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A Comparative Examination of the Nature of Change in Macroeconomic Policies

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Abstract

This article examines the impact of economic crises on macroeconomic policies in Ireland in the late 1950s and Sweden in the early 1980s, framed within the context of the policy change literature. Each of these countries' responses to the crises affecting them, tempered as they were by historical and political factors, provides valuable insights into their political economies. These findings enable us to compare and contrast the nature of each crisis and the policy responses adopted. The value of such comparison is in the perspective it offers, contributing to the goal of building a body of increasingly complete explanatory theory (Mahler, 1995).

JEL classification: F50, P16, E65.

Keywords: crisis, economic policy, change, ideational, paradigm.

1. Introduction

This paper examines the impact of economic crises on macroeconomic policies in Ireland in the 1950s and Sweden in the early 1980s, framed within the context of the policy change literature. These cases were selected for examination based upon the criteria of "most similar" and "most different". Employing the criteria of "most similar," we selected from states that have been stable democracies since the first half of the 20th century and were founding members of the Organization for Economic Cooperation and Development (OECD). These conditions tie together the principles of representative democracy and free market economy. For the criteria of "most different," we utilized Lijphart's (1999) categories of majoritarian and consensual democracies. This category permits us to control for varying institutional arrangements. By employing this approach we are trying to ensure that the cases examined, though not identical, are comparable.

Ireland and Sweden are small, long-standing, democracies and encompass parliamentary, republican, constitutional monarchical and unitary systems of governance. They are both peripheral European states, as well as being small economies. Despite their similarities, in the periods in which we examine them, their economic performances contrasted sharply. Sweden was a prosperous welfare state during much of the latter half of the 20th century, while Ireland struggled to achieve sustained economic growth. Nevertheless, their similarities ensure "the contexts of analysis are analytically equivalent, to a significant degree, while their differences place the parallel processes of change in sharp relief" (Collier, 1997: 40).

Macroeconomic policies were selected for examination as commentators (academics and journalists) tend to focus primarily upon macroeconomic policy instruments, while dealing with the broader sweep of policies affected at the time would have required more space that is available here. Each country's response to the crisis afflicting it, tempered as it was by a combination of historical and political factors, provides an insight into that political economy. These findings enable us to compare and contrast the nature of each crisis and the policy responses each country adopted. Through studying politics comparatively we can discover trends and achieve an understanding of broader characteristics (Blondel, 1995: 3). Thus, the value of comparison is in the perspective it offers and its goal of building a body of increasingly complete explanatory theory (Mahler 1995; Mayer et al. 1993).

2. The Policy Change Literature

Policy change is a complex process and must be seen in the context of societal and political change (Feldstein, 1994). A crisis implies prevailing policies cannot be sustained without deterioration (Haggard and Kaufman, 1995: 14). An economic crisis can influence policy preferences leading to policy change (Stevenson, 2001: 621). Due to the complexities in trying to understand the nature of policy change, the issue has been approached from a variety of perspectives.

Advocacy collation theory focuses on coalitions sharing core policy beliefs, on policy-oriented learning and on external system events to explain radical policy change (Meijerink, 2005: 1061). An advocacy coalition consists of "elected and agency officials, interest group leaders, researchers who share a particular belief system" (Sabatier, 1988: 139). The epistemic communities explanation focuses on networks of individuals who share policy relevant knowledge as they seek to achieve policy change (Haas, 1992: 3). According to the advocacy coalition approach, for policy change to occur, an external shock is required, such as a macroeconomic crisis (Sabatier and Jenkins-Simth 1999; Nohrstedt, 2005: 1042). For the epistemic community approach, policy change may be triggered by uncertainty over the seriousness of problems in the polity (Meijerink, 2005: 1063).

Based on the concept of windows of opportunity the policy streams approach to policy change incorporates a role for the policy entrepreneur in engendering change (Kingdon, 1995; Zahariadis, 1999). Windows of opportunity arise due to exogenous shocks (Garrett and Lange, 1995). For policy change to occur, when a window of opportunity forms, policy entrepreneurs attempt to gain political support for the solutions they put forward (Zahariadis, 1999). To do this, policy entrepreneurs link problems, ideas and politics to draw attention to issues and bring them onto government agendas (Mintrom and Norman, 2009: 655).

For Baumgartner and Jones (1993), the process of policy change is marked by long periods of stability disrupted by instances of radical change. The punctuated equilibrium approach illustrates how policy entrepreneurs opposed to extant policy develop alternative ideas and seek support for this new idea. For policy change to occur, opponents of extant policy must create new perceptions of the issue at stake and search for support for their newly created policy ideas (Meijerink, 2005: 1064). Should a board range of these societal actors perceive the paradigm underlying extant policy is inadequate, then ideational collapse will occur (Legros, 2000: 419). However, "even when ideational collapse occurs, failure to reach consensus on a replacement could produce continuity, as society reflexively re-embraces the old orthodoxy" (Legro, 2000: 424). Thus, in the wake of policy failure and ideational collapse, there is no guarantee that a new idea will become policy. The critical junctures framework, developed by Hogan and Doyle (2007; 2008), formalized this argument. It posits that a critical juncture is made up of three sequential events: crisis, ideational change and policy change.

