

Norway in the 1980s: Competitive Adaptation or Structural Crisis? A Comment on Katzenstein's Small-State/Flexible-Adjustment Thesis

Atle Midttun,¹ The Norwegian School of Management

The article comments on Katzenstein's small-state/flexible adjustment thesis on the basis of the recent economic development in Norway. It is argued that the Norwegian case in the 1970s and 1980s provides a quasi-experimental situation where the years before and after the 1986 oil-price fall permit a discussion of some of the limitations of his theory. The article argues that the Katzenstein thesis needs qualifications on at least three points:

- (1) Size and competitive exposure do not always coincide, as assumed in a strong formulation of the thesis.
- (2) A discussion of national competitiveness based on highly aggregated indicators may miss important sectoral differences that can be of crucial importance to the national political economy.
- (3) The question of the adaptive effects of integrative, negotiated and non-polarized styles of policy-making in small states has to be modified.

Because Katzenstein's basic idea seems theoretically sound, and seems to hold up to at least aggregated data, the issue is not rejection, but rather a modification, and an attempt to specify some of the elements that constitute the relevant condition-set.

Scandinavian Political Economy and the Small-State Flexible Adaptation Debate

Scandinavian Political Studies has recently devoted several articles to addressing the issue of flexible adaptation in the Scandinavian economies (Vol. 12, no. 4, 1989). These articles present interesting empirical discussions of recent trends in Scandinavian political economy, and whether the development of these economies can be considered flexible or not.

In the articles on Denmark, Finland and Norway (Andersson 1989, Nielsen & Pedersen 1989, Nielsen 1989, Mjøset 1989), Katzenstein's discussion of small states and flexible adaptation is a central element. Katzenstein's thesis is, however, generally taken as a point of departure for substantive analysis, and not itself explored in any theoretical detail.

This article reverses the research agenda and explores how Scandinavian

Norway in the 1980s: Competitive Adaptation or Structural Crisis? A Comment on Katzenstein's Small-State/Flexible-Adjustment Thesis

Atle Midttun,¹ The Norwegian School of Management

The article comments on Katzenstein's small-state/flexible adjustment thesis on the basis of the recent economic development in Norway. It is argued that the Norwegian case in the 1970s and 1980s provides a quasi-experimental situation where the years before and after the 1986 oil-price fall permit a discussion of some of the limitations of his theory. The article argues that the Katzenstein thesis needs qualifications on at least three points:

- (1) Size and competitive exposure do not always coincide, as assumed in a strong formulation of the thesis.
- (2) A discussion of national competitiveness based on highly aggregated indicators may miss important sectoral differences that can be of crucial importance to the national political economy.
- (3) The question of the adaptive effects of integrative, negotiated and non-polarized styles of policy-making in small states has to be modified.

Because Katzenstein's basic idea seems theoretically sound, and seems to hold up to at least aggregated data, the issue is not rejection, but rather a modification, and an attempt to specify some of the elements that constitute the relevant condition-set.

Scandinavian Political Economy and the Small-State Flexible Adaptation Debate

Scandinavian Political Studies has recently devoted several articles to addressing the issue of flexible adaptation in the Scandinavian economies (Vol. 12, no. 4, 1989). These articles present interesting empirical discussions of recent trends in Scandinavian political economy, and whether the development of these economies can be considered flexible or not.

In the articles on Denmark, Finland and Norway (Andersson 1989, Nielsen & Pedersen 1989, Nielsen 1989, Mjøset 1989), Katzenstein's discussion of small states and flexible adaptation is a central element. Katzenstein's thesis is, however, generally taken as a point of departure for substantive analysis, and not itself explored in any theoretical detail.

This article reverses the research agenda and explores how Scandinavian

economic development can be utilized to shed further light on the Katzenstein thesis.

Small States and Economic Adaptation

It has been argued that the international market exposure and the strategic disadvantage of smallness in negotiations of international terms of trade forces small European market economies to develop patterns of active and flexible adjustment. For large states with sizeable domestic markets where imports and exports play a minor role, adjustment to the external competitive environment seems far less compelling.

The international market exposure of small economies stems from a need on both the export and import side. These countries are faced with the need to export in order to reap advantages of scale and diversification for their industry in international markets. They are also faced with the need to import in order to serve national consumer demands for the breadth of products that domestic industry cannot rationally provide. This line of argumentation is well known from standard economic analyses (Normann 1983).

More recently, however, Katzenstein (1985) has pointed out that the reasons for small states' flexible adaptation to their economic environment is not only economic, but also political and economic in character. The adjustment of small European market economies to meet international competitive forces is – in Katzenstein's view – seen to rely heavily on their political-institutional and political-cultural traditions. Small European countries are, typically, politically well integrated and well developed welfare states where negotiation, rather than polarization, characterizes their policy styles. They generally score high on corporatist policy integration (Schmitter 1981) and low on political polarization.

According to Katzenstein, the turbulent and compelling international environment and relative internal homogeneity of small states seem to have fostered a spirit of political cooperation to counter international challenges in an active but flexible way. Flexible adjustment, in Katzenstein's terms, thus involves active state intervention in the form of incomes policy, a large public sector and generous social welfare expenditures. This, he argues, is a strategy well suited both to adjusting to unforeseen developments and to holding together domestic societies continuously threatened by the external instabilities of international markets.

Katzenstein's thesis that smallness furthers flexible adaptation seems reasonably supported by average data on the economic performance of advanced industrial states throughout the 1960s and 1970s (Katzenstein 1985, Table 8). However, even his own data suggest high variations within both small and large nations in rankings on such indicators as unem-

ployment, GDP growth, inflation and balance of payments, indicating that the main thesis needs considerable qualification.

Katzenstein himself provides an empirical contribution to such a qualification in the form of descriptions of national economic conditions and economic policies. He does not, however, fully sum up the implications of this description for his main thesis. The concluding chapter (Katzenstein 1985, Chapter 5) thus asserts the main argument without much qualification.

This article seeks to qualify the Katzenstein thesis, based on a study of the development of the Norwegian economy in the 1980s. Norwegian development seems to contradict Katzenstein's analysis on a number of points. The Norwegian case in the 1970s and 1980s has given us a quasi-experimental situation where the years before and after the 1986 oil-price fall permit a discussion of some of the limitations of his theory. Because Katzenstein's basic idea seems theoretically sound, and seems to hold up at least to aggregated data, the issue is not rejection, but rather a modification, and an attempt to specify some of the elements that constitute the relevant condition-set.

The Small-State/Flexible-Adaptation Thesis: Three Critical Comments

Katzenstein's core argument is that there are clear differences between small and large European states in their adaptation to the international environment. The large-small dimension for him coincides with distinct profiles both on the political and economic level, and with distinct patterns of international adaptation.

A strong formulation of the Katzenstein thesis has the following logic. Small states are liberal in their market orientations. Because of their small size, they are dependent on world markets and protectionism is not a viable option for them.

