The pursuit of growth. Growth regimes, growth strategies and welfare reforms in advanced capitalist economies

Anke Hassel, Bruno Palier, Sonja Avlijas

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1. Introduction[1]

The "Trente Glorieuses", the thirty prosperous years following World War II, were characterized by a continuous level of high growth in gross domestic product (GDP) (4% on average in the Organisation for Economic Co-operation and Development (OECD) countries) and a low rate of unemployment (below 2% for most OECD countries). In all OECD countries, growth and job creation were based on vast productivity gains in mass production in manufacturing industries and on mass consumption, which were at the core of "Fordism" (Boyer 1990). This spectacular period of continuous growth and job creation was associated with the rapid expansion of the welfare state. Social spending increased fivefold between 1945 and the late 1970s in the OECD countries (Flora 1986). The development of the welfare state enabled a redistribution of the increasing wealth, but it also contributed to growth by supporting citizens' consumption and by enhancing workers' productivity through educational, training, and health policies.

Since the mid-1970s, however, in most OECD countries average growth rates have been lower and average unemployment levels higher than during the Trente Glorieuses. Unemployment levels have increased since the early 1970s by 5 to 10% and have more or less hovered between 5 and 20% since the 1980s in the OECD (Emmenegger et al. 2012). Moreover, the share of atypical employment in the overall OECD workforce (part-time and fixed-term combined) has grown from around 10% to between 25 and 35%, depending on the specific country (idem).

It has now become clear that advanced industrialized countries have undergone major economic restructuring since the 1970s. The internationalization and globalization of production, as well as the diffusion of information and communication technologies (ICT), have posed enormous challenges to mature industrialized countries. Deindustrialization is associated with job losses and declining growth rates and it is having a strong, negative impact on the sustainability of welfare states (Pierson 1996). In the process of restructuring, countries' socio-economic systems have changed. The Netherlands, once viewed as a classic coordinated market economy and traditionally a conservative welfare state, today has the biggest private system of pension funds in the Western world (measured as % of GDP). Sweden, a coordinated market economy known for its generous and egalitarian welfare system, has experienced rapidly rising levels of inequality, in particular among household incomes. On the other hand, countries classified as liberal market economies, such as the United Kingdom, Australia, and New Zealand, have higher minimum wages (measured in % of average hourly pay) than Germany, Belgium, and the Netherlands (Schulten and Lübker 2019), which are traditionally classified as coordinated market economies. In Western Europe, Germany is the country with the largest low-pay segment as of 2019 and has had the biggest increase in working poor since the late 1990s (Spannagel et al. 2017). The established wisdom that divided the advanced industrialized world

[1] This article is a summary of Hassel and Palier (2020) and Avlijas et al. (2020). It contains a substantial overlap with both chapters.

into two camps of socially balanced, Continental European economies versus unequal, Anglo-Saxon economies should be revisited.

In this article, we provide an explanation for the various trajectories of change of rich countries over the last four decades based on Hassel and Palier (2020) and Avlijas et al. (2020). We develop an analytical framework to study how economies and welfare systems have been adapted to the common challenges of post-industrialization, financialization, and the knowledge economy and show that, despite the global interconnectedness of modern economies, national trajectories of growth and policy-making remain distinct.

Our explanation focuses on the pursuit of different growth strategies in contemporary advanced capitalist economies. Growth strategies are in large parts welfare reforms. Governments use the policy tools of the welfare state such as housing policy, pensions, minimum wages and education as facilitators for growth. They pursue them in different ways depending on the growth regime their economies are embedded in. We argue that the restructuring of welfare systems in advanced economies are largely a result of the growth strategies governments adopt.

The next section offers an overview of two key concepts used to build our argument: i) the complementary relationship between national growth and welfare regimes and ii) growth strategies through which growth and welfare regimes are reformed in the new era of globalization, ICT and financialization driven growth. Section 3 then identifies five distinct growth regimes in Europe, followed by the analysis of the ties between growth strategies and welfare reforms in section 4. Section 5 concludes.

2. Welfare Reforms and Growth Strategies

Growth regimes are long-term sets of institutions that specialize in particular economic activities: manufacturing exports, financial services, dynamic services or as part of the supply chain for multinational companies. Integrating insights of the Regulation School and the comparative welfare state literature with the Varieties of Capitalism (VoC) account, Bruno Amable distinguished five types of capitalism[2] (Amable 2003). Like other comparative political economists, he assumes that institutions shape economic relations, and proposes a categorization of these institutions, in order to understand the differences between these five types of capitalism. Namely, he shows that institutions differ in areas of product market competition, labor market and labor relations, social protection, education systems, and financial systems (Amable 2003).

Recently, the "growth model" literature, in particular Baccaro and Pontusson (2016), re-emphasize the role of demand for economic growth. They propose "to distinguish three different alternatives to the traditional Fordist model of wage-led growth: consumption-led growth financed by credit, investment-led growth and export-led growth" (2016, 186). They focus on what they consider to be the two main models: the consumption-led and the export-led growth models, with four possible cases: Germany, relying exclusively on exports; the UK,

[2] Neoliberal or market-based capitalism, Continental European capitalism, social-democratic capitalism, Mediterranean capitalism, and Asian capitalism.

driven by domestic demand (financed by credit); Sweden, as a combination of consumption and exports; and Italy, where neither exports nor consumption seem to work.

Export-led growth is associated with a regime in which economic relationships are negotiated and controlled by economic players (employers and unions), who have coordinated interaction, especially with regard to wage-setting and training. In many coordinated market economies (CMEs), high levels of centralization and the coordination of wage-setting help to contain wage pressure and, therefore, control the real exchange rate. They also contribute to a compressed wage structure, which gives incentives to train the low-skilled and asks the high-skilled to forego higher wages. Wage moderation allows for higher investment. All these elements are favourable to the competitiveness of exports. Fiscal and monetary policies are rather restrictive, due to the high share of exposed sectors in the economy (Hall and Soskice 2001; Scharpf 2020). By contrast, liberal market economies (LMEs) have a tendency to rely more on domestic demand for their growth, which can be associated with a regime where dynamic services, and especially the financial sector, play a bigger role (and allow access to consumption through credit, see Crouch 2009 and 2013).

The "growth model" literature's focus on aggregate demand is a necessary complement to the previous generation of research which concentrated on the supply side of the economy. It does not seem to contradict the older classification of the economies, but rather enrich it. The mere binary distinction (the role of exports versus domestic demand in stimulating growth), however, while elegant in its simplicity, overlooks the stark differences between economies, such as the United States and France, on the one hand (both recognized as domestic, demand-led growth models), and Sweden and Germany, on the other (both classified as export-led growth models). These countries differ significantly on other accounts, such as their levels of financialization, ICT use, private debt, the capacity to use currency devaluation, as well as their levels of inequality, and ultimately their rates of economic growth and employment. As acknowledged by Baccaro and Pontusson (2016), we therefore need to further the analysis of the variety of domestic demand-led and export-led growth models, their origins, and implications.

In order to do so, we need a more detailed understanding of the nature of exports, as well as the nature of domestic demand. Different types of export-led growth models have developed, specializing in either the export of manufactured goods or of dynamic services. Also, on the side of domestic demand, it is important to distinguish between different types of domestic consumption-led growth, depending on the drivers of demand, which can be wage increases, financed by private debt or public spending on social benefits.

