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A Turn to Export-Led Growth? Rethinking the Growth Models in Greece and Portugal

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Abstract

The global financial crisis in 2007 and, more recently, the Covid-19 pandemic renewed interest in capitalist divergence and the evolution of growth models in the Eurozone. The varieties of capitalism (VoC) approach and more recently post-Keynesian research, especially the growth model (GM) perspective, have made important contributions to comparative political economy. However, the focus on either the 'supply-side' or 'demand-side' aspects of modern models of capitalism has offered a limited framework to explain capitalist diversity in the global economy. This article brings insights from both the VoC and GM perspectives and provides a more comprehensive understanding of the evolution of the growth models in Greece and Portugal. The argument is that although both countries implemented internal devaluation and contractionary policies to curtail domestic demand and transform their economies into export-led ones, they have been stuck in a suppressed demand-led growth model since the global financial crisis.

Keywords: comparative political economy; Greece; growth models; Portugal; Southern Europe; varieties of capitalism

Introduction

The global financial crisis in 2007 and, more recently, the Covid-19 pandemic renewed the academic and policy debates regarding capitalist divergence and the evolution of growth models in the Eurozone. Several contributions have been made to the comparative political economy (CPE) literature, offering new accounts to explain capitalist diversity. The varieties of capitalism (VoC) and other more recent accounts based on post-Keynesian approaches, especially the growth model (GM) perspective, offer variety in a growing body of literature on modern capitalism. Some CPE authors have focused on an institutional and supply-side analysis of capitalist economies (Hall and Soskice, 2001), whilst others have taken a demand-side approach to analysing the various models of capitalism (Baccaro and Pontusson, 2016; Stockhammer and Ali, 2018). Such contributions have enriched the CPE research agenda. However, scrutiny of these contributions, and particularly the VoC's isolation of the supply-side and the GM's emphasis on the demand-side aspects, seems unproductive in trying to explain capitalist evolution and change.

The global financial crisis put the European economies, particularly the southern European countries, at the centre of the CPE research. When the financial crisis spread from the United States to the European periphery, Greece, Portugal and Ireland could not refinance their mounting debt and lost access to the financial markets. The European Union (EU) and the International Monetary Fund (IMF) offered financial assistance to these countries in exchange for contractionary policies. The European response to the crisis favoured internal devaluation to transform the demand-led economies in Southern Europe into export-led countries (European Commission, 2012, p. 2). This article focuses on two southern European countries, Greece and Portugal, which implemented internal devaluation policies to restore their competitiveness and transform their growth models into export-led ones (European Commission, 2012). This article evaluates the extent to which, and how, the internal devaluation affected the growth models in Greece and Portugal in the aftermath of the global financial crisis.

The contribution of this article is threefold. First, it moves beyond the unproductive debate between the VoC and GM perspectives by bringing them into a fruitful dialogue. Second, the article offers an advanced analysis that incorporates supply-side and demand-side factors and their interaction in explaining capitalist diversity and change. Third, although other scholars have examined the effects of the global financial crisis and internal devaluation on Southern Europe and highlighted the factors that impede a robust economic recovery (Gräbner et al., 2020; Storm and Naastepad, 2015), this article provides a novel approach that integrates VoC and GM perspectives to explain how demand-side and supply-side factors interacted in both countries and therefore brings new evidence to illustrate the evolution of growth models after the global financial crisis.

The article is organised as follows: in Section I, it reviews the recent CPE literature and VoC's important contribution and also its shortcomings. Then, it analyses the more recent literature on the GM perspective and develops a new approach to test how demand-side and supply-side factors interact and shape modern capitalist economies. Section II analyses the interaction of demand-side and supply-side factors and the creation of a demand-led growth model in Greece and Portugal before the global financial crisis. Section III examines such factors after the crisis and the extent to which the internal devaluation policies led to export-led growth in Greece and Portugal. The final section summarises the research findings and the contribution to the CPE literature and concludes.

I. CPE: Looking Beyond VoC Versus GM

Building upon the CPE literature, this article brings insights from both the VoC and GM perspectives to explain the evolution of growth models in Southern Europe. Peter Hall and David Soskice's VoC perspective emerged as the most influential research agenda in CPE in the early 2000s. Hall and Soskice (2001) linked historical institutionalism and institutional economics to explain the formation of capitalism in different countries. VoC places supply-side factors at the centre of its research inquiry, especially the structure of the economy, industrial relations, labour markets, education and training systems. VoC's comparative analysis of institutional variation provides a significant understanding of how capitalism works in different countries.

Hall and Soskice (2001) also emphasise the role of firms, positioning them as central actors in a capitalist economy. However, institutions play a primary role in shaping the framework for interactions amongst firms and other actors, regulating economic behaviour and imposing sanctions for rule violations. This analytical framework distinguishes between two political economies: liberal market economies and co-ordinated market economies. In the former, firms co-ordinate through market competition and formal contracts. In the latter, firms rely on collaborative, as opposed to competitive, methods to interact with other actors, fostering long-term relationships with stakeholders. Hall and Soskice (2001) classified the Organisation for Economic Co-operation and Development (OECD) countries as liberal market economies (e.g., the United States, Canada and Britain) and co-ordinated market economies (e.g., Germany and the Netherlands).

They also identified Greece, Portugal, Italy and Spain as another 'variety' of capitalism – the mixed market economies – that are marked by a large agriculture sector, co-operative corporate governance and liberal labour markets. Mixed market economies maintain fragmented production systems in terms of territory and firm size, a relatively low-skilled workforce, and tend to perform poorly in terms of innovation, productivity and exports (Molina and Rhodes, 2007).

The VoC perspective has been very influential amongst CPE scholars and has dominated the CPE field in the last two decades. However, its theoretical assumptions have not been unchallenged (Baccaro and Pontusson, 2016; Stockhammer and Ali, 2018; Streeck and Thelen, 2005). The global financial crisis in 2007 triggered a new wave of CPE literature that challenged the VoC's perception of political economy, supply-side focus and concepts. The GM literature has recently opened up promising paths for CPE. It aims to overcome VoC's supply-side focus, static analysis and limited research framework. This new perspective, rooted in post-Keynesian economics, focuses on the role of aggregate demand in shaping diverse capitalist models. Based on Kaleckian economic foundations, Baccaro and Pontusson (2016, p. 176) place demand-side factors and particularly income distribution at the core of their theoretical approach. Their framework centres on the key components of aggregate demand: government spending, public and private investment, consumption, net exports and their role in wage-led growth models. By emphasising national macroeconomic policies and global economic shifts, this approach provides new insights into the formation of capitalist diversity. Taking a historical perspective, Baccaro and Pontusson (2016) argue that financialisation and de-industrialisation in the Western capitalist world have transformed traditional growth models. Economic liberalisation, marked by labour market deregulation and a decline in unions' power, has fostered asymmetrical income distribution. These complex shifts have triggered different growth strategies, leading to diverging growth models such as export-driven and demand-led regimes.

