Globalization and the US Political Economy: The Domestic Sources of Liberal Leadership

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ABSTRACT: The US economy has been outpacing many relatively laggard economies in Western Europe and Japan. What is the basis for American economic success in a more globalized world economy? Starting from the basic tenets of the ‘models of capitalism’ literature, this paper modifies this approach, embedding domestic market structures in the broader global economy to understand how this effects economic performance. The liberal market institutions and entrepreneurial culture of the United States, it is argued, are especially well suited to exploit the opportunities of globalization, allowing the US to generate technological and organizational successes in increasingly competitive world markets. This analysis thus adds the idea of global complementarity of models of capitalism – the extent to which any given model conforms to the incentives of global markets. Global complementarity reduces relative opportunity costs and leads to improved economic performance. Models that buck global trends pay a rising price for doing so, and this should be reflected in relatively poor performance. As such, the US does offer something of an exemplary model for the global era. However, institutions and policies of the American political economy cannot simply be transplanted. The domestic roots of American prosperity include not only a market-oriented policy framework, but also cultural and ideational traits (i.e., an openness to risk, high levels of entrepreneurialism) not easily engendered in new environments. Thus the US stands out as a liberal leader, but not necessarily a straightforward model for others to follow.
Introduction

One should perhaps be forgiving of academics who attempt to peer into the future. If one were to return to the world of 1990 and review the literature of comparative political economy, an obvious conclusion would emerge. The US was in decline, outclassed and out-innovated the Japan, who willingly manipulated and exploited non-market business relationships (heresy in the American free market canon) to gobble up global market share. It was only a matter of time until they surpassed the US as the global leader.

Unfortunately for those Cassandras, things did not quite turn out this way. The US economy has been outpacing many relatively laggard economies in Western Europe and Japan, and doing so during a period of increasing globalization. What is the basis for American economic success in a more globalized world economy? Starting from the basic tenets of the ‘models of capitalism’ literature, this paper modifies this approach, embedding domestic market structures in the broader global economy to understand how this effects economic performance. The liberal market institutions and entrepreneurial culture of the United States, it is argued, are especially well suited to exploit the opportunities of globalization, allowing the US to generate technological and organizational successes in increasingly competitive world markets. This analysis thus adds the idea of global complementarity of models of capitalism – the extent to which any given model conforms to the incentives of global markets. Global complementarity reduces relative opportunity costs and leads to improved economic performance. Models that buck global trends pay a rising price for doing so, and this should be reflected in relatively poor performance. As such, the US does offer something of an exemplary model for the global era. However, institutions and policies of the American political economy cannot simply be transplanted. The domestic roots of American prosperity include not only a market-oriented policy framework, but also cultural and ideational traits (i.e., an openness to risk, high levels of entrepreneurialism) not easily engendered in new environments. Thus the US stands out as a liberal leader, but not necessarily a straightforward model for others to follow.

The US as a Leading Economy

Over the past decade, despite the sharp recession that followed the bursting of the ‘dot com’ bubble combined with the economic effects of the 9/11 attack, the United States has been a leading performer on measures output and income, employment, and productivity.\(^1\) Contrasting US performance against the other G-7 economies, America has not only retained but expanded its economic lead over the past decade.

The most striking comparison comes in regards to national output and income, particularly when expressed as per capita GDP. As Figure 1 shows, the other major industrial (G-7) economies were converging on American income levels through the 1970s and into the early 1980s. Relative to America, per capita GDP among the other major economies leveled off in the mid-eighties and started to decline in the 1990s. The exceptions were Canada, which has seen a bit of an upturn as of late, and the UK, which kept pace with US growth throughout the period. The most dramatic declines were seen in Germany\(^2\) and Japan, the latter of which had been widely expected to become the global pacesetter in the late 1980s. These trends translate into an

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\(^1\) The one area we need not examine is inflation, as none of the G-7 economies have face inflationary problems since the 1980s. Japan, on the other hand, has suffered from periods of deflation in the last decade.

\(^2\) Note that the data for Germany in Figure 1 only includes the eastern Länder after 1998.
approximately 30% gap in average income between the US and the euro zone states (Figure 2). Trends in rates of growth (Table 1) do not give any indication of these variations abating. As a recent Swedish think tank study exposed (no doubt to elicit maximum shock value), if the per capita GDPs of the nations of Europe were compared against the individual states of the US, France, Germany and Italy would only score better than the five poorest American states (Bergström and Gidehag, 2004).

The American economy has also been a ‘jobs machine’ since 1990. Despite having a rate of employment growth in the 1990s (1.3%) that was actually down from previous decades, it was for times the rate of four major European economies (Sorrentino and Moy, 2002: 20). Moving from a position of steadily higher unemployment in the 1960s and 1970s, America’s comparative rates fell below those of other major economies since the mid-1980s and, with the exception of Japan (where unemployment rates are rising) and Great Britain (where they have fallen below US levels since 2002), the US has maintained its employment lead (Figure 4). Unemployment rates are not only higher in Europe, but represent a more chronic problem. Roughly half of Europe’s unemployed have been out of a job for more than a year, compared to less than 10% for the US.\footnote{Thus the burden of unemployment falls on a smaller proportion of the population in Europe than America, were losing one’s job is a more widespread yet transitory phenomenon.} All of this translates into substantially higher employment ratios (employment as a percentage of the adult population) than the other G-7 economies, particularly compared to France and Italy (Figure 5), which represents a substantial underutilization of labor in these economies. The bulk of American jobs growth came in services, including healthcare, financial services, and the retail sector (Sorrentino and Moy, 2002: 23). Despite the tendency to portray service jobs as ‘part-time, minimum wage, burger-flippers’, the percentage of part-time workers in the US actually declined from 1983-2000 (it went up in Europe; Sorrentino and Moy, 2002, p. 25), healthcare and financial services both offer above average hourly wages, and the U.S. Bureau of Labor Statistics reports that average hourly retail wage in 2004 was $12.07, an approximately 50% increase from 1990 (BLS website).