Instead of juxtaposing the demand-focused growth model perspective of Baccaro and Pontusson with the more supply-side VoC perspective of Hall and Soskice, we propose an augmented synthesis with our own approach that uses the notion of "growth regimes". Adopting a growth regimes perspective allows us to gather insights of both perspectives and provide a more detailed and differentiated account of diverse developments of capitalist economies, while also examining their evolution.

2.1 Growth regimes

*A **growth regime,** in its broadest sense, is **a mode of governance of the economy.** It encompasses the institutional, policy, and organizational frameworks that shape the specialization of firms and the consumption and saving patterns of the population, as well as the use of technology and work organization. A growth regime can be based on a particular*

type of innovation, the evolution of a particular high-value-added industry, the use of fiscal and monetary policy, and policy instruments that affect the employment rate and human capital. The (welfare) state is an important component of growth regimes for economic management.

Growth regimes, therefore, not only include all the components of the neoclassical model of growth, in particular labor, capital, and technology, and the specification of aggregate production functions, but, moreover, they give them a particular framework. While neoclassical growth theory has become more sophisticated in specifying particular aspects of the production function, such as consumer behavior, it is generally not interested in institutional and policy configurations, either between countries or across time, beyond a very general view on institutions such as property rights (Acemoglu and Johnson 2005). The inclusion of a variety of institutions, sectors, and policies (including social protection policies) distinguishes different types of growth regimes. In order to emphasize the interactions and complementarities between the various components of each institutional configuration, we use the notion of regime and "growth regime" rather than "growth model".[3]

We consider that there are three important aspects of growth regimes:

- **The engine of growth** – sectors that contribute to wealth creation, job creation, and productivity gains: i.e. agriculture, manufacturing, services (high/low value-added services), finance, housing, knowledge-based activities, and ICT.

- **The institutions organizing the economy**: 1. modes of financing the economy and corporate governance; 2. product market regulation (including industrial policies, subsidies, state ownership); 3. industrial relations, modes and rules of wage-setting, labor market rules and organizations; 4. skill-formation systems (education and vocational training); 5. social protection policies (social insurance, social investment and social assistance).[4]

- **The main components of aggregate demand**: private consumption (household and firms), private investment, public spending (consumption and investment), and net exports (Baccaro and Pontusson, 2016).

Our understanding of growth regimes is comprehensive and embraces both the demand side and the supply side of the economy (See Figure 1). It assumes that socio-economic institutions, as established in the comparative political economy literature, shape the key dynamics of growth. These institutions inform both the supply and demand sides. For instance, wage-bargaining institutions, on the one hand, support the skill-formation system, as centralized wage-bargaining provides wage limits for skilled labor. In tandem with different kinds of training institutions, welfare systems and wage-bargaining institutions prop up particular skill patterns and, thereby, form a skills regime (Chevalier 2020). At the same time, wage-bargaining institutions determine the wage structure in an economy, which, in turn, affects the demand side (Baccaro and Pontusson 2020; Johnston 2020). Higher wage increases, as well as lower levels of wage inequality, should prompt higher levels of domestic demand. Similarly, equity-based corporate finance and fluid capital markets facilitate financialization, which impacts the

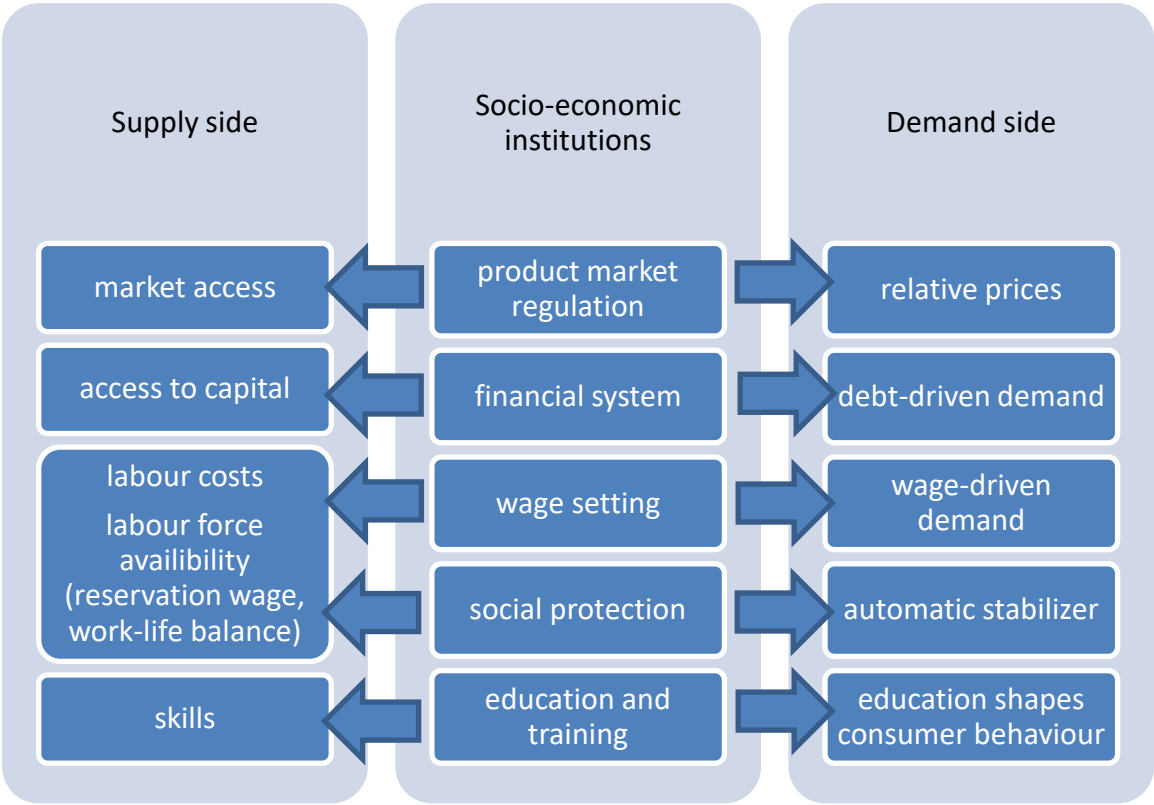
[3] We use the terminology of "growth model" when we refer to the literature that focuses on the demand side of the economy.

[4] We elaborate here on the five institutions already identified by Amable (2003).

demand side by creating credit (Reisenbichler 2020). On the other hand, the fluidity and availability of corporate finance also interact with opportunities for radical innovation on the supply side (Wren 2020).

In a specific growth regime, the interaction between the supply and the demand sides of the economy are influenced by the same economic institutions. These institutions also prompt economic actors to specialize in particular kinds of economic activities and political actors to attempt to support and reinforce these specializations with their economic policies.

Figure 1: The institutional foundations of growth regimes [5]



2.2 Growth and welfare regimes

The welfare state is at the core of growth regimes of national political economies because social policies affect both the demand and the supply side of the economy. For instance, the provision of unemployment benefits affects the activation of the unemployed and therefore labour supply and sustain domestic demand at the same time. Education policies shape the skill-set of a society and – if provided by the public sector – present a big pool of public sector jobs and thereby demand. It therefore matters substantially for the growth trajectory of a national political economy how the welfare state is constructed.

