German capitalism and the European crisis: part of the solution or part of the problem?

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1. Introduction

Germany is riding high once again. It is true that the German economy suffered its worst slump since the founding of the Federal Republic owing to the global crisis of 2008, but the effects on its labour market were less severe than in any other EU country. The German ‘employment miracle’ was born and was held up for admiration all around the world. What happened next was what Chancellor Merkel had predicted early on: Germany emerged from the crisis ‘stronger than before’. This second part of the success story began with particularly high growth rates from autumn 2009 onwards. But Germany’s export-driven industry, on which it was based, came in for criticism within the EU and, above all, in France. Even greater consternation was caused in some countries by the attempts of German politicians to declare their model an example for the rest of the EU and in particular for the Eurozone. Ultimately, however, much of the criticism has been ineffectual: in view of the euro crisis, Germany now dominates EU affairs more than ever.

What lies behind this success story – if or to the extent that it is one? Should, and could, other countries follow Germany’s example? We shall attempt to answer these questions in three steps, by outlining the changes in Germany’s socio-economic model before the crisis and then during the crisis, and lastly by turning our attention to the uncertain present and future.

2. Before the crisis

At the core of what was long described as the German variant of ‘coordinated’ or ‘Rhenish’ capitalism was a combination of economic
A triumph of failed ideas – European models of capitalism in the crisis

dynamism and relatively little social inequality. Until about 20 years ago, institutions such as the industrial relations system, labour legislation and the welfare state helped the economy as a whole, as well as large swathes of society to benefit from the success of its export-oriented industry that was based on high value added and high-quality manufacturing, and reliant on ‘patient capital’ and skilled employees. The sudden monetary incorporation of East Germany, however, was followed by a decade and a half of thorough political and economic transformation, which in its radicalism far outstripped the adjustments to the neoliberal mainstream that took place in most other EU countries (cf. Lehndorff et al. 2009). As a result, the German model had a new look on the eve of the major crisis of 2008/2009: a re-energised and highly efficient export industry in an environment of increasing social and institutional disintegration and fragmentation. These contradictory circumstances are explained in more detail below, with the aim of better understanding two issues: in what way did Germany contribute to initiating the crisis, and what role did Germany play in the outbreak and persistence of the euro crisis?

2.1 Germany’s special role in the Eurozone

The starting point for our analysis is the weakness of wage growth in Germany: nowhere else in the EU had workers’ pay risen as little as in Germany from the start of the decade until the onset of the crisis. Unit wage costs stagnated and even declined somewhat in manufacturing industry (Niechoj et al. 2011). This contributed to a huge increase in export surpluses in the past decade. The export successes of German manufacturing – machine building and motor industries account for over one-third of goods exported from Germany – are of course deeply rooted in a high degree of specialisation and product quality, the service orientation of companies and their employees’ skills and flexibility (Lehndorff et al. 2009). Nevertheless, as the Deutsche Bundesbank (2011a: 17) cautiously put it, Germany’s export success in the past decade received ‘an impetus from the improvement in price competitiveness’.¹ For instance, it was no

¹ The European Central Bank (ECB 2011) calculates that Germany’s price competitiveness compared with that of its main international trading partners grew by 16 per
accident that the remarkable rise in export surpluses coincided with the introduction of the euro (Figure 1). The elimination of the exchange rate adjustment mechanism within the currency union, with which Germany conducts approximately two-fifths of its foreign trade, means that goods-based competitiveness is linked to the rise in price competitiveness (Horn and Stephan 2005).

![Figure 1](image)

Source: Deutsche Bundesbank; own calculations.

The other side of this coin was the imbalance in the domestic economy: between 2001 and 2008, three-quarters of Germany’s economic growth was attributable to the export surplus, whereas domestic demand contributed just one-quarter (Priewe and Rietzler 2010: 64). Thus, sluggish wage growth prevented both a transfer of the growth stimulus deriving from the export boom to the domestic market and a concomitant rise in imports, which would have enabled other countries to benefit from the export-derived growth stimulus enjoyed by German manufacturing industry (Joebges et al. 2010: 10). Germany’s special role within the EU in this respect is reflected in GDP growth rates, in cent between 1999 and the start of 2011 (basis: GDP deflator). The only other EMU countries with positive values are Finland (6.4 per cent), Austria (4.6 per cent) and France (3.2 per cent). The Bundesbank (2011a: 33) points out that the cost benefits gained had ‘evidently been utilised partly to raise profit margins’. We shall examine this aspect in more detail below.
price levels and in disposable household income since 2001: German growth rates almost continually lay below the EU average (Table 1).