Of greater importance long term is that US productivity shot ahead over the last decade. This is a reversal of the trend of the latter 20th Century. The US emerged from the Second World War with its industrial base not only undamaged but greatly expanded and a commanding productivity advantage, an advantage in terms of levels of productivity that it has yet to surrender (see the top part of Table 1). However, given the economic advantages of follower economies (i.e., being able to import proven technologies and methods), faster productivity growth allowed the other major economies to close in on US productivity levels. Starting with a GDP per hour worked just 44% of the United States’ in 1950, Europe narrowed the difference to 94% by 1995. Indeed, even through the first half of the 1990s, total economy productivity growth rates for the EU were higher than the US. This situation reversed after 1995, with the US rate accelerating and European and Japanese rates slowing. As a result, by 2004 European output per hour had slipped back to 85%, a fifth of the gains of the previous 45 years being lost (Gordon, 2004b, Table 1)\footnote{‘Europe’ for Gordon includes the EU-15 minus Greece, Portugal and Spain.}. A similar trend can be seen for Japan and Canada, as well as across the range of productivity measures (bottom half of Table 1). In short, the US economy is becoming comparatively more productive, European and Japanese economies less so.

The bigger question is whether this represents a fundamental change in trend. The spurt in American productivity in the late-1990s is generally attributed to increased investment in information and communications technology (ICT) and its spread throughout the economy.
(Oliner and Sichel, 2002). From this perspective, the bulk of investment in ICT in the US has largely run its course and has slowed in recent years. This should allow other economies to catch-up to American levels of ICT investment and diffusion, producing a realignment of productivity growth rates. However, the increased rate of American productivity was not primarily driven by ICT-producing industries like Microsoft and Intel. Productivity growth rates for these industries were roughly the same in Europe and America; one need only note the competitiveness of Ericsson and Nokia (Gordon, 2002b, Table 3). Almost all of the aggregate productivity differences between the US and Europe stemmed from improvements in American ICT-using service industries, primarily securities, wholesale trades, and retail trades (van Ark, Inklaar, and McGuckin, 2003). As Gordon notes, these gains did not accrue simply by installing electronic checkouts and inventory scanners, but also by reorganizing the structure of American retailing, driven by ‘big box’ retail operations like Wal-Mart, Home Depot, and Best Buy (Gordon, 2002B, p. 9). Such gains in service productivity are distinctly lacking in Europe and Japan, where extensive governmental and social impediments limiting the prevalence of ‘big box’ stores.5 The recent vocal and public killing of the EU directive to liberalize trade in services, despite the fact that it could create as many as 600,000 jobs across the Union, does not bode well for any the removal of such barriers in the near term (“Not at Your Service”). More to the point, as the American economy has recovered, the rate of productivity growth has, in fact, increased.6

Taking this all together, we see an American economy that is richer, provides a higher level of employment, and is more productive that the major European or Asian competitors. Of course, not all is doom and gloom for the rest of the world. Major European economies may be lumbering, but the economies of smaller EU states – the Netherlands, Denmark, Finland, and most exceptionally Ireland7 – have kept pace with the US in terms of output and jobs. Nor is the US economy without its flaws, especially the ballooning budget and current account deficits. The fiscal deficit for 2004 was $412 billion or 3.6% of GDP, although the CBO projects the deficit to decline over the next five years. America’s international balance also slipped further into the red, with the current account deficit plunging to a record $617 billion (5.7% of GDP) in 2004.8 These twin deficits have produced a sharp fall in the dollar, especially against the euro. Then, of course, there is the demographic and fiscal bomb provided by Social Security and Medicare, although this is hardly a problem unique to the US. America has shortage of economic problems of its own.

Many Europeans especially would also recoil at the suggestion that Americans have a vastly better standard of living. There are aspects of the American economy that increase GDP but not necessarily national welfare: extensive road and building construction to connect scattered suburbs (now exurbs) to inner cities; more money spent on heating and cooling to

5 Although Ikea is an exception. These include land use regulations to protect greenfield sites, restrictive shop-closing hours, congestion in central city locations, and restrictive labor rules. Equally, reliance on public transportation limits the ability to do large shopping orders, decreasing the attractiveness of such operations to consumers.
6 The BLS reports that output per hour in the non-farm business sector rose by 4.3%, 4.4%, and 4.0% in the last three years, respectively.
7 Ireland had a per capita GDP that was 55% of America’s in 1990. By 2002, it was 87%, better than any of the other economies listed in Figure 2. A ‘Celtic tiger’ indeed!
8 Farrell, Ghai, and Shavers (2005) note that the headline current account number probably overstates the real deficit by about 25% as this part of it is represented by re-imports of products and parts from American multinational corporations with operations abroad.
combat America’s harsher climate; more money spent on business and home security; and the costs of keeping nearly 2 million people incarcerated (Gordon, 2004b). America’s market-driven economy leaves workers less secure, more unequal, and with a higher percentage of the population in poverty. An International Labor Organization index of ‘Economic Security’ ranked the US 25th out of 90 countries (Sweden ranked Number 1; ILO, 2004). The average Gini coefficient in 2000 was 30.8 for the entire OECD, 28.6 for the EU-15, and 36.7 for the US. The percentage of people in poverty – defined by the OECD as an income less than 50% of the median9 – is 17.1% compared to 10.1% for the OECD as a whole. (OECD, Society at a Glance, 2005b).

Nor might European economies be as bad off as at first glance. The redistributive ‘European social model’ provides the security and equality that Americans lack. Labor market regulations and shop-closing hours protect workers from putting in the long hours of their American counterparts. Indeed, workers in the US log about 350 more hours per year than their counterparts in France and Germany.10 Land use regulations inhibit urban sprawl while extensive and affordable public transportation staves off long and lonely commutes. Charming city center shopping districts have much on the often characterless American strip mall. Taking all of these ‘quality of life’ factors into account, a corrected comparison of US vs. European standards of living might eliminate about half of the gap in per capita GDP by one estimate (Gordon, 2004b). Economist Olivier Blanchard argues that Europeans have essentially made a choice to use some of the postwar productivity gains against the United States, drawing roughly even in output per hour by the mid-1990s, to increase leisure and long vacations rather than income (Blanchard, 2003).11 It is not Europeans who are producing too little, but Americans how are consuming too little leisure (“Mirror, Mirror…” 2004).

