

# SOCIAL DEMOCRACY READER 2

*Simon Vaut et al.*

## Economics and Social Democracy



AKADEMIE  
FÜR SOZIALE  
DEMOKRATIE

FRIEDRICH  
EBERT   
STIFTUNG



ISBN 978-3-86872-698-5 3rd, updated edition

Published by



**Friedrich-Ebert-Stiftung**

**German Edition: Political Academy, Bonn December 2009**

**English Edition: Division for International  
Cooperation, Berlin May 2011**

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Responsible: Dr. Christian Krell / Project Manager: Jochen Dahm

Printed by: Druckerei Brandt GmbH, Bonn // Layout and composition: DIE.PROJEKTOREN, Berlin

Translated by: James Patterson

Cover photo: Frédéric Cilon; Nyul/Hans12/Chesse, fotolia

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# FOREWORD to the 3rd German edition

The financial and economic crisis was a turning point. The problems that confront us go beyond mere coping with the particular consequences of the crisis, and concern the very foundations of our society. We have to decide today how we want to live and work, not just over the next few years, but over the coming decades. What would a fair and solidarity-based economic order look like? What kind of balance must be found between state and market? How can a modern, value-oriented social democratic economic policy prevail?

These are key questions for anyone wishing to have their say and actively participate in politics. The belief in the uncontrolled market has been sidelined. Now an opportunity presents itself to set a new course. But only those who know where they are going will be able to inspire others to embrace their ideas and achieve their goals. All the more reason to be certain about one's own course. The aim of this reader is to help achieve this certainty. Important economic theories are explained, economic orders described, key values and orientations are characterised and the question is asked, what these values mean for a concrete social democratic economic policy. Clearly, no definitive answers can be provided. What makes a successful social democratic economic policy must constantly be thought through and justified anew. This volume therefore is not aimed at providing definitive answers, but rather represents an invitation to read and reflect further.

This is the second volume of the series »Social Democracy Readers« and builds on the reader *Foundations of Social Democracy*. In the latter the core values of social democracy are clarified, the social models of liberals, conservatives and social democrats are compared and the differences between libertarian democracy and social democracy are presented. The third volume in the series is called *Welfare State and Social Democracy*.

No discussion of the economy of the twenty-first century can leave out of account the radical changes brought in by globalisation. Another volume will appear in this series of readers entitled *Globalisation and Social Democracy*, in which globalisation will be examined in terms of its influence on the shaping and framework of the economic order. The background of globalisation and possibilities for shaping it politically will also be analysed.

We would like to thank Simon Vaut and Tobias Gombert. Simon Vaut wrote the bulk of the reader. Tobias Gombert has shown extraordinary competence and considerable dedication in the assistance he has provided in the editing and educational work. We also thank Thomas Meyer and Michael Dauderstädt for their advice on the conception of the reader, Wilhelm Nölling for his helpful comments and all those who participated for their outstanding cooperation. Without their contribution, this reader would not have been possible; any shortcomings are our responsibility.

The symbol of the Academy for Social Democracy is a compass. The purpose of the Academy for the Friedrich-Ebert-Stiftung is to provide a framework within which standpoints and orientations can be clarified. We would be delighted if you took advantage of this in choosing your own political path. Social democracy positively depends on constant public debate and commitment.



Dr. Christian Krell  
*Head*  
*Academy for Social Democracy*



Jochen Dahm  
*Project Leader*  
*Social Democracy Readers*

Bonn, December 2009

# FOREWORD to the International Edition

The outbreak of the 2008 financial and economic crisis once more brought into sharp focus present-day global interdependencies and interconnections. The situation in which we find ourselves as a result differs fundamentally from the global economic tremors of previous decades. This is due, not only to the sheer scale of the economic crisis, but above all to the conjunction of a wide variety of crisis phenomena. The financial and economic crisis should not be considered in isolation. Rather it is connected to an overwhelming environmental and climate crisis, a structural crisis with regard to justice and, in many regions, the exhaustion of the predominant – export-oriented – growth model. It is important that these overlapping symptoms are addressed as a whole.

At the same time, however, this was also a crisis of economic science, which for years has been immured within its own ideological edifice, unable to provide answers to the crisis's complexity. Dominated by the neoclassical mainstream and far removed from a productive economic pluralism no practicable remedies could be formulated which fit the world view of standard economic theory.

Preoccupation with theory is no mere academic indulgence. The worldviews of economic theory enframe political debates and concrete strategies and practical options are based on them. The vivid presentation of key theoretical approaches in economics from Adam Smith to the present day is therefore an important feature of this second Social Democracy Reader (the first, *Foundations of Social Democracy*, has already appeared in English).

However, interpretative sovereignty is determined first and foremost in economic policy practice. In the past few months in particular the debate on sustainable economic and social models has got under way, across the board. After years of stagnation once again the concept of growth and the relations between market and state, the economy and society are being reconsidered. However, these debates, too, are still characterised by a high degree of uncertainty with regard to the regulatory and social policy bases of »good« or »sustainable« development concepts.

For that reason I am delighted that this volume also compares the different economic policy programmes of German political parties, concrete economic policies and, not least, the basic economic policy orientations of social democracy.

The Social Democracy Readers have their origins in the Friedrich-Ebert-Stiftung's activities in political education in Germany. Most of the examples used in the Readers reflect politics and society in Germany or in other OECD countries. Nevertheless, they illustrate political ideal models and courses of action which also have relevance in other socio-political contexts. Underlying the international work of the Friedrich-Ebert-Stiftung in more than 100 countries is the conviction that the core values and ideals of social democracy know no borders.

I therefore wish the international edition of the Social Democracy Readers a large and committed readership.

A handwritten signature in blue ink that reads "Christiane Kesper". The signature is fluid and cursive, with the first letter 'C' being particularly large and stylized.

Christiane Kesper

*Director*

*Division for International Cooperation*

# 1. INTRODUCTION

*What kind of economic policy is in keeping with social democracy?*

Former German Chancellor Gerhard Schröder said in his inaugural speech in 1998 that his coalition's economic policy was not right-wing nor left-wing, but a modern economic policy.

But are there really no economic policy differences any more between liberals, conservatives and social democrats?<sup>1</sup> Is there an economic theory which pertains distinctly to social democracy?

Or are there really only »modern« and »old-fashioned« economic theories? But who would claim to represent an old-fashioned theory and what does »modern« really mean in this context? The football coach Otto Rehagel once said: »Whoever wins is »modern««. In a political context this means that a modern economic policy is whatever policy succeeds.

*How is success measured in economic policy?*

But how is this success to be measured? Some say that it consists of the greatest possible prosperity and growth. Others emphasise equality and fairness: an economic order should not therefore lead to inequality, exploitation and injustice. Gaining ground are those who call for sustainability, resource conservation and the environment as benchmarks of economic success: growth must not result in over-exploitation.

*Balance between economic growth, social equality and environmental sustainability*

The core values of social democracy are freedom, justice and solidarity. In terms of a party platform, therefore, there can be only one answer from the standpoint of social democracy. All three principles – that is, first growth, second social equality and third sustainability – have to be brought into harmony.

But how to get there has not been mapped out in advance. A modern, value-oriented economic policy will, on one reading of Gerhard Schröder's words, make use exclusively – and in knee-jerk fashion – of neither classically left-wing nor right-wing economic policy instruments. A modern, value-oriented social democratic economic policy is above all results-oriented. Its aim is to bring about a society in which freedom, justice, solidarity and extensive social, economic and cultural basic rights are implemented for all.

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<sup>1</sup> Both masculine and feminine forms are used in this text. Where this is not possible on linguistic grounds both sexes are intended.

This reader will offer basic orientation on the questions of what theoretical foundations social democracy can make use of; which economic systems and orders favour the realisation of its ambitions; how things stand with regard to economic orders in other countries; and what these theoretical problems might mean for policymaking.

		Economic-policy orientation of social democracy (Chapter 4)							
		Liberal democracy			Social democracy				
Thematic structure of the reader	Object of the reader „Foundations of Social Democracy“					Libertarian democracy			
	Object of the reader „Economics and Social Democracy“								
	Chapter 2	Theory	Marx		Keynes		Smith		
	Chapter 3.1	System				Capitalism			
	Chapter 3.2	Orders	Authoritarian		Coordinated		Uncoordinated		
	Chapter 6	Countries			Sweden	Japan	Germany	UK	USA
	Chapter 5	Comparison of party programmes							
	Chapter 7	Practical examples							

First, at the level of **economic theory**, a description will be given of the analyses and conclusions of the most influential economists in history: Adam Smith, Karl Marx and John Maynard Keynes. The ideal-types of economic liberalism, anti-capitalism and managed capitalism which will be derived from this will then be assessed from today’s perspective and with a view to the goals of social democracy (Chapter 2).

At the level of **economic systems and orders** the connection between capitalism and democracy will be looked into and the two economic orders which dominate in Western industrialised countries – coordinated and uncoordinated capitalism – will be presented (Chapter 3).

At the level of economic policy programmes, on the one hand, the **economic policy orientation of social democracy** is developed on the basis of the interaction between core values, basic rights and economic policy principles (Chapter 4).

On the other hand, based on the criteria of coordinated and uncoordinated economic orders and the economic policy orientation of social democracy described above, the **economic policy programmes** of the **parties** represented in the Bundestag will be compared on the basis of their policy platforms (Chapter 5).

A comparison of the different economic orders in the **USA, the UK, Germany, Japan and Sweden** (Chapter 6) and specific examples of policy proposals in the economic policy areas of **privatisation, environmental industrial policy, decent work and codetermination** (Chapter 7) round off the volume.

The question concerning social democratic economic policy also touches on a number of different levels which will be taken up in this volume, in particular the issue of what distinguishes social democracy itself.

A first answer to this question is offered by the SPD in its basic programme:

*»The Social Democrats not only guarantee civil, political and cultural basic rights for all, but also social and economic rights. This safeguards the equal social participation of all by means of social democratisation, especially codetermination, the preventive social welfare state based on civil rights and a coordinated market economy ensuring the precedence of democracy over markets.«*  
(Hamburg Programme 2007: 19)

## 2. FOUNDATIONAL ECONOMIC THEORIES

### In this chapter

- the historically most influential economic theories are presented;
- their contemporary significance is considered;
- their importance for social democracy is presented.

»Practical men, who believe themselves to be quite exempt from any intellectual influence, are usually the slaves of some defunct economist«, wrote John Maynard Keynes (Keynes 1966: 323), himself one of the most important economists in history. In this chapter the essentials of his theories and those of the two other most important and influential economists, Adam Smith and Karl Marx, are presented and compared. This marks out the three poles of the historically most important economic theories.

But is it worth troubling oneself with the ideas of economists who lived so long ago? Do their explanations still apply to a constantly changing globalised world or are they outdated, no longer comprehensible and refuted by history?

Why and in what ways do these theories have significance for social democracy? They can be of use in two ways.

First, in many instances they constitute »ideological quarries« which policy can take advantage of. Getting acquainted with these sources can help in examining the substance of economic policy arguments, ensuring that one is not »blinded« by ideology.

Second, although social democracy is not entirely in thrall to any of the three economic theories, but constitutes a general normative framework, it does draw on all three theories, albeit with a clear preference towards managed capitalism as described by Keynes.

They have been subject to severe criticism. There have been countless attempts to refute them. They have been pronounced dead – but regularly prove that there is life in the old dog yet. No one seriously concerned with economics can ignore the ideas of Smith, Marx and Keynes.

*Three great economists: Smith, Marx and Keynes*

*Are the classics still relevant?*

*»Ideological quarries«*

*Social democracy: Borrowings from all three*

*The historical context: Smith: Middle of the 18th century*

Any examination of these classics must take into consideration the context of their respective epochs. Adam Smith formulated his ideas in the middle of the eighteenth century, in the age of mercantilism, which taught monarchs that they should finance the luxury of their courts by controlling trade and directing the economy. Smith developed his scepticism towards the state, therefore, based on his experiences of extravagant, self-enriching monarchies, in contrast to, for example, a modern welfare state.

*Marx: Middle of the nineteenth century*

Marx's eloquent critique of capitalism in the mid-nineteenth century sought an answer to the impoverishment of the masses during early industrialisation and the first wave of globalisation. Today the perception of his ideas is shaped by the state socialism of the twentieth century, which gives a sometimes distorted picture.

*Keynes: The 1930s*

Finally, in the 1930s Keynes analysed an economic liberalism which, in view of the global economic crisis, was obviously coming apart at the seams. His *General Theory of Employment, Interest and Money* was not least an attempt to offer proposals for the stabilisation of the economic system in order to prevent other democracies from descending into radical dictatorship. With the global financial crisis which began in 2007 Keynes's ideas have enjoyed a renaissance. Both his observations on global financial market regulation and state investment programmes are being intensely debated again.

*Timeless ideas and economic models*

Consideration of the three great economists Smith, Marx and Keynes, besides providing basic orientation, has another, very practical advantage. Many economic models and explanations familiar to us today and which we deploy frequently, without knowing their origin, were formulated by them.

	Smith	Marx	Keynes
When	Mid-eighteenth century	Mid-nineteenth century	1930s
Occasion	Mercantilism, absolutism	Industrialisation and impoverishment of the workers	Global economic crisis and emergence of dictatorships
Main aim	Freedom from the mercantilist state	Improvement of the situation of the workers and their liberation from exploitation	Safeguarding democracy by stabilising the economy and the labour market
Links to social democracy	Freedom and the model of cooperation	Model of »decent work« and the issue of the balance between labour and capital	Model of the coordinated economy and active economic policy

The image of the »invisible hand of the market«, for example, was introduced by Adam Smith. It is supposed to explain the efficiency of the market. Today it is sometimes used in the form of a mythological transfiguration in accordance with which the market can fix anything.

In contrast, anyone seeking a policy which can ensure »decent work« cannot ignore Marx. It was he who came up with the crucial concept of the »alienation of labour«.

Keynes, finally, coined the oft cited saying »in the long run we are all dead«. He was calling for the state to take responsibility for counteracting market failures. His remark is directed primarily against those who rely on the long-term – which often means a very long time indeed – ability of the market to heal itself instead of the economic policy responsibility of the state.

*Smith: The »invisible hand of the market«*

*Marx: »Decent work«*

*Keynes: »In the long run we are all dead«*

**Further reading:**  
*Nikolaus Piper (ed.) (1996), Die großen Ökonomen: Leben und Werk der wirtschaftswissenschaftlichen Vordenker, Stuttgart.*

## 2.1. Adam Smith – Founder of Economic Liberalism

Smith: »The Wealth of Nations«

Historical context:  
Mercantilism in the  
mid-eighteenth  
century

Smith's aim:  
overcoming  
mercantilism

The foundational work of economic liberalism is »The Wealth of Nations«, published by Adam Smith in 1776.

At this time Great Britain found itself in a period of transition from mercantilism to capitalism (Gerstenberger 2006: 40, 57–65; and Conert 2002: 64).

At this time Great Britain found itself in a period of transition from mercantilism to capitalism (Gerstenberger 2006: 40, 57–65; and Conert 2002: 64).

In the mercantilist era, which lasted from the sixteenth to the eighteenth century, princes and kings measured the success of their economic policy in terms of the amount of gold and silver they were able to amass. Trade was regarded as a zero-sum game: whatever a country obtained was at the expense of another country. Imports of goods were therefore subject to high protective tariffs and the import of commodities was promoted. Royal courts tried to direct the economy. The guilds regulated in detail who could pursue which activities and in what quantity of goods could be produced.

Smith wrote what one might call his »capitalist manifesto« in order to break open this rigid economic order. His ideas fell on fertile soil and he contributed to the liberalisation of the economy and trade.

Smith fundamentally transformed the theory of what constituted the wealth of a national economy. He measured wealth exclusively in terms of work performed and not, as the mercantilists did, in terms of gold reserves.

**Adam Smith** (1723–1790) is regarded as the father of economic liberalism and lived and worked as a moral philosopher and customs official in Scotland.

He put forward the thesis that, assuming the free play of market forces, prosperity would be maximised if everyone pursues their own interest. Smith published the book *An Inquiry into the Nature and Causes of the Wealth of Nations* (usually referred to simply as *The Wealth of Nations*), which can be regarded as the foundation of the modern economy, in 1776. His basic ideas are taught in economic textbooks to this day.

Less well known is the fact that the moral philosopher Smith, in *The Theory of Moral Sentiments*, declared that fairness, trust and honesty are essential for economic activity and that mutual sympathy is the most important motivating force behind social coexistence.

According to Smith there are three sources from which general prosperity can be achieved:

- striving for one's own interest and property
- division of labour and specialisation
- free trade and competition

He described by way of an example how striving for one's own interest and property can be productive and ultimately serve the common good.

*»It is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own self interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages«*  
(Smith 1974: 17).

In the very first sentence of *The Wealth of Nations* Smith described the division of labour as the essential driving force of economic development:

*»The greatest improvement in the productive powers of labour, and the greater part of the skill, dexterity, and judgment with which it is anywhere directed, or applied, seem to have been the effects of the division of labour«*  
(Smith 1974: 9).

He explained the benefits of the division of labour using the example of a pin factory. An individual pin-maker can produce only a few pins a day. However, if production is divided up into several stages, each performed by a specialist worker concentrating on one »distinct operation«, several thousand pins can be produced in a day.

Finally, Smith advocated free trade and free competition. Much as in the case of the division of labour between different workers, parties who can trade freely with one another can specialise in what they do best. Overall productivity can be increased in this way. Allocation through the »invisible hand of the market«, according to Smith, is more efficient and creates more incentives than any form of central economic planning. Smith gave the example of trade between Scotland and Portugal.

*Three sources of prosperity*

*Striving for one's own interest*

*Productivity through the division of labour*

*Prosperity through free trade and competition*

*Taking advantage of »comparative advantage« through trade*

While Scotland was particularly good at producing wool, Portugal was good at producing wine. Smith called this a comparative advantage. If the two countries concentrated on their own specific products and traded instead of trying at great expense to produce both wine and wool both would benefit.

This consideration diverged from the contemporary view that trade is a zero-sum game. Ironically, as a customs official Smith was responsible for the observance of mercantilist trade regulations for over a decade.

*What is »Laisser-faire«?*

In order to let the sources of prosperity – pursuit of profit, division of labour, trade and competition – do their work the state, according to Smith, should influence the market only indirectly, leaving it as much freedom as possible. This led to the so-called »laissez-faire« doctrine.<sup>2</sup> It implies that the state should confine itself to ensuring public safety, national defence, legal certainty, infrastructure and education and otherwise should not intervene in the market. This will result in the greatest possible productivity.

*Unleashing the productive forces*

Smith laid the theoretical foundations for the liberalisation of the economy which, primarily in the nineteenth century with industrialisation, unleashed hitherto unprecedented productive forces. Smith assumed that a free market economy would automatically find a balance and did not foresee crises and recessions.

*Problems with the division of labour*

Similar to Marx, who analysed the exploitation of the workers and the alienation of labour, Smith was also aware of the dark side of capitalism. He feared that constant refinement of the division of labour would lead to the »mental mutilation« of workers and, to make up for it, called for more educational opportunities.

*Smith: The Theory of Moral Sentiments*

In his lesser known work *The Theory of Moral Sentiments* (1759) Smith describes people's need to behave decently and fairly and to overcome their egoism as beings with collective needs. He thereby refutes those who wish to rope him in as principal witness for the view of humanity as the purely utility-maximising homo oeconomicus.

Smith regarded himself as, first and foremost, a moral philosopher rather than as an economist, emphasising the importance of fairness, trust and honesty in business dealings.

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<sup>2</sup> Laissez faire (French) means something like »letting [people] do as [they] choose«.

Individual interests → Common good

**State as regulatory framework**

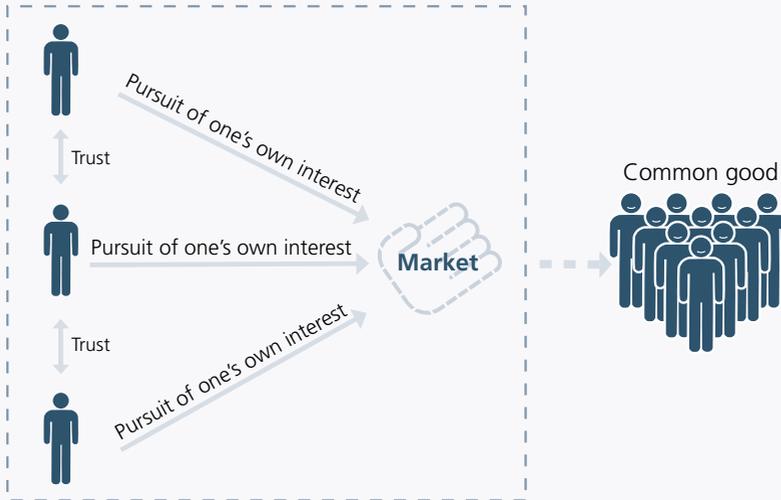


Figure 1: Smith: Promoting the common good through self-interest

The classic theory of economic liberalism, which was based on Smith, remained dominant until the global economic crisis of 1929. Only in the wake of the latter did widespread doubts emerge concerning whether markets led by the invisible hand always achieve equilibrium. The severe crisis and the sustained high unemployment which followed it could not be explained on the basis of the *laissez-faire* approach. Classic economic liberalism was shaken to its foundations. Nobel Prize winner Joseph Stiglitz, looking back, has remarked that »the reason the invisible hand often seems invisible is that it is not there« (Stiglitz 2002).

The next few decades comprised the era of Keynesianism, as described in the next section. Only after years in the wilderness did economic liberalism undergo a renaissance, from the 1980s, in the hands of the neoliberals.

The most famous of the economists who revived, developed and propagated Smith's ideas were Friedrich August von Hayek and Milton Friedman. The lat-

ter established an economic liberal ideology which also became known as the »Chicago School« (Friedman was a professor in Chicago). However, the neoliberals confined Smith's ideas to his critique of the state and his advocacy of the free market. Hayek and Friedman disregarded his »theory of moral sentiments«.

*Reinterpretation  
under Thatcher and  
Reagan*

Their reinterpretation of Smith's work became extremely influential, especially in the USA under President Ronald Reagan and in the UK under Prime Minister Margaret Thatcher. The guiding principle of the policies of both these figures was that the state is not part of the solution to the problem, it is the problem. That meant deregulation, privatisation and the reduction of state benefits.

*Washington  
Consensus*

Believers in the market also exercised great influence over the policies of the World Bank and the International Monetary Fund. Within the framework of the so-called Washington Consensus these institutions spread the economic liberal ideology, for example, in Latin America, the post-communist states and, after the 1997 Asian crisis, in Southeast Asia. The deregulation of financial markets was also decisively influenced by this ideology. Its consequences included the worst crisis in the global financial architecture for decades and a global recession from 2008. The scope and magnitude of the crisis have led to an economic and political rethink. Instead of economic liberalism with its blind faith in the market, now gaining the upper hand are those seeking a new balance between state and market and who emphasise the primacy of politics over the economy.

**Further reading:**

*Helen Winter and  
Thomas Rommel (1999), Adam  
Smith für Anfänger.  
Der Wohlstand  
der Nationen: eine  
Leseintroduction,  
Munich.*

## 2.2. Karl Marx's Critique of Capitalism

**Karl Heinrich Marx** (1818–1883) was a German philosopher and political journalist.

What liberal economists saw as stability and growth as a result of the development of the free market Marx described as class conflict, exploitation, impoverishment and a crisis-prone system which could lead to a revolution of the proletariat.

Marx's most important economic publication (partly posthumous) was »Das Kapital« (Capital), whose three volumes appeared between 1867 and 1894. The »Communist Manifesto«, published in 1848, exerted enormous political influence.

The critique of capitalism of the German philosopher Karl Marx is often seen as a theoretical counterblast to Smith's ideas. That is only partly true: Marx studied Smith's work closely and came to similar conclusions. If anything, the forces of production and innovativeness of capitalism are emphasised even more strongly by Marx than by Smith. However, Marx drew very different conclusions. Unlike Smith Marx saw capitalism as inherently unstable and destructive, leading

not to the »wealth of nations«, but to the impoverishment of the vast majority of workers.

In order to be able to understand Marx's ideas one has to put oneself in the precarious circumstances of workers during the period of early industrialisation in the nineteenth century. A document from the Museum of Industrial Culture in Duisburg conveys this vividly: (Baier u. a. 2002: 18):

*»While the affluent built an exclusive residential area on the outskirts of the city dreary rows of ugly apartment houses were built for the workers which were overcrowded, unhygienic and overpriced ... For example, often a whole family and a lodger slept in one room, with several people sharing a bed in rotation: sleeping patterns corresponded to shift work. Working conditions in the factories were geared entirely to the machines to which the workers who served them had to adapt themselves. Seventy-hour working weeks were the rule and in the textile industry even 80 hours. Child labour was widespread, social security was almost unknown and health care was poor.«*

This description applies more or less to living and working conditions in many poorer countries today.

*Marx: Relations to Smith*

*Historical context: Early industrialisation in the mid-nineteenth century*

*Exploitation as a  
consequence of  
capitalism*

Marx regarded these inhuman living and working conditions not as an unfortunate accident, but as a necessary consequence of capitalism. According to his analysis the free market led inevitably to misery and exploitation since the profits of the capitalists are the result of the exploitation of the workers.

*The concept of  
»surplus value«*

Of central importance is Marx's theory of »surplus value«, which he presented in the first volume of *Capital* in 1867 and set out in the volumes which appeared posthumously. Surplus value is the value which the entrepreneur can realise as profit in exchange over and above his invested capital: for example, if he has put 100 euros into production (which would be a proportionate reward for the goods and all means of production) but realises 110 euros on the market. According to Marx this surplus value can be obtained systematically only from value-creating labour. In other words, if the worker creates more value than he receives in the form of wages.

**Surplus value** arises, according to Marx's labour theory of value, from the profit obtained by the entrepreneur from the output of the workers after the deduction of wage costs and expenditure on the means of production. Surplus value is therefore synonymous with the exploitation of the workers. Marx distinguishes further between absolute surplus value, which comes into being simply through overtime (longer working time), and relative surplus value, which is achieved through increasing productivity (Wirtschaftslexikon 2009).

Marx described how the workers received only the wages needed to maintain their subsistence. The capitalists, in contrast, enriched themselves from the difference between this wage and the surplus value the workers created.

He assumed that the capitalist – driven by ever increasing competition – tries to increase this surplus value. Wages fall further, working time is increased and the deployment of machinery is stepped up. The consequence is rising unemployment. At the same time, competitors are gradually driven out of the market. Finally, society is increasingly divided between those without property and a small group in whose hands capital is concentrated.

In the so-called *Economic and Philosophical Manuscripts* written in 1884, besides the concept of »surplus value«, Marx also identified the notion of the

**Further reading:**

*Volker Happe,  
Gustav Horn and  
Kim Otto (2009),  
Das Wirtschafts-  
lexikon. Begriffe.  
Zahlen. Zusammen-  
hänge, Bonn.<sup>3</sup>*

<sup>3</sup> We would like to thank the publisher J.H.W. Dietz Nachf., Bonn, for the opportunity to use definitions from its Economic Lexicon in this volume.

»alienation of labour«. In this Marx (as Adam Smith had done) discerned the dark side of the division of labour in production. In mass production the worker is involved only in extremely limited and monotonous stages of production. He is deprived of contact with the ultimate product and the satisfaction associated with producing it.

For Adam Smith, competition and the division of labour were the well-springs of progress. Marx, by contrast, regarded competition and the division of labour as the root evil of capitalism and the cause of exploitation and alienation. He perceived that production advances in his time benefited only the capital owners, while impoverishing the workers.

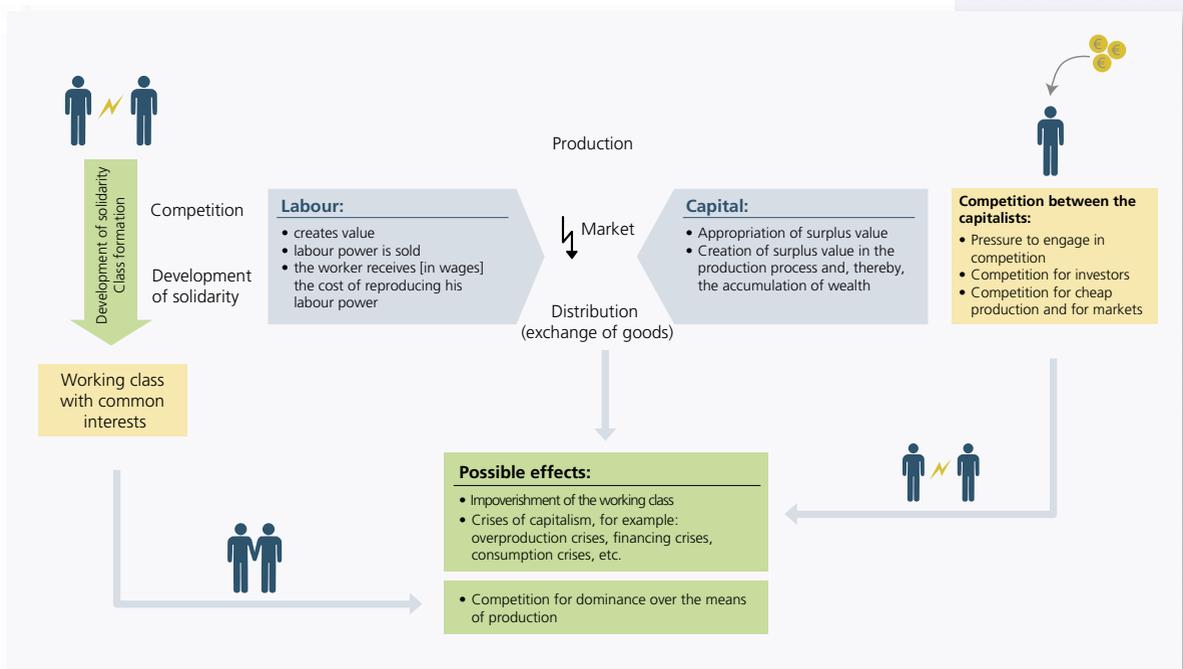


Figure 2: Basic structure of Marx's argument

*Instability of  
capitalism*

A profit-oriented economic order, according to Marx, is unstable and crisis-prone. In his view, it could lead ultimately to a revolution by the exploited.<sup>4</sup>

*»Centralisation of the means of production and socialisation of labour at last reach a point where they become incompatible with their capitalist integument. This integument is burst asunder. The knell of capitalist private property sounds.«*  
(Marx 1991: 684 f.)

*Private ownership  
of the means of  
production as the  
hallmark of a class  
society*

A final key concept in Marx's theoretical armoury, which he addresses primarily in the Communist Manifesto of 1848, is »property« or »ownership«, particularly in the sense of private ownership of the means of production.

Private ownership of the means of production, for Marx, is a distinguishing feature of capitalism's class society. After the proletarian revolution predicted by Marx in his early writings private ownership would, in his opinion, be abolished. The working class, due to the low – barely sufficient to maintain subsistence – wages it receives, has no chance of acquiring significant property. The capitalists, in contrast, appropriated their property through exploitation.

*Political demands  
in the Communist  
Manifesto*

Marx therefore demanded in the Communist Manifesto, among other things:

- centralisation of credit in the hands of the state through a national bank with state capital and a sole monopoly
- centralisation of transport in the hands of the state
- multiplication of state-owned companies, means of production, cultivation and improvement of all estates in accordance with a communal plan (see Marx/Engels 1987: 54).

*Problems of  
nationalisation*

Marx's most important interpreter, Friedrich Engels, saw problems in such nationalisation: »the more [the state] proceeds to the taking over of productive forces, the more does it actually become the national capitalist, the more citizens does it exploit ... the capitalist relation is not done away with. It is rather brought to a head« (Engels 1988: 553f).

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<sup>4</sup> In the literature on Marx different answers are given to the question of whether he considered revolution a necessary or only a possible historical development. Decisive in this respect is the question of whether one distinguishes between different phases of Marx's work or take his oeuvre as a whole. For further reading, see: Heinrich (2004: 169–78).

The following quotation is attributed to the economist John Kenneth Galbraith: »Under capitalism, man exploits man. Under communism, it's just the opposite.« States such as the Soviet Union and the former East Germany (DDR), which carried out the demands of the Communist Manifesto for centralisation and nationalisation of the banks, the transport system and the means of production, failed.

Marx interpreted history as a result of class struggles, which reach their peak in the encounter between the bourgeoisie and the proletariat and could culminate ultimately in a proletarian revolution. He developed the utopia of a classless society without competition and private ownership of the means of production.

History has shown, however, that the impoverishment of the workers described by Marx and the increasing concentration of property among capital owners is not inevitable. It was possible to distribute the gains in prosperity more fairly, not least through the organisation and solidarity of the workers in trade unions and the creation and consolidation of the welfare state.

The terms **»Bourgeoisie«** and **»Proletariat«** which Marx used refer to the opposing classes. The term »proletarian« is derived from the Latin »proletarius« (»belonging to the lowest social stratum«). The term »bourgeoisie« is derived from the French and refers to the »full-fledged property-owning stratum« (entrepreneurs, capitalists, managers, rentiers).

The concentration of capital was breached by the »creative destruction« described by Austrian economist Joseph Schumpeter. He depicts how companies are perpetually reorganised as a result of innovations, competition, crises and new markets.

*»The opening up of new markets, foreign or domestic, and the organizational development from the craft shop and factory to such concerns as U.S. Steel illustrate the same process ... that incessantly revolutionizes the economic structure from within, incessantly destroying the old one, incessantly creating a new one. This process of creative destruction is the essential fact about capitalism.« (Schumpeter 1942: 137f).*

*History as the result of class struggles*

*Impoverishment is not inevitable*

*Schumpeter: »creative destruction«*

The automobile industry replaced coachmen, blacksmiths and stable boys. The typewriter manufacturer has to make way for the computer manufacturer. These are examples of creative destruction which, on the one hand, promotes innovation but, on the other hand, creates new uncertainties and requires enormous flexibility from people.

*Failure of state  
socialism*

The experiment with state socialism, which based itself on Marx, has failed and its theoreticians have been discredited. Has the theory therefore been refuted? The fact is that, so far, no functional alternative has been found to an economic order based on market efficiency and private property, which has stood up in practice.

*Enduring value of  
Marx's analyses*

Marx was a better analyst than guide. No practicable solutions can be derived from his doctrines and his predictions have not come true. However, his analyses still attract attention. More than anyone else Marx heightens one's awareness of the dangers and crises of an unrestrained capitalism.

*How should Marx  
be classified?  
Willy Brandt:  
»the pursuit of  
freedom«*

How should Marx be classified, therefore? Perhaps in the manner recommended by Willi Brandt on a visit to the Karl-Marx-Haus in Trier in 1997: »One does justice to Marx best by taking him down from his pedestal, in both a positive and a negative sense. Whatever people have made of Marx or would like to make of him, the pursuit of freedom, the liberation of man from servitude and abject dependence was the principal motif of his thought and actions.«

**Further reading:**

*Francis Wheen  
(2008), Marx's  
»Das Kapital«:  
A Biography*

## 2.3. John Maynard Keynes: The Management of Capitalism

**John Maynard Keynes** (1883–1946) was a British economist who had a major influence on twentieth century economic theory.

In his influential work *General Theory of Employment, Interest and Money* (1936) he called into question the ability of markets to heal themselves and founded what came to be known as »Keynesianism«, the aim of which is to steer capitalism.

Keynes also worked on the development of the Bretton Woods system which laid down the rules for the global economy and financial markets in the post-War period.

Both Adam Smith's doctrine of free capitalism with as little state intervention as possible and Karl Marx's rejection of competition and private ownership of the means of production, therefore, are problematic. Is there a middle way of coordinated capitalism which harnesses the market's productive forces, but counteracts and cushions its destructive forces?

The British economist John Maynard Keynes analysed the Janus-faced<sup>5</sup> nature of capitalism: while

efficient and productive, it is also structurally unstable. Although he believed in a market order based on property and competition he was critical of the neo-classical school, which referred back to Smith's doctrines.

For example, he criticised the fact that its »assumptions are seldom or never satisfied, with the result that it cannot solve the economic problems of the actual world« (Keynes 1966: 319).

In the face of the profound global economic crisis in 1929 Keynes also called into question the »invisible hand«. The market had not found its level again, which is what Smith's assumptions would lead one to expect, but rather unemployment had remained at a high level and economic stagnation had set in.

Keynes identified a downward spiral: if fewer goods are produced and workers are laid off consumers and producers become uncertain and spend less money (»panic saving«). Demand continues to fall, companies produce less and cut more jobs, people save still more, and so on. The crisis goes from bad to worse

*Keynes –  
A middle way?*

*Keynes's critique  
of the Neoclassical  
School*

*Doubts about the  
»invisible hand«*

*Danger of an  
economic  
downward spiral*

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<sup>5</sup> The Roman god Janus was endowed with two heads, one facing forward and the other backward.

and the economy risks falling into a lasting depression. In the wake of the world economic crisis, in which this is exactly what happened, this fell on fertile soil. Keynes not only recognised situations in which the free market does not function but, in the form of anti-cyclical economic management, developed ideas about how to counteract it.

*Active intervention  
by the state  
called for*

In an economic downturn the state must intervene in the market and make up for private demand, borrowing and issuing more money. It could give people money directly, for example, by reducing taxes. However, this approach could fall flat if people continued to save in response to uncertainty. More effective is for the state to spend directly, for example, by building roads or schools. As a result of this additional spending more people would be employed, who would then consume more, create demand and set in motion a positive spiral. Keynes put it like this:

*Economic  
management by  
the state*

*»If we spend more than 150 million pounds everyone will have a higher income; and those who are unemployed no longer need unemployment benefit. In addition, this spending will bring many other people into employment. The money will circulate in the economy and be spent on all manner of goods and not be concentrated on a few industries.«*

(Keynes 1939, quoted in Weinert 2008)

*»In the long run,  
we are all dead«*

This was his justification for abandoning the belief that the market always achieves equilibrium, as Smith had assumed. His remark – already mentioned – that »in the long run we are all dead« is well known. This amounted to an appeal for the state to take responsibility: it is more important to create jobs and growth today than to trust vaguely in some better future and a self-regulating market.

Keynes conceded, however, that market intervention is risky: it is difficult to know when to step in and to what extent. He wrote:

*»The outstanding fact is the extreme precariousness of the basis of knowledge on which our estimates of prospective yield have to be made. Our knowledge of the factors which will govern the yield of an investment some years hence is usually very slight and often negligible.«*

(Keynes 1966: 126)

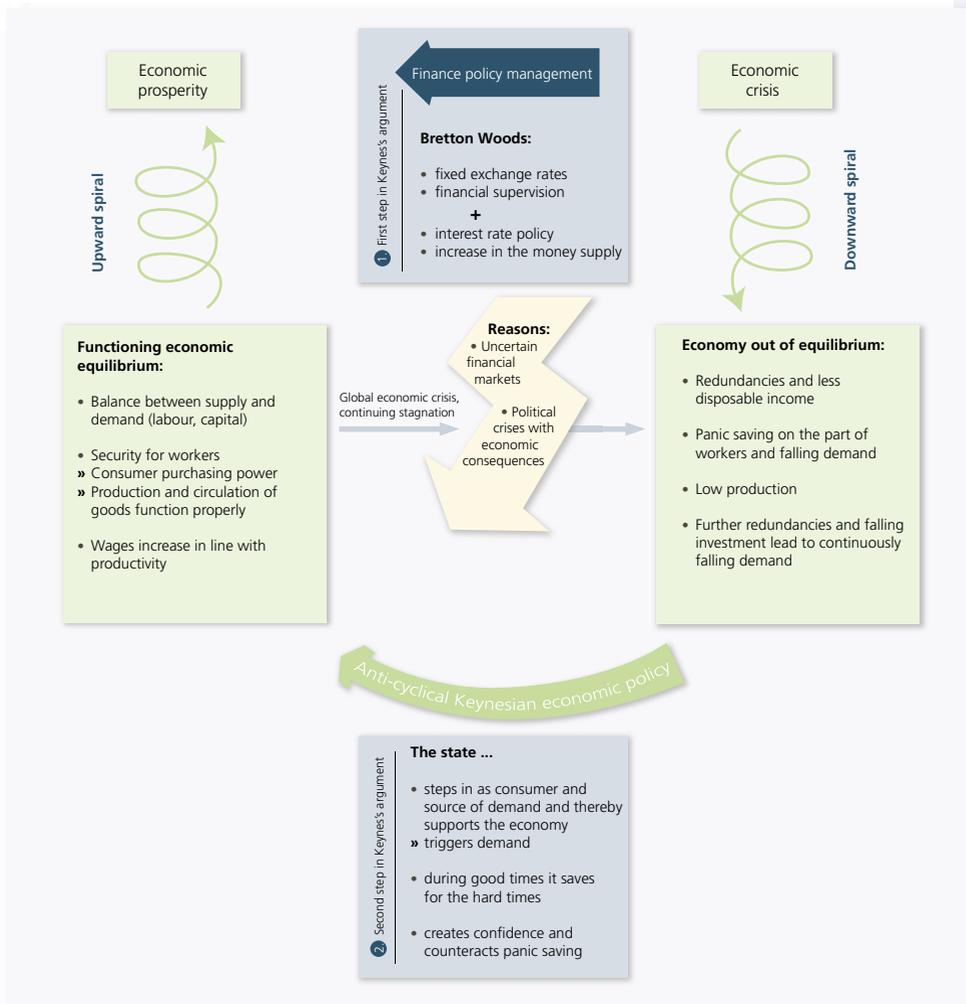


Figure 3: Basic structure of Keynes's argument

Keynes's analyses and recommendations that the state must intervene in the market were such a formative influence on his time that his opposition to both Smith and Marx is often described as a »Keynesian revolution«. Reactions to his ideas have reflected this. (Economic) liberals and conservatives have described Keynes as a closet socialist, while Marxists have reproached him with having too much faith in the market. What is certain is that Keynes, in an effort to oppose the emerging dictatorships – not only in Germany – sought to preserve democracy.

*The so-called  
Keynesian  
Revolution*

*»The authoritarian state systems of today seem to solve the problem of unemployment at the expense of efficiency and of freedom. It is certain that the world will not much longer tolerate the unemployment which, apart from brief intervals of excitement, is associated and, in my opinion, inevitably associated with present-day capitalistic individualism. But it may be possible by a right analysis of the problem to cure the disease whilst preserving efficiency and freedom.«*  
(Keynes 1966: 321)

*Fundamental Psychological Law*

Furthermore, with his »Fundamental Psychological Law«, Keynes supplied a reason why redistribution can be not only socially desirable, but also economically rational. A dynamic economy requires sufficient demand. Top earners tend to save a high proportion of their income. To stimulate demand it makes therefore sense to give low earners, whose rate of saving is lower, more income.

*Keynes's influence on the twentieth century*

Finally, Keynes played a decisive role in the construction of the so-called Bretton Woods system.

Keynes's influence is unmatched by any other economist in the twentieth century. Keynes's recommendations were implemented first in the United States within the framework of President Roosevelt's »New Deal« from 1933. First, public investment – for example, in infrastructure – was increased significantly. Second, consumption was boosted by an increase in social security benefits, since those on low – or with no – incomes have a low rate of saving. Keynes's doctrines remained the economic orthodoxy into the 1970s. In Germany, they were represented in particular by the economist Karl Schiller, who was SPD Minister of Economic Affairs and Minister of Finance between 1966 and 1972. During this period even the conservative US President Richard Nixon declared: »We are all Keynesians now«.

**Bretton-Woods-System:** In 1944, at a conference at Bretton Woods in the USA, the international financial architecture of the post-War period was agreed. At its core was an international currency system under which exchange rate fluctuations were curbed through a linkage to the US dollar. The International Monetary Fund (IMF) and the World Bank were set up as institutions for international lending and financial market regulation. The Bretton Woods system remained in place until 1973. After currency market turbulence the dollar peg of exchange rates had to be given up.

*Problems with Keynesianism*

From the mid-1970s, however, Keynesianism experienced a crisis. On the one hand, anti-cyclical budgetary policy did not function in the manner envisaged

by Keynes. Although spending was increased during crisis periods government debt was not repaid when the economy took a turn for the better. As a result, public debt piled up and the scope for deficit spending was progressively reduced as crisis followed crisis. On top of all this came the two oil crises. The enormous oil price hikes generated a vicious circle: wages were raised, but higher energy prices ate up the additional income, in response to which wages were increased yet again, leading to rises in inflation, which in turn further increased wage pressure. Economic stimulus packages were ineffective. There was economic stagnation coupled with high inflation («stagflation»). Neoliberal and new classical economists stepped forward, emphasising enterprise-friendly supply-side policy: efforts to boost locational advantages through cost reductions, budget consolidation and austerity measures were the order of the day.

**Stagflation:** When economic stagnation and inflation coincide (Wirtschaftslexikon 2009).

After years of economic liberalism the calls for state intervention in a largely deregulated market –

among other things as a result of the financial market crisis which began in 2007 – are growing louder. A return to Keynes is also discernible. That is not really surprising since what Keynes wrote about international financial markets is more apposite than ever:

*»Speculators may do no harm as bubbles on a steady stream of enterprise. But the position is serious when enterprise becomes the bubble on a whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done.«*  
(Keynes 1966: 134)

**Further reading:**

Reinhard Blomert (2007), John Maynard Keynes, Reinbek.  
Heinz-J. Bontrup (2006), Keynes wollte den Kapitalismus retten. Zum 60. Todestag von Sir John Maynard Keynes, Bonn.

## 2.4. Ideal Types of Economic Theory

In everyday political debate the ideas of Smith, Marx and Keynes are ubiquitous. If a liberal (in the sense of »economic liberal«) politician seeks to strip down the state to its core functions and declares that the state is not part of the solution but the problem itself, this is in line with the thought of Adam Smith. In periods of unrestrained globalised capitalism, in which markets increasingly come apart at the seams, Keynes's solutions with regard to the management of the market economy become relevant again. And in the face of images of factories in developing countries in which workers stitch clothes for 14 hours a day for exploitative wages Marx's analyses come easily to mind.

That is not surprising because, ideal-typically,<sup>6</sup> Smith, Marx and Keynes represent three very different economic world views which are repeatedly rolled out when questions of distribution, relations between market and state and other economic policy issues come to the fore. The three ideal-types can be described as follows:

### 1. Pure capitalism

1. The state should keep out of economic processes. Striving for property is the driving force of economic activity and should therefore not be infringed (the libertarian view, following Smith).

### 2. Anti-capitalism

2. The capitalist economic system, which is based on private ownership of the means of production and competition, leads to the exploitation and impoverishment of the masses. For that reason, it should be abolished (the communist view, following Marx).

### 3. Managed capitalism

3. The economic order is based on property and the market economy, but the state, through regulation, redistribution and macroeconomic management – in other words, through the deliberate management of demand – intervenes in the economy. Property is safeguarded, but it is socially embedded and has obligations towards society (social democracy, following Keynes).

*»As much market as possible, and as much planning as necessary«*

From economic theory it is clear that the unrestrained market breaks down in the same way as attempts to do without a market order. History shows that both market radicalism and the complete abolition of the market have failed.

<sup>6</sup> »Ideal-typical« is meant here in the sense of sociologist Max Weber, namely the deliberate exaggeration of reality in order to order or capture segments of social reality theoretically. But »ideal-typical« also means that in this introductory volume only a simplified glimpse of the relevant ideas is possible.

Capitalism has to be guided and managed, if the goals of social democracy are to be achieved. The SPD's Godesburg Programme of 1959, thanks to the efforts of economist Karl Schiller, who at that time exerted considerable influence over the SPD, put it in a nutshell: »As much market as possible, and as much planning as necessary.«

As already mentioned, the theories presented here must be assessed in their historical context. Clearly, capitalism has not collapsed as a result of its internal contradictions, as Marx predicted. However, it has not settled down into a harmonious equilibrium, as Smith had expected. The twentieth century was characterised by hitherto unprecedented prosperity for large segments of the population, but also by social upheavals and countless crises. How can these developments be evaluated from a social democratic standpoint? Matthias Platzeck, Peer Steinbrück and Frank-Walter Steinmeier offer a possible answer in their 2007 book »Auf der Höhe der Zeit« (Up to Date):

*»Against the narrowly economic thought of the orthodox Marxists, on the one hand, and of the liberals on the other, ›revisionist‹ social democrats around Eduard Bernstein posited both the primacy of politics and the principles of reform and progress, compromise and interest reconciliation across class lines. Where others put their trust in the spontaneous development of economic and historical forces social democrats emphasised the active and pragmatic management of transformation. They wanted proactively to combine market dynamism with social reform and renewal of society in order systematically to make growth and prosperity accessible to all segments of the population. Not only to reconcile the market economy, democracy and social cohesion with one another, but by political means also to bring about their positive interaction: this was the historically new and unprecedented plan for progress put forward by social democrats at the beginning of the twentieth century. For the first time, they were able to reconcile in practical terms and with unprecedented success what had previously always been regarded as incompatible and mutually hostile: a dynamic market economy, a vibrant democracy and social cohesion. Sociologist Ralf Dahrendorf's notion of the ›social democratic twentieth century‹ is therefore fully justified. ... It is important once more to recall clearly how hard won was the victory of social democracy against its opponents – and how vulnerable the fruits of this success are in the twenty-first century. ... A self-conscious social democratic party must therefore urgently reflect on how enormously important and pioneering those*

*What answers to these questions can social democratic politicians offer?*

*ideas still are for the world of the twenty-first century which it developed originally in its encounters with Marxist orthodoxy and liberal laissez-faire. Because in terms of the fundamental internal mutual tension between markets, democracy and society nothing has changed in the era of globalisation.«*  
(Platzeck, Steinbrück and Steinmeier 2007: 19–21)

## 2.5. Economics Today

*Where does  
economics stand  
today?*

After the presentation of the historically most important economists the question arises of where economics stands today. How difficult it is to answer this question is illustrated by the following story.

*A difficult question:  
an example*

On the occasion of the UK's accession to the European Community in 1973 a letter appeared in *The Times* newspaper signed by 154 economists stating that Britain's EC membership would probably bring more disadvantages than benefits. The next day a statement by 142 (different) economists was published which declared that Britain's entry would probably bring more economic benefits than disadvantages. This was followed by a letter from a reader which hypothesised that economists would probably bring the UK more economic disadvantages than advantages (quoted in Wagner and Wiegard 2002: 773).

*No dominant view:  
two reasons*

This anecdote shows that there is no dominant view in economics. There are two main reasons for this

*First: no science is  
build on »rock«*

First, economics, like all sciences, is in the words of philosopher Karl Popper built not on rock but on marshland. In other words, the data, facts and observations from which economists draw their conclusions are subject to imprecision or can simply be wrong.

*Second: economic  
utterances are  
value-laden*

Second, economics in particular is value-laden. Unlike the natural sciences its assumptions and theories are determined by views of humanity and society. An economist who believes that man is a utility-maximising *homo oeconomicus* will reach different conclusions from an economist who regards man as a complex social being.

A sobering reminder that economics, which is supposedly built on hard facts, also includes a great deal of ideology and that therefore economists' recommendations must always be examined critically was published by economic journalist Andreas Hoffmann:

*»I cannot get on an aeroplane without thinking about subsidies. Economists hate subsidies. Subsidies come from the dark side, they paralyse the economy. However, without subsidies there would be no Airbus in the sky. We only fly Airbus because some heads of government wanted to build aeroplanes. Otherwise, Boeing would rule the skies like Bill Gates rules the world of computers. ... Or take the power of the trade unions. Allegedly, trade unions hinder enterprises in their pursuit of profit. Why then have precisely German car makers and machine building, metalworking and electrical firms been so successful throughout the world? In fact, they should have failed because their trade unions are the strongest? ... It is not much use referring to the real world with proper economic experts. One is likely to receive a disapproving look, followed by a declaration that reality is not the issue but rather the »economic policy approach«. ... But why is the map so utterly wrong so often? The First World War should never have broken out because economists regarded it as unprofitable. Eight days before Black Thursday in October 1929 star economist Irving Fischer said that there would never be a stock market crash. Not one of the five recessions which have taken place in Germany has been scientifically predicted; nor was the Internet boom in the 1990s. In autumn 2002 the Institute predicted 1.3 per cent growth for 2003: in the event, the economy shrank by 0.2 per cent. At present, everyone is racking their brains about why jobs are being created in Germany and the economy is growing again. Oil is too expensive and Angela Merkel is bungling the reforms.« (Süddeutsche Zeitung, 16 September 2006)*

But of course economics is not an exact science, able to make precise predictions but, on the basis of assumptions, puts forward more or less plausible empirically grounded theses.

What consequences can be drawn from this realisation. Certainly not that economics should therefore be regarded as unscientific or that its assertions can be interpreted entirely arbitrarily. However, it is important that economists be open about their assumptions and points of view, allowing those who read them to categorise and interpret them against this background.

*Economics is not an exact science*

*Consequence: make clear one's own particular standpoint*

*Two camps:  
supply-side and  
demand-side policy*

Roughly speaking, economists today can be divided into the supply-side camp and the demand-side camp, the boundary between which – to be sure – is fluid and subject to many overlaps.

### **Supply-side Policy**

*Supply-side policy:  
Adam Smith,  
David Ricardo,  
John Stuart Mill*

Supply side-oriented economic policy stands in the tradition of Adam Smith's classical theory, developed by David Ricardo, John Stuart Mill and others. The policy demands that arise from this market liberal theory and its hostility to the state include the creation of conditions that are as favourable as possible for enterprises, enabling them to make good profits. Hence the term »supply-side policy«: the supply of goods and services should be optimised. From this, according to the theory, demand will arise automatically. The state should impinge upon the market as little as possible. Subsidies, public ownership and regulation should be minimised, and taxes and social security contributions should be kept as low as possible. The Central Bank should ensure the stability of the currency, but should not encroach upon the economic cycle.

### **Demand-side Policy**

*Demand-side policy:  
John Maynard  
Keynes*

Demand side-oriented economic policy was founded by John Maynard Keynes and relies on the state playing an active role in promoting employment and managing the economic cycle. Key to this is the maintenance of constant demand in the economy. To this end, wages must grow at least in line with productivity. Henry Ford, who introduced mass production in his factories, thereby boosting productivity, advocated higher wages for the benefit of demand. He is supposed to have commented in this connection that »cars do not buy cars«.

If private consumption and investment slacken the state must step into the breach with investment programmes and employment-intensive measures. As a result of this additional demand enterprises will start investing again, employment will grow and private consumption increase. The Central Bank should do its bit for economic recovery by means of lower interest rates and expansion of the money supply.

### **Distinguishing Features**

*Different concep-  
tions of wages*

A key distinguishing feature of a supply side- as opposed to a demand side-oriented economic policy concerns wages. The former regards wages as a burdensome cost factor which, particularly during crisis periods, have to be reduced. The

latter, by contrast, interprets wages as the decisive demand factor in the economy which must be raised during economic downturns to ensure that a downward spiral does not set in, as was the case in the world economic crisis in the 1920s. Some economists regard lack of demand as the cause of Germany's economic stagnation between 2001 and 2005. Through a combination of years of wage restraint and falling public investment domestic demand fell significantly, putting a strain on the German economy. As a way out of the crisis wage increases and economic stimulus packages were called for (Horn 2005). However, there are two problems with demand policy. First, in practice it has proved difficult during more favourable economic periods to pay back the public debts incurred: among other things, this is why the national debt has relentlessly increased. Ultimately, the scope for economic stimulus programmes and political action progressively diminishes. Second, the conjunction of demand stimulus and a central bank policy of flooding the market with money sometimes led to inflationary wage spirals. At the same time, inflation encouraged »panic saving«, causing consumption to stagnate. The logical outcome of this development at the end of the 1970s was a fatal combination of stagnation and inflation: so-called stagflation.

Which of the two theories is more influential? As already mentioned, from the global economic crisis in the 1920s into the 1970s Keynesian demand policy dominated internationally. As a reaction to the stagnating world economy and the spread of inflation (stagflation), however, at the end of the 1970s neoclassical supply policy experienced a revival. Supply-side policy was advocated from the 1980s by Ronald Reagan in the USA and by Margaret Thatcher in the UK, as well as by – albeit in a diluted form – Helmut Kohl in Germany. In the 1990s, this economic policy direction was reflected in the so-called Washington Consensus and spread virulently throughout the world. Above all, the World Bank and the International Monetary Fund propagated a liberalisation policy which called for tax cuts, privatisation, deregulation, free trade and cutbacks in subsidies. The idea was to boost the market and roll back the state. Former chief economist of the World Bank and Nobel Prize winner Joseph E. Stiglitz has since become a prominent critic of the Washington Consensus. He regards blind faith in supply-side theory as primarily ideological and lacking empirical underpinning. The fact is that there are states which have adhered to the recipes of market liberalisation and whose economies have stagnated, while others have forged ahead both socially and economically on the basis of stronger coordination and management of markets (Stiglitz 2002).

*From Keynesianism in the 1970s to the Washington Consensus in the 1990s*

**Further reading:**  
*A good overview of the background to this debate may be found in the excellent and easily comprehensible book by Peter Bofinger, »Grundzüge der Volkswirtschaftslehre« (2007).*

*A majority of  
German economists  
are supply side-  
oriented*

At present, the majority of German economists appear to be inclined towards supply-side policy. When in 2005 the Red-Green Coalition openly considered reflationary public spending in order to boost demand – in other words, classic Keynesian policy – more than 250 economics professors called for a supply side-oriented economic policy in the so-called »Hamburg Appeal«. Economists who advocate a demand oriented policy have been on the defensive for years, but now they are increasingly getting a hearing.

*Keynesian answers  
to the financial  
market crisis in 2008*

Keynes's demand side theory can explain, for example, why the financial market crisis hit the real economy so rapidly and deeply in 2008, triggering a global recession. Accordingly, many countries have responded with classic Keynesian policies of demand stimulus, expanding public spending and boosting household purchasing power.

The financial and economic crisis since 2008 has led to a major rethink. Even the chairman of the Deutsche Bank, Josef Ackermann, now says: »I don't believe in the self-healing powers of the market any more« (Ackermann 2008) and is calling for a global financial supervision. Market radicals are now on the defensive and Keynes's doctrines are being rediscovered. His theories explain this severe crisis and point towards possible ways out of it.

Keynes's relevance is not mere coincidence: ultimately, his major work – the *General Theory of Employment, Interest and Money* – is the offspring of the global economic crisis of the 1930s, which in a number of ways resembles the current situation. Then, as now, arising from financial market disruption, economies worldwide slumped simultaneously, setting in motion a downward spiral. Due to a lack of purchasing power and worries about the possible advent of an even deeper crisis households are consuming less, enterprises are postponing investment and the banks are still barely lending. Less is being produced, as a result of which jobs are being lost and consumption sinking even further. The crisis of the 1930s was ended initially by an extension of market regulation and state investment programmes based on Keynes's ideas.

How can the origins of the crisis on the US real estate market in 2007 be explained? A gigantic speculative bubble had built up which brought the international banking system to the brink of collapse. Keynes's pupil Hyman Minsky had a plausible explanation for this, based on the work of his teacher (Minsky

1986). During long periods of economic growth greed and an appetite for risk increase. In pursuit of higher profits ever greater risks are taken. Competition between banks tempts them into circumventing regulations with new financial products in order to fund risky investments. When too much risk accumulates the whole house of cards collapses, as we have seen. Minsky's solution is state regulation to protect the market from itself and to avoid financial crises. Keynes called for an end to unregulated global financial markets as early as 1926 in his essay »The End of Laisser Faire« (Keynes 1926). He was also involved in the practical development of regulations for the world market. Among other things, he participated in the Bretton Woods conference, at which a regime for world financial markets was drawn up, which led to several decades of stability. Now this topic is once more on the international agenda. The G20 summit in London in April 2009 has also been described as an attempt at a second Bretton Woods. Small, but important steps were taken in this direction: the global regulation of hedge funds and rating agencies was agreed and a forum for financial stability set up at the International Monetary Fund.

But what ways out of the current crisis might we discern in Keynes? Economic cycles are usually managed by interest rate policy. Accordingly, central banks worldwide lowered interest rates in response to the 2008 crisis. Because of the severity of the crisis, however, these measures did not have their customary effect. Money was hoarded, as Keynes had predicted would happen in particularly grave crises. In order to make up for absent private investment and consumption Keynes called for debt-financed state investment. Numerous countries reacted in 2008 and 2009 with a classic Keynesian policy of demand stimulus by increasing public spending and boosting household purchasing power to an unprecedented extent. After sizable economic stimulus packages had been decided in the USA, China and Europe at the G20 summit in April 2009 the world's leading economies agreed to pump 1.1 trillion US dollars into the economy worldwide. The (social democratic) then British Finance Minister Alistair Darling referred expressly to Keynes in his announcement of his government's economic stimulus package.

Economic research institutes often represent a basic school of thought (supply side- or demand side-oriented) in economic theory and orient themselves in accordance with it. The five major economic research institutes in Germany can also be classified primarily as either supply-side or demand-side oriented. Their

research has a not inconsiderable influence on the economic policy debate. It is therefore important to recognise their basic economic convictions and to bear them in mind when evaluating their analyses and recommendations. All five work together, however, in particular on economic prognoses, which form the basis of public budgets and influence the planning of many firms.

- The Deutsches Institut für Wirtschaftsforschung (DIW) (German Institute for Economic Research) in Berlin, headed by Professor Gert G. Wagner ([www.diw.de](http://www.diw.de)), is primarily demand side-oriented.
- The Institut für Wirtschaftsforschung Halle (IWH) (Halle Institute for Economic Research) in Halle/Saale, headed by Professor Ulrich Blum ([www.iwh-halle.de](http://www.iwh-halle.de)), is primarily supply side-oriented.
- The Institut für Weltwirtschaft (IfW) (Kiel Institute for the World Economy) in Kiel, headed by Professor Dennis J. Snower ([www.ifw.de](http://www.ifw.de)), is primarily supply side-oriented.
- The Rheinisch-Westfälisches Institut für Wirtschaftsforschung (RWI) (North Rhine-Westphalian Institute for Economic Research) in Essen, headed by Professor Christoph M. Schmidt ([www.rwi-essen.de](http://www.rwi-essen.de)), is supply side-oriented.
- The IFO Institut für Wirtschaftsforschung e. V. (IFO) (IFO Institute for Economic Research) in Munich, headed by Professor Hans-Werner Sinn ([www.ifo.de](http://www.ifo.de)), is supply side-oriented and easily the most market-liberal of the five institutes.

In addition, there are the supply side-oriented Institut der deutschen Wirtschaft Köln (IW) (Cologne Institute for Economic Research, headed by Professor Michael Hüther: [www.iwkoeln.de](http://www.iwkoeln.de)), which has close ties to employers; the demand side-oriented Wirtschafts- und Sozialwissenschaftliches Institut (WSI) (Institute of Economics and Social Science, headed by Professor Heide Pfarr: [www.wsi.de](http://www.wsi.de)) which is close to the trade unions; and the affiliated Institut für Makroökonomie und Konjunkturforschung (IMK) (Institute for Macroeconomics and Business Fluctuations Research, headed by Professor Gustav Horn ).

**Further reading:**

*Michael Dauderstädt (2009), Krisenzeiten: Was Schulden vermögen und was Vermögen schulden, Friedrich-Ebert-Stiftung (ed.), Bonn.*

	Supply side policy	Demand side policy
<b>Basic idea</b>	Create the most favourable conditions possible for enterprises, enabling them to make good profits	Ensure constant demand by state support of employment and management of the economy
<b>School of thought</b>	Adam Smith, David Ricardo, John Stuart Mill	John Maynard Keynes
<b>Conception of the state</b>	Passive state	Active state
<b>View of wages</b>	Wages are a key cost factor	Wages are a demand factor and must increase in line with productivity
<b>Role of the central bank</b>	It should ensure monetary stability	It should ensure monetary stability and help to maintain employment and constant growth
<b>Dominant influence</b>	From the 1980s	Between the 1930s and the 1970s, and increasingly since 2008
<b>Institute</b>	<p>Institut für Wirtschaftsforschung Halle (IWH)</p> <p>Institut für Weltwirtschaft (IfW)</p> <p>Rheinisch-Westfälisches Institut für Wirtschaftsforschung (RWI)</p> <p>IFO Institut für Wirtschaftsforschung e. V. (IFO)</p> <p>Institut der deutschen Wirtschaft Köln (IW)</p>	<p>Deutsches Institut für Wirtschaftsforschung (DIW)</p> <p>Wirtschafts- und Sozialwissenschaftliches Institut (WSI)</p> <p>Institut für Makroökonomie und Konjunkturforschung (IMK)</p>

## **Tensions between the market, codetermination, regulation and political governance**

*Balance between  
the market,  
democracy and  
social cohesion*

The question arises, after consideration of the basic economic theories, of how social democrats can build a modern value-based economic policy on their foundations. A compass is provided for this purpose by the orientations of social democracy, which are explained in the next two chapters. At this point, however, the tensions which have to be reconciled in accordance with social democratic doctrines should be presented (cf. Meyer 2005b: 67).

*Growth and fairness*

### 1. Productivity and growth versus social justice and social security

The pursuit of personal interest and property releases enormous forces, as both Smith and Marx described. The market and competition bring it about that scarce resources go where they can be used most productively. This has proved to be much more efficient than a planned economy could ever be.

On the other hand, the market leads to unequal distribution and, with its cyclical fluctuations and susceptibility to crisis, structurally unstable, as Keynes described. As a result, markets must be subject to a political framework in such a way that crises are contained. The welfare state must safeguard people against the risks of the market. Through progressive – that is, increasing with income – income taxes, as well as inheritance and property taxes, »fair« distribution must be achieved. Furthermore, the state must manage the economic cycle by means of spending, tax and interest rate policy. That means that in economic crises public spending should be increased in order to keep consumption stable and people's willingness to invest should be stimulated by cheap loans.

*Flexibility and  
security*

### 2. Flexibility and innovation versus the protection of dependent employment and comprehensive social security

Competition leads to innovation, certainly. However, the ruptures and crises which also accompany it must be alleviated by safeguarding workers with employment protection and social benefits. Far-reaching structural transformation – for example, the decline of the coal and steel industry in the

Ruhr – can be directed towards the creation of new jobs only by means of specific structural policy.

### 3. Property and competition versus social integration and regulation

Economic systems which have attempted largely to dispense with ownership rights to the means of production and competition have always failed. Every successful economic system is based on property and competition. However, that does not exempt ownership from social responsibility. For example, Article 14 of Germany's Constitution (*Grundgesetz*) states that »Property and the right of inheritance shall be guaranteed. ... [but] [p]roperty entails obligations. Its use shall also serve the public good.« In order to try to ensure fairness in the market and to prevent the market dominance of individual actors competition must be regulated.

### 4. Enterprise autonomy versus codetermination and imposition of a political framework

From the right to property follows the right to engage in commercial activity. However, corporate decision-making should not be confined to capital owners, but also include those who, by their labour power, contribute to the creation of value. Corporate decision-making should therefore be constrained by codetermination.

Four dimensions arise from this:

- the imposition of a political framework
- the unfolding of the logic of the market
- rights of employee involvement and codetermination
- macroeconomic regulation

Taken together this means that in an economic system based on the values of social democracy the logic of the market can unfold within a political framework. Property »entails obligations« and is also subordinate to »the public good«. This is ensured, among other things, by the participation of workers in enterprise decision-making, besides the capital owners. Overall economic stability is ensured by macroeconomic regulation: in other words, the state, by means of budgetary and interest rate policy, attempts to bring about stable growth and high employment.

*Property and social embeddedness*

*Enterprise decision-making and codetermination*

*Four dimensions of economic policy*

### **What does that mean for social democracy?**

- Anyone interested in economic issues should become acquainted with the various theoretical foundations and be able to identify different ideologies.
- Social democracy makes use not only of one, but of various theoretical approaches.
- At the centre, however, lies managed capitalism, of the kind which Keynes called for.
- However, social democrats also draw on Marx's critique of capitalism, besides the efficiency and productivity of the market described by Smith.
- An economic system should also be based on competition and private property. However, markets must be regulated, economic crises must be actively combated by the state and codetermination and participation must be ensured.

# 3. ECONOMIC SYSTEMS AND ECONOMIC ORDERS

## In this chapter

- the relations between capitalism and democracy are discussed, which are both tense and mutually supportive;
- different varieties of capitalism are described which are distinguished from one another in terms of their level of coordination;
- the concept of »social market economy« is explained; and
- both the positive influences and the drawbacks of globalisation are presented from a social democratic standpoint.

## 3.1. Capitalism and Democracy



»Does super-capitalism destroy democracy?«, asked the economic publication *Manager Magazin* on its cover page in March 2008. This provocative headline was accompanied by a picture of a locust. The leading article asserts that the globalised market economy<sup>7</sup> could call into question the credibility of democracy. It goes on to declare that many people no longer believe that they can benefit from the globalised economy. As a result, trust in economics and politics is diminishing.

*Does »super-capitalism« destroy democracy?*

The article in *Manager Magazin* concerns a fundamental tension between democracy and capitalism.

<sup>7</sup> Market economy or capitalism – is there a difference in the meaning of these terms? Substantively, both concepts refer to an economic system based on private property and competition. In terms of everyday usage, it is often found that »market economy« tends to be used by advocates of a liberal economic system, while »capitalism« tends to be used by those critical of the market. The use of the two terms in this book, however, should not be taken to imply adherence to any particular ideology.

*Historically intertwined: democracy and capitalism*

Historically, the emergence of democracy and that of capitalism were closely intertwined. Democracies were frequently established in connection with the development of free markets. It was in Europe in the eighteenth and nineteenth centuries that the call for individual freedom with an economy based on free competition and private property first arose (see the remarks on Adam Smith in Chapter 2). This demand was accompanied by a desire for legal certainty and binding basic rights, as well as a demand for political participation and representation of citizens in the state. The first democracy of the new era was ushered in by the independence of the United States of America, with the cry »no taxation without representation«: in other words, the demand that economic and political participation belong together. After 1989, economic liberalisation and democratisation also went hand in hand in Europe's post-communist states.

*Are democratic states really more successful economically?*

For a long time it seemed obvious that democratic states are fundamentally more successful economically than non-democratic ones. The prosperity of the West and the economic collapse of the Eastern Bloc seemed to confirm this. In the meantime, however, it can be seen that there are also states which are not democratic but have nevertheless experienced high economic growth within the framework of a capitalist economic system. China is the most urgent example of this, which has been developing economically since its transformation into a capitalist country at the end of the 1970s but without democratising in the process. In a number of other countries, too, synchronous economic and political liberalisation has not (yet?) taken place. This is confirmed by the »Economic Freedom of the World« Index, published annually, which rates economic and political freedom. In the top two places with regard to economic freedom stand Hong Kong and Singapore.

It is important to emphasise that there are (still?) authoritarian states with planned economies and others with capitalist systems. All existing democratic states, however, are based on a market economy.

*Tensions between capitalism and democracy*

However, relations between democracy and capitalism are far from tension-free. Democracy is based on equality: »one person, one vote«. Every vote has the same weight. The market economy, however, is based on inequality. In a capitalist economic system the »cake« is divided up into various large pieces. There can be redistribution, but if it is taken so far that everyone's piece of the cake is the same size there is no incentive, for example, to work harder.

Inequality can lead, among other things, to a state in which economically strong actors develop such a powerful veto position that a »defective democracy« emerges. The political scientist Wolfgang Merkel defines such a democracy as follows: »Defective democracies are systems of government characterised by the presence of broadly functional democratic election regimes for regulating access to power, but which come to be deprived, as a result of the disruption of the functioning of one or more sub-regimes, of the complementary pillars which in a well-functioning democracy are indispensable to ensure freedom, equality and control« (Merkel et al. 2003: 66).

This means that, although elections take place and other elements of democracy are present, they are undermined by various factors of disruption. This is the case, for example, when an actor in a society is economically so powerful that he is able to exercise a veto in relation to collective decisions. To take an example: it is conceivable that an investor who is in a position to blackmail a state by raising doubts about whether in the end he will locate production there will be granted political concessions, such as reductions in environmental or labour standards. This represents an infringement of democratic principles.

In the first volume of the series of readers of which the present volume is a part the tensions between democracy and market capitalism are presented (pp. 58-62 and 84ff), based on Thomas Meyer's book *Theory of Social Democracy*.

The figure on p. 46 depicts the paradox of democracy. According to this, capitalism is, on the one hand, a precondition of democracy. On the other hand, an insufficiently regulated market can create conditions which are inconsistent with the participation of all and thereby lead to a defective democracy.

It is this, together with the awareness of the risks of capitalism with regard to democracy, that distinguishes social democracy from libertarian democracy. Libertarian economists, such as Milton Friedman, assert that the market economy also leads to political freedom and democracy.

*Inequality can lead to »defective democracies«*

*Sources of disruption for democracy*

*Relationship between democracy and market capitalism according to Thomas Meyer*

*Paradox of democracy*

*Milton Friedman: The market economy leads to democracy*

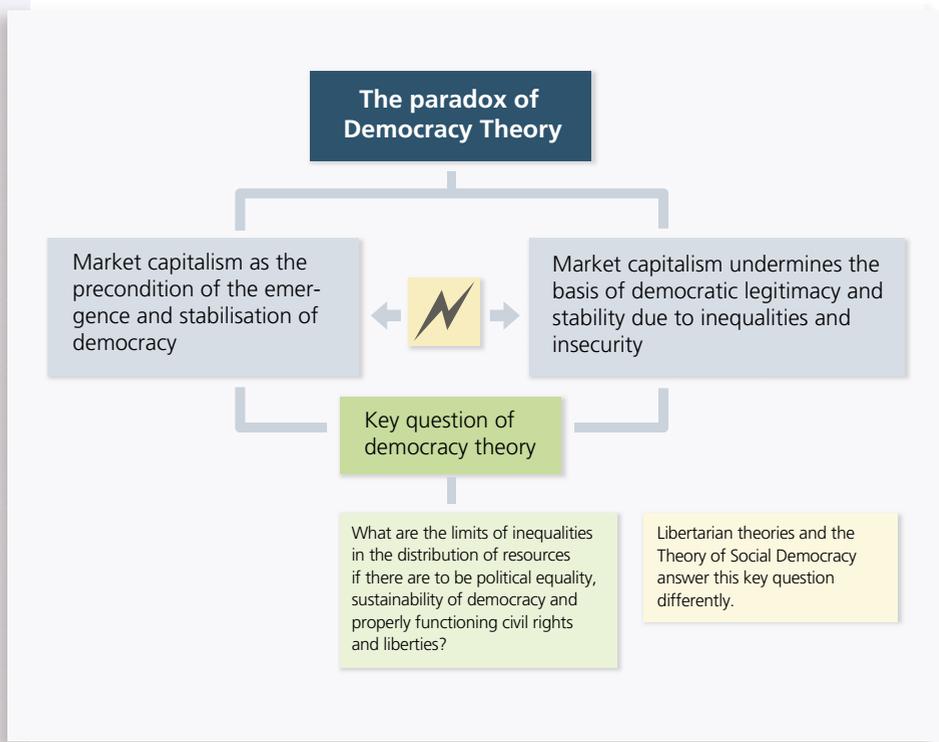


Figure 4: The paradox of democratic theory

Counterexample:  
Chile

Friedman provided his own counterexample. He scandalised many of his colleagues by advising the brutal military junta in Chile in the 1970s. The dictator Augusto Pinochet followed Friedman's prescription of extreme liberalisation of the economy. Instead of what the libertarian economist had expected, this did not lead to more political freedom, never mind democracy. On the contrary, the economic upturn stabilised the dictatorship. Chile eventually became democratic again, but later than other Latin American countries.

Topicality of the  
issue of »democracy  
and capitalism«

Why is it that the tensions between capitalism and democracy are increasingly receiving attention, even in economics magazines. The American economist and former Secretary of State for Labor under Bill Clinton Robert Reich offers one answer to this in his 2008 book *Supercapitalism: The Battle for Democracy in an Age of Big Business* (the subtitle of the German edition is: »How the economy is undermining our democracy«). He describes the period from the post-war years to the 1980s as almost the golden age of moderate capitalism (almost, because

this period should not be viewed uncritically either: Reich mentions, for example, the lack of economic opportunities for women and minorities). In Western societies in the post-War era rising living standards and minimum social standards could be achieved as the result of a consensus between the trade unions, employers and governments. Compared to the *laisser-faire* economics which

**Supercapitalism** is a term coined by Robert Reich to describe the development of capitalism under the conditions of globalisation.

had gone before this represented enormous progress. In the »supercapitalism« of the globalised economy, however, income inequalities have been increasing again. Workers'

rights and social standards are in jeopardy and corporate social responsibility is diminishing. Robert Reich's conclusions are similar to those of *Manager Magazin*, mentioned above, and Thomas Meyer: the market's centrifugal forces can undermine democracy. Reich therefore calls for the stronger embedding of the market by means of regulation and a reinforcement of workers' rights.

## 3.2. Coordinated and Uncoordinated Capitalism

In Chapter 2 of this volume a number of ideal-types of economic systems were presented with reference to the economists Smith, Marx and Keynes. In the real world, there are many mixed models. Peter A. Hall and David Soskice (2001) have identified two models in Western industrialised nations, labelled »uncoordinated« and »coordinated« capitalism in their book *Varieties of Capitalism*. This approach has considerable explanatory power for the analysis and evaluation of economic systems.

Within this framework economic systems are distinguished in terms of the following dimensions:

- Financial system
- Labour relations
- Education and training system
- Relations between enterprises

## Uncoordinated capitalism

Liberal, uncoordinated capitalism is characterised as follows in terms of these dimensions:

### *Financial system*

- Financial system: enterprise financing takes place largely through the capital market (shares). This means that enterprises operate in accordance with the so-called »shareholder value principle«. Under this system capital owners are also willing to invest in risky companies, speculating on the possibility of obtaining high profits very quickly.

### *Labour relations*

- Employment relations are primarily short term (»hire and fire«) and employment protection is weak. Wages are negotiated on an individual basis or at enterprise level. Employers' associations and trade unions are relatively weak.

### *Education and training system*

- Education and training system: The emphasis is on training generalists. This means that education is largely general and tends not to lead to occupational qualifications. This facilitates labour market mobility between different occupations, but it also results in a lack of occupation-specific specialist knowledge.

### *Relations between enterprises*

- Relations between enterprises: There are few interlinkages between companies (such as when enterprises have seats on one another's supervisory boards) and little industry-wide cooperation (for example, in research). Branch associations are rather lobbyists for their member companies and not actors with responsibility with regard to society as a whole.

This system can adapt itself flexibly and quickly to changes in the market. This means that this production model favours innovation-oriented industries, but is also more unstable and more uncertain for the workers.

## Coordinated Capitalism

Coordinated capitalism has the following characteristics:

### *Financial system*

- Financial system: Financing usually takes the form of bank loans. This is more »patient« capital than is the case in the shareholder value model and favours longer-term investment. Certainly, this form of enterprise financing does not prevent established market actors such as entrepreneurs from

obtaining access to capital. Management is controlled and judged not only by the market but also by other actors, such as banks, employees and state actors (stakeholder model).

- Labour relations: Wages are negotiated in a coordinated fashion across individual firms at the sectoral level (collective agreements). Long-term employment relations predominate. Stability and social justice are linked to one another. There are well-organised employers' associations and trade unions, as well as worker participation.
- Education and training system: The training model combines company-specific with branch-wide qualifications and is run by the peak organisations of employees and employers (dual training system). In this way, company- and branch-specific know-how is imparted.
- Relations between enterprises: Interconnections between companies are common by way of cross-holdings. Branch associations play an important role in the political system.

Coordinated capitalism is characterised by a high level of stability and less dynamism and flexibility than uncoordinated capitalism. In this system existing product lines and processes are modified constantly and in detail. Innovation tends to take place in small steps. The system is able to adapt to new problem situations only slowly.

The two systems have specific advantages and disadvantages. In terms of performance and competitiveness neither model is fundamentally superior to the other. Drawing distinctions between the two is enlightening for two reasons:

1. Analytically: The model makes it possible to explain why different production models develop. The »Anglo-Saxon« (in economic terms) countries, with their flexible labour markets and easy access to risk capital, favour innovation-oriented industries, for example, in information technology. It is therefore not by chance that IT firms, such as Google, Microsoft and a plethora of start-ups are native to the USA. Countries with coordinated capitalism, such as Sweden and Germany, have highly competitive industries, for example, in the automobile sector or machine building. Goods are produced

*Labour relations*

*Education and training system*

*Relations between enterprises*

*Usefulness of drawing distinctions*

*Analytical level*

there which have very long planning periods due to the high capital investment involved. In these industries there are no fundamental innovations but rather constant improvements. These factors favour locations in which well-educated and well-trained workers are available who tend to remain with their firms over the long term and where »patient« capital is available.

2. The two models can be distinguished from a normative standpoint. Social democratic values are realised rather in countries with coordinated capitalism. Long-term employment relations offer employees more security than a »hire and fire« labour market. Similarly, enterprises which invest for the long term and are not driven primarily by considerations of short-term profits encourage a more stable labour market.

**Social Market Economy:** For the German variant of coordinated capitalism, since the post-War period the term »social market economy« or, alluding to the former seat of government of the Federal Republic of Germany (Bonn), »Rhine capitalism« has become established. The social market economy was a reaction to the social upheavals of industrialisation, on the one hand, and the horrors of the Nazi dictatorship, on the other. It constitutes an attempt at a third way between unfettered capitalism and a social economic order. The attraction of the latter in the post-War period should not be underestimated. The German Constitution (*Grundgesetz*) which had just been adopted was not committed to a particular economic order. Article 15 makes possible the nationalisation of the means of production. The political parties were also to some extent critical of capitalism: the North Rhine-Westphalian branch of the CDU, in its Ahlen Programme of 1947, declared itself in favour of a »Christian socialism« and the SPD demanded the nationalisation of primary industries. The social market economy was also an attempt to win over the German population for the market economy and democracy.

The economist Alfred Müller-Armack had a decisive influence on the concept, explaining in his 1947 book *Wirtschaftslenkung und Marktwirtschaft* (Economic management and market economy):

»We talk of a social market economy in order to characterise this third form of economic policy. This means ... that the market economy appears to us necessary as the supporting framework of the future economic order, although this should not be a liberal market economy, left to its own devices, but a purposefully managed – and indeed socially managed – market economy« (Müller-Armack 1947: 88).

That meant real competition, free pricing and private ownership of the means of production, on the one hand, and social justice by means of social insurance and progressive taxation, on the other hand. The role of the state was not precisely determined. In the early years of the

Federal Republic market intervention was limited, for example, in order to prevent monopolies. From the 1970s influence over the economy was extended, among other things through economic management.

Rhine capitalism was respected throughout the world because it managed to reconcile economic and employment growth with an expanding welfare state. Other European countries also sought to emulate this model. The Lisbon Treaty also defines the social market economy as a goal of the European Union.

Ludwig Erhard's promise of »prosperity for all« was certainly not kept for everyone since, among other things, with the oil crises of the 1970s and reunification new social problems emerged, in particular on the labour market. However, it was possible to create a broad middle class which decisively stabilised the young democracy.

The popularity of the idea has in the meantime led to a certain arbitrariness. Like in a Rorschach test virtually any ideas can be projected onto it.

The basic programme of the DGB characterises the social market economy as a »major historical advance«. And one organisation founded by the employers' association Gesamtmetall is called the »New Social Market Economy Initiative«. Nearly every political tendency, therefore, has appealed to the social market economy, admittedly in terms of considerable variation with regard to the balance between social policy, regulation and market economy.

## 3.3. New Framework as a Result of Globalisation

*Globalisation –  
»The world is flat«*

*Drivers of  
globalisation*

*1. Dismantling of  
trade barriers*

»The world is flat« is the title of a book which appeared in 2006. But what does this metaphor mean? Author Thomas Friedmann postulates that, due to globalisation, the world economy has entered a new era in which global competition has increased enormously. National economies can isolate themselves only to a minor extent. The playing field of global competition has been levelled – it is flat. Friedmann identifies a number of drivers of globalisation:

- Since the 1950s, trade barriers have been gradually dismantled by international agreement. By means of the agreements of the World Trade Organisation (WTO) – or of its predecessor GATT – customs duties have been lowered and import restrictions lifted. Since the 1970s, exchange rates between national currencies have been largely free. Within the regional free trade zones of the European Union and NAFTA (USA, Canada and Mexico) practically all trade restrictions have been removed. Mercosur in Latin America and ASEAN in South-east Asia aspire to the same thing.
- Hitherto, Europe, the USA and Japan have been the dominant forces on world markets. But now more and more countries are competing with them. Since the 1970s, China has been gradually opening up its previously isolated planned economy to the world market and the market economy, recording high growth as a result. Now it is the biggest exporter in the world, having overtaken Germany. After the turning point of 1989 the former Soviet republics and Eastern Europe have made the transition to market economies and are competing in world trade. India, too, started to liberalise its previously protectionist and strongly regulated economy at around that time and is now on course to emulate China with regard to economic growth. In this way, more than two billion people have newly entered into global competition.
- Technical innovations have accelerated these two politically driven processes. The cost of international telephone calls has been reduced to a fraction of its former levels by fibre-optic technology so that call centres in India can receive calls from the USA. Over the Internet, orders can be transmitted from Hamburg to Shanghai in a matter of seconds. Software for a firm in Paris can be developed in Bangalore, India. Accounting can be shifted to

*2. Rise of emerging  
economies*

*3. Technical  
innovation*

Prague from London. Modern logistics make possible complex production chains so that individual parts can be produced and assembled in different locations and, finally, sold all over the world. Transport costs for shipping have fallen and air travel is no longer a luxury.

Who are the winners of this globalisation? Knowledge economies are profiting the most. In other words, countries with research-intensive industries for which the global market offers enormous sales opportunities. The reason for this is that once, say, an iPod has been developed – at great cost – it can be manufactured at relatively low unit costs and sold by the million on the world market. In a locally bounded market the development costs might outweigh the potential profits. The profitability of a software program, a song or a movie, once they have been produced, increases the bigger the sales market.

The same applies with regard to highly developed industrial goods. A new model of automobile, for example, can be developed only over a long period – from five to ten years – and at high cost. New technologies, such as hybrid propulsion, pay only if there is a large market for the cars produced. The automobile industries in Japan and Germany, which invest large sums in development, have therefore profited enormously from globalisation. Generally speaking, countries with a high level of education and training, which are attractive to researchers and creative knowledge workers, have been globalisation winners.

With regard to bulk goods the situation is different. Suppose a factory makes, for example, t-shirts: the costs increase at virtually the same rate as the number produced. Competitive advantages due to better education/training levels and infrastructure are of much less consequence with regard to goods that are simple to produce, in which research and development play little role. As a result, the production of bulk goods is virtually disappearing in high wage countries. Their production is migrating to countries in which manufacturing costs are lowest. The textile industry used to be one of the biggest branches of industry in Europe; now it has shrunk to a number of niches, for example, designer clothing. Mass production has moved to India, Bangladesh and China.

That means that both knowledge economies, which offer products with high development costs or creative input, and countries which manufacture bulk products at a good price can profit from globalisation. And indeed this is what

*Winners from  
globalisation:  
knowledge  
economies*

*Effects of high value  
industrial goods*

*Effects with regard  
to bulk goods*

*Benefits of  
globalisation*

has happened: Germany, long »world export champion«, exports high quality cars and capital goods all over the world. Italian and French designers design luxury clothing for the whole world. The American IT companies Google and Microsoft are as well known in China and Russia as in their home country. On the other hand, knowledge economies benefit from the import of cheaper bulk products: toasters, stockings, IKEA furniture – in other words, anything that can be produced in China, Eastern Europe and other low wage economies has become cheaper in relation to purchasing power over the past two decades.

*The shadow of  
globalisation*

But these developments also have their dark side.

*Widening of the  
income gap*

1. Not everyone has profited to the same extent from globalisation: many do not benefit at all and some have simply been cut adrift from it. It is small comfort to workers in a textile factory in Europe that the IT firm next door has a full order book, if their company closes down in order to shift production to a low wage country. Overall, prosperity has risen in both affluent and developing countries. Economic growth worldwide in the two decades since 1990 has been greater than ever before. In China alone since the 1970s 400 million people have risen above the UN-defined absolute poverty line – although a not insubstantial proportion of them are in precarious employment. At the same time, however, the distribution of prosperity is more unequal than ever before. In particular in the developing countries – but also in the affluent countries – the income gap continues to grow.

*Lack of international  
social standards*

2. The liberalisation of world trade was a difficult process, taking several decades. However, this so-called »negative« globalisation, within the framework of which regulations were abolished, took place much more quickly than the process of »positive« globalisation, namely the establishment of new standards which have become necessary, which is making little progress. For example, the Kyoto Protocol on climate protection has still not been ratified by all states after 15 years and is not being complied with by all the states that have committed themselves to it. Global social standards, such as ILO norms on the protection of workers, are not binding. The UN covenants on basic social and economic rights are binding under international law, but have no real bite. There is still a long way to go before these rights are implemented.

The worry is frequently expressed that globalisation is a »race to the bottom« concerning the lowest social and environmental standards. But this thesis is contradicted by the fact that the countries with the highest social and environmental standards are also the most competitive. This includes especially the Scandinavian countries, with their exemplary environmental regulations and the most extensive welfare systems in the world, financed by high taxes. High costs, then, are not necessarily a competitive disadvantage when, as in Finland, Sweden, Norway and Denmark, they lead to excellent education and training systems and research, excellent infrastructure, efficient, corruption-free administration and social peace. A highly developed welfare state, in other words, can boost competitiveness and prosperity even in the context of open markets. Needless to say, this is strongly conditional on a number of factors: if countries do not offer more in terms of quality than they incur in costs they will lose out in globalisation. Finally, it does not follow from the fact that the countries with the highest standards benefit most from globalisation that these standards will spread automatically.

*Does the pressure of competition require the lowering of social and environmental standards?*

*Counter-example: Scandinavia*

### **What does this mean for social democracy?**

- Capitalism and democracy are closely interwoven in their origins.
- Capitalism can lead to inequalities which undermine democracy. Social democracy must find an answer to this.
- From the social democratic standpoint coordinated capitalism is the best model. It ensures a more stable economic order with more social justice and more long-term employment relations than uncoordinated capitalism.
- Globalisation has resulted in worldwide economic progress and a high level of economic dynamism. But it has also thrown up new social issues.

## 4. ECONOMIC POLICY ORIENTATIONS OF SOCIAL DEMOCRACY

*Christian Krell and Simon Vaut*

### **In this chapter**

- the economic policy orientations of social democracy are presented;
- the core values of social democracy are identified: freedom, justice and solidarity;
- the fundamental rights for whose full recognition and implementation social democracy strives are described;
- finally, the principles of sustainability, social equality and growth are presented, which must characterise a social democratic economic policy if it is oriented towards core values and fundamental rights.

For the purpose of clarifying social democracy's economic policy orientation we shall briefly step outside the narrow economic policy framework and examine in depth the values in terms of which social democracy approaches society as a whole. This is because policy development must always – even in relation to specific areas, such as economic or social policy – keep the whole of society in view.

### 4.1. Core Values

Freedom, justice and solidarity – these are the main core values of social democracy. Social democracy strives for a society in which these values are realised. The core values of social democracy are of equal importance and mutually dependent, supporting but also constraining one another.

The core values of social democracy and their origins are described and explained in detail in the reader »Foundations of Social Democracy«. In this volume, therefore, we shall give only a brief definition.

*Freedom, justice  
and solidarity*

- Freedom means living a self-determined life. This means, in the first instance, freedom from the arbitrary interference of the state or society. Real freedom is achieved, however, only when the economic and social conditions are in place which enable freedom to be exercised.
- Justice is based on the equal dignity of all people and requires not only equality before the law, but also equal opportunities with regard to participation and social security, regardless of family background, social origin, property or gender.
- Solidarity is people's willingness to stand by and to help one another. Social Democrat Johannes Rau once described solidarity as the mortar which keeps society together.

The history of these three core values is remarkable. Their historical roots lie in the Enlightenment, originating as a revolutionary slogan. The demand for »freedom, equality and fraternity« characterised the French Revolution in 1789. Since the middle of the eighteenth century the workers' movement has invoked these demands. When the beginnings of the SPD were established by Ferdinand Lassalle in 1863 workers embroidered »freedom, equality and fraternity« on their banners.

The SPD, finally, was the first party to establish the core values of freedom, justice and solidarity in its basic programme, the Godesberg Programme, in 1959. Nearly two decades later (1978) the CDU also invoked these three core values in its first basic programme, albeit based on a different understanding.

Today, these core values are no longer the demands of a revolutionary movement, but are basically accepted by all important political tendencies. However, it would be wrong to assume an all-party consensus on the core values of »freedom, justice and solidarity«.

There are still important differences, at two levels, between political tendencies with regard to the core values.

*Freedom: a self-determined life*

*Justice: participation and security*

*Solidarity: standing by one another*

*Historical roots*

**Further reading:**  
*Tobias Gombert (2009), Foundations of Social Democracy, Social Democracy Readers, Volume 1, Berlin, pp. 11–37*

1. Understanding of individual core values

Needless to say, the individual core values can be interpreted in different ways. For example, not everyone means the same thing by freedom. Liberal tendencies, for example, emphasise the so-called negative civil rights and liberties, chiefly rights of protection against state arbitrariness and the protection of private property. Social democracy, however, goes beyond that, emphasising that real freedom also depends on positively enabling civil rights and liberties. Real freedom from a social democratic perspective means, for example with regard to freedom of speech, that it is not enough to establish the right to free expression of opinions; it is also necessary to put people in a position – by means of education and so on – to make effective use of their freedom of speech.

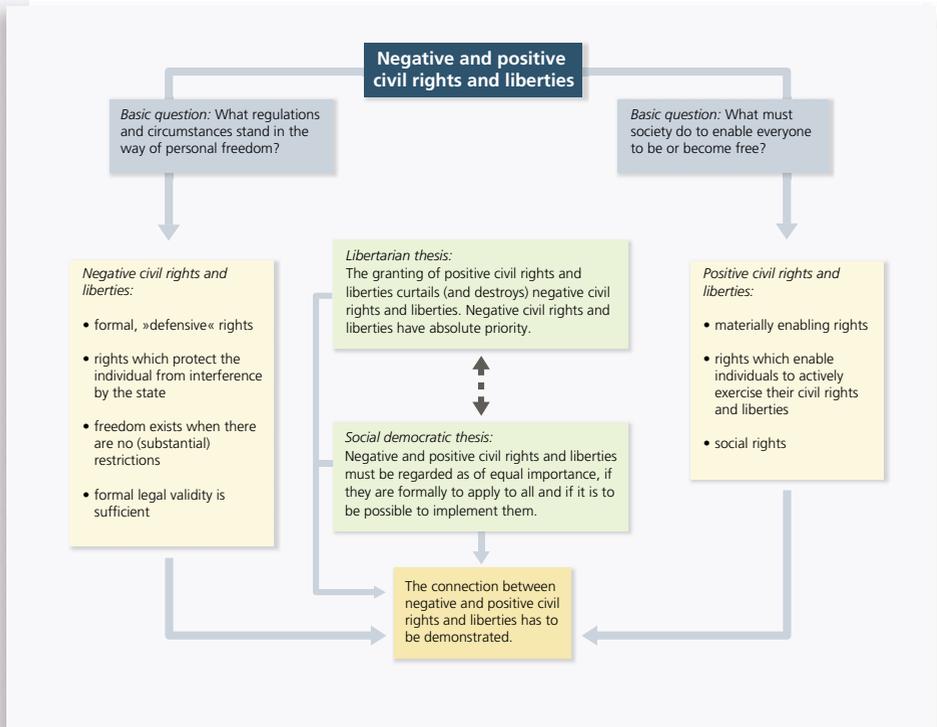


Figure 5: Negative and positive civil rights and liberties

## 2. Mutual Relations of the Core Values

But in addition to the interpretation of individual core values it is also important to consider their mutual relations. It makes a great difference whether the core values are ranked equally or one particular core value is regarded as more significant than another. This can be illustrated in terms of political liberalism (in the traditional, not the contemporary US sense): in the liberal understanding of the core values freedom has pride of place. Freedom – for example, competitive freedom or the freedom of ownership – tend to be ascribed more importance than the value of justice (or »fairness«), which can restrict the freedom of ownership. Social democracy, however, does not rank the core values differently: it emphasises that they are all of equal rank.

It is clear that even though all important political tendencies in Germany invoke the core values of freedom, justice and solidarity they often interpret them in very different ways.

## 4.2. Basic Rights

Examination of what the outlined core values mean for the economic policy orientation of social democracy gives rise to a twofold problem:

First of all, the core values are not undisputed. Various political tendencies, but also different cultures associate them with different things. They therefore do not constitute a broad and generally accepted basis for an economic policy orientation.

Second, the core values function at a very high level of abstraction. Any description of economic policy orientations, however, must be concrete. The core values alone are not sufficient to serve as precise and concrete instructions for an economic policy orientation.

The core values of social democracy, therefore, represent an important framework when it comes to describing a social democratic economic policy. This framework, however, must be established on a broader and more reliable basis and filled out with precise and concrete requirements.

*Different emphases with regard to the core values*

*Core values as the basis of economic policy orientations: two problems*

*1. The core values are not undisputed*

*2. The core values are very abstract*

*Reference point:  
human rights cov-  
enants of the United  
Nations*

The »mentors« of social democracy have always been concerned with this challenge. The political scientist Thomas Meyer has proposed, among other things, in answer to these challenges that social democracy refers not only to core or basic values but also to basic rights. As key reference points for any theory of social democracy Meyer nominates the basic rights laid down in the human rights covenants of the United Nations (UN). This is explained in detail in the reader *Foundations of Social Democracy*.

A number of arguments suggest that reference should be made to the UN covenants in determining the economic policy orientations of social democracy:

*Transcultural and  
transnational*

- The UN covenants are, globally, the most coherent, legally binding, transcultural and transnational source for basic rights and thereby for human co-existence.
- The UN covenants formulate very concrete and precise economic rights for every individual person.

The basic rights laid down in the UN covenants will therefore be described in detail here and consideration given to what they mean for a social democratic economic policy and how social democracy differs from other political tendencies in this respect.

*1966: two UN  
covenants*

In 1966, the UN drafted two international covenants on human rights.

*1. UN covenant  
on civil and  
political rights*

The covenant on civil and political rights (civil covenant) names primarily the so-called negative civil rights and liberties; in other words, protective rights against arbitrary interference by the state or society in personal freedoms. These include, for example, the right to personal freedom and security (Article 9), the right »to hold opinions without interference« and the right to free elections by secret ballot (Article 29).

*2. UN social  
covenant*

The covenant on economic, social and cultural rights (social covenant) names primarily positive civil rights and liberties; in other words, enabling rights which are intended to facilitate and promote the freedom of the individual through measures enacted by the state and society. These include, for example, the right to work (Article 6), the right to »just«, safe and healthy conditions of work (Article 7), the right to freely organise trade unions (Article 8), the right to social security (Article 9) and the right to free education and equally accessible higher education (Article 13).

The civil covenant has now been ratified by 151 states and the social covenant by 148 states. However, the fact that the covenants have also been signed by states which systematically infringe fundamental civil rights and liberties should give us pause. It is clear that the formal validity of the UN covenants alone is insufficient to achieve the »ideal of free human beings enjoying freedom from fear and want« described in the covenants. Rights and their implementation are often poles apart.

Furthermore, the rights of the social covenant do not oblige states to the immediate implementation of the basic rights, but only to strive for the gradual realisation of the basic rights. The covenant describes an obligation on states to act in such a way that the formal rights which have been granted will actually be achieved and promoted.

It is the aim of social democracy to implement the basic political, civil, social, economic and cultural rights enshrined in the UN covenants everywhere in such a way that they not only apply formally but have a practical effect. Social democracy is, in essence, a programme for the consistent implementation of the positive and negative civil rights and liberties throughout the world.

But can civil rights and liberties be weighed against one another? Are they really of equal weight? Or are some more important than others? Oskar Lafontaine, for example, ignited a debate on the issue when in an interview he raised the question of how important freedom of speech really was to AIDS victims in Africa (Der Tagesspiegel, 15 August 2008). Does that mean that civil rights and liberties only help the well-to-do who are able to express themselves through the media? Does someone benefit from freedom of the press if they are so poor that they cannot even afford to buy a newspaper? The Nobel Prize winning Indian economist Amartya Sen has asserted that »there has never been a famine in a democratic country with free media« (Sen 1999). In other words, famines are usually caused by distribution problems in the sense of inadequate access to the available foodstuffs. A government which has to answer to its citizens and wishes to be re-elected cannot afford to ignore social abuses over the long term, especially if they are made public by a free media. Freedom, according to Sen, therefore leads to social equality. He believes that state and society must create the basis for autonomous action and freedom. This means that freedom exists only when there is a minimum degree of social security and so-called services of general interest (for example, for health and education).

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*The rights contained in the UN social covenant and their implementation are often poles apart*

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*Social democracy: realisation of the UN covenants*

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*Can civil rights and liberties be weighed against one another?*

*Negative and positive basic rights are mutually dependent*

*Willy Brandt:  
»Freedom from need and fear, too«*

*Different models of democracy...*

*... with common roots*

Basic civil and social rights, positive and negative civil rights and liberties are therefore mutually dependent and cannot be played off against one another. Willy Brandt also emphasised this connection in his farewell speech as party leader: »If I have to say what, besides peace, is more important to me than anything else, there are no ifs or buts: freedom; freedom for the many, not for the few; freedom of conscience and opinion. Also freedom from need and fear« (Brandt 1987: 32). What mattered to Willy Brandt, therefore, was, on the one hand, freedom from arbitrariness and oppression – in other words, the negative civil rights and liberties – and on the other hand, the freedom granted by a materially secure life: in other words, the positive civil rights and liberties. Social democracy clearly differs from libertarian democracy in terms of its clear advocacy of the real global implementation of basic rights.

### **Social Democracy and Libertarian Democracy**

Social democracy and libertarian democracy are, first and foremost, theoretical ideal-types: they are hard to find in the real world. However, it is important to attempt to visualise these different models of democracy in order to establish one's own standpoint.

Both libertarian democracy and social democracy are based on the model of liberal democracy and so have common roots:

- pluralistic democracy with the rule of law;
- political power bound by a constitution;
- popular sovereignty organised on the basis of the principle of the democratic majority.

However, they are clearly distinguished with regard to the relations between positive and negative civil rights and liberties. Libertarian democracy takes the view that the granting of positive civil rights and liberties curtails and can even destroy negative civil rights and liberties. Social democracy, on the other hand, is based on the assumption that negative and positive civil rights and liberties must be regarded as equal if they are to apply to all formally and to really make a difference.

The merely formal validity of civil rights and liberties, as proposed by libertarian democracy, is not enough, from a social democratic standpoint, because economic inequalities can lead to (see Meyer 2005b: 15):

- relations of dependence and subordination;
- inhumane working conditions;
- unequal opportunities to exercise political citizenship rights.

Let us take the example of the expression of opinions. From a libertarian standpoint it suffices if the state does nothing to restrict freedom of speech: for example, if it refrains from press censorship. From the standpoint of social democracy, however, the state must take a decisive step further and actively promote real and equal opportunities for the expression of opinions. This includes equal access to information and receiving an education in order to be able to form opinions in the first place. Furthermore, the ownership rights of those who run the mass media have to be formed in such a way that they cannot use their media power to impose their views above all others. Such misuse infringes the social obligations pertaining to private ownership, which is an important characteristic of social democracy. From a libertarian standpoint such interference in freedom of ownership is inconceivable.

Despite their common roots social democracy and libertarian democracy are based on different assumptions which lead to very different objectives with regard to the economic order.

There are substantial differences, for example, in their understanding of the market. Libertarian democracy understands markets as an expression of freedom and therefore strives for a self-regulating market. Social democracy, by contrast, emphasises that entirely free markets can lead to outcomes which are undesirable for society as a whole. The financial market crisis of 2008 is one example of this. Social democracy therefore calls for the societal embedding of markets by means of politically imposed frameworks and state regulation.

Clearly, social democracy and libertarian democracy, although historically they have similar points of reference in liberal democracy, differ markedly from one another, especially in terms of economic policy.

*Mere formal validity of civil rights and liberties is not enough*

*Example: freedom of speech*

*Different objectives of social democracy and of libertarian democracy*

*Societal embedding of markets is necessary*

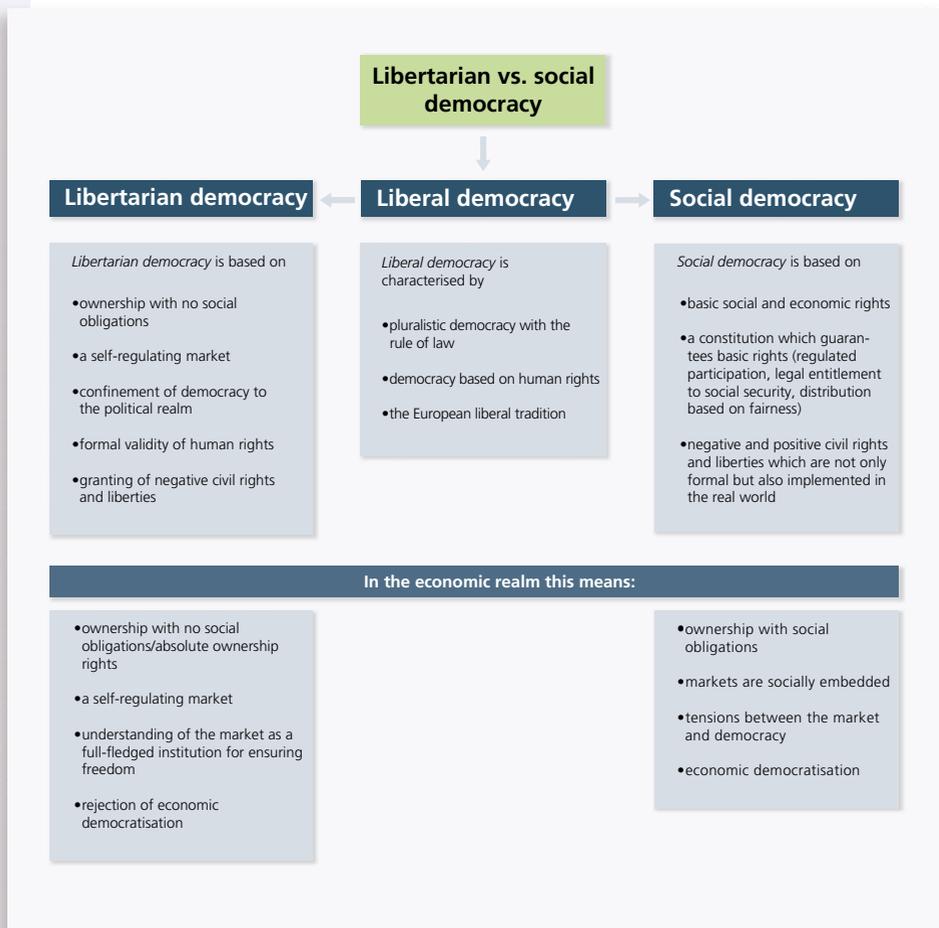


Figure 6: Comparison of liberal, libertarian and social democracy (including in economic terms)

The social democratic understanding of the market is also expressed in the SPD's Hamburg Programme:

»In our understanding, markets are a necessary form of economic coordination and superior to the alternatives. Markets left to their own devices, however, are both socially and environmentally blind. They are unable by themselves to provide public goods in sufficient quantities. If markets are to fulfil their potential, they need the regulation of a state which is able to apply sanctions, effective laws and fair prices.« (Hamburg Programme 2007: 17)

## 4.3. Principles of Economic Policy

What, in concrete terms, do the core values and basic rights of social democracy mean for social democratic economic policy?

The view represented here is that a social democratic policy that wishes to realise its core values and implement basic rights in the real world must take its bearings from three principles:

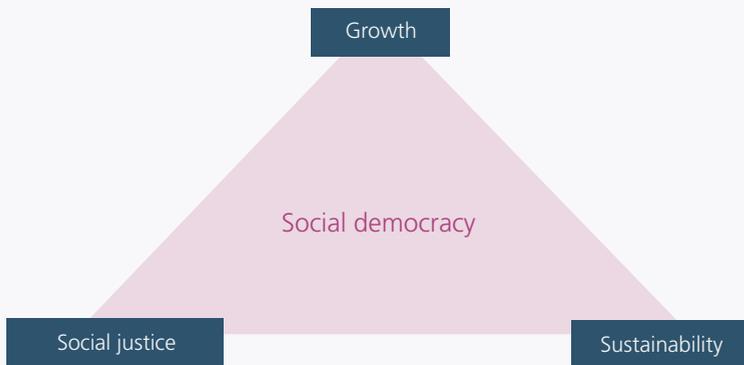
- growth
- social justice
- sustainability

From the standpoint of social democracy these three principles must have equal consideration in economic policy. This distinguishes social democracy from conservatives, libertarians and left-wing populists, who each concentrate on only one of these principles. Only when these principles are given equal rank will there be qualitative growth, and thus sustainable progress which is oriented to the common good.

All economic policy measures can be measured in terms of whether they do equal justice to these principles. These principles therefore represent criteria for a social democratic economic policy.

*Three principles*

*Growth, social  
justice and  
sustainability*



*Figure 7: Triangle of social democratic economic policy principles*

## Growth

*UN social covenant:  
»Freedom from fear  
and need«*

In the formulation of the UN covenants people should be able to live »free from fear and need«. In concrete terms this means »steady economic, social and cultural development and full and productive employment«. Freedom from need presupposes basic material support. For this purpose a country needs a GNP which can ensure a minimum level of prosperity, enabling every person to exercise their basic rights. This concerns, on the one hand, individual wealth, but also, on the other hand, the prosperity of society as a whole, because sufficient resources must be available for publicly defined tasks.

*A minimum amount  
of growth is a  
precondition of a  
free and just society,  
grounded on  
solidarity*

A free and just society grounded on solidarity therefore requires prosperity. This prosperity must be achieved and ensured first and foremost by economic growth. Only by means of high productivity and value creation can space be created for individual and societal prosperity. Historically, it is evident that when national economies are growing sustainably the distribution of the national product tends to be fairer than during periods of economic recession. Growth is therefore a condition of the realisation of the values and aims of social democracy, as presented in this volume.

**Economic growth:** An increase in gross domestic product (GDP); in other words, growth in the market value of all goods and services produced in a national economy. The general assumption is that there is always growth of one sort or another. For example, stagnation is termed »zero growth«, while if production falls, it is considered to be negative growth. If prices increase, however, at least in the case of nominal economic growth, this is regarded as positive. In the case of real growth, by contrast, price increases are excluded. (Wirtschaftslexikon 2009)

*What does  
»growth« mean?*

But what precisely does »growth« mean? Social Democrats' conception of the right kind of growth has changed in recent decades.

*1967, Law on Sta-  
bility and Growth:  
»constant and ade-  
quate growth«*

In 1967, under the aegis of the Social Democrat Minister for Economic Affairs and later Finance Minister Karl Schiller »constant and adequate economic growth« was laid down as a central political goal in the Law on Stability and Growth. Also postulated as economic policy goals were low unemployment, low inflation and foreign trade equilibrium, all four goals making up the so-called »magic square«. Accordingly, the task of the state is to balance out economic fluctuations and prevent recessions, in keeping with Keynesian theory.

## »Growth« in the Hamburg Programme

*»Wealth and high quality of life have always been priorities in Social Democratic economic policy. In the past, progress was understood mainly in terms of quantitative growth. Nowadays we are forced by rapid climate change, the overburdening of ecosystems and the growth of the world population to give development a new, future-oriented direction. Whether development also amounts to progress depends on this. We want sustainable progress, a dynamic economy, social justice and environmental responsibility in unison. This requires qualitative growth in combination with reduced consumption of resources. People should have the opportunity to earn their own living by means of decent work, free from exploitation. Each person should receive their fair share of the wealth created.«*

(Hamburg Programme 2007: 42)

Among other things, the influential study *The Limits of Growth*, which appeared in 1972, heightened awareness that growth also involves consumption of raw materials and damage to the environment. As a result, the question of whether growth is desirable or possible over the long term was discussed more intensively.

In the meantime, a more complex conception of growth has been adopted which seeks to combine technological innovation, environmental renewal and social cohesion. In this context, in 2000, under the

leadership of Social Democratic government heads, the so-called Lisbon Strategy was agreed, the goal of which was to make Europe the most competitive and dynamic economic area in the world within ten years.

The understanding of growth, therefore, has been subject to constant change. Growth euphoria in the 1960s was followed by a critical attitude in the 1970s. In the meantime, a more subtle view has emerged based on a qualitative conception of growth which is to promote social progress with, among other things, reduced resource consumption. This more complex view makes it possible to balance growth with sustainability and social equality.

## Social Equality

Social equality as a principle of economic policy is imperative from a social democratic standpoint. It also makes sense economically.

1972, »*The Limits of Growth*«: critique of the focus on growth

2000, Lisbon Strategy: complex conception of growth

Concept of qualitative growth taking into consideration resource consumption and social progress

*UN social covenant:  
»adequate standard  
of living«*

If the core values and basic rights of social democracy are to be taken seriously an economic policy must be pursued which is characterised by social equality. It is not only the core values of justice, freedom and solidarity which urge this, but also the basic rights formulated in the UN covenants. For example, an »adequate standard of living« is demanded, but also that women should be »guaranteed conditions of work not inferior to those enjoyed by men, with equal pay for equal work«; that »adequate food, clothing and housing« be ensured; that there is a »right to education«; and that therefore the »full development of the human personality« should be guaranteed.

Social democracy strives for a society based on social citizenship, in which each person is guaranteed a life which realises their human dignity safeguarded by the necessary material support in order to ensure that they can participate in both social and democratic life, regardless of their success in market terms. Economic growth, therefore, is a necessary condition from a social democratic standpoint, but not an end in itself, and it must take social equality and justice into consideration. The proceeds of a dynamic and productive economy have to be distributed fairly. This will ensure that people are able to earn their living by decent work free from concerns about their future and receive a fair share of growth of the national product.

*Social equality laid  
down in the German  
Constitution*

In Germany, social equality in the economic order is also laid down in Article 19 of the Constitution, which defines the Federal Republic of Germany as a »social federal state«. Furthermore, Article 14 establishes the social obligations of private property: »Property entails obligations. Its use shall also serve the public good.«

*Social obligations  
of private property:  
examples*

Owners of residential buildings, for example, may not abuse them as objects of speculation but must maintain them and rent them out. Managers have a responsibility not only with regard to shareholders' dividends but also to society as a whole, for example, by preserving jobs and protecting the environment. Anyone who receives a particularly large share of a society's wealth should in turn do a lot for society. The social obligations of property constitute an essential trait of social democracy.

*Is there a contradic-  
tion between social  
equality and the  
merit principle?*

But doesn't social equality contradict the merit principle of the market economy? Doesn't social equality hinder the performance incentives which are important

for a dynamic economy and growth? These questions point towards real tensions between a growth orientation and social equality.

However, the reverse is true: the development of productivity and growth always require a social basis. Value creation needs a minimum level of social equality. The US economist Rodrik, for example, has proved that states which ensure a high level of social security are also economically successful states. This is the result, among other things, of the fact that social security heightens personal motivation. People who benefit from social protection are more willing to deal with change, take risks and innovate (see Rodrik 1997: 178ff).

This connection is hardly controversial. Even Hans-Werner Sinn, today the president of the business friendly IFO Institute for Economic Research (IFO) in Munich emphasised in 1985, in his inaugural lecture at the Ludwig-Maximilian-Universität, that: »[solidarity] gives young people the security and self-confidence they need to take advantage of risky but promising opportunities. To that extent I am not convinced that the widespread view is correct that the welfare state is too costly for us. On the contrary, I consider it eminently possible that it was only the welfare state that made it possible to release the level of productive forces that was responsible for the economic upturn during the post-war period« (Sinn 1986: 566–77).

*Rodrik: Value creation requires social equality!*

*Even critics admit that a welfare state promotes productivity*

*Balance between growth orientation and social equality*

### **»Social equality« in the Hamburg Programme:**

*»Income and property are not fairly distributed in Germany. The aim of Social Democratic tax policy is to curb inequality and to foster equal opportunities. We support wage increases which are related to productivity growth and inflation. We want to see more property in the hands of the workers. Workers' participation in enterprise capital as an additional source of income ensures a fairer share for the employees in a firm's success. It also boosts innovation and productivity.« (Hamburg Programme 2007: 43f)*

Social democracy, therefore, strives to achieve a balance between an orientation towards growth and social equality. A specific example of this is the Swedish model. In the country study in Chapter 6 it is clear that one reason for Sweden's considerable economic success has been the high level of social equality there.

## Sustainability

Sustainability is the third key principle of a social democratic economic policy. Sustainability encompasses an environmental, an economic and a social dimension.

*The concept of  
»sustainability«  
originated in  
forestry*

Environmental issues are often linked to sustainability. In fact, the first reflections on sustainability arose from environmental considerations. The concept of »sustainability« originated in forestry: no more timber should be removed from a forest than can grow again, declared agriculturalist and writer on forestry Georg Ludwig Hartig in the eighteenth century. Today, environmental sustainability means that the environment must, as far as possible, be kept intact as an indispensable basis of life for succeeding generations. Resource conservation, climate protection, species protection and limits on environmental pollution are therefore key aspects. The basic rights laid down in the UN social covenant also emphasise, with reference to the »improvement of all aspects of environmental ... hygiene« (Article 12) that, first and foremost, the natural bases of life must be protected for everyone. Not only because otherwise future generations will be deprived of the basic conditions of existence, but also because in the here and now people need clean drinking water and healthy air.

At an early stage Social Democrats pointed out the importance of sustainability.

*1983, Brundtland  
Commission*

In 1983, the idea of sustainability was taken up by the Brundtland Commission (named after the former Norwegian Prime Minister) appointed by the United Nations. It declared that:

*»Durable development is development which satisfies the needs of the present without endangering the ability of future generations to satisfy their own needs«  
(cited in Hauff 1987: 46).*

*The economic  
dimension of  
sustainability*

But the concept of »sustainability« has an economic dimension, besides the environmental one. The Final Report presented by a committee of inquiry of the German Bundestag on »The concept of sustainability – from model to implementation« in 1998 stated that economic sustainability means that wealth creation must also be possible for future generations, too, in order to maintain the social

market economy. To that end, public spending – in particular, on the welfare state – must be robustly funded and there must be long-term investment in education, research and infrastructure.

The importance of economic sustainability is particularly evident in the face of the global financial crisis. The short-term pursuit of profit which takes no account of sustainability not only endangers individual companies but may also destabilise entire economies.

*Cautionary example*

### **»Sustainability« in the SPD's Hamburg Programme:**

*»The principle of sustainability means: thinking in terms of the future, resisting both the primacy of short-termism and the dominance of economic considerations and the logic of business management. It means conceiving of politics in terms of society and understanding democratic variety, environmental durability, social integration and cultural participation as guiding principles of social democratic policy«*

(Hamburg Programme 2007: 17f).

But sustainability also has a social dimension: social sustainability means the permanent participation of all members of society and the durable reconciliation of social tensions. In other words, the sustainable securing of basic needs and social participation.

*Hamburg Programme:  
»Sustainability means: thinking in terms of the future«*

## **Qualitative Growth – Implementation of the Three Principles on an Equal Footing**

Growth, social equality and sustainability: it is the aim of social democratic economic policy to implement these three principles on an equal basis. But is that even possible? Does not social equality restrict a society's growth opportunities? Doesn't growth ultimately need raw materials and therefore lead to a reduction of sustainability? There appear to be tensions between the three principles. How can they be implemented on an equal footing?

*Are there tensions between the three principles?*

Willy Brandt addressed this issue as early as 1973 with regard to the principles of growth and sustainability:

Willy Brandt on the relationship between growth and sustainability

*»Neither the individual nor society can live at the expense of nature. In that way the development of our environment will run counter to human well-being. ... Noise, air and water pollution in fact call into question the benefits of economic growth. Nevertheless, I would warn against taking the intellectual short-cut of seeking the way out in, for example, a general reduction of growth and productivity. It is much more a matter of the where, how and to what purpose of economic growth – and of understanding that growth and economic principles must be in the service of humanity. If »circumstances« are not to rule over us, but we want to rule over them we must give the matter more thought and, at least once in a while, work a bit harder« (Willy Brandt, inaugural speech, 18 January 1973).*

Key questions: growth where, how and for what purpose?

What Brandt was saying is that there can be no unconditional advocacy of the principle of growth. We must always carefully consider where, how and for what purpose growth is to be produced. Whose interests will it serve and who will profit from it? Social Democrats therefore must abjure any notion of blind growth in favour of qualitative growth which takes into consideration social equality and sustainability on equal terms.

Sustainability can promote growth. Example: environmental industrial policy (Chapter 7)

If, in the spirit of Willy Brandt, one considers the matter more closely it quickly emerges that, although there are some tensions between the three principles, they are also mutually dependent and support one another. It has already become clear that social equality is a condition of a dynamic economy. Also, environmental sustainability can promote growth. In Germany the branches of industry devoted to regenerative energies are among the more important economic growth engines and safeguard a large number of jobs. In the practical example of environmental industrial policy in Chapter 7 a similar connection is described.

### **»Qualitative Growth« in the SPD's Hamburg Programme:**

*»We are working for sustainable progress, combining economic dynamism, social justice and environmental common sense. By means of qualitative growth we wish to overcome poverty and exploitation, make possible prosperity and decent work for all and do something about looming climate change. It is important also to safeguard the natural bases of life for future generations and to improve the quality of life. To that end we wish to put the possibilities opened up by scientific and technological progress in the service of humanity« (Hamburg Programme 2007: 5).*

From the combination of growth, social equality and sustainability emerges qualitative growth

It seems, therefore, that although the demand to treat the three principles of growth, social equality and sustainability on equal terms

is a major challenge, it also represents a major opportunity. The consequences to which the three principles give rise must be constantly re-examined and renegotiated. There are no ultimate truths here. But if these principles are treated equally qualitative growth emerges from which society as a whole benefits.

## 4.4. Excursus: Measuring Qualitative Growth

How can economic progress be expressed numerically? The most common indicator used to depict economic development is Gross Domestic Product (GDP). GDP is the total value of all goods and services produced in a country in a given year. If GDP grows, people talk about an economic upturn; when it stagnates or even shrinks, the talk is of a recession. There is no denying the significance of GDP: public budgets, reducing unemployment and society's prosperity all depend on economic growth.

However, GDP also has a number of blind spots with regard to the measurement of economic progress. In particular, from a Social Democratic standpoint, the picture which arises from an exclusive focus on GDP is incomplete, because it merely describes how much has been produced overall. But that says nothing about the following issues:

- How is GDP distributed? Is the distribution fair? Does a minority receive the bulk of resources? What are the criteria of distribution? Need, performance or in accordance with social class?
- To what extent is production environmentally sustainable? Are resources invested in environmental protection? Or is growth obtained at the expense of the overexploitation of nature?
- How is growth generated and where do the proceeds flow? Is it brought by running up household and public debt? Or is there investment in infrastructure, education and research so that long-term growth is possible?
- How are non-monetary activities taken into consideration? Does GDP rise only because more work is done? If voluntary or family work is converted into gainful employment why does GDP rise although in fact the same is produced?

*Economic progress  
= GDP?*

*Blind spots of GDP*

*1. Distribution*

*2. Environment*

*3. Sustainability*

*4. Unpaid work*

In order to answer these questions a more complex concept of economic progress and a more differentiated concept of growth must be developed, which goes beyond the question of how much an economy produces in total.

Traditional growth concept	Expanded growth concept
<ul style="list-style-type: none"><li>Economic performance overall</li></ul>	<ul style="list-style-type: none"><li>Economic performance overall</li><li>Social equality</li><li>Sustainable development</li></ul>

There are a number of approaches which try to express growth more comprehensively. One is that of World Bank economist and winner of the alternative »Nobel Prize« Herman E. Daly (Daly/Cobb 1989; Daly 1996) who has played a part in the development of a method of calculation for real progress, the *Genuine Progress Indicator* (GPI). With this method GDP is supplemented by factors intended to depict the real costs and benefits of economic activity (Lawn 2003). The factors which make up this indicator besides GDP include, among others, social income distribution, unpaid and voluntary work, increases in education, crime, leisure time, resource consumption, environmental damage and investment in public infrastructure. The calculation of the GPI and of similar indicators is, to be sure, very complex and the precise details of composition and assessment are controversial. However, despite justified criticism, such calculations make an important contribution to uncovering the weaknesses of the usual calculation methods, including GDP.

The NGO »Redefining Progress« regularly publishes – at [www.progress.org](http://www.progress.org) – the GPI for the OECD countries. From this it is clear that progress measured by GPI can be much smaller than GDP growth might lead one to believe. Above all, the inclusion of environmental damage and social injustice shows that in some countries the GPI is even declining.

The efforts to find alternatives to GDP are continuing: French President Nicolas Sarkozy has launched a high-level expert commission to develop indicators which take into account quality of life, social progress and environmental considerations. The idea is that the government will take on board the results of this commission in its future actions.

**Further reading:**

Michael Dauderstädt (2007), *Soziale Produktivität oder Umverteilung? Herausforderungen für eine Politik der neuen Wertschöpfung*, Berliner Republik 3/2007. Hagen Krämer (2009), *Wen beglückt das BIP?, Wiso direkt*, Friedrich-Ebert-Stiftung (ed.), Bonn.

# 5. COMPARISON OF THE ECONOMIC PROGRAMMES OF POLITICAL PARTIES

*Tobias Gombert*

## **In this chapter**

- the programmes of the five political parties represented in the Bundestag are compared;
- their aims are analysed based on the model of coordinated and uncoordinated economies;
- the parties are categorised in terms of their positions on qualitative growth as envisaged by the Social Democrats.

Which party is generally considered most competent with regard to economic policy? Which party can best solve the problems of the labour market? Which party has the best ideas on social policy? These questions are posed in every media analysis conducted on (general) election night. Generally speaking, the centre-right parties are believed to possess competence for the economy, while the left are generally assumed to possess competence with regard to social policy. This basic identification of the parties remains relatively stable and documents a general orientation in the evaluation of political parties. But is it accurate? The answer is both »yes« and »no«.

This classification reflects to a limited extent the respective guiding principles or main focus of the parties. Certainly, the questions are also somewhat deceptive: they do not define economic and social policy competence, nor do they connect the two competences. An economic policy model, however, is not limited to economic policy conduct in the narrow sense but must also concern itself much more broadly with its integration with social policy and other policy areas. Economic policy is social policy – a functional economy is always embedded in a societal system and this must be taken into consideration. Any examination of a party's economic policy programme, therefore, must necessarily look closely at its overall programme and then explain the role that the economy is to play within the framework of the economic system aimed at.

The image of the compass is again useful in this respect: not only the economy which is aimed at but also the point of departure of a particular orientation must be described (as in the preceding chapters).

Indeed, the parties differ clearly in respect of their analyses of the current state of affairs and their ideas on how things ought to be – as can be inferred from their respective programmes. In what follows the economic policy portions of the party programmes will be presented, in terms of the categories used to describe coordinated and uncoordinated economies.<sup>8</sup>

## 5.1. Hamburg Programme – Basic Programme of the Social Democratic Party of Germany

In 2007, the Social Democratic Party of Germany (SPD) adopted the so-called Hamburg Programme. It is the latest of a long line of political programmes. The crux of its economic policy ideas have remained the same, with minor variations, since the Godesberg Programme of 1959: »Our slogan is: as much competition as possible and as much state regulation as necessary« (p. 43).

Accordingly, the underlying idea is first and foremost a coordinated market economy, although it does not consider state and market as merely juxtaposed: politics has primacy. However, this economic policy approach clearly assumes that there should be only so much »state regulation« as »necessary«: in other words, political intervention must be »essential«. But why is a »regulating state« necessary?

The need for and limits of a regulating state are based on two key considerations: first, the defects of an unregulated – or insufficiently regulated – state are examined; second, the aims of democratic socialism (p. 16f) are striven for, which can be guaranteed only by an active and democratic society with a regulating

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<sup>8</sup> The categories presented previously will be abridged in the current context: the category »relations between enterprises« is hardly to be found in party programmes and therefore will not be considered here.

state. Defects and objectives, taking an overall view, outline the gaps and the social policy task which the SPD has given itself with its programme.

The virtues, but also the defects of the market are summarised concisely in the Hamburg Programme: »For us, the market is a necessary instrument, which is superior to other forms of economic coordination. However, left to its own devices the market is socially and environmentally blind. It is incapable of spontaneously providing public goods to an adequate degree« (p. 17). Social, economic and environmental responsibility is therefore not achievable through the market but only by means of a societal and political orientation. In particular, the effects of a globalised market, the global chasm between poverty and wealth and the environmental crisis are not solved by the market but rather exacerbated. Regulation and social negotiation and control are urgently required if economic value creation is to benefit all.

»Democratic socialism remains for us a vision of a free and just society based on solidarity, whose realisation is our permanent task. The principle of our action is social democracy« (p. 16f). A goal is therefore juxtaposed to the current state of affairs, oriented towards the core values and their absolute validity and virtue for all persons, not only in Germany but throughout the world. This goal is therefore supported by ideas about development: the goal cannot be achieved by state decree but only if state and civil society actors work together: »Because of our adherence to this aim we insist on the primacy of democratic politics and reject

### **Goal: »Equality«**

*»We want equal and fair participation of men and women in gainful employment which is adequate to their needs. Work which is done predominantly by women is often worse paid. For work of equal value there must be an equal wage. ... This requires legal measures for the equal participation of women in leading positions in enterprises, administration, science and research, as well as on supervisory boards« (Hamburg Programme 2007: 41).*

the subordination of the political, which must not be reduced to the state, but also includes civil society alliances and networks, as well as people's free, self-determined action« (p. 17).

In particular, globalisation, gender equality and the increased significance of the EU are named as challenges for a modern economic pol-

icy. The coordinated form of the market should – in light of the abovementioned defects of the market and the goals of the party – be further developed.

**Financial system:** A separate chapter in the Hamburg Programme is devoted to the influence of the capital and financial markets. This reflects the increased importance for society of the financing and control

of enterprises (in Germany, too): »We want to harness the potential of capital markets for qualitative growth« (pp. 46–47). However, the disadvantages and the increased risk of crises are also taken on board: »Where financial markets seek to generate only short-term profits they jeopardise enterprises' long-term growth strategies and so destroy jobs. By means of company law we want to strengthen the position of investors who aim at a long-term commitment rather than quick profits. We need rules for investors and funds which prevent the pursuit of a one-sided profit orientation at the expense of the long-term maintenance of enterprises. With the increasing international integration of commodity and financial markets their international regulation becomes more and more important« (p. 47). Besides that, because of their long-term orientation towards sustainability, savings banks and cooperative banks must be preserved: they play an essential role for small and medium-sized companies and can also be a key factor in the local economy.

**Labour relations:** The SPD considers itself part of the tradition of the workers' movement. Consequently, it focuses on the implementation and improvement of workers' rights. To that end, current regulations within the framework of the basic economic order should be maintained: free collective bargaining and general collective agreements should remain. A general shift of decision-making from the bargaining partners to enterprises should not take place. Minimum wages should underpin free collective bargaining. In enterprises the principle

### **Goal: »Codetermination«**

*»Where the nation-state is no longer able to provide markets with social and environmental frameworks the European Union must do so, instead. ... Where economic activity crosses borders, workers' rights must not cease to apply at those borders. We therefore want to safeguard and enhance codetermination in European companies. In order to strengthen and enforce free collective bargaining we favour a European legal foundation for cross-border collective bargaining and collective agreements«*

(Hamburg Programme 2007: 26, 28 f.)

of »internal company democracy« should be implemented: codetermination by works councils and participation in supervisory boards should be strengthened. Two new aspects were included in the Hamburg Programme which are likely to influence labour relations both directly and indirectly in favour of the employees: workers' financial participation should be increased by means of industry-wide funds. Also, unemployment insurance should be converted into employment insurance, which would financially underpin training/education and periods devoted to family responsibilities and thus contribute to strengthening the position of the employees in relation to the employer in labour relations.

**Occupational training and further training system:** The dual training system with its school-based component for which the state is responsible, on the one hand, and its workplace component, on the other, should be retained. However, a solidarity-based financing system is needed for occupational training. This clearly goes beyond the existing alliance aimed at creating more training places. The first degree should remain – or once more become – free of charge. Further education and training as the third pillar of occupational training should be afforded high priority.

**Industrial policy:** The sectors which should be promoted by both state and society as a matter of priority are the new lead markets (for example, renewable energies, the service and health care sectors, but also local crafts). Investment in public infrastructure stands out as an essential task.

Overall, the Hamburg Programme calls for an economic policy oriented towards qualitative growth: social equality, environmental sustainability and growth should be fostered equally.

## 5.2. Principles for Germany – Programme of the CDU<sup>9</sup>

The CDU also presented a new party platform in 2007. In essence, it regards the social market economy as a successful model, also for the future: »The CDU is the party of the social market economy ... The CDU rejects socialist and other forms of collectivism. This also applies to unrestrained capitalism which relies solely on the market and which has no answer for the social problems of our time. The social market economy remains our model in the reunified Germany and in the age of globalisation« (p. 46f).

The rejection of »collectivism« also finds expression in the model of »entrepreneurship« which is both core and basis of the social market economy: »The CDU is committed to liberal and socially responsible entrepreneurship. It is entrepreneurs and company managers who are able to create future-proof jobs and whose reputation and cultural identity help shape Germany's standing in the world. To be successful, entrepreneurs need freedom and appropriate conditions and incentives« (p. 49).

It is already evident that the central idea is widely divergent from that of the SPD, with regard to both aims and methods: free and socially responsible entrepreneurship and an appeal to moral and social responsibility on the part of the CDU – regulation and democratic cooperation to realise basic rights for all people on the part of the SPD. The CDU tends to leave it to the individual entrepreneur's sense of responsibility to see that social responsibility towards society and workers prevails.

For the CDU, then, the role of politics is distinctly smaller: »The social market economy is a competitive order. Politics in the social market economy is ›*Ordnungspolitik*‹<sup>10</sup>« (p. 49). The tasks of the state are, therefore, to ensure freedom of trade and contract, protection against market barriers and protection against abuses of power by dominant companies, as well as market transparency and the international opening up of markets under fair terms of competition« (see pp. 49 and 52).

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9 Christlich Demokratische Union Deutschlands – Christian Democratic Union

10 The basic principle of »*Ordnungspolitik*« is that »the state is supposed to create a framework within which market forces are to interact and unfold their dynamism under competitive conditions« (Hans Tietmeyer, speech on the occasion of the awarding of the Special Prize 1997 of the German-British Forum in London on 15/12/97).

The role of the state in relation to the market economy, therefore, is oriented towards the basic features of a liberal understanding, although it also contains some regulatory components.

**Financial system:** The increasing significance of the international capital and financial markets is evaluated positively and the opportunities for investment in Germany are emphasised: »Funds in search of investment opportunities, such as private equity funds, can also help companies in Germany to become more competitive and more innovative« (p. 52). The risk lies primarily in the market power of private investment groups – according to the CDU, resort to the existing international organisations is sufficient to provide for a »reliable framework« and transparency (cf. p. 52).

**Labour relations:** The CDU's approach to labour relations derives from the social ethics of Christianity (p. 50). This refers to individual potential for development: »Enterprises needs well educated, creative and motivated employees in order to be successful. Employees need opportunities for participation, responsibility and freedom in which to be able to develop their capabilities thoroughly and successfully. Education and training ensure their employability and productivity. Employees also need, so that they can plan their lives, basic employment and social security safeguards. They are entitled to an appropriate share in social prosperity« (p. 50). Collective protection and collective organisation of labour relations are viewed critically. For example, although free collective bargaining is maintained the bargaining parties are called on to move away from rigid branch collective agreements and »to cede a major part of their responsibilities to individual companies« (p. 58). By means of legally enabled »enterprise alliances for jobs« enterprise regulations are to be reinforced in relation to those of collective agreements. This would be little short of a revolution in labour law and it is already being hotly debated among labour law experts. Codetermination is called for, but with reference rather to the strengthening of the enterprise level as against the collective agreement level.

**Occupational training and further training system:** The CDU is also in favour of the dual system of occupational training because it is a »locational advantage in international competition and the best prophylactic against youth unemployment« (p. 38). Both private and public employers have called for more training places to be made available, although based on a »sense of

responsibility and targeted incentives« and not as a result of state compulsion (p. 39). »Socially responsible study fees« are to be levied at state institutes of higher education.

All in all, the CDU presents itself as the custodian of the social market economy, which is based on the model of the socially responsible entrepreneur. As regards economic policy the CDU's approach owes a great deal to liberal ideas, for example, in the form of various proposals for deregulation.

### 5.3. »The Future Is Green« – Basic Programme of Bündnis 90/ Die Grünen<sup>11</sup>

Alliance 90/The Greens presented their party programme as early as 2002. It is by far the longest of the party programmes compared here. The main issue is the conversion of society into a social and environmental market economy and towards the solar age. The overexploitation of environmental resources is considered the core problem for the future. The necessary conversion, however, is presented as a project which has not only environmental, but also social consequences and requirements.

With regard to social policy Alliance 90/The Greens want to distinguish themselves from the other parties on the basis of their liberal – but not market liberal – ideas: »The existing social market economy, which is too much oriented towards enterprise profit-making, has not lived up to expectations and must be urgently transformed. Social concerns cannot be reduced to a matter of state authority. Without freedom for all social groups; without self-determination for citizens; without subsidiarity; social solidarity becomes ossified in bureaucracy. For us, what is needed is to support civil society with the resources of the state, while at the same time limiting the state. This distinguishes us from the state socialist, conservative and market liberal political models« (p. 43). Alliance 90/The Greens therefore call for a »governance framework« in which environmental, social and cultural interests are guaranteed (p. 46).

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11 Alliance 90/The Greens

**Financial system:** Alliance 90/The Greens are highly critical of the financial system in its current form. What is needed, they believe, is to break the power of the »market dominating global players«: »This requires, on the one hand, a democratically responsible framework and, on the other, environmental information and education, economic incentives for the development of environmentally-friendly technologies and products, and agreements with industry« (p. 27f). They therefore attribute particular significance to the embedding of markets: »The gap between economic globalisation and the deficient political control and embedding of this process must be closed. The European Union is the most far-reaching approach conceived to date to the development of a joint responsibility among states which, to that end, have surrendered part of their sovereignty. The EU must give up its neoliberal fixation in economic policy and play a more active international role in the social and environmental shaping of globalisation« (p. 17). This is extended to the global economy: the further development of international institutions and the introduction of binding regulations and minimum standards for financial transactions are called for (p. 59). The role of »house banks« and savings banks, which are particularly important to small and medium-sized companies, is not mentioned by Alliance 90/The Greens – in contrast to the SPD – despite the fact that the promotion of regional economies is one of their focal issues (p. 54f).

**Labour relations:** The starting point for Alliance 90/The Greens with regard to labour relations is that »as many people as possible should be able to function as conscious actors in economic life« (p. 47). In order to be able to achieve this free collective bargaining and strong bargaining partners should be emphasised, as well as strong works councils. At the same time, »the growing differentiation between economic development and employment structure [calls for] regional- and branch-specific collective bargaining solutions« (p. 48), even though general collective agreements are considered important. It is obvious that this means framework collective agreements and, supplementing that, more flexible and more individual branch-specific and regional collective agreements. Alliance 90/The Greens also advocate »people's participation in productive wealth« (p. 131). They deliberately leave it open whether this is to encompass company agreements or inter-company funds. At the same time, they demand that co-ownership and codetermination be discussed together and that plant and company codetermination »be adapted to changing societal requirements and needs« (p. 131). What requirements and needs these might be the text does not divulge.

**Occupational training and further training:** With regard to occupational training it is vital, as far as Alliance 90/The Greens are concerned, that each person must have the opportunity, in a learning society, to shape their educational/training career individually (p. 99). The focus here is on a shorter period of initial education and accompanying occupational further training: a kind of modular system (p. 99). To this end, initial education should concentrate – for the purpose of sustainability – on (occupational and interdisciplinary) »core qualifications« (p. 100). Companies would be responsible for making available more specific training related to concrete everyday practice in the firm. In comparison to the SPD and the CDU these ideas lack precise formulation: whether the dual system of occupational training is to be retained and whether firms are to continue to be responsible – both financially and, together with vocational schools, for study content – remains open. Whether and how the possibilities of lifelong learning are to be ensured financially and organisationally also remains an open question: there is mention only of the parties to collective agreements and of the fact that there must be »a balance between private and public resources« (p. 103).

All in all, Alliance 90/The Greens present a programme oriented towards sustainability. With regard to relations between state and economy – in other words, with regard to the question of how a coordinated market economy might look – the programme turns out to be a hybrid of liberal approaches (for example, a regulatory framework, but also individual participation in the training system) and social democratic approaches. Whether this is a logical model of society remains to be seen.

## 5.4. The »Wiesbaden Principles« of the FDP<sup>12</sup>

Out of the five parties represented in the Bundestag the FDP's programme is the oldest: the »Wiesbaden Principles« of 1997. The FDP considers its »unique selling proposition« to be its commitment to (economic) liberalism: »The FDP as the party of organised liberalism stands out from all other parties, which seek to bring about progress by trusting in the state and state intervention, because of its commitment to reason, plurality and competition« (p. 6). The role of the state, then, is both a core criticism and the political starting point for the FDP: a »bureaucratic state economy« (p. 14) hinders, as a result of »bureaucratic incrustations« the free and flexible unfolding of economy and society: »Liberals want, instead of a state economy with the best of social and environmental intentions, a market economy with the best social and environmental results« (p. 6). The true path, according to the liberals, is first to bring about economic efficiency – by abolishing state intervention and cartels of powerful interest groups – in order to be able to achieve »social efficiency« (cf. p. 14). This is also reflected in the demand to include a provision on privatisation in the Constitution which would establish that priority be given to the private sector with regard to all tasks that it can perform at least equally efficiently (p. 30). As its model the FDP proclaims a »social and environmental market economy«. However, it defines this quite differently from the CDU, on the one hand, and Alliance 90/The Greens, on the other.

**Financial system:** The financial and capital system should be free. This curt formula best sums up the FDP's position. »In keeping with the requirements of the market« means here that a strong European Union should maintain competitiveness. For the Liberals in 1997 that meant: »instead of ownership by the people Liberals want a people of owners. Opportunities for ownership motivate performance, create social security and promote a sense of responsibility. It is the precondition of a new risk culture and a new culture of personal independence« (p. 15). This leads to the conclusion that entrepreneurs' own financing capacities should be enhanced as much as possible, by means of private wealth, but also through the capital market and the elimination of »barriers to competition«. The task of the state is only regulatory: »a stable common European currency is required to make the German and the European economies more internationally competitive. The Monetary Union completes the Single Market« (p. 25). The main focus of the FDP is the creation of good conditions for investors and thus to boost people's willingness to invest.

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12 Freie Demokratische Partei – Free Democratic Party

**Labour relations:** The FDP succinctly summarises its ideas for change in the area of labour relations as follows: »Workers should become co-entrepreneurs« (p. 14). To that end, the ownership rate with regard to productive assets must be increased significantly. By contrast, the FDP is critical of »codetermination through officials«. The party programme is not forthcoming on the question of whether this reflects a desire to abolish, limit or merely supplement collective codetermination via works councils and workers' participation in supervisory boards. Even with regard to the demand for workers' participation in productive assets it remains open how opportunities to exert influence over enterprise and plant decision-making are to be organised for employees. However, the notion of independent co-entrepreneurs suggests that it is to involve »individual agreements«. General collective agreements (p. 14), on the other hand, are clearly rejected, while general opening clauses are to be established (by law?) which leave companies free to organise workers' participation in whatever form they wish. The fact that the FDP's proposals, although only touched on, suggest a revolution in German labour law cannot be disguised. General (legal) opening clauses endanger the very basis of free collective bargaining. Granting priority to plant agreements points, in addition, to an overturning of the existing legal pyramid, which encompasses both the priority of laws and collective agreements over company and individual agreements and the so-called »favourability principle« (»the regulation most favourable to the workers shall be applied«). How such a considerable boost in the power of enterprises might be controlled remains entirely open.

**Occupational training and further training:** The FDP's statements on occupational training and further training are primarily general in nature. Here, too, »openness and competition« are the order of the day; »encrustations and regimentation« should be eliminated; and private provision should be promoted or permitted (cf. p. 24). Otherwise, it is merely emphasised that the »flexible adaptation and further development of occupational qualifications in all areas« are needed (p. 14).

Overall, the FDP programme represents a call for an uncoordinated market economy. Virtually all problems are attributed to state and bureaucratic encrustations; virtually every problem can be solved by granting more freedom to the market. Freedom is defined as freedom from (state) compulsion. In its liberalistic radicalism this programme leaves little to be desired.

## 5.5. The »Key Programmatic Points« of »Die Linke«

Die Linke (The Left), the party which was formed from the merger of the PDS (Partei des Demokratischen Sozialismus – Party of Democratic Socialism) and the WASG (Arbeit & soziale Gerechtigkeit-Die Wahlalternative – Labour and Social Justice-The Electoral Alternative), has not yet produced a proper party programme. However, there is a »programmatic founding document« which was adopted by the joint party congress of the WASG and »Linkspartei.PDS« in March 2007 and formally (within the framework of the Law on Political Parties) represents the required party programme. It has to be said that the contents of this »programmatic founding document« are not coherent, comprising a mere litany of intentions. The party's Programme Committee presented a first draft of a new party programme in March 2010.

Die Linke's principal aim is to implement an alternative to »unbridled capitalism«, namely a »renewal based on principles of solidarity and the consistent democratic structuring of society« (p. 1): »democracy, freedom, equality, justice, internationalism and solidarity are our fundamental value orientations ... Freedom and social security, democracy and socialism are contingent on one another« (p. 2). To this end, the Constitutional provisions which make possible the state expropriation of key areas of the economy are to be used in order to bring into being an »efficient and democratic economy« based on both private and public ownership (p. 3).

Die Linke claims to stand for a comprehensive change in policies and perspectives. How far such »change« would go is difficult to elicit from the founding document and it remains to be seen which political wing will assert itself.

**Financial system:** The functioning of the international financial and capital markets is regarded by Die Linke as a fundamental factor giving rise to crises and inequality in today's society: »via the global financial markets capital's profit expectations can assert themselves worldwide and without restraint ... The flexibilisation of production and the labour market tailored to the needs of capital destroy family and social life. ... Neoliberal capitalism entails de-democratisation. Immense power is concentrated in international financial funds, transnational concerns and the supranational organisations of global capitalism: the World Trade Organisation, the International Monetary Fund, the World Bank and so on. They are not subject to any democratic control« (p. 5).

The financial system should, according to Die Linke, be restructured. To that end, they demand the »democratic control of the financial markets«, on the one hand, and the »decentralisation of private economic power«, among other things by a tightening up of anti-trust legislation, on the other hand. In addition, the financial system should be supplemented by the promotion of forms of a solidaristic economy (for example, cooperatives) (p. 11) and the expansion of the public sector (p. 8), as well as »employment promoting future-oriented investment programmes« (p. 9f).

**Labour relations:** For Die Linke »work« is not just a matter of earning one's living: »We strive for a society in which every woman and every man is able to work for a living wage. Gainful employment, work in families and partnerships, work to help organise society and participation in cultural and social life must be possible for everyone« (p. 7). With regard to gainful employment Die Linke advocates the much stricter regulation of labour relations by means of the law and collective agreements. For example, the party calls for the retention of free collective bargaining, a »legal minimum wage sufficient to secure people's livelihood«, a »higher degree of employment protection«, »strong codetermination rights for all employees« and the »general applicability of collective agreements«. Company codetermination based on parity is called for (p. 13). There should also be a right to strike for political aims, so far prohibited by the obligation to avoid industrial action during wage negotiations (p. 13). These examples show that Die Linke believes in control of the economy by the state and society.

**Occupational training and further training:** In this connection Die Linke point to social inequality and the task of restructuring the education system in the direction of full participation. With regard to vocational training this includes a demand for a »basic right to training«: »Employers' evasion of their responsibility for occupational training must be halted. We advocate the provision of a wide range of training places. This requires statutory assessment based financing« (p. 17). Training and further training should be promoted by the state (p. 17).

Overall, Die Linke believes more strongly in the state than any other party. As far as can be seen, this will continue to be within the framework of a coordinated market economy. But there is no clear commitment to this. Two things in par-

ticular mark out Die Linke from the other parties. First, key areas of the economy are to be nationalised. How far this nationalisation would go and what form it would take is not specified. Second, there is only a brief description of how the public finances would be structured and be able to provide sufficient wealth to meet all the demands put on the state. Certainly, a party programme does not have to contain a funding and implementation plan, but this is a decisive issue when it comes to the realistic implementation of proposals.

## 5.6. Evaluation of the Programmes in accordance with the Aims of Social Democracy

Social democracy – as it is understood in this volume – takes its bearings from the formal validity and the practical realisation of the covenants of basic rights laid down by the United Nations in 1966 and ratified by the vast majority of countries. It is clear from everything that has been said so far that in particular coordinated market economies – such as those in Scandinavia – come closest to meeting the normative demands of social democracy.

With regard to economic policy aims and objectives Simon Vaut and Christian Krell have presented the three goals of growth, social equality and sustainability as characteristic of social democracy. This raises the question of the manner in which the various political parties are committed to continuing or changing the coordinated market economy.

The party programmes of the five parties represented in the Bundestag amount to »declarations of intent« which provide information on the direction in which the parties – once in power – wish to develop the German economy and German society. The extent to which the parties adhere to their programmes cannot be examined here. However, the reactions and policy proposals of the CDU and the FDP with regard to the financial market crisis in autumn 2008 showed that the general orientation of programmes and concrete political action by no means always correspond. For example, the FDP recently called for a strong state and the CDU – running counter to its economic liberal wing – declared its support for substantial guarantees and loans.

The positions of the parties can be summarised as follows (inevitably from a partial standpoint):

- The **CDU** represents, in this context, a **coordinated market economy at a lower** level than today. Remnants of economic liberalism are combined with individual entrepreneurship as an ethic. Collective forms of codetermination and control tend to be rejected or are to be reduced or made more flexible.
- The **FDP** in its programme advocates **an uncoordinated and liberalistic market economy**. In what way their model of society is to be a »social and environmental market economy« is not readily discernible.
- **Alliance 90/The Greens** are committed to a coordinated market economy which is to be restructured in the direction of a »solar society«. To that end, they borrow liberal ideas, civil society elements and elements of collective control. Overall, the party programme of Alliance 90/The Greens is the longest, although it is short on detail with regard to a coordinated economy.
- **Die Linke** emphatically represents regulation of the economy and advocates a state which protects the individual. It differs from the other four parties in two ways above all: on the one hand, it has developed only »programmatic points« (although a draft party programme has now been presented), and on the other hand, it is an open question whether it really takes the »market economy« as its model.
- The **SPD** commits itself in its programme to a **coordinated market economy** and its expansion. This expansion refers to the comprehensive civil rights and liberties laid down in the UN covenants. But it also addresses the need to adapt governance appropriately. This concerns primarily sustainability, the internationalisation of financial markets, the flexibilisation of economic processes and social protection.

In these terms, the parties can be categorised as follows with regard to the three economic policy goals:

The CDU and the FDP exhibit a clear affinity towards the goal of growth, to which they tend to subordinate the other goals. They are sceptical of the notion of »social equality«.

Alliance 90/The Greens, with their idea of the »solar restructuring« of the social and environmental market economy, take their bearings mainly from the goal of environmental sustainability. »Social equality« is supported, while a clear subordination of the goal of »qualitative growth« can be assumed.

Die Linke has a distinct orientation towards the goal of »social equality«.

The SPD takes an equal and balanced approach to the three goals.

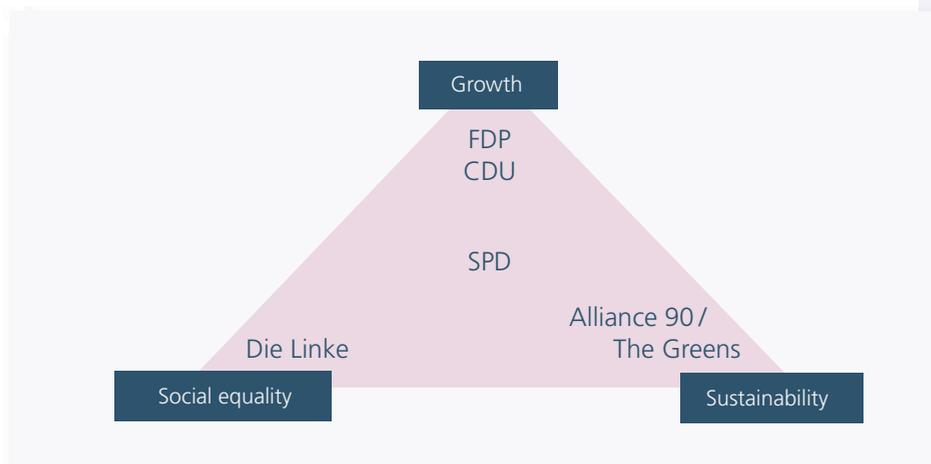


Figure 8: Schematic presentation of the parties according to their economic policy goals

Returning to the initial question: attempts to draw sharp distinctions between the parties' economic and social competence are dangerously reductive and not particularly meaningful in terms of policy assessment. However, the analysis of party programmes also shows that the parties have very different goals concerning how the economy should be socially organised and embedded. Only by looking at this further framework is it possible to find one's bearings in the party landscape and get in a position to judge.

## 6. ECONOMIC ORDERS: COUNTRY MODELS

### What this chapter is about:

- Based on the preceding differentiation in terms of coordinated and uncoordinated types of capitalism various economic systems will be compared in accordance with the theory of David Soskice and Peter A. Hall.
- Under examination will be financing systems, labour relations, education/training systems and the mutual relations of firms.
- The focus of our attention will be the USA, the UK, Germany, Sweden and Japan.
- They cover a wide range, with the USA corresponding closest to the uncoordinated ideal-type and Sweden closest to the coordinated one.
- These different economic models can co-exist even during periods of open markets. They are characterised by a host of prerequisites and are assessed very differently from a social democratic perspective.

### 6.1. USA<sup>13</sup>

*Simon Vaut*

*Typical uncoordinated market economy*

The USA is the classic example of an uncoordinated market economy (Meyer 2005a: 279 ff.), traditionally professing market liberalism, scepticism with regard to state intervention and individualism. The American economic system is chiefly oriented towards the goals of servicing consumerism («giving the consumers what they want») and increasing wealth – at the expense of basic social rights (Gilpin 2001: 150).

However, this judgement can be qualified depending on the historical period in question. In the 1930s, for example, President Franklin D. Roosevelt, with his »New Deal«, an enormous economic stimulus programme, believed in stronger

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<sup>13</sup> The presentation of the USA and Germany here follows the presentation in Meyer (2005a: 279–282) to a considerable extent. We would like to thank the author for granting his permission.

coordination of the economy. The policies of President Lyndon B. Johnson in the 1960s also went in this direction, with his »war on poverty«. But even during these periods the US economy in general remained to a large extent uncoordinated. The policies of President Ronald Reagan (1980s) and President George W. Bush, on the other hand, aimed to minimise economic coordination as far as possible.

### **Financial system**

The financing of US companies takes place mainly through the capital market. This increases the transparency of financial data since listed companies must regularly publish their balance sheets. Company strategies are determined largely by the desire of shareholders for the highest possible dividends. This is known as the shareholder value principle.

Access to capital depends on shareholders' evaluation of the company's earnings outlook. Mergers and takeovers are less regulated than in other countries. For this reason, company managements in the USA are under unrelenting pressure to register the highest possible profits in the shortest possible time. Inadequate yields can lead to dismissal of the management, capital withdrawal via the stock market or takeover.

### **Labour relations**

Organisations of capital and labour in the USA are primarily lobbying organisations for branch interests rather than actors with responsibilities towards society as a whole. In comparison to those in coordinated market economies trade unions and employers' associations are generally weak and lack influential umbrella organisations. In some sectors, however, there are assertive trade unions which represent particular interests effectively. For example, in California there is a well-organised trade union for prison warders which exerts a not inconsiderable influence on policy, including regulation of the penal system. The individual interests of the organised members take precedence over the public interest, however. Statutory employment protection is barely developed in the USA. For this reason, labour relations are characterised by short-term employment relations and enterprise-level wage negotiations. General collective agreements like those found in coordinated market economies are largely unknown as a result of the progressive weakening of trade unions in the USA in recent decades. Robert Reich attributes the decline in the trade union organisation rate from 33 per cent in 1955 to only 8 per cent in 2006 to two factors: first, companies' deliberate anti-trade union

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*Financing through the capital market*

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*Pressure for short-term profits*

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*The actions of employer and employee organisations are not oriented to society as a whole*

---

*Scarcely any employment protection*

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*Weak trade unions as a consequence of anti-trade union policies*

policies and second, increasingly anti-trade union government policy. President Ronald Reagan, for example, imposed a lifetime civil service employment ban on striking air traffic controllers in 1981 (Reich 2008: 108ff).

### **Education and training system**

A generally more flexible labour market is also supported by an education and training system which tends to provide general qualifications which are applicable across firms and branches. Workers can be taken on short-term or laid off («hire and fire») fairly easily, depending on the state of the economy. Since the labour market is relatively unregulated and subject to significant fluctuations American workers tend to invest in general qualifications which they can also use in their next job. And since the employers' associations are fairly weak companies are unable to cooperate in industry-specific training programmes. As a result, workers in the USA are trained in general skills which are particularly suited to the service sector, which is very susceptible to changes in the state of the economy. For many firms and sectors this leads to a lack of qualified workers.

Shortfalls with regard to publicly financed sciences are partly made up by cross-subsidies from the arms industry. Many innovations applied in the civil sector originated from military developments, for example, in aircraft construction, satellite technology and information technology (Reich 2008).

### **Relations between companies**

American companies compete with one another much more than companies in coordinated market economies, such as Sweden or Germany, which focus on cooperation with other companies, with the state and with the trade unions (Hinchmann 2006: 350). Firms are integrated to only a minor degree: neither banks nor other firms have seats on their supervisory boards. In the USA, the notion of economic freedom has always been dominant so that the state intervenes in the market only in order to maintain its functionality and, for example, to prevent the formation of cartels. The strong anti-trust legislation is designed to prevent companies from engaging in, for example, price-fixing.

### **Summary: USA**

The largely uncoordinated market economy in the USA offers companies the opportunity to react flexibly to market developments, but it increases the pressure to adapt to market changes on a short-term basis. The American system of labour

*General  
qualifications*

*Cross-subsidisation  
of research by the  
arms industry*

*Low level of corpo-  
rate integration*

*Largely uncoor-  
dinated market  
economy*

USA		
<b>GDP per capita 2008</b>	38,800 €	GDP per capita in terms of purchasing power standards (PPS); 1 PPS corresponds to the purchasing power of 1 euro (EU27 average) (source: Eurostat)
<b>Average economic growth 1990–2007</b>	2.0 %	Average annual economic growth per capita at constant prices (source: Human Development Index 2009, p. 195)
<b>National debt 2008</b>	70.7 %	National debt as a percentage of GDP (source: Bundesministerium für Finanzen, Monatsbericht 12/2009, p. 99)
<b>Current account balance</b>	– 4.9 %	Balance of all exports and imports of goods as a percentage of GDP (source: International Monetary Fund: World Economic Outlook 10/2009, p. 187)
<b>Employment rate 2008</b>	70.9 % (65.5 %)	Proportion of persons of working age (figure for women given in brackets) aged 15–64 out of the whole population (source: Eurostat)
<b>Unemployment rate 2008</b>	5.8 %	Proportion of unemployed persons in the working age population (source: Eurostat)
<b>Income inequality in terms of the Gini coefficient</b>	40.8 %	Ratio indicating the unequal distribution of income; 100% = maximum inequality (source: Human Development Report 2009, p. 195)
<b>Women's incomes in comparison to men's incomes</b>	62 %	Percentage of women's incomes in comparison to those of men (source: Human Development Index 2009, p. 186)
<b>Poverty Index 2009</b>	15.2 %	The Poverty Index is composed of various indicators (including life expectancy, literacy rate and access to health care); 0 = minimum poverty, 100 = maximum poverty (source: Human Development Report 2009, p. 180)
<b>Unionisation rate 2007</b>	11.6 %	Proportion of the working age population organised in trade unions (source: OECD)

relations is, accordingly, less effective in the development of costly production strategies which require long-term stable employment. Instead, it favours innovative sectors dependent on risk capital, such as information technology, as well as a large service sector based on a generalist educational profile and lower wages.

*Juxtaposition of  
private wealth and  
public poverty*

The economic system of the USA has long enabled it to achieve higher growth rates than European countries: since the 1990s the American economy has grown by an average 3 per cent a year, while the EU countries have managed only 2.2 per cent. Long-term development in the wake of the crisis remains to be seen, however. But these prosperity gains are distributed more and more unequally. While in the 1950s directors' salaries exceeded those of the lowest paid workers in the same company by 25 times, today, on average, the figure is 350 times (Reich 2008: 144). Due to the chronically underfinanced state budget a juxtaposition of private wealth and public poverty prevails. This leads, among other things, to a poor public infrastructure in comparison to other countries (Hinchmann 2006: 352).

*Change of direction  
after the election of  
Barack Obama?*

Since the coming into office of the new US government at the beginning of 2009 the ideology of a lean state which regulates and intervenes little, characteristic of the Reagan and Bush eras, has gone onto the defensive. The health care reforms, economic stimulus packages and increased financial oversight passed under Obama are moving the USA in the direction of more regulation, more coordination and a higher public spending ratio.

## 6.2. Great Britain

*Christian Krell*

Great Britain is often described as the pioneer of capitalism. Industrialisation, free trade and liberalism developed there earlier than in many other countries. At the same time, the dark side of unbridled capitalism also became clear particularly early. Friedrich Engels based his description of the inhuman living and working conditions of dependent workers in the mid-nineteenth century on »the condition of the working classes in England«.

Since Engels's study appeared, admittedly, a good deal has changed in British capitalism. But continuities can also be discerned. The British economic order is still markedly liberal. International comparative capitalism research describes Great Britain, therefore, as an uncoordinated liberal market economy.

In what follows, the main features of the British economy are described.

### **Financing system and ownership structure**

In British capitalism a company's current profit situation is key to its financing. For investment British companies need the »impatient« money of the dynamic share and financial markets. Accordingly, high profitability is the main condition of access to capital. This distinguishes Great Britain, for example, from the economic system which has long characterised Germany in which house banks work together with companies over the long term and thus acquire a good understanding of them, including their strategies and structures. In the United Kingdom, investors and financiers make decisions on the basis of publicly accessible evaluation criteria. Profitability takes priority in this respect.

Ownership structures in Great Britain are very different from those in coordinated market economies. While in the latter holdings in companies are characteristically in the hands of investors with long-term and strategic interests – for example, other companies, banks or the public sector – around 80 per cent of the owners of British companies are financial and private investors whose top priority is generally the highest possible profitability.

So-called hostile company takeovers – also for the purpose of rapid profit-taking – are much easier than in coordinated market economies on account of the

*Pioneer of  
capitalism...*

*... and of its dark side*

*Uncoordinated  
liberal market  
economy*

*Financing through  
the financial and  
stock markets*

*Ownership  
structure: high  
proportion of  
financial and private  
investors*

extensive possibilities provided by market financing and the structure of the financial markets.

The strong orientation towards profitability – linked to their markedly hierarchical internal structure – of British companies enables them, on the one hand, to carry out rapid restructuring in the direction of new and more profitable markets; less productive branches of the business are quickly cut back. On the other hand, however, this orientation leads to the »short-termism« characteristic of the British economy – its orientation towards what can be achieved quickly.

### **Labour relations**

There have been periods during which British trade unions appeared to be particularly strong. The so-called »winter of discontent« is one example of this. In 1978–79, a national strike paralysed the public sector in Great Britain: rubbish was not taken away, local public transport came to a standstill and the dead were not buried. In fact, however, periods of intensive strike action do not indicate strong trade unions. Strong and well-organised trade unions are, as a rule, in a position to assert the interests of the workers in negotiations, without having to resort to strikes. Accordingly, the »winter of discontent« was rather the expression of inadequate negotiating power. The British trade unions are weak by international comparison. That is primarily due to the fact that the British trade union landscape is relatively fragmented. In the 1990s, there were still over 300 trade unions. These are organised not by branch but by occupational groups, as a result of which often a multitude of trade unions are represented in a workplace. A second reason for the weakness of British trade unions is that in Great Britain, typically for liberal market economies, there is no obligation on companies to introduce works councils or other forms of worker representation. Codetermination, of the kind which exists, for example, in the German coal and steel industry, is largely unknown in Great Britain. Finally, trade union rights were systematically curtailed by the conservative Thatcher government (1979–1990). Accordingly, the level of unionisation today is comparatively low. In Great Britain the proportion of the working population organised in trade unions is just under 30 per cent. The public sector is much better organised than the private sector.

Like the employees, the employers are also relatively poorly organised. Umbrella organisations with teeth are virtually non-existent and the significance of employers' associations is declining.

*Orientation towards what can be achieved in the short term*

*Only apparently strong trade unions*

*Marked fragmentation of trade unions*

*No obligatory workers' representation*

*Overall, a lower level of unionisation*

On the basis of these structures wage rates are generally negotiated at the enterprise level or are the result of individual negotiation processes between employers and employees. Since 1999, there has been a lower wage threshold, in the form of a minimum wage, which cannot be undercut.

*Wage negotiations at enterprise level but with a minimum wage*

Relations between companies and individual employees are much more strongly determined by market forces than in coordinated market economies. Employees tend to remain at companies for a comparatively short time and as a result tend to have little company loyalty. Redundancies are relatively easy to impose since the weak trade unions cannot effectively prevent them and employment protection is weak. At the same time, qualified employees find it easier to get a new job in flexible labour markets.

*Little employment protection*

British companies are generally much more hierarchically organised than companies in coordinated market economies. Besides the dominance of the chief executive officer (CEO) this also finds expression in work organisation. For example, team work among highly qualified workers, of the kind frequently encountered in Germany, is rare in Great Britain, where a conventional and strictly maintained division of labour is typical (Wood 2001: 250).

*Strong hierarchisation within companies*

### **Training and further training system**

In Great Britain's flexible labour markets occupation-specific qualifications are thin on the ground. The reasons for this are easily comprehensible from an employer's standpoint:

*Provision of general skills*

First, because employees tend to stay with a particular company for a relatively short time there is always the danger that investment in individuals will not pay or may even benefit a rival company. Second, because of the extreme flexibility of labour markets qualified workers can be taken on – and, if need be, let go – quite quickly.

Furthermore, there are few incentives on the employee's side to acquire firm-specific qualifications since the comparatively short time spent at a given employer inculcates the idea that a concentration on general skills which can be used in other firms or branches is more worthwhile.

The almost inevitable outcome of this lack of emphasis on occupational qualifications is that productivity in British companies is relatively low in comparison to, for

example, German companies and that liberal market economies tend overall to focus on products which are simple to process and standardised production methods.

### **Relations between companies**

Relations between firms are based on market relations and legally enforceable formal legal relations. Companies are scarcely integrated with one another. Technology transfer takes place primarily through the exchange of highly qualified scientific or technological personnel. The movement of scientists and engineers from research institutes into the private sector and back again is more frequent than in traditional coordinated market economies. On the other hand, joint research projects between companies or long-term cooperation networks are rarer.

### **Evaluation and summary**

The British type of capitalism is much closer to the US economic system than to continental European economies. The advantages of British capitalism, as a result, are a relatively high employment rate and a low unemployment rate. Its disadvantages are the continuing low productivity of British companies in comparison to US or German companies and their short-term profit orientation. On top of that, in the current economic downturn all the drawbacks of markedly flexible labour markets are coming to the surface: workers can be made redundant easily and the unemployment figures are rising sharply.

However, it is important to note that such categorisations are never conclusive. The British political system, with its first-past-the-post elections and centralised state structure, means that individual governments can rapidly implement far-reaching structural changes.

*Scarcely any  
integration between  
companies*

*Very close to the US  
economic system*

Great Britain		
<b>GDP per capita 2008</b>	29,200 €	GDP per capita in terms of purchasing power standards (PPS); 1 PPS corresponds to the purchasing power of 1 euro (EU27 average) (source: Eurostat)
<b>Average economic growth 1990–2007</b>	2.4 %	Average annual economic growth per capita at constant prices (source: Human Development Index 2009, p. 195)
<b>National debt 2008</b>	52.0 %	National debt as a percentage of GDP (source: Bundesministerium für Finanzen, Monatsbericht 12/2009, p. 99)
<b>Current account balance</b>	-1.7 %	Balance of all exports and imports of goods as a percentage of GDP (source: International Monetary Fund: World Economic Outlook 10/2009, p. 187)
<b>Employment rate 2008</b>	71.5 % (65.8 %)	Proportion of persons of working age (figure for women given in brackets) aged 15–64 out of the whole population (source: Eurostat)
<b>Unemployment rate 2008</b>	5.6 %	Proportion of unemployed persons in the working age population (source: Eurostat)
<b>Income inequality in terms of the Gini coefficient</b>	36 %	Ratio indicating the unequal distribution of income; 100% = maximum inequality (source: Human Development Report 2009, p. 195)
<b>Women's incomes in comparison to men's incomes</b>	67 %	Percentage of women's incomes in comparison to those of men (source: Human Development Index 2009, p. 186)
<b>Poverty Index 2009</b>	14,6 %	The Poverty Index is composed of various indicators (including life expectancy, literacy rate and access to health care); 0 = minimum poverty, 100 = maximum poverty (source: Human Development Report 2009, p. 180)
<b>Unionisation rate 2007</b>	28 %	Proportion of the working age population organised in trade unions (source: OECD)

## 6.3. Germany

*Simon Vaut*

*Germany is a coordinated market economy*

Germany is a typical coordinated market economy (Meyer 2005a: 280ff) and was long regarded as a model of an exemplary combination of economic dynamism, political stability and social equality (Egle 2006: 273–326). With rising unemployment and the economic stagnation which set in in the 1990s, however, the German model lost its sheen and was even described by *The Economist* as »the sick man of Europe«. The economic upturn in recent years seems to have refuted this judgement but it remains to be seen whether even Germany will meet the challenge posed by the financial market crisis.

*Company financing through the banks*

### **Financing system**

In Germany, company financing via the capital market plays only a minor role. Enterprise management is therefore evaluated not solely by the market but also by the banks and other enterprises interlinked with the enterprise, as well as employees' representatives and state actors. This can favour the personal exchange of information and the development of trust. The financing of companies takes place mainly through bank loans. In the granting of these loans, besides financial data, a company's reputation and network play a role. Investors obtain information on the reputation and operations of a firm, in turn, via close networks of connections. This access to »patient capital« that is not dependent on short-term yields enables companies to invest in long-term projects and to retain a well qualified workforce even during periods of economic crisis. This tallies with the observation that managements in Germany feel under less pressure to maximise immediate profits or to react swiftly to a fall in the company share price. Tax regulations, laws and broad networks of interlinked companies tend to discourage hostile takeovers. This interlinking of companies and banks has, it is true, been criticised as a »bank cartel« (Bury and Schmidt 1996) because it makes access to capital more difficult for new market entrants and favours insiders. Developments in recent years, however, indicate that such industrial relationships are breaking up in Germany and international involvements are increasing, as explained in the following section.

*Access to »patient« capital*

## Excursus: The End of Germany Plc?

At first largely unremarked upon in the political debate Germany has, slowly but surely, undergone an enormous change since the 1990s, which has been described as the »winding up« of Germany Plc. The expression »Germany Plc« refers to the traditional interlinking of bank and industry in Germany. The origins of these ties can be traced to the imperial era. This integration served, among other things, as a bulkhead externally and to maintain stability internally. Under pressure from globalisation, however, the system of house banks and cross-holdings has proved to be an impediment, in particular when German firms would like to participate in the global capital market (Egle 2006: 291).

As a result, in recent years these mutual capital holdings of banks and industry have decreased significantly. German companies have become more specialised and internationalised.

The interlinking of companies – particularly between banks and industry – in Germany has tended to come apart in recent years. This shows how much globalisation has changed Germany's economic system.

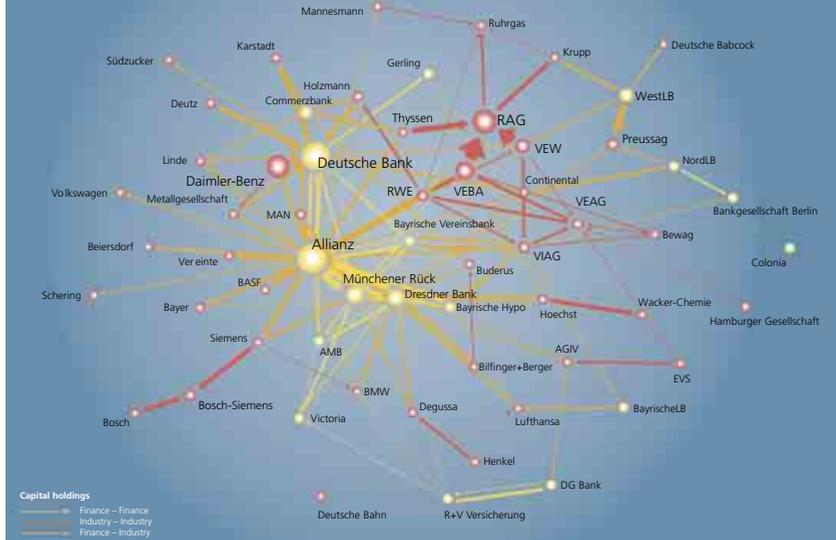
The time series data of the Max Planck Institute for the Study of Societies in Cologne verify this: in contrast to the dense network of capital linkages that existed in 1996 it is now much thinner.

German companies, as a result, have become much more open to the international capital market. Germany has thus moved away somewhat from the model of coordinated capitalism towards an uncoordinated model. The takeover of the venerable German company Mannesmann by the British mobile phone group Vodafone in 2001 had previously been considered inconceivable and represented something of a caesura. Today (mid-2010), ten of the 30 DAX companies are in majority foreign ownership: in 2000 there were only three. During the same period the inflow of foreign direct investment (FDI) has tripled, while German holdings in international markets have also increased.

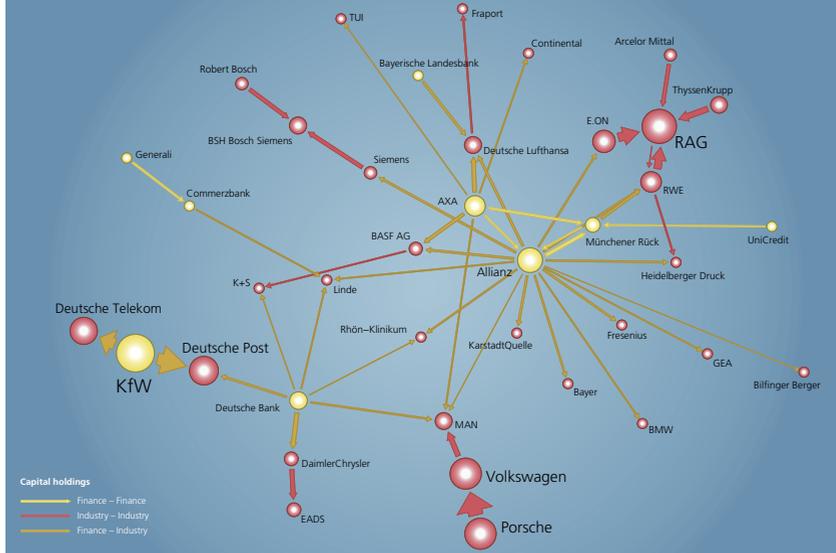
*Is the interlinking  
of banks and  
companies  
unravelling?*

*Tendency towards  
the uncoordinated  
model*

## Cross-holdings in Germany 1996



## Cross-holdings in Germany 2006



© 2008 Lothar Krempel, Max-Planck-Institut für Gesellschaftsforschung, available at: [www.mpifg.de/people/lk/](http://www.mpifg.de/people/lk/); data from the Monopoly Commission (Monopolkommission), available at: <http://www.monopolkommission.de>

This de-linking has been encouraged by the abolition of taxes on capital gains. This was previously 53 per cent, which made the sale of shareholdings extremely unattractive and contributed to the rigidity of industry and bank interlinkages.

The trend towards internationalisation and increased FDI is continuing. Having said that, a debate has begun on whether this openness to »sovereign wealth funds« and private equity funds should be limited.

The overall assessment of the winding up of Germany Plc is mixed. On the one hand, the opening up to international capital with investment and know-how has helped to keep many German companies competitive and has enabled them to improve their position on world markets. Unit wage costs have decreased significantly, in contrast to all other European countries. Exports increased by 50 per cent in the course of a decade – far more than in neighbouring countries (source: Economist Intelligence Unit 2006). On the other hand, the pressure for yield and a short-term orientation have increased, heightening uncertainty in labour relations.

The risk of more takeovers of German companies by private equity funds and hedge funds is being widely debated, generally with reference to a plague of locusts. The main criticism is that these companies are interested solely in short-term results.

The German Council of Economic Advisers (Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung) stated in its 2005 annual report: »In the foreground of the debate in Germany stood the risks for companies. It was feared that short-term oriented financial investors were acquiring holdings in companies, stripping their assets and unlocking their reserves in order to sell the holding again, leaving the company much weakened«. In response the Risk Limitation Act was introduced in 2008, which obliges investors to disclose the origin of their funds, as well as their aims (Sachverständigenrat 2005: 35).

### **Labour relations**

In Germany, the unionisation rate is modest by international comparison, at 20 per cent (Stand 2007: p. 111). However, free collective bargaining gives them considerable influence over wage formation and working conditions (Egle 2006: 290). Trade unions and employers' associations are sector-specific: for example,

*Advantages and disadvantages of international capital flows*

*Free collective bargaining*

*Wage negotiations  
sector-specific*

for the metal industry, there is IG Metall and Gesamtmetall. This means that the coordination of wage negotiations takes place within the confines of this sector, ensuring that workers in the same industry can expect the same wages. As a result of these homogenous wages there is no wage competition between companies for the best qualified workers (Hassel 2006: 14).

*Codetermination*

Workers' participation with regard to issues of work organisation and personnel decisions is well developed in Germany by international comparison. The Works Constitution Act regulates the size, competences and exemptions of works councils. Joint-stock companies are statutorily subject to codetermination if they have more than 500 employees. That means, for example, that workers delegate representatives to the supervisory board of a company.

*The importance  
of the dual  
training system*

**Training system**

The complex production systems of many German companies often require well qualified workers. To that end the dual training system, with its combination of high practical relevance and technical depth, has proved to be invaluable (Egle 2006: 287). It is a »core institution of German capitalism« (Hassel 2006: 13). Those undergoing training are paid relatively little, but in exchange young people are generally guaranteed qualified entry into the labour market, which gives Germany one of the lowest rates of youth unemployment (as a proportion of the adult unemployment rate) in the OECD (Hassel 2006: 15).

Their comparatively high specialist qualifications give workers more negotiating power than in countries in which training systems are more general and workers thus more interchangeable. Quality-oriented production entails a certain dependence on well qualified workers. In order to protect themselves against ever more far-reaching demands on the part of their employees and to prevent other firms wooing away well qualified workers German firms have established coordinated wage negotiations between employers and employees in the industrial relations system. This results in the alignment of wages for comparable skills across industrial sectors. This makes it more difficult to poach workers with industry-specific skills.

*Training system  
in jeopardy*

However, the dual training system is under threat from three directions. In economic upturns companies are happy to take on trainees as good value and flexible workers. In periods of economic stagnation there tends to be a shortage of

training places. If this shortage continues for an extended period it tends to be self-perpetuating because those who are unable to get a training place swell the ranks of those looking for training in the following year, stepping up competition. Secondly, companies are shirking their training responsibilities. And thirdly, the »half-life« of knowledge and know-how is becoming shorter and shorter. Virtually no training can set a worker up for life. Germany, with its underdeveloped provisions for training and further training, has yet to find an answer to the challenges of a more rapidly changing world of work.

### **Relations between companies**

The managements of large German companies rarely have the opportunity to take important decisions unilaterally. Instead, the agreement of supervisory boards and networks must be obtained in which, besides banks, other companies, employees and state actors are represented. As a result, it is not so much the short-term interests of shareholders in yield that determine company decision-making as the interests of a number of other stakeholders.

The role of the state in Germany's political economy after the Second World War can best be described as a facilitating or enabling one. Although its opportunities to intervene directly in economic processes were limited by federal structures and a number of independent institutions, such as the Bundesbank and the Federal Cartel Office, the state did develop the ability to promote the self-organisation of societal groups and quasi-public corporatist actors and to provide them with the necessary, partly constitutional means so that areas of the economy could regulate and administer themselves which elsewhere are regulated by the state or left to the market. The European Central Bank (ECB) and its monetary independence, as well as the European Commissioner for Competition follow the political-economic principles which apply in the Federal Republic and therefore do not disrupt that system. Furthermore, the state transfers a considerable proportion of GDP to the social security system and pursues the Constitutional provision on »equal living conditions« in all federal states by means of the system of regional redistribution (Streeck 1995).

### **Assessment**

Germany's economic system is mid-way between the Anglo-Saxon market economy and the Scandinavian welfare state (Schmidt 2000).

*A number of interests are involved in company decision-making*

*Germany: between Scandinavia and the USA*

In Germany, employment relations tend to be more long-term: on average, employees work for the same employer for more than ten years, in comparison to eight years and seven years in the UK and the USA, respectively (Streeck 1995). Cooperative labour relations and a highly qualified labour force result in productivity increases which makes it possible to pay skilled workers well and to reduce working time (Hassel 2006).

Wage distribution is therefore relatively narrow in Germany and skilled workers, in contrast to other countries, belong to the middle class. This class is very broad in Germany: 66 per cent of the population count as middle class in comparison to 26 per cent in the UK and 44 per cent in the USA (Rössel 2005).

As a result of economic crises, however, the German model has come under criticism since the 1990s. In particular in the 2005 general election conservatives launched a debate on how Germany was falling behind, alleging that the country was no longer internationally competitive. Despite these prophecies of doom, however, Germany, long the world's number one exporter (it is still second, behind China), has again and again manifested its strong competitiveness. This is due, among other things, to the high quality of its complex industrial goods, especially in the automobile industry and in mechanical engineering and construction. The proportion of industrial workers has remained steadily around 10 per cent higher than in the other OECD countries (Egle 2006: 292).

Germany		
<b>GDP per capita 2008</b>	29,100 €	GDP per capita in terms of purchasing power standards (PPS); 1 PPS corresponds to the purchasing power of 1 euro (EU27 average) (source: Eurostat)
<b>Average economic growth 1990–2007</b>	1.4 %	Average annual economic growth per capita at constant prices (source: Human Development Index 2009, p. 195)
<b>National debt 2008</b>	65.9 %	National debt as a percentage of GDP (source: Bundesministerium für Finanzen, Monatsbericht 12/2009, p. 99)
<b>Current account balance</b>	6.4 %	Balance of all exports and imports of goods as a percentage of GDP (source: International Monetary Fund: World Economic Outlook 10/2009, p. 187)
<b>Employment rate 2008</b>	70.7 % (65.4 %)	Proportion of persons of working age (figure for women given in brackets) aged 15–64 out of the whole population (source: Eurostat)
<b>Unemployment rate 2008</b>	7.3 %	Proportion of unemployed persons in the working age population (source: Eurostat)
<b>Income inequality in terms of the Gini coefficient</b>	28.3 %	Ratio indicating the unequal distribution of income; 100 % = maximum inequality (source: Human Development Report 2009, p. 195)
<b>Women's incomes in comparison to men's incomes</b>	59 %	Percentage of women's incomes in comparison to those of men (source: Human Development Index 2009, p. 186)
<b>Poverty Index 2009</b>	10.1 %	The Poverty Index is composed of various indicators (including life expectancy, literacy rate and access to health care); 0 = minimum poverty, 100 = maximum poverty (source: Human Development Report 2009, p. 180)
<b>Unionisation rate 2007</b>	19.9 %	Proportion of the working age population organised in trade unions (source: OECD)

## 6.4. Japan

*Werner Pascha*

Japan is regarded as a typical instance of the coordinated market economy. Within the spectrum of coordinated market economies Hall and Soskice (2001: 34) categorise Japan in terms of (industrial) »group-based coordination«. That means that the coordination of economic activities takes place by means of cross-sectoral business conglomerates – in Japan, via the so-called keiretsu.

Like Germany, Japan was regarded as a model of how to achieve economic prosperity and social equality at the same time (Kevenhörster, Pascha and Shire 2003).

By the time of the economic crisis of the early 1990s at the latest, however, this nimbus had faded. The trigger of the economic crisis was the »bubble economy«; in other words, the bursting of a speculative bubble. Hesitantly at first, market liberal reforms were introduced, in particular during the government of Prime Minister Koizumi (2001–2006).

### **Financing system**

Japan's financing system in the post-war period has been bank-oriented. For decades, the main financing instrument for companies was bank loans.

The banks, in turn, were to a considerable degree reliant on the central bank during the early post-war period due to the lack of capital. Via the central bank the state assumed a major role, directly in relation to the banks and indirectly in relation to companies.

Overall, it was the large undertakings that benefited from the system. The state made favourable interest rates available to them if they met strategic targets. A high investment rate and strong growth were the consequences, from which the workforce also benefited (Aoki and Saxonhouse 2000).

Since the 1970s much has changed, however. Companies and banks, as a result of economic internationalisation and liberalisation, have been able to free themselves from their close ties with the state. In particular, large companies were able to obtain financing through the capital market. One unintended consequence of this change was the already mentioned »bubble economy« of the late 1980s

*Japan: Long a model of economic prosperity and social equality*

*Company financing by the banks*

(Amyx 2004). In 1997, a package of measures known as the »big bang« was passed. The idea was to make Japan more attractive as a financial centre. But it is only since 2003 that the long-term effects of the bursting of the bubble could be resolved in the banking system.

### **Labour relations**

The labour system in Japan has been oriented towards long-term employment since before the Second World War, although it was only after the war that it really blossomed (Demes 1998). Regular wage increases, six-monthly bonuses depending on company performance, attractive social benefits and good opportunities for promotion were designed to maintain the loyalty of skilled workers.

This system provided firms with flexible, reliable workers who had an interest in the firm's success and strove to promote it. However, the main beneficiaries were male, regular workers at large companies – in other words, only around one-third of the working population.

One of the dark sides of this was the strong dependence of even privileged workers on their company. Professional experience was tightly linked to one firm. Low mobility between firms, a lot of overtime and postings which disregarded the needs of family life were the virtually inevitable consequence.

On the positive side, income differences in Japan remained reasonable, even between top management and ordinary workers.

In Japan, company trade unions became the norm during the post-war period. Even when conflicts were frequent both company management and company trade union pulled together. Representation of employees' interests in smaller companies or among those in irregular employment was negligible. Overall, the role of the trade unions is continuing to decrease due to the increasing diversification of employment relations and employee interests.

The system of long-term employment is also in retreat (Haak 2006). In the crisis-stricken 1990s, older, highly paid workers were primarily affected. Irregular employment – for example, part-time work or subcontracted work – have become much more important. Since 2003, the average wage has barely increased despite relative economic success.

*Long-term  
employment...*

*...with a dark side*

*Company trade  
unions*

## Education and Training System

Since the late nineteenth century the state has guaranteed a basic education through state institutions. Virtually all young people now complete more than nine years of compulsory schooling. For a long time the aim of education was to promote diligence, tenacity and social integration and to transmit essential knowledge rather than to stimulate creativity or to cultivate an independent personality (Münch and Eswein 1998). This meant that graduates were optimally suited for firms which themselves wanted to provide firm-specific skills.

In companies, »job rotation« and »training on the job« are the order of the day, as a result of which the acquired skills are so firm-specific that moving to another company is scarcely possible. Another characteristic of the training system is that young people are »sorted« in accordance with their ability as defined above. By means of this filtering well-paying large companies can easily identify the best applicants, while less well-positioned school leavers have to make do with inferior positions.

For some time worries have been increasing that the predominance of diligent but less creative workers is not compatible with remaining at the cutting edge of technological and organisational progress. In addition, the one-sided focus on young labour market entrants is no longer appropriate in the face of a rapidly aging society. Schools and universities should therefore develop creativity and individuality, and also make provision for older people. On top of that, firms are trying to wean themselves off traditional forms of employment and in-house training measures. The employment of foreign graduates, the acceptance of qualified women in management and so on represent major challenges, however.

## Relations between companies

There are a whole range of ties between Japanese companies: many observers speak of a network economy (Lincoln and Gerlach 2004). Horizontal conglomerates, such as Mitsubishi or Sumitomo, are composed of companies in different branches which are interlinked via exchanges of personnel, capital and other mechanisms. In competition with other conglomerates they have cultivated considerable competitive advantages without becoming bogged down in traditional branch specialisations.

Vertical conglomerates establish ties along the value chain. While the parent company – for example, Toyota – can ensure quality in final assembly and is

responsible for strategic matters, a first group of suppliers takes care of key system components. The subordinate levels mainly comprising smaller suppliers concern themselves with individual components. Such supplier pyramids make possible great flexibility and versatility, even if the lower levels have to shoulder a considerable burden when economic difficulties ensue.

Further relations between banks and companies arise out of the credit-oriented finance system. In the post-war period banks have performed a supervisory role as house banks and thus were often more important than shareholders. The Japanese system of corporate governance was shaped internally by the management hierarchy and externally by the banks (Dirks and Otto 1998). If a company got into difficulties the banks were expected to support it in order to prevent systemic crises. In return, the state undertook to guarantee the continuing existence even of the weakest banking institutions. With the personal ties between bankers and companies, and to some extent also civil servants, long-term strategies were possible. On the other hand, this could also lead to problematic arrangements, not excluding corruption.

In the meantime, the system has come under considerable pressure. The increasing dependence on the international capital markets is forcing companies to make their relationships and governance more transparent. This is giving rise to the danger that Japanese companies will have to become as short-termist as Western companies and that the strengths of long-term trust-based cooperation will be lost.

### **Assessment**

Japan's »group-based« coordinated capitalism was best suited to bring out the strengths of its industrial sector in the post-War period. It was able gradually to improve its largely standardised industrial products and to put them onto the world market in large quantities, while maintaining good quality and constantly increasing productivity. Bank financing and supervision made it possible to pursue long-term strategies. Powerful conglomerates organised the resources needed to realise these strategies. The education system made the requisite workers available.

Although this mechanism created some social and political problems – for example, differences between large and small companies, a lack of opportunities for personal development and a certain proclivity to corruption, overall most Japanese benefited from the economic boom.

*Company supervision by the banks*

*Optimisation of industrial production...*

*... but also social and political problems*

In the wake of internationalisation and technological and organisational progress, however, the system has reached its limits. Social equality is being undermined and putting the government under considerable pressure – a major reason for the unstable governments since the demise of market reformer Koizumi.

In the meantime, the question has arisen of how far Japan's economic system is moving in the direction of the uncoordinated Anglo-American model (Dore 2000; Pascha 2004; Streeck/Yamamura 2003). However, it seems that Japan will not opt for uncoordinated capitalism. The strongest indication of that is developments in corporate governance. In particular, the combination of capital market orientation, market-oriented personnel policy and openness of governance characteristic of an uncoordinated model is still little in evidence. Rather intermediate forms dominate, for example, the integration of a more open personnel policy with an otherwise traditional post-War model (Aoki/Jackson/Miyajima 2007).

A new and internally coherent overall system has not yet manifested itself.

Japan		
<b>GDP per capita 2008</b>	27,800 €	GDP per capita in terms of purchasing power standards (PPS); 1 PPS corresponds to the purchasing power of 1 euro (EU27 average) (source: Eurostat)
<b>Average economic growth 1990–2007</b>	1.0 %	Average annual economic growth per capita at constant prices (source: Human Development Index 2009, p. 195)
<b>National debt 2008</b>	173.1 %	National debt as a percentage of GDP (source: Bundesministerium für Finanzen, Monatsbericht 12/2009, