

Program for the Study of Germany and Europe
Working Paper Series #2.3
Is Regulatory Convergence Efficient?*

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Abstract

One of the important themes in the new institutionalism is the convergence of market regulations in a world with three powerful clusters of countries (Western Europe, North America, and East Asia) on a small number of regimes, like disorganized capitalism, free market capitalism, and coordinated market capitalism. This paper examines the political-economic theory of regulatory convergence. It reconstructs and compares three welfarist approaches: the optimal regulatory regime (Tinbergen), the rule of constitutional law (Buchanan), and regulatory rivalry (Hayek). The paper concludes that most plausible results of convergence theory are completely opposite to the expressed political intentions of the theorists. Tinbergen's theory predicts neoliberalism, not social democracy. The theories of Buchanan and Hayek predict respectively a consensual or spontaneous formation of corporatist regulations, not the return of classical constitutionalism or liberalism. The paper summons new institutionalists to repair the weak scientific elements of convergence theory and to make a distinction between the ideological origins of this theory and its unintended ideological consequences.

*This paper was originally prepared for the panel "Deregulation and Efficiency?" in the CES Workshop "Deregulating the Economy," April 24-26, 1992. It was revised May 1992. For helpful comments I am grateful to Thomas Koelble and Fritz Soellner.

First draft; comments invited.

I. Introduction

All capitalist economies are regulated by law. Governments enforce certain rules that either facilitate or restrict freedom of exchange, freedom of competition, private property rights and dispersion of economic power. Since the 1970's, many OECD countries are going to a process of regulatory reform. The beginning of this process is clear. It is the deregulation movement that focussed on the social costs of restricting legal rules, the intrinsic burden of numerous and complicated rules, the retreat of the state apparatus and the return of private ordering, in particular in the financial markets, the market for public utilities (communication, transport) and the labour market. The outcome of regulatory reform is much less clear. There is considerable disagreement on the impact of deregulation; the phenomenon of re-regulation; the relation between market rules and economic development, macroeconomic coordination, organization of firms and wage bargaining; and the resemblances and differences of regulatory change in different sectors and countries.¹

This paper examines the last-mentioned topic. It has been argued that the OECD countries converge to disorganized capitalism, marked by autonomous and globally operating companies - separated from banks, fragmentation of the working class and trade-union power, limited intervention by nation-states and flexible specialization. The most important qualification of this hypothesis concerns the emerging dualism between deregulated market economies (the United States, the United Kingdom) and coordinated market economies (Germany, Japan, Sweden, Switzerland). In the second system, business is more collectively organized and transactions are based on relatively long-term and high-trust relations.² The idea of two regimes is often seen as a divergence claim.³ However, if one takes

¹ See, for example, on the contested relation between regulation and economic development Robert Wade (1990). Governing the Market. Princeton: University Press.

² See Scott Lash and John Urry (1987). The End of Organized Capitalism. Cambridge: Polity Press and the critique of their convergence hypothesis in David Soskice (1991), "The Institutional Infrastructure for International Competitiveness", in A.B. Atkinson and R. Brunetta (eds.), The Economics of the New Europe, London: MacMillan and Idem, Lectures on Western European Political Economies in the 1980s, Background Note, Center for European Studies, Harvard University, October 1991.

³ Cf. John H. Goldthorpe (1984), "The End of Convergence", in Idem, Order and Conflict in Contemporary Capitalism, Oxford: Clarendon Press and Michael J. Piore and Charles E. Sabel (1984). The Second Industrial Divide. New York:

a completely unpatterned differentiation of national regimes as the relevant benchmark, this idea boils down to a weakened convergence claim. Although it does not predict one specific regime, its prediction of a clustering of nations towards two regimes amounts to substantive integration. I will confine myself to the theoretical base of convergence claims and leave its empirical testing aside. I try to show that the concept of efficiency can be used to support different stories on the convergence of market rules.

Regulatory change may be conceived in terms of optimization of social welfare. This is the integral view of efficiency.⁴ It appeals to many institutionalists with a commitment to progress. The canonical case is the Marxian theory on the dynamics of productive relations. Productive relations like legal relations (e.g., rules for laying off workers) will change when and because they do not correspond with productive forces. Certain regulations fetter the use of resources (e.g., unemployment) or its development, especially the rate of technical development that is objectively possible. These regulations are unstable and will be replaced at some point. The time required for replacement is largely determined by the time required to solve problems of

Basic Books.

- ⁴ There is also a second view of efficiency in welfare economics. It argues that the concept of efficiency guides our assessment of the consequences of regulatory change, in particular its impact on the welfare of consumers. The concept may be an element of utilitarian ethics (Marshall, Pigou) or of professional economic analysis or counselling (Pareto, Bergson). But it certainly does not serve the purpose of explanation or prediction. Indeed, there is a gap between the analysis of factual aspects of regulation (what happened? why? what will possibly, probably and certainly happen?) and the analysis of its efficient and wasteful aspects. This view calls for a division between politics and historical trends on the one hand, and ethical economics and models for rational decisionmaking (marginal-cost pricing, etc.) on the other. See, for example, part 5 of Richard Schmalensee and Robert D. Willig (1989). Handbook of Industrial Organization. Vol. II. Amsterdam: North-Holland. Another example is Przeworski's demarcation between the social-democratic idea of an optimal economic regime and the transition of economic regimes in Eastern Europe and Latin America, which is anything but guided by collective optimization. See Adam Przeworski (1991). Democracy and the Market. Cambridge: University Press.

collective political action.⁵

It is impossible to discuss here all institutionalist approaches to converging rules, from Marx and Veblen to the French regulation school and other schools in the new institutionalism.⁶ I focus on three approaches which are quite under-exposed in the new institutionalist literature. These are:

- optimal economic regime (Tinbergen);
- constitutional contract (Buchanan);
- cultural evolution (Hayek).⁷

Tinbergian efficiency is the realization of the goals of economic policy. Tinbergen suggests that these goals are derived from certain fundamental aims like freedom and democracy. He refers to the following goals: economic growth, price stability, full employment, balance-of-payments equilibrium and a fair distribution of income and wealth. Tinbergen's convergence claim refers to

⁵ There is a strange resemblance between the historical materialist account of deregulation in analytical marxism and simple supply-side economics.

⁶ See Thorstein Veblen (1915). Imperial Germany and the Industrial Revolution. New Brunswick: Transaction Publishers, 1990, Stephen A. Marglin and Juliet B. Schor (1990). The Golden Age of Capitalism. Oxford: Clarendon and Robert Boyer (1989), "The Capital Labor Relations in OECD Countries", in Juliet B. Schor (ed.). Capital Labor Relations, forthcoming. See on new institutionalism James G. March and Johan P. Olson (1989). Rediscovering Institutions. New York: Free Press, Walter W. Powell and Paul J. Dimaggio (eds.) (1991). The New Institutionalism in Organizational Analysis. Chicago: University Press, and Sven Steinmo and Kathleen Thelen (eds.) (1992). The New Institutionalism. Cambridge: University Press. In a broad definition it includes rational-choice institutionalism, for instance, Douglas C. North (1990). Institutions, Institutional Change and Economic Performance. Cambridge: University Press and Elinor Ostrom (1990). Governing the Commons. Cambridge: University Press.

