated by our Swedish case study, the way governing parties respond to electoral pressures can also play an important role in the recalibration of growth models.

In what follows, we begin in Section 2 by articulating how the Growth Models perspective that we champion differs from the Varieties of Capitalism which has been the dominant paradigm in Comparative Political Economy for several decades. We then set out our conception of the politics of growth models in three steps: in Section 3, by considering the role of key sectors; in Section 4, by bringing in the dimension of class and class power; and, in Section 5, by discussing the role of parties and electoral politics. We illustrate these themes through stylized case studies of Germany, Spain, and Sweden in Sections 6–8. Section 9 provides some concluding remarks.

## 2 THE COMPARATIVE CAPITALISMS DEBATE

A signature feature of Comparative Political Economy (CPE) is the idea that there are several ways to organize a capitalist economy. CPE scholars have long emphasized the role of institutions that shape the supply side of the economy, enabling as well as incentivizing firms to develop core competences and pursue different production strategies: systems of corporate finance and control, industrial relations, and vocational training. The Varieties of Capitalism (VoC) framework developed by Hall and Soskice (2001) represents the most coherent statement of this broadly shared perspective. To recapitulate very briefly, the VoC framework identifies two fundamentally different types of economies: liberal market economies (LMEs) and coordinated market economies (CMEs). Specializing in economic activities that involve general skills, high-tech as well as low-end services, LMEs are distinguished by institutional arrangements that allow for rapid redeployment of human capital as well other assets. By contrast, CMEs specialize in economic activities that involve industry- and firm-specific skills and depend on institutions that solve the problems of credible commitment associated with the production of such skills. As the institutional ecosystem provides key firms with unique institutional capacities, each regime is efficient in its own way: LMEs excel in radical (product) innovation while CMEs excel in incremental (process) innovation.

Like earlier CPE scholarship, the VoC literature challenges the idea that globalization generates convergence between varieties of capitalism. In the VoC framework,

globalization instead serves to crystallize differences between regimes. Thus VoC scholars suggested, in the late 1990s, that Sweden, exemplifying the social democratic variant of coordinated capitalism, was becoming more like Germany, while the UK was becoming more like the US, but Germany and the US were becoming more – rather than less – distinct from each other as each economy capitalized on its distinctive advantages, and organized business rallied in defense of existing institutions (Soskice 1999; Iversen and Pontusson 2000).

The alternative perspective sketched by Baccaro and Pontusson (2016) conceives capitalist diversity as the result of different demand drivers of growth. From this perspective, institutional endowments and associated institutional complementarities (or the lack thereof) are of secondary importance in explaining the divergent trajectories among advanced capitalist countries. Instead, our approach starts with the channels through which aggregate demand expands (or fails to expand). The Growth Models perspective remains within the CPE tradition in that it seeks to understand cross-national diversity, but ‘growth models’ are not only demand-driven as opposed to supply-side driven: they are also more unstable than the types of capitalism identified by Zysman (1983) and Katzenstein (1985) as well as Hall and Soskice (2001).

Inspired by the Neo-Kaleckian tradition in macroeconomics (Palley 2012; Lavoie and Stockhammer 2013; Lavoie 2014) and the French Regulation school (Boyer 2004; 2015), the Growth Models perspective takes common trends as well as country-specific trajectories into consideration. A key theme of the Regulationist literature was the generalized crisis of ‘wage-led’ or ‘Fordist’ growth (Boyer and Saillard 2002; Boyer 2004). As commonly recognized, this growth model was premised on real wages growing in line with productivity increases, stimulating both domestic consumption and investment. The indexation of real wages to productivity was institutionally mediated by the presence of strong unions, and multi-employer wage-bargaining systems and the weakening of these institutions, along with global capital mobility and financialization, render the wage-led growth model, at best, very precarious.

Real wages falling behind productivity growth produces a tendency for aggregate demand to stagnate through various mechanisms, notably the greater propensity to consume out of labor income than out of profit income and the demand sensitivity of investment (Lavoie and Stockhammer 2013). Whether countries are able to escape this common stagnationist tendency hinges on their ability to find viable alternatives to wage-led growth (Stockhammer 2015). One alternative, exemplified by the UK prior to the global financial crisis of 2007–2008, consists of stimulating consumption by easing the access to credit. Another alternative is the export-led model that Germany has successfully pursued since the 1990s. The Swedish case represents, we think, a third model, which combines growth driven by credit-financed consumption as well as exports. And yet other models – for instance, Ireland’s foreign direct investment (FDI)-led growth, which stimulates investment and exports while boosting the innovative capacities of the economy by attracting foreign capital (Bohle and Regan 2021) – can readily be added to this typology.<sup>2</sup>

2. To clarify, we do not use the term ‘growth models’ in the same way as Post-Keynesian economists use it. In the Post-Keynesian literature, a ‘demand regime’ refers to the short-term response of demand/output to a shift in the functional distribution of income (Bhaduri and Marglin 1990) while a ‘growth regime’ takes into account the long-term implications of the distributional shift (through its impact on the investment function and/or on productivity). Both ‘demand’ and ‘growth’ regimes are counterfactual entities: they depend on some structural parameters of the economy (for example, propensities to consume, sensitivity of investment to demand and profit

Crucially, our approach to growth models hinges on the claim that the ability to combine different demand drivers of growth differs across countries. For example, domestic consumption growth may be complementary to export growth (Sweden in the pre-crisis period) or there may be a trade-off between them (Germany), such that policies that expand wage growth and domestic consumption lead to a decline of export-led growth. Also, there is no guarantee that countries will find a viable growth driver. For example, economic stagnation has been the dominant tendency of Italy since the mid 1990s (Baccaro and Pontusson 2016).