The question remains whether such qualifications are appropriate or, even if so, sufficient to substantially reduce or eliminate the considerable differences that the national aggregates show. All else being equal, higher per capita GDP leads to a higher material standard of living. American houses have, for example, roughly twice the square footage of European dwellings and are more likely to be stocked with major appliances like dishwashers and clothes dryers (Bergström and Gidehag, 2004, pp. 16-23). Equally, the level of poverty is mitigated to some extent by the prevalence of ‘luxury items’ among the poor. Approximately three quarters of those in poverty own a car, air conditioner, and a video or DVD player; 63% have cable or satellite television (Bergström and Gidehag, 2004, p. 22). That lower European per capita GDP reflects voluntary leisure (as output per hour remains higher or equal to the US) is a shaky proposition, as highlighted in a 2005 OECD report (OECD, 2005a). For one, only a few European countries (France and Norway) have substantially higher output per hour than the US. More importantly, the report attributes the gap in per capita income to a combination of ineffective labor utilization across states and lower labor productivity.12 Thus even if other

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9 Given a higher median per capita GDP, this means that the poverty line in the US is higher in real terms than other states.
10 This gap derives not from a rise in US hours, but from a sharp decrease in averaged hours worked per year by Europeans, a trend that has only emerged over the last two decades.
11 He also maintains that the continued erosion of European productivity stems from reforms in labor markets.
12 Labor utilization was defined in this report as the total number of hours worked divided by the population. Labor productivity was GDP per hour worked. The report also notes that countries with low labor utilization may not be employing many low productivity workers. Bring such workers back into the economy and increasing the number of hours worked would, in the short-term, decreases productivity relative to the United States. (OECD, p. 18)
countries achieved employment rates comparable to the US, gaps in the national aggregates would remain.

And a certain note of caution is warranted before incorporating subjective quality of life considerations into cross-national economic comparisons. It would be inappropriate, after all, to qualify the figures on one side of the ledger without similarly adjusting the other. So we cannot eliminate heating and cooling costs, as Gordon suggests, from America’s GDP figures without making similar adjustments to European and other countries accounts. (Moreover, anyone who has spent a summer south of the Mason-Dixon line would question the proposition that air conditioning is not ‘welfare enhancing’!) The bigger problem with bringing subjective criteria in is that they are, well, subjective. So while we may all agree that a growing national economy is generally better than a shrinking one, it is much harder to agree whether something like the spread of ‘big box’ retail stores is a social good or a social bad. Without some agreement on these points, a highly unlikely proposition, criteria for comparison becomes rather random and arbitrary. Moreover it is tough to quantify ‘quality of life’. It eminently plausible to maintain that Europe’s social model improves the standard of living in a way that does not show up in national aggregates, but we have no easy way to know how much of a difference this makes.

All of this leads back to the previous question: Are such qualifications sufficient to explain away the roughly 30% gap between American and European per capita GDP? Taking all the above into account, there is simply not sufficiently strong or tangible evidence to discount the *prima facie* case that the American economy, at least since around 1990, has outpaced most of her major competitors. The next question: Why? More to the point, why did this change occur when it did? To attempt to answer these questions, we must first turn to a discussion of globalization and models of capitalism.

**Globalization and Models of Capitalism**

Globalization is central to exploring almost any significant issue of international political or economic development in the early 21st century. At the same time, defining and debating this phenomenon has a mind-numbing quality – an endless argument over whether the glass is half empty or half full (in which, of course, everyone is at least somewhat right). Nevertheless, clarification is needed. A viable working definition is that “Globalization…denotes the expanding scale, growing magnitude, speeding up and deepening impact of transcontinental flows and patterns of social interaction” (Held and McGrew, 2003) While globalization touches on many different areas – political integration, state power, the spread of Western/American culture, the global distribution of wealth, business strategies, environmental degradation, security issues, etc. – the concern here is primarily with economic globalization. The economic side of globalization encompasses first the *internationalization of economic activity*, represented by large and growing flows of trade and capital between countries, producing increasing economic interdependence. These are facilitated by *technological changes* in terms of the exponential development of computer processing and information technology. New technology allows corporations to maximize efficiency and profits by adopting *globalized production structures* whereby elements of final products are made in the most economically beneficial locale and brought together in an integrated world production and marketing structure. Taken together these

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13 For some, Wal-Mart is an exemplary company that delivers value to the consumer and is a retailing market leader. To others it is a destroyer of small town businesses and an exploiter of workers (both at home and abroad) is thus portrayed by some in the US as just short of Satan and by others as the savior of the and a market leader.
represent a fundamental and significant transformation of the international economy which alters the challenges and opportunities faced by national economies.

Still, the underlying logic of capitalist economic development remains the same. Economic success is the result of the activity of firms buying and selling in order to maximize profits by establishing competitive advantages (Porter, 1990). The ability to achieve this is primarily a function of the relative productivity of the economy. This ‘old economy’ rule is still alive and well. What have been altered are the paths to productivity. The dominant stable technologies and pervasive Fordist mass production methods of the past have been superseded by the IT revolution, compressed product life cycles, and rapidly changing markets. The accelerated speed of change puts a premium on an innovative environment with a steady supply of new ideas and the ability to quickly redeploy resources (including labor) to more productive areas of endeavor. Yet deterritorialization and the intensification of international transactions means that corporations have a greater ability to exercise their ‘exit option’ and seek optimum locations for various stages of the production process (‘offshoring’). Companies or countries that are unable to adapt to changes in the global economy are likely to lose out as business moves to more productive locales. The transformations of the international economy bundled into the concept of globalization therefore favor national economic structures that are productive, innovative, and adaptive.