A growing body of literature is devoted to identifying aspects of incremental policy change. This recognises continuity during upheavals and gradual change in times of peace that eventually become transformative (Djelic and Quack, 2003: 309–10; Thelen, 2004: 292). Institutions and policies change in subtle, but often significant ways, by a variety of mechanisms, including layering, conversion, displacement and drift. Layering is the placing of new constituents in established institutional frameworks. Conversion is the integration of new groups into institutions, forcing change in the roles these institutions perform. Displacement occurs when new models emerge, calling into question existing organizations (Streeck and Thelen, 2005: 19), while drift refers the absence of institutional stability (Thelen, 2004). As Sheingate (2003: 186) argues, to provide a nuanced account of policy change, we must move beyond the conception of institutions as bastions of equilibrium.

Thus, the literature looks primarily at the importance of external shocks for initiating policy change. However, policy change may be triggered by uncertainty as to the problems in the economy. The key players in policy change literature are policy and political entrepreneurs and coalitions of actors sharing a common belief or policy relevant knowledge. The key concept in the policy change literature is ideas, extant ideas that underlie existing policies and alternative ideas that attack current policies. Thus, the literature sees these components as critical to the policy change process.

3. Ireland 1950s – The State of the Economy

After independence in 1922 the first Irish Free State government employed a free trade policy, centered on agriculture. However, after Fianna Fáil came to power in 1932, in the depths of the Great Depression, economic policy came to focus upon protectionism and developing domestic industries behind tariff barriers. This was a process underway in many countries at the time, however Irish protectionism was driven by cultural isolationist factors related to the country's history as a British colony. The view that political independence could be a key determinant of economic progress had huge influence on the ideas that shaped the economic nationalism underlying Fianna Fail's protectionist policy from the 1930s onwards (Ó Tuathaigh, 1986). Independence came to be equated with an economic nationalism that manifested itself in protectionism. The naivety was that just because economic policy was homemade did not make it better. For Ireland, the benefits of protectionism – meagre industrial expansion – had been reaped by the 1940s (Haughton, 1995). By the 1950s, Irish industry was supplying as much of the domestic market as it could and the opportunities for expanding employment further were limited. The OECD (1958: 15) stated that development in the industrial sector, in spite of some changes, depended on a small and static home market.

Table 1 shows that debt/GNP ratio deteriorated between 1951 and 1959 and the level of economic openness reached a decade long low in 1959. For the other four indicators, their low points came at various times during the 1950s. Unemployment peaked at almost 10 percent in 1953. However, this figure conceals the tens of thousands of people emigrating annually. In 1951, inflation peaked at over 11 percent, while by 1959 the economy experienced deflation. The economy shrank by over 2 percent in 1958, having previously contracted in 1956, with only anemic growth in 1957. Between 1951 and 1958 GDP rose by less than 1 percent per annum, employment declined by 12 percent and the population dropped to its lowest ever level (Haughton, 1995). From this table it is clear that the Irish economy was in crisis.

Table 1: Ireland's Main Economic Indicators, 1950 – 1960

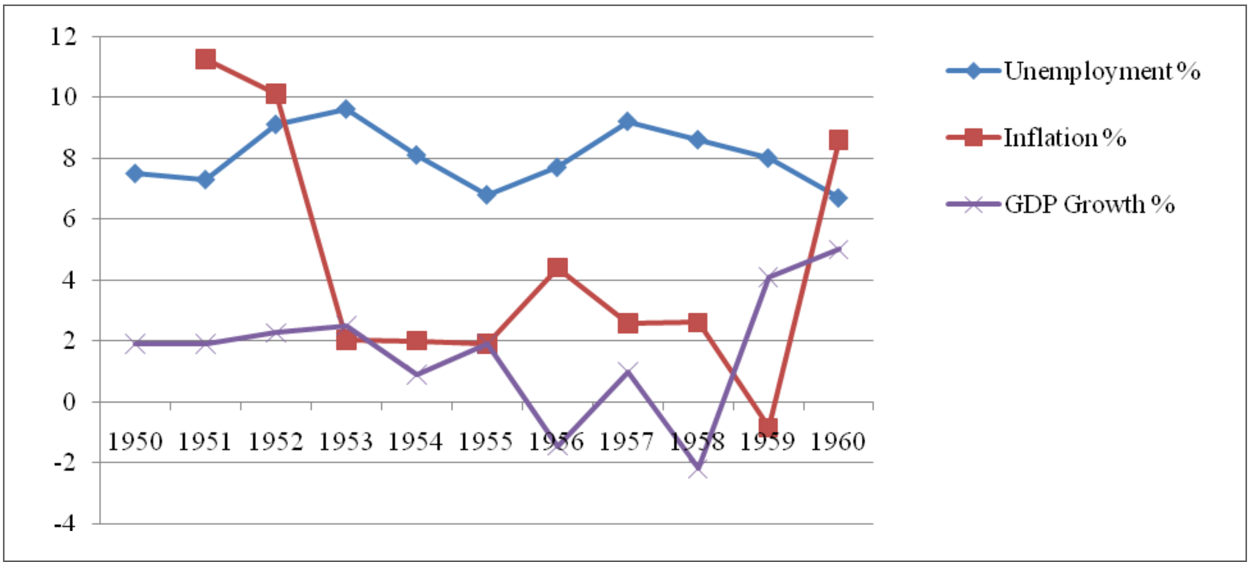
Year	Unemploy-ment	Inflation	Government Debt to GNP	Growth Rates in Real GDP	Industrial Disputes days lost	Economic Openness[1]
	%	%	ratio	%	('000s)	
1950	7.5	0.0	N/A	1.9	217	70.9
1951	7.3	11.25	49.9	1.9	545	82.6
1952	9.1	10.1	N/A	2.26	529	69.6
1953	9.6	2.04	N/A	2.5	82	66.9
1954	8.1	2.0	N/A	0.9	67	65.5
1955	6.8	1.9	N/A	1.9	236	67.2
1956	7.7	4.4	N/A	-1.45	48	63.9
1957	9.2	2.57	N/A	0.98	92	62.7
1958	8.6	2.6	N/A	-2.2	126	62.9
1959	8.0	-0.85	55.5	4.1	124	62.7
1960	6.7	0.86	57.5	5.0	80	64.7