⁷ This distinction not only allows for a test for three authoritative research programs in economics, but also supports the test of three fundamental ideas about the capitalist state in political science: states pursue goals of their own, states respond to preferences of citizens, states act in the interest of those who own mobile productive wealth. See Adam Przeworski (1990). The State and the Economy under Capitalism. Chur: Harwood Academic Publishers.

efficient regulations in a social-democratic mixed economy. Buchanan's definition of efficiency is equally contingent. It is the realization of the unanimous constitutional preferences of social contractors. This is a specific interpretation of Pareto's conception of efficiency. Buchanan's convergence claim refers to efficient regulations in a neoliberal market economy, based on classical constitutionalism. Hayek's definition of efficiency is the expansion of the opportunity for welfare of any unknown citizen picked at random. He suggests two proxies, namely maximization of the size of the population and progress, that is, technological development, growth of scientific knowledge, growth of the national product per capita and a rising living standard of every citizen. Hayek's convergence claim refers to efficient regulations in a neoliberal market economy, based on classical liberalism.

I will argue that these original claims have to be reformulated in order to save the underlying theory. My reconstruction leads to results that are opposite to the expressed political intentions of the three theorists. The Tinbergian story may account for contemporary neoliberalism, while the stories of Buchanan and Hayek may explain the return of collectivist regulatory regimes!

The reconstruction leads to three testable hypotheses. First, centralized convergence can lead to a liberal regulatory regime if certain conditions in the Tinbergen model are fulfilled in any relevant pair of countries. They are a degree of insulation of the executive branch, a liberal content of the Ordnungspolitische Konzeption of the economic leadership, a mechanism of interaction between leaders, and the absence of strong divergent countertendencies (section II).

Second, regulation can be based on constitutional agreement and simulation of constitutional agreement (political consensus, corporatist compromise, administrative settlement). This may lead to regulatory convergence in a group of democratic countries. But this is unlikely, insofar as the (quasi-)constitutional path of convergence will be less simultaneous, less focused on narrow economic efficiency, slower, more oriented to domestic issues and, finally, more corporatist than the path of centralized convergence (section III).

Third, regulatory rivalry can result in corporatist regulation, instead of classical liberalism, the outcome that Hayek himself predicted. This depends on two variables, namely, the emergence of a leading nation with corporatist regulations (indicated by population growth, immigration, take-over in a wide sense and the status of role model), and the movement of regulatory imitation by countries that are trying to catch up (section IV).

The paper ends with some general remarks about the scientific and ideological status of the argument about efficient regulatory convergence. I summon new institutionalism to take positive

efficiency theory seriously (section V).

II. The Optimal Regulatory Regime

The idea of convergence on the optimal economic regime was invented by Jan Tinbergen (1959, 1961, 1964).⁸ He assumed that policymakers are insulated from society, in the sense that they can formulate and impose their own goals. The general goal of these policymakers is the maximal welfare of the present and future population of their nation. There is mutual reinforcement between the capacity of experts and technocratic benevolence. The optimal regime is market-based as far as outputs with decreasing returns to scale and without substantial externalities are concerned. It is state-based where there are increasing returns to scale (leading to monopolies) and substantial externalities. State control is at the lowest level of decisionmaking, owing to considerations with respect to the scope of welfare consequences and the costs of governance. The areas of state control are legal ordering, the supply of money, roads and education facilities, taxation, and income redistribution.

Tinbergen's convergence claim implies that capitalist countries in the West and communist countries in the East will move close to this intermediate and mixed regime, when and because political leadership will simultaneously promote state expansion in the West and market expansion in the East. The modified theory of the optimal economic regime brings in the international differences between the goals of economic policy. It takes the special goals of communist policymakers concerning merit goods and planning priorities into account. But it does stick to the prediction of convergence, albeit partial convergence.⁹

This convergence theory is clearly falsified in the 1980s by regulatory reform and other forms of state contraction in the West and the abolition of central planning in the East. Its logical structure has been forcefully criticised by eminent scholars like

⁸ Jan Tinbergen (1959), "The Theory of the Optimum Regime", in Idem, Selected Papers. Amsterdam: North Holland, Idem (1961), "Do Communist Economies and Free Economies Show a Converging Pattern?", Soviet Studies, 12, no.4 and Idem (1964). Central Planning. New Haven: Yale University Press.

⁹ J. van den Doel (1971), Konvergentie en Evolutie (Convergence and Evolution). Assen: Van Gorcum. Cf. Clark Kerr (1983). The Future of Industrial Societies. Cambridge: Harvard University Press, pp.13-16, 27.

Kornai and Ellman.¹⁰ It neglects the trade-off with respect to policy instrument choice, that is, regulation or something else: full state ownership, fiscal incentives, consultation, etc. Public-choice theorists ridicule its model of political behaviour as being unrealistic, methodologically unsound, and naive and frightfully socialist at the same time.

Despite all this, I think that the notion of convergence of 24 OECD countries on an optimal regulatory regime is not foolish.¹¹ Majone (1990) has recently described some striking examples of convergence in which European elites (political leaders, top civil servants, experts) imitate the best elements of foreign models, in particular the American model. He refers to the development of competition policy in the 1950s (like the German Kartellgesetz of 1957), the growth of European Community regulation (like the emission standards for auto's) and the impact of the American deregulation movement on the telecommunications policies of different European countries. In the Netherlands, the deregulation movement took off in the early 1980s when both conservative and liberal economists and legal scholars began to tell success stories about deregulation in the 1976-1981 period of Carter/Reagan. Majone points at the effective transformation of the Dutch PTT into a limited liability

¹⁰ Janos Kornai (1983), "Convergence Theory and Historical Reality", Society and Labour, 30 and Michael J. Ellman (1984). Collectivisation, Convergence and Capitalism. London: Academic Press, Chapter XVIII. See also Gérard Roland (1990), "Gorbachev and the Common European Home", Kyklos, 4.

¹¹ The focus on a group of rich countries is both conventional and plausible. See, for instance, on the convergence of macroeconomic performance William J. Baumol, Sue Anne Batey Blackman and Edward N. Wolff (1989), Productivity and American Leadership, Cambridge: MIT Press, pp.85-113 and Angus Maddison (1991), Dynamic Forces in Capitalist Development. New York: Oxford University Press, pp.128-166. If the gap between a pair of countries is too wide, neither supply-based convergence nor demand-based convergence will occur. This explains why catch-up theory (Veblen, Gerschenkron, Kuznets, Abramovitz) cannot explain endemic underdevelopment of certain countries. Baumol c.s. discover a convergence club that includes industrial, intermediate and centrally planned countries but excludes less developed countries. Cf. Mancur Olson (1992), "Why Are Differences in Per-Capita Income so Large and Persistent?", paper presented at the workshop on economic growth of the Harvard Department of Economics, April 8.

holding company.¹²

These stylized facts indicate the return of liberalism in regulatory policy. Can the theory of the optimal regulatory regime make sense of convergence towards neoliberalism? I think it can, provided that the following conditions are fulfilled in any relevant pair of countries.

The first condition is that insulation of the executive branch should be demonstrated and explained. The existence of insulation is illustrated by the White House oversight of deregulation during the Reagan administration.¹³ The account of such cases is driven by two questions. How frequently and to what extent are policy makers autonomous? What conditions promote autonomy in a democratic setting? Friedman refers to ignorance of the public: "The average person knows very little about efficiency in the economic sense, and, subjectively, does not feel that she or the polity suffer when manufacturers or suppliers are regulated closely".¹⁴ Public ignorance is probably more comprehensive and rational in the arcane areas of antitrust and capital market regulation than in visible areas of social regulation. Likewise, consumers' voice is more likely in the process of regulatory reform with respect to airlines, railroads, and telecommunications (in particular television) than with respect to trucks, natural gas and labour

¹² Giandomenico Majone (1990), "Cross-National Sources of Regulatory Policymaking in Europe and the United States", Journal of Public Policy, 11. Stephen Breyer suggests that the extent to which one can transfer American experience to communities with different institutional histories is still a matter for speculation. For Majone, however, it is a fact that European policy makers since 1945 were always free from intellectual doubt here: Giandomenico Majone (ed.) (1990), Deregulation or Re-regulation?. New York: St. Martin's Press, pp.5, 7. See also Breyer (1989)'s comments on "Francis McGowan and Paul Seabright, Deregulating European Airlines", Economic Policy, 9, pp.335-338, in which he points at differences concerning the before-deregulation state (regulation or nationalization, uniform service or special service for business and vacation travellers) and the after-deregulation state (the costs of new airport spaces and the existence of substitutes like trains).