### 3 SECTORAL INTERESTS IN MACROECONOMIC POLICY

Our framework for understanding the political foundations of the growth model posits, in a first step, that sectors have distinct ‘policy requirements’ and, as a corollary, that macroeconomic policies have sector-specific implications. Most obviously, sectors that cater primarily to domestic demand and sectors that cater primarily to foreign demand have very different needs with regard to wage growth. For the former, Keynes’s classic fallacy of composition applies: each company would like to reduce costs by paying lower wages than its competitors, but the aggregation of individual choices reduces demand for all companies. The same logic does not apply to an industry relying on foreign demand: in this case, individual and collective rationality are better aligned in that, all else being equal, a reduction of wages relative to international competitors leads to an increase in competitiveness and greater demand for the industry as a whole as well as for individual firms.

In brief, policies promoting wage repression are detrimental for sectors relying on domestic demand and more acceptable, even beneficial, for sectors relying on foreign demand. Two qualifications must immediately be noted: first, the detrimental consequence of wage repression for sectors catering to domestic demand might be offset if domestic demand is stimulated by credit expansion, and, secondly, wage repression may have negative effects for export-oriented sectors too if it undermines the loyalty and commitment of their core workforce. For the latter reason, sectors producing high value-added exports tend to favor wage-repression policies that target the wages of workers engaged in the production of goods and services consumed by their employees rather than the wages of their own core employees (Günther and Höpner 2022).

Another important distinction, partially overlapping with the distinction between sheltered and exposed sectors, is the distinction between sectors whose demand is especially sensitive to the real interest rate and those that are sensitive to the real exchange rate. The two variables are linked by the behavior of prices. Keeping the nominal interest rate fixed, higher domestic inflation reduces the real interest rate. By the same token, if foreign prices do not change and the nominal exchange rate does not adjust (due to fixed exchange rates or a currency union), higher domestic inflation leads to real exchange-rate appreciation.

share, real exchange rate, and demand sensitivity of imports and exports). Actual growth in turn depends on whether public policy is consistent or inconsistent with the underlying growth model (Lavoie and Stockhammer 2012). By contrast, our growth models are purely descriptive entities and are operationalized through growth decomposition exercises – for example, we refer to Germany as ‘export-led’ because German growth in the period between 1995 and 2015 is largely attributable to (import-corrected) export growth.

Construction is the most obvious example of an interest-rate-sensitive sector. Low real interest rates stimulate demand for housing, and simultaneously make it cheaper for households and firms (both financial and non-financial) to borrow, thus stimulating loan generation by banks. However, the financial sector dislikes inflation intensely because it erodes the real value of liquid financial assets (Mosley 2003). The distinct interests of construction and finance become compatible when inflation is contained within the housing sector, that is, house prices rise while wage and general price inflation remains subdued. The latter condition is likely to hold when the labor market is weakly regulated, and in particular when precarious employment conditions curtail unionization or otherwise keep worker power in check. House prices rising faster than other prices creates opportunities for capital gains that strengthen the balance sheet of households and also produce a wealth effect that stimulates household expenditures to the benefit of other sectors of the economy (Boyer 2000).<sup>3</sup>

By contrast, export-oriented manufacturing is an exchange-rate-sensitive sector, especially if the price sensitivity of exports (or of import-competing domestic producers) is high. A key requirement in this case is a fixed exchange-rate regime, or ideally a single currency, which prevents the nominal exchange rate from adjusting to differences between domestic and foreign inflation. Domestic prices are a function of unit labor costs, that is, nominal wages divided by labor productivity. Keeping labor productivity constant, persistent wage moderation will lead to a depreciation of the real exchange rate and this will stimulate external demand (Höpner and Lutter 2017). External demand, in turn, will generate income and spur investment, with knock-on effects for the domestic economy as well. Crucially, export-led growth is a feasible growth strategy if the export sector is sufficiently large to overcome the depressive effect of wage moderation (Bowles and Boyer 1995).