Which economies are likely to be best at dealing with globalization? The search for an answer leads to the ‘models of capitalism’ school (Representative texts include Berger and Dore, 1996; Hollingsworth and Boyer, 1997; Crouch and Streeck, 1997; Coates, 2000; and Hall and Soskice, 2000.) Capitalist economies are not uniform and interchangeable. Rather, markets are embedded in specific institutional, regulatory and social structures that shape national development. Actors in capitalist economies may face common problems – managing industrial relations, gaining access to finance, securing a properly trained workforce, dealing with suppliers and clients (Hall and Soskice, 2001, p. 7) – but they have developed diverse institutional means to resolve them. Thus the focus is on institutional cross-national variations in the organization of business and corporate governance, the structure of corporate finance, the patterns of labor relationships, the prevalence of corporatist interest intermediation, the pattern of human capital and labor skills formation, the role of the state in regulating economic interaction, etc. The core principles of the models of capitalism paradigm are thus (a) a belief in capitalism as a socially embedded construction; (b) that different capitalisms can be distinguished by their underlying institutional configurations; and, perhaps most importantly, (c) that these organizational differences are crucial in determining relative levels of economic performance (Phillips, 2004).

This school has not, unfortunately, settled on a categorization scheme. The primary breakdown is between Anglo-American (or neoliberal) states; state-led or ‘developmental’ models, as found in Japan and East Asia, but sometimes also including France; and social welfare or coordinated models common to Western Europe. Sometimes the framework is narrowed: Coates (2000) distinguishes only between liberal and ‘trust-based’ models, while Hall and Soskice (2001) note only liberal market economies’ (LMEs) and ‘coordinated market economies’ (CMEs), although the assumption is that all other states fall in between the two ends of this spectrum. Scholars have also gone in the other direction, creating separate models for almost every national system, implying a distinct ‘Swedish model’, ‘Japanese model’ and ‘Rhineland model’ (and begging the question of whether these can be described as ‘models’).

What is the purported influence of these different models in practice? Take, for example, the Hall and Soskice dichotomy between LMEs and CMEs. The United States is the prime
example of a liberal economy. Corporate finance focuses on the sale of equity shares, requiring managers to be attentive to current corporate earnings. Industrial relations are contractual and transient; managers can craft corporate strategy as they see fit. Education and training emphasize general, hence transferable, skills. Inter-firm networks are discouraged by the regulatory structure (i.e., antitrust). Innovations are treated as proprietary, allowing windfall profits to be reaped from new technologies, and putting a premium on being a ‘first mover’. Germany, in contrast is the epitome of a CME. Firms have access to ‘patient capital’ through major banks or other corporations. Such investments are monitored less through profit reports and more through insider information. Banks hold seats on the boards of directors and companies are linked through dense business networks. This allows the sharing of technological and organizational know-how. Corporate managers rarely have full freedom to shape corporate strategy as the structure of corporate governance and the dominant business ethos demands consensus decision-making, including labor. Industrial relations are governed by industry-wide coordinated bargaining, equalizing wages across skill-levels (generally at a high level), encouraging a committed and stable labor force. Training thus pushes industry or firm-specific skills.

A key point is that this is more than just a grab bag of policies. Rather it is an interconnected model that serves to produce *institutional complementarities*. A state’s economic institutions offer certain opportunities for companies and companies are likely to gravitate toward strategies that conform to the dominant modes of coordination within an economy, be they market or non-market. When cumulated across the entire economy these create certain *comparative institutional advantages* across these economies. CMEs thus excel in incremental innovations in existing products and processes, the markets for which are often driven more by quality than price (i.e., capital goods, machine tools, consumer durables). LMEs are stronger in radical innovations in fast-moving technology sectors where flexibility is crucial, not only in regards to labor, but also general management and investment decisions. In short, different models of capitalism have different strengths and, by emphasizing those strengths, they can continue to prosper without fundamentally altering their core institutional framework.

Contention arises when this is connected back to globalization. To what extent must national capitalisms adapt to the transformation of the global economy? One formulation suggests states operating in a global economy, driven by increased product competition and footloose capital, have no choice but to liberalize both their institutions and policies -- the so-called ‘convergence hypothesis’ (Ohmae, 1990; Friedman, 2000). The facts on the ground, however, belie such a conclusion. Despite a general trend toward reduced state control and greater liberalization, the economic structures found in North America, Western Europe, and East Asia still remain unique and distinct.

On the other side are those – many of which would fall into the models of capitalism school -- who see globalization as a contingent process, one that is mediated and interpreted through national economic arrangements. Far from forcing convergence on Anglo-American practice, coordinated economies may possess unique advantages in dealing with the rigors of globalization that will allow them to not only maintain their economic identity, but continue to prosper (Schmidt, 2002; Swank, 2002). Yet there are two problems with this approach, both interconnected. First, it has a ‘nationalist bias’, seeing nationally based social and economic structures as the primary determinant of economic outcomes and downplaying the influences of systemic forces. A deeper issue is what can be called a ‘reverse convergence hypothesis’

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14 Hall and Soskice (pp. 41-44) use patent data to show that this is not just theoretical speculation; indeed, the pattern of technological innovations for Germany and the US is that predicted by the CME/LME dichotomy.
problem. Going back to the seminal work of Andrew Shonfield (1965), the intellectual raison d’être of models of capitalism is not only to show that there are different forms of capitalism, but also to connect these to economic performance. If models are not connected to economic performance, then what is the point of such detailed study? In practice this literature has always found its voice in contrast to the liberal orthodoxy of mainstream economics. The basic message is that there is indeed an alternative to liberal market economies (Goodin, 2003) and, what is more, these alternatives often perform better than their liberal counterparts. Corporatist economies could best deal with the inflationary disruptions of the 1970s. Coordinated economic development, whether practiced in its Japanese or German variety, could best address the rising competitive pressures of the 1980s. In the 1990s, however, the relatively superior performance of corporatist and coordinated economies that underscored these arguments evaporated. More recent incarnations of models of capitalism, especially Hall and Soskice, argue that no model is inherently superior to the other: ‘…both liberal and coordinated market economies seem capable of providing satisfactory levels of long-run economic performance…’ (Hall and Soskice, 2001, p. 21).15 There are thus multiple paths to prosperity. This is what is meant by a ‘reverse convergence hypothesis’: that we will continue to find a diversity of capitalisms, but convergence in performance. Hall and Gingerich (2001) qualify the point by arguing that institutional coherence rather than any particular model was the key to economic growth, implying a U-shaped relationship between the level of economic coordination and growth. States that are neither clearly CMEs nor LMEs suffer should prosper. A follow up study by Kenworthy (2004), however, found not significant relationship, U-shaped or otherwise, between models and performance. Moreover, if institutional coherence were the key to prosperity, and Germany and the United States were the exemplars of the CME and LME formulation, then we would expect both to be thriving. Yet Germany remains stagnant. Nor does this argument, whether undiluted or qualified, address the question of changes in performance over time. Why is that coordinated model that worked so well for Germany in the 1970s and 1980s doing so poorly now? Why is the United States pulling back ahead?16

