



Playing Games of Right and Wrong about Capitalism

Book review of *Democracy and Prosperity; Reinventing Capitalism through a Turbulent Century* by David Iversen and David Soskice

By Francisca Wals

To say that it doesn't happen often that an academic book of biblical proportions ends up at the top of mainstream book charts, would be an understatement. Yet in early 2014, it happened to the work of a young, until then quite unknown, French economist: Thomas Piketty. In his nearly 600-page *Capital in the Twenty-First Century* Piketty defends his thesis that capital undermines the welfare state. He does so by arguing that an ever increasing concentration of mobile capital in the hands of a few, combined with fiscal competition between countries, will lead to "a total disappearance of taxes on capital"—and thus to a dramatic reduction in the redistribution of welfare. This hellfire and brimstone message turned out to have an intuitive appeal to many. Millions of copies of his version of *Das Kapital* were sold worldwide and Piketty was awarded with the status of an intellectual rock star.

But whoever thought Piketty was right, is wrong. At least, that is what political economists Torben Iversen and David Soskice argue in their book *Democracy and Prosperity; Reinventing Capitalism through a Turbulent Century* (2019). Their main argument for this rather bold claim is that Piketty fails to account for the remarkable resilience of advanced capitalist democracies throughout, what the authors call, "the arguably most turbulent century of human history". That is, after becoming an advanced capitalist democracy, none of the countries to which this predicate applies has reverted back to authoritarianism or a significantly lower GDP. This resilience is what the authors call "a major puzzle"; one that, in their view, Piketty and many other thinkers have failed to solve.

Popular Views Turned Upside Down

In contrast, Iversen and Soskice propose a theory that aims to fill this blank and which thereby turns widely held ideas about democracy and capitalism upside down. Instead of assuming or concluding that it is "markets against politics, with markets winning out"—as they summarize their intellectual opponents' view—they picture the relationship between democracy, the nation-state and capitalism as being mutually supportive. That is, their framework's three protagonists (state, voters and capital) are supposedly in a stable state of symbiosis, the supporting arguments for which are intelligent and intricately intertwined to the extent that a summary within the scope of this article necessarily falls short of its richness. Nonetheless, their analysis may be reconstructed as follows.

Firstly, **states** have a central role in safeguarding the essential conditions for the flourishing of advanced (that is, knowledge-based) capitalism. They do so by (1) incentivizing innovation through the

enforcement of competition; (2) enabling skill formation through adaptive educational systems; and (3) facilitating capitalization thereof through the provision of fitting infrastructures and institutions. Secondly, political parties that direct these tasks care for their reputation among **voters**. Since people vote in their own interest, and the electoral majority's interest is aligned with the development of advanced capitalist sectors, politicians who are known for their successful economic management will be (re)elected. Thirdly, the skills of highly educated voters (in their capacity as workers) are chased by advanced **capital**. These workers' skills are only operationally effective when physically matched with specific technologies and skills of other workers. That is, in the book's terminology, workers and technology are "cospecific" and need to be "colocated", which results in a geographically differentiated pattern of "skill-clustered networks". These networks are immobile: large groups of people and the technologies they work with are generally very costly to relocate. Advanced capitalist companies are therefore "nationally embedded" and not "footloose". They have no viable exit strategy out of the country they are based in—either with their headquarters or subsidiary locations—in the event something happens against their interest, say the levying of taxes. States can therefore blithely tax these companies, which empowers and enables them to govern their territories as they see fit—which brings us back to the beginning of this circular story.

The upshot is that advanced capitalist democracies produce their own electoral support, which comes from highly skilled workers who have a stake in the growth of the economy. In return for their votes, they receive education and fulfilling jobs—if not for themselves, then for their children. Companies have to compete with each other and they are geographically tied to the cities where their workers reside. It is on these grounds, then, that Iversen and Soskice base their conclusion that the democratic state is more powerful than capital, instead of the other way around as is so often thought.

Taken together, these elements indeed provide an appealing solution to the "major puzzle" mentioned above: the stability of advanced capitalist democracies from their formation in the late-nineteenth and early-twentieth centuries up until now. In addition, Iversen and Soskice's model is able to account for a broad range of real-world phenomena of the recent past and present—from the simultaneous rise of populism and cosmopolitan political parties to the persistence of varieties of capitalism despite globalization and the almost insurmountable difficulties that middle-income countries face in transitioning to an advanced capitalist democracy. This surely adds to the strength of their approach. Yet explanatory success with regarding to the past does not guarantee the same for the future—and this is exactly where the theory is lacking, as I will clarify below.