In sum, macroeconomic policies favor certain sectors and penalize others. It stands to reason, then, that sectoral actors have conflicting preferences about the monetary, fiscal, exchange-rate, and wage-formation policies that influence real exchange rates and interest rates. As emphasized by the supply-side-oriented CPE literature (for example, Thelen 2019), they also have conflicting preferences with respect to the design of social insurance, spending on education, and R&D policy, but there is arguably more space for package deals that simultaneously satisfy multiple constituencies ('logrolling') in these other policy domains. In many instances, policy choices in these other domains might be interpreted, we think, as side payments to sectors whose interests would be better served by different macroeconomic policies.<sup>4</sup>

#### 4 SOCIAL CLASS AND POWER RESOURCES

As indicated at the outset, our approach to the politics of growth models draws on earlier work in Comparative and International Political Economy that conceives politics in terms of coalitions of 'producer groups' defined by class as well as sectoral or, in other words, 'cross-class alliances' (Gourevitch 1986; Swenson 1991; Frieden and Rogowski 1996; Thelen 2014). Much of this literature might be faulted for using a

3. Under conditions of stable wage inflation, inflation-targeting central banks will keep nominal interest rates low even though asset prices increase (Carlin and Soskice 2015).

4. See Hassel and Palier (2021) for an ambitious framework that bridges the divide between supply-side and demand-side policies and focuses attention on linkages between growth strategies and welfare-state reforms.

simple dichotomy between ‘labor’ and ‘business,’ with the former category apparently referring to all ‘wage earners.’ In our view, more fine-grained class distinctions need to be deployed and more attention should be paid to the question of how people’s position in the class structure conditions the salience of sectoral interests.

Following Iversen and Soskice (2001), a reasonable working hypothesis is that the skills of manual workers without university education tend to be sector-specific. Thus, the interests of skilled workers are more closely tied to the prosperity and prospects of the firm and the sector in which they work than the interests of ‘routine workers.’ The latter care more about macroeconomic conditions and, in particular, about the level of unemployment in the economy as a whole.

Within the middle class, broadly conceived, there are certainly occupations (for example, medical doctors) whose skills are very sector-specific, but the skills of individuals with tertiary education tend to be portable across sectors. For example, high-level managers frequently move, not only between firms but also between sectors. In addition, ownership of financial assets is constitutive of being in the ‘upper middle class’ and income from financial assets reduces the salience of sectoral interests relative to class interests even if the skills that generate labor income are sector-specific. In short, we posit that sectoral interests are most salient to skilled manual workers and that sectoral interests divide the working class to a greater extent than the middle class.

The concept of sector specificity can also be applied to capital. As documented by Krippner (2011) for the US, the distinction between finance and manufacturing has become blurred as financial activities have become an increasingly important source of profits for large manufacturing corporations since the early 1990s. Still, it remains meaningful, we think, to distinguish between capitalists who own and manage diversified portfolios of financial assets and capitalists who own controlling shares in one or several corporations, whatever the activities of those corporations might be. We posit that large stakeholders as well as executive managers share in the sectoral interests of the corporations that they control, but these interests may be ambiguous in the case of corporations whose economic activities are spread across several sectors.

We now have the basic elements necessary to map the contours of growth coalitions, defined as an enduring cross-class coalition of sectoral interests, first and foremost groups of corporate owners and executive managers but also workers with sector-specific skills. The groups that constitute such a coalition share similar preferences with regard to macroeconomic and sectoral policies. The inclusion of different sectoral and class interests depends on the specific features of the growth model. For reasons to be discussed, the Swedish growth model provides for the accommodation of a wider range of organized interests than either the German or the Spanish growth model.

Haffert and Mertens (2019) provide an interesting illustration of the way growth coalitions operate. Through a time-series cross-sectional analysis, they show that tax policies are shaped by the underlying growth model: the more the growth model is consumption- and debt-led, the lower taxes on consumption are (vice versa for export-led growth). Through a case study of Germany, they also show that the German government used the proceeds of a value-added tax increase to finance a decrease in social security contributions, reducing export prices (through reduced labor costs) while boosting domestic prices. This ‘fiscal devaluation’ was adamantly opposed by both labor and capital groups in domestic sectors such as construction and retailing, but business associations representing export-oriented sectors supported it. For cross-pressured unions in exposed unions, sectoral interests prevailed over class interests.

Are unskilled workers without strong sectoral attachments ever part of a growth coalition? Iversen and Soskice (2019) argue that technological change has broken ‘Fordist’ complementarities between semi-skilled and skilled workers, leading to political marginalization of low-skilled workers. In our view, patterns of inclusion and exclusion of low-skilled workers depend on the growth model and on power resources (Korpi 2006). If growth is export-led and export competitiveness depends importantly on keeping the real exchange rate down and the profit share up through nominal and real wage moderation, accommodation of the interests of routine workers becomes difficult. However, routine workers may force policy-makers to accommodate their interests through collective organization, operationalized in the first instance through unionization. Everything else being equal, unionization provides workers with bargaining power and this power must somehow be appeased through policy concessions. Accommodation of routine manual workers may push firms to reduce the price sensitivity of demand through innovation and reorganization, and thus rebalance the growth model. Alternatively, it may undermine the viability of the growth model and lead to a crisis.

## 5 PARTIES AND ELECTORAL POLITICS

Even under very generous assumptions about linkages between core sectors and other parts of the economic structure, the beneficiaries of a growth model are likely to represent a minority of the voting population. How does a growth coalition prevent the emergence of an adverse electoral coalition composed of workers and capitalists from rival sectors or groups with no specific labor market attachments? In other words, how does a growth coalition ensure its electoral viability?

In an influential contribution, Beramendi et al. (2015, p. 62) argue that ‘electoral partisan politics ... should drive explanatory accounts of policy choice in political economy’ (see also Häusermann and Kriesi 2015; Kitschelt and Rehm 2015). For these authors, the main mechanism of policy selection is voter choice in competitive elections. Voters are seen as having well-defined policy preferences on issues, and every vote carries the same weight. From these premises, it follows that voters select growth-model policies based on alternative proposals made by political parties, leaving little meaningful space for organized interests and ‘growth coalitions’ in our understanding of this term.<sup>5</sup>

We agree that elections cannot be ignored. There is no guarantee that the dominant *growth coalition* will also be the dominant *electoral* coalition. Nonetheless, we posit that the key policy foundations of a growth model are shielded from electoral competition through various mechanisms. First, the basic planks of macroeconomic policy are heavily institutionalized and not at the direct disposal of electoral majorities. Monetary policy, for example, has been entrusted to independent central banks. In the eurozone, fiscal policy, too, is heavily constrained by European fiscal rules or constitutional provisions such as ‘debt brakes.’

5. At the same time, Beramendi et al. (2015) suggest that macroeconomic policy and industrial policy are not salient issues, due to convergence between left and right or delegation to supranational authorities, and that electoral politics primarily concern other issues (welfare provisions, immigration, education, and the environment). In our view, convergence and delegation are part of the *explanandum* and should not be taken for granted.

Second, economic policy is a highly technical domain which lends itself more to the ‘quiet politics’ of technical agencies and committees, in which well-defined sectoral interests are more likely to be heard, than to the ‘noisy politics’ of electoral competition (Culpepper 2010). In line with this intuition, Hübscher and Sattler (2022) present evidence of a mismatch between voter preferences and the policies of governments with regard to fiscal policies. They find that voters are opposed to austerity *both* in domestic demand-oriented Britain and in export-oriented Germany. Yet countries relying on export-led growth are considerably more likely to pursue austerity than countries relying on domestic demand.

Third, established parties are likely to converge on policies that are key for the growth model, thus limiting the space for electoral competition to non-threatening issues.<sup>6</sup> Hübscher and Sattler (2022) show that left- and right-leaning governments are equally likely to implement austerity in export-led growth models, while they are much less likely to do so in domestic demand-led models. They rationalize this finding by hypothesizing that governments of different political orientations internalize the functional requirements of the respective growth models. However, partisan differences become relevant in countries in which the two growth drivers contribute approximately equally. In these ‘balanced’ models, left-leaning governments are less likely to implement austerity than right-leaning governments.

Building on the Gramscian notion of hegemony, it is also plausible to argue that stable growth coalitions successfully project their key interests as the ‘national interest.’ In Gramsci’s (1992) core formulation, the success of such ‘framing effects’ requires material concessions targeted on potentially disruptive subordinate groups (Przeworski 1985, ch. 4). In any case, there is little doubt that the ability to shape perceptions of ‘how the economy works’ contributes to reducing the electoral vulnerability of the growth model (Blyth 2002; Schmidt 2008).

The above discussion suggests that a growth coalition – composed of groups and sectors that are key to the success of the growth model – has greater influence on public policy formation than other social groups, and that under conditions of ‘normal politics,’ partisan competition is unlikely to upset it. This state of affairs is not unchangeable, though. When growth withers away – either due to external shocks or to the accumulation of endogenous dysfunctions – and the circle of beneficiaries becomes excessively narrow, previously ‘quiet’ politics becomes progressively more ‘noisy.’ The media start questioning the received wisdom about how the economy works (Culpepper 2021). Citizens develop distinct preferences over issues they previously took for granted. Anti-system parties and political entrepreneurs inside established parties politicize the newly salient issues and seek to enhance their electoral appeal by reaching out to the ‘losers’ of the growth model (Hopkin 2020). In these circumstances, it becomes increasingly difficult for the growth coalition to insulate itself from electoral competition and the growth model itself may become implicated in partisan electoral politics.<sup>7</sup>

6. This formulation draws some inspiration from the cartel party thesis, as articulated by Blyth and Katz (2005) and Hopkin and Blyth (2018). For our present purposes, it is not necessary to engage with the question of whether or not ‘cartelization’ is a necessary condition for parties to converge on key growth-model policies.

7. Inspired by Amable and Palombarini (2009), Baccaro and Pontusson (2019) used the Gramscian label of ‘dominant social blocs’ to refer to the coalitional underpinnings of growth models. We now prefer the label of ‘growth coalitions’ because it brings the potential for tensions between interest-group politics and electoral politics in focus.



## 6 THE POLITICS OF EXPORT-LED GROWTH IN GERMANY

We now turn to stylized case studies to illustrate and flesh out some of the propositions set out above, starting with Germany as the representative case of the export-led growth model. Between 1995 and 2015, German growth was largely pulled by exports (75 percent), while the growth contribution of domestic demand was small (−4 percent).<sup>8</sup> By comparison, growth was overwhelmingly pulled by domestic demand in the US and the UK in the same period (89 percent and 82 percent, respectively). Furthermore, exports were the most dynamic component of German aggregate demand in every five-year period between 1995 and 2015, including in the post-global-financial-crisis period. Exports accounted for 62 percent of total growth in 2011–2015, but the following years saw a much greater role for domestic demand, which accounted for 81 percent of total growth in 2016–2018. Thus, there was a rebalancing towards the end of the 2010s. It remains to be seen if it will continue in the post-pandemic phase.