¹³ Susan Rose-Ackerman (1992). Rethinking the Progressive Agenda. New York: Free Press, pp.151-153. In the CES workshop, David Soskice pointed at a similar connection between deregulation and centralization of government control in the United Kingdom.

¹⁴ Friedman, *Ibid.*, p.73.

markets. Public ignorance is only one condition for insulation. We need a list of conditions that are relevant to all OECD countries. The crucial condition concerns the insulation of government from producers' organizations.

The second condition is that the Ordnungspolitische Konzeptionen of policymakers from any pair of countries should be similar.¹⁵ Tinbergen introduced, sometimes unwittingly, a social-democratic conception of regulation. He also refers to humanistic socialism.¹⁶ It has become conventional in the comparative analysis of deregulation in the 1980s to construct a new liberal or new conservative consensus at the elite level as an independent variable. Research on the impact of policy ideas of agents, apart from or against their interests, is certainly fruitful.¹⁷ But, as to regulatory policy, a lot depends on the correct specification of the independent variable. Let me clarify this point.

There is a standard economic analysis that classifies market failure as rationale for intervention. It refers to externalities, limitation or promotion of competition, missing information markets, imperfect price information and asymmetric information about product quality.¹⁸ But there is no distinct theory that classifies political visions with respect to market failure. One example of such a vision is Ordo Liberalism, which was developed by German scholars like Böhm, Eucken, Müller-Armack and Röpke, and which contributed to the postwar development of the social market economy in Germany.¹⁹ In fact, there is an entire family of liberal conceptions of regulatory policy. The constitutive plurality between a social-democratic conception and a liberal one, does not imply that these conceptions themselves are all convertible.

¹⁵ This is Walter Eucken's canonical term.

¹⁶ Jan Tinbergen (1976). Reshaping the International Order. New York: E.P. Dutton, p.63.

¹⁷ See Robert B. Reich (ed.) (1988), The Power of Public Ideas. Cambridge: Harvard University Press and Peter Hall (ed.) (1989). The Political Power of Economic Ideas. Princeton: University Press.

¹⁸ See Michael Waterson (1988). Regulation of the Firm and Natural Monopoly. Oxford: Basil Blackwell, Schmalensee and Willig, *Ibid.*, and John Kay and John Vickers (1990), "Regulatory Reform", in Majone, *Ibid.*

¹⁹ In the CES workshop, Chris Allen, Jerry Riemer, Joel Trachtman, Norbert Walter and Nick Ziegler all referred to the impact of Ordo Liberalism on the German style of regulation and advocated a fresh analysis of its historical and present relevance.

Indeed, there is competitive plurality between classical liberalism, laissez-faire liberalism (the new learning), behavioural or pragmatic liberalism (fiscal incentives and market solutions), republican liberalism and social liberalism.

Hayek represents classical liberalism. In *The Constitution of Liberty* (1960) he draws a distinction between primary regulation on the rules of just conduct that is liberty-based, and secondary regulation on the rules of market conduct that is welfare-based. Secondary regulation of things like the provision of standardized information or food and the conditions of industrial labour is legitimate, provided that there are, respectively, a presumption of liberty (that is, compatibility with the rule of law, in particular primary regulation), substantive political considerations about the public interest, net public benefits, clear majority support, and priority of the softest and most libertarian intervention that is possible.

Laissez-faire liberalism is represented today by the new learning in industrial organization on the virtue of market concentration, the temporary nature of profits, the instability of barriers of entry that are not sanctioned by the state, and the importance of potential competition (contestable markets). Its implementation would imply the abolition and limitation of antitrust regulation.²⁰

Behavioral or pragmatic liberalism is very popular in environmental economics. A representative statement is Baumol (1991).²¹ He proposes the replacement of direct controls by fiscal incentives like emission charges and emission trading. Such incentives promote the social responsibility of businessmen and the adoption of the market mechanism for the realization of legitimate public goals.

Republican liberalism is reformulated in great length by Sunstein (1990). He goes beyond efficiency, in the sense that he sees autonomy as the ultimate end, along with welfare, and that he accepts two reasons for regulation next to the usual reason of interdependency problems of rational market agents. These reasons concern the protection of community goals and autonomous preferences. Republican regulation is the outcome of the meta-

²⁰ See K.D. George (1990), "Lessons from UK Merger policy", in Admiraal, *Ibid.*, pp.75-76 and, above all, Walter Adams and James W. Brock (1991), Antitrust Economics on Trial, Princeton: University Press.

²¹ William J. Baumol (1991). Perfect Markets and Easy Virtue. Cambridge (Ma.): Basil Blackwell. Cf. Tom Tietenberg (1991), "Economic Instruments for Environmental Regulation", in Dieter Helm (ed.). Economic Policy towards the Environment. Cambridge (Ma.): Basil Blackwell.

principles of political accountability and political deliberation; constitutional principles like federalism, priority of disadvantaged groups, and hearing-, property-, contract- and welfare rights; institutional concerns like judicial review and general taxation, and principles that counteract statutory failure, like proportionality.²²

The outlines of social liberalism are recently formulated by Rose-Ackerman (1992). She accepts Sunstein's focus on the contribution of courts to fully democratic regulation, but combines this with a focus on policy analysis by experts.²³

I infer from this brief survey that liberalism in general, with its characteristic features of an insulated and strong government and efficiency as an important goal or constraint, does not necessarily lead to convergence of regulations. The essential condition is similarity of specific liberal Ordnungspolitische Konzeptionen in a set of countries.²⁴

The third condition is that the mechanism of interaction between policymakers should be clarified. This is done by Colin Bennett, so a summary will suffice here.²⁵ Bennett identifies several important processes of convergence of policy goals, policy contents, policy instruments, policy outcomes or policy styles. The first is emulation, that is, that mode of diffusion of policy ideas that is based on the utilization of evidence about a foreign programme and a drawing of lessons from that experience. The second process is communication in elite networks and policy communities. The third

²² Cass R. Sunstein (1990). After the Rights Revolution. Cambridge: Harvard University Press.

²³ Rose-Ackerman, Ibid.

²⁴ The conceptual and empirical possibility of insulation of the state from the pressure of interest groups is questioned by recent work of Joshua Cohen and Joel Rogers (forthcoming). They develop a radical Ordnungspolitische Konzeption, called associative democracy. This is an alternative to both the Keynesian/social-democratic consensus and the liberal consensus.

²⁵ Colin J. Bennett (1991), "What is Policy Convergence and What Causes It?", British Journal of Political Science, 21, part 2. In the CES workshop, Michael Moran suggested that emulation is the outstanding mechanism of convergence in financial markets. He referred to the work of Susan Strange. A complete analysis of these mechanisms must account for the variable of geographical, historical and cultural proximity. Do policy-makers only learn from their neighbours, the last crisis and their friends?

is prior harmonization, pushed by the recognition of interdependence. The last process is penetration, that is, adaptation that is forced by the existence of participating external agents, like global authorities or companies. Penetration is least consistent with Tinbergen's requirement of insulation. The third condition explains why Tinbergen's original convergence claim presupposed the end of the Cold War. When there is no peaceful interaction, that is, when spies are hired and neoclassical economists are fired, mutual learning based on rational emulation, open communication and harmonization does not occur. Bennett gives many examples of regulatory emulation (e.g., the Swedish decision to adopt a standard for exposure to vinyl chloride gas by the US Occupational, Safety and Health Administration), regulatory communication (the aviation community), regulatory harmonization (chemicals and multinationals in the European Community) and regulatory pressure (the American telecommunications industry).