Such questions can be addressed if we think not only in terms of comparative institutional advantages, but also how globalization increases or decreases the relative costs and benefits of different institutional matrices; how does globalization alter the opportunity cost of the alternate models of capitalism. The argument here is not that the competitive advantages of coordinated market economies will disappear; they will still likely have a strong position in incremental innovation in established technology.17 The point is more that increasing global competition and a greater emphasis on rapid innovation and technological change will serve to produce increasing institutional returns for liberal market economies. To state the point conversely, a

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15 They differ in their social, not their economic costs, with the liberal model being more corrosive of the social fabric -- politically useful argument to maintain social democratic structures in the face of liberal insistence that they serve as a barrier to growth in an integrated world economy (Goodin, 2003).

16 One might retort that what we are seeing is just normal variations in the business cycle and macroeconomic policies across states. So we should expect different models to be up and down at different times. However, the trends since World War II do not show regular variation, but rather a sustained period of catch-up by more coordinated economies through the 1970s, followed by relative convergence in the late 1980s and early 1990s, followed by superior performance by more liberal economies since the mid-1990s.

17 This might be congruent if globalization produced more of a division of labor among major economies, with CMEs receiving those operations that benefit from their comparative institutional advantages. I would still maintain, however, that even under these circumstances they will face diminishing institutional returns as it limits the potential opportunities for growth. My thanks to Georg Menz of Goldsmiths College, University of London for making me aware of this angle.
globalizing world economy imposes rising opportunity costs for continuing to pursue coordinated strategies as opposed to market oriented policies. One might interpret this as a restatement of the convergence hypothesis, but it most assuredly is not, because it is acknowledged that globalization is filtered through domestic institutions which alter the national responses. Institutional complementarities remain that encourage actors to pursue the same strategies long after their relative efficiency has declined. (One need only examine the history of the British economy after World War II to understand this process.) Nor do I posit any predictions regarding domestic policy options. Indeed, this is a failing of both the convergence and diversity models – they each are primarily concerned with government economic policy. Here the concern is the likely economic outcomes produced by different institutional policy preferences. What is missing from existing accounts is a clear connection between models, globalization, and performance. What is missing is an understanding of the global complementarity of models of capitalism. To the extent that the structures of a model conform to broader structure of changes in the global economy, the opportunity costs of pursuing that type of capitalism will decline, leading to improved economic performance. Models that buck global trends pay a rising price for doing so, and this should be reflected in relatively poor performance. Although a thorough cross-national test of this hypothesis remains to be completed, a preliminary examination was supportive of the proposition (Casey, 2004). The next question is whether this can be used to explain America’s improved economic performance.

The Domestic Roots of American Economic Strength

As the US represents the archetypal liberal market political economy, its basic institutional framework is well understood ground and I will offer only a brief overview, focusing on the organization of capital, the organization of labor, the role of the state, and relevant cultural traits. From this brief review we can focus more intently on which factors serve to truly differentiate American economic performance from the other major economies. In broad terms, the American political economy is doing better as globalization advances in the international economy because it is ‘adaptively efficient’ in the meaning posed by Douglass North: possessing formal and informal institutions that provides incentives to accept and undertake risk and flexibly adapt to changing circumstances (North, 1990 and 2005).

The organization of capital relates to such aspects as the nature of corporate finance, inter-firm relations, and the relative concentration or segmentation of control. The most notable point for the US is a heavy reliance on equity financing. (Total capitalization of US stock markets as a percentage of GDP is thus almost twice that of Japan and three times that of the German economy.) This requires firms to be attentive to the bottom line of short-term profits and share prices of stocks. It also means that firms have a hands-off relationship with investors that rely instead on publicly available information to value the company. (There is in such a system a moral hazard of managers ‘cooking the books’ to run up stock prices, yet those that do so, as Bernie Ebbers of WorldCom is finding out, may find themselves a ‘guest of the state’ for many years to come.) Within this framework, mergers, acquisitions and hostile takeovers are deemed acceptable for companies facing declining share prices by regulators. At the same time, strong antitrust keeps firms formally segmented and markets competitive, and further serves to hinder the development of the sort of network relationships and close cooperation among firms

18 Phillips (2004) is an exception, although her concern is more on understanding processes of regional integration.

19 The section that follows is based on both Hall and Soskice and my own interpretation.
common to Japan and Germany. Formal contracting is more prominent, and technology transfer assured by licensing across companies, creating in itself an imperative to be the ‘first mover’ in a market. All told, this structure creates strong imperatives for constantly upgrading productivity, profitability, and innovation in response to rapidly changing markets.

Rather than being mediated through unions, labor relations in the US are largely direct market relations between employers and employees. The number of workers in labor unions has steadily declined since the 1950s, and, according to the US Census Bureau, now stands at only 12.9% for the workforce as a whole, dropping down to 8.2% for private sector workers, with the aggregate figure boosted by substantially higher unionization among public sector employees (37.2%). Labor relations in general can be described as conflictual, but the balance of power in that conflict clearly rests with management, which has substantial latitude to hire and fire workers in response to changes in demand and profitability; hence the regular spates of corporate downsizing. This lack of long-term commitment on the management side is equally met on the labor side, where workers, especially those with in demand skills, may jump from job to job seeking better opportunities. The labor market is flexible, but also volatile, and harsh to those lacking the training or ability to easily switch employment. Since employment relationships are fluid, there is little incentive for companies to invest in firm- or industry-specific training and skills. Thus both the vocational and general educational infrastructure stands separate from industry. Such a generically skilled workforce is better suited to the needs of service industries rather than manufacturing, facilitating the greater intensity of services in the US economy.