Germany's export-led growth model is underpinned by *institutions* and therefore not easily modifiable through changes in government policy. An inflexible exchange-rate regime (the euro) prevents the correction of competitiveness imbalances, an industrial-relations regime facilitates competitive disinflation, and a system of fiscal federalism severely constrains the fiscal capacity of local governments. These institutions jointly undergird Germany's *undervaluation* regime (Höpner 2018).

Historically, Germany has had lower wage and price inflation than other European countries. This trend should lead to nominal exchange-rate appreciation. However, the euro has made such adjustment impossible. Within the euro, every percentage point of German nominal disinflation translates into real devaluation vis-à-vis other members of the eurozone. In the pre-crisis period this led to a yawning gap in real exchange rates between the periphery of the eurozone and Germany, and correspondingly to account imbalances (Scharpf 2011). Furthermore, as a single currency that encompasses 'strong' and 'weak' countries, the exchange rate of the euro vis-à-vis the rest of the world is in all likelihood lower than the exchange rate of a Deutsche Mark would be.

The wage-bargaining system provides the second plank of the undervaluation regime. The German industrial relations system is no longer as 'coordinated' as it once was, having undergone significant liberalization since the 1990s (Hassel 2014; Baccaro and Howell 2017). Various factors (for example, German unification, greater competitive pressures in export markets) induced German export-oriented companies to engage in a cost-cutting campaign. This was accomplished through the threat of decentralization, through a wave of concessionary bargaining at the plant level, and through the introduction of OT (*ohne Tarifvertrag*) membership. Parts suppliers started leaving their employer associations in the 1990s because they felt the industry-level standards had become too expensive for them. In turn, employer associations responded by allowing OT membership, that is, by allowing companies to remain

8. The figures in parentheses are based on import-adjusted demand contributions to growth. Differently from standard decomposition exercises (for example, Baccaro and Pontusson 2016), which subtract imports solely from exports, import-adjusted demand contributions decompose imports between the part absorbed by domestic demand (for consumption, investment, government expenditures purposes) and the part absorbed by exports (imported intermediate products that are directly or indirectly incorporated into exports) (Auboin and Borino 2017). See the online appendix to Baccaro and Neimanns (2022) for a presentation of methodology. The data are drawn from the OECD Input-Output and Trade in Value Added databases.

members even though they did not apply the contractual standards. The practice of OT membership originated in the manufacturing sector, but became particularly diffuse in low-wage service sectors such as retailing, which had traditionally relied on extension of collective-bargaining agreements to take wages out of competition. With OT membership, employer associations became less willing to allow for statutory extension, because this threatened their OT members. Furthermore, intersectoral dynamics also played a role. In Germany, intersectoral employer associations can exercise a veto power on the sectoral extension of collective-bargaining agreements even when the sectoral social partners agree to it. Dominated by export-oriented sectors, the intersectoral employer associations frequently used their veto power to block statutory extension in service sectors, thus contributing to decoupling wages in low-skilled service sectors from manufacturing wages. Keeping service-sector wages low was expedient for export-led companies because it shifted the costs of real exchange-rate disinflation onto the domestic sectors (Günther and Höpner 2022).

Public-sector workers are not only more highly unionized than those in other sectors, but also have little to fear from relocation and competitive pressures. Yet wage growth was subdued in the German public sector as well (Di Carlo 2018). Another institution explains this phenomenon: German fiscal federalism. A tax reform, implemented in steps between 2000 and 2005, led to a loss of revenue for Länder and municipalities, which are responsible for 90 percent of public-sector employment. The consequence was that the Länder were forced to cut expenditures, putting downward pressure on public-sector wages.

The combination of an inflexible exchange-rate regime and mechanisms that ensure wage moderation both in the private and in the public sector provides the German export-led growth model with solid institutional foundations, which protect it from changes in government majorities. Furthermore, there is also evidence that the largest German parties converged on key policies undergirding the growth model. Thus a center-left government took the key policy decisions of the early 2000s: fiscal consolidation, pressures to decentralize wage setting and facilitate atypical employment, and a thorough overhaul of unemployment insurance.

As the two main parties saw their electoral support erode to the benefit of challenger parties from the mid 1990s onwards, it was relatively easy for them (compared to Sweden, as discussed later in the paper) to form grand coalitions and keep the fundamental orientation towards export-led growth unchanged. If the German trajectory until the early 2000s can be interpreted as an inevitable response to the external shock of unification, the policy approach taken after 2005 is difficult to make sense of without attributing to policy-makers a deliberate intent to shore up the devaluation regime. After a short-lived fiscal expansion during the global financial crisis and Great Recession of 2008–2009, fiscal policy quickly became ‘austere’ again, even though there clearly was room (and arguably need) for fiscal expansion. The introduction of the minimum wage in 2015 increased wages in low-skilled service sectors and slightly strengthened domestic demand (Marx and Starke 2017), but the largest contribution to growth continued to come from exports until the late 2010s.