Sources: Leddin, Anthony J., & B. M. Walsh. 1998. The Macroeconomy of Ireland. (4th ed.) Dublin: Gill & Macmillan; Mitchell, B. R. 1993. *International Historical Statistics. Europe 1750-1988*. (3rd ed.) Hong Kong: Stockton Press; Eurostat Yearbook 1997. Luxembourg: Office for Official Publications of the European Communities; Heston, A., Summers, R. & B. Aten. 2002. Penn World Table Version 6.1, Center for International Comparisons at the University of Pennsylvania (CICUP).

The OECD (1961: 5) and the Central Bank of Ireland (1961: 5) saw the 1950s as a time of economic depression. Agricultural production was abnormally low, industrial output was faltering (OECD, 1961: 8) and there was a large external trade deficit (Central Bank of Ireland, 1957: 27). In a damning indictment of the economic situation, the Central Bank (1959: 32) stated that "a study of events during the past ten years, of the courses that have been pursued and of their consequences, is a necessary preliminary to the formulation of any sound proposals for the improvement of the national economy." The Central Bank (1957: 34) also observed that "the present economic and financial situation scarcely justifies the retention of confidence in large-scale expenditure on public works and social amenities as a means of stimulating useful economic activity." This report spoke of the dangers of insolvency and the loss of economic sovereignty and how this would result in a level of emigration to dwarf anything previously experienced.

The national/international media expressed negative opinions on the economy. The *Irish Independent* (1959a: 4) argued that the foundations of the economy were in need of repair. *Time International* (1958: 44) remarked that there had been few economic advances for Ireland during the 1950s. *The Irish Times* (1959a: 9) observed that employment in the economy was in decline and the cost of living had gone "sky high". *The Economist* (1959: 15) concluded that prior to 1959 most indicators of Irish economic performance were dire. It went on to argue that righting the economy would be the paramount task confronting the country. *The Sunday Press* (1987: 12) referred to "a general economic collapse" in Ireland and a lack of will to tackle the problem. By mid 1958 the *Irish Independent* (1958a: 11) was arguing that economic isolation was impractical.

Figure 1: Unemployment, Inflation, GDP Growth Rates



Sources: Leddin, Anthony J., & B. M. Walsh. 1998. The Macroeconomy of Ireland. (4th ed.) Dublin: Gill & Macmillan; Mitchell, B. R. 1993. *International Historical Statistics. Europe 1750-1988.* (3rd ed.) Hong Kong: Stockton Press.

"In the 1950s, Ireland's relative [economic] performance was disastrous, poorer than that of the UK as well as the European average" (Ó Gráda and O'Rourke, 1995: 214). In 1957, manufacturing output was no higher than in 1953, while building activity was stagnant. All activity in the industrial sector depended upon a static home market (OEEC, 1958: 15). "By the middle of the 1950s a serious crisis of confidence developed, caused by widespread anxiety that the performance of the economy was so poor the country was falling behind Western European standards, not only in productivity, but in the social benefits productivity might be expected to confer" (Lyons, 1973: 618).

According to Whitaker (1973: 415), by 1957, the economy was plumbing the depths of hopelessness. Stop-go policies, in which adverse balance of payments signaled drastic fiscal actions were to follow, produced severe and unnecessary fiscal contractions in 1952 and 1957 (Kennedy and Dowling, 1975). In the late 1950s, the outlook for the economy was depressing, while the economies of Europe achieved strong growth (MacSharry and White, 2000: 14-19).

4. Ireland 1950s – The Policy Response

The economic stagnation of the 1950s led to a "vigorous debate on the economy" (O'Day, 2000: 27). A questioning of protectionism was conducted at the national level among civil society groups and within the media. This was justified by the need for additional capital to permit the expansion of industry, to increase employment and reduce emigration. The *Irish Independent*

(1958b: 9) observed that there was a pressing need to increase exports. The Federation of Irish Manufacturers (FIM) called for an investigation of the impact on Irish industry of a managed free trade regime (*Irish Independent*, 1958c: 10). This debate was influenced by economists warning that if a free trade area was established in Europe, Ireland would have no option but to join (Ainsworth, 1956: 2). By the late 1940s, the General Agreement on Tariffs and Trade (GATT) was created and a few years later the European Coal and Steel Community (ECSC) came into existence. Protectionism, acceptable in the context of the 1930s, was swimming against the tide of trade liberalization by the 1950s.

In response, the collation government of Fine Gael and the Labour Party (1954-1957) initially stretched protectionist policy to incorporate aspects of attracting foreign investment and encouraging exports. It was a last ditch effort to maintain some element of protectionism. However, Taoiseach John A. Costello came to realise that increasing employment would require foreign investment (The Irish Times, 1954: 9). Thereafter, the Minister for Industry and Commerce, William Norton "signalled the growing need to attract foreign direct investment to facilitate industrial expansion" (Donnelly, 2007: 144). Norton was to subsequently travel repeatedly to America seeking to attract investment in Ireland (Ainsworth, 1956: 2). The Finance Act of 1956 was introduced to encourage exports by Irish and foreign owned companies (Donnelly, 2007: 145). The Industrial Development Authority (IDA), established in 1949 to encourage indigenous industries, was permitted in 1956 to distribute grants to foreign owned export-orientated industries (Suarez, 2001). Within a short time, the IDA was advocating export led industrialization, with foreign investment as its driving force. Export Profit Tax Relief (EPTR) was introduced in 1956 at the level of 50 percent for 5 years (Breznitz, 2007: 152). EPTR sent two messages: first, Ireland was pro-enterprise through rewarding profit; second, the country favored a long-term investment (MacSharry and White, 2000: 246-7). These alterations to protectionism were an admission by the government of the failure of the philosophy underlying this approach, as they contained a direct, if unintended, challenge to the philosophy's intellectual coherence (Tansey, 1998: 12).