Table 1  Real GDP growth, inflation rate and disposable household income, Germany and the EU-27, 2001–2008
(annual growth rates in per cent)

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The imbalances expressed in these figures are sometimes discussed in Europe under the heading ‘Germany is exporting too much’. They could equally – and perhaps more aptly – be encapsulated in the statement ‘Germany is importing too little’, since the weakness of the domestic market is primarily a manifestation of the increasing inequality in the redistribution of income and capital. We shall return later to the significance of this distinction.

What lies behind the weak growth of wages in Germany, often referred to as ‘wage moderation’? Can it be said, as critics at home and abroad tend to assume, that the trade unions are being guided in their pay policy by the increase in the price competitiveness of export industry? ‘Competitive corporatism’ does of course exist (on this point see Urban in this volume), but this in turn forms part of a more complex phenomenon. The attempt to understand these issues takes us to the very heart of the upheavals in Germany’s socio-economic model.

2.2  ‘Wage moderation’ – what is it?

Anyone looking at the trend in collective agreements on wages from 2000 to 2010 will make what is perhaps a surprising discovery. Collectively agreed wages and salaries have risen most sharply in none other than metalworking and chemicals, the two sectors of industry that
are most wide open to international competition. Even though the comparatively strong and assertive trade unions in these sectors have been unable to avert an ongoing redistribution of income to the detriment of wage-earners, pay rises have more or less exhausted the so-called ‘distribution-neutral’ room for manoeuvre, which is defined as the sum of the inflation rate and productivity growth in the economy as a whole (Bispinck 2011). Therefore the main causes of the low average pay rises as agreed upon in collective agreements clearly lie in those sectors that are exposed to global competition only slightly or not at all: the construction industry (where wage levels are under pressure as a result of labour mobility), the retail trade and, in particular, the public sector which lags behind all the other major sectors. This focuses our attention on the first structural change, namely a dismantling of the traditional architecture of German-style pattern bargaining. The gap between labour costs in industry and services has therefore become – and increasingly so – wider than in any other EU country, meaning that a whole range of domestic inputs have become considerably cheaper for manufacturing industry (Horn et al. 2007).

The second structural change finds expression in the fact that effective pay rises from 2000 to 2010 lay on average almost 50 per cent below the collectively agreed rates of increase (nominally 12.7 per cent as opposed to 23.6 per cent), meaning that real per capita wages fell by 4 per cent (Bispinck 2011). The reasons for this were:

– the weakening of the trade unions: their net organisational density fell from about 30 per cent in the mid-1990s to around 20 per cent on the eve of the crisis (ICTWSS Database 2011);

– a decline in the collective bargaining coverage of firms: just over 60 per cent of German employees were still covered by sectoral or company agreements in 2009, including 50 per cent in East Germany (Ellguth and Kohaut 2008; IAB 2010);

– a systematic weakening, on the initiative of the employers’ umbrella association, of the extension mechanism which permits collective agreements to be declared universally binding by the federal government (Bispinck and Schulten 2009);
numerous local derogations from regional sectoral collective agreements since the start of the 2000s: these pay cuts and extensions of working time would have turned the system of regional sectoral agreements into an empty shell, especially in the metalworking industry, had the unions not fought this trend by improved internal coordination and mobilisation of the membership (Haipeter 2009).

Over and above these institutional changes – thirdly – deep cracks appeared in the very foundations of the institutions. Although the following changes are not specific to Germany, when taken in combination with the abovementioned institutional upheavals they reinforce the braking effect on earned incomes:

- owing to outsourcing and reorganisation of supply chains, increasingly large parts of industry have been transferred to industrial and service companies with lower labour standards;
- the privatisation of services previously supplied by the public sector has had a similar effect. Large sectors with fierce low-wage competition – for example, postal delivery – have been created in connection with the EU services directive;
- various tax reforms since 1998 have led to a substantial loss of revenue for the public purse (amounting to 2.5 per cent of GDP in 2010; Truger and Teichmann 2010). This has put a huge amount of pressure on the wages (and also the working time) of employees in the public sector.