Small states are also corporatist in their political orientation. They seek domestic cooperation through corporatist arrangements, through which they seek to smoothen the turbulence created by international markets. Both these factors lead to policies of flexible adjustment by small steps in small states' adaptation to international market forces.

Conversely, large states are protectionist in their market orientations. Katzenstein describes two variants of protectionist policies pursued by large states: the US, *liberal variant* that tends to export the costs of change when traditional market approaches fail by adopting a variety of limited *ad hoc* protectionist policies. The *statist variant*, exemplified by Japan, assumes that the country is endowed with the means and the institutions to preempt the costs of change through policies that pursue the structural transformation of their economies.

Table 1. Core Elements in Katzenstein's Argument.

	Large	Small
political characteristics	polarized	corporatist domestic compensation
market characteristics	protectionist	liberal
patterns of adaptation to international markets	export of costs of change few decisive blows	flexible adjustment small steps

Large states are also polarized in their political orientation. They allow polarized political relations and strong-arm methods with dramatic shifts in policies. Both these factors lead to export of costs of change to the international economy and international market policies characterized by large steps and by 'few decisive blows'.

The central elements in the above argument are schematized in Table 1.

The Norwegian experience of the 1980s indicates that Katzenstein's theory needs modification on at least three points. Firstly, Katzenstein's postulate of a necessary relation between smallness and exposure to international competitive pressure should be treated as a probabilistic rather than as an absolute relation. The experience of countries with territorially based attractive resources, such as for instance petroleum resources in the Norwegian case, is that they can use them to soften international competitive pressures. This may allow them considerable freedom to pursue economic policies resembling those that Katzenstein attributes to large states. Thus, Katzenstein's assumption of a market dynamic forcing small states to flexible adaptation needs qualification, or a more explicit *ceteris paribus* clause.

Secondly, continuing this line of argument, it seems necessary to differentiate between sectors of the economy when evaluating economic adaptation. A small country may be 'large' in one sector and 'smaller' in others. Hence the problems of adaptation characterizing large and small states may be present in one country simultaneously and create internal interaction effects that are not well handled in Katzenstein's model. This makes it particularly important to focus on the interplay between sectors with different levels of competitiveness, and with different degrees of sheltering against international market forces.

Thirdly, there is reason to question Katzenstein's evaluation of a small state's corporatist institutions and arrangements. He is undoubtedly correct in his characterization of the political relations of small states as dominantly corporatist. His analysis here corresponds with a number of others, for example Schmitter (1981). However, his strong expectations of the positive

implications of neocorporatist relations and institutions for economic adaptation again need serious qualification.

The Norwegian experience shows that under conditions of super-profits from one or more sectors of the economy, corporatist institutions, at least of the solidaristic type, may easily lead to internal redistribution and general wage expectations that far exceed the capacity of other parts of the economy. Corporatist institutions and expectations based on solidaristic negotiated regimes may thus move the economy as a whole away from, rather than towards, international competitiveness. The following sections discuss each of the three objections in further detail.

Smallness and Competitive Exposure

As a small open economy Norway shares, with other small European states, the need to obtain advantages of scale and diversification for its industry in international markets (Normann 1983). However, the large size of Norway's energy-based 'ground rent'² sets it in a special position. The comparative advantage of cheap, abundant hydropower resources has given Norway a stable basis for industrial expansion in electrometal, electrometallurgical, electrochemical and paper and pulp industries for several decades (Hodne 1975). The oligopolized international oil market has also until recently given the country a huge economic surplus from its oil production.

The exclusive character of its resource endowments and the oligopolistic character of international markets have sheltered the ground-rent sectors from normal competition, and have allowed the country to reap super-profits without relying on competitive skills.

Through various transfer mechanisms, the existence of the ground-rent economy has also affected economic adaptation in other industrial sectors. The surplus from hydropower and oil has allowed Norway to cushion other sectors of its economy from international competition more persistently than most other small countries.

The cushioning effect became most pronounced with the development of the petroleum sector. From the mid-1970s oil and gas production became a major source of export, passing the entire industrial sector in importance by the early 1980s, when petroleum and gas alone stood for over a third of the Norwegian export volume (see Table 2).

In periods of continuously high oil profits, oil and gas export has been able to compensate for both the decline of the merchant marine as well as for the poor performance of industrial exports, leaving the country with a dangerously one-sided petro-economy. The Norwegian economy has come to rely more heavily on ground rent than ever before, and experienced the dramatic consequences when the oil prices fell from about \$30 to less than

Table 2. Sector Shares of Total Norwegian Export (%)

	Agr./Fish	Petro. & Gas	Oil/Mining (without P & G)	Manuf.	El/Gas	Constr.	Trade/ Hotel	Transp.	Finance	Service
1962	3.00	0.00	1.75	43.68	0.07	0.00	1.80	48.53	0.15	1.01
1965	2.19	0.00	1.53	48.06	0.25	0.00	1.63	45.77	0.14	0.43
1968	1.31	0.00	1.70	47.46	0.27	0.13	1.66	46.40	0.13	0.94
1971	1.09	0.06	1.70	49.72	0.25	0.00	2.01	44.79	0.15	0.24
1974	0.91	0.93	2.05	54.19	0.63	0.35	1.61	38.71	0.36	0.27
1977	0.76	12.01	1.61	52.70	0.18	1.07	1.20	29.60	0.50	0.38
1980	0.72	33.13	0.86	37.58	0.21	0.41	0.95	25.39	0.47	0.29
1983	0.92	37.85	0.77	35.81	0.50	0.97	0.87	20.85	0.89	0.58
1986	1.61	31.05	0.86	39.88	0.11	0.40	0.85	22.91	1.69	0.64

Source: Norwegian Central Bureau of Statistics.
Export statistics and national accounts

Table 3. Oil-Price Development (NOK/tonnes).

1980	1229
1981	1518
1982	1543
1983	1587
1984	1720
1985	1720
1986	806
1987	889
1988	700

Source: Quarterly Oil and Gas statistics, Central Bureau of Statistics of Norway, 2nd quarter.

half that figure in 1986 (see Table 3). The following loss of oil revenue leads up to the present recession, the deepest experienced since the 1930s in terms of unemployment. Rather than incremental flexible adaptation, the Norwegian adjustment to international competition in the 1970s and the 1980s has, therefore, been characterized by ground-rent-based expansionism and a severe economic recession when oil prices dropped. The cushioning effect of the ground-rent sectors, when energy prices were high, has led to a structural conservatism in the rest of the economy resembling the policies of larger nations with limited external market exposure. This has made the adjustment process more dramatic once the ground-rent surplus declined, and Norway regained its small-state status.

Sectoral Differentiation and Economic Adaptation

Further elaboration on the maladaptive effects of the oil-rent surplus on the industrial economy leads to the second criticism of the Katzenstein thesis, its lack of differentiation between different sectors of the economy when evaluating economic adaptation.