The protectionist policy matrix, made up of a range of different legislation, special import levies and customs duties, and developed over more than generation, was fraying (Donnelly, 2007: 149-150). Lynch (1959: 7) argued that as the old economic policies had failed what was needed was a new and clear sense of direction. He suggested that closer economic cooperation with Britain was not at variance with Irish nationhood. The Irish Times (1959d: 7) argued that the results of protectionism were twofold: the sheltering from competition of inefficient firms producing inferior goods and the resultant bad will Irish exporters had to face abroad. In this fraught environment of disappointing economic performance and policy failure, existing ideational orthodoxy was contested and this, coupled with a general consensus among agents that this orthodoxy was inadequate, resulted in its collapse. As a result, "1957 is conventionally thought of as the end of an era, making the final exhaustion of the ideas of the first generation of political leaders" (Garvin, 1982: 37).

During the 1957 general election Fianna Fáil attacked the economic model it had created a generation before and the prevailing economic stagnation. Senior Fianna Fáil politician Seán Lemass argued that increased employment would only come from exports and that this was possible by attracting in foreign capital and through tax exemption for exporting firms (The Irish Times, 1957a: 1). Since the early 1950s, he had argued that tariffs and restrictions against foreign investment, that had long protected native industries, be revised (Savage, 1999: 18). By early 1955, Lemass was calling for a re-examination of economic policy. Another member of Fianna Fáil, Erskin Childers, declared that 1957 was an election to make "tremendous changes to economic and national policy" and "unless exports were enormously increased Ireland would sink to a fourth rate state" (The Irish Times, 1957b: 5).

Following Fianna Fáil's victory, Lemass, the new Minister for Industry and Commerce, "began the process of opening up the state to foreign investment" (Girvin, 1994: 125), a process tentatively begun under the preceding coalition government (Donnelly, 2007: 140ff). Lemass, who had once championed protectionism, under the influenced of T.K. Whitaker, Secretary of the Department of Finance, became convinced that "developing industry to supply the home market had reached its limit" (Donnelly, 2007: 154). T. K. Whitaker was committed to a policy of export-led economic growth, a commitment that stemmed from his recognition that economic policies pursued to that time had failed (Lee, 1989: 343). He advanced a three-pronged strategy within Finance – more planning, fewer tariff barriers and a greater emphasis on productive investment. His document *Economic Development*, regarded as "a watershed in the modern economic history of the country" (Lyons, 1973: 628), proposed the gradual transition to free trade, the introduction of grants and tax concessions to encourage export orientated manufacturing and the inducement of direct investment by foreign export oriented manufacturers. It stated "the policies, hitherto followed, though given a fair trial, have not resulted in a viable economy" (Economic Development, 1958: 2). *Economic Development* marked the culmination of a major strand of activism within parts of the higher echelons of the civil service (Murphy, 1997). It advocated the abandonment of the protectionist programme Fianna Fáil pioneered since the 1930s. This was to prove the genesis of a new paradigm with which to manage the economy.

Whitaker, Ireland's premier civil servant, was a powerful policy entrepreneur, as his ideas, as set out in *Economic Development,* formed the backbone of the 1958 government White Paper, *First Programme for Economic Expansion* (Horgan, 1997). This document laid out a coherent set of economic ideas which argued that the way forward for the economy was through industrial expansion based on production for the export market. Although *Economic Development* and the *First Programme for Economic Expansion* were vague as to policy instruments and targets, they presaged a new consensus on the need for a more outward-looking economic policy.

Despite the recognition that extant policy had failed, few politicians, either in the government, or opposition, initially took notice of either policy document, apart from Leamss (Murphy, 2005: 32). The newspapers also ignored *Economic Development* upon it appearance. It is astonishing how what was to proved the most important Irish economic policy document garnered almost no attention upon publication, its significance initially recognised only by the entrepreneurial network (Whitaker and his colleagues within the Department of Finance) that fostered it and by Lemass the political entrepreneur who championed it. However, gradually a variety of policy entrepreneurs such as the newspapers, trade unions and other interest groups came to support the ideas contained in *Economic Development.* The result was a fundamental reappraisal of the policies pursued since the 1930s.