The last condition is that the relation between convergence and divergence should be explained. Any convergence claim should be falsifiable. Any counterclaim that is supposed to take us from observation of diversity to a negative judgement of convergence theory should be explicit and careful. This condition applies to all three approaches. And all these approaches may refer to three sources of diversity: diverse environments or initial states, diverse procedures of change (the so-called state dependencies) and diverse goals of collective agents. Indeed, Vickers (1991) has argued that all these sources were active in the British case of regulatory policy, namely, the size of the nationalized sector, the close connection between vigorous deregulation and competition promotion initiatives and the course and timing of privatization (in particular the assets of the public enterprises being sold) and the different goals of the Secretary of State for the relevant government department, the regulatory body in question and the Monopolies and Mergers Commission.²⁶

Any approach of (regulatory) convergence is (i) fully wrong if differences are stable or even increasing; (ii) partly wrong if its prediction merely fits a subset of the countries in the sample²⁷; (iii) incomplete if the predicted convergence occurs in tandem with unpredicted divergence, and (iv) not applicable if convergence occurs in areas beyond its range (say suburbanization). Tinbergen's approach is special for two reasons. In the first place, it excludes the possibility of goal variety within and between

²⁶ John Vickers (1991), "Government Regulatory Policy", Oxford Review of Economic Policy, 7, no.3.

²⁷ This distinction is overlooked in Goldthorpe (1984)'s justly famous prediction of two regimes, corporatism and dualism.

governmental organizations. If there is divergence, it has to be deduced from diverse cross-national circumstances and policy processes. In the second place, it predicts decreasing differences with respect to certain, well-specified elements of the economic order, for instance, power relations between state officials and natural monopolists. It does not try to explain all dimensions of industrial society (contents of knowledge, patterns of work and living, values), as Kerr does.²⁸

All this sounds very abstract. Consider, then, the following case. It has been argued that both Germany and the United Kingdom adopt negotiated compliance in the implementation and enforcement of regulations (bargaining between regulators and firms), instead of enforced compliance. As to environmental regulation, however, the Germans use general rules (principles, programma statements), explicit standards, and consultation, while the British use pragmatic policies, implicit standards, and discretion of governmental officials.²⁹ These statements yield a mixed score, which was to be expected. They imply that the theory of a unique regulatory regime is, respectively, generally right and precisely wrong. But perhaps this theory is partly wrong (if its predictions do not fit France or the United States), incomplete (if it does not predict divergent implementation of identical laws) or not applicable (if it does not take legal tradition into account). The comparative study of styles of regulation (Kelman, Vogel) is a new field full of promise. Here, clarity with respect to the critical role of divergence will be essential to a fair empirical assessment of the theory of convergent economic regulations.

My conclusion is that centralized convergence can result in a liberal set of regulations, instead of Tinbergian social democracy. This will be determined by four variables in any relevant pair of countries, namely, the degree of insulation of the executive branch, the liberal content of the Ordnungspolitische Konzeption of the economic leadership (policymakers), the mechanisms of interaction between leaders, and the absence of strong diverging countertendencies.

III. The Rule of Constitutional Law

James Buchanan draws an important distinction between collective action within law (postconstitutional politics) and collective

²⁸ Kerr, *Ibid.*, pp.47, 72, 85.

²⁹ The first statement is made in Alan Peacock (ed.) (1984). The Regulation Game. Oxford: Basil Blackwell. The second statement is made in Albert Weale (1990), "Can Homo Economicus Have a Political Theory?", Political Studies, 3.

action taken to change the law (constitutional politics). According to Buchanan's pessimistic thesis on the rise of Leviathan, regulatory policy in all liberal democracies is marked by several kinds of political failure. There is capture of regulatory laws and agencies by the producers, their associations or the coalitions in which they participate (with progressive politicians and consumers): "The familiar examples are political controls over (or interferences with) terms of potential voluntary exchanges of goods and services: controls over wages, prices, interest rates, rents, entry into and exit from occupations, industries and locations. In each case, the political controls are motivated by producer group interests, which seek to secure benefits (monopoly rents) at the expense of the citizenry generally".³⁰

Other kinds of political failure are the lack of policy information resulting in excessive or redundant reduction of outputs with negative externalities; fettering of private ordering (self-regulation) because of preference of the liability rule (compensation ex post) over the property rule (compensation ex ante) and overestimation of the negative effects of entrepreneurial projects in partisan and bureaucratic politics, the bureaucratic preference of regulation over fiscal incentives, and the peculiar operation of the majority rule. If the group of voters who are both buyers (voters who buy the industry's product) and sufferers (voters who consume the spillover damage generated by production) is bigger than the numerical difference between the group of voters who are pure buyers (no consumption of externality) and the group of pure sufferers (no buying of product), then the political majority may support regulation instead of taxation. This is the case when there is a coalition of the buyer-sufferers and the unaffected, who happen to have a collectivist ideology and use the voting booth to express ideology, since there is no financial stake as in the case of Pigovian taxation.³¹

In this quasi-Hobbesian state of accumulative, yet suboptimal regulation, rational and self-interested citizens will try to get the potential efficiency gains of regulatory reform by introducing or improving constitutional rules. Buchanan's explicit social contract (justice as democratic mutual advantage) is about constitutional judgement and decisionmaking. Constitutional rule is

³⁰ James M. Buchanan (1991). The Economics and the Ethics of Constitutional Order. Ann Arbor: University of Michigan Press, p.92. My italics.

³¹ See on the regulatory majority Buchanan, *Ibid.*, pp.67-79. Taxation will occur when there is a coalition between sufferers or buyers and the unaffected, who happen to benefit from the distribution of tax revenues. The political weight of the voters who represent the polluting companies is almost nil.

based upon the absence of extreme duress, freedom of exit (of both secession and migration), asymmetric freedom of entry (the obligation to join constitutional bargaining), uncertainty with respect to future personal interests and the rule of unanimity. It is Buchanan's positive and empirical statement that a Pareto optimal regulatory policy will generally not come about through day-to-day politics, that is, pressure and counterpressure of interest groups, competition between parties, logrolling within legislatures and bureaucratic politics. Such a policy must come about through a revolution with constitutional goals and means. It will probably lead to a smaller public sector and more self-regulation within civil society, This implies regulatory convergence, since Buchanan's approach is general. The explicit exception is Japan, which has two fundamental options: moral communitarianism or moral anarchy.³²

It is not hard to understand that this theory of the regulatory social contract is fundamentally flawed.³³ Buchanan suggests that all modern regulation till the 1970s can be reduced to producers' pressure, including trade union pressure. However, in many cases the majority for command-and-controls regulation was extraordinarily wide (public utilities) or it was minimal, in the sense that it had to overcome the resistance of producers (social regulation). The theory predicts that democratic coalitions will not bring about formal deregulation or will establish formal deregulation with no substantial impact. In both cases individual producers will stay outside these coalitions, in order to maintain protectionism by capture. There is some truth in this, in the sense that the libertarian dream of rapid dismembering of the regulatory state was not realized and that some unions, in particular American unions, opposed deregulation from the start and lost their battle.³⁴

³² James M. Buchanan (1986). Liberty, State and Market. New York: University Press, pp.117-118.