## 7 THE POLITICS OF CONSTRUCTION-LED GROWTH IN SPAIN

Spain before the global financial crisis and Great Recession illustrates the *modus operandi* of a very different growth model from that of Germany, one in which domestic demand is the key growth driver and construction is the key sector (together with

banking). In the period between 1995 and 2015, Spanish growth was 2.1 percent per year on average, higher than in France, Germany, and Italy, and (import-adjusted) domestic demand accounted for 63.5 percent of total growth. However, there is a big difference between the pre-crisis and the post-crisis period in the case of Spain. In the pre-crisis period, Spanish growth was largely pulled by domestic demand, which accounted for 61.5 percent in 1996–2000 and 97.9 percent in 2001–2005. With the euro crisis destroying domestic demand (and imports), total growth fell to zero in 2011–2015 and the growth contribution of domestic demand became negative (–1 percent per year). In this period, the only stimulus to growth came from exports. It would be incorrect to say there was a shift towards export-led growth in the post-crisis period (Kohler and Stockhammer 2021). In fact, when Spain returned to relatively fast growth in 2015–2018 (2.8 percent per year), domestic demand was again the main contributor, accounting for 65 percent of growth.

Within domestic demand, investments played a key role in Spain, growing from 22 percent of GDP in 1995 to 30 percent in 2006. Specifically, construction investments increased from 14 percent to 21 percent of GDP in this period. The construction sector, already large in comparative perspective (9 percent of value-added in 1995), peaked at 12 percent of value-added in 2006. By comparison, the German construction sector contracted from 7 percent of value-added in 1995 to 4 percent in 2007. Furthermore, Spanish house prices more than tripled between the early 1990s and the mid 2000s, while household debt more than doubled as a percentage of disposable income. In brief, all the elements of a debt-driven construction boom were present in Spain.

Membership of the euro favored the construction boom by creating the opposite macroeconomic configuration to the German one. The spread between Spanish and German long-term nominal interest rates declined from 4.5 percent in 1995 to 0.2 percent in 1999, and continued to decline after Spain joined the euro, reaching 0 percent in 2003. However, inflation remained higher than in Germany (by 1.5 percent on average between 1999 and 2007). The consequence was that Spanish long-term real interest rates fell from 6.1 percent in 1995 to 2.6 percent in 1999 to a low of 0.1 percent in 2005. Low real interest rates and an appreciating real exchange rate produced a loss of competitiveness and the accumulation of large current-account deficits before the global financial crisis and Great Recession, which however did not lead to corrective measures until the euro crisis, when capital inflows suddenly stopped.

Interestingly, the demand boom had little to do with growing real wages, and much more to do with credit expansion (Perez and Matsaganis 2018; Cárdenas et al. 2021). Although the wage bill grew thanks to employment creation and a higher employment intensity of growth, real hourly wages did not increase at all between 1995 and 2007, not only in the economy as a whole but also in the booming construction sector. In this period, Spain had even greater real wage moderation than Germany. By contrast, credit to the private non-financial sector almost quadrupled, reaching a peak of 223 percent of GDP in 2009. Credit to non-financial firms increased the most, from 62 percent of GDP in 1995 to 168 percent in 2009, but credit to households also grew from 31 percent in 1995 to 85 percent in 2009. By contrast, private-sector credit shrank in Germany over the same period. Contrary to a popular argument, which sees foreign banks finance the Spanish demand boom by intermediating foreign savings through capital outflows (for example, Quaglia and Royo 2015; Dellepiane-Avellaneda et al. 2021), the bulk of credit was created by domestic banks. While the stock of foreign loans peaked at 53 percent of GDP in 2007, the stock of domestic banks' loans was almost three times larger. Small local saving banks (*cajas*) played a key role in the financing of local development projects (Ruiz et al. 2015).

Spain's main government parties, the conservative PP and the socialist PSOE, while diverging fundamentally on other issues, such as same-sex marriage, shared the same construction-centric economic model and implemented similar policies. In 1998 the PP passed a 'build anywhere' law, by which virtually any land could be reclassified as 'suitable for development,' except land of special naturalistic significance (and even in such cases, exceptions were frequently made) (Burriel 2011). In Spain, responsibility for zoning regulation rests with municipal authorities. Thus, municipalities started to compete with each other to reclassify as much land as possible as 'suitable for development,' in order to attract large development projects, which would bring higher incomes and tax revenues. In turn, developers financed their investments with loans extended by the local *cajas*. This type of intertwining of local politics, housing development, and regional banks was as much a characteristic of PP-run localities in Murcia and Valencia as of socialist-run Andalusia or autonomist Catalonia (López and Rodríguez 2011). Furthermore, the PP strengthened housing demand by deregulating the mortgage market, which led to the emergence of the second-largest securitization market in Europe after the UK (Dellepiane-Avellaneda et al. 2021). Confirming party convergence on key policies for the growth model, when the PP lost the elections in 2004, the PSOE made no attempt to reverse the decisions of its predecessors, letting the housing bubble balloon until 2007.