In 1959, Lemass succeeded Éamon de Valera as Taoiseach. The state of the economy, and the ideas propagated by Lemass and Whitaker, persuaded the opposition parties to support the government, as they came to "realised that the Irish economy could not survive in isolation" (Murphy, 1997: 57). During the Dáil debate on Lemass' election as Taoiseach, the leader of the opposition party Fine Gael remarked that the magnitude of the economic problems could only be righted by a tremendous effort from all sections of the community (Dáil Éireann Debates, 2 December, 1958, Vol. 171). Daniel Desmond of the Labour Party argued it was time for the political establishment to realise that the problems with the economy superseded the party politics (*Irish Independent*, 1959b: 9). Lemass said "the task of this generation is to consolidate the economic foundations of our political independence" (*The Irish Times*, 1959b: 8). He stressed that "we have got to demonstrate beyond question the capacity to develop a viable economy" (Dáil Éireann Debates, 28 April, 1959, Vol. 174). That there was consensus on this issue between such bitter rivals as Fianna Fáil and Fine Gael, should not be underestimated. While opposition parties might be expected to talk down an economy, when the government is in agreement with their evaluations, then normal politics has been suspended – a situation that only arises in democracies when they face severe challenges. In the early summer of 1959, as Lemass was assuming power, the leading interest groups in society were beginning to row in behind what

Economic Development stood for (*The Irish Times*, 1959c: 9). Lemass now had both the mandate and opportunity to inject the new ideas into the policy arena. This fact, combined with the overall mood of economic despair in the country, was to permit Lemass slaughter a number of previously sacred political cows (Lee, 1989: 341).

As Taoiseach (1959-1966) Lemass displayed a vigorous entrepreneurial leadership (McCarthy, 1973: 22). Under his guidance, an outward-orientated economic strategy, containing increasingly liberal trade policies, became the bedrock of Irish macroeconomic policy (OECD, 1962: 12; O'Donnell, 1998: 4). Joining the European Economic Community (EEC) became a central platform of this transformed policy paradigm. Adjusting industries to competition led public policy into the realms of industrial relations and pay bargaining. Lemass understood that the government had to play a more active role in the Irish economy, but realized that the success of this strategy assumed a new partnership with different interest groups, which would become players in the policy game (Murphy, 1997: 58). The trade unions and employer organisations were brought into the policy-making environment. Thus, "the dialogue between state and major socio-economic groups acquired a regular and institutional character" (Peillon, 1995: 370).

During the economic crisis of the 1950s the coalition government's opening of the economy stretched the protectionist paradigm. Extant policy's failure to deal with the economy's problems led to the collapse of ideas underlying protectionism. This situation created a window of opportunity for Lemass, acting as the political entrepreneur, to replace protectionism, embedded over the preceding decades, with an outward orientated paradigm advocated by policy entrepreneurs such as Whitaker. A strong advocacy coalition developed around Lemass and the ideas that he championed. That Lemass was a senior politician fits with Campbell's (2004) argument that change is more likely if the political entrepreneur commands more resources. The alternative policies implemented by Lemass punctuated the policy equilibrium with the result that a dramatic policy change ensued.

5. Sweden 1981/1982 – The State of the Economy

After the 1973 oil crisis Sweden experienced an enduring recession and stagflation. Although among the world's richest countries, Sweden and its model of centralised corporatist collective bargaining began to strain under the burden of supporting its expansive social welfare system (*Time International*, 1976: 8). The economy was no longer growing as fast as it had and the industrial sector – the source of Sweden's prosperity – began to shrink (Lundberg, 1982: 199). This contributed to the Social Democratic Party's (*Socialdemokratiska Arbetarepartiet* (SAP)) loss of power for the first time in 44 years in 1976. The SAP had been the most dominant political party in Western European politics. Thereafter, the SAP shifted more to the right of the political spectrum. The non-socialist government commissioned reports on the economy that were infused with "the rising currents of monetarism, public choice theory, and neo-liberalism that were to come to the fore in the coming decade" (Andersson, 2006: 101). The second oil crisis reinforced the impact of the first. Economic performance during the first two years of the 1980s was poor. Furthermore, in spite of the adjustment policies pursued by the authorities, correction of the imbalances that had built up since the 1970s was slow and the economy remained in disequilibrium (OECD, 1984: 7).

Full employment came to depend increasingly on the expansion of the public sector (OECD, 1992: 62). Consequently, growth in public expenditure outstripped the growth of the economy (OECD, 1984: 9). The public sector's share of GNP rose under the non-socialists (1976-1982), so that by 1982 public sector expenditure constituted 67 percent of GNP (OECD, 1990: 59). This explains how the number of public sector jobs increased by 43 percent between 1972 and 1982, coming to outnumber those in private industry after 1978 (Gress, 1988). There were also signs of conflict between the growing army of public-sector employees and private sector counterparts. "In the 1970s, wages exploded in a self-destructive series of agreements that placed Swedish firms in the un-competitive position of having the highest paid labour force in the world" (Ahlén, 1989: 333).

Productivity growth declined significantly from 1970 onwards, due to the size of the public-sector (Lindbeck, 1997). This had a knock on effect on the level of exports, which stagnated over the decade (Ryden and Bergstrom, 1982). Worryingly, Sweden's share of the world economy dropped 40 percent during that decade (Peterson, 1987). Foreign competition made substantial inroads on the Swedish domestic market, as suggested by the steady rise in the share of imported manufactured goods (OECD, 1984: 12).