³³ Buchanan himself gives two explanations for the continued absence of his type of revolution. First, the winners may refuse to compensate the losers or to acknowledge their entitlements. Second, the winners may prefer a new majority coalition to the expensive process of unanimity-based bargaining: Buchanan (1992), *Ibid.*, p.103. The empirical standing of this account seems to be stronger than its normative standing.

³⁴ See Rose-Ackerman, *Ibid.*, p.149 for the first statement. There is a tension between the statement that deregulation was purely formal and futile, and the statement that it was a decisive break that could not be stopped by weak unions.

But the general picture is clearly wrong if we look at regulatory reform since the 1970's at both sides of the Atlantic. Formal deregulation was majority-based. It has major microeconomic consequences. It was supported by peak-associations of employers. And the opposition of trade unions was selective, often temporary and sometimes effective, in the sense that U.S. style deregulation was blocked.³⁵ Of course, one can argue that there is re-regulation or that we live in the regulatory stage of human history, indicated by the sheer number of statutory laws or the futility of conventions, moral principles and social norms in big, complex, and plural societies. This general argument is actually endorsed by Buchanan, but it is completely different argument which I will leave aside.³⁶

Finally, Buchanan gets stuck in something I call Lijphart's paradox. Lijphart makes a distinction between majoritarian democracy and consensus democracy. Majoritarian democracy differs from consensus democracy as to type of executive (oversized cabinets versus minimal winning ones), party system (multiparty versus two parties) and several other clustered variables. A majoritarian democracy goes together with a pluralist interest group system. A consensus democracy goes together with corporatism, that is, interest group concertation.³⁷ The deregulation movement was relatively more militant in majoritarian democracies like the United Kingdom and the United States, but in the first country there is no written and rigid constitution, and in the second country the first aim of the movement was to eliminate regulatory burdens and costs, not to rewrite the constitution. In consensus democracies like the Netherlands the deregulation movement was weaker. However, regulatory reform came about more gradually, based upon parliamentary consensus, corporatist consensus and the elite

³⁵ Lowell Turner (1992), "Industrial Relations and the Organization of Work in Germany", in Lawrence Mishel and Paula B. Voos (eds.). Unions and Economic Competitiveness. Armonk: M.E. Sharpe, p.239.

³⁶ See the evidence in David Vogel (1989). Fluctuating Fortunes. New York: Basic Books; Dennis Swann (1988). The Retreat of the State. New York: Harvester, pp.306-317, Majone (ed.), *Ibid.*; Jonathan R.T. Hughes (1991). The Governmental Habit Redux. Princeton: University Press, pp.198-199, 205-207; MacAvoy, *Ibid.*, and Itzhak Swary and Barry Topf (1992). Global Financial Deregulation. Cambridge (Ma.): Basil Blackwell.

³⁷ Arend Lijphart and Markus M.L. Crepaz (1991), "Corporatism and Consensus Democracy in Eighteen Countries", British Journal of Political Science, 21, part 2.

consensus on European integration.³⁸ Buchanan's theory cannot explain this, unless he redefines the notion of regulatory agreement.

This leads to the following revision of the idea of a regulatory social contract. Next to the Buchanan setting of foundational, hypothetical and constitutional contracting on regulation, there are three other democratic settings. The first setting is political consensus. Consensus is a combination of patterns of agreement in public opinion, voting behaviour of the mass electorate, party strategy (especially convergence of competing parties towards the position of the median voter) and voting behaviour of representatives in parliament. Perhaps the new liberal approach to deregulation in the 1980's was supported by such a consensus. This proposition can be tested with opinion data.³⁹

The second setting is corporatist compromise. This is a settlement between representative elites within separate social groups, e.g., capitalists and workers, and between these elites and the political elite that represents the state. The settlement may contain a formal, even written agreement on regulation, but the notion of compromise may also refer to a protracted informal process of Lijphartian accommodation. In other words, there may be a linkage between the second and the first setting.

Przeworski (1985, 1991) has written extensively about the contribution of class compromise to the transition from market capitalism to organized capitalism, and from totalitarianism and authoritarianism to democracy. The analogy between the last transition and regulatory reform is quite striking. The problem is the introduction of self-enforcing regulations, when all relevant agents have some minimum probability of doing well under the new regime. The crucial agents are the losing groups who have outside options, that is, options to subvert deregulation or provoke others to subvert it. They need guarantees. In the case of deregulation the losers are entrenched firms, parts of the civil service, and some trade unions. Their outside options are, respectively, capital flight, policy blockade, strikes, and, generally, noncompliance (the informal sector). Deregulation must lead to fair and effective markets and policies, in the sense that (i) all the relevant parties get a chance to win from time to time in the competition of interests and values, and (ii) losing under the new regulatory regime is more attractive than a future under the alternatives. Perhaps it can be shown that the most successful cases of

³⁸ Cf. K. Hellingmans and K.J.M. Mortelmans (1989). Economisch publiekrecht (Economic Public Law). Deventer: Gouda Quint, pp.50-51.

³⁹ Cf. Elim Papadakis (1992), "Public Opinion, Public Policy and the Welfare State", Political Studies, 40.

transition from command-and-controls regulation to liberal regulation in a broad sense fulfill Przeworski's condition: every major player must have a fair chance to win or must believe that losing will not be that bad.⁴⁰

The third setting is the administrative settlement. This is an agreement between the administration and the business community (firms, industries, employers' associations), based upon Goodin's (1986) principle of voluntary agreement, that is, policymaking by consultation, cooperation and noncommittal covenants.⁴¹ The administrative agreement is a form of soft public policy that promotes private ordering amongst producers. It is intended to preempt hard public policy (taxation, regulation). These agreements are now fashionable in the environmental policy of Germany and the Netherlands. Agreements are made between the Dutch Department of the Environment and certain business sectors on voluntary limitation of noxious production (spray cans) or the use of noxious materials (batteries).⁴² The general effectiveness of these agreements - the degree of cooperation of firms - is mixed. In the United States Alfred Kahn came very close to administrative agreement. He applied the method of consensual and learning-based regulation as chairman of the New York Public Service Commission and the Civil Aeronautics Board.⁴³

It is clear that we need more empirical evidence about the democratic politics of regulatory reform. The comparative literature on the crisis of the welfare state (taxation, public expenditure) appears to be more advanced than the comparative literature on the crisis of the regulatory state. My preliminary conclusion is that regulatory convergence based on certain social-contract procedures is not impossible. There is, after all, the historical example of convergence on constitutional human rights. There may be convergence in a group of democratic countries based on constitutional agreement or simulation of constitutional agreement (political consensus, corporatist compromise, administrative settlement). But it is unlikely, insofar as the path of (quasi-)constitutional convergence will differ from the path of

⁴⁰ Przeworski, *Ibid.*, p.33. This condition is a workable alternative to Buchanan's condition of unanimity, which gives special weight to the status quo.

⁴¹ Robert E. Goodin (1986), "The Principle of Voluntary Agreement". Public Administration, 64.

⁴² Jos de Beus (1991), "The Ecological Social Contract", in R.J. In 't Veld and D.J. Kraan (eds.), Environmental Protection. Boston: Kluwer, p.199.

⁴³ Thomas K. McGraw (1984). Prophets of Regulation. Cambridge: Harvard University Press, chapter 7.

centralized convergence on Tinbergen's optimum. It will be less simultaneous and less focused on economic efficiency in a narrow sense (non-distorted prices, etc.), slower (since there are large groups with blocking power involved), more oriented towards domestic issues, and, finally, more corporatist, in the sense that the relations between state and civil society are not marked by mutual insulation but regular exchange.

