Geoffrey Garrett/Peter Lange, "Internationalization, Institutions, and Political Change," in Keohane & Milner, eds., *Internationalization and Domestic Politics*

Introduction: Garrett and Lange consider the question: "how and why extant institutions mediate in the relationship between internationally induced changes in the policy preferences of domestic actors, on the one hand, and political outcomes (both policy and institutional change), on the other" (49). They concentrate on two types of institutions: (a) socioeconomic institutions, which organize interests in the private sector, and (b) formal institutions, which aggregate these interests in the public arena and determine the responsiveness of governments to them. Finally, they consider possibilities for endogenous institutional change in different types of polities.

The Model: Garrett and Lange's model has four stages. (Note: The objective of all governments is to retain office, which means that redistributing wealth in favor of the governments core political constituencies dominates concerns about aggregate economic performance.)
First stage: Change in international economic conditions causes changes in the preferences and the power of domestic actors and those changes are affected by the country's position in the international economy (refer to Frieden and Rogowski).
Second stage: Socioeconomic institutions "both condition the distributional policy demands resulting from changes in economic actors' preferences and influence the macroeconomic outcomes associated with different combinations of government policies and international economic conditions." (52). See 'Labor Market Institutions' below.

> *Hypothesis*: "the better existing socioeconomic institutions perform under changing conditions in global markets, the greater is the latitude for governments to maintain policies that further their distributional interests – even in the face of a change in the balance of societal preferences away from these policies." (53)

Third stage: Responsiveness of governments to changes in domestic preferences vary with:

(a) Regime type (the more democratic, the more responsive)
(b) Preference aggregation, or different electoral rules. If productivity is the same across sectors, the outcomes across different rules is the same. But if productivity differs across sectors, then all democratic processes will be biased in favor of the non-traded sector.
(c) The more institutions privilege groups that form the core bases of support for incumbent governments, the stronger are the incentives for governments to maintain policies and institutions that benefit these constituencies.
(d) Veto players (the more veto players, the less responsive)
(e) Bureaucratic autonomy (read: literature on central bank independence following the rational expectations model; generally only apply to tradable sector).

Fourth stage: Governments may have incentives to alter the institutions to reduce the jarring between distributional politics and economic performance. This is only likely when governments are risk-accepting, when conjunctural conditions are favorable, and when time horizons are long, because there are costs to the government of lost support from its core political constituency.

Hypothetical Economy: An economy is divided into a tradables sector and a non-tradables sector. If the economy is dominated by non-tradables and productivity across sectors is the same, then policies that defined the Keynesian welfare state are likely (KWS= heavy reliance on Keynesian demand management, capital controls, industrial policies, substantial public provision of welfare and other social services). Now, the share of output by the tradables sector increases considerably, but employment is slightly larger in the non-tradables sector. What happens depends on the institutional conditions.

Labor Market Institutions: *Hypothesis:* Performance will be better in economies with weak labor institutions or strong and centralized labor institutions. Performance will be weaker where labor market institutions are strong but decentralized.
Explanation: In the tradables sector, the welfare of workers depends on their competitiveness in the global market; a rise in wages means a rise in costs of production, which may make the industry uncompetitive and cause unemployment. An increase in wages in the non-tradables will affect interest rates, inflation, etc., which may be potentially damaging to their international competitiveness. In the non-tradables, the same constraints to not apply so they don't fear losing their jobs so much from pushing up their wages.
Weak labor institutions: Government policy will reflect the preferences of the tradable sector more in the new hypothetical economy. A weakening of the KWS will increase pressures on non-tradable sector workers and reduce their ability to push up wages.
Strong, but uncoordinated labor institutions: Less and less coherent change in economic policies and worse economic performance expected than under weak labor institutions because workers in the non-tradable sector can push up wages.
Strong and coordinated labor institutions: The consequences are less clear, but likely to include wage restraint, compensation for workers in the non-tradable sector, and structural adjustment to move jobs into the tradables sector.

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Formal Political Institutions: See Third Stage under 'The Model.' These five points indicate that an increase in the economic importance of the tradables sector will only lead to a reduction of the KWS if:

(a) political system is democratic
(b) labor unions are weak and decentralized
(c) electoral bias against economically powerful sectors is minimized
(d) political authority is concentrated in a single institution
(e) central bank is independent of the government

A political economy with these conditions does not exist.

Endogenous Institutional Change: See Fourth Stage under 'The Model.'