A fourth deadweight on wage progression are upheavals in the architecture of labour market regulation, carried out since 2003 (the so-called ‘Hartz reforms’):

- The fundamental change in the unemployment insurance system (Knuth 2010), which reduced the payment of unemployment benefit to twelve months, followed by means-tested welfare payments, and compels people to accept job
offers with low skill requirements and poor labour standards, has exerted downward pressure on many parts of the labour market (Bosch and Kalina 2008; Erlinghagen 2010).

— The de facto abrogation by the German government of the European directive on equal pay in temporary agency work, which included an ‘unless otherwise agreed in collective bargaining’ clause, paved the way for dumping-level collective agreements in this sector (Weinkopf and Vanselow 2008). The number of temporary workers doubled between 2000 and December 2010, reaching almost 3 per cent of all employees (BA 2011). In 2006, temporary agency staff earned on average only just over half as much per hour as standard workers (Destatis 2009).

— A strong incentive for the expansion of atypical employment came from the public subsidies for low pay and in particular from the promotion of so-called ‘mini-jobs’ with monthly wages up to €400. Some 15 per cent of all wage-earners – most of them women – are nowadays employed exclusively in these marginal part-time jobs, and two-thirds of them earn a low hourly wage, even though a significant majority have vocational qualifications (Weinkopf 2009).

The impact of the mini-job scheme is closely related to the continued existence of the conservative welfare state, which partially forces and partially encourages women to limit their participation in working life: the lack of childcare facilities makes it difficult for many women with small children to return to work rapidly, while the tax and social security system makes the unequal distribution of earned income financially attractive for married couples (Bosch/Jansen 2010). Even though this system, rooted in the 1950s, is coming in for more and more

2. A commentator in the Financial Times Deutschland summarised the situation as follows: ‘Wage costs per unit of production in Germany, incredibly, fell by almost 4 per cent in the two years following the introduction of the Hartz IV measures, having risen until 2005. This is all the more bizarre in that unemployment decreased by almost a million at the same time – which according to the rules of supply and demand ought to have led to higher, not lower, pressure on pay. This can hardly be explained at all, except by the shock of the Hartz measures’ (Fricke 2010).
criticism and partial modifications are being made (such as the introduction of a Swedish-style parental allowance), its stability basically remains intact, contrasting markedly with the enthusiastic neoliberal-inspired reforms in other areas.

The combination of upheavals in Germany’s labour market institutions, on the one hand, and the dogged defence of the welfare state based on a conservative gender model, on the other, is at its most blatant in the growth of the low-wage sector. The number of employees earning less than two-thirds of median pay has risen by half since the mid-1990s, accounting for 22 per cent of all employees on the eve of the crisis. What is particularly noteworthy is that only a minority of them – approximately one-fifth – are entirely lacking in vocational or academic training. The heated arguments about how to end this state of affairs have so far resulted in nothing more than the introduction of minimum wage levels in a few sectors; as yet there is no general statutory minimum wage in Germany (Bosch and Kalina 2010).

This negative wage drift is what lies behind the decline in (price-adjusted) average pay of all workers in the 2000s. The drop in real pay was unique in Europe and was also something new for Germany, especially during a phase of economic growth. The overall state of affairs was summed up in this way by a commentator in the Financial Times Deutschland: ‘Hartz IV is poisoning Europe’ (Münchau 2010).

2.3 Where to put the money?

Stagnating or even declining average rates of pay contrasted with labour productivity that was rising steadily (albeit not excessively). As a result, the adjusted share of wages and salaries declined by more than 6 percentage points from the start of the decade to the eve of the crisis (Figure 2). This dynamic of mounting inequality was among the most pronounced in the EU (ILO 2010).

The gap was at its widest during the 2004–2008 growth phase, when a slight decline in net pay contrasted with a rise of roughly 20 per cent in capital income and profits (Brenke 2011). The reference made to net income indicates that changes in the primary distribution were offset by the secondary distribution to a lesser extent than had previously been
the norm. In fact, the abovementioned tax reforms had markedly reduced the top rate of income tax, as well as taxes on capital income and company profits.

Figure 2  **Wage share, Germany, 2000–2010 (percentage of GDP)**

Contrary to the predictions of the main neoliberal-inspired players in the fields of economics and politics, the growing inequality did not produce any notable stimulus for investment and growth (Priewe and Rietzler 2010). This makes sense, given the stagnation on the domestic market. Furthermore, for the same reason, imports could not keep pace with exports. The statement ‘Germany is importing too little’ therefore sheds more light on the problem than the assertion ‘Germany is exporting too much’.

At the same time, the massive redistribution in Germany in favour of profits and capital income contributed significantly to the onset of the crisis (Horn *et al.* 2009), in that suitable ‘homes’ had to be sought for financial capital somewhere other than in the domestic production of goods and consumable services. And such homes were of course found: German profits and capital income played a major role in fuelling the booming financial market bubble. The SPD-led federal government had carried out numerous deregulations of the financial sector, opening the door wide for such action (Huffschild 2010). Germany had the second-largest capital surplus in the world, after China. Unlike China, however, which rose to the position of number-one foreign creditor of the US government, German investors became the number-one foreign
creditors of the indebted US private sector (Horn 2011). German banks were also the biggest lenders to Greece, Ireland, Portugal and Spain (Bofinger 2010). The German economy was therefore not a victim of the crisis, but contributed significantly to preparing the ground for it. Or, as a commentator in the British Guardian put it: ‘Germany blew the bubbles that popped up in the rest of Europe’ (Chakrabortty 2011).

These, then, were the contradictory circumstances in which German capitalism entered the crisis. But how did it manage to recover from the crisis so swiftly and even – apparently at least – to emerge from it with renewed vigour?

3. During the crisis

The collapse of the German economy from September 2009 onwards was particularly dramatic owing to its extreme dependence on exports and was surpassed only in countries where financial and property bubbles were bursting. That made the stability on Germany’s labour market all the more bewildering. In a nutshell, what had happened in 2008 and 2009 was this: whereas before the crisis the upheaval in the German socio-economic model had contributed actively to the emergence of imbalances in the European and international economies, the stabilisation of the labour market and economy during the crisis was in fact attributable to a reactivation of those elements of the German model that had survived the eagerness of the neoliberals to dismantle them in previous years.

3.1 A revival of traditional strengths

The reactivation of former virtues began with the sudden – albeit temporary – abandonment of many neoliberal dogmas that had until then been standard elements of government policy. In direct contrast to all the constantly repeated tenets, extensive stimulus packages were introduced virtually overnight. The 2009 Bundestag elections lay just around the corner and, given the billions of euros in expenditure and guarantees proffered to bail out the banks, any hesitation about saving the ‘real economy’ would have been politically disastrous for the two main government parties.
The government’s recovery plan was predicated on active cooperation with both the employers’ associations and the trade unions. An informal type of ‘crisis corporatism’ (see Urban in this volume) arose at all levels – from Chancellor Merkel’s close contacts with individual union leaders to thousands of emergency coalitions formed at establishment level.

The biggest direct effect of crisis corporatism was to avert massive job losses in the crisis-stricken industrial sector. Admittedly, a substantial number of temporary agency workers were laid off. But in the labour market as a whole this decrease in employment – statistically, temporary agency work belongs to the service sector – was actually slightly outweighed by a rise in employment in other service segments. But what this reference to temporary work makes plain is that crisis corporatism could well include recourse to external flexibility whenever it was necessary to safeguard core staff. The biggest role, however, was played by internal flexibility. This was new, or rather – new once again. Only a few years beforehand, during the previous phase of recession and stagnation, many companies had trimmed their workforces to such an extent that they encountered difficulties and staff shortages when the economy recovered. This experience was still a recent memory, and in order to retain their skilled workforces companies were now prepared to suffer even sizeable productivity losses in the short term.

The return of internal flexibility found its most striking expression in the substantial reduction in per capita working time, which is widely regarded as the most important explanation of the gap between the drop in GDP and the stability of employment (OECD 2010). It was achieved by harnessing the many and varied resources of the German socio-economic model – partly new resources, but mainly its traditional strengths and others rediscovered during the crisis, which had survived the disruption and upheavals of the previous years.3 The most prominent role was played by the short-time working arrangements, which were deployed to an extent that was perhaps comparable to the crisis of the mid-1970s (Herzog-Stein et al. 2011). But other factors had a bearing on the cuts in working hours, too: the use of existing collective agreements on employment safeguards, an abandonment of overtime

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3. For more detail on what follows, see Bosch (2011) and Lehndorff (2011).
and a using-up of the credits accruing on working-time accounts, which in some cases had burgeoned in recent years (Bogedan et al. 2011). These last forms of individual working time reductions, above all, had at least as powerful an effect on the volume of labour in the overall economy as did (collective) short-time working (Fuchs et al. 2010).

The less high-profile resources of the German socio-economic model, which enabled internal flexibility to be prioritised during the crisis, included – despite all of its problems – the vocational training system, whose strategic importance for companies and employees alike was not challenged even during the crisis (Voss-Dahm 2011). The immediate effect of this was that, initially, the youth unemployment rate did not rise sharply; by 2011 it had even fallen below its 2008 level (although, as in other European countries, the proportion of young people in insecure jobs is well above the average rate for all age groups; Destatis 2011).

3.2 Scarring effects of the neoliberal upheaval

Returning to the traditional strengths of the German socio-economic model was undoubtedly the main cause of the so-called ‘employment miracle’ during the economic crisis. The upheaval of the previous years nevertheless made itself felt. The rapid, sharp decline in temporary agency work showed how far the dualisation of the labour market had already progressed. It was only thanks to the brevity of the crisis that this had not yet been reflected in the overall balance of the labour market. Less obvious, but equally important, is the dualisation in respect of the much-praised flexibility of working time. During the crisis the ability to dismantle working-time buffers was often regarded as a blessing, but these buffers had of course been built up previously – above all in the form of substantial credits on working-time accounts. In the metalworking industry, for example, the average real working time of full-time employees had increased by an hour between 2003 and 2008, whereas initially the number of core staff had been further reduced (Lehndorff et al. 2010).

The rediscovery of traditional virtues should not, therefore, obscure the fact that old strengths were marked by new weaknesses. Likewise, the revived Social Partnership was not the old one, but a new one – and
with a totally different balance of power. The contradictions, imbalances and fragilities which had taken hold within the German model following the neoliberal-inspired upheaval of the 1990s onwards persisted during the crisis – and are still with us today.

Their persistence first became apparent – paradoxically – in the state of the economy. Sudden and dramatic though the collapse into crisis was, the upturn from the second half of 2009 onwards was equally rapid – and both were export-driven. This was fortunate, since the upturn came about so quickly that the crisis had not yet infected the service sector (because redundancies in industry were postponed and because of comparatively good wage growth in the previous year). Many manufacturing firms in Germany were, in a sense, awaiting the turn of events with their engines running idle. In many instances the crisis had also been used for streamlining purposes. Once foreign demand picked up again in the third quarter of 2009, the skilled core staff were still on board, short-time working was terminated, the laid-off temporary workers were reinstated and the now-empty working-time accounts could be restocked. The traffic lights turned green – mainly thanks to foreign demand, as usual. Business could resume or, rather, carry on as before the crisis.

4. After the crisis?

The heading of this chapter ends with a question mark for obvious reasons. The first phase of the major economic crisis may have been overcome for now in Germany and some other countries, but the huge problems affecting the Eurozone and the US economy stoke fears of a fresh collapse. Germany is contributing to these uncertainties, just as it helped to prepare the ground for the economic crisis. And, as before the crisis, the external impression is quite different this time too: the German economy’s growth rates until spring 2011 were among Europe’s strongest since late 2009, and Germany is regarded as a mainstay of stability in an environment dominated by the euro crisis and excessive government debt. But here, too, appearances are deceptive: so far there are no signs whatsoever of a move away from the bad habits that led us into the crisis and have been analysed above. In essence, what Paul Krugman (2010) described as ‘the strange triumph of failed ideas’ with reference to the United States applies likewise to Germany: ‘Free-
market fundamentalists have been wrong about everything — yet they now dominate the political scene more thoroughly than ever.’ However, one key distinction must be drawn between now and the time before 2008, and perhaps also between Germany and the United States: ‘free-market fundamentalism’ has become very unpopular in Germany. Thus German fundamentalists are having to engage in a dizzying balancing act between rhetoric and practical policies. The vehicle for this act is the alleged need for short-time reductions of sovereign debt as a top priority.

Before turning to this overarching topic, we shall briefly outline the most evident signs of a return to the basic economic constellation that existed prior to the crisis.

4.1 ‘Beggar and lecture thy neighbour’

The biggest proportion of the GDP growth achieved in 2010 – a remarkable 3.6 per cent – consisted of the external component (1.3 per cent) and fixed capital investments (1.1 per cent), which once again were driven to a large extent by very positive export expectations. The contributions from government (0.4 per cent) and private (0.3 per cent) consumption expenditure lagged a long way behind (Hohlfeld et al. 2011). Thus Germany is ‘not really an economic driver, but is partly being pulled along by the outside world’ (Niechoj et al. 2011, p. 18). Despite a slight uplift in collective pay deals in 2011, these will lie below the inflation rate on average (Bispinck/WSI-Tarifarchiv 2011). As for the near future, it is not yet possible to tell whether the trade unions, where they still remain resilient enough, will try to go beyond the attempt to ‘exhaust the scope for redistribution’ and once again make the goal of income redistribution an element of their effective pay policy.

Other indicators also point to ‘pre-crisis reloaded’: the proportion of low-wage employees and households rose again in 2009, even going slightly above the pre-crisis level (Bosch 2011). Similarly, the number of temporary employees in late 2010 exceeded the maximum level reached before the crisis: about half of the increase in employment during the first year of the recovery since mid-2009 is attributable to temporary agency work (BA 2011). Last but not least, after short-time working was scaled down, working time has lengthened again – with all the
problematic implications for job creation that one might expect: in the first quarter of 2011 the actual working time of full-time employees had already returned to the pre-crisis mark of just under 41 hours per week (IAQ 2011). After a very short while the prediction made by Bosch (2011: 282) was already borne out: the ‘dualisation of the German labour market was not so evident in the crisis, but may become more visible in recovery.’

The obstacles to pursuing this course are mounting, however, first of all on domestic political and economic grounds. Many industrial companies are becoming increasingly concerned about a future lack of skilled manpower. While the validity of these concerns is open to doubt, the problems associated with demographic change and an ageing workforce do lend grist to the mill of those who prioritise sustainable human resources strategies rather than the short-term exploitation of pay differentials in dualised labour markets. Secondly, the political obstacles are also mounting. Trade union pressure for unconditional equal pay for temporary workers and for a statutory minimum wage is garnering ever more support from the public. So far, this has changed nothing as regards the factors described above, which led to the expansion of the low-wage sector and to the stagnation, or even decline, in average pay. This is all the more true in that none of the existing or potential parties of government is calling into question one particularly heavy burden on future wage growth, namely the so-called Hartz reforms. Nonetheless, the wage restraint strategy is unlikely to operate quite as smoothly in future as it did before the crisis.

There could, in addition, be external economic reasons. Since 2009, the German government has turned wage restraint into a piece of ‘advice’ given to other countries. More accurately, other countries are virtually being compelled to follow Germany’s lead in order to become more competitive and reduce their government debt. The problem here, at least within the Eurozone, is that if everyone were to follow Germany’s example the country could continue to pursue its existing export surplus strategy only at the cost of greater pressure on pay and an even greater extension of the low-wage sector in Germany. Whether or not this could be implemented at a domestic level is debatable. Paradoxically, therefore, Germany’s policy of ‘beggar and lecture thy neighbour’ is in the process of undermining the prerequisites for its success to date.
Another problematic element may be an attempt, in the absence of an expanding domestic market, to steer soaring capital income into the international financial bubble that is once again growing in size and continues to be mostly unregulated. US private sector debt is now of much less significance as a source of returns for German banks, and the strong commitment, for example, to Irish or Spanish government bonds at attractive interest rates is shrinking progressively, on account of the associated risks (Horn et al. 2011). No equally attractive alternatives are evident in the present global economic climate. This makes the markets ‘nervous’ and an export-dependent economy such as Germany’s especially volatile.

All of this is happening against the backdrop of a sudden rise in government debt.

4.2 A lifebelt for neoliberalism

‘The crisis started with too much private debt and leverage, which became public debt and deficits as crisis and recession triggered fiscal deterioration and private losses were mostly socialized via bailouts of financial systems’ (Roubini 2010). The extent of, and level reached by, the upsurge in Germany’s public debt (from 65 per cent in 2007 to 83 per cent in 2010) corresponds roughly to the average level for all EMU Member States (Horn et al. 2011). In fact, new debt has so far risen less rapidly than was originally feared, since the growth of the economy and the tax take in 2009 and 2010 were surprisingly robust. This created scope for the abovementioned, albeit small, positive contribution to growth made by public spending in 2010 – a virtuous circle that was denied to other countries, given the alleged need to reduce new debt immediately. There was, in addition, a little-noticed side-effect of the continuing crisis in the Eurozone: German federal treasury bills became such a sought-after investment that their yields temporarily fell from just under 5 per cent in mid-2007 to a historic low of roughly 2 per cent from summer 2010. That is, when writing this chapter in late 2011, for more than a year the interest rate for German government bonds has provided for the refinancing of public debt at zero cost in real terms amidst what is widely perceived as a European ‘debt crisis’. This remarkable ‘safe haven effect’ (Deutsche Bundesbank 2011b: 42) has
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substantially moderated the rise in the Federal Republic’s budget deficit and must be regarded as a kind of crisis dividend.\(^4\)

These factors have so far enabled German politicians to moderate the pace of the austerity approach. But it is becoming clear that the consolidation measures being introduced are focused primarily on cutting welfare spending (Heise and Lierse 2011). For the time being, the ‘need to cut government spending’ is being portrayed as something that will demand considerably more sacrifices in other countries than in Germany. What is more, the constant references to other countries, which ought at long last to begin managing their economies as efficiently as the Germans, and for whose debts ‘we Germans’ should not have to take responsibility, represent an ideological stance that – as already happened at the start of the crisis – made Germany appear to be a victim of the crisis and not one of its creators. In essence, this argument is similar to that of right-wing populists in other European countries.\(^5\)

But even under the austerity regime, the days of ‘beggar and lecture thy neighbour’ are numbered. There is much to be said for the assumption that, in light of ever-increasing private wealth, public poverty in Germany will become more and more painful in the short- and medium-term future. Over the past two decades public investment as a share of GDP has fallen to a level far below the EU average (Dullien and Schieritz 2011). The public finance difficulties are particularly noticeable at regional level and above all in municipalities. However, the endogenous strengths of the German economy derive increasingly from investment not just in bricks and mortar but primarily in people: from an efficient education and training system to all the social services

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\(^4\) It should be noted that this crisis dividend is acknowledged neither by German policymakers nor by commentators. Since the beginning of the Eurozone crisis the focus has been put on the denial of what is called a ‘transfer union’ to countries with high public debts. What is neglected, however, is the transfers caused by the imbalances within the Eurozone which have been quite beneficial for German economic elites over the past ten years and continue to be so for the time being.

\(^5\) The following statement by the president of the French Front National, made in summer 2011, will serve as an example: ‘We have enough poverty, adversity and unemployment at home to refuse to see tens of billions of French euros, earned through the work of French people, paid to other countries. We have enough debt of our own to refuse to pay for that of others. The Germans have fully understood this, and are now refusing all further efforts to restock the coffers of other countries’ (M. Le Pen 2011).
that make it possible to draw much more heavily on skilled female labour. A constitutional cap on government debt, which German politicians believe should be extended to all the euro countries, has already been introduced in Germany with the approval of all the current and potential parties of government. The painful effects of these constraints on future government action will become all too apparent in the course of the current decade – including in Germany (Truger and Teichmann 2010).

Meanwhile, the political agenda is dominated by the foot-dragging of German politicians, prompted by domestic concerns and dogma alike, over a solution to the crisis in the Eurozone. This enhances the crisis dividend for the German government in the short term, but in the medium term the foundations of monetary union will be further undermined. Equally important, perhaps, is an ideological effect of this policy: the focus being attached to government debt serves as a lifebelt for ‘failed ideas’. The neoliberal policy of dismembering the public sector is being pursued with the help of a new ‘justification’.