The social coalition directly profiting from the housing-based economy included developers, bankers, and middle- and upper-class property owners (who often owned multiple houses). Low-skilled workers benefited from the expansion of employment opportunities brought about by the construction frenzy. Firms and workers in adjoining sectors such as infrastructural development and tourism also had a stake in the growth model. By 2007, 85 percent of Spanish households owned at least one house (López and Rodríguez 2011). Even low-income households could use their appreciating housing assets as collateral for consumption finance.

After the crisis, small construction companies went bankrupt, construction workers lost their jobs, and low-income households lost their homes. The local *cajas* were wiped out by a wave of restructuring and only two out of 45 survived. However, large banks like BBVA and Banco Santander consolidated their position in the domestic market and further expanded their reach into foreign markets (Quaglia and Royo 2015). Similarly, large construction groups like Acciona and the ACS Group also benefited from the disappearance of small firms and expanded their activities abroad. Overall, the core growth coalition shrank but did not fundamentally change.

## 8 THE POLITICS OF GROWTH-MODEL RECALIBRATION IN SWEDEN

Averaging 2.6 percent, Sweden's annual growth rate between 1995 and 2015 was higher than both Germany's and Spain's, and higher than the OECD average. Decomposing GDP growth in the manner described above suggests that two-thirds of growth were attributable to domestic demand and one-third to import-adjusted exports. In the late 1990s, growth was equally pulled (50–50) by exports and domestic demand. However, the story of the Swedish 'balanced' growth model (Baccaro and Pontusson 2016) is not so much about equal weight of growth drivers; rather, it is about sequence and compatibility of growth drivers. While the German growth model became increasingly reliant on exports from the early 1990s onwards, repressing domestic consumption, in Sweden export-led growth pulled the economy out of the recession of the early 1990s,

but then generated consumption growth and boosted the growth of import-competing and sheltered services.

Furthermore, the extent of rebalancing after the global financial crisis was much more extensive in Sweden than in Germany. Like the economic recoveries of the early 1980s and mid 1990s, the Swedish recovery of 2010–2011 followed in the wake of a sharp depreciation of the value of the krona and a restoration of the profit share in manufacturing, but sluggish foreign demand, first and foremost due to the austerity measures of eurozone member states, rendered the export-led growth less robust than in the past. The center-right parties in power at the time responded to this situation by stimulating domestic demand via tax cuts. More importantly over the long run, the central bank (*Riksbanken*) embarked on a sustained campaign to boost economic growth by cutting interest rates and quantitative easing from 2012 onwards.

With exports of goods and services accounting for 45 percent of GDP in 2020 (down from an all-time high of 49.8 percent in 2008), the Swedish economy remains highly export dependent, but the balance shifted towards greater reliance on domestic growth drivers in the 2010s. The manufacturing sector's share of total business value-added declined in the pre-crisis period as well as the post-crisis period. While this decline was more than offset by the expansion of export-oriented services in the pre-crisis period, the share of total value-added attributed to sheltered services has increased steadily and the share of exposed services has remained stable in the post-crisis period. Perhaps most strikingly, real estate and construction increased their combined share of total value-added from 13.0 percent in 2008 to 15.4 percent in 2019.<sup>9</sup>

Moreover, wage growth exceeded labor productivity growth by a considerable margin, stimulating internal demand. At the same time, expansionary monetary policy measures and favorable tax treatment of mortgages have boosted construction and sustained private consumption since the early the 2010s. In marked contrast to Germany, household indebtedness rose sharply in Sweden as well as the UK and the US from the mid 1990s until the crisis and, in contrast to the UK and the US, the growth of household indebtedness continued unabated through the 2010s in Sweden. In this respect, the rebalanced Swedish growth model of the 2010s bears some resemblance to the construction-led growth model exemplified by pre-crisis Spain.

The different trajectories followed by Sweden and Germany raise two questions which are important for the politics of growth models. First, why did Sweden not follow Germany to become an export-led growth model in the 1990s? And, second, why did Sweden take a 'domestic turn' in the 2010s? Regarding the first question, it is noteworthy that Volvo and other large, export-oriented engineering firms pushed hard for decentralization of wage bargaining in the mid 1980s (see Pontusson and Swenson 1996). The fundamental objective behind this employer offensive was to decouple wage developments in exposed and sheltered sectors and thus to create the conditions for an export-led growth model akin to the model that Germany adopted a decade later. With the tacit support of the Metalworkers' union, wage formation indeed became more decentralized in the 1980s, but wage growth in sheltered services continued to keep pace with wage growth in export-oriented manufacturing. Two considerations are key for understanding why Swedish engineering employers failed to achieve their fundamental objective. To begin with, social democratic governments in the 1980s were (still) unwilling to let the rate of unemployment rise above 4 percent. Second, Sweden's powerful public-sector unions insisted on the wages of their members keeping up with the wages in exposed sectors as well as wage solidarity within the

9. Based on the OECD STAN Database (ISIC Rev. 4, 2020 Edition).

public sector, putting upward pressure on wages in private services. In other words, partisan politics (a social democratic government with strong ties to the union movement) and the bargaining power of public-sector employees, a well-organized interest group outside the growth coalition, prevented the emergence of a purely export-led growth model in the 1980s.