According to Baccaro and Benassi (2017, p. 90), distributive policies significantly affect growth models. Macroeconomic policies impact aggregate demand and, therefore, investment, wages and consumption. Governments may boost growth through higher public spending and real wage increases, fostering consumption. However, such consumption-led growth may conflict with export-led growth determinants because higher wages are expected to make domestic production more expensive for consumers abroad, resulting in higher current account deficits and public debts (Losada, 2020). Overall, in export-led models, growth is largely based on low domestic demand, a sizable export sector and a positive balance between goods and services (Hein et al., 2020, p. 7). In debt-led models, growth is dependent on domestic demand and corporate and households' balances, leading to current account deficits and high public and private debts (Sapir, 2019).

The VoC and GM approaches have been very influential in CPE. However, both perspectives only partly explain the various models of capitalism. VoC offers an advanced framework to understand the role of institutions, the structure of the economy, the firms and the industrial relations that shape different types of capitalist economies. However, it presents limited insights into the effects of fiscal policies on private investment, consumption and overall economic performance in various growth models (Stockhammer and Ali, 2018). The VoC literature also offers a limited framework to understand the ways in which demand-side factors affect the structural and supply-side aspects of the economy.

Furthermore, VoC underestimates the complex international economic developments that have affected national and local economic realities in the last decades. The emergence of economic liberalism as a predominant paradigm worldwide, based on higher capital mobility, labour market deregulation and rapid financialisation, has transformed the national models of capitalism (Thelen, 2014). The relations amongst capital markets, states, firms and consumers have been affected in diverse ways (Engelen and Konings, 2010). In particular, the financial system significantly influences the investments, savings and spending decisions of governments, firms and consumers. VoC scholars have underestimated those shifts in their analytical framework and categorisation of capitalist models.

Finally, VoC's emphasis on economic agents, such as 'firms' and 'sectors', overlooks the complex interplay between political actors and economic structures. VoC lacks the methodological tools to fully capture the politics and power struggles that shape and reshape institutions and policies at a national level (Thelen, 2014). The heterogeneity of socio-economic interests and distribution conflicts significantly affect the growth patterns in capitalist economies (Amable et al., 2019, p. 435). The state-economic elites' relationships set the political and economic foundations of growth models (Baccaro and Pontusson, 2022). A comprehensive analysis of how politics is embedded in institutions and institutional evolution is essential for understanding the formation and evolution of models of capitalism. VoC, in its current form, lacks the analytical depth needed to capture these political and social dimensions and therefore provides a static view of national models of capitalism.

The GM approach offers an in-depth understanding of fiscal and monetary policies and their effects on demand in modern economies. It provides an advanced analysis of how changes in macroeconomic policies affect economic activity and, more broadly, growth models (Stockhammer, 2016). However, by emphasising the role of wage policies and demand per se, GM does not account for the supply-side framework within which government fiscal and welfare policies are developed. The historical process of capital formation, the level of development of the production capabilities and the local institutions set the foundations of capitalist models; however, they seem to play a secondary role in the GM analysis of capitalist economies. The GM approach overestimates the role of wage policies and aggregate demand themselves in transforming demand-led into export-led growth models. It underestimates the structure of the economy, institutions and national and local politics that may restrain export performance. The GM's framework offers a limited analysis of how macroeconomic policies and aggregate demand interact with supply-side factors in transforming the growth patterns in various capitalist economies.

The Reconciliation of the VoC and GM Perspectives

This article takes the current CPE debate forward by bringing insights from the VoC and GM perspectives to provide a comprehensive understanding of the capitalist diversity and growth model evolution in Greece and Portugal. Despite the ongoing VoC and GM debate, some proponents of both schools have recently begun to recognise the value of the other perspective and acknowledge that insights from these, often presented as rival accounts, can add value in understanding growth patterns in modern economies (Baccaro et al., 2022; Fazzari et al., 2020). To exemplify this, Baccaro et al. (2022, p. 25) recently asserted that 'if a country wants to increase its feasible growth rate, it cannot simply expand aggregate demand. It will have to increase the attractiveness of its exports, or reduce the desirability of imports, which requires appropriate supply-side policies that upgrade its production structure'.

Despite such an acknowledgement, the current literature lacks a systematic approach to studying the interaction of the demand-side and supply-side aspects of growth. This article lays the foundations to bring VoC and GM together, moving beyond the isolation of the 'supply-side' and 'demand-side' factors in explaining capitalist diversity and change. The incorporation of macroeconomic policies and demand into the VoC analytical framework sheds light on the way that demand-side reforms affect supply-side factors such as productive capabilities, technological capacity and innovation and offers an advanced understanding of national economies. To assess the complex ways in which demand-side and supply-side factors interact in shaping and transforming growth models, this article formulates three interrelated testable hypotheses and brings evidence from Greece and Portugal to evaluate them.

The article is grounded in the theoretical assumption that individual countries maintain a particular level of development in their supply-side economies. Based on the historical process of capital accumulation and institutional framework, countries develop production capabilities, technological capacity, labour skills and design policies for innovation and productivity (Hall and Soskice, 2001). Commencing with this existing economic structure, national governments pursue macroeconomic policies that affect the prevalent supply-side features and the broader economic structures at the national level. Fiscal and monetary policies affect economic behaviour across the economy. Firms and households adjust their economic activity, particularly their investment and spending decisions, according to the macroeconomic environment within which they operate (Stockhammer, 2016). Such economic decisions affect the broader direction of economic activity in national economies.

Households amend their expenditures considering the government's fiscal, welfare and tax policies. Under fiscal expansion conditions, households may increase their spending, whilst under fiscal contraction conditions, they may reassess their spending decisions and lower their levels of consumption (Stockhammer and Ali, 2018). Similarly, firms make decisions about exports based on the levels of domestic and foreign demand. Under conditions of high domestic demand, firms may focus on the domestic market, whilst under low demand conditions, they may opt for exporting their products to markets beyond the national borders (Baccaro and Pontusson, 2016). In the former case, firms may target domestic demand, undervaluing investment in supply-side factors. In the latter case, firms may invest in new technological capacity, innovation and labour skills, facilitating the upgrade of the supply-side economy to compete in international markets. Therefore, fiscal policy change and aggregate demand may transform the supply-side economy. To assess the above, this article tests the following overarching hypothesis (H):

H: Demand-side policy reforms transform the supply-side aspects of the growth model.