Central government's expenditure grew at a faster pace by the end of the 1970s than at the beginning of the decade, while revenues stagnated. With a sluggish economy, stagnant revenues and rising expenditures, the government's budget deficits accelerated during the 1970s, reaching 13 percent of GNP in 1982 (Siven, 1984: 17) five times its level in 1976 (Osnos, 1982: A15). The Riksbank predicted that "the deficit on the national budget would grow from around SKr78 billion under the 1982-83 budget to some SKr90 billion in 1983-1984" (Dullforce, 1982: 1). By 1982 Sweden's debt/GNP ratio stood at 59.3 percent, whereas 12 month before it had been 50.8 percent, its growth an indication of the size of the budget deficit. "In an international context, both the level of the budget deficit, and the swing in the budget balance since the mid-1970s has been more pronounced than in most other OECD countries" (OECD, 1982: 16). The budget deficits were financed through international borrowing and as a consequence, the debt/GNP ratio increased by 250 percent in the six years between 1976 and 1982 (Siven, 1984: 17). However, there was no political mandate for either radical budget cuts or revenue enhancements. To avoid internal disputes, the non-socialists parties in government wanted neither to raise taxes nor be accused of trying to dismantle the welfare state (Branegan, 1982: 32). In 1981, inflation hit 12.1 percent and unemployment reached 3.1 percent in 1982, its highest level since 1945 (Appendix A). Although this would have been a low figure elsewhere, it was a scandal in a country accustomed to full employment (Apple Jr., 1982: 3). However, many economists believed unemployment was closer to 16 percent if it included the jobless in training programs, workers forced into early retirement and those who had given up looking for work (Branegan, 1982: 32).

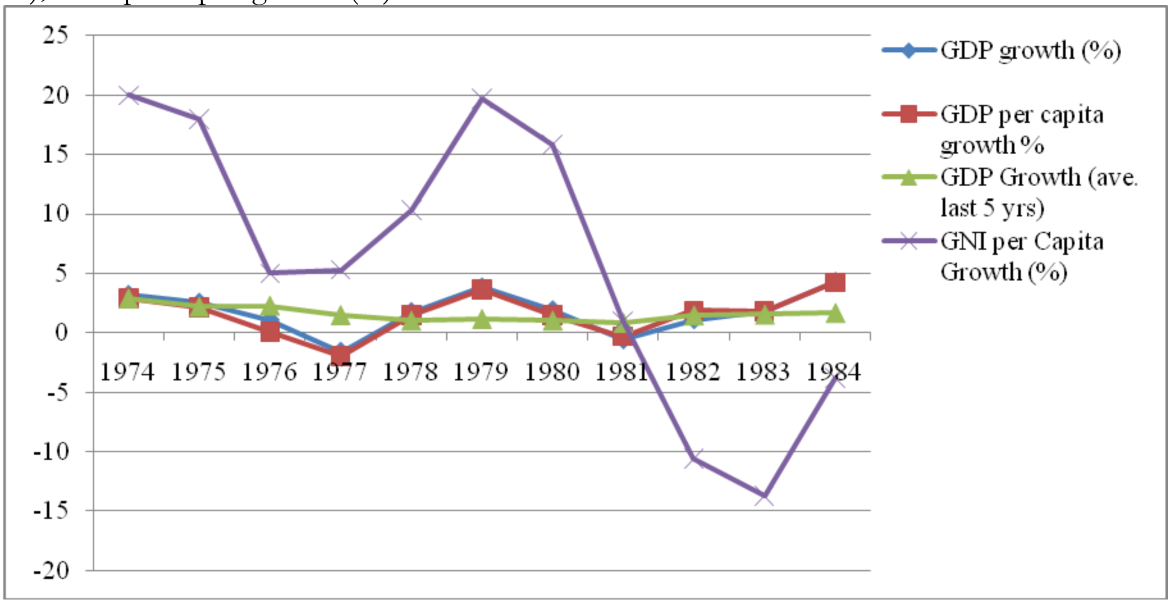
Table 2: Sweden's Main Economic Indicators, 1973 – 1983

Year	Unemploy-ment	Inflation	Government Debt to GNP	Growth Rates in Real GDP	Industrial Disputes days lost	Economic Openness[1]
	%	%	ratio	%	('000s)	
1973	2.5	6.7	22.6	3.9	12	50.90327
1974	2.0	9.9	24.2	4.3	58	63.73183
1975	1.6	9.8	24.4	2.2	366	55.24588
1976	1.6	10.3	23.6	1.2	25	55.70874
1977	1.8	11.4	26.5	-2.0	87	55.18196
1978	2.2	10.0	31.8	1.3	37	54.19376
1979	2.1	7.2	37.9	4.3	29	60.43795
1980	2.0	13.7	43.2	1.9	4,478	60.14818
1981	2.5	12.1	50.8	-0.6	209	59.64625
1982	3.1	8.6	59.3	1.1	2	64.93382
1983	3.5	9.0	64.6	1.8	37	68.92182

Sources: Mitchell, B. R. 1993. *International Historical Statistics. Europe 1750-1988*. (3rd ed.) Hong Kong: Stockton Press; Eurostat Yearbook 1997. Luxembourg: Office for Official Publications of the European Communities; Heston, A., Summers, R. & B. Aten. 2002. Penn World Table Version 6.1, Center for International Comparisons at the University of Pennsylvania (CICUP); OECD, 1995. Labour Force Statistics. OECD: Paris; Statistical Annex of European Economy, Spring 2003.

For Swedes, the state of the economy constituted an unprecedented situation. Economic growth, which had averaged 2.5 percent throughout the 1970s, contracted in 1981 and expanded by only 1 percent in 1982. Figure 2 shows that all indicators of GDP growth were low in the early 1980s, while GNI per capita growth collapsed. In the context of the international recession of the early 1980s, the budget deficit prevented the government pursuing a counter-cyclical fiscal policy.

Figure 2: Sweden (1974-1984) GDP Growth(%); GDP per capita growth(%); GDP growth(5 yr. av); GNI per capita growth (%)



Source: Data Gob, Government Indicators Database

Branegan (1982: 32) argued that the Swedish economy, once the envy of Europe, had been hobbled by foreign debt, an adverse balance of payments, slow growth and unemployment. Compounding matters, Swedes were reluctant to see the welfare state cut back and to accept the remedies proposed to deal with their problems. "'The welfare state is in a crisis of legitimacy'", observed Hans Vetterberg, Sweden's leading public opinion analyst, "'we can no longer afford to keep expanding it'" (Osnos, 1982: A15).