The failure to decouple wages in the exposed and sheltered sectors in turn put pressure on manufacturing firms to invest in new technologies and incentivized capitalists to diversify their holdings. The manufacturing firms that spearheaded the export-led recovery of the 1990s were firms that had invested heavily in information and communication technologies over the previous decade (Erixon 2011). Beyond traditional manufacturing, business services emerged as a leading export sector in this period and, as documented by Thelen (2019), key groups in the Swedish business community also diversified by taking advantage of opportunities created by the privatization of education and publicly financed care services.

The diversification of the growth coalition in Sweden has facilitated the maintenance of a balanced growth model in that labor costs are less of a concern for the leading export sectors than was the case in the 1970s and 1980s. Organized business did not mobilize against macroeconomic policies that served to boost domestic demand in the 2010s. At the same time, electoral politics must be taken into account in order to explain why Sweden pursued more expansionary macroeconomic policies than Germany in the post-crisis period. In both countries, the Great Recession and the sluggishness of the subsequent recovery reinforced rising political disaffection among many voters, especially low-income voters, and the appeal of populist parties. Differently from the German case, however, the long-standing fragmentation of the center-right rules out the formation of grand-coalition governments in Sweden. Competition among the ‘bourgeois’ parties makes it difficult for one (or two) of these parties to enter into a formal coalition with the social democrats. Since the entry of the populist Sweden Democrats into parliament in 2010, neither of the center-left bloc nor the center-right has commanded a parliamentary majority in the 2010s. In this new situation, minority coalition governments of the center-right (2010–2014) and the center-left (2014–the present) have eschewed austerity measures that seemed likely to weaken their re-election prospects and the mainstream parties have converged on delegating much of macroeconomic management to the *Riksbank*.

## 9 CONCLUDING REMARKS

The politics of growth models that we have sketched in this paper brings together two traditions in Comparative Political Economy: the producer-group perspective (Gourevitch 1986; Swenson 1991; Thelen 2014) and the electoral perspective (Beramendi et al. 2015). Each can be individually faulted for neglecting the other dimension, but their combination, we posit, goes a long way towards explaining the diversity of growth models in advanced countries.

Growth models rest on growth coalitions with distinct sectoral profiles. In most times and circumstances, producer-group politics prevails and the key policy planks of the growth model are shielded from electoral competition. Various mechanisms concur to produce this outcome. First, macroeconomic policy rests on institutions which are out of reach for electoral majorities. For example, monetary policy is the prerogative of an independent central bank, which in the eurozone is not even a national institution. Fiscal policy is also strongly constrained by supranational rules (such as the Stability

and Growth Pact) or constitutional provisions (for example, regarding ‘balanced budgets’ or ‘debt brakes’). Second, economic policy issues are unlikely to be highly salient for voters, thus ‘quiet politics’ is the dominant mode (Culpepper 2010). Third, established parties converge on policies which are crucial for the growth model. Our case studies suggest that this happened in Germany, where both the SPD and the CDU shared a commitment to strengthen the competitiveness of the export sector, and in Spain, where both the PP and PSOE shared a commitment to create favorable conditions for the construction industry and associated financial activities.

Growth coalitions might also shape the way voters think about economic relationships. When normative consensus goes beyond elites and affects individual perceptions as well, then a growth coalition is hegemonic in the sense of Gramsci and deserves the appellation of ‘dominant.’ Whether a growth coalition is ‘dominant’ in this sense needs to be verified empirically, for example through public opinion surveys.

Electoral competition features most clearly in moments of crisis. When the growth model becomes dysfunctional, either due to the endogenous accumulation of problems or to external shocks, politics shifts from ‘quiet’ to ‘noisy’ mode. New political entrepreneurs, within or outside mainstream parties, repoliticize issues previously seen as sacrosanct or taken for granted and reach out to the growing pool of losers. In these circumstances, elections may bring about fundamental change in the growth model. To visualize this scenario, think what could have happened if Sanders had won the American election or the Five Star Movement had obtained an electoral majority in the Italian parliament.

Electoral politics also acts as a constraint on what a growth coalition is able to achieve in normal times. This is brought out by the Swedish case. Swedish manufacturing exporters tried but failed to bring about the same decoupling between export-sector and protected-sector wages that the German employers accomplished. They failed because the Swedish social democrats had strong ties to public-sector unions and the fragmentation of ‘bourgeois’ parties ruled out a German-style grand coalition. With the German route sealed off, Swedish capital had to look for alternatives and started to diversify into services.

The framework we have sketched opens up several avenues for research at the intersection between political science, Post-Keynesian economics, and sociology. We list just a few of them: What exactly are the mechanisms that produce the shift between normal/quiet and crisis/noisy politics for the growth model? To what extent do parties converge on key macroeconomic policy issues? What is the role of the media, both old and new, in making economic policy issues salient for voters? We hope other researchers will join us in the exploration of these questions.

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