The role of the state in America also differs from other major economies, most notably on the substantially smaller segment of the economy that is funneled through state coffers compared to European economies. The government handles more than a third (35.9% for 2003) of the US economy, and despite the rhetorical turn from Keynesianism, fiscal policy is still used to stimulate the economy; note the Bush tax cuts. But this compares to 48.9% for the euro area, and 41.2% for the OECD as a whole. The only OECD nation with a lower share was South Korea. This has meant that direct interventions in the economy are less frequent and tend to occur more in response to special circumstances, such as the substantial subsidies offered to airlines post-9/11 (although defense spending has over the years served as something of a backhand industrial policy). At least since the Reagan Administration, governments have relied more on the indirect manipulation of the economy through monetary policy. There is, to be sure, a web of regulations governing the economy, but there are comparatively fewer, less intrusive, and more aimed at upholding market competition rather than supplanting it, especially when it comes to labor markets, than in other states. Quantitatively and qualitatively, the American government plays a lesser role in the economy.

If the story were stopped there, we would be left with a classic liberal explanation. America prospers because the corporate structure, highly competitive and reliant beholden to the stock markets on profits, forces companies to seek maximum efficiency in order to secure profits; that workers are generally rather than specifically trained and labor markets sufficiently flexible to allow managers to respond quickly to changes in market conditions, particularly in the service sector; and that a relatively unobtrusive state manages not to distort markets through excessive taxation or heavy handed regulation. In short, markets are allowed to achieve maximum efficiency, enhancing growth and national welfare. To a great degree, this

\footnote{Anecdotal but illustrative of this point is the recent ending of a strike at the Diamond Walnut Company plant in Stockton, CA, a strike which began on September 4, 1991.}

\footnote{This represents another means of technology transfer (Hall and Soskice, 2001, p. 31).}
characterization is correct. These above described traits do indeed serve to improve the economy’s productivity, innovativeness, and adaptability, and as such are certainly a major part of the answer as to why the country has done well as globalization has progressed. But this would still leave a rather incomplete picture. I would argue that it is the (economically) positive social and cultural milieu of the United States that combines with this liberal institutional framework to allow firms and individuals to adapt efficiently to globalization. If we think of institutions as the set of rules, both formal and informal, that guide actors’ behavior, and pose the point in the terminology of models of capitalism, the argument here is that the informal institutions of American culture create institutional complementarities with the organizations of the political economy that produce outcomes that are adaptively efficient in dealing with the challenges of globalization. The American model of capitalism thus manifests global complementarity.

This draws the analysis to questions of American culture. Despite the characterization of ‘American exceptionalism’, many of the sorts of institutions that Douglass North (1990 and 2005) argues distinguish prosperous from impoverished economies – stable governments, the rule of law, enforcement of contracts, free and deliberative democratic discourse, etc. – are common all developed democracies. It is all too easy, furthermore, to slip into hyperbolic rhetoric regarding ‘rugged individualism’ and ‘American ingenuity’. The point here is to focus concretely on those parts of American culture that are discernibly and measurably different from other states and that can be directly connected to economic performance. So what aspects of American culture are relevant to this point? Three seem relevant: an individualistic strain that manifests as a constrained egalitarianism; a strong belief in the potential for upward mobility as manifest in the idea of the ‘American Dream’; and, most important of all, a higher propensity for entrepreneurialism.

The divergence in support for individualist as opposed to collectivist values between the United States and other nations, particularly European polities, is well documented (see, for example, Wilson, 1998). Class identification has never been a major force in American economic or political life, hindering the development of a social democratic party. As the data in Table 2 indicates, Americans offer meager support for policies of economic redistribution or government guarantees of basic standards of living, and downright hostility to welfare programs intended to help the poor. It is easy, of course, to mischaracterize modern America as some sort of laissez faire state reminiscent of the Victorian era. For all the rhetoric of individualism, Americans still want plenty of things from their government. It is questionable whether President Bush will be able to sell his program for partially privatizing Social Security to a public that is loath to give up a guaranteed state pension for the riskier (albeit potentially more lucrative) returns of a personal account. Nevertheless, such programs tend to be posed in terms of individual benefits; the political market for social solidarity is small. Individualism thus erects bounds to the extent of welfare provision and this translates into an American state that provides far fewer direct services – most notably offering no national healthcare -- than any other major democracy.

The flipside of individualism is a belief in the potential for upward mobility encapsulated in the ideal of the ‘American Dream’. The conception of America as a ‘land of opportunity’ where anybody can make anything of his or herself to the maximum of their drive and abilities is deeply embedded in the American psyche, re-nourished from generation to generation by a steady flow of immigrants.22 (After all, one generally emigrates in order to better one’s status.)

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22 It is thus a sad irony that many conservative commentators who otherwise espouse the glories of American capitalism wish to clamp down on immigration.
Perhaps this is all just part of the American myth, but as the bottom of Table 2 shows, Americans truly believe that ‘myth’. Of course, there is a dark side to the American Dream. Failure to strive vigorously for improvement is taken as an indication of unacceptable laziness, which helps to explain the scant sympathy (or public money) Americans have for those who are economically or socially marginalized. It also makes for a more materialistic culture with a tendency to gauge worth by wealth. There are those who suggest, moreover, that while this ideal may have once been valid, the free market, tax cutting policies of recent administrations has torn it asunder (Krugman, 2004). Ultimately, however, the importance of a belief in the potential for upward mobility is not a function of its objective validity. It is a subjective belief which, if held by the bulk of the populace, may serve to produce growth enhancing behaviors. The survey data does not indicate that most think this dream has died.