6. Sweden 1981/1982 – The Policy Response

Although right wing parties formed a number of governments between 1976 and 1982, none was in a position to challenge the SAP as the single largest political party in Sweden. On many issues the non-socialist parties remained divided (Peterson, 1987: 33), consequently the coalition could not agree on a set of policies to counteract the deteriorating economic situation (Olsen, 1984). Ironically, these right wing administrations nationalised and subsidised weak industries, something the SAP had resisted during its decades in power (OECD, 1978: 21). *Dagens Nyheter* argues that until the massive expansion of the public sector Sweden experienced decades of consistent growth[1]. The problem was that the public sector took up spare labour in a recession, but did not shed it during economic expansion. Consequently, productivity in the private sector declined[2]. The non-socialist parties' failure to improve economic performance led to

[1] Dagens Nyheter, 27 January, 1991, p. 7.
[2] Dagens Nyheter, 3 January, 1992, p. 4.

disenchantment. By 1981, the non-socialist coalition held only 102 of the 350 seats in the *Riksdag*[3].

In autumn 1981, a 10 percent devaluation of the krona was conducted and in the spring of 1982 the non-socialist coalition government introduced an austerity program. The government hoped its attempts to combat the economy's problems would generate respect for non-socialist policies; instead they generated criticism and initiated a debate on the economy. The reductions in pensions, sick pay and subsidies for food, to slow the growing deficit, alienated large sections of an electorate already burdened with taxes (*Time International*, 1982: 23). Consequently, the opposition SAP gained in popularity (Hadenius, 1997: 129-30).

The 1982 election, dominated by talk of economic crisis (Osnos 1982: A15), was regarded as determining whether public opinion had shifted away from social democracy. Debates surrounding the economy failed to generate a coherent set of alternative ideas, although policy entrepreneurs such as the Swedish Employers' Federation (*Svenska Arbetsgivarforening* (SAF)) created Centre for Business and Policy Studies (SNS) and Timbro had begun to disseminate monetarist ideas (Blyth 2002: 214-15). However, no political entrepreneur emerged during this period of ideational contestation. This was primarily because no politician, for fear of electoral suicide, was willing to openly propose the abandonment of the welfare state, or its associated policies, despite the failure of these policies to meet contemporary challenges. Legro (2000) argues that the failure of change agents to cluster around a new economic ideational paradigm means that societal actors will invariably re-embrace an existing orthodoxy.

During the campaign the SAP, under Olof Plame, attacked the viability of another non-socialist government. The party presented a Crisis Programme on how Sweden could save and work its way out of the crisis. This was to be a mildly reflationary programme, as a palliative for a public ill at ease with the economy's failings. Nearly all the economic ideas they presented were variations upon existing themes. In lieu of alternatives, the ideas underpinning the policies of the welfare state endured. However, the problems with the economy deprived the non-socialist government of credibility (Mjoset, 1992).

SAP won the election with a set of proposals to correct extant policies and by exploiting voters' growing fears over rising unemployment and their disenchantment with the policies of the outgoing Prime Minister Thorbjörn Fälldin (*Time International*, 1982: 23). With Olof Palme's return, traditional socialist policies went to the top of the agenda, albeit in altered form. The SAP government's recovery program was entitled the Third Way (Apple Jr., 1982: 3). It argued that renewed growth required redistribution of income from labour to capital. This also marked a major change in SAP economic planning, behind which lay the influence of its research department which, since 1976, had achieved ascendancy over the Trade Union Confederation's (*Landsorganisationen i Sverige* (LO)) research department within the labour movement (Meidner, 1989). The subsequent cuts in the public sector and restraint in wage negotiations resulted in divisions between the SAP and the LO (Andersson, 2006: 116). Palme effectively rejected the non-socialists approach of squeezing inflation out of the economy at the risk of higher unemployment. Instead, he intended to keep people in employment by paying them less and by giving Swedish industry a real cost advantage to allow for expansion. This marked an attempt to demonstrate the SAP's capacity to revitalise the economy while maintaining a level of social democracy (Martin, 2000: 234; Walters, 1987: 65).

The Third Way was a wide-ranging stabilization program encompassing demand management measures, as well as initiatives to promote structural change and ensure an equitable distribution of the burden of adjustment (OECD, 1984: 21). The SAP was determined to pour funds into job-creating industries and to increase taxes for that purpose. The party planned to spend $100 million, and hoped to attract an addition $350 million in private investment, to create 40,000 jobs (Apple Jr., 1982: 3). The centerpiece of Finance Minister Kjell-Olof Feldt's strategy

[3] http://www.const.sns.se/swedishpolitics/

was the devaluation of the krona by 16 percent (Walters, 1987: 74). The SAP had identified labour costs as the key to international competiveness. This was implemented in conjunction with a price freeze and increases in sales and corporate taxes, in a sweeping "crisis plan" to stimulate the economy and eliminate its imbalances (Dullforce 1982: 1).

According to the OECD (1984: 21) the objective was to achieve export led, investment-driven, recovery. The LO, the largest trade union association, accommodated devaluation by demanding average wage increases of 2.5 percent in ensuing bargaining. The devaluation and international economic recovery resulted in high earnings and export expansion (Ahlén 1989: 333). The thrust of SAP policies pointed in a different direction than previously, with Feldt determined to give priority to private sector growth, profits and market forces. A series of structural reforms were introduced overturning the traditional priorities of the SAP. Under pressure for more individual freedom, and the internationalisation of the economy, these reforms saw the SAP move in a neo-liberal direction (Taylor, 1991: 3).