This article develops two additional sub-hypotheses to show under which conditions demand-side and supply-side factors interact in modern capitalist economies. It goes beyond the VoC perspective, which undervalues the role of 'politics' in modern capitalist societies, to show the ways in which economic and political elites affect the direction of growth models. It also goes further than the GM's emphasis on the government's fiscal policy to show the ways in which the government's broader growth agenda affects the supply-side economy.

According to Baccaro et al. (2022, p. 30), the reproduction of growth models depends on the presence of a political coalition of corporate elites and government officials that favour a common growth policy agenda. Growth coalitions, together with political parties, seek to maintain their ability to mobilise an electoral majority to promote such a policy agenda. The latter influences government policy to stimulate or depress different components of aggregate demand, affecting the distribution of profits and income across the economy (Baccaro et al., 2022, p. 29). In times of economic expansion, growth coalitions may favour expansionary fiscal policies, in the context of low interest rates, to ease fiscal constraints and build political and social alliances across capitalist societies (Esping-Andersen, 1985). However, in times of crisis, the contractionary conditions constrain the ability of the growth coalitions to stimulate demand and maintain social alliances through generous welfare policies. In such times, growth coalitions may change their policy orientation towards a new growth agenda that allows them to mobilise societal actors and formulate new social alliances (Hopkin and Voss, 2022). Such a new growth agenda may promote investment in supply-side aspects of the economy to develop new export capabilities, improve the quality of exports and enhance competitiveness. Hence, the change in demand-side policy may lead the growth coalition to develop a new growth agenda that transforms the supply-side economy. To evaluate the above, this article tests the following sub-hypothesis (h1):

h1: The growth coalition develops a new growth agenda that transforms the supply-side aspects of the growth model.

By connecting VoC with the GM approach, this article also focuses on the effects of the financial system on national economies. The VoC literature tends to underestimate the impact of financial transformation on growth models. On the other hand, the GM approach offers a more advanced framework to explain how economic liberalisation and financialisation have affected growth models since the late 1980s (Stockhammer and Kohler, 2020). However, GM sets financialisation per se as the driving force behind the divergence of growth models in the capitalist world. Instead, this article studies the ways in which structural and political patterns interact with the financial sector and credit in capitalist economies. The rise of a modern financial sector and households' easier access to credit produce disparate effects and transform growth models in various ways (Engelen and Konings, 2010). Under conditions of low interest rates and easy access to credit, households increase their spending and consumption (Stockhammer and Kohler, 2020). Under such conditions, firms may target the domestic market and undervalue investment to upgrade production capabilities, enhance productivity and improve export competitiveness. In contrast, under conditions of high interest rates and restrained access to credit, households decrease their consumption, and firms may turn to markets abroad (Baccaro and Pontusson, 2016). To compete in international markets, firms may invest in improving their production capabilities and upgrading the supply-side economy. Therefore, households' access to credit may change the supply-side economy. To assess the above, this article tests the following sub-hypothesis (h2):

h2: Households' access to credit transforms the supply-side aspects of the growth model.

Overall, this article develops and assesses an overarching hypothesis (H) to identify the causal relations between the demand-side and supply-side aspects of growth. It also evaluates two sub-hypotheses (h1 and h2) to show under which conditions the demand-side factors interact with the supply-side ones. In Sections II and III, we use evidence from the cases of Greece and Portugal to first assess the sub-hypotheses and then the overarching hypothesis and the relations amongst them in both the pre-crisis era and the post-crisis era, respectively. This approach allows us to offer insights into the extent to which and under which conditions, if any, demand-side policies could transform the supply-side factors of the economy.

II. The Political Economy of Greece and Portugal in the Pre-crisis Era

Greece and Portugal underwent distinct processes of political liberalisation following the overthrow of the authoritarian regimes in the 1970s; nonetheless, they both encountered a comparable economic transformation. In this subsection, we assess sub-hypothesis h1 to show to what extent the growth coalition that emerged following the end of the dictatorships in the 1970s shaped an agenda that transformed the supply-side aspects of the growth models in Greece and Portugal.

The Emergence of a New Growth Coalition and the Demand-Led Growth Paradigm

The Greek economic elite initiated the country's accession to the European Community after the end of the dictatorship in the mid-1970s (Pagoulatos, 2003, pp. 80–110). In the eyes of the Greek economic elites, accession to the European Community was the path to modernisation, economic acceleration and convergence with the high-performing economies in Europe (Featherstone, 2005). This pro-European economic elite has, based on high levels of domestic demand and consumption, formed a growth coalition that has been dominating Greece's political life since the 1980s. The growth coalition was supported by both dominant political parties, the social-democratic Panhellenic Socialist Movement (PASOK) and the centre-right New Democracy, which propelled Greece towards economic liberalisation and deeper European integration.

After Greece's accession to the European Community in 1981, the prevailing growth coalition, led by the PASOK government, pursued a Keynesian wage-led growth programme, increasing the minimum wage, pensions and public spending to stimulate demand and build a modern national welfare system. Such an expansionary fiscal policy led to a substantial government deficit and debt accumulation in the 1980s (Pagoulatos, 2003, p. 95). Despite occasional attempts to limit public spending by the new centre-right New Democracy government, the prevailing growth coalition persisted in stimulating demand in the 1990s. Based on this economic paradigm, PASOK and New Democracy developed networks of political support in urban and rural areas, dominating the political system before the global financial crisis (Doxiadis, 2013).

Portugal also experienced a rapid process of economic liberalisation after the Carnation Revolution in 1974 and the abolition of the revolutionary constitution. The emergence of a new liberal economic elite gradually formed a new growth coalition that was supported by various liberal political parties, especially the Social Democratic Party (PSD), the Socialist Party (PS) and the People's Party (CDS-PP), and opened the way for the transition to a model of a 'free market' economy in the 1980s (Moreira et al., 2014). The accession to the European Community accelerated the liberalisation of the Portuguese economy and society.

The European integration process and financial deregulation allowed the predominant liberal coalition to favour policies to stimulate domestic demand, which gradually strengthened the inward-looking non-tradable sectors of the economy, mainly construction, real estate and retail trade (Moreira et al., 2014; Reis, 2013). The new policy paradigm favoured policies to build political support amongst the emerging middle class and downgraded policies to improve the supply-side aspects of the economy, especially the weak production base, the skills shortages and the low added-value production (Dooley, 2018).