Social policies have often been perceived as a tool to compensate for the most negative impacts of capitalism, and are rarely analyzed in their connection to, and their positive interaction with,

[5] We would like to thank Georg Picot for helpful suggestions improving this graph.

the economy (Iversen and Soskice 2015). However, Iversen and Soskice (2015, 82) remind us that

> social protection (including job protection, unemployment benefits, income protection, and a host of related policies, such as active labor market programs and industry subsidies) encourages workers to acquire skills that are co-specific to employers, which in turn enhances the ability of firms to compete in international markets. Central features of the welfare state are thus linked to the economy in a manner that creates beneficial complementarities.

The welfare state occupies a prominent place in the VoC literature. CMEs and LMEs are not defined but underwritten by important functions of the welfare state. As noted earlier, CMEs are based on non-market mechanisms, such as long-term relationships between employer and employees. The skills in which workers and firms invest are insured by welfare state policies, such as unemployment insurance. In LMEs, by contrast, economic relations are governed by market mechanisms, by which wage levels are determined by individual productivity. LMEs tend to feature a universal, but minimalist, welfare state. Workers have access to social protection, such as health insurance, mainly through their job contract.

For each type of political economy, the functioning of and differences in the skill-formation systems and the way the labor market and the welfare systems are organized are crucial. Taken together, these sets of institutions (educational system, labor market rules, and social protection) are key elements of what the comparative welfare state literature would call "welfare regimes". Comparative research has shown that these three key elements often (but not always) systematically complement each other, and thus work as a system to form a "regime" (Esping-Andersen, 1990). For instance, centralized wage-setting institutions go hand-in-hand with more comprehensive social protection systems and often focus on mid-level (specific) skills, whereas decentralized wage-setting and a low-regulated labor market go hand-in-hand with educational systems that provide general skills (with little involvement from both the state and employers) and residual social policies.

Education, labor market regulation, social insurances, and other social policies thus contribute to both the supply and the demand sides of the economy (see Figure 1). In this sense, the welfare regime is an integral part of growth regimes. On the demand side, these elements provide certain levels of consumer spending (assistance benefits, unemployment benefits, old-age pensions, etc.), act as automatic stabilizers, and can also provide a minimum reservation wage. On the supply side, they can contribute to increasing productivity and increasing employment through specific employment policies and/or education policies. Welfare systems provide different types of skills that are employed in different production regimes (Estevez-Abe et al. 2001; Streeck 1991). Unemployment insurance and other social insurance, associated with specific employment statuses, protect skill acquisition. Avlijas et al. (2020) detail the various configurations to be currently found between growth regimes and welfare regimes in Europe.

The interplay between the supply and demand side of a national economy remains the key variable in the political toolbox of governments when attempting to stimulate economic growth. Governments can choose to spend to increase demand or to improve the supply side by enhancing skills or markets. When governments employ policy tools to adjust both sides, they encounter trade-offs, decisions regarding priorities, and calculations of political costs. In the end, governments choose a combination of supply and demand policies. Besides political and

electoral factors, the choice of instruments is also shaped by the institutional environment of the economy and, particularly, by the dominant economic sectors in a country.

2.3 Growth strategies

As the world is changing, we need to enrich comparative political economy theories to improve our understanding of how growth regimes are changing. We argue that growth regimes have indeed changed over time and that these changes are largely due to reforms implemented by governments and collective economic and social actors, such as employers' representatives and trade unions ("producer groups" in the political economy literature).

The series of decisions taken by governments are not random. They define a specific way to stimulate growth and job creation. They are taken in particular institutional and economic contexts and reflect specific political compromises. Taken together, they form a more or less coherent set of (economic and social) goals and (economic and social) policies that we call "growth strategies". *By growth strategy, we refer to a (relatively coherent) series of decisions and reforms, taken by either governments or producers' groups (economic and social actors) in order to boost growth and stimulate job creation in a specific nation, and the rationale for these decisions.* Governments develop either explicit or implicit growth strategies. The fact that we are using the notion of strategies does not mean that we believe that governments perfectly know what the consequences of their actions are (see below), but that they have some intention, that they pursue a general aim to boost employment and growth, and that there is at least some coherence in a series of economic and social policy decisions.

To give examples of what we mean by "growth strategies", one can refer to the most explicit ones, like those formulated by international organizations. In 1994, the famous World Bank (1994) report on "averting the old-age crisis" presented its new pension model and the reforms leading to it as a growth strategy.[6] One could also refer to the "Jobs Strategy" developed by the OECD (1994) during the 1990s: the aim was to promote (liberalizing) labor market reforms in order to boost job creation.

At the EU level, in 2000, the Lisbon Strategy was explicitly presented as a "growth strategy". It aimed to "make Europe's economy the most competitive and dynamic knowledge-based economy, capable of sustainable economic growth with more and better jobs and greater social cohesion" (EU European Council 2000). The details of this strategy include many different aspects from investment in research and development to the modernization of social protection systems. Adopted in 2010, the subsequent "Europe 2020 strategy" focused on "smart, sustainable and inclusive growth", including specific social policies and reforms. Within these strategies, a diagnosis of the structural changes in the economy (such as the evolution of the knowledge-based economy) and in societies (such as aging or the entry of women into the labor force) is put forward, and prescriptions on what governments should do to reorient their economies and favor growth and job creation are then presented. When pursuing the implementation of these strategies, governments are expected to reform some of the institutions that are constitutive of a growth regime and thus have the potential to transform the existing

[6] The full title of the report is: *Averting the old age crisis: policies to protect the old and promote growth* (World Bank, 1994), the argument being that switching from PAYGO pension systems to fully-funded schemes would both preserve future pensioners from the negative impact of demographic imbalances and create funds that would attract and increase investments in the economy.

one. All the strategies referred to above push for important reforms in the labor market, education, training, and social policies.

While international organizations explicitly use the terminology of "growth strategy", national governments are less explicit. Presenting and analyzing the national logic of action, the manner in which various economic agree to find a specific way to boost growth and jobs, and assessing coherence of the implemented policies and reforms is more a task undertaken by social scientists. We assume that, when looking at economic and social reforms implemented in a country, one can detect a strategy, i.e. "a pattern in the stream of decisions" to refer here to Henry Mintzberg's approach to strategy (Mintzberg 1979, 582). As suggested by Fritz Scharpf to us, some countries may have differentiated strategic capacities. Sweden and France may have been able to proactively design growth strategies (at least in the post-war era), while others have developed their growth strategies through an evolutionary process of mutual coordination and adaptation. Our notion of growth strategy assumes less of an ex ante strategic planning capacity and more of a progressive (and post hoc) discovery of what Mintzberg calls an emergent strategy.[7]

The policy fields and reforms differ from one country to another (in content and in timing). These differences reveal a certain level of internal consistency and coherence within individual countries that might be reconstituted as strategy. The internal consistency partly derives from the diagnosis of the problem to be solved and partly in the proposed solutions. Most of the coherence in the policies adopted to solve the identified problem comes, however, from the specific national growth and welfare regimes, since they structure the decisions taken and the strategies adopted in a specific country. These solutions to revive growth and stimulate job creation are shaped by the existing growth and welfare regimes. When adjusting to new contexts, these reforms can, however, contribute to progressively reshaping and transforming existing growth regimes.

