

§ Contesting Deregulation §

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CONTESTING DEREGULATION

Debates, Practices and Developments in the West since the 1970s

Edited by Knud Andresen and Stefan Müller



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CHAPTER 2

Continuity and Change in Germany's Social Market Economy

A Matter of Economic Style?

ALEXANDER EBNER

Introduction

Recent discussions in the research strand of comparative capitalism have reconsidered the matter of institutional change in distinct varieties of capitalism by highlighting the aspect of ideas and discourses. The German variety of capitalism, and its politico-economic paradigm of the social market economy, provides a particularly relevant case in point. In outlining this case, the first section of this chapter discusses key components of the German variety of capitalism, in particular its system of production and related complementarities. The second section addresses the corresponding dynamics of continuity and change. It outlines policy-related efforts at institutional reform that have been shifting various institutional and structural components of the German model while confirming its basic rationale of combined market and non-market coordination. In examining the corresponding dimension of ideas and discourse, the third section explores the concept of the social market economy and its intellectual evolution in terms of the notion of economic style, as put forward most prominently by Alfred Müller-Armack.

Varieties of Capitalism and the Problem of Institutional Change

The comparative analysis of capitalist market economies perceives capitalism as a system of socio-economic interactions within an institutional order, which takes different forms at different times and in different places. This broad perspective of comparative capitalism usually proceeds by comparing national institutional configurations that define comparative advantages for firms and industries.¹ The ‘varieties of capitalism’ approach has emerged as a potent line of reasoning in these endeavours. It undertakes a firm-centred analysis of micro-behaviour in the exploration of national types of capitalist development, approached in terms of the institutional foundations of competitive advantage, which determine firms’ strategies. These include the systems of finance, corporate governance, industrial relations, education and training, and inter-firm relations. In this institutional context, firms face coordination problems in their relationships with other firms and agents, which are reflected in the level of transaction costs. Two ‘ideal types’ of capitalism are differentiated: liberal market economies with a dominant pattern of market coordination through investment in transferable assets, and coordinated market economies with a dominant pattern of strategic coordination through investment in specific assets.²

In the related firm-centred perspective, liberal types of capitalist economies such as the United States share the market-oriented characteristics of short-term company finance, deregulated labour markets, general education and strong inter-company competition. In coordinated economies such as Germany, firms’ strategic behaviour is coordinated to a much larger extent through non-market mechanisms, characterized by long-term company finance, cooperative industrial relations, high levels of firm-specific vocational training and inter-firm cooperation in technology and standardization, framed by industry associations. Liberal market economies exhibit advantages in radical innovation, due to their flexible institutional setting that is more conducive to entrepreneurial start-ups and their need for venture capital. Coordinated market economies tend to specialize in incremental innovations within stable organizational settings, based on endowments of skilled manual workers, long-term capital investment and cooperative labour relations. Crucially, these capitalist varieties specialize in industrial areas that complement their particular institutional advantages. As no single ‘best model’ is achievable, and the gradual character of path-dependent institutional change excludes isomorphic convergence, the diversity of capitalist models prevails. However, the liberal model may prove supreme in times of rapid technological change, whereas firms from coordinated economies operate best within established technological paradigms.³

On this view, the systemic dynamism of institutional stability and change is fuelled by the impact of complementarities among the major institutional subsystems of the prevailing capitalist varieties. This scenario implies that each set of institutions depends on other sets in order to function effectively. In the words of Hall and Soskice, '[i]t suggests that nations with a particular type of coordination in one sphere of the economy should tend to develop complementary practices in other spheres as well'.⁴ This phenomenon is caused by positive feedback effects: 'One set of institutions is said to be complementary to another when its presence raises the returns available from the other'.⁵ A telling example of these complementarities in the post-war model of German capitalism is provided by the positive feedback mechanisms between the system of corporate governance that would allow for long-term financial relations, the firm-centred system of education and training with its long-term investments in human capital, and the cooperative system of industrial relations with its long-term outlook on economic performance.⁶