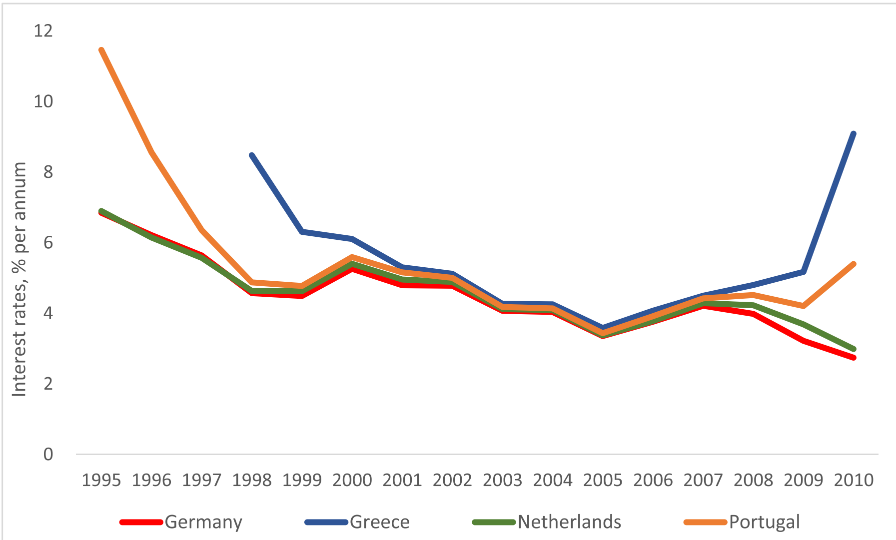
In parallel, Greece's and Portugal's entry into the Single European Market triggered a rapid economic transformation. The exposure to high levels of external competition along with the gradual abolition of industrial policy resulted in a dramatic degradation of the countries' supply-side economies and production capabilities. Large-sized and medium-sized firms, exposed to competition, struggled to survive and were gradually replaced by small and flexible firms (Giannitsis, 1988). Greece and Portugal went through a rapid process of de-industrialisation in the early 1990s (Dooley, 2018; Giannitsis, 2013). Therefore, evidence from Greece and Portugal supports sub-hypothesis h1 because the emergence of a new liberal growth coalition set the economic agenda for a new growth model after the collapse of the authoritarian regimes in the 1970s. The growth coalitions gradually shaped a new economic paradigm that stimulated demand to build political and social alliances amongst the emerging middle class in urban centres and opened the way for the demand-led growth model in both countries.

The Easier Access to Credit Facilitates the Transition to a Demand-Led Growth Model

At the turn of the millennium, Greece and Portugal followed an expansionary fiscal policy and pursued deregulation reforms in the labour and product markets. In this subsection, we assess sub-hypothesis h2 to show to what extent the easier access to credit transformed the supply-side economy in both countries.

Greece's and Portugal's access to the Eurozone, along with the financial liberalisation, enabled the growth coalitions in both countries to pursue further policies to stimulate demand and accelerate growth in the first decade of the Eurozone. As Figure 1 shows, the entry into the Eurozone opened the way, under European Central Bank policy, for the convergence of interest rates for the member states over the period from 2000 until the financial crisis in 2007. Greece and Portugal experienced enhanced access to credit in terms that were not only more favourable but also comparable to those enjoyed by other dynamic European economies such as Germany and the Netherlands.

Figure 1: Long-Term Interest Rates, Percentage per Annum, 1995–2010. [Colour figure can be viewed at wileyonlinelibrary.com]



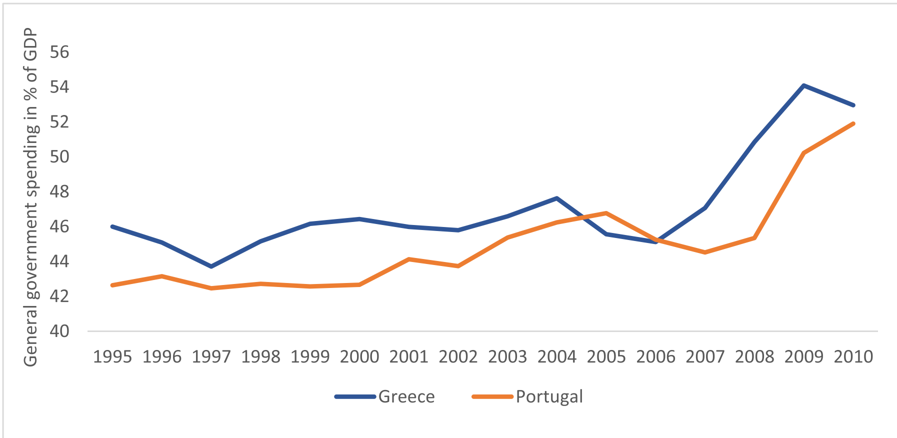
Note: All figures in Section II cover the period from 1995 to 2010, illustrating the evolution of the examined variables before Greece's and Portugal's accession to the Eurozone and extending to the countries' agreements with the EU and IMF in 2010 and 2011, respectively.
Source: OECD.

This easier access to credit allowed the growth coalitions to maintain their expansionary fiscal policies, further increasing public spending and promoting generous welfare policies in both countries. Despite the fact that Portugal pursued a less expansionary fiscal policy than Greece, both countries, as Figure 2 shows, increased their public spending dramatically in the mid-2000s. The fiscal expansion boosted further domestic demand ahead of the financial crisis.

In tandem, the financial deregulation that was initiated with the Capital Adequacy Directive in 1991 and the EU Banking Directive in 1993 opened the way for the Greek and Portuguese banking sectors to create new banking products, take higher risks and increase loans for households (Dooley, 2018, p. 79). Financialisation and the high credit flows to households expanded domestic demand and resulted in higher levels of households' consumption. As Figure 3 illustrates, households' spending as a percentage of gross domestic product (GDP) remained persistently high and well above other European economies such as Germany and the Netherlands in both countries before the financial crisis.

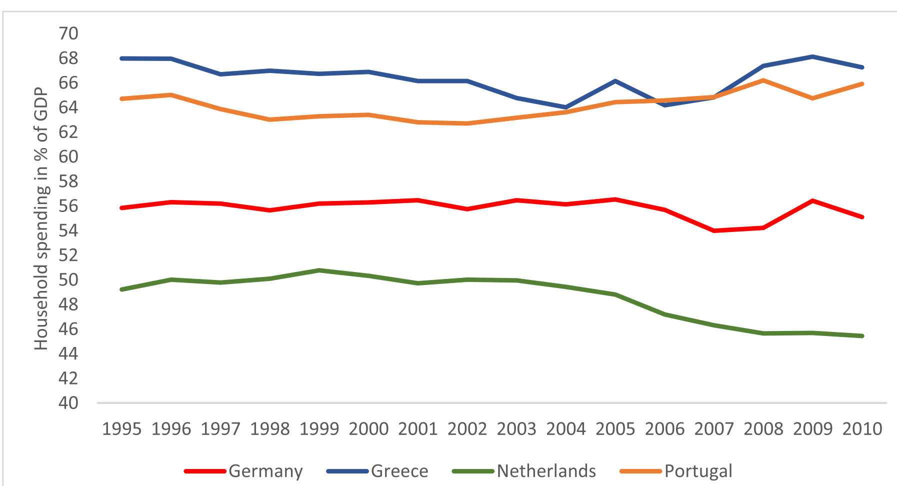
The easier access of households to credit acted as demand injections for both economies. In Greece, households' spending was directed towards housing construction, real estate and retail trade. Similarly, in Portugal, the easier access to credit led to the expansion of non-tradable sectors, mainly real estate and retail trade (Giannitsis, 2013; Reis, 2013).

