Abbreviations

A	Austria
AUS	Australia
B	Belgium
CDN	Canada
CH	Switzerland
D	Germany
DK	Denmark
E	Spain
F	France
GR	Greece
I	Italy
IRL	Ireland
FIN	Finland
JAP	Japan
LUX	Luxembourg
N	Norway
NL	The Netherlands
NZ	New Zealand
P	Portugal
S	Sweden
UK	United Kingdom
USA	United States

1 Introduction

Studying varieties of welfare capitalism

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Despite claims to convergence, modern capitalism still comes in a limited variety. While the neo-liberal doctrine gained in currency in the 1980s and led to deregulatory reforms advanced by the United States and the United Kingdom, many economic observers were struck by the resilience of 'Rhenish' (coordinated) capitalism in Continental Europe and Japan (Albert 1993). The same holds true for the area of social policy: Welfare retrenchment has been propagated with some success in Anglo-American liberal welfare states, yet the more generous and expensive social security systems of Continental and Northern Europe have proven to be more entrenched (Pierson 1996). Although there are pressures towards convergence due to economic internationalisation and socioeconomic changes, cross-national diversity both in economic and social policy still dominates the political landscape (Berger and Dore 1996; Crouch and Streeck 1997; Kitschelt *et al.* 1999).

Over the last decade, two strands of research have underlined the importance of institutional variations for economic activities and social policy. In comparative political economy, the *Varieties of Capitalism* approach (Hall and Soskice, forthcoming) claims that coordinated market economies operate differently from 'free market' economies.[1] And cross-national welfare-state research, most prominently Esping-Andersen's *Three Worlds of Welfare Capitalism* (1990), has detected different welfare regimes with significant variations in redistribution and market compatibility.[2] Both approaches focus on the cross-national institutional variations in their respective policy field, but the links between particular forms of social protection and specific economic systems have yet to be adequately examined. This volume begins to bridge the two fields of research and ventures to unravel some of these linkages on both the analytical and the empirical level.

Let us consider investment into skills as an example that may exemplify how the production system and the system of social protection can be interlinked. Assuming rational behaviour, we would expect industrial workers to be willing to acquire particular skills only if such investment pays off in the long run. If the skills are not firm-specific and if they are sought after on the labour market, workers can expect to find employment with another firm at the current pay level if they lose their current job. However, in the case of firm-specific skills, skilled workers would either need credible employer commitments for long-term employment or even better external reassurances. Thus, strong employment protection through labour law and collective agreements may convince them that they will remain employed even in hard times, and that their wages will keep in line with pay trends in other firms. And if they are laid off, they would expect to be compensated fairly and long enough to seek a similar job or be adequately retrained (Estevez-Abe *et al.* 1999).

This example indicates that there are certain 'institutional complementarities' between different production regimes, industrial relations practices and social protection systems. Moreover, we would expect these to vary systematically across production systems and protection regimes. For instance, American workers with general skills receive premium market wages when there is high demand for their skills, but have no statutory employment protection; Japanese workers are willing to obtain firm-specific skills since they trust the commitment of large firms to guarantee 'lifelong' employment and occupational benefits; German skilled workers expect to be compensated during unemployment and retrained if they have been laid off. In a comparative empirical study, Huber and Stephens 'contend that within a given country, different aspects of the welfare state "fit" together and "fit" with different aspects of the production regimes, in particular their labour market components' (Huber and Stephens 1999: 3). Yet they warn that 'this "fit" ... is not a one-to-one correspondence between a whole configuration of welfare state and production regimes' (Huber and Stephens 1999: 3).

Thus far, as Peter Hall observes, 'we do not have a clear understanding of how ... different kinds of welfare states interact with different models of the economy' (Hall 1997: 196). This volume is an attempt to overcome the prevailing research gap in exploring the multiple interfaces between capitalist production and social protection. We believe that for a better understanding of modern welfare states, we need to consider social protection provided by social security systems, collective bargaining practices and employment regimes. Our knowledge of modern welfare states, and especially the sources of their current crises, remains limited until we reconsider the economic foundation on which they stand. Moreover, the productive function of social protection has often been overlooked due to the focus on redistribution as the main goal of welfare state policies. Hence, we also believe that for a better understanding of modern capitalism we ought to take into account the important impact of the welfare state on employment, skill acquisition, wage setting and investment. For instance, an analysis of the current problems of the German welfare state would be incomplete without considering its economic base, as would an assessment of Germany's economic crisis without considering the consequences of the current welfare state (see Hemerijck and Manow, Chapter 10 in this volume). The German social insurance system supports an export-oriented, high-quality production model, but the contributions to social insurance have become so high that employment growth in services is thwarted. This low employment level in turn endangers social policy financing and increases payroll taxes, thus leading to a vicious circle of 'welfare without work' (Esping-Andersen 1996a,b; Scharpf, Chapter 12). Thus there are mutual interdependencies between social security and the production system which affect both economic performance and the vulnerability of a given welfare state.

That the production system–welfare regime nexus has gained little attention thus far is particularly surprising, given the similarities of the analytical approach between Hall and Soskice's *Varieties of Capitalism* approach and Esping-Andersen's *Three Worlds of Welfare Capitalism*. In this introduction, we will describe the approaches taken by comparative political economy and welfare state research. Then, we will briefly describe the different areas of mutual impact and interdependency between production and protection and present the contributions to this volume. Finally, we will discuss the importance of comparative and historical analysis for studying the welfare–economy linkages.

Varieties of capitalism

Proponents of the Varieties of Capitalism approach in comparative political economy study the 'social systems of production' (Hollingsworth and Boyer 1997b) which are at the basis of national capitalist economies. This approach builds on the work of Andrew Shonfield (1965) on post-war economic policy and the subsequent neo-corporatist studies of organised capitalism in the 1970s (Goldthorpe 1984; Lehmbruch and Schmitter 1982; Schmitter and Lehmbruch 1981), yet it also imports insights from institutional economics (Williamson 1975). Challenging the thesis of convergence, several comparative readers have looked at the resilience and specificity of national capitalist models, contrasting the uncoordinated Anglo-American market economies with the German, Japanese or Scandinavian coordinated market economies (Berger and Dore 1996; Crouch and Streeck 1997; Hollingsworth *et al.* 1994; Hollingsworth and Boyer 1997a; Kitschelt *et al.* 1999). In addition, several comparative studies include particular policy fields, such as the link between vocational training and production systems (Crouch *et al.* 1999; Culpepper and Finegold 1999) or the role of central banks on wage formation (Iversen *et al.* 2000). In our view, the Varieties of Capitalism approach is marked by three features (see Hall and Soskice 1999): (1) it is a *systemic account* of the functioning of the institutional components of economic systems, (2) it distinguishes *national models* of production and maps their comparative advantages, and (3) it seeks a *micro-foundation* of how institutions shape actors' behaviour and reinforce existing institutional infrastructures.

Systemic accounts of contemporary capitalism

One major feature of the Varieties of Capitalism approach is the assumption that economic activity is socially embedded and that 'institutions matter' (Granovetter 1985). While the approach acknowledges the role of actors, it seeks a 'systemic' account of the institutional architecture of contemporary market economies, focusing on the 'total cake of "institutions of governance" of the various ingredient institutions' (Dore 1997: 24). Its proponents assume that institutions coalesce in the social system of production, 'this occurs – in part – because institutions are embedded in a culture in which their logic is symbolically grounded, organisationally structured, technically and materially constrained, politically defended, and historically shaped by specific rules and norms' (Hollingsworth and Boyer 1997b: 266). The institutional landscape is relatively inert: It provides constraints on the behaviour of economic agents and offers them specific opportunities, limits their strategic alternatives for individual and collective action, and encourages them to employ certain strategies rather than others.

In this view, particular institutions seem to hang together in a systemic way. Social practices as diverse as the Japanese lifelong employment and cross-shareholding between firms within the same *keiretsu* (inter-firm groups) seem to be interrelated (Dore 1997). These linkages represent – in game-theoretic parlance – 'strategic complementarities' (Cooper 1999; Milgrom and Roberts 1994; Soskice 1999), that is, mutually reinforcing and enabling institutional configurations. Thus 'two institutions can be said to be complementary if the presence (or efficiency) of one increases the returns (or efficiency) available from the other' (Hall and Soskice 1999: 10). Although this perspective has the danger of assuming too much coherence and intentionality (Stinchcombe 1968), it is a useful heuristic for identifying particular institutional equilibria as they coexist and co-evolve in time and place. Since we cannot assume that institutions arose in the past for reasons of their current complementary functionality, we also need to explain how complementary practices have co-evolved historically and have reproduced and reinforced each other by positive feedback (Pierson 2000).

Therefore the new comparative political economy literature attempts to trace chains of causation that run through different institutional subsystems and tries to reconstruct how strategic complementarities have emerged over long historical periods. By looking at the social system of production, this approach adopts an interdisciplinary perspective, taking insights from organisational theory, industrial sociology and industrial relations. Indeed scholars have shifted their focus. Having once concentrated on industrial governance in the narrow sense, they now study systems of corporatist bargaining and specific production systems, which enables them to analyse a broader 'ensemble of institutions' and more general governance structures in contemporary capitalism. *Prima facie*, most of these institutions seem to be only loosely coupled to the production system: legal traditions, standard setting, vocational training, financial systems, national 'systems of innovation' and monetary regimes. Much of the new comparative political economy literature shows how particular strategic complementarities between these institutional features and the economy can provide national systems with beneficial constraints (Streeck 1997) that could prove to be competitive advantages (Soskice 1991, 1999). That particular systems of social protection also shape the character of a 'national system of production' and thus have to be analysed in the same light as institutions mentioned above is the main claim motivating the different investigations into the welfare–economy nexus in this edited volume.

National models of capitalism

The current debate over economic globalisation and the competitiveness of national market economies has revitalised the 'convergence or diversity' controversy (Boyer 1996; Kitschelt *et al.* 1999; Rhodes and van Apeldoorn 1997). Studies in comparative political economy have shown that considerable diversity in national responses still prevails despite similar global and secular pressures on advanced industrialised countries and despite the diffusion of 'best practices' (Boyer 1996; Crouch 1996; Kastendiek 1990). National economies embody different mixes of social institutions, regulation and governance modes. 'Since the nation-state has been the unit providing the legal regulation on which many forms of coordination depend and within which the institutions supporting coordination have developed, systematic differences in forms of coordination and firm behaviour tend to be found across nations' (Hall 1997: 298).

'Institutional isomorphism' (DiMaggio and Powell 1983), the copying of institutional features for the sake of legitimation, provides one of many social mechanisms by which nationally distinct modes of economic activity become widespread. In the same vein, Ronald Dore claims that the behaviour of individuals in 'unstructured or weakly structured situations is determined by the behavioural dispositions they have acquired in the context of well-established institutions, and the way they behave determines the form that emerging or changing institutions take' (Dore 1997: 28). Given vested interests to maintain current comparative advantages, the established institutional landscape is largely entrenched. Modern capitalism shows a variety of governance forms between market and hierarchy, ranging from less to highly 'liquid' markets, and from less to highly 'negotiated' hierarchies (Crouch and Streeck 1997). Moreover, markets and hierarchies are complemented by and supplemented with varying degrees of additional coordination and governance, such as formal associations and informal networks, and they are subject to varying degrees of state regulation (Streeck and Schmitter 1985a; Powell 1990). Thus, different state traditions also account for the nationally different modes of market making and 'market breaking' and, consequentially, for the differences in economic performance from country to country. This line of argument has led to a renaissance of earlier insights from industrial sociology, on the distinctiveness of 'the' British vs 'the' Japanese firm (Dore 1973), for example.

Today's comparative political economy is marked by juxtapositions of two polar models of economic activities: Fordist vs specialised production (Piore and Sabel 1984); Anglo-Saxon vs Rhenish capitalism (Albert 1993); deregulated vs institutionalised political economies (Crouch and Streeck 1997); coordinated vs uncoordinated market economies (Soskice 1999). These converse concepts represent not only ideal-typical models of economic governance, they also serve as analytical devices to describe the dominant *national* models of economic governance in comparative empirical studies.[3] These authors claim that it is possible to distinguish particular national models of capitalism that differ in their institutional setup across the main subsystems. If there are distinct national models competing in a world economy, and if these models remain distinct despite trade liberalisation and the internationalisation of markets, then we can infer that a particular institutional configuration represents a 'viable' mix of comparative advantages and disadvantages.

Case studies of national economies, most importantly of the United States and the United Kingdom in comparison with Germany and Japan, have been used

Table 1.1 Two varieties of capitalism: Uncoordinated vs coordinated market economies

	Uncoordinated market economy	*Coordinated market economy*
Prime examples	USA, UK	Germany, Japan
Financial and economic governance	Short-term financial markets equity financing (shareholder value); limited business coordination, antitrust laws	Long-term patient capital debt financing (stakeholder value); strong business associations, inter-company networks
Production system	Low-skill production; mass products; numeric flexibilisation	High-skill production; high-quality products; flexible specialisation
Management–labour relations	Decentralised bargaining; contentious workplace relations	Coordinated bargaining; statutory worker representation
Training and employment	General education; short tenure, high turnover and inter-firm mobility	Vocational training; long tenure, low turnover and intra-firm mobility

Sources: Hollingsworth and Boyer (1997b); Soskice (1991, 1999); cf. Ebbinghaus (1999).

to show the contrast between coordinated and uncoordinated market economies (Soskice 1991, 1999; see Table 1.1). Empirically, some political economies seem to be hybrid cases that are situated between or even depart from the two conceptual poles of coordinated vs uncoordinated market economies. A national economy may be considered as a mixed case if there are subsystems, regions or economic sectors that divert from the dominant mode. For instance, the 'Third Italy' with its dense regional network and flexible specialisation diverts from the economy in northern and southern Italy. Moreover, economies with traditions of state intervention, like France (Schmidt 1996), cannot be easily accommodated within the coordinated–uncoordinated framework, as the editors of *Varieties of Capitalism* acknowledge (Hall and Soskice 1999). To juxtapose coordinated and uncoordinated market economies is not to deny that we find substantial variations between Continental European, Scandinavian and Asian coordinated economies, and it is certainly possible to discern subtle differences among Anglo-Saxon market economies.

Micro-logic

In contrast to earlier comparative studies of the macro-configurations conducive to economic growth and stability (e.g. Goldthorpe 1984), recent comparative case studies explain the micro-logic behind the variations in macroeconomic performance more systematically (see Hall 1997). As transaction-cost theory became an important part of modern economic analysis (Williamson 1981), economists

became more receptive to the role of information, trust, institutions and histories of cooperation. As a consequence of the 'economic turn' in political science (Levi 2000), the comparative political economy literature now explains macroeconomic outcomes as being the result of individual choices by economic agents. This actor-centred institutional analysis (Mayntz and Scharpf 1995; Scharpf 1997) often uses game theory to explain equilibria under particular institutional configurations and actor constellations.

The Varieties of Capitalism approach is actor-centred in that it is 'firm-centred', putting 'special emphasis on companies as the fundamental unit in a capitalist economy adjusting to economic shocks' (Hall and Soskice 1999: 4). The relations between economic actors are crucial for their strategic capacity: does the institutional configuration and the actor constellation provide opportunities for coordination? A good example for this kind of analytical inquiry is the collective action problem involved in an employer's decision to provide the common good of non-firm-specific vocational training. This problem has attracted the attention of many political economists (Crouch *et al.* 1999; Culpepper and Finegold 1999). Recent studies on the role of employers in social policy development have also focused on the micro-level to explain national policy outcomes (Mares 1998; Martin 2000; Martin and Swank 1999; Swenson 1997). Depending on the firm structures, employer preferences vary as to the trade-off between social risk distribution and control over employees (Mares 1998). While employers' pre-strategic preference may be to fight against *any* social spending programme, there are instances when they are in favour of compulsory social insurance. Whether cross-class coalitions will form between employers and workers in order to take social risks out of competition depends on the associational capacities and the production regimes that are in place (Swenson 1997, 1999, 2000).

Worlds of welfare regimes

Esping-Andersen's *Three Worlds of Welfare Capitalism* (1990) has made a major impact on comparative welfare state analysis over the last decade. Adopting a political economy approach, his analysis has some striking similarities with the new Varieties of Capitalism approach. First of all, analysing social security systems in a wider, systemic perspective comes relatively close to the focus on national systems of production used by comparative political economists. Second, Esping-Andersen's regime analysis stresses cross-national differences across welfare states, which cluster, in fact, around at least three (if not more) 'worlds of welfare capitalism'. Here there are interesting parallels to the political economy perspective that claims that national models of production differ systematically.[4] Finally, following the political economy view, Esping-Andersen and others have started to explore the welfare–economy nexus, especially the linkages between welfare state policies and labour markets. Let us examine these three aspects of welfare regime analysis, see which parallels they have with *Varieties of Capitalism*, and look at how bridges between the two approaches can be built.

Welfare regime analysis

The concept of 'regimes' indicates that welfare states are not merely a heterogeneous ensemble of disjoint social programmes, but that they are interrelated. 'To talk of "a regime" is to denote the fact that in the relation between state and economy a complex of legal and organisational features are systematically interwoven' (Esping-Andersen 1990: 2). Much like the Varieties of Capitalism approach, such an analysis assumes and stresses the systemness which reflects distinct 'principles' of welfare provision: 'Welfare regimes bunch particular values together with particular programmes and policies' (Goodin *et al.* 1999: 5). The comparative welfare regime approach seeks to elicit the regime differences by using ideal-typical models, which, like typologies, have 'an obvious attraction in being able to characterise whole systems with the related implication that different systemic features "hang together"' (Lange and Meadwell 1991: 84). Analysing welfare regimes is, therefore, a persuasive heuristic in comparing welfare states.

Going beyond the quantitative approaches that measured welfare state expansion only by social expenditures, Esping-Andersen evaluates the different welfare regimes using three multifaceted dimensions: (1) the degree of de-commodification (the extension of social rights independent of market mechanisms); (2) the system of stratification (i.e. inequality in outcome); and (3) the state–market–family mix (i.e. the form and locus of social protection) (Esping-Andersen 1990: 21–3; see Kohl 1993: 69–70). Following T. H. Marshall (1950), Esping-Andersen stresses the redistributive function of social policy: do universal citizenship rights provide protection to every citizen? Drawing on Polanyi's view of a social movement for social protection against the vagaries of free markets (Polanyi 1944), Esping-Andersen's approach measures the welfare states by their degree of 'de-commodification' (Esping-Andersen 1990). To what extent are benefits and services provided without any consideration of market forces, and to what degree do citizens have social entitlements that make them independent from market forces? In addition, his consideration of stratification highlights important differences in solidarity or social risk pooling (de Swaan 1988). For example, if occupational groups are covered by separate insurance schemes, this reinforces status differences and intra-class cleavages (Baldwin 1990). Finally, an important dimension of welfare regime variations is the location of social provisions: is the state, the market, voluntary associations or the family the main provider of social support by transfers and services? In fact, welfare regime analysis does not presume that the welfare state is the main provider. Instead, it studies the public–private mix as the major differentiation across welfare societies (Kolberg 1992; Rein and Rainwater 1986).

Esping-Andersen's distinction between different ideal-typical welfare regimes focused on differences along the dimensions of de-commodification, social stratification and public–private mix (see Table 1.2). Esping-Andersen's 'worlds' of welfare capitalism build on Richard Titmuss' (Titmuss 1958, 1974) earlier distinction between three different welfare models: the residual model, the industrial-achievement or merit-oriented model, and the institutional welfare state model.

Table 1.2 Esping-Andersen's three worlds of welfare capitalism

Regimes	*'Liberal'*	*'Conservative'*	*'Social-democratic'*
Prime examples:	USA, UK	Germany	Sweden
De-commodification	Low	Medium	High
Social rights	Need based	Employment-related	Universal
Welfare provision	Mixed services	Transfer payments	Public services
Benefits	Flat benefits	Contribution-related	Redistributive

Sources: Esping-Andersen (1990); cf. Kohl (1993).

The residual welfare model limits the role of the state in intervening into the market to providing basic benefits and services to the needy. The industrial-achievement model applies the social insurance principle most extensively, making benefits dependent on employment and contributions. In the institutionalised model, the welfare state intervenes most vigorously into market allocation by implementing redistributive social policies, guaranteeing universal rights and providing public services to all citizens. While Titmuss only sketched these different models as possible organising principles of some social programmes, Esping-Andersen uses the three models to describe national welfare regimes and cross-national variations.

Real worlds of welfare

Esping-Andersen's three worlds of welfare capitalism do not only reflect different principles of social protection, they are also the outcome of unique legacies of state-building and specific socio-political forces (and ideologies) that have put their stamp on welfare states (Esping-Andersen 1990; see also earlier Flora 1986; Rokkan 1999). According to Esping-Andersen, the main differences reflect three political traditions: liberal conceptions of a residual welfare state that should not intervene into 'free' markets by limiting work incentives and individual choice; paternalist Conservative state traditions and Christian-democratic conceptions of 'subsidiarity' (van Kersbergen 1995); and, finally, social-democratic conceptions of a universalist and redistributive welfare state. The *Liberal* welfare state provides relatively low flat benefits to all citizens in order not to interfere with individual self-help and market incomes, its level of de-commodification is low. *Conservative* welfare states have a medium level of de-commodification. They provide various occupational or social groups with extensive social transfer payments which are largely based on employment and contributions. Finally, *social-democratic* labour movements (in alliance with other social groups, especially farmers) expanded the universalist de-commodifying Scandinavian welfare states to provide universal social benefits and extend public services to all citizens.

Although these ideal-typical models are partly abstractions from the historical traits of the Scandinavian, Germanic and Anglo-American welfare-state development, we should not reify them. They are primarily pragmatic conceptual devices for comparison (Kohl 1993: 75). While empirical accounts of cross-national variations in different social policy fields are often confusing, such a regime analysis provides a prism through which to shed light on salient aspects of welfare states and their interaction. Certainly, Esping-Andersen largely conceives the historical trajectories as the result of different distributions of power resources, thereby overemphasising the role of ideology and deliberate political strategy (Kohl 1993; Offe 1993). While some researchers have criticised the conflation of ideal and real type in Esping-Andersen's regime analysis (Rieger 1998), others refute the path-dependency argument, claiming that many welfare states have restructured and thus are not fixed in one particular regime (Borchert 1998; see also Crouch, Chapter 5). Only comparative historical analysis can show how particular regimes have emerged and whether they have changed over time. Yet, despite this criticism, it remains true that Esping-Andersen's analytical framework has proven extremely helpful for the comparative study of welfare states.

More recently, some comparative studies have challenged the limitation to three worlds of welfare capitalism, making strong cases for additional 'families of nations' (Castles and Mitchell 1993). As Castles (1995) and Ferrera (1996) point out, the southern European welfare states should not be subsumed under the heading of 'the' conservative regime, given the importance of family, clientelism and dualist labour markets. Some observers have claimed that the 'radical' antipodal welfare states of Australia and New Zealand (Castles and Mitchell 1993) are distinct from the Anglo-American liberal welfare-state regimes: since inequality is reduced by high wages, industrial relations play an important role in welfare outcomes. Finally, the classification of the Japanese case poses some problems: is it a unique case of Confucian welfare ideology or a hybrid mix of liberalism and conservative welfare regime ingredients (Esping-Andersen 1997; Goodman and Peng 1996; Gould 1993; Jacobs 1998; Leibfried 1994)? Interestingly, all these 'outliers' do not conform to narrowly conceived welfare-state boundaries, suggesting that there are important interactions between social policies and the political economy (or family structure).[5] Indeed, there might be functional equivalents between social protection with the help of welfare policies and other means that reallocate and redistribute resources with a welfare-enhancing goal. In the case of Italy, the impact of a shadow economy and family solidarity provides non-state support; in Australia, it is the successful bargaining for high wages and the juridical arbitration of labour conflicts; in Japan, the peculiar long-term company employment policies – just to give a few examples.

The political economy nexus

Esping-Andersen conceives welfare states as being 'fundamental forces in the organisation and stratification of modern economies' (Esping-Andersen 1990: 159). He views the welfare state as the 'principal institution in the construction of different models of post-war capitalism (Esping-Andersen 1990: 5)'. Yet, exactly how the welfare state covaries with other features of modern capitalism remains largely unexplained and underinvestigated. In his own research, Esping-Andersen focused on the labour market as part of the welfare state–economy nexus

(Kolberg and Esping-Andersen 1991; Esping-Andersen 1993, 1996a). Indeed, welfare states shape employment regimes, they have an impact on overall employment rates, the gender gap in participation rates, the average length of unemployment, the proportion of skilled to unskilled work, and the possible pathways into and out of work. These linkages are regime-specific. For instance, Continental 'welfare-without-work' societies responded to increasing unemployment with labour shedding strategies that fostered early retirement (Esping-Andersen 1996b; see Ebbinghaus, Chapter 4, and Hemerijck and Manow, Chapter 10). While Esping-Andersen has provided ample evidence that particular welfare-state regimes and employment regimes 'tend to coincide' (Esping-Andersen 1990: 159), the relationship and mutual influence between the spheres of capitalist production and social protection reach beyond the labour market and may be more fundamental than 'coincidental'.[6]

Despite claims of convergence due to globalisation, comparative studies still find an 'elective affinity between the types of production regime, patterns of socio-economic inequality and protection through welfare states, and the constitution of corporate political actors in parties and interest groups' (Kitschelt *et al.* 1999: 3). Nevertheless, the welfare–economy nexus is still almost completely absent from the analysis of the institutional features which influence economic performance and the organisation of production and exchange. The state of the debate is marked either by programmatic statements that call for a more thorough analysis of the work–welfare interplay (Hollingsworth and Boyer 1997a: 447–9; Hall 1997: 196) or by studies that identify patterns of systematic correlation between the spheres of production and social protection with the help of macroeconomic indicators (Huber and Stephens 1999). This lack of attention for the specific links between both spheres has been partly due to the fact that the function of the welfare state is often only seen as constraining the market (Hollingsworth and Boyer 1997a: 447–9). The welfare state is merely conceived as an 'institutionalised counter-principle of capitalism' (Lepsius) and social policy is predominantly perceived as 'politics against markets' (Esping-Andersen). Thus the importance of the welfare state for a nation's social system of production has been underestimated in the past.

While Esping-Andersen's work has begun a fruitful debate about the many interfaces between advanced welfare states and the organisation of contemporary capitalism, many additional linkages between both spheres – besides the labour–market nexus – remain to be explored. A comparison between welfare regimes and production systems reveals some elective affinities (Huber and Stephens 1999): Uncoordinated market economies go hand in hand with 'liberal' welfare states and low social expenditure (which is also true for the antipodes). Yet among coordinated market economies, we do find much more variation (Ebbinghaus 1999): Germanic social market economies and 'Christian-democratic' Continental welfare states go together as do Nordic neo-corporatist economies with 'social-democratic' universalist welfare regimes, and Latin state-led market economies and late-coming welfare states. Finally, Japan's coordinated market economy has a hybrid welfare regime that combines residual public and extensive private welfare arrangements. The obvious greater differentiation in welfare regimes may lead to a new reconsideration of the intra-regime variations among 'coordinated' market economies and to further study of the 'functional alternatives' and possible disfunctionality of different welfare regimes in coordinated market economies.

While there are unexplored institutional complementarities or elective affinities between the welfare state and the production regime, there is also a trade-off between equality and efficiency (Okun 1975; Esping-Andersen 1993). In the comparative political economy perspective, however, this trade-off is rather specific to a particular regime, and not a universal problem of all welfare states: a particular welfare-state regime can undermine the 'comparative institutional advantages' (see Hall 1997) of a given production regime, or the economic development can overstrain the buffering capacity of a given welfare-state regime. Some observers consider the impact of globalisation on welfare states to be far less important than endogenous challenges such as demographic shifts (Pierson 1998). Changes in the production systems due to the globalisation of financial markets and international economic competition may have dire consequences for welfare states, if there is indeed a complementarity between both realms. Related questions arise: Which kinds of political coalitions may emerge and develop vested interests in a given production and welfare-state regime (Manow 2000)? And what will happen in the future if one or both spheres come under pressure to change – will this undermine the remaining institutional 'complementarity'?

Studying welfare state–economy linkages

Following Esping-Andersen, we use the concept of 'regime' to denote the fact that 'a complex of legal and organisational features are systematically interwoven' (1990: 2). A neat separation of welfare-state regimes from other aspects of a national political economy, such as industrial relations, production systems, employment regimes and financial governance, is often difficult – the boundaries between these institutional complexes are often blurred both conceptually and empirically. Nevertheless, we need to delineate non-overlapping typologies in order to avoid a tautology when speaking of institutional complementarities between components of two conceptually differentiated spheres. Therefore we subsume the core programmes of social protection under the conception of the welfare regime: social insurance, social assistance, labour market policies and social services. Yet there are also social policies – 'private', occupational welfare benefits (Shalev 1996), for example, that are borderline cases between publicly mandated social policies and company-related benefits derived from a company's human resource policy. While we need to separate the different spheres conceptually, it is the possible linkages and interdependencies between these institutional complexes that are the main focus of this volume.

This book revolves around possible linkages between social protection and three areas of the political economy that are often specialised fields of research, though the 'Varieties of Capitalism' approach attempts to integrate all three in the analysis of capitalist systems. The first area is the system of industrial relations, comprising corporate actors, such as the state, labour and employers, and the laws and rules governing the conditions of employment relations, most importantly via collective bargaining. The second area entails the production system and employment regime, which involves the social organisation of the production process and the employment strategies of firms. Finally, the financial and corporate finance system is the third area, which defines the specificity of a capitalist system: the way financial markets are organised, companies are controlled and investments are financed. Let us briefly discuss some of the linkages between welfare states and these areas of the political economy and introduce examples from the following chapters.

Industrial relations

The 'social partners' – organised labour and capital – have not only played an important role in the expansion of modern welfare states, but they have also influenced the current reform processes (Esping-Andersen 1992; Pierson 1995; Swenson 1991, 1999). In addition, collective bargaining between employers and unions can have an important impact on welfare outcomes. But the reverse is also true: social policy can affect labour relations. Thus wage bargaining is conducted in the shadow of social wages and the non-wage labour costs set by social policy legislation (Hassel and Ebbinghaus 2000). Collectively negotiated wages, which affect the demand for labour and thus employment levels, are a major variable for employment-based and payroll-financed welfare states.

The policy stance of unions and employer associations was often assumed to be fixed: unions would promote universal welfare states, and employers would oppose each and every step leading to an expansion of social rights. Yet the preferences of unions and employers seem to vary with the social composition of their membership and the strategic interaction between collective actors. In Chapter 3 *Isabela Mares* uses a historical and game-theoretic analysis to reconstruct the strategic bargaining between unions, employers and the state over unemployment insurance in the interwar years in France and Germany. Although employers may be generally opposed to social insurance, the actual position of capital was a strategic response to the range of political options on the social policy agenda. *Mares* shows that compulsory unemployment insurance emerged in Germany thanks to a cross-class alliance with unions, while French employers remained opposed to anything but local unemployment assistance outside the control of unions.

Comparative studies have shown major cross-national differences in industrial relations from decentralised to centralised, voluntarist to corporatist and sectionalist to encompassing interest intermediation (Crouch 1993; Visser 1990). For countries with similar welfare regimes and social partnership models, we would expect common problems of economic coordination and adaptation. Several authors in this volume investigate the interplay between both realms and its impact on labour market performance. *Hugh Compston* (Chapter 6) compares the different degrees of state intervention in favour of working time reductions in Europe, discussing factors such as union density and union participation in economic policy making. *Anke Hassel* (Chapter 7) studies the impact of fragmented or encompassing associations and particularistic or solidaristic wage policies on the growth potential for low-wage–low-productivity sectors in Britain and Germany. *Bernhard Ebbinghaus* (Chapter 4) discusses the different forms of collusion between employers and organised labour in using early retirement as a labour shedding strategy in Europe, Japan and the USA. Whether organised labour and capital use labour shedding to ease the costs of economic adjustment while maintaining industrial peace depends not only on the available pathways to public pre-retirement programmes but also on the exigencies of national labour relations and production systems at the workplace.

These findings suggest intricate interdependencies between labour relations and labour market outcomes. In the German case, for instance, the system of collective bargaining is firmly entrenched and the social partners are powerful. The state, on the other hand, has limited capacity to intervene in industrial relations. Since strong unions and legal employment protection prevent German firms from being able to reduce wages or downsize their workforce, they can only achieve 'flexibility' by using such labour supply strategies as working time reduction or early retirement. But the causal link can also be reversed. Building on an argument developed by Peter Swenson, *Philip Manow* shows in Chapter 2 that employers in Germany and Japan were in favour of expanding welfare-state programmes. These policies promised to stabilise the sector-wide collective bargaining system and relieve it from the pressures stemming from the wage compression and wage stickiness resulting from coordinated wage bargaining.

Unions and employer organisations can derive organisational strength and influence outside the realm of collective bargaining if they have an institutionalised role in the self-administration of social insurance, as *Colin Crouch* argues in Chapter 5. However, he shows that there is no simple and fixed correspondence between particular types of industrial relations (contestative, pluralist or neo-corporatist) and specific welfare regimes. He warns about the dangers of over-straining path-dependency arguments and the analytical rigidities inherent in an approach that labels countries as having only one regime type. Analysis must allow for hybrid or 'mongrel' cases and for change over time. *Crouch* advocates an 'institutional probabilism' (Hirschman), stating that certain trajectories of change or continuity are more likely than others. The devolution of the British corporatism of the early 1970s into the market liberalism of the 1980s and 1990s is a case in point. Interpreting regimes as the 'diversified inheritance of action possibilities', *Crouch* emphasises that the development of an institutional setting can never be entirely explained by its legacy alone.

Production and employment regimes

Social policies are often seen as 'politics against markets', as the promotion of equity over efficiency (Esping-Andersen 1993). They are thought to have a de-commodifying, non-market related impact on the labour market and the labour contract. However, social policies also affect labour costs and alter work incentives. High labour costs due to social protection could represent a 'beneficial constraint' (Streeck 1997) for employers, forcing them to pursue a production strategy that emphasises high quality and flexible specialisation. But there are also negative effects, as *Anke Hassel, Anne Wren* and *Fritz Scharpf* demonstrate in their chapters. High non-wage labour costs hamper employment growth in the low-productivity service sector. While the encompassing Scandinavian welfare states provide many of the (social) services in the public sector and finance them largely through taxes, the Continental European welfare states with their strong emphasis on social contributions perform poorly when it comes to job growth in private and public services. How countries react to the structural change from an industrial economy to a service economy thus depends on the institutional architecture of their welfare states and their industrial relations systems. In contrast to the 1950s and 1960s, advanced capitalist societies face a trilemma. They can only achieve two of three macroeconomic goals – income equality, full employment and balanced budgets (see *Anne Wren*, Chapter 11). As *Fritz Scharpf* demonstrates in Chapter 12, the societal choices OECD countries made differed widely. Not fully determined by the given institutions in a country, these choices have ultimately been political ones, as *Anne Wren* argues in Chapter 11. Taking the three different ideological traditions, Social Democracy, neo-liberalism and Christian Democracy, *Anne Wren* describes the different distributive choices in France, the UK and the Netherlands, respectively.

Instead of contrasting the employment consequences of different welfare regimes, *Anton Hemerijck* and *Philip Manow* compare in Chapter 10 the responses of the more similar Dutch and German welfare state to the 'welfare-without-work' (Esping-Andersen 1992) dilemma. The successful labour market reforms in the Netherlands and the reform stalemate in Germany suggest that it is less the similar problem configuration than the nation-specific institutional and political capacities which explain the divergent reform trajectories. Small *intra*-regime differences between otherwise very similar industrial relations or social protection systems can lead to entirely different outcomes, thus calling for a much more fine-grained institutional analysis than *inter*-regime comparisons writ-large commonly imply.

Finally, one of the major burdens of today's welfare states is posed by structural unemployment which has increased the cost push on employment-related social spending and reduced the general tax and social wage base. On the other hand, welfare states may also serve an important function in stabilising, maintaining and enhancing production regimes by providing an educated and healthy labour force which is shielded from social risks. For example, we would expect a high degree of covariation between the transportability of welfare entitlements and of worker's skills, both of which play a large role in labour mobility. The more occupational benefits firms offer, the more likely workers will be to invest in firm-specific skills. Coordinated vs uncoordinated economies may differ from each other in the degree to which the welfare state provides economic actors opportunities for long-term engagements. As *Anke Hassel* points out in Chapter 7, only the interaction between the state, organised capital and labour can account for labour market outcomes. The effectiveness of a liberal or a Continental regime with respect to employment growth in the low-productivity sector also has important repercussions on welfare financing. If employers are free to hire and fire, this has profound impact on the willingness of workers to acquire firm-specific skills. A low-trust, low-productivity, low-skills, low-wage equilibrium is self-enforcing, while the opposite equilibrium can arise if organised labour and capital can use the welfare state to alleviate the costs of economic coordination. Moreover, the participation in social administration and institutionalised workplace participation make the long-term gains from cooperation superior to the short-term payoff from 'defection'. Therefore, the welfare state can provide external resources that support an infrastructure of cooperation between unions and business in general, and between workers and managers at the workplace level. The different industrial relations and welfare regime configurations affect not only the peaceful or confrontational nature of labour conflicts, but the feasibility of more skill intensive or more Fordist production systems as well, as *Bernhard Ebbinghaus* shows in Chapter 4.

Occupational welfare, financial systems and corporate governance

Several contributions to this volume focus on the public–private welfare mix, in particular the role of private occupational pensions. Although companies may provide occupational pensions merely for reasons of their human resource strategy (binding skilled workers to their company), these private pensions are part of a welfare state's social provision since they are at least partly regulated by the state and they interact with public pensions (see *Bernhard Ebbinghaus*, Chapter 4). Moreover, the public regulation of private pensions as financial instruments and the way they are taxed proves to be crucial (see *Margarita Estevez-Abe*, Chapter 9, and *Gregory Jackson* and *Sigurt Vitols*, Chapter 8). If we are to examine occupational welfare benefits, it is important to include Japan and the USA in our investigation, two prime cases of very different 'capitalisms' and welfare regimes. Their inclusion not only corrects for the Euro-centric bias of many comparative welfare-state studies, their peculiar private–public mixes show important commonalties and differences that are revealing for the intricate interaction between welfare regimes and production systems. Many scholars label the American and Japanese welfare states as liberal or residual, following Esping-Andersen (1990, 1997), but this squares oddly with the stark differences between the United States' 'free' market economy and Japan's coordinated market economy. Whereas in the American case, as *Ebbinghaus* shows, these occupational pensions remained part of a Fordist production and employment policy of 'hiring and firing', the Japanese companies provide occupational pensions and reemployment practices as a means to build long-term employment relationships. These differences in production and employment regimes are also linked to different forms of corporate governance: Japanese companies use their institutionalised links to firms within their group to find reemployment for their retired workers, while American hostile takeovers may lead to a 'raid' of pension funds, ending the previous employer commitment.

Moreover, *Estevez-Abe* and *Jackson and Vitols* map different types of interaction between occupational pensions and financial markets: Japanese pension funds and German book reserves reinforce 'patient' capital, whereas American and British pension funds amplified short-term financial market pressures. *Gregory Jackson* and *Sigurt Vitols* (Chapter 8) compare the two varieties of capitalism with two forms of pension systems: market-based pension regimes in Britain and the United States, and solidaristic pension regimes in Germany and Japan. Their research suggests that different pension systems do indeed have a differential impact on financial systems and corporate governance, reinforcing free market and coordinated capitalism, respectively. *Margarita Estevez-Abe* (Chapter 9) complements a comparative with a historical analysis of Japanese pension funds in order to uncover the forgotten link: the welfare–finance nexus. The design of Japanese pension funds and their state regulation helped to consolidate the bank-dominated financing system and stable stockholding systems upon which Japan's coordinated capitalism is based.

Analysing linkages through comparative-historical analysis

Although the contributions to this volume set out to identify the possible linkages between welfare regimes and political economies, they do not claim that there is a unidirectional or deterministic relationship. The linkages of the welfare state–political economy nexus are often rather indirect and conditional, depending on the type of regime in place. Therefore, a historical and comparative institutionalist analysis is needed to unravel the possible linkages. One of the principal aims of this book is thus to map several 'covariations' between the varieties of capitalism and the different worlds of welfare capitalism. Two methodologies may help us to explore the 'elective affinities' of production systems and welfare regimes. One approach applies 'process tracing' (Katzenstein) of the 'historically rooted trajectories of growth' (Zysman 1994). Yet unless path dependency is omnipresent, history may be less of a guide in judging the functional complementarities of today's structure and the challenges to its continuity. The other approach applies comparative analysis, which can help to reveal current institutional complementarities. In a comparative analysis, which tends to be more static, the coexistence and mutual support of 'equilibrium institutions' (see Shepsle 1986) can be delineated. However, without a historical analysis, there is the danger of the retrospective fallacy that sees today's institutional complementarity as the rational calculation of actors, disregarding that it might be merely the outcome of unintended consequences and unforeseen contingencies.

In order to understand the linkage of the welfare state and political economy, historical institutionalists have studied their origins and co-evolution over time. What are the origins and formation of welfare states and how did this legacy affect the development of labour relations, production and employment regimes, or the financial systems? While some have turned to history as a 'method' to check the validity of general theories (see Ragin 1987), most historical institutionalists are turning to history as a 'theory' (Immergut 1998: 19): 'They emphasise the irregularities rather than the regularities of history and demonstrate the limits of universal causal models'. The contingencies of history play an important role – the welfare state and its industrial economy were shaped under particular historical conditions, circumstances and coincidences. Thus the sequencing in the evolution of particular institutions has a long-term impact. For instance, the late formation of compulsory social insurance had an impact on the chances of voluntary insurance schemes or employers' occupational schemes of becoming entrenched. Path-dependent processes have been described by historical institutionalists. They point at the institutional inertia of processes that are often inefficient, unintended and accidental (Pierson 1997). There is hardly an 'efficiency of history'. Politics cannot easily change historically derived institutions, as functionalist or rational choice theorists imply (March and Olsen 1984). Instead, institutional change is a complex and a contingent process, and often an undetermined one.

Cross-national comparison, while often also historical in its approach, adds another methodology for unravelling the linkage between institutional arrangements. Instead of studying the institutionalisation processes over time, the comparative method makes it possible to analyse the coexistence of institutions in a snapshot manner (Ragin 1987). What kind of welfare state coincides with what kind of labour relations, production system, employment regimes or financial systems? Cross-national analysis drawing on typologies and statistical methods has been used to detect the overlap between particular welfare-state regimes and specific aspects of their political economy. Correlation statistics may not be very informative since they assume a functionalist logic and universal causality. Comparative institutionalists, on the other hand, argue quite convincingly that there are 'contextual logics of causality' (Immergut 1998). Hence, if there are linkages between the welfare state and political economy, we would expect them to take on particular forms in both realms. As Weber pointed out, there are 'elective affinities' between the two institutional complexes more or less 'tightly' coupled. When they are tightly coupled, we would expect changes over time in one realm to cause changes in the other realm, while this would be more open in the case of loosely coupled systems. However, we often face a small-*n* problem. We have more explanatory variables than cases, and more complex interaction effects than we can model in statistical analysis. If we want to go further than macro-configuration analysis, we may not only need historical accounts, but also assessment of the level of micro-processes.

Comparing Welfare Capitalism combines a plurality of approaches: Some authors have opted to trace historical processes, such as the co-evolution of production systems and protection regimes, some to compare at the macro-level the elective affinities between welfare regimes and economic variables and some to use game theory to reconstruct micro-level interest formation. By studying the linkages between welfare states and political economies, we hope that we can contribute not only in identifying institutional complementarities but also in suggesting causal mechanisms for their co-evolution and their mutual feedback. In the concluding Part V, Michael Shalev in his commentary (Chapter 13) calls for a reconsideration of the 'politics of elective affinities', i.e. how political forces have shaped the

linkages between welfare state and political economy. Going a step further, the editors discuss several avenues for future research in their outlook (Chapter 14): exploring the feedback processes between politics and policy, combining new perspectives on gender and the life course, and investigating the role of social concertation in the adaptation of welfare states to the challenges of increased economic internationalisation. We hope that this volume is only one of many future collective endeavours to bridge the disciplinary divide and explore the indirect linkages between production and protection.

Notes

1 For a review of the recent literature on comparative political economy, see Hall (1997).
2 See the recent overview on comparative welfare-state research (Pierson 2000).
3 Originally, different forms of 'industrial order' and 'economic governance' were studied predominantly on the sector level (Hollingsworth *et al.* 1994; Streeck and Schmitter 1985b), while more recent contributions emphasise the importance of national models by providing studies on selected countries (Berger and Dore 1996; Crouch and Streeck 1997; Hall and Soskice, forthcoming; Hollingsworth and Boyer 1997a).
4 However, it should be emphasised that both approaches differ in an important theoretical/methodological respect: the comparative welfare-state research lacks the strict micro-foundation that we find in the Varieties of Capitalism literature. Instead, different welfare regimes are perceived to embody different (liberal, conservative, socialist) 'principles' of social protection (see Esping-Andersen 1990).
5 Responding to some of his critics, Esping-Andersen stresses now the family and household structures, including gender divisions of labour (Esping-Andersen 1999).
6 More recently, Esping-Andersen acknowledges the covariation with industrial relation systems (Esping-Andersen 1999), for a discussion of such covariations see the contribution by Crouch, this volume and Ebbinghaus (1999).

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Part I

The origins and development of welfare capitalism