Crudely speaking, we may conceive of the Norwegian economy as a dual economy, with the ground-rent-based petroleum sector and energy-intensive electrometallurgical, electrochemical and paper and pulp industries on one side, and the rest of the economy on the other. We are then leaving out of account the shipping sector, which may deserve a category of its own.

The dual economy is by no means a recent phenomenon in Norway, but goes back to the turn of the century. Since then Norway has on the one hand had a ground-rent-based large-scale industry exploiting cheap hydroelectricity directed at international markets, and on the other hand small and medium-sized industry primarily oriented towards the domestic

market (Hodne 1975, Jess Olsen 1980). In the 1970s and 1980s, however, the duality of the Norwegian economy has been reinforced by the much larger, and less industrially dispersed petroleum economy. Whereas the need to export hydropower through industrial goods had served to integrate hydro-rent into the Norwegian industrial economy, petro ground rent could be harvested by direct export of petroleum products with relatively less stimulation of domestic industry. Except for the considerable deliveries in construction of oil rigs and other petroleum-producing facilities, the petro sector has become a 'money machine' pouring ground rent into Norwegian society.

Patterns of International Competitiveness

The Norwegian dual economy is clearly reflected in two distinct patterns of industrial competitiveness. On the one hand, ground-rent industries, such as basic metals, paper and pulp, and electrochemicals where access to cheap hydropower is a core element, have largely been able to maintain their competitive position *vis-à-vis* international markets throughout the last decade. On the other hand, the non-ground-rent sectors have been losing domestic market share.

The change is particularly dramatic in textiles, with an increase in import shares of more than 100 percent over the past decade. But the increase is also considerable for wood and mineral production, as well as for production of fabricated metal. As can be seen from Table 4, the average loss of domestic market shares for the non-ground-rent sectors over the last decade has been dramatic. The unweighted average of import shares for these sectors has risen from 46 percent to 82 percent.

Within the ground-rent sector of industry – consisting of traditional Norwegian export industries like basic metals, paper and electrochemicals – where Norway holds sizeable parts of the European and world markets, import shares have remained fairly constant. The relative import increase in these sectors has only been about 6 percent from 37 percent to 43 percent since the late 1970s.

Export shares have remained comparatively more stable, with some increases in textiles and chemicals, stable shares for wood, basic metals and fabricated metals, and some decrease in paper (see Table 5). The net domestic shifts in the import/export balance for Norwegian industry over the past ten years are therefore primarily determined by loss of domestic markets and not by loss of markets abroad.

However, the table also reveals the export differences between the two sectors of the Norwegian economy. Whereas the ground-rent-based sectors have an average export rate of close to 50 percent of domestic production, the comparable ratio for the rest of industry is below 20 percent.

In the face of the increasing internationalization of industrial markets,

Table 4. Import Shares for Norwegian Industrial Sectors Relative to Gross Domestic Sector Production (%).

	1978	1979	1980	1981	1982	1983	1984	1985	1986
Food etc. (SIC 31)	9.06	9.77	10.19	8.74	7.79	7.94	8.25	8.79	9.25
Textiles etc. (SIC 32)	133.60	141.82	149.06	152.19	170.53	188.35	204.61	236.17	269.26
Wood Products (SIC 33)	17.59	18.53	19.73	20.11	22.76	25.29	27.40	30.94	35.74
Paper Products (SIC 34)	13.71	15.47	16.34	14.82	15.31	14.96	15.21	15.80	16.32
Chemicals (SIC 35)	55.89	49.43	59.58	56.19	60.38	56.23	55.30	57.48	70.79
Mineral Products (SIC 36)	26.20	26.32	28.09	27.15	29.74	30.89	34.63	35.17	37.86
Basic Metals (SIC 37)	41.29	39.15	46.10	43.89	47.30	35.51	35.94	40.50	43.25
Fabricated Metal (SIC 38)	46.50	46.57	44.41	50.91	56.64	56.78	53.01	54.38	56.98
Average non-ground-rent sect.	46.59	48.60	50.30	51.82	57.49	61.85	65.58	73.09	81.80
Average ground-rent sect.	36.9	34.68	40.67	38.30	40.99	35.57	35.48	37.93	43.25

Source: Norwegian Bureau of Statistics.
 Import statistics and national accounts.

Table 5. Export Shares for Norwegian Industrial Sectors Relative to Gross Domestic Sector Production (%).

	1978	1979	1980	1981	1982	1983	1984	1985	1986
Food etc. (SIC 31)	19.17	22.15	19.05	22.30	17.06	18.92	20.30	16.60	15.22
Textiles etc. (SIC 32)	21.12	24.25	24.84	24.10	25.19	26.31	25.47	29.59	29.79
Wood Products (SIC 33)	6.48	8.48	8.31	6.14	6.04	7.46	8.87	6.97	6.37
Paper Products (SIC 34)	23.75	26.30	26.42	24.71	23.83	24.01	24.92	24.88	22.29
Chemicals (SIC 35)	33.78	32.69	34.61	38.40	39.00	38.58	38.86	39.79	41.33
Mineral Products (SIC 36)	9.13	10.51	10.70	9.55	8.50	8.33	10.06	9.32	8.15
Basic Metals (SIC 37)	89.48	80.58	77.55	78.39	79.39	82.49	82.83	80.27	74.07
Fabricated Metal (SIC 38)	32.72	31.89	29.36	29.42	33.26	34.89	33.61	35.37	32.77
Average, non-ground-rent sect.	17.24	19.46	18.45	18.32	18.01	19.18	19.66	19.57	18.46
Average, ground-rent sect.	49.00	46.52	46.19	47.17	47.41	48.36	48.87	48.31	45.90

Source: Norwegian Bureau of Statistics.
Export statistics and national accounts.

Norwegian industry outside the ground-rent sectors has, with some notable exceptions, been losing out. Industry has thus had to fall back on ground-rent-based production where Norwegian companies have had sufficient size, competence and international networks to survive in more internationalized market contexts.

This development has probably been stimulated by the price and wage effects of the petro-economy. As noted in the previous section, oil has come to play a major role in the Norwegian economy (20 percent of BNP), with a corresponding potential for buffering domestic industry against external market forces.

From Industrial Producer to Market Place for International Products

The weak competitiveness of Norwegian industry in the 1970s and 1980s is also reflected in foreign investments in the Norwegian economy. Since the mid-1970s the relative size of foreign investments in industrial and other sectors has changed to the advantage of the latter (Midttun et al. 1987). Whereas the vast majority of foreign investments in the 1960s went to the industrial sector, foreign capital now pours increasingly into other parts of the economy (see Figure 1). One of the effects of the inflated petroeconomy seems to have been the transformation of the Norwegian domestic economy into an attractive market place for high-priced foreign commodities and away from an industrial producer.

The shift of foreign investments away from industry has also been a shift away from export orientation. An increasing share of investments now goes into sheltered areas of the economy like trade, transport and finance, and into areas mainly exposed to domestic competition (Midttun et al. 1987.)³ As shown in Figure 2, the share of total foreign investment in the Norwegian economy in sectors exposed to international competition fell from 20.7 percent to 11.2 percent from 1977 to 1983.

The revenue from the oil economy has, because of the spillover to other sectors of the economy, resulted in high income and price levels that made Norway an attractive market place for international products, as long as the oil surplus continued to obtain. The parallel weakening of the country's export base and the loss of market shares by domestic industry can hardly be judged as a competitive adaptation, and must rather be seen as a dangerously one-sided addiction to oil revenue.

This unbalance in the domestic economy remains hidden, and will not appear in data of the aggregated Norwegian economy as long as the oil surplus continues to flow. Hence our argument for a more detailed sectoral analysis before assessing a country's competitive adaptation.

The Norwegian pattern of adaptation to the international economy in the 1980s is clearly far away from the flexible incrementalism that according

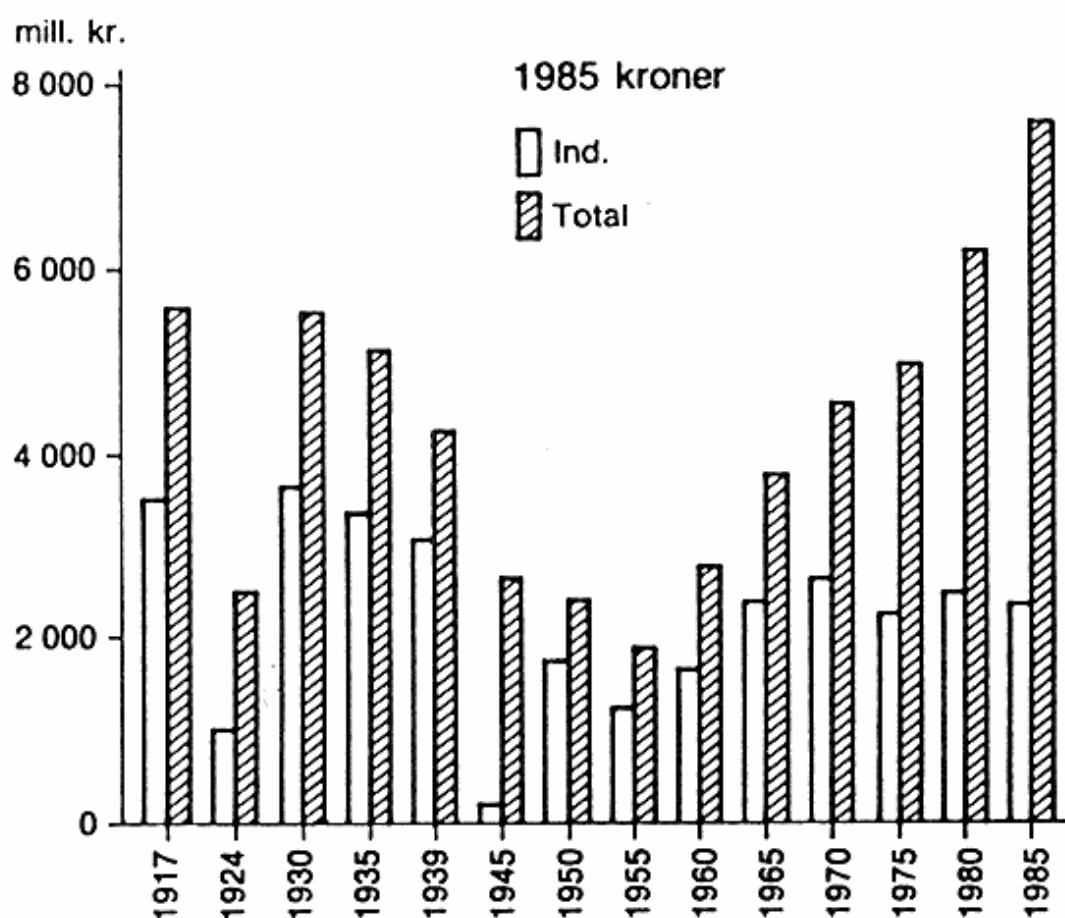


Fig. 1. Foreign Investments in Norway 1917-85. *Source:* Midttun et al. (1987) based on data from the Norwegian Central Bureau of Statistics (special runs).

to Katzenstein characterizes other small European states. It illustrates that Norway's ground-rent-based economy has both advantages and disadvantages compared to other small European market economies. The advantages are, among others:

- (1) The creation of a number of internationally oriented Norwegian companies, with size and competence to participate fully in the international economy.
- (2) Extensive exports and a decisive contribution to the national trade balance.
- (3) The accumulation of capital to finance large-scale international operations.
- (4) The creation of jobs and industrial activity in regions with few employment alternatives.

However, from the point of view of industrial adaptation in the non-ground-rent sectors of the economy, there are also serious disadvantages:

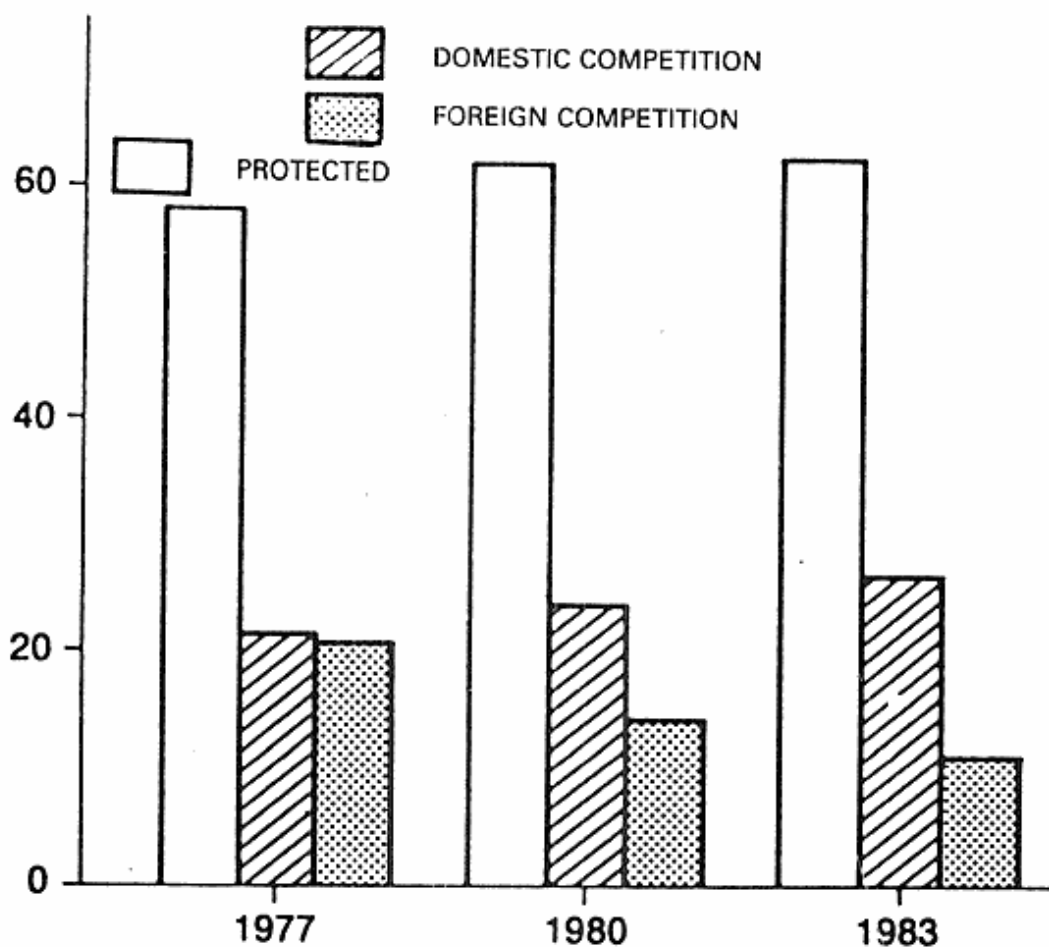


Fig. 2. Foreign Investment in the Norwegian Economy According to Degree of Market Protection.⁵ Source: Midttun et al. (1987) based on data from the Norwegian Central Bureau of Statistics (special runs).

- (1) The extensive profits and the high incomes from the ground-rent sectors have tended to spread similar expectations to other sectors of the economy, creating a price/cost development that is a serious handicap for Norwegian industry.
- (2) The combination of ground-rent incomes and state ownership of major enterprises in the ground-rent sectors has provided the state with considerable freedom in integrating political and economic goals. Because of its rich resource endowments, Norway has lacked the economic and political motivation that has pushed a number of other economies to pursue industrial restructuring. Through various state subsidies, it has been possible to secure the operation of a number of industries that are not competitive by international standards.

Small States and Neocorporatist Institutions: Are They Always Beneficial?

Katzenstein's contribution to the discussion of competitiveness lies in his coupling of economic and political factors into one consistent line of argumentation. We here recall his main argument: that corporatist institutions are an essential part in shaping the flexible adaptation of small nations to international markets, because they serve to integrate labour, business and government into firm, evolving, collaborative arrangements. The corporatist style of national policy-making, he claims, allows for relatively stable but flexible domestic policy responses in the face of a turbulent and uncontrollable market environment.

Norway definitely fits Katzenstein's neocorporatist characterization. It shares characteristic sociopolitical features such as non-polarized political relations, advanced incomes policies, a large public sector and generous social welfare expenditures. In fact, Norway fits this characterization prototypically, ranking, for instance, as no. 2 on Schmitter's corporatism scale (Schmitter 1981). On the basis of Katzenstein's model, we would therefore expect that Norway, because of its political decision-making system, could lead to strategies of active flexible adaptation. Under the surplus period of the Norwegian ground-rent economy, however, these same institutions and political traditions have led to extensive subsidization and policies of industrial conservatism.

For both the hydro and the oil sectors, the 'harvesting' of ground rent has been conceived as a legitimate collective right of Norwegian society, as one would expect in a solidaristically oriented neocorporatist country. One precondition for the collective acquisition of ground rent in Norway has been state ownership of the means of production combined with a detailed licensing and regulation system.

In the hydropower sector, collective acquisition has been exercised through exclusive state and municipal ownership over hydro-resources, and considerable state ownership in the electrometallurgical and electrochemical industries. In the new offshore oil sector, collective interests have been taken care of by the state, both through an elaborate concession system and the direct participation of the state oil company, Statoil.

Under a period when centralized corporatist policy-making came into question in several other countries, Norwegian oil revenue secured its survival under conservative/liberal and labour governments alike. Norway during this period developed a special form of super-corporatism based on extensive transfers of state revenue (Andersen & Midttun 1989).

Hence, when most other European countries in the late 1970s and early 1980s were struggling to restructure their industrial economy, Norwegian corporatist redistribution was still left undisturbed, and the country could

maintain ambitious programmes of health-care services, regional support, and direct and indirect subsidies to industry, as well as a growth in wages far beyond that of its competitors.

The abolition of foreign trade problems and hence a compelling pressure for industrial restructuring, as well as the price and wage spillover from the plentiful harvesting of ground rent, has put the Norwegian economy in a state of continuous boom throughout the early and middle 1980s. In this situation domestic markets as well as domestic policy-making served more as an amplifier of structural misfit than as a stimulator to internationally competitive industrial restructuring.

The reliance on wide redistribution of oil revenue finally led the Norwegian economy into a severe recession in 1987, after the fall in oil prices from around \$30 per barrel to less than half of that figure. The soaring of the oil surplus forced the nation to rely on other parts of the economy. These parts were, however, severely hampered by uncompetitive price and wage levels generated by the redistributive programmes and wage drift under the oil boom.

Price and Wage Developments, the Spillover from the Oil Surplus

Cushioned by the oil economy, domestic labour and commodity markets responded to the oil revenue with a boom-like expansion. A relatively restrictive central wage policy was undermined by increasing wage drift. In the mid-1980s as much as 70 to 80 percent of the wage increase for some groups came from local bargaining (Andersen & Midttun 1989).

The result has been structural conservatism and an increasing competitive gap. The annual increase in Norwegian wages throughout the 1980s has been much higher than for its trading partners, which has led to a considerable wage gap during the 1980s (Figure 3).

Public decision-making added to this inflation and structure-preserving development by supporting wide subsidization of industrial and regional redistribution policies. Major private companies were saved by public transfer of considerable subsidies and credit guarantees, and state companies received extensive capital transfers.

The Norwegian wage development must therefore also be seen against the extensive increase in the Norwegian cost of living. Compared to major trading partners like the other Scandinavian countries, Great Britain and West Germany, the rise in Norwegian costs has been extensive (Figure 4). The only country coming close to Norway is Sweden, but Swedish cost development, although higher than that of Norway in 1982 to 1985, has not been as stable, and Norway therefore comes out highest when the whole period is considered.

The Norwegian case illustrates that the neocorporatist, integrated and

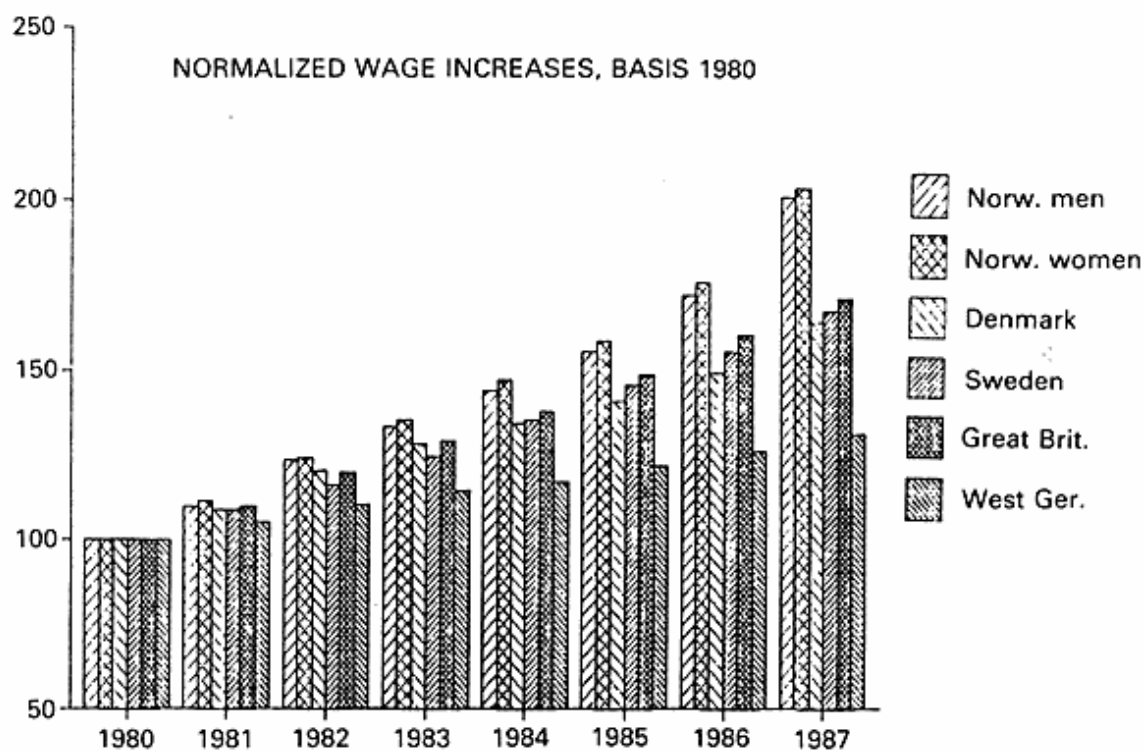
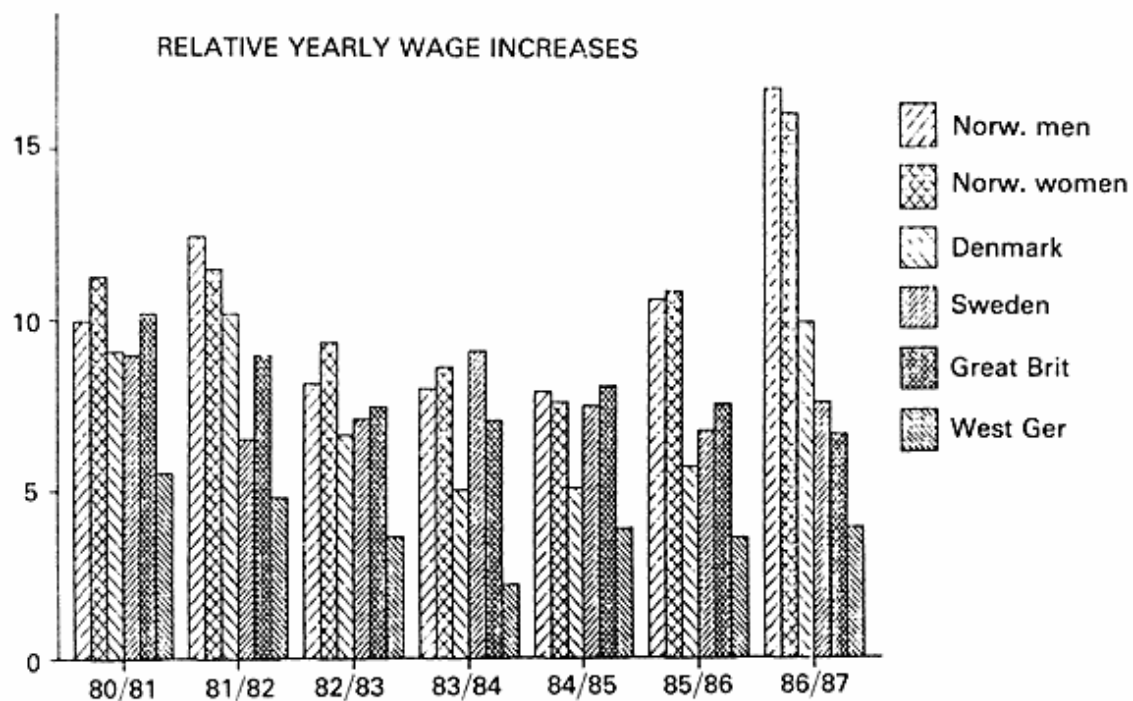


Fig. 3. Relative Yearly Wage Increases and Cumulated Wage Differences for Norway and Selected Trading Partners. Sources: Wage and price statistics, Confederation of Norwegian Business and Industry and the Norwegian Central Bureau of Statistics.

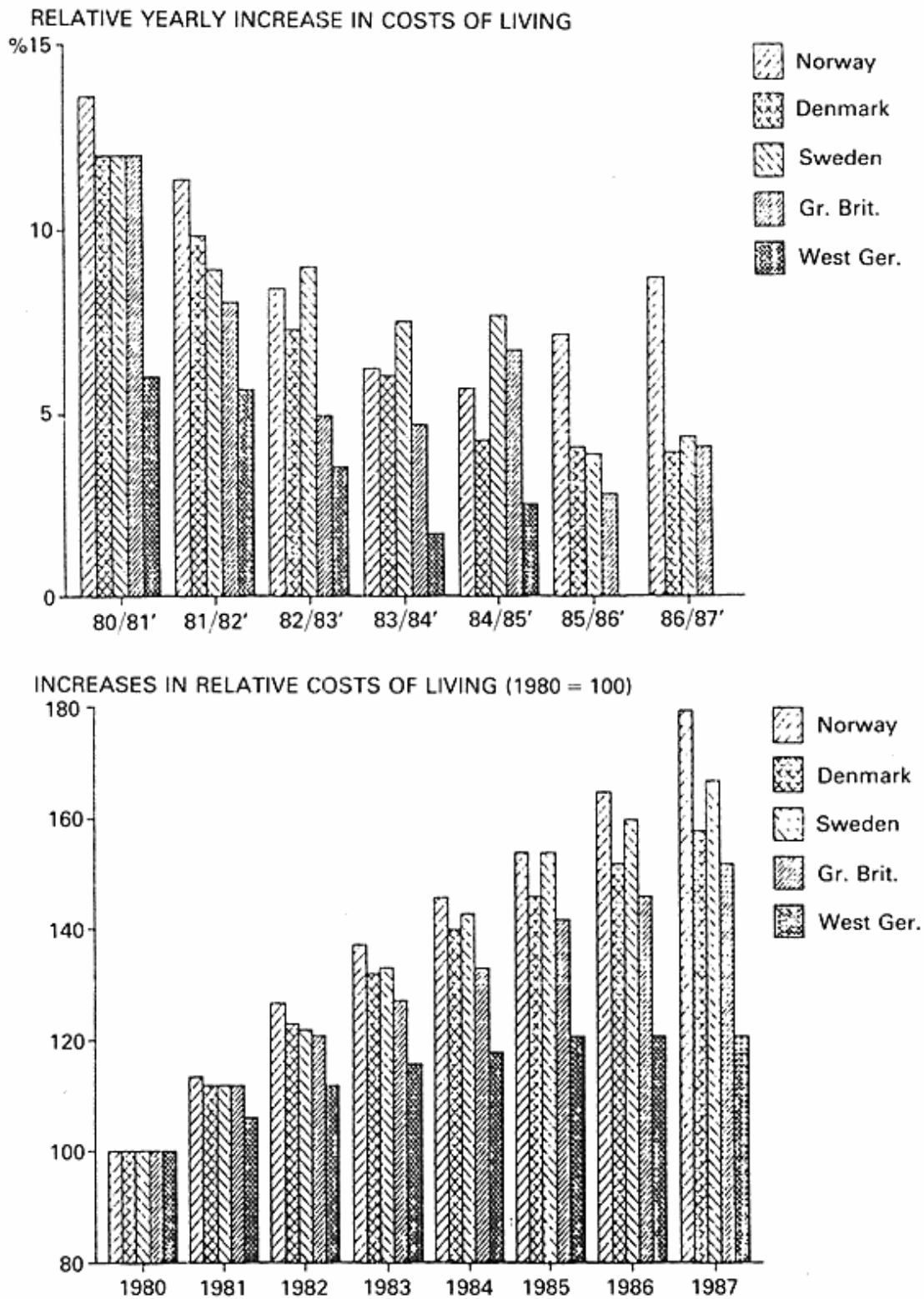


Fig. 4. Relative Yearly Increases in Living Costs, and Cumulated Living Cost Differences for Norway and Selected Trading Partners. Sources: Wage and price statistics, Confederation of Norwegian Business and Industry and the Norwegian Central Bureau of Statistics.

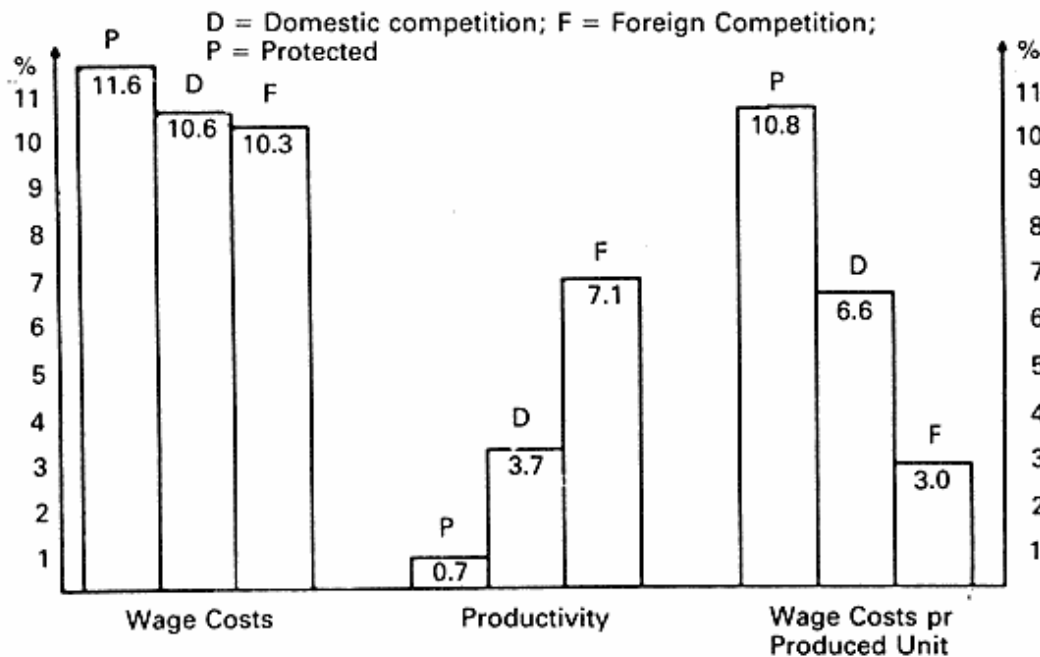


Fig. 5. Wage Costs and Productivity in Norwegian Industry, 1983-87 (average % change/year). Sources: OECD, IMF and the Norwegian Central Bureau of Statistics.

non-polarized policy relations are in themselves no guarantee for flexible adaptation to international market relations. Under ground-rent affluence these policy relations and institutional traditions have become channels for redistribution with the effect of increasing wage transfers to sectors of the economy that are not exposed to international competition (see Figure 5). The structural implications when the surplus disappears have largely been neglected.

Small States, Flexibility and the Double Bind of the Dual Economy

The Norwegian case in the 1970s and 1980s has given us a quasi-experimental situation where the years before and after the 1986 oil-price fall allows a critical test of some aspects of Katzenstein's thesis on small states and flexible adaptation. The previous discussion has shown the need to modify the Katzenstein thesis, at least in its strong formulation, on three points.

Firstly, competitive exposure and size do not always coincide. Although Katzenstein probably argues convincingly for coupling smallness and flexible adaptation as a general rule, this does not hold *mutatis mutandis*. The Norwegian pattern of adaptation to international market forces in this period has been one of dramatic shifts from boom to crisis, rather than

the flexible incremental adaptation predicted by the small-state flexible-adaptation thesis. A further development of this model needs a closer specification of the relevant condition set, one element obviously being control for sizeable ground-rent surplus.

Secondly, the Norwegian experience in our opinion highlights the need for a careful sectoral evaluation of competitiveness. When the Norwegian case is discussed on the basis of nationally aggregated indicators, as in Katzenstein's model, the disadaptive effect for the main bulk of the industrial economy of 'over adaptation' in one sector is missed, or grossly underestimated.

In the early and mid-1980s oil revenues led to stable growth in a period when large parts of the Western economy experienced stagnating economic development. The soaring of oil ground rent following the dramatic fall in oil prices since 1986, however, revealed that the habituation to a stable ground-rent income had left large parts of the economy internationally uncompetitive. The cushioning effect of the petro-economy in a period of high oil prices has—as shown in preceding sections—delayed the structural adaptation of the rest of the economy, resulting in a competitive gap that inevitably led to a crisis once the cushion was taken away.

The third field where Katzenstein's thesis needs to be explicitly modified is on the question of the adaptive effects of corporatism. Again, the adaptive effects of the integrative, negotiated and non-polarized style of policy-making in small states seem to be highly contingent on external competitive pressure.

The Norwegian experience indicates how a strong welfare state with extensive corporatist intermediation has, against a background of ground-rent affluence, served as a means for redistribution, rather than as a tool for securing the long-run competitiveness of the total Norwegian economy.

Democratic-corporatist governance, with extensive participation of organizations in all phases of policy-making (J. P. Olsen 1983), has itself more easily facilitated widely dispersed redistribution than it has strategies of selective priority aimed at facilitating industrial competitiveness and adaptation. The cooperative mode of policy-making rooted in both the corporative-functional and territorial-electoral channels seems to lead to the avoidance of polarizing political choices, such as a structure-transforming industrial policy.

The compelling presence of an international competitive challenge, therefore, seems to be a prerequisite for forcing an advanced welfare state with corporatist decision-making to employ its organizational and integrative power to further competitively oriented, industrial policy goals.

Despite these critical comments, however, I still consider Katzenstein's thesis to be basically plausible, in a weaker, probabilistic formulation. The previous discussion should, therefore, be understood as an attempt to

specify the relevant conditions for the validity of the thesis, rather than an attempt to falsify it. Some of these conditions are already included in Katzenstein's broad institutional description, but their relation to his main thesis remains mostly implicit, and needs to be more explicitly brought out.

NOTES

1. I am grateful to Cheng Yat Yiu for assistance with the data compilation.
2. By 'ground rent' we here simply refer to super-profits (above average profits) harvested through control over territorially based resources.
3. The distinctions between sheltered, export-competing and import-competing activities are based on a typology used by the Norwegian Central Bureau of Statistics. For details see standard industrial classification issues (as no. 9 in the series Manuals from the Central Bureau of Statistics).

REFERENCES

- Andersen, S. S. & Midttun, A. 1989. 'The Articulation of Capital Interests in Norway', *Research Report, European University Institute* (Florence).
- Andersson, J. O. 1989. 'Controlled Restructuring in Finland?' *Scandinavian Political Studies* 12 (4).
- Hodne, F. 1975. *An Economic History of Norway 1815-1970*. Bergen: Tapir.
- Katzenstein, P. J. 1985. *Small States in World Markets*. Ithaca: Cornell University Press.
- Midttun, A., Noreng, Ö. & Nygaard, A. 1987. *Foreign Investments in Norwegian Industry* (in Norwegian). Oslo: Tano.
- Midttun, A. 1988. 'The Negotiated Political Economy of a Heavy Industrial Sector: The Norwegian Hydropower Complex in the 1970s and 1980s', *Scandinavian Political Studies* 11 (2).
- Mjøset, L. 1989. 'Norway's Full-Employment Oil Economy - Flexible Adjustment or Paralyzing Rigidities?' *Scandinavian Political Studies* 12 (4).
- Nielsen, K. & Pedersen, O. K. 1989. 'Is Small Still Flexible? - An Evaluation of Recent Trends in Danish Politics'. *Scandinavian Political Studies* 12 (4).
- Nielsen, K. 1989. 'Flexible Adjustment and Political Stability: The Terms of the Debate'. *Scandinavian Political Studies* 12 (4).
- Normann, V. 1983. *A Small Open Economy* (in Norwegian). Bergen: Norwegian University Press.
- OED (Ministry of Petroleum and Industry) 1986. *Facts about the Norwegian Oil Sector*.
- Olsen, J. P. 1983. *Organized Democracy*. Bergen: Norwegian University Press.
- Olsen, O. J. 1980. *Industripolitik i Danmark, Norge og Sverige*. Copenhagen: Paludan.
- Norwegian Central Bureau of Statistics: *National Accounts and Export/Import Statistics*. NOU (1982). 'Energy Intensive Industry. Consequences of Increased Energy Prices' (in Norwegian), *Norwegian Public Research Series* No. 49.
- Porter, M. E. 1986. 'Changing Patterns of International Competition', *California Management Review* 28 (2).
- Schmitter, P. 1981. 'Interest Mediation and Regime Governability in Contemporary Western Europe and North America', in Berger S., ed, *Organizing Interests in Western Europe*. Cambridge: Cambridge University Press.
- Schmitter, P. & Lembruch, G. (eds.) 1979. *Trends towards Corporatist Intermediation*, *Contemporary Political Sociology* Vol. 1. London: Sage.

specify the relevant conditions for the validity of the thesis, rather than an attempt to falsify it. Some of these conditions are already included in Katzenstein's broad institutional description, but their relation to his main thesis remains mostly implicit, and needs to be more explicitly brought out.

NOTES

1. I am grateful to Cheng Yat Yiu for assistance with the data compilation.
2. By 'ground rent' we here simply refer to super-profits (above average profits) harvested through control over territorially based resources.
3. The distinctions between sheltered, export-competing and import-competing activities are based on a typology used by the Norwegian Central Bureau of Statistics. For details see standard industrial classification issues (as no. 9 in the series Manuals from the Central Bureau of Statistics).

REFERENCES

- Andersen, S. S. & Midttun, A. 1989. 'The Articulation of Capital Interests in Norway', *Research Report, European University Institute* (Florence).
- Andersson, J. O. 1989. 'Controlled Restructuring in Finland?' *Scandinavian Political Studies* 12 (4).
- Hodne, F. 1975. *An Economic History of Norway 1815-1970*. Bergen: Tapir.
- Katzenstein, P. J. 1985. *Small States in World Markets*. Ithaca: Cornell University Press.
- Midttun, A., Noreng, Ö. & Nygaard, A. 1987. *Foreign Investments in Norwegian Industry* (in Norwegian). Oslo: Tano.
- Midttun, A. 1988. 'The Negotiated Political Economy of a Heavy Industrial Sector: The Norwegian Hydropower Complex in the 1970s and 1980s', *Scandinavian Political Studies* 11 (2).
- Mjøset, L. 1989. 'Norway's Full-Employment Oil Economy - Flexible Adjustment or Paralyzing Rigidities?' *Scandinavian Political Studies* 12 (4).
- Nielsen, K. & Pedersen, O. K. 1989. 'Is Small Still Flexible? - An Evaluation of Recent Trends in Danish Politics'. *Scandinavian Political Studies* 12 (4).
- Nielsen, K. 1989. 'Flexible Adjustment and Political Stability: The Terms of the Debate'. *Scandinavian Political Studies* 12 (4).
- Normann, V. 1983. *A Small Open Economy* (in Norwegian). Bergen: Norwegian University Press.
- OED (Ministry of Petroleum and Industry) 1986. *Facts about the Norwegian Oil Sector*.
- Olsen, J. P. 1983. *Organized Democracy*. Bergen: Norwegian University Press.
- Olsen, O. J. 1980. *Industripolitik i Danmark, Norge og Sverige*. Copenhagen: Paludan.
- Norwegian Central Bureau of Statistics: *National Accounts and Export/Import Statistics*. NOU (1982). 'Energy Intensive Industry. Consequences of Increased Energy Prices' (in Norwegian), *Norwegian Public Research Series* No. 49.
- Porter, M. E. 1986. 'Changing Patterns of International Competition', *California Management Review* 28 (2).
- Schmitter, P. 1981. 'Interest Mediation and Regime Governability in Contemporary Western Europe and North America', in Berger S., ed, *Organizing Interests in Western Europe*. Cambridge: Cambridge University Press.
- Schmitter, P. & Lembruch, G. (eds.) 1979. *Trends towards Corporatist Intermediation*, *Contemporary Political Sociology* Vol. 1. London: Sage.