Figure 2: General Government Spending in Percentage of GDP, 1995–2010. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: See Figure 1 note.
Source: OECD.

Figure 3: Household Spending in Percentage of GDP, 1995–2010. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: See Figure 1 note.
Source: OECD.

The households' high consumption levels allowed firms to focus on the domestic market, and investment in supply-side factors, such as technological capacity, innovation and labour skills, was neglected (Reis, 2013). Hence, the empirical findings support sub-hypothesis h2 because the easier access to credit boosted further domestic demand and consumption, gradually downgrading the supply-side economy in both countries. Based on such an economic policy paradigm, Greece and Portugal, according to Eurostat (2002), witnessed high growth rates in the first decade of the Eurozone. Both countries were in a process of convergence with the other Eurozone countries. However, the economic expansion laid the foundation for a rapid transformation towards a fragile consumption-led growth model.

The Transition to a Demand-Led Growth Model

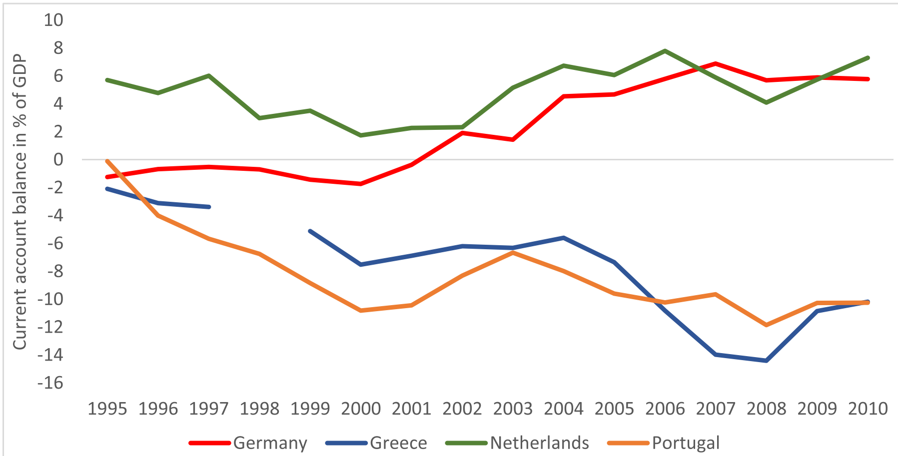
The growth coalition's shared consensus on policies to stimulate domestic demand, coupled with households' privileged access to low interest rates, resulted in the expansion of non-tradable sectors at the expense of the tradable economy in the 2000s. In this subsection, we assess, taking into consideration the validation of sub-hypotheses h1 and h2, the overarching hypothesis H. The objective is to demonstrate the extent to which changes in demand-side policies have transformed the supply-side economy.

Greece and Portugal went through a rapid de-industrialisation process in the pre-crisis era. Both countries maintained industrial sectors that were amongst the weakest in the Eurozone before the crisis (OECD, 2017a). The weak production base and low-technology products, together with higher competition in the context of the European Single Market, led to a gradual loss of competitiveness. Investment in research and development to reverse this trend remained stagnant in both countries before the crisis (Eurostat, 2016). Policies to boost demand were pursued at the expense of a systematic supply-side growth agenda and therefore led to the decline of the supply-side economy (Giannitsis, 2013).

The emergence of a new demand-led growth model impeded higher export performance and gradually led to large trade deficits in both countries. In 2000, the adoption of an overvalued currency, the Euro, made their exports more expensive compared with their competitors (Amaral, 2013). Under those circumstances, producers turned to domestic demand rather than to the European and global markets. The abolition of the Multi-Fibre Arrangement in 2005 ended the restrictions on clothing exports from developing to developed economies, leading Greek and Portuguese exports into further decline. In the 2000s, as depicted in Figure 4, Greece and Portugal faced a substantial and persistent current account deficit, in contrast to the performance of Germany and the Netherlands, two of the most significant export-driven Eurozone economies.

Despite the fact that successive governments in Portugal maintained the government deficit and debt at manageable levels, the trajectory of both the Greek and Portuguese economies was not sustainable at the turn of the millennium. The growth coalition's expansionary fiscal policy, together with households' easier access to credit, opened the way for the demise of supply-side aspects of growth and the transition to a consumption-led growth model. Therefore, the empirical findings confirm the overarching hypothesis H, showing that demand-led policies transformed – as both sub-hypotheses h1 and h2 are satisfied – the supply-side aspects of the growth model before the crisis. Such a demand-led growth model made Greece and Portugal vulnerable to the global financial crisis.

Figure 4: Current Account Balance in Percentage of GDP, 1995–2010. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: See Figure 1 note. Also, data for Greece in 1998 are not available.
Source: World Bank.

III. Turning to an Export-Led Growth Model? The Political Economy of Greece and Portugal in the Post-crisis Era

The outbreak of the global financial crisis and its spread to the Eurozone made Greece and Portugal lose access to the capital markets and rendered them unable to service their increasing public debt. The European response to the financial crisis favoured labour cost reduction policies to suppress demand and transform these countries from demand-led to export-led economies (European Commission, 2012, p. 2). Greece and Portugal, under the EU and IMF financial assistance programmes, implemented contractionary policies that decreased domestic demand in the aftermath of the crisis. To assess the extent to which internal devaluation transformed Greece and Portugal towards an export-led growth model and to evaluate the causal relations between demand-side and supply-side aspects of growth, this article tests the same sub-hypotheses (h1 and h2) and overarching hypothesis (H) and the relations amongst them in the post-crisis era.