Even in contexts where "strategies" are not explicit, governments have developed standardized responses to economic threats that correspond to their own economic specialization and regime. The reactions by governments to the economic recession following the financial crisis illustrate this point. For instance, the German government responded to the financial crisis by immediately protecting the economy's manufacturing base through short-shift working arrangements and a "cash-for-clunkers" program. In the UK, all attempts to rein in financial services industries (especially at the EU level) have been scrutinized as to whether and to what extent they might endanger the competitive advantage of the City of London. These governmental responses to the financial crisis reveal an underlying economic growth strategy.

These examples of (more or less) short-term government strategies to protect the economic base of national political economies are embedded in broader institutional settings that define the production and welfare regime of a country. As is illustrated by Baccaro and Pontusson (2020) and Picot (2020), there are many government decisions that follow the same pattern of

[7] As Mintzberg reminds us, the ancient Greeks used the notion of strategy to describe the art of the army general, and strategy is often associated with strategic planning. Through his empirical observation of firms' strategy-making, Mintzberg, however, proposes an approach to strategy that inspired our own approach, meaning not a plan for action, but a pattern in action in a series of decisions. As Mintzberg states: "Ask almost anyone what strategy is, and they will define it as a plan of some sort, an explicit guide to future behavior. Then ask them what strategy a competitor or a government or even they themselves have actually pursued. Chances are they will describe consistency in past behavior—a pattern in action over time. Not 'planning', nor 'expression of intention', but 'patterns in action'" (Mintzberg, 1987, p.67–68).

protecting/ enhancing/ renewing the existing growth regime. These decisions and policy reforms are influenced by the dominant production regime and profile – i.e. manufacturing or finance, export-oriented or domestic demand, etc. – and have implications for the reforms of the welfare state. In other words, a country dominated by financial services has a different approach to welfare reform than a country dominated by manufacturing.

Obviously, the production regime is not the only factor at play. Electoral rules, political institutions, political parties, and other external events matter as well (Beramendi et al. 2015; Hall 2020). Policy-makers can adopt growth strategies that are not necessarily in line with the growth regime for reasons such as party ideology or values or with the aim of developing a new growth regime. There is also reverse causality: political institutions have shaped production regimes, as Iversen and Soskice have argued (2009). However, we assume that growth and welfare regimes play an important role in these strategies. This is partly because the preference of the dominant sector informs policy-makers as to what the priorities of economic and social policies should be (see also Iversen and Soskice 2013; Baccaro and Pontusson 2020).

Business groups in the dominant sector(s) have privileged access to governments and to media reporting about the economic situation. The interests of the business community might be in conflict with government priorities, and we do not assume that business will always have the upper hand. But we do expect government policy-making to take into account the demands of the dominant business community and their strategies to cope with economic and welfare state restructuring. Depending on the kind of dominant business community, we presume a variety of business preferences for welfare state reforms. These preferences are analyzed in details by Martin (2020). In many cases, these preferences may be supported by workers in key industries. As workers and their representatives are aware of the relevance of the industry and are usually the beneficiaries of the economic specialization process, they might support the business community in their political demands for government policies. Cross-class coalitions are, therefore, sector- or country-specific and, by and large, focused on or coming from the economy's dominant sector (for the importance of producers' coalitions in shaping growth strategies, see Thelen 2020).

Growth strategies often involve significant welfare reforms. International organizations regularly suggest reforms of the welfare state to reach economic and employment objectives. The EU, OECD, and World Bank emphasize the necessity of reforming education and skill-formation systems, advocating structural reforms of labor markets, wage-bargaining, and social protection systems in the name of boosting growth and creating more jobs. The EU's 2000 competitiveness strategy associates economic policy orientations (austerity, growth through cost-competitiveness and export capacities) with welfare reforms (cuts in welfare spending, as well as the "structural reforms" of labor markets, pensions, and healthcare systems) (Heins and De la Porte 2015).

At the national level, welfare states have been, and continue to be, reformed in the name of job creation and growth. Since the 1990s, especially in Europe, many of the policy reforms implemented by governments concerned mostly the welfare system in a broad sense: changes in wage policies, in labor market regulation, in employment policies, in educational and training policies, and in social policies. The neoliberal governments of Thatcher and Major in the UK were famous for their privatization policies (which partly included pension schemes), but also for having liberalized the labor market and increased pressure and conditionality on unemployed persons. Nordic countries implemented labor market and pension reforms in the early 1990s. Gerhard Schröder gained his reputation through his labor market and

unemployment insurance reforms in Germany in the early 2000s. Emmanuel Macron is accumulating reforms in France's welfare domain (labor market deregulation, training, unemployment benefits, and pensions).

One possible reason that these labor market, skill formation, and social policy domains are so prominent in governments' agenda when they want to boost growth and create jobs is that these fields are still under the jurisdiction of national governments. By contrast, the management of other economic policy fields that constitute the specific growth regime, such as product market regulation, financial rules, and monetary policy, are being increasingly overtaken by supranational bodies because of liberalization, globalization, and/or the independence of central banks. This situation holds particularly in the EU and the Eurozone area (see Scharpf 2020; Johnston 2020).

The policy response to the financial crisis and the subsequent Eurozone crisis has triggered fierce debates among economists on both sides of the Atlantic about policy measures to combat stagnation and weak growth. US macroeconomists insist on demand deficiency as a major part of the problem and suggest stronger economic stimuli as the answer. Policy-makers in Europe, however, have largely opted for austerity policies, hoping for supply-side economic restructuring. Underlying this debate is, however, the question of what is seen as the engine of growth and job creation in national economies. In the following, we distinguish between five types of growth regimes in the contemporary advanced economies.

3. Five growth regimes in Europe

3.1 Export and demand-driven growth in the 21st century

As discussed in the current comparative political economy debate, and by Baccaro and Pontusson (2020), Picot (2020), and Scharpf (2020), there can be two main types of drivers of economic growth: foreign demand (exports) or domestic demand (household and government consumption). In Table 1 we divide the countries into exporters and consumers, based on 2016 data.

Table 1: Export share in GDP of OECD countries (2016)

Consumers	% of exports in GDP	Exporters	% of exports in GDP
Australia	21.2	Austria	52.5
Canada	31.5	Belgium	79.4
Finland	34.8	Czech Republic	79.6
France	30.2	Denmark	53.4
Greece	30.1	Estonia	77.5
Italy	29.6	Germany	46.0
Japan	16.3	Hungary	87.2
New Zealand	26.4	Ireland	120.8
Spain	33.1	Korea	40.1
United Kingdom	28.4	Luxembourg	213
United States	11.9	Netherlands	79.5
		Poland	52.2

		Portugal	40.2
		Slovak Republic	93.7
		Slovenia	78.0
		Sweden	43.3
		Switzerland	65.7

Source: OECD. Note: Exporters are open economies with an export share of around and above 40% of GDP. Consumers are more closed economies. Latest available data. https://data.oecd.org/trade/trade-in-goods-and-services.htm#indicator-chart accessed January 29, 2020.