IV. Regulatory Rivalry

The basic idea of the old Hayek in Law Legislation and Liberty is that the most important rules of human conduct are not constructed by rational policymakers or social contractors but emerge spontaneously.⁴⁴ It is as if the nations do not pick winning rules, but the process of natural and social change picks the winning countries. In Hayek's framework international competition is entirely possible without synoptic collective rationality, in particular without competitiveness as a purpose of vested interests or as a genuinely public purpose.

Hayek's explanatory sketch of cultural evolution is a scheme with six stages: the original stage of tradition - the breakthrough by innovating minorities - the emergence of appropriate rules - the articulation of these rules - the stabilization - the new breakthrough. He starts with a given variation of traditional rules. Then there is the arrival of pattern-breakers, like Hirschman's raisers of the voice. They practise new forms of conduct, not because they understand them to be better but because the groups which act on them prosper more than others and grow. The breaks are introduced by small minorities and become established via gradual diffusion within the group. The mechanisms are individual imitation by other group members, intended or unintended; migration to other groups that are less repressive or conformistic; formation of new groups, or collective imitation by the group.

The next stage is selection of appropriate rules. The rules that remain correspond with the environment, guarantee group survival and increase the opportunity for personal success of all members. Then there is articulation, that is, the emergence of special rules for enforcing, interpreting and revising rules. One example is the differentiation between moral and legal rules. This stage is marked by conflict, leadership and the formation of group authority. At the next stage, one will observe the survival of ordered groups,

⁴⁴ Friedrich A. Hayek (1982). Law, Legislation and Liberty. London: Routledge. Hayek sees traditional rules (mindlessly repeating or imitating today what one's ancestors did yesteryear) in the middle between the broad base of instincts and the small top of regulations.

characterized by durability, peace and a dual (social and personal) orientation of group members. This relatively stable order is the best answer to rapid change of the environment. It becomes apparent in three ways: the growth of the ordered groups both internal (population growth) and external (immigration), the take-over of less successful groups, and/or the imitation of the order of the dominant group by the other groups.

Hayek applies this scheme on the history of the commercial society and the history of the rule of law. I will not summarize his conjectural history à la Adam Smith nor his behavioural theory of the liberal order. The main point here is a convergence claim about the open society with a classically liberal regime. Its features are:

- market rules: recognition of private property, enforcement of contractual obligations, competition with fellow craftsmen in the same trade, variability of initially customary prices, lending of money, particularly of interest, and, last but not least, autonomy of families and firms;
- the rule of law, in particular the protection of a private domain (negative liberty);
- the liberal state: separation between church and state, constitutional democracy, an independent judiciary that promotes common law, the provision of pure public goods by the executive branch, competition policy, etc.;
- the moral discipline of liberalism: private individual responsibility, egoism (or non-Tuism), economic rationality, prudence (private savings), belief in social progress, and the bourgeois work ethic.

Hayek claims that open societies with this specific regulatory regime will attain progress and, subsequently, hegemony. The indicators are, again, population growth, immigration, take-over (geo-political, military, commercial, technological), and the reputation of capitalism as a cultural role model. Divergence will exist, if (i) there is no acknowledged leader or hegemon, (ii) there are some nations which do not play the game of competition, and/or (iii) cultural evolution is completely internal, that is, within closed national communities. It goes without saying that the American hegemony from the 1940s till the 1980s, the collapse of communism, and the collapse of the GDR with a vengeance, fit smoothly into Hayek's scheme. Indeed, he foresaw the instability of inefficient and unfree nations, not in the second half of 1989 but already in the interwar debate on socialist calculation and the cold-war debate on the compatibility of liberal democracy and state intervention.

Again, it is easy to point at some deep flaws. First, there is Elster's argument that evolution can only attain local maxima and not global maxima, since it does not promote synoptic rationality,

in particular waiting- and investment behaviour.⁴⁵ Second, there is a clear inconsistency between Hayek's Austrian theory of cultural evolution and the Austrian methodology of methodological individualism, the feedback mechanism of the invisible hand (the absence of prudence, rationality and central planning), the decisive and expanding role of liberty (not coercive group discipline), and falsifiability.⁴⁶

Third, Hayek is ambiguous about the analogy between the capitalist firm and the society. On the hand, he avoids the rationalist, nationalist, communitarian and quasi-Leninist idea of society as a large-scale firm. This includes the most recent variant which endorses competitiveness as the overarching purpose, specified as the nation's ability to be the home base for successfully globally competitive companies (Porter), to achieve high factor incomes when exposed to international market forces (Pfaller) or to be the habitat of citizens within a nation-state who live well and improve their quality of life, now and in the future (Reich).⁴⁷

On the other hand, Hayek forgets to bring in the legitimacy of the classical liberal conception of the public purpose, he underestimates the public understanding of positive consequences of cultural evolution and sustained competition (which is minimally necessary to make his system work), and he neglects that the decline of nations is much more indeterminate than the decline of companies in a market economy.⁴⁸ Winning nations may face stagnation of population growth, they may not be inclined to take over other nations (but cooperate with them), and they may imitate the rules of laggard nations. Losing nations may survive and even be politically stable during protracted periods. Albert has argued

⁴⁵ Elster's second argument is that social environments change must faster than natural environments, which makes even the best evolutionary regime fragile (the Roman catholic church comes to mind here). This argument applies to all theories on institutional change, including all convergence claims.

⁴⁶ This critical claim is spelled out in J.W. de Beus (1989). Markt, democratie en vrijheid (Market, Democracy and Freedom). Zwolle: Tjeenk Willink, chapter VI.

⁴⁷ Michael E. Porter (1990). The Competitive Advantage of Nations. New York: Free press, p.19, Alfred Pfaller, Ian Gough and Göran Therborn (1991). Can the Welfare State Compete?. London: MacMillan, p.6; Robert B. Reich (1992). The Work of Nations. New York: Vintage, p.244.

⁴⁸ See on the Hayekian decline of firms Alexis Jacquemin (1987). The New Industrial Organization. Cambridge: MIT Press, chapter 6.

that the American model is economically and socially inferior to the Rhineland model. Still, the American model is expanding, which is indicated by open self-enrichment, an unraveling consensus, individualization, decline of union density and deregulation in the Western European countries that represent Rhineland. Albert refers to cultural causes, such as popular hedonism, the reputation of the US in the mass media, the force of the American dream among the mobile people in poor countries and failing foresight of citizens (short-run private welfare). Such arguments about cross-cutting economic and cultural trends make no sense in Hayek's model.⁴⁹

Lastly, Hayek does not have a convincing explanation of the survival, success or superiority of capitalist countries with welfare statist and corporatist regimes. How did they manage to catch up and even surpass the American leader? His political assessment is that these regimes demonstrate the involution of European (indeed Victorian) civilization, just like communism does. The underlying model, however, allows for another analysis. The reform of classical liberalism in the Nordic countries and Western Europe may have been a stable evolutionary strategy in entirely new circumstances. In other words, it is quite possible to accept Hayek's evolution theory but to question his political specification of the convergence claim at the present cultural stage.

I am prepared to take this last argument even further. There is a scientific reason to take Hayek's framework seriously. The contemporary Bostonian literature on global competition is constructivist. Take a closer look at the proposals of Porter, Kuttner, Reich and Thurow.⁵⁰ The first economist discusses the best strategy of companies and governments with respect to domestic factor and demand conditions and the value chain structure of related and supporting industries. Porter proposes, inter alia, the abolition of product liability and regulation of competition (constrained entry and pricing) and the enforcement of standards for product performance, product safety and environmental impact of products. The latter rules are a competitive advantage, since they pressure firms to improve quality, upgrade technology and cater for

⁴⁹ Michel Albert (1991). Capitalisme contre Capitalisme. Paris: Seuil. I do not endorse Albert's full argument, however. The prediction of American cultural hegemony without economic and social foundations is sloppy.