Fiscal policy was held tight and the slimming of the public sector would, it was argued, create crowding in effects (Mjoset, 1992: 349). The public sector austerity strategy, with a profit explosion and wage restraint, created tension between the SAP and LO. Nevertheless, the government restored welfare entitlements cut by the non-socialists (OECD, 1984: 23). To placate the LO, the SAP, in the face of SAF opposition, introduced wage-earner funds in 1983. In 1976 the LO proposed a levy on corporate profits be used to transfer control of enterprises with more than 50 employees to the unions. At the time the SAP had been sceptical about the idea (Whyman and Burkitt, 1993: 612). "Industrialists regarded the funds as a device to achieve bureaucratic control of industry" (Gress, 1988: 130). However, the version implemented in 1983 had been heavily modified from Rudolf Meidner's proposal in 1976 (Gould, 1993). It was transformed "from an overtly socialist union proposal to a number of toothless share holding funds" (Meidner, 1993: 223). Consequently, the modified version of the funds dissatisfied the LO (Lewin, 1985a: 296). To maintain the welfare state the SAP had prioritized private sector growth. The Third Way marked a reversal in the SAP's perspective on social policy, moving from an emphasis on investment in growth to an emphasis on cost reduction (Andersson, 2006: 124).

Despite social democracy's failures, Sweden, as a society, displayed a reluctance to abandon this model. None of the political party leaders were willing to dismantle this pillar of Swedish society, as all sought to maintain its existence in one form or another. On returning to office, the SAP reasserted its commitment to the Swedish model's precepts of an active role for government in stimulating economic growth and maintaining full employment (Walters, 1987: 74). The SAP presented its Third Way proposals for public expenditure cuts and prioritizing the private sector. This strategy, while damaging the SAP's relationship with its trade union allies, contributed to Swedish economic expansion in conjunction with an international economy recovery. The economic crisis provided a window of opportunity for the SAP to implement new economic policies that altered the established policy approach that had existed over the preceding decades. The ad hoc changes made by the Palme government, to ensure that the welfare state endured, stretched extant economic philosophy. Transferring increasing income from labour to capital undermined the extant philosophy's intellectual coherence. For Kjellberg (1992: 88) this marked the demise of the Swedish Model. As the *Financial Times* stated, Palme's return did not mean that socialism triumphed, but that the non-socialist parties had not succeeded in adjusting the expectations of the electorate to Sweden's straitened economic circumstances

7. Conclusion

In examining the Irish and Swedish policy responses to the economic crises, this article highlights the interdependence of politics and economics. Conducting this examination within the context of the policy change literature assists our understanding of the process of policy change.

In Ireland, the failure of protectionist policy was compounded by a number of ad hoc amendments that undermined its coherence. With extant economic policy punctuated, policy entrepreneurs' ideas on how to fix the economy attracted the attention of Seán Lemass who, playing the role of political entrepreneur, used the window of opportunity the economic crisis had created to take economic policy in a different direction. Political consensus developed around the new policy idea of free trade, which saw a transformation in the hierarchy of the goals behind economic policy. As a result, Ireland adopted a radically different approach to managing its economy. This move was to reverse a policy course that the wider Irish political elite had followed slavishly for a generation.

In Sweden, economic policy was failing by the beginning of the 1980s. This was due to a combination of the after effects of the oil crises and a bloated welfare state. However, no politician wanted to challenge the monolithic welfare state, despite the fact that it did not seem to be accommodating capitalism any longer. As a result, a genuine policy alternative did not emerge, with the SAP only shifting economic policy to the centre with its Third Way programme. This programme, placing priority on private sector growth and initiative while shrinking the public sector, was seen as necessary to make the economy more dynamic and growth oriented in order to maintain a level of social democracy. Thus, the overarching economic policy remained largely intact. However, ad hoc alternations to this policy only served to undermine its intellectual coherence, as had happened in Ireland with protectionism almost 30 years before. Nevertheless, Sweden soldiered on with its faltering policy, reluctant to confront its limitations.

In both countries, economic crises provided windows of opportunity for policy changes to occur. Extant macroeconomic policy failed in Ireland in the 1950s and in Sweden in the early 1980s, with the result that the ideas underlying extant macroeconomic policy collapsed. In the wake of perceived policy failure the critical issue was for policy entrepreneurs to come forward with alternative ideas on how to fix the economy and for these ideas to find a champion in the political environment. Thus, new ideas and the positions of those who champion these ideas, are crucial in determining the nature of the policy change that occurs in response to policy failure. Policy failure on its own is not sufficient for policy change to occur.

The cases examined here are not purely of historical interest. They serve to illustrate the cross national diversity of crisis experiences and responses that always has to be recognised in political economy analysis. In the wake of the current global financial crisis we have been presented with the spectacle a range of countries, as well as sub national jurisdictions, struggling to prevent economic collapse. Iceland has seen its financial system fail spectacularly; Greece and Ireland are both in the midst of political and economic turmoil that has raised serious questions about the future of both the Euro and the wider European Project. There are growing concerns about the sovereign debt situations in Portugal, Spain, and Italy. California, ground zero for the US subprime mortgage debacle, is being referred to as a failed economy and a failed state (Harris, 2009: 32). Thus, the historical issues considered in this paper have a significant contemporary echo.

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