5. **Looking ahead: beware the German model!**

Some 15 years ago, in the heyday of the dotcom boom and the political victory of privatisation and labour market deregulation missionaries all over the advanced capitalist world, a group of non-mainstream US economists published a book titled ‘Beware the U.S. model’ (Mishel and Schmitt 1995). The intention was to ‘provide concerned Europeans with views of the actual American experience’ (Faux 1995: x) by highlighting the downside of the US economic success story of these years, including the growing low-wage sector, income deterioration and rising inequality. As we know today these were exactly the problems which gave way to the subprime bubble of the past decade which eventually sparked the world economic and financial crisis (Krugman 2009). Of course, the economy and the social order of Germany today cannot be put on a level with the US in the 1990s. However, the enormous pressures exerted by Europe’s strongest economy and its political leaders, based on a combination of persistent and massive current account surpluses with an actual fiscal dictatorship within the monetary union, is about to suffocate economic recovery and social equity in many other EU countries. The side effects on the world economy may
be substantial, and the backlash on the German economy will be inevitable. Thus it is time to modify the earlier warnings of our US colleagues: Beware the German model.

Today’s German model of capitalism – a hybrid consisting of a few preserved components of ‘Rhenish capitalism’, neoliberal-inspired reconstructions and demolitions of this classic model over the past 20 years, along with stubborn refusals to reform the conservative welfare state – may be admired at home and abroad as a model of success. Such praise overlooks three facts. First, the ‘employment miracle’ of the years 2008–2009 is attributable primarily to those elements of Rhenish capitalism that survived the so-called reforms of the previous years. Second, the economic success of the past decade – and once again since 2009 – relies to a considerable extent on a combination of renewed vigour in manufacturing industry (which, likewise, would have been unthinkable without the surviving elements of the classic German model) with increasing social differentiation and division. As a result, average pay has stagnated and even declined, which not only makes Germany more price-competitive – especially compared with the other Eurozone countries – but also makes the fate of the German economy ever more dependent on the success of its export industry. Third, specifically through its neglect of the domestic market and by widening the income differentials on which it relies, this new German capitalism is helping to destabilise the Monetary Union, as well as to create a global economic imbalance and ever more financial bubbles.

This supposed model of success is far more fragile and vulnerable than its advocates would have us believe. A Monetary Union that accepts this model as an example and goes along with the political dominance of its leaders is skating on very thin ice. The heavier the millstone that Germany imposes on the Monetary Union, the greater the danger that the ice will break.

Most paradoxical thing of all is that Germany, its economy and its society, have a great potential to play a positive role in Europe. German industry could develop its strengths in the field of environmental renewal, buoyed by a comparatively broad consensus in society on the sustainable use of natural resources. A better social balance within Europe’s biggest economy would lessen the constant pressure on other countries in the region, and especially on the Monetary Union, to make
social security cutbacks and reduce wages. Germany could become the engine of a more sustainable new way forward for the EU in social and environmental terms. This would, among other things, be very beneficial for democracy in the EU and its Member States.

However, such a new way forward can be achieved only with root-and-branch reform of the German socio-economic model – a reform that would restore to this term its lost connotations. Its most important elements include, first, a bolstering of public investment and social services, which will not be feasible without substantially increased taxes on capital revenues, profits and higher incomes; second, a gender-related modernisation of the welfare state; and third, support for the weakened collective bargaining system by means of a statutory minimum wage, extended universal application of collective agreements, unconditional equal pay for temporary workers and an obligation for public procurement contracts to comply with (universally applicable) collective agreements. Such reforms would, moreover, trigger a virtuous circle for the national budget, consisting of growing revenues, improved services and a reduction in inequality.

But all this is a long way off. Meanwhile, the ‘failed ideas’ are triumphing yet again. The paradoxical basis of this triumph is the sudden rise in public debt, caused by the faith in these very ideas, and its vehicle is the austerity regime being imposed on the Eurozone. All this goes to show that, this time round, the failed ideas are not being held out as a promise of fortune; instead, their latest triumph is based on intimidation and fear. This is nonetheless a sign of realism, in that a refusal to learn can only generate further crises. We can only hope that the European project will not be among its next victims.

**Bibliography**