⁵⁰ See Porter, *Ibid.*, Robert Kuttner (1991). The End of Laissez-Faire. Philadelphia: University of Pennsylvania Press, Reich, *Ibid.*, and Lester Thurow (1992). Head to Head. New York: William Morrow. Many proposals are America-oriented.

the desires of a growing group of sophisticated consumers.⁵¹

Kuttner suggest measures to promote global regulation, managed and reciprocity-based trade, the relative level of schooling, the foresight of parties in the capital market, public investment (technology), the reversal of deregulation, health insurance and private savings.⁵² Reich's positive economic nationalism is a way to join the global web of high-value enterprises. It contains progressive income taxation, public infrastructural investment, education and on-the-job training: everybody should have the opportunity to become a symbolic analyst instead of a routine worker or an in-person servant. Thurow's head-to-head competition between Europe, Japan and the United States is about leadership in seven key sectors: microelectronics, biotechnology, the new materials-science industries, telecommunications, civilian aviation, robotics plus machine tools, and computers plus software.

All these authors share the view that global competition is determined by strategically rational collective actors. They support Porter's argument about governmental policy, e.g., regulatory policy, as a crucial variable that influences the determinants of competitiveness (irrespective of definition). It is true that Porter refers to chance as a second variable, but he does not develop a theoretical and detailed account of spontaneous regulation. Here, Hayek's theory may be helpful, since he focuses on the spontaneous nature of regulatory competition and observes rule-guided behaviour instead of fully rational behaviour, without denying critical historical junctures of collective imitation and rule articulation, like the American Constitution.⁵³

I do not think that some such account is redundant. Many American institutionalists dream about the American adoption of European industrial relations (mesocorporatism).⁵⁴ But they do not explain

⁵¹ Porter, *Ibid.*, pp.378, 585-586, 598, 647-649, 664.

⁵² See Kuttner, *Ibid.*, chapter eight and Idem, "Facing Up to Industrial Policy", New York Times Magazine, April 19 1992. Kuttner brings in a new view on the global benefits of managed trade (Krugman, Dixit, and others). As to Kuttner's politics, however, Krugman keeps his distance: Paul Krugman (1992). The Age of Diminished Expectations. Cambridge: MIT Press, p.111.

⁵³ Friedrich A. Hayek (1960). The Constitution of Liberty. London: Routledge, p.184.

⁵⁴ See, for example, Kuttner (1991), *Ibid.*, pp.281-284 and Mishel and Voos, *Ibid.* In the CES workshop, Kuttner mentioned a number of American employers's associations that favor imitation of the European (German) model.

this reversal in the pattern of regulatory convergence in which Europe, and not the United States or Japan, plays the dual part of the leader and the role model, except for the time-worn argument about the rise of a new New Deal coalition between enlightened corporate leaders, trade unionists, and liberal politicians and intellectuals. They also forget Hayek's uncomfortable lesson about the essential by-product nature of certain social states. The union practices in the leading European economies were not constructed with the explicit and official intention to realize competitiveness and efficiency. They were often second-best from the viewpoint of labour (social policy, industrial democracy, macrocorporatism), and the discovery of their positive economic impact came much later. In short, we need to spell out the Hayekian hypothesis of regulatory rivalry or race at a global level.

This is done by Siebert.⁵⁵ He suggests a generalization of the Cassis-de-Dyon ruling of the European Court of Justice. A product legally brought to market in one country of the European Community can automatically enter the market of other countries. Thus, in the trade of products it is not the regulation of the country of destination, but that of the country of origin that applies. This rule facilitates arbitration of firms and households in the single European market, that is, taking advantage of any differential like tax, price, location and regulation differences.

If there are mobile factors of production (capital, skilled labour, basic knowledge) and if these factors are scarce, the immobile factors (land, unskilled labour, policy, taxes, wages, etc.) will as it were compete for the mobile factors. This is institutional competition. Immobile factors, including the regulatory setting, determine the price of the mobile factors before arbitration takes place and thus influence the attractiveness of a region or nation. After arbitrage, prices for mobile factors should be equal. The arbitrage of consumers and companies "voting" with their purses and feet, will give governments a strong incentive to adjust regulations. It will clearly reveal which national regulatory system is best in the eyes of the market agents. Accordingly, there will be pressure on national regulations to converge over time.

Siebert applies this hypothesis to the European case of harmonization of different national legal systems. As long as the users of governmental services are identical to the taxpayer-voters, there will eventually be no zero regulation ("dumping". "lowest common denominator") but optimal regulation, determined by the willingness to pay of the average unit. Siebert hopes that this optimal regime will be a neoliberal mixture of federalism, global arrangements with respect to global problems (monetary stability,

⁵⁵ Horst Siebert (1991). The New Economic Landscape in Europe. Cambridge (Ma.): Basil Blackwell. Siebert also refers to Tiebout's work on fiscal decentralization.

sustainable environment), common law and liberalization of sectors like banks, insurance, road freight, airlines, electricity, postal and telecommunication services and public procurement.⁵⁶

But here the consistent adherents of corporatism may enter and twist the model of institutional competition. Let's assume that their behavioural theory of corporatist bargaining is correct and that their empirical results concerning the superior macroeconomic and microeconomic performance of this regime (high growth, low unemployment and inflation, industrial peace, competitiveness, etc.) are robust, in the sense that they also hold under the current condition of fierce competition in open international markets. Then regulatory rivalry within and between the three blocks Europe, East Asia and Northern America will lead to convergence on corporatist regulations with respect to business finance, wage bargaining, and education and learning, and so on. Certain American and British firms will change their regulatory routines (since they observe that they are not profitable). They will try out Japanese, Swedish or German routines. The corporatist regulations are selected through the Hayekian mechanism of bankruptcy for some, growth for others, and emulation of expanding firms. There will be a system-wide ratification of such regulation at the governmental level, but not as a first mover but as a closure of the new regime that solves certain inconsistencies. In short, it is possible that regulatory rivalry crowds out neoliberalism and picks neocorporatism.⁵⁷

My conclusion is that regulatory rivalry can result in convergence on corporatist regulation, instead of Hayekian liberalism. This depends on two variables, namely, the emergence of a leading nation with this regime and the movement of regulatory imitation by countries that are trying to catch up.

⁵⁶ A concise survey of deregulation in the European Community is Loukas Tsoukalis (1991). The New European Economy. Oxford: Clarendon Press, chapter 5.

⁵⁷ There is no space here to specify this argument. One of the difficulties is the Calmfors-Driffil (1988) result on the optimality of centralized and decentralized wage bargaining. See David Soskice (1990), "Wage Determination", Oxford Review of Economic Policy, 6, no.4. Another difficulty is the timing of governmental solutions to interdependency problems: John R. Bowman (1989). Capitalist Collective Action. Cambridge: University Press and Mark S. Mizuchi (1992). The Structure of Corporate Political Action. Cambridge: Harvard University Press.

VI. Conclusion

I will not try to summarize the main points of the paper, but I will make a few general concluding remarks to put the discussion in perspective.

After Berlin and Popper, many have argued that grand scientific theory of the dynamics of economic order is swindle. They point at the inability of the academic community to predict the timing of large-scale change, like the limitation of welfare state expansion, the decentralization and return of managers' power in corporatist industrial relations, the rise and fall of Euroclerosis or the collapse of communism. They invoke Elster's theorem: it is impossible to predict the long-term, global and net equilibrium consequences of any large-scale change of any economic order.⁵⁸ And they leave us with three options: speculation, abdication of predictive power, or general prediction as a test of theoretical propositions. These are rather poor options, since dinner-talk is seldom supreme (which was Lionel Robbins's word of praise for Schumpeter's *Capitalism, Socialism, and Democracy*). Ranke's "nur zeigen wie es eigentlich gewesen" does not fit the ambition of political economy and the so-called global or conditional prediction is completely Popperian in spirit, yet often without strong behavioural foundations.

This methodological detour is particularly relevant to efficiency-based arguments. First, efficiency may be the first virtue of the regulatory state, on a par with equality as the first virtue of the welfare state. But it is a criterion that is marked by plurality, as Amartya Sen time and again has shown. There are alternative conceptions and different aspects within these conceptions. Do we mean opulence (Smith), allocative efficiency (Pareto), counterfactual compensation of losers (Kaldor-Hicks-Scitovsky), the national dividend or aggregate monetary welfare (Pigou), dynamic efficiency or innovation of tools (Schumpeter), the goals of economic policy (Bergson-Samuelson), motivational efficiency (Leibenstein), productive wealth (Coase-Posner), or consumers' sovereignty (Hutt)?

Furthermore, there is a well-known distinction between fundamental market regulation (protection of free enterprise by the principles of property, tort and contract), regulation of industrial relations (protection of labour, especially the bargaining power and social security of workers) and social regulation (protection of citizens, e.g., against occupational unsafety, pollution and discrimination). These are three consecutive generations of regulations. Which

⁵⁸ See on this theorem Jos de Beus, "Applying First World Economy to the Second World's March into Civil Society", in J. van den Broeck and D. van den Bulcke (eds.) (1992). Changing Economic Order. Groningen: Wolters-Noordhoff.

interpretation of efficiency makes sense in the explanation of which generation of regulations?

Secondly, the reduction of regulations and other rules of conduct, like social norms, moral or religious principles and conventions, to collective rationality often breaks down. Elster focuses on social norms and argues that (i) some actual norms make everybody worse off, or at the very least, they do not make almost everybody better off (e.g., American norms with respect to work, consumption and compensation of chief executives), (ii) some norms that would make everybody better off are not in fact observed (e.g., a norm with respect to standing in line in a densely populated country like the Netherlands), and (iii) explanations of Pareto-efficient norms in the real world are inadequate, unless the feedback mechanism is shown that specifies how the good - indeed first-best - consequences of the norm contribute to its maintenance.⁵⁹

Elster's message resembles the message of De Jong, an expert on industrial organization. He infers from the cycle of mergers and cartels in the oil industry since 1872 that the argument of firm efficiency, regarding economies of scale and scope, internalization of activities with high transaction costs or concentration of tasks in the hand of the ablest managers, cannot explain why presumably efficient mergers did not take place in the 1930s and 1950s, and why generally 55-60 % of the mergers are failures or unprofitable.⁶⁰ So the question remains: which theory explains the combination of efficient and inefficient regulations in the real world?

Thirdly, the institutionalists' vice is the overestimation of the weight of regulations. For example, Olson has argued that a dense network of interest groups that act like distributive coalitions increases the complexity of regulation and promotes political competition at the cost of market competition in a broad Schumpeterian sense. The impact of these practices on the relative

⁵⁹ Jon Elster (1989). The Cement of Society. Cambridge: University Press, pp.139-140. The best answer to Elster is, of course, a focus in the study of social movements and political coalitions on uncertainty, conservatism, trade-offs, transaction costs, leadership as the manipulation of beliefs based on counterfactuals (like Pareto's efficiency), interdependency problems (with respect to coordination, cooperation, bargaining and fair distribution) and problems of organization and implementation.

⁶⁰ H.W. de Jong (1990), "Mergers and Competition Policies", in: P.H. Admiraal (ed.), Merger and Competition Policy in the European Community, Cambridge (Ma.): Basil Blackwell, pp.51, 52, 58.

economic growth in a country - a proxy of efficiency - is indirect and negative.⁶¹ Yet Maddison (1987) could not find substantial evidence concerning the relation between social regulation and slowdown. He estimated a reduction of American output of 0.04 % in the period 1950-1973 and of 0.16 % in the period 1973-1984. The negative impact of social regulation in Japan, France, Germany, the United Kingdom and the Netherlands was even less: Maddison's estimates are half of these percentages.⁶² The MIT commission on Industrial Productivity (1989) concluded that the very idea that the American economy on the whole, and especially the international competitiveness of American industry, has been adversely affected by regulation is not strongly supported by empirical evidence. Environmental, health, and safety regulations in the 1970s were responsible for no more than 10 to 15 percent of the productivity slowdown during those years.⁶³

Everybody agrees that regulations matter. But the real issue is: how do we identify the size of the regulated sectors, the connection between legal rules and non-legal ones, the public benefits and costs of distinct types of regulatory practices in different countries, and, of course, (since similar practices cannot explain different efficiency rates) the differences between these practices?⁶⁴

I have tried to show that the original convergence claims of

⁶¹ Mancur Olson (1982). The Rise and Decline of Nations. New Haven: Yale University Press, pp.69-73.

⁶² Angus Maddison (1987), "Growth and Slowdown in Advanced Capitalist Economies", Journal of Economic Literature, 25, p.673. Maddison thinks the United States are special for the size of the legal profession, the tradition of litigation and the adversary relations between business and government. His judgement is too general, since there was in 1988 1 lawyer per 1500 residents in Germany but 1 per 2400 in the Netherlands (and 1 per 350 in the US) and since there may be convergence here on the leader: see Lawrence M. Friedman (1990), The Republic of Choice. Cambridge: Harvard University Press, pp.13-15.

⁶³ Michel L. Dertouzos, Richard K. Lester and Robert M. Solow (1989). Made in America. New York: Harper Perennial, p.110.

⁶⁴ MacAvoy adopts a precise conception of the regulated sector and finds that American regulation contributes to an annual loss of GNP between 1.5 and 2 %. See Paul W. MacAvoy (1992). Industrial Regulation and the Performance of the American Economy. New York: W.W. Norton, pp.18, 108.

Tinbergen, Buchanan and Hayek display certain shortcomings. The paper offers some reconstruction of these claims. Further research is needed in order to determine which theoretical approach provides the best answer to the major questions mentioned above. The reconstructed convergence claims by themselves are strong, in the sense that they are all based on rather stringent conditions. Still, I invite new institutionalists to take the scientific idea of optimization of social welfare seriously. It points at three important underlying forces of regulatory change: cooperative leadership in economic policy, democratic deliberation and action with respect to the market domain, and the invisible and surprisingly positive consequences of institutional competition.

There is a tendency to reject efficiency theory because of its ideological reputation. However, I draw a distinction between the expressed ideological meaning of a model and its scientific use. The present state of regulatory reform is turbulent and chaotic. It is often said that in this state, the optimistic nineteenth-century vision of democratic or humanistic socialism is aging faster than the pessimistic eighteenth-century vision of constitutional liberalism. Yet even a cursory examination of the underlying analytical models gives a more complex result. If the model of Tinbergen is realistic, regulations may come closer to the neoliberal vision. But if the models of Buchanan and Hayek are realistic, regulations may come closer to the neocorporatist vision. New institutionalists are prone to prefer neocorporatism to neoliberalism and Tinbergens's constructivism to the traditionalisms of Buchanan and Hayek. There is, then, no escape from an old puzzle: what is the best fit between sensible progressive vision and plausible analytical model?

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