An important implication of this view of complementarities is that viable policy changes must be compatible with existing institutional patterns; that is, they must be 'incentive compatible' with the coordination mechanisms of the prevailing political-economic system. Critical reconsiderations of this viewpoint have underlined the wide scope for institutional 'hybridization', which changes the quality of complementarities by adding new institutional components. On a conceptual level, speaking of hybridization implies dealing with deviations from empirically grounded ideal types, and thus allows for an understanding of capitalist diversity in terms of institutional recombination and change.⁷ In related terms, institutions do not represent optimal solutions to coordination problems, but rather temporary stable compromises in a setting of social conflicts that mirror the heterogeneity of the underlying interests. It follows that institutional change as a manifestation of social power asymmetries is subject to political considerations and influences, thus bringing the problems of institutional change closer to the domain of political economy.⁸ Institutional change in varieties of capitalism, therefore, is to be perceived as a subtle political process that is covered by the temporary stability of formal institutional regimes. At this point, state-market relations, as well as the organizational pattern of interest groups, have a major role to play in shaping national pathways of change.⁹ Similarly, the notions of path dependence and lock-in are said to characterize the evolution of the institutional setting of capitalist economies most adequately. In analytically comparing the options of incremental and abrupt processes of change, as well as its continuous and discontinuous results, both incremental and discontinuous change shape market liberalization as a major trend of the institutional transformation of advanced capitalist economies.¹⁰

Nevertheless, in discussing strategic efforts in the promotion of institutional change, the role of interests needs to be augmented by ideas and discourses. Such ideational institutionalism highlights the discursive dimension of institutions in shaping perceptions and understandings in the diverse orientations of policy-related affairs.¹¹ This leads to a perception of institutional change that accounts for both the involved structures and agents by invoking the role of ideas in terms of the cultural underpinnings of institutional change as reflected by the prevailing sets of norms and paradigms that both enable and constrain strategic action.¹² In related terms, the notion of discursive institutionalism sets out to explore the role of ideas and discourse in the politics of institutional change. Ideas are defined as the substantive content of discursive efforts in the interactive conveying of policies, providing a context of inter-subjective meaning.¹³ In effect, these considerations of institutional change hint at the matter of ideas and discourses in understanding the dynamics of persistence and change in distinct varieties of capitalism. Indeed, in international comparison, different knowledge regimes in support of specific policy ideas may result in major differences concerning policy performance.¹⁴ An example of these ideational variations and their actual policy impact is provided by the impact of distinct sets of ideas on monetary policy and currency affairs that have been most relevant in the setting of the German model of the social market economy.¹⁵ In line with these aspects, the following section discusses the German variety of capitalism, followed by a reconsideration of its long-standing ideational framework that has been framing adaptive changes in its institutional setting.

Continuity and Change in the Germany Variety of Capitalism

The German economy has been Europe's export-oriented 'growth motor' throughout the post-war era, combining competitive openness with an extensive welfare state, framed by a favourable international economic environment with expanding trade and investment.¹⁶ The corresponding production model has been based on flexible specialization; that is, a sectoral production model in industries such as machine tools and automobiles, with an adaptive flexibility to handle rapid shifts in demand based on a skilled workforce, cooperative industrial relations and high levels of social compensation.¹⁷ In related terms, diversified quality production characterizes Germany's competitive advantages in the specialized production of high quality manufactured goods. Again, the adaptive flexibility of this production system and the integrated role of the workforce in industrial relations are decisive.¹⁸

Based on these conditions, the key complementarities in the German coordinated market economy evolved on the basis of systemic linkages between the following subsystems:¹⁹

- Corporate governance: permitting the flow of long-term financial resources with reputational monitoring as a non-market coordination mechanism in the financial sector.
- Industrial relations: permitting cooperative capital–labour relations with strategic bargaining and situational moderation in centralized wage setting as exercised by employers’ associations and trade unions.
- Education and training: permitting sunk investment in firm- and industry-specific types of skills and human capital, organized in an encompassing framework that involves self-governing business associations.
- Inter-company relations: permitting the non-market diffusion of common standards and practices that support a cooperative mode of inter-firm technology transfer.

The corresponding pattern of managerial organization in large business firms has been held together by centralized stakeholder supervision, often coordinated by major banks. The basic rationale of this system of non-market coordination involves comprehensive institutional constraints favouring consensual patterns of activity.²⁰

Historically, the German variety of capitalism emanated from the period of post-war reconstruction that led to sustained economic growth throughout the 1950s and 1960s. This was labelled the ‘*Wirtschaftswunder*’ (economic miracle), and was dominated intellectually by a pragmatic type of ordoliberalism.²¹ The steady decline of this growth performance led to an intermezzo of Keynesian regulation from the mid-1960s to the late 1970s, institutionalized in the format of the *Stabilitätsgesetz* from 1967 with its complex policy concerns for full employment, monetary stability, balanced foreign trade and steady economic growth. However, even this new type of economic policy was presented as a synthesis of ordoliberal ideas and a Keynesian approach.²² Germany passed comparatively unscathed through the international stagflation phase of the 1970s by flexibly adapting its production regime, especially the mechanisms of wage coordination. Even the crisis of corporatist regulation in the late 1970s and the liberal-conservative power shift that came with the Kohl government in 1982 did not entail a political-economic break with non-market coordination.²³ Nevertheless, the economic challenges of structural change during the 1970s brought a reconsideration of policy ideas, now heralding supply-side strategies of privatization and deregulation that would become dominant in the 1980s.²⁴ During the 1990s, mass unemployment, growth stagnation and the fiscal burdens of reunification exerted further pressure for institutional reform, aggravated by the adverse

impact of international macroeconomic policy conditions, in particular the Maastricht Treaty criteria.²⁵ Accordingly, the German model of the social market economy and its related policy paradigms have been subject to patterns of path dependence and institutional adaptation to changing internal and external conditions.

In this context, German policy discourse has been preoccupied with institutional changes intended to reinvent the system of the social market economy. In the ensuing ‘clash of cultures of production regime’, economic problems have been attributed to a lack of market dynamics in relational coordination. Thus, there have been efforts at liberalization that have seemingly been aimed at transplanting elements of liberal market economies into the setting of the German coordinated market economy.²⁶ The corresponding reconfiguration of the coordination environment of business firms pinpoints the key complementarities of the German variety of capitalism. This involves the drive for market-oriented corporate governance as well as flexibility in wage setting and labour regulations with an emphasis on the productivity of local firms, thus also reconfiguring the German brand of corporatism. Both ‘social partners’, involving employer associations and trade unions respectively, are experiencing decreasing organizational capacity, although institutional codetermination, which gives the unions a strong standing in supervisory boards and works councils of large firms, remains firmly in place.²⁷ Similar patterns of selective change apply to the financial system with its bank-based governance procedures in capital allocation, based on equity and monitoring interdependencies. Although it has opened up for capital markets, it still differs from market-based financial systems, as reflected in the marginal role of markets for corporate control. Also, the role of venture capital in Germany is still far from the one it plays in liberal market economies. The failure of Germany’s ‘*Neuer Markt*’ and its dissolution in 2004 indicate that institutional transplants from liberal varieties of capitalism may lose their momentum due to a mismatch with the complementary institutions of the German variety of capitalism.²⁸

Institutional reform has also addressed social policy and unemployment. The importance of this area is accentuated by the fact that one-third of Germany’s GDP is allocated to social policy, financing budgets for social transfers in areas such as unemployment benefits, health-care provision and old-age pensions. The combination of labour market policy and social policy has been a key issue since the 1970s, and it remained a fundamental concern during the 1990s, confronting fiscal pressures exercised by persistent unemployment and further aggravated by reunification and demographic change. Related liberalization efforts are well exemplified by the local differentiation of wage coordination and the activation approach in labour market policy, accompanied by the establishment of a secondary labour market with

low-wage and part-time jobs intended to boost employment in a manner more typical of liberal varieties of capitalism, and thus deviating from the ideological norms of the German model.²⁹ This orientation became a priority after the failure of neo-corporatist labour market initiatives in the shape of the doomed efforts such as the '*Bündnis für Arbeit*', part of the red-green Schröder government's efforts to implement the reform proposals of the '*Agenda 2010*' programme, with its key components of labour market activation and social policies that intensified the dualism of the labour market with far-reaching social consequences.³⁰ In effect, market-oriented reforms have fuelled the differentiation of household incomes since the 1980s, with a further polarization during the 2000s.³¹ In this setting, a particularly revealing issue is social attitudes about conflicts of interest between different wealth and income groups. In fact, conflict levels in Germany were moderate even during the 1980s, whereas the relative proportions of those noticing an intensification of social conflicts between capital and labour, or between the wealthy and the less well off, rose above 70 per cent in the 2000s.³²

Nevertheless, despite political and social changes, any assessment of the corresponding reform efforts needs to account for the fact that the main institutional patterns of coordination in the German variety of capitalism persist.³³ In examining the corresponding dimension of ideas and discourses, which seems to have contributed to the prevailing combination of adaptive change and systemic continuity, the following section explores the concept of the social market economy as an integrative ideological factor in the development of the German variety of capitalism.

The Concept of the Social Market Economy as an Economic Style

The production regime of the German variety of capitalism is still largely shaped by the rationale of diversified quality production, as exemplified by industries such as automobiles and tool-making. Reform projects that favour a drive for adaptive flexibility without due consideration of systemic complementarities and interactions among the major institutional components are thus doomed to create unintended inefficiencies.³⁴ These aspects of industrial flexibility and social integration have been framed by the ideological setting of a neo-corporatist consensus democracy that provides the political backbone for the international competitiveness of the German variety of capitalism.³⁵ When it comes to understanding patterns of persistence and change, a key aspect of these institutional complementarities is outlined by the prevailing policy paradigms and ideas. In the German case, the corresponding ideas point to the ordoliberal credo that is associated with the

competitive order of the market system, to be executed by a strong state with a level of policy competence able to reject the demands of special interest groups.³⁶ Both this policy orientation and its institutional framework coincide with the integrative ideas of the ‘social market economy’. This approach was originally presented in the analytical terms of a distinct style of economic life, a well-established line of reasoning in the historical comparison of economic systems – with normative implications that would echo traditions of German *Socialpolitik*.³⁷

Conceptually, the notion of economic style is in the tradition of the German Historical School and its diverse manifestations in economic sociology and political economy.³⁸ Arthur Spiethoff’s related work built on Max Weber and Werner Sombart, among others, as his notion of economic style or *Wirtschaftsstil* is intended to provide analytical tools for grasping the nature of an economic formation by highlighting its most important characteristics. These involve attitudes and habits of economic action, the natural and technological basis of economic life, the social structure of economy and society, as well as their institutional underpinnings, accompanied by the dynamism of economic growth.³⁹ In this manner, Spiethoff’s notion of economic style encompasses material and structural as well as institutional and cultural elements, without establishing a hierarchy of priorities, while it remains sensitive to the indeterminateness of historical processes.⁴⁰ In subsequent debates on these issues, Alfred Müller-Armack’s approach to economic styles has proved to be most influential in the domain of comparative economic systems, also due to related elaborations on the concept of the social market economy. An assessment of Müller-Armack’s approach needs to account for the major change that occurred in the intellectual atmosphere of German economics after the Second World War, shifting from historicist positions to ordoliberal thought. Pioneering contributions of ordoliberal theorists would focus on the relationship between economic, legal and social issues, as exemplified by Walter Eucken. The corresponding ordoliberal credo related the competitive order of market processes, primarily based on a market price system, with a set of well-established property rights and competition-promoting policies by a strong state, framed by institutional pillars such as religion-based communities.⁴¹

Paralleling these concerns, Müller-Armack’s reasoning combined theoretical positions of ordoliberal theory with Weberian and Sombartian motifs, highlighting a culturally sensitive understanding of the role of religion and related worldviews in economic life.⁴² The intellectual context of the German Historical School mattered most for that particular perspective, in accordance with Müller-Armack’s general interest in the contours of economic development.⁴³ In reconsidering Weberian arguments on the genesis of modern capitalism, Müller-Armack used religious worldviews as

a criterion for the historical-geographical identification of certain economic styles, as they shape economic, political and technological attitudes in a particular historical and spatial setting.⁴⁴ Economic styles should represent the 'unity of expression and attitude' of a certain people or nation in a particular historical period; that is, as a unity of the cultural expressions of economic and sociocultural life and its underlying worldviews. These styles of economic life would become subject to fragmentation over time, resulting in ever more complex style configurations.⁴⁵

Based on these considerations, Müller-Armack formulated the concept of the social market economy as an economic style of reconciliation in the face of the economic, social and political fragmentation that shaped Germany after 1945. This fragmentation was supposed to be overcome by social regulation of market competition without giving way to contemporary programmes on socialist planning, which had become prevalent in both the Social Democratic and Christian Democratic camps during the late 1940s.⁴⁶ From the outset, an 'irenic formula' was to reconcile diverse worldviews and ideologies: an 'enlightened' Catholic social philosophy with its principles of social balance and subsidiarity was to be combined with the Protestant ethos of communal cooperation, socialist concerns for the social question and liberal principles of progress in liberty.⁴⁷ The resulting model of the social market economy was meant to represent a new economic style that would reach beyond the *laissez-faire* principles of liberal capitalism and the centralized planning efforts of state socialism. It was intended to emphasize a socially managed market mechanism with its flexible price system.⁴⁸ This would go together with the acknowledgement of market failure and the possible incongruence of market process and social justice. In effect, the competitive order was to be embedded in an institutional framework that provides for integration and reconciliation through common norms and values.⁴⁹ It is noteworthy that subsequently formulated policy conclusions on European integration since the 1950s also referred to the requirements of such an ethical-cultural style consensus.⁵⁰ Indeed, according to Müller-Armack, both the social market economy and European integration could be perceived as outstanding types of integrative ideas.⁵¹

This integrative character of the concept of the social market economy also informs its conceptual adaptiveness concerning the actual combinations of market competition and social concerns. While motives of a religious-cultural framing of economic and social affairs remained crucial in the conceptualization of the social market economy, later presentations of the subject would follow a much more secular mode of argumentation that confronted the market-distorting interventionism of structural policies and the expansion of the welfare state. A second phase of the social market economy was to focus on interrelations between economy and society, again combining

the logic of market competition with social regulation through a strong state. This perspective would become prevalent during the 1970s, when the decline of the post-war age of full employment, monetary stability and fiscal consolidation seemed to herald a new set of legitimization problems of capitalist market economies.⁵² In fact, however, this line of reasoning proved to be fairly compatible with major strands of social democracy, as put forward by Karl Schiller in the context of contemporary efforts at promoting a neo-corporatist steering model of the economy. Already in the aftermath of the Godesberg Programme of the SPD in 1959 with its market-embracing components, social democratic discourses on economic policy had largely accepted the basic formula of the social market economy with its reconciliatory motives.⁵³ Thus, the reform discussions of the 1970s did not alter the basic formula of the adaptive framework of the social market economy, and nor did the ecological concerns that would dominate the 1980s. The intellectual underpinnings of social democratic reform efforts under Chancellor Schröder in the late 1990s finally renewed the original agenda of the social market economy by focusing on the competitive activation of society that already existed on the individual level.⁵⁴ In this manner, the notion of the social market economy persists as an integrative idea in the German variety of capitalism.

Conclusion

The institutional integration and coherence of political-economic systems requires supportive configurations of ideas and discourses. This aspect informs the debate on the comparative institutional analysis of capitalist varieties as outlined above with regard to the German variety of capitalism and the concept of the social market economy. A particularly relevant point of departure in this endeavour is the reconsideration of the system of production and related complementarities that shape a particular variety of capitalism. The corresponding complementarities define a corridor of reform efforts and thus effectuate institutional changes. In the case of Germany, recent efforts at institutional reform have shifted the established patterns of market and non-market coordination towards a more market-oriented constellation, yet without giving up key positions of non-market coordination in economic and social affairs. Even though privatization and deregulation have stimulated an expansion of the private sector and its related logic of market competition, it is fair to state that key features of the German model persist. With regard to the underlying role of ideas and discourses, the concept of the social market economy stands out as an integrative factor in mediating

continuity and change. Its intellectual profile fits the adaptive flexibility of the German variety of capitalism in general.

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