The Resilience of the Growth Coalition and the Failure to Promote an Export-Oriented Policy Agenda

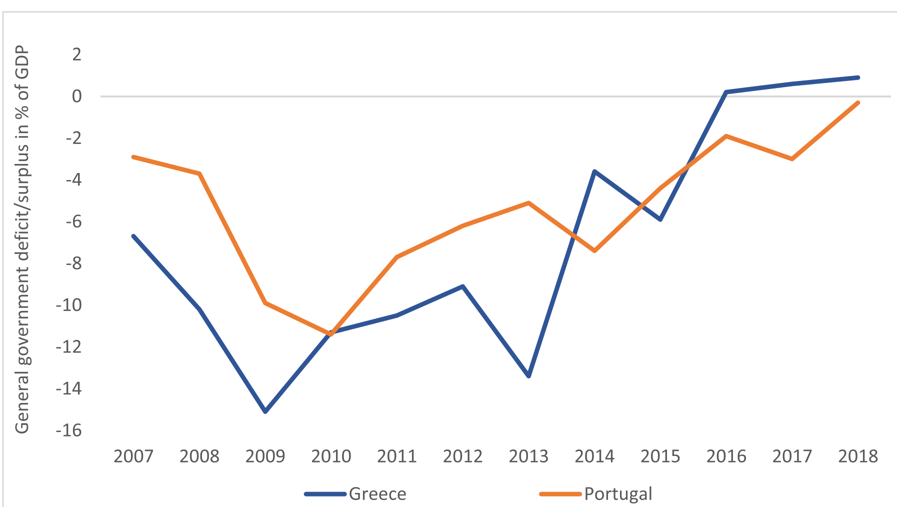
Greece and Portugal pursued a drastic fiscal policy change in the aftermath of the crisis. The externally imposed austerity compelled the predominant growth coalition to implement contractionary policies, which diverged from the macroeconomic approach that had been employed prior to the crisis. In this subsection, we assess sub-hypothesis h1 to show to what extent the growth coalition shaped a new growth agenda to transform the supply-side economy in Greece and Portugal after the crisis.

In Greece, the successive government pursued a significant fiscal adjustment that was primarily based on public expenditure cuts in 2010–2012, followed by a large increase in taxes in 2012–2018. After decades of a high fiscal deficit, which reached 15% of GDP in 2009, Greece achieved a surplus of 0.9% of GDP in 2018, as illustrated in Figure 5. The adjustment in Portugal was not as rapid and deep as in the Greek case. About half of the contractionary measures were taken early on, in 2011, whilst the remaining measures were allocated to 2012–2014. Portugal also achieved a significant fiscal adjustment from a deficit of 9.9% of GDP in 2009 to a deficit of 0.3% of GDP in 2018. Both countries, as Figure 5 shows, achieved a substantial fiscal adjustment after the crisis.

The fiscal adjustment had a dramatic impact on economic activity. The simultaneous decrease in wages and increase in taxes significantly eroded the purchasing power of the middle class, leading to a dramatic decline in disposable income and economic stagnation. Households could not spend as they had before, and, as Figure 6 illustrates, demand fell dramatically in both countries after the crisis.

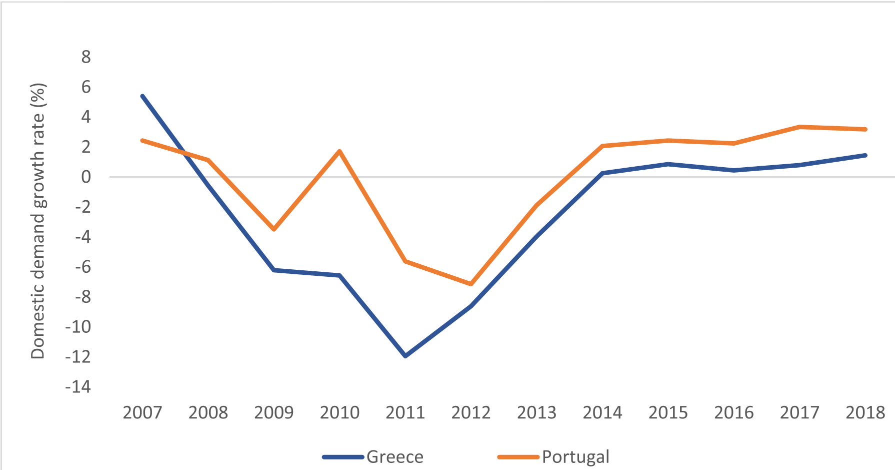
The externally enforced internal devaluation policies suppressed domestic demand and laid the foundations for a transition away from the demand-led policies in Greece and Portugal. However, the prevailing growth coalitions demonstrated political resilience; despite altering fiscal policy, they maintained their political dominance after the crisis. In Greece, the governing political parties PASOK and New Democracy, underpinning the predominant growth paradigm, formed a coalition government to preserve the elements of the pre-crisis growth agenda. The election of a new left-wing government in 2015, led by the Radical Left, SYRIZA, favoured economic recovery based on stimulation of domestic demand rather than policies to boost supply-side growth (Katsourides, 2016).

Figure 5: General Government Deficit/Surplus in Percentage of GDP, 2007–2018. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: All figures in Section III cover the period from 2007 to 2018, illustrating the evolution of the examined variables following the outbreak of the global financial crisis and the subsequent introduction of internal devaluation policies in Greece and Portugal until the conclusion of the EU and IMF financial assistance programmes in 2018.
Source: OECD.

Figure 6: Domestic Demand, Annual Growth Rate (%), 2007–2018. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: See Figure 5 note.
Source: OECD.

The SYRIZA-led government signalled the perpetuation of, rather than a change to, the pre-crisis growth agenda.

In Portugal, the Social Democratic Party (PSD) formed a coalition government with the People's Party (CDS-PP) to implement internal devaluation policies. Despite contractionary policies, PSD and CDS-PP maintained their political networks and remained in power until the end of the crisis (Serra-Silva and Santos, 2023). The growth coalition did not develop a new export-promotion growth agenda to mobilise firms towards exports and foster structural change towards dynamic export-led growth after the crisis.

Despite the political changes, the growth coalitions in both countries remained inward looking, and firms barely developed networks to facilitate export activity. Policies to support firms' transformation to compete with firms in other European economies were neglected (Giannitsis, 2013, pp. 155–160). Greece and Portugal are still dominated by small and family-owned firms producing less competitive products (Doxiadis, 2013, pp. 108–115). Most of them suffer from inefficient division of labour and resource scarcity in terms of upgrading their operations and building networks towards markets abroad. In neither country did the growth coalition favour policies to improve the weak production base. The latter impeded the emergence of a dynamic export sector after the crisis.

The growth coalitions also undervalued policies to improve labour skills in both countries. In Portugal, skills shortages have remained a major restraining factor in the country's transition to an export-led growth model. Portugal has amongst the lowest percentages of training in the working population because about 60% of the workforce has just 9 years of education (Almeida et al., 2006). Greece performs relatively well compared with Portugal on most education and labour skills metrics. However, successive Greek governments have not promoted policies to facilitate the transition of the labour force to export industries (Perez and Matsaganis, 2019). Labour skills in export sectors have remained largely underdeveloped and have impeded a dynamic export performance.

Therefore, evidence from Greece and Portugal shows no support for sub-hypothesis h1 because the growth coalitions and the governing political parties in both countries have adhered – even since the crisis – to the pre-crisis growth policy paradigm. The growth coalitions have not developed a new growth agenda to transform the supply-side economy in favour of an export-led growth model.

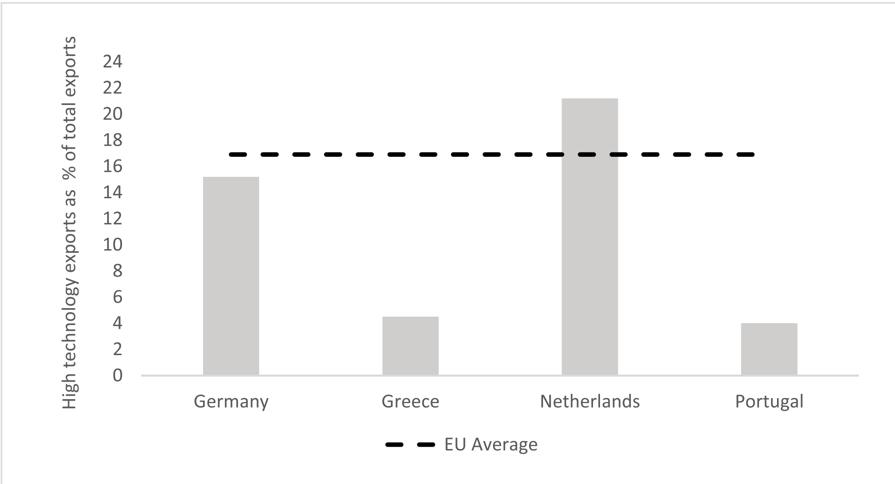
The Restrained Access to Credit

The onset of the global financial crisis had a dramatic effect on the banking sector in the Eurozone, causing significant disruptions in credit flows to the southern European economies, with Greece and Portugal being particularly affected. In this subsection, we evaluate sub-hypothesis h2 to show to what extent households' limited access to credit transformed the supply-side economy in both countries following the crisis.

According to Hausmann and Rodrik (2003), the transition to an export-led growth model requires a large transfer of productive capital to the export sectors. However, in Greece and Portugal, the banking crisis restrained the transfer of capital to export industries and negatively affected the prospects of a growth model transformation. In the aftermath of the crisis, concessionary credit to Greece and Portugal came to an end. At the same time, the crisis and contractionary policies impacted the capacity of households and firms to fulfil their lending commitments, resulting in the banking sector accumulating substantial levels of non-performing loans. The latter increased from 2.5% and 3.1% in 2008 to 37.4% and 16.6% of total gross loans in 2016 in Greece and Portugal, respectively (World Bank, 2017). In these conditions, the banking sector faced constraints in offering new lending to households at pre-crisis levels. The limited access to credit amongst households consequently contributed to a further decline in consumption.

Contrary to hypothesis h2, the restrained access of households to credit and the resulting decline in domestic demand did not open the way for firms to turn to international markets. The banking crisis also affected the credit flows to small and medium enterprises (SMEs) and impeded their transformation towards export activity. The new lending to SMEs declined from €12.9 billion in 2009 to €1.2 billion in 2015 in Greece and from €23.1 billion to €11.8 billion in Portugal in the same period (OECD, 2017b). Greek and Portuguese firms faced dramatic liquidity issues and therefore did not invest in the supply-side economy to upgrade their production capabilities, produce high added-value products and build trade networks with foreign markets. According to the OECD (2019), gross domestic spending on research and development remained low after the crisis, accounting for 1.2% in Greece and 1.3% in Portugal in 2018, whilst the EU average was 2% of GDP in the same year. After nearly a decade of internal devaluation policies, the exports of high-technology products remained low, as Figure 7 illustrates, accounting for 4.5% and 4% of total exports in Greece and Portugal in 2018, respectively. These figures were significantly below not only those of other export-led economies in the Eurozone but also the EU average, which stood at 16.9% of total exports in the same year. Greece and Portugal have been stuck at a low level of technology, which has impeded a dynamic export performance.

Figure 7: Exports of High-Technology Products as a Share of Total Exports, 2018. [Colour figure can be viewed at wileyonlinelibrary.com]



Source: Eurostat.

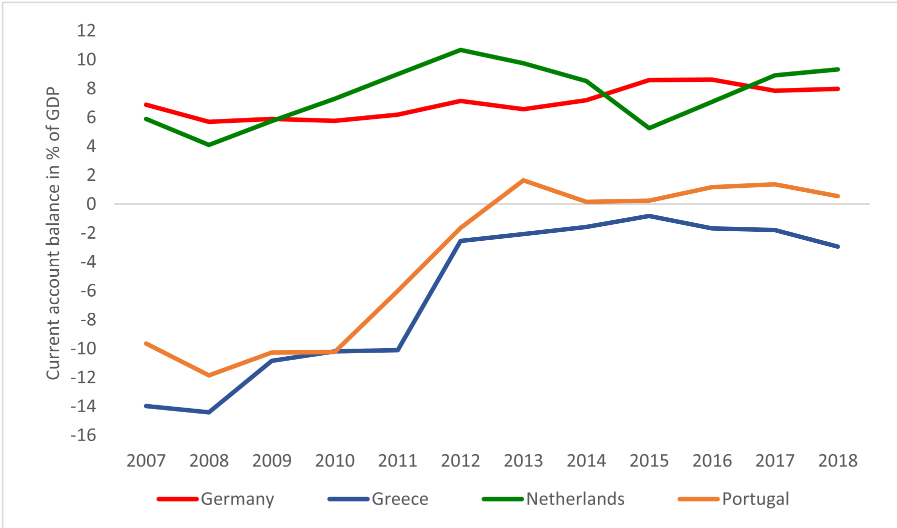
Overall, households' restrained access to credit and the subsequent drop in domestic demand might have paved the way for firms to look beyond the domestic market, resulting in new investment in the supply-side economy to compete in international markets. However, the constrained access to credit also affected firms' capability to invest in upgrading their weak production base, addressing skills shortages and transitioning to higher added-value products. Therefore, the empirical findings do not align with sub-hypothesis h2, suggesting that households' limited access to credit alone was not sufficient to transform the supply-side economy after the crisis.

The Suppression of Domestic Demand and the Stalled Transition to an Export-Led Growth Model

The global financial crisis and externally imposed austerity led to a dramatic decrease in public spending and aggregate demand in both countries. However, the predominant growth coalitions did not favour a new export agenda to facilitate the transition to an export-led growth model. Concurrently, the banking crisis and firms' restrained access to credit constrained investment in the supply-side aspects of the economy. In this subsection, we assess, taking into consideration the refutation of sub-hypotheses h1 and h2, the overarching hypothesis H in the post-crisis era. The objective is to demonstrate the extent to which changes in demand-side policies have transformed the supply-side economy and opened the way for an export-led growth model in the aftermath of the crisis.

Greece and Portugal, based on the rapid decrease in domestic demand, achieved a remarkable current account adjustment. As shown in Figure 8, successive Greek governments reduced the trade deficit from 14% in 2007 to 2.9% of GDP in 2018. Portugal followed a similar trajectory. After two decades, Portuguese exports surpassed imports, transforming a persistent trade deficit into a surplus. After a 9.7% current account deficit

Figure 8: Current Account Balance in Percentage of GDP, 2007–2018. [Colour figure can be viewed at wileyonlinelibrary.com]



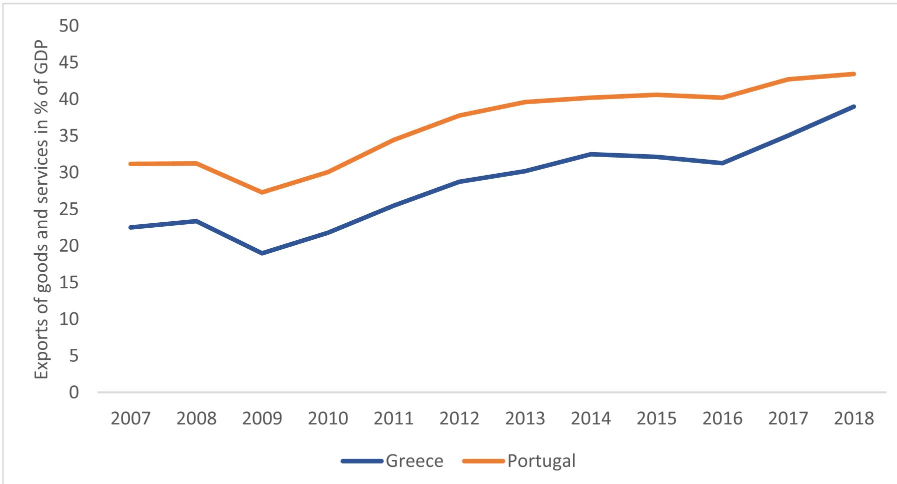
Note: See Figure 5 note.
Source: World Bank.

in 2007, Portugal achieved a surplus of 0.5% of GDP in 2018. Despite both countries achieving a trade adjustment, they have remained significantly below the export-led economies of the Eurozone, such as Germany and the Netherlands, since the crisis.

The adjustment in the current account resulted from economic contraction, leading to reduced purchasing power and imports, rather than indicating a transition to an export-led growth model. As depicted in Figure 9, despite the apparent upward trajectory of exports of goods and services as a percentage of GDP over the reported period, this trend primarily stems from the sharp decline in GDP in both countries rather than indicating a sustainable transition towards dynamic export-led growth. In Greece, the GDP witnessed, according to the World Bank (2015), a significant downturn, plummeting from $318.9 billion in 2007 to $195.68 billion in 2015, nearly a decade after the onset of the crisis. Similarly, Portugal experienced a decline in GDP from $240.5 billion to $199.39 billion over the same period. Although Portugal has outperformed Greece in terms of export performance, neither country has transitioned to an export-led growth model. Moreover, both countries continue to lag significantly behind the export-led economies of the Eurozone. Therefore, changes in demand-side policies seem to have negligible effects on export performance.

Greece's and Portugal's export shares in global trade have also stagnated. According to UNCTAD (2019), Greece's share of global exports constituted 0.17% and 0.2% in 2007 and 2018, respectively, and Portugal's share constituted 0.37% and 0.35% in the same period. The substantial shift in demand-side policies has not facilitated investment to address the supply-side weaknesses in both countries and therefore has not paved the way for the transition to a new export-led growth model.

Figure 9: Exports of Goods and Services in Percentage of GDP, 2007–2018. [Colour figure can be viewed at wileyonlinelibrary.com]



Note: See Figure 5 note.
Source: World Bank.

The global financial crisis and internal devaluation led to fiscal contraction and curtailed domestic demand in Greece and Portugal; however, both economies remained trapped in a suppressed demand-led growth model. The resilience of the growth coalition and the failure to develop a new export agenda, together with restrained access to credit, did not open the way to transforming the supply-side economy. Overall, evidence from Greece and Portugal shows no support for the overarching hypothesis H, as neither sub-hypothesis h1 nor h2 is satisfied, and therefore, demand-side policy reforms have not transformed the supply-side economy in either country since the crisis.

Conclusions

The global financial crisis and internal devaluation have renewed interest in Southern Europe and the capitalist models in the crisis-hit countries. VoC and, more recently, the GM perspective have made important contributions to analysing modern capitalism and offered a rich theoretical and empirical framework in CPE. However, the current literature often presents these accounts as rivals and tends to focus on either the 'supply-side' or 'demand-side' aspects to analyse modern capitalist growth models.

Instead, this article brings the VoC and GM perspectives together and offers an advanced understanding of capitalist diversity and change. It sets the foundations for a systematic analysis of the causal relations between demand-side and supply-side aspects of growth. It makes an important contribution to the current CPE literature by showing the complex ways in which demand-side policy reforms may transform the supply-side aspects of the growth model. It shows that a demand-side policy shift requires two conditions to be satisfied to transform the supply-side aspects of growth: the policy re-orientation of the growth coalition and a dynamic financial sector to facilitate a change in the supply-side economy. Therefore, this article, based on the reconciliation of the VoC and GM approaches, offers a comprehensive understanding of capitalist evolution and change. It opens up new research areas to study the interaction between demand-side and supply-side patterns in various growth models and calls for further research that goes beyond the VoC–GM debate on theorising capitalism. At the empirical level, it shows that before the crisis, the growth coalition policies (sub-hypothesis h1) and access to credit (sub-hypothesis h2) opened the way for the decline of the supply-side economy (overarching hypothesis H) and led to a demand-led growth model in both countries. After the crisis, the resilience of a growth coalition that favoured the pre-crisis growth paradigm (sub-hypothesis h1) and restrained access to credit (sub-hypothesis h2) constrained the transformation of the supply-side economy (overarching hypothesis H), especially the weak production base, the skills shortages and the low added-value exports, which impeded a dynamic export-led growth model in Greece and Portugal.

Greece and Portugal should pursue an alternative growth strategy that would allow them to grow sustainably in the Eurozone. First, both countries should strike a balance between stimulating domestic demand and pursuing policies to upgrade the supply side of the economy. Second, the growth coalitions in both countries should develop modern industrial policies with targeted investments to improve production capabilities, enhance labour skills and upgrade domestic production towards high added-value products. Such an approach would allow both countries to maintain sustainable growth and resilience in the years to come.

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