Yet the crucial socio-cultural difference is that the United States continues to be a very entrepreneurial nation. Entrepreneurs are the central players to the Schumpeterian characterization of capitalism as ‘creative destruction’ (Formai, 2001) and there is little doubt that increased rates of entrepreneurship contribute to job creation and overall economic growth (European Commission, 2003, p. 6). Economies are engineered to perform to a certain level (i.e., poorly if lacking the requisite Northian institutions, such as stable property rights) and fueled by the inputs of labor, capital and technology. Entrepreneurialism may thus be thought of as the ‘fuel additive’ that keeps the American economic engine functioning at peak performance.

The empirical evidence of American entrepreneurial superiority is incontrovertible. Figure 6, which is drawn from the Global Entrepreneurial Monitor (GEM), an international research program directed by Babson College in the US and London Business School, shows that the level of ‘Total Entrepreneurial Activity’ (the percentage of the adult population engaged in entrepreneurial activity) for the United States is substantially higher than all of the other major economies (Minniti, et al., 2004). Rates are also higher for when it comes to entrepreneurial activity by firms – bringing new products and services to the market (Minniti, et al., 2004, p. 11). In a Eurobarometer study of entrepreneurialism in the EU and competitor countries, Europeans were less likely to desire to be self-employed, or to see this as viable possibility in the near future (Figure 7). Europeans also tend to see more obstacles in the way of starting a new business (Figure 8), particularly in terms of administrative barriers (4th question). But they also weigh the psychological costs of failure (2nd question) much more heavily. American entrepreneurs are also more likely to have started a business in order to seize a business opportunity (71%) compared to Europeans (55%). Twice as many Americans did so for reasons of necessity, i.e., lack of other employment possibilities (Eurobarometer, 2004, p. 36) The GEM study cited some standard factors of economic factors, such as easy access to physical infrastructure, to explain American performance, but noted that “…the most marked difference between the United States and the world average is the strength of US cultural and social norms…” (Minniti, et al., 2004, p.

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23 One might be puzzled by the even higher rates in some poorer countries. Business are started both out of desire to seize on a new opportunity or simply be your own boss, but in other instances out of necessity, because regular employment is in too short supply. Entrepreneurialism in the developed world leans more toward the former, while the latter motivation is more prevalent in LDCs. This is backed up by evidence in the GEM study on the motivation of American entrepreneurs (p. 11). One should not, therefore, assume from Figure 6 that Uganda is a vastly more entrepreneurial and dynamic economy than the United States!

24 Note that there is little difference on the issue of financial support, which belies the idea that the main American strength is a vibrant venture capital industry. The average investor, however, is more likely to get funds from informal investors (family, friends, and fellow entrepreneurs) than from institutional venture capitalists, who tend to focus on the ‘super star’ start-ups (Minniti et al., p. 27).
Entrepreneurialism is first and foremost a state of mind that blends risk-taking with creativity and innovation (European Commission, 2003, p. 6). More Americans have this state of mind than elsewhere.25

But a favorable mindset is not enough; one needs to be able to turn that propensity into growth enhancing action. This is where the United States’ liberal market economy comes back in. Europeans may be more risk averse not just because of personal proclivities, but also because higher taxes on the self-employed reduce the potential gains to be reaped from risky enterprises, or because of the greater financial and legal penalties for bankruptcy (European Commission, 2003, p. 12). America’s system bolsters entrepreneurialism by facilitating failure and encouraging another try. Institutions also affect entrepreneurs once they are established. An OECD study showed little difference in exit and entry rates for firms (so-called ‘churning’) across the Atlantic. US firms, however, tended to start smaller and expand employment much more quickly if they survive, indicating a greater potential for experimentation – the crux of creative destruction – followed by exploitation of successes among American businesses. This difference was attributed to heavy-handed labor market regulation that discourages European companies from hiring new workers. This also has a detrimental effect on productivity growth, particularly in industries with evolving technology (Scarpetta, et al., 2002). In other words, there is an institutional complementarity between America’s entrepreneurial culture and liberal labor markets. That this sort of cultural-regulatory complementarity may be systematic is suggested in Figure 9, which shows entrepreneurial activity rates against an OCED index of employment protection legislation. States with greater employment protection tend to have fewer entrepreneurs.

The above analysis shows that the United States is indeed a leading economy and that the domestic institutions highlighted by the models of capitalism literature are the foundation of that prosperity, although this analysis puts greater weight on cultural traits and how these interact with (complement) the formal institutions and regulation of the economy. The bigger point is that the relative benefit of this particular structure is improving with globalization. Globalization not only opens up wider range of opportunities and influences economic activity down to the level of individuals in society. Given their focus on macro and meso-level institutions, theories of models of capitalism miss this point. The real question is not how national institutions filter or mediate globalization, but how individuals in society react to it. What we see in the United States is a society more willing to respond directly to globalization and able to do so through a market-oriented political economy rather than seeking to mute the impact of global markets through political intervention. The problem for other economies is one of opportunities lost.

In sum, we see an American system that is productive, innovative, adaptive, and complementary to the global economy. This translates into declining opportunity costs for pursuing development along these lines which, in turn, leads to improved growth and productivity performance. This is why the US economy has outpaced many coordinated economies over the last decade.

Conclusions

The logical conclusion of this argument would be a generic endorsement of liberal market economies as optimal for a globalizing world. The US is the exemplar of this model and

25 Looking at the Eurobarometer data, the fundamental motivations and behaviors of Europeans who become entrepreneurs is little different from their American counterparts. There simply are fewer of them.
its economy is flourishing and looks likely to do so for some time. If we follow the models of capitalism logic, mimicry would be in order. And it is likely, as Robert Goodin (2003) has argued that given the time and effort required to build up the sort of trusting relationships required for a coordinated market economy, it is far more logic for those states that have not gravitated to either one of these models to choose to adopt liberalism – the transition costs are much lower. Given the idea of global complementarity espoused above, and the real material loses that can be incurred for economic configurations that are not ‘adaptively efficient’ (i.e., European labor markets), liberalization is indeed the best strategy for states to follow in response to globalization. But there's the rub. America ‘works’ because of its liberal institutions, but positive outcomes occur also because these institutions operate in an entrepreneurial milieu. It is not only that people can seize the opportunities of markets, it is that they will. Institutions can be exported; culture cannot. In other words, even if Europe removed all of the regulatory, legal, and tax impediments to entrepreneurialism, it is not clear that those countries would still match American levels. The United States is a liberal leader, but not necessarily one that others can easily follow.

A second point to note is the need to more clearly connect theories of models of capitalism with our understanding of the international economy. Phillips (2004) makes the point that we have created false and damaging division between CPE and IPE. The dominant authors of models of capitalism, grounded in historical institutionalism and path dependence, observe globalization, shrug their shoulders and say ‘same as it ever was’. Yet the relative performance of major economies has changed over time and this cannot be explained by largely static domestic institutions. The explanation must come from somewhere and exploring the connections between how models work in particular international contexts seems the most fruitful path to follow.

Following from this point is a challenge to future research, both my own and others. Fitting with the overall thrust of this paper, most of the major liberal market economies are, indeed, doing well while many of the major coordinated economies have been sluggish. But some more coordinate economies – the Netherlands, Finland – have also been doing quite well. Obviously national economies are driven by factors unique to each state, but this approach is premised on the idea that there are consistent patterns of variation across states both in institutional form and performance. Thus we are presented with a puzzle – and one not easily deciphered using existing conceptual lenses. This is no small point as it strikes at the underlying rationale and utility of a large body of literature, but it is a point that must be addressed if the models of capitalism approach is to continue as a dominant model in comparative political economy.
Sources:


Gordon, Robert J. (2004b) “Why was Europe left at the Station When America’s Productivity Locomotive Departed?” CEPR Working Paper.


Blackwell.


Table 1: G-7 Comparative Productivity, 2004

<table>
<thead>
<tr>
<th>GDP</th>
<th>Canada</th>
<th>France</th>
<th>Germany</th>
<th>Italy</th>
<th>Japan</th>
<th>U.K.</th>
<th>U.S.A</th>
</tr>
</thead>
<tbody>
<tr>
<td>per capita</td>
<td>78.8</td>
<td>75.1</td>
<td>70.3</td>
<td>69.7</td>
<td>76.2</td>
<td>78.1</td>
<td>100.0</td>
</tr>
<tr>
<td>per person employed</td>
<td>76.4</td>
<td>88.9</td>
<td>77.2</td>
<td>77.8</td>
<td>72.8</td>
<td>79.2</td>
<td>100.0</td>
</tr>
<tr>
<td>per hour worked</td>
<td>79.0</td>
<td>115.6</td>
<td>97.0</td>
<td>89.0</td>
<td>75.1</td>
<td>88.9</td>
<td>100.0</td>
</tr>
</tbody>
</table>

Change since 1995

<table>
<thead>
<tr>
<th>GDP</th>
<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td>per capita</td>
<td>0.3</td>
<td>-4.3</td>
<td>-7.9</td>
<td>-6.5</td>
<td>-6.9</td>
<td>0.6</td>
<td>0.0</td>
</tr>
<tr>
<td>per person employed</td>
<td>-6.2</td>
<td>-10.2</td>
<td>-7.0</td>
<td>-15.7</td>
<td>-3.3</td>
<td>-3.8</td>
<td>0.0</td>
</tr>
<tr>
<td>per hour worked</td>
<td>-6.3</td>
<td>-4.2</td>
<td>-5.9</td>
<td>-17.4</td>
<td>-1.0</td>
<td>-3.7</td>
<td>0.0</td>
</tr>
</tbody>
</table>

Source: Groningen Growth and Development Centre (GGDC) Total Economy Database.
<table>
<thead>
<tr>
<th>Limited support for egalitarianism….</th>
<th>Supporting statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government should reduce income differentials.</td>
<td>32.6%</td>
</tr>
<tr>
<td>Poverty because of lack of effort by the poor themselves.</td>
<td>91.4%*</td>
</tr>
</tbody>
</table>

...belief in upward mobility and the 'American Dream'.

<table>
<thead>
<tr>
<th>Supporting statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effort is rewarded in America.</td>
</tr>
<tr>
<td>Intelligence and skill is rewarded in America.</td>
</tr>
<tr>
<td>Private enterprise will solve America's problems.</td>
</tr>
<tr>
<td>Pride in American economic achievements.</td>
</tr>
</tbody>
</table>

Source: General Social Survey Cumulative Data File, 1972-2002
*% saying this was very or somewhat important
Figure 1: G-7 per capita GDP, 1960-2002

Source: OECD

*West Germany only through 1998.
Figure 2: G-7 per capita GDP at PPP, 2003

Source: OECD
Figure 3: Real GDP Growth, 1991-2004

Source: OECD
Figure 4: Standardized Unemployment Rates +/- US Rate, 1985-2003

Source: OECD
Figure 5: Employment Ratio*

Source: OECD

*Employment/population ages 15-64
Figure 6: Comparative Entrepreneurial Activity Rates, 2003

Source: Minniti, et al., Figure 1
Figure 7: US and EU Views on Self-Employment

...which would you prefer?

![Bar chart showing preferences for being an employee vs. being self-employed in EU-15 and US. EU-15: 51% for being an employee, 45% for being self-employed. US: 61% for being an employee, 34% for being self-employed.]

...self-employment feasible in the next 5 years?

![Bar chart showing feasibility of self-employment in the next 5 years in EU-15 and US. EU-15: 30% feasible, 68% unfeasible. US: 43% feasible, 54% unfeasible.]

Figure 8: US-EU Opinions on Difficulties in Starting a New Business

- It is difficult to obtain sufficient information on how to start a business
- One should not start a business if there is a risk that one might fail
- The current economic climate is not favorable for people who want to start their own business
- It is difficult to start one's own business due to the complex administrative procedures
- It is difficult to start one's own business due to lack of financial support

Source: Eurostat
Figure 9: Entrepreneurship and Employment Protection Legislation

Entrepreneurship data (TEA on left scale) from GEM, Employment Protection Index (right scale) from the OECD.
Source: GEM Global Entrepreneurship Monitor