A Future Like the Past?

Through the lens of their analytical framework, the authors explicitly conjecture that there is a high likelihood of "a future like the present" in which advanced nation-states "will continue to produce democratic majorities for policies and institutions that sustain the system". To support this prognosis, they repeatedly emphasize how "the system" as they model it is resilient to (potentially) subversive changes—be they political in the form of populism, economic in the form of a financial crises, or technological in the form of disruptive innovations. One could therefore be tempted to conclude that Iversen and Soskice's model naturally ties in with the Sustainable Society Theme of the University of Groningen, since under their assumptions advanced capitalist democracies more or less automatically fulfill the Theme's aims "to contribute to the realization of future societies with high quality of life". Yet there are good reasons to doubt whether the future for democracies and their inhabitants will indeed be as bright as the authors think.

First, it may very well be the case that advanced capitalism will *not* be able to keep the majority of workers happy. That is, for highly educated workers to be employed in fulfilling jobs—the very aspect

that has made working in advanced capitalist sectors so attractive—may not be a matter of course in the near future, as technological innovations increasingly displace even medium- and high-skill jobs. Soskice and Iversen grant as much when they write that new technologies will predominantly offer opportunities for “the most talented, well-educated, and creative individuals” and that even among these, “dispersion in ... job opportunities is increasing”. But since they simplistically assume that the well-educated losers on the labor market will be contented by pursuing subsidized careers, they fail to recognize that the fierce competition among workers and the increasing strenuousness of professional demands spurred by skill-biased technological change are likely to take a severe toll on many people’s—possibly the majority’s—mental health. As Malcolm Harris has convincingly shown in his book *Kids These Days. Human Capital and the Making of Millennials* (2017), this is already the case for the youngest generations. If this trend persists, political parties promoting further development of advanced economic sectors—and thereby of technological innovation—will lose their constituency. In this way, skill-biased technological development may not only detract from overall quality of life, but also from the stability of advanced democracies.

A second point of critique related to the fact that Iversen and Soskice’s outlook hinges on the assumption that advanced capitalist companies will remain nationally embedded even in the face of technological change, because of enduring cospecificity and colocationality. Therefore, as the authors conjecture, these characteristics of advanced capitalist sectors will continue to give governments power to tax and spend in a way that satisfies the majority of their voters—ensuring that the constellation remains stable. However, this line of reasoning and the assumptions underlying it display the authors’ rather archaic picture of economic value creation as being production-centered, and of globalization of economic activities as proceeding through the establishment of a network of subsidiary companies. In recent years, online platform businesses have gained in economic importance in all sorts of sectors, ranging from hospitality to transport, and from durable consumer goods to delivery services. As reputed economists such as Jean Tirole and Michael Munger have argued, this development implies that in the near future the lion’s share of economic value creation may very well be generated by dispersed, ‘loose’ networks of individuals and small businesses while big revenue streams accrue to the headquarters of the platforms that facilitate the matches between them. This transformation of the economy’s fabric is likely to decrease the importance of cospecificity and colocationality of companies’ assets, and thereby of the power of governments to levy taxes.

This inference may sound familiar. It was indeed Thomas Piketty who conjectured that “fiscal competition will gradually lead to total disappearance of taxes on capital in the twenty-first century”. Of course, it remains to be seen whether his grim outlook is closer to future facts than the rather optimistic predictions that Iversen and Soskice make. Nonetheless, however this battle of these theories may eventually be settled (if at all), *Democracy and Prosperity* is a highly recommended read, especially for those interested in political economy, economic geography and/or innovation studies. The rich analyses it contains are not only thought-provoking, but also able to account for many macro, meso and micro phenomena, at least of the present and recent past. It shows intellectual courage to take up a theoretical endeavor like that.

Iversen, T. & Soskice, D. (2019). *Democracy and Prosperity; Reinventing Capitalism through a Turbulent Century*. Princeton, NJ: Princeton University Press.

Recommended readings

Harris, M. (2017). *Kids These Days; Human Capital and the Making of Millennials*. New York: Little, Brown and Company.

Munger, M. (2018). *Tomorrow 3.0; Transaction Costs and the Sharing Economy*. Cambridge: Cambridge University Press.

Tirole, J. (2017). *Economics for the Common Good*. Princeton: Princeton University Press.

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