During the Fordist era, economies benefitted from advances in productivity and more technological upgrading on the supply side that allowed for a wage increase, but there were already differences between countries favoring more domestic demand or more exports.[8] Deficit-spending to boost consumption is a kick-start for ailing economies and, since the early 1970s, most countries have compensated for lower growth rates through higher public spending (Streeck 2014; Picot 2020). Today, the source for domestic demand has diversified even more. Demand stimulus to the domestic economy stems from raising household incomes either through wages, social benefits, public deficits, or the capacity to access credit (Picot 2020). As financial services are a key component of consumption, new financial products stimulate domestic demand.

Nevertheless, countries can (also or alternatively) privilege the export of goods in order to maintain high-value-added employment by producing for world markets. Exports can thus temporarily protect the manufacturing industry from deindustrialization (Dauth et al. 2017). But countries can also specialize in high-value-added, high-skill services to boost exports, as is demonstrated by Wren (2020). Export-led growth regimes specialize in export commodities that may require different types of skills and social protection. In all these cases, value-added in exposed sectors is higher than it would be if the country focused on domestic markets. Thus, manufacturing and other exposed sectors are privileged over other protected sectors.

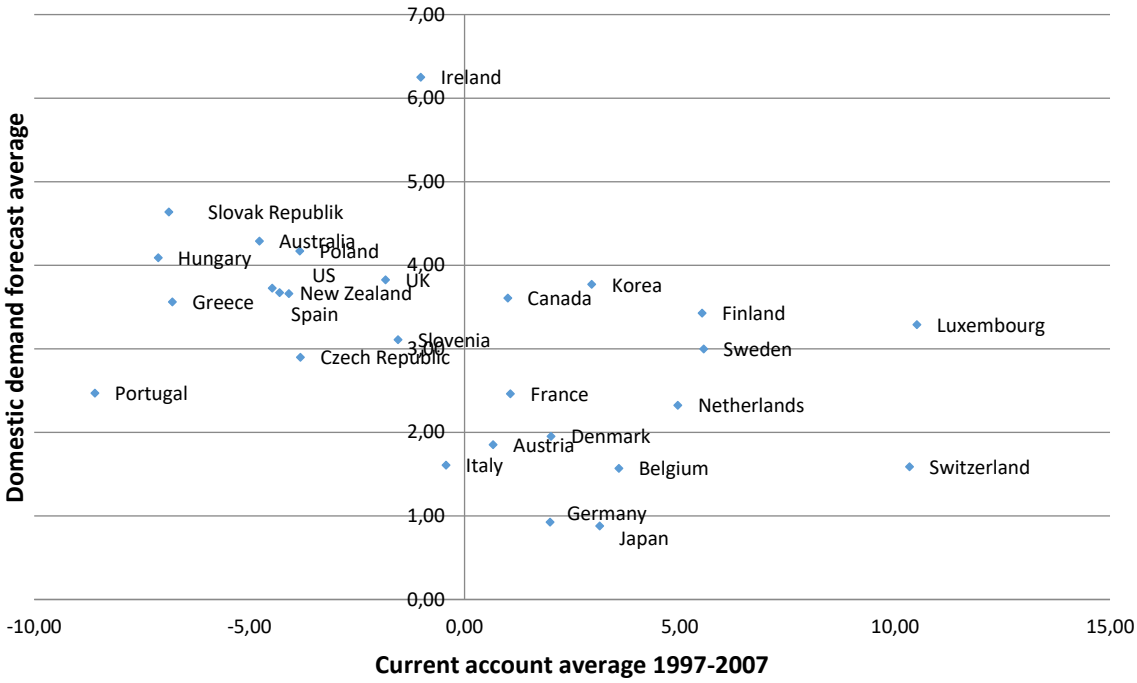
As discussed by Baccaro and Pontusson (2020), it is not clear to what extent both strategies can co-exist. Theoretically, domestic consumption-led growth regimes do not undermine export-led growth as long as higher labor costs do not endanger competitiveness.[9] Empirically, there seems to be a trade-off between export-led and domestic consumption-led growth (see Figure 2 and Picot 2020). Figure 2 indicates that the higher a country's current account surplus is, the lower the increase in domestic demand. This was at least the case during the period before the financial crisis.[10] Furthermore, as analyzed by Scharpf (2020), the export-led growth model is currently imposed on all countries of the Eurozone, including those who had a domestic demand-led growth regime (see also Hall 2018; Hassel 2017; Iversen and Soskice 2018).

[8] Germany was already focused on wage moderation and supporting its exporting industry in the 1950s (Höpner 2019), and the Nordic countries, as many other small countries, relied on exports to boost growth and wages (Katzenstein 1985).

[9] Baccaro and Pontusson (2016) argue that the Fordist growth regime is, in principle, domestic demand-led (wage-led in their terminology). Only extreme versions of export-led growth, which are dependent on price-sensitive manufacturing exports, might turn against demand in order to control labor costs and the real exchange rate.

[10] After 2008 and the start of the financial crisis the correlation between change in domestic demand and current account turns positive (until 2016), as domestic demand countries experience austerity and export-driven economies temporarily stimulate domestic demand (Baccaro and Pontusson 2020).

Figure 2: Current account balance, 1997-2007 and change in domestic demand, 1997–2007 in %



Source: OECD Statistics, Key Short-term Economic Indicators; Domestic demand forecast.

3.2 Five types of Growth Regimes

If one distinguishes between those economies that rely on exports as a source of growth and those that do not, we see a clear pattern. All English-speaking LMEs (in VoC terminology), except Ireland, and most Southern European economies (including France) are largely domestic demand-led economies, whereas both Nordic and Continental, as well as Eastern European economies are nearly all export-focused. Here, we are able to broaden the scope of Baccaro and Pontusson's growth models approach beyond the four countries that have been the focus of their work.

If we look closely at the different components of growth regimes as we defined them earlier (i.e. the various engines of growth, institutions organizing the economy and the main component of aggregate demand), we can distinguish five different configurations — three types of export-led growth regimes and two types of domestic demand-led ones.

Among the export-focused countries, we identify three subgroups:

- Countries which combine an export focus with strong domestic demand, such as all Nordic economies but one (Denmark is an exception as far as demand is concerned), Luxembourg, and the Netherlands (this is what Baccaro and Pontusson call "balanced growth models"). They are progressively shifting from the manufacturing industry to dynamic services as the key driver of growth, benefitting from financialization to feed the growth of ICT-based service sectors. They have also developed low-pay private services.

- Countries where export of manufacturing goods is the main driver of growth, with low growth in domestic demand (below 2%) before the financial crisis, such as Germany, but also Austria, Belgium, and Switzerland. These countries rely heavily on the competitive position of companies in high-quality manufacturing and often use the most refined mechanisms of diversified quality production (Streeck 1991) to protect this position. They primarily benefit from high growth rates in emerging economies that satisfy their demand for machinery and high-end consumer goods.
- Countries with increasing shares of exports, but negative current accounts and relatively high rates of domestic demand, such as those in Central and Eastern Europe. Like the previous subgroup, these countries follow a manufacturing, export-oriented strategy (Bohle and Greskovits 2012, Picot 2020). They are heavily integrated into German-based production networks and depend even more on low prices (hence low wages and low welfare). They (together with Ireland) are also highly dependent on foreign direct investment (FDI) (Bohle and Greskovits 2012, Bohle and Regan 2019).

We can also identify two sub-groups among the countries relying foremost on domestic consumption and demand-led growth:

- Countries with a high level of domestic consumption, a high degree of financialization, and also high development of ICT (all the English-speaking LMEs of the VoC framework but one: Ireland). As restructuring is more rapid, and fluctuations more pronounced, these economies saw deindustrialization earlier, and more deeply, than the CMEs of Northern Europe. For example, the decline of British manufacturing took place already in the 1960s, when British companies could no longer deliver high-quality products at a reasonable price due to higher levels of industrial conflict, lower investment in training and quality, and difficulties in implementing wage moderation. Colin Crouch (2009) has convincingly shown how easy access to credit and a vibrant housing market have been key to consumption-based growth in the UK and the US since the 1980s.
- Countries with a high level of domestic consumption but relatively low level of financialization and ICT development (mostly the countries of Southern Europe, including France). This is due to relatively easy access to cheap credit (especially after introduction of the Euro) and generous "consumption-oriented" social insurance (Beramendi et al. 2015). In Southern Europe, labor market institutions appear to be centralized, and corporate finance is closer to the model typical of the CMEs. However, these regulations and institutions do not deliver the same collective goods as in typical CMEs (Molina and Rhodes 2007; Hassel 2014). Because their coordination depends on the intervention of the (welfare) state, governments have pursued a more active, consumption-led growth policy and let wages and social spending rise (see also Höpner and Lutter 2014). Therefore, this type of countries generally has a lower export orientation.

As explained above, the domestic-demand regimes can easily connect with financialization, which has an expanding effect on the economy through higher consumption due to wealth effects (Boyer 2000). Wealth effects are primarily created by house price inflation. But, financialization itself, through its capacity to finance start-ups and new economic activities, can also facilitate the development of new, high-end sectors, based on ICT, that can lead to national consumption as well as to exports (Uber or Amazon rely on the national consumption of services, but are global companies) (see Wren 2020). Domestic demand can thus be fueled by financialization, which, in turn, is driven by the housing market, pension privatization, and low

savings rates. The current account deficit also drives financialization, as it attracts foreign financial assets, which in turn expand financial services in countries with trade deficits.

By contrast, as indicated partly in Figure 2, a high share of exports and a current account surplus are often correlated with comparatively lower rates of increase in domestic demand. As a result, we generally see a complementary relationship between countries' trade deficits and surpluses (Iversen and Soskice 2013). Still, financialization has also occurred in some countries with an export-based growth regime. In particular, the Nordic countries and the Netherlands have combined domestic demand policies via financialization with an export strategy (see Baccaro and Pontusson 2020; Thelen 2020). However, another possibility for stimulating domestic demand is to rely on private and public debt that supports wage increases and/or consumption-oriented social benefits, as is typical in Southern Europe.

As far as ICT is concerned, all advanced countries are affected by the ICT revolution and embrace investment in ICT. Nevertheless, investment in ICT is higher in countries with higher levels of financialization. This potentially puts the Continental European countries apart from the Nordic countries (including the Netherlands), which have higher rates of domestic demand, financialization, and ICT investment compared to the German-speaking CMEs (see Wren 2020).

Southern European countries have embraced financialization to some extent, as home ownership rates are high and house prices have become inflated. It is, however, less related to ICT innovation, but is a primarily domestic, consumption-driven regime.[11]

In Table 2, we summarize the main traits of the five identified growth regimes, including those we have highlighted in this section (i.e. the demand driver of growth, the current account situation, the degree of financialization and the development of the knowledge economy) as well as those related to the labor market, education, and welfare systems. The table is heuristic in nature with empirical observations clustering to ideal types rather than defined characterizations. The different growth regimes show a number of characteristics that are particularly relevant for understanding the specific growth strategies developed by different countries.

[11] Data on Eastern Europe regarding financialization and ICT are very limited. They have low levels of financialization but high levels of home ownership, which might trigger faster financialization in the future.

Table 2: Characteristics of the five growth regimes

	Dynamic services export-led growth regime	High-quality manufacturing export-led growth regime	FDI-financed export-led growth regime	Finance-based domestic demand-led growth regimes	Publicly financed domestic demand-led growth regime
Demand drivers of growth	Export	Export	Export	Domestic consumption	Domestic consumption
Current account	Surplus	Surplus	Mixed	Deficit	Deficit
Financialization	High	Low	Low	High	Low
Knowledge economy (ICT)	High	Medium	Low	High	Low
Education system	Inclusive high-level	Inclusive mid-level	Inclusive mid-level	Elitist	Elitist
Social protection	Social investment	Social insurance	Social insurance	Private insurance and investment	Social insurance
Wage-setting	Coordinated	Coordinated	Deregulated	Deregulated	Regulated

Source: Table 2 is based on empirical observations, Hassel and Palier 2020 Figure 1.2 and Table 1.1, Chevalier (2020) on education; Palier and Hay (2017) on social protection, and Visser (2019) ICTWSS database on wage-setting.

4. Growth Strategies and Welfare Reforms

Depending mostly on the specific institutional context defined by the specific growth regimes they are embedded in, governments have chosen different types of growth strategies to boost growth and job creations over the last decades. As mentioned earlier, these growth strategies push for different types of welfare state reforms. We analyze the various types of growth strategies and welfare state reforms in this section.

Policy decisions are embedded in given economic structures and tend to buttress existing patterns of economic or sectoral specialization. However, they can also contribute to the transformation of growth regimes. For instance, financialization that sustains domestic demand can also contribute to the development of information and communications technology (ICT)-based sectors (Hassel and Palier 2020), which in turn require an investment in higher skills (Wren 2020). Thelen (2020) shows how labor market reforms, as well as vocational training reforms, have accompanied bifurcation of the Dutch growth regime and diversification of the Swedish one.

In this section, we present in a stylized way the main mechanisms through which the different components of welfare system reforms interact with one another and with growth strategies. We associate each of the five growth strategies with a typical set of changes in welfare policy that, combined, can be characterized as a more or less distinct type of welfare system reform. We focus here on the main welfare policy arenas: the labor market, wages, pensions, housing,

education (social investment), and social benefits (social spending). In practice, the different types of welfare system reforms do not have to be mutually exclusive, but some policies are incompatible. As we show, for example, increasing wages and maintaining high social benefits might conflict with a policy that focuses on wage moderation in order to foster the export of manufacturing goods.

4.1 Manufacturing export-based growth strategy and the dualization of welfare

This growth strategy focuses on protecting traditional manufacturing industries in a context of globalization and deindustrialization, which requires maintaining the quality and productivity of the sector, while keeping prices low. The emphasis is on controlling labor costs via wage moderation (Johnston 2020). As long as external demand compensates for the lack of domestic demand, wage moderation does not undermine growth.

Wage moderation and the preservation of quality in manufacturing labor is achieved through the protection of labor market insiders, close cooperation with manufacturing trade unions regarding investment and technology, and enhancement of skills through liaison with entities providing further or continuing education. Core workers in the manufacturing sector are promised employment protection in exchange for wage restraint and willingness to change jobs within the firm. As plant-level labor representatives prefer long-term investments and job security over short-term wage gains, local plant-level deals accumulate to shape sectoral policies of trade union wage restraint.

Since export capacity is key to this strategy, the real exchange rate is a central concern. Policies that might negatively affect the real exchange rate, such as accommodating fiscal or monetary policies and wage increases, are repressed institutionally and politically. These policy responses have repercussions not only for fiscal spending for education and childcare but also for labor market policies.

As demand stimulation is not an option, supply-side measures to reduce the reservation wage are introduced. The strategy also depends on the emergence of a cheap and flexible service sector, which makes domestic services affordable. Thus, dualization and supply-side labor market policies feed directly into the pattern of economic specialization (Palier and Thelen 2010; Hassel 2014). Companies use industrial restructuring to weed out less-productive service segments of the production processes from highly productive manufacturing ones. They thereby introduce an internal segmentation of their workforce and adopt changes in labor market rules that allow for a dualization of labor markets. The social partners, i.e. employers' and employees' representatives, tolerate the emergence of atypical employment and a low-pay segment in other sectors, including in services, in order to save the manufacturing industry (Palier and Thelen 2010).

Other welfare reforms aimed at securing cost competitiveness are complementary to the manufacturing export-based growth strategy. Pension and health reforms aim to limit the increase in social contributions to constrain non-wage labor costs. With regard to housing policy, Reisenbichler (2020) shows that conservative housing finance policies are designed to restrain demand and dynamic housing markets in order to keep down the cost of living, wages, and inflation. Dynamic housing markets are not central in such a growth strategy also because wage moderation further depresses the demand for mortgages and because central banks in these economies are mostly preoccupied with low inflation, price stability, and market discipline.

4.2 Exports of dynamic services growth strategy and social investment

In the dynamic services-driven growth strategy, governments aim to boost the quality and innovation capacity of the business community in order to remain competitive in the knowledge economy. They invest in education and the (re-)training of the workforce, as well as human capital more generally. A certain degree of labor force flexibility is required to adapt the economy to innovation and change, as well as to external competitive pressures. At the same time, workers need to be able to switch sectors, while preserving or renewing their skills. Since skill and social protection cannot be provided through employment security (which would lead to an economy that is too rigid and unable to innovate), protection and the formation and renewal of skills are provided to all by the (welfare) state. This allows workers to concurrently invest in their human capital through publicly financed training and education schemes, while staying flexible in the labor market. Unemployment insurance also leads to a greater acceptance of risk, which enhances the workforce's capacity to cope with innovation (Boyer 2000, 6).

Therefore, social investment and social expenditure go hand in hand in this strategy, and they serve to boost labor productivity. Both factors, along with growing innovation, lead to wage expansion. Higher wages affect consumer behavior and stimulate domestic demand, which subsequently expands. Hence, this strategy allows for the combination of export-led and domestic demand-led growth.

This growth strategy requires that firms have access to venture capital which facilitates financialization. The welfare system can serve as a base for providing an expansion of finance, through either pension funds or the development of private, social, and educational services. While a highly developed welfare state lowers the demand for market-based tools for risk diversification through private insurance, privatization of social services might be pursued as part of the expansion of dynamic services.

Expanding financial markets helps to facilitate innovation in the knowledge-based economy. While there are similarities between the dynamic services-based growth strategy and the financialization-based one described in section 4.4 below, there is a key difference with regard to the role of the state. In the dynamic services-based growth strategy, the state foots the bill for public services, even through private providers, while financialization is pursued as a complementary strategy. Furthermore, despite the growing privatization and marketization of pensions, the state provides universal minimum pensions that reduce the individual market-based risk that citizens face vis-à-vis their retirement income, while social partners (not private companies) own the pension funds (Anderson 2019).

The aim of housing policy in this strategy is to provide universal access to housing for workers. It is therefore a form of social investment, along with education and childcare, since its main policy aim is to improve workers' quality of life and thus boost their productivity. While private providers are included in service provision, the government regulates the market for all citizens and allows them access to social housing, rather than limiting its intervention only to those below a certain income threshold. In that sense, the role of the state in the housing market is strong, even when financial markets participate widely. As Reichenbichler (2020) underlines, a dynamic market for housing finance is not an impediment to the dynamic services-based growth strategy. Wage growth and the expansion of domestic demand and credit underwrite a dynamic housing market. This is in contrast to the manufacturing export-based strategy, which is concerned with cost competitiveness of exports and therefore restraining wage growth.

4.3 FDI-financed export-led growth strategy and fiscal and social attractiveness

There is a third family of export-led growth regimes in which exports represent a significant share of GDP (see Table 1), but the countries tend to run negative current accounts and maintain relatively high levels of domestic demand (Figure 2). These countries have in common that FDI is important for their economies, which makes them "FDI-led growth regimes" (Nölke and Vliegenthart 2009; Bohle and Greskovits 2012; Bohle and Regan 2019). They also share some basic fiscal and social policies aimed at attracting FDI. Their growth strategy seeks to make the most of their position in the global economy and find a niche in the global supply chains of multinational firms.

To implement this growth strategy, governments use fiscal and tax tools to attract FDI. Fiscal exemptions and cash subsidies complement low corporate taxation in order to target the foreign investment to a particular sector of specialization. Some countries aim to attract multinational manufacturing firms (such as German or French automobile companies in Hungary) while others may want to attract American high-tech companies, for instance in Ireland (Bohle and Regan 2019).

Low labor costs are obtained through comparatively low levels of public social spending and non-wage labor costs. Policies thus focus on the liberalization of labor markets and social protection, welfare state retrenchment, and privatization in order to increase social attractiveness for foreign investors. When implemented, this growth strategy usually entails a deep transformation of the economy towards the sectors which attract FDI and may produce losers (domestic firm owners, workers from other non-favored sectors, or low-productivity workers in FDI sectors). In these cases, some social compensation mechanisms are introduced.

Depending on which sectors attract high FDI, education and social policies may also be used to positively reinforce the strategy in favor of either (medium-skilled) manufacturing specialization, or (more or less dynamic) services (as in the Baltic countries, see Avlijas forthcoming in 2021). If a government wants to develop its comparative advantage in manufacturing, the maintenance of social insurance and a medium-skill educational system is necessary, and thus a compensatory welfare system (which also allows compensation for the losers of restructuring, for instance through early retirement) is favored over broader social investment. In contrast, if the government wants to provide foreign investors with a general-skilled workforce in order to develop ever more dynamic services, educational and social investment is more advantageous than compensatory social insurance.

4.4 Financialization-based growth strategy and the commodification of welfare

The financialization strategy uses privatization and marketization of education and welfare (especially pensions and housing) to drive the overall financialization of the economy. This growth strategy relies on limiting public welfare and the rise of private social protection and education. Private welfare policies and access to mortgages encourage individuals to take responsibility for their own welfare through financial means. In the case of pensions, for example, while privatization shifts the responsibility for provision to private actors, financial services, and employers, marketization introduces market mechanisms into both public and private pension plans. Both reallocate retirement risks onto individuals and financialize their daily lives (Ebbinghaus 2015, 61; Hassel et al. 2019).

In terms of housing, homeownership becomes the piggy-bank of the middle classes as a form of additional retirement income (or savings).

In addition, financial centers provide well-paid jobs for some and attract investors. The growth of real incomes, in combination with a greater supply of financial instruments and a greater demand for housing, spurs both credit- and income-driven consumption and thus stimulates domestic demand. Rising house prices in a growing economy boost the wealth effect of financialization as they contribute to the wealth of homeowners.

Greater financialization also drives technological innovation in dynamic services and greater demand for human capital investment. Innovation, particularly through ICT, is fostered by high levels of venture capital and general skills, but these are subordinated to the financial sector. The financial sector is important not only in terms of employment and added value, but also as a means for facilitating and shaping the real economy. Finance-driven economies offer particular services to international investors, particularly investment and mutual funds. The effects spill over onto the high street as well: the housing market keeps driving the wealth effect of financial growth, and house price inflation is not controlled (Reisenbichler 2020).

Low wages in low-skill service sectors, a result of weakening trade union power and labor market liberalization, serve to stimulate domestic demand for personal and consumer services (Wren 2020; Morel 2015). The significant wage discrepancy between high- and low-skill service jobs also boosts the demand for (higher) education. The financialization strategy relies on the growing demand for education as an opportunity to reduce state funding for and enhance, via educational loans, market access to education. This further fuels the financialization-driven growth model and increases competition, especially in the higher education sector.

Because of comparatively high rates of growth and a dynamic labor market, people are not exposed to long spells of unemployment, hence there is less demand for social protection. The fact that only a minimal safety net against poverty is in place favors the existence of a low-wage labor market, which boosts the productivity of highly skilled workers, as they can outsource many of their non-work-related responsibilities to cheap service workers (Morel 2015). At the same time, given that domestic demand is the key driver of financialization, the state protects low-skill incomes to a certain extent, for example, via income tax credits on earnings or a minimum wage, so that they do not end up having a negative effect on growth.

Therefore, the “beast” of financialization is fed through state retrenchment, privatization, and marketization of pensions, housing, and education, expansive wages, and the repression of social spending. These interactions create a cycle of economic growth and job creation, on the one hand, and a higher systemic risk from financial crises and growing wealth and income inequality, on the other.

4.5 Publicly financed domestic demand-based growth strategy

The basis of this growth strategy is government support for households and companies in order to maintain domestic demand. The nature of this strategy is thus embedded in state spending, although it can be complemented by the financialization-driven strategy, which further boosts domestic demand, or by manufacturing exports.

In the ideal type of domestic demand-driven growth strategy, a generous national minimum wage and generous compensation through social benefits (especially pensions) feed household

consumption, while companies are supported via state involvement, devaluation, and some protection against foreign trade and investment that reduces competitive pressure on firms (Molina and Rhodes 2007). Traditional firms benefit, as they are met with relatively low levels of product-market competition because of protectionist policies, which allow them to offer high employment protection to workers and face little pressure to boost competitiveness. In order to compensate for the lack of price competitiveness in international markets, the state ensures currency devaluation. Firms are also not constrained by short-term profits, because the financial system is centralized and bank-based rather than driven by financial investors, which further accommodates high employment protection. The state is, in turn, left with few resources to invest in innovation, but is also discouraged from investing, as its key focus is to preserve privileges for the traditionally dominant sector.

A low degree of financialization is reflected in the low penetration of private financial markets into pension and housing provision and in the reduced support for investment in innovation and the knowledge economy, which would be facilitated through a market for new financial products and services (Hassel and Palier 2020). The absence of strong competitive pressure from global trade also discourages innovation, both at firm and state level, which exacerbates the vicious circle of pro-protectionist and anti-innovation policies (Capussela 2018).

The high level of employment protection, along with state protection of companies and their benefits, discourages workers from investing in their skills. This leads to low public demand for education, low enrollment rates in tertiary education, a weak and underfunded higher education system, weak vocational training, and no lifelong learning. A workforce with limited skills and education levels further limits the implementation of a high-skill and innovation-oriented industrial strategy. At the same time, an economy that is not based on knowledge and innovation does not demand these skills, which further undermines investment in human capital.

The decline of competitiveness leads to the shedding of labor in manufacturing and a further expansion of small firms in the service economy. Structural trends toward deindustrialization drive the dualization of the labor market. These structural pressures are reflected in the growing portion of labor market outsiders, i.e. flexible temporary and part-time contracts, which mostly affect new entrants into the labor market (younger workers). The growing precariousness of the labor force generates additional demand for non-employment-related social protection expenditures, while the public purse is being progressively depleted, as the country cannot find a sustainable engine for growth.

Beyond these interactions, the domestic demand-driven growth strategy is entrenched and reinforced politically. State spending is electorally constrained and geared towards protecting the vested interests of pensioners and the wealthy, as well as labor market insiders who benefit from social protection. These groups are favored over youth, who are consequently unable to access well-protected jobs and face a faltering economy that does not demand high skills. In this context, we see a political reinforcement of the economic division between pensioners and the wealthy, on the one hand, and youth and the poor, on the other.

Being caught in this vicious circle of low growth and high state expenditure, the domestic demand-based growth strategy is least adapted to the new global drivers of growth (financialization and digitalization). For members of the Eurozone, export competitiveness is further undermined by the country's inability to devalue its exchange rate. Because of the Eurozone context, this growth strategy is also especially susceptible and non-resilient to

systemic shocks such as financial crises, as well as to external pressures to maintain the stability of the EMU.

These pressures have led to an externally imposed, austerity-based agenda of "competitive impoverishment". While the extent of the competitive impoverishment strategy has varied across countries, it is premised on the idea that the welfare state represents an impediment to growth and that internal devaluation of labor costs via deregulation of employment protection, reduction of minimum wages, and institutional weakening of unions and collective bargaining are necessary (Scharpf 2020).

5. Conclusion

This article has identified five main growth regimes in contemporary advanced economies. Different growth regimes are connected with different types of growth strategies and welfare state reforms. Analyzing the linkages between welfare states and growth strategies helps us to understand why welfare state reforms have been undertaken and their timing and content. While we do not pretend to provide a full explanation of welfare state reform trajectories, our account expands on the existing welfare state literature by answering why welfare state reform takes place even when it is politically costly.

With this approach we have taken a step towards understanding why these trajectories of change have varied across countries and which mechanisms and drivers have shaped them. To address these questions, some authors emphasize the electoral process, including the changing composition of the electorate and their policy preferences (Beramendi et al 2015), while others focus on producer coalitions or social blocs and institutional legacies (Baccaro and Pontusson 2019). Some authors argue that there is a kind of division of labor here: electoral politics are dealing with very salient issues ("loud politics"), e.g. redistributive issues resulting from welfare state reforms, while business and producer groups deal with much less salient issues ("quiet politics"), such as economic policies (Culpepper 2010). By underlining the strong connections between welfare reforms and growth policies, we argue that one cannot just separate these two worlds of politics. There is a need to better understand how they interact. Like Hall (2020), we argue that both processes work in tandem.

To the current debate, we add the importance of governments' actions and their growth strategies. Policy-making by governments does not take place in a black box, automatically following demands of the electorate (through parties) or those of dominant social blocs. In reality, governments are sandwiched between the demands of voters, on the one hand, and preferences of producer groups, on the other. These demands exert pressures, which can even go in opposite directions, but also give governments a pivotal role in shaping the evolution of capitalist economies.

The approach of this article is grounded in the broad literature of comparative political economy as it has evolved over the last 30 years starting with Esping-Andersen's Three Worlds of Welfare Capitalism (1990). It aims to present a perspective on how to integrate a completely new kind of economy, the knowledge economy, into these theories. It takes financialization and digitalization as a process of reorganisation of economies that need to take government policies seriously. In this sense, we think that we are only at the beginning of understanding new paradigms of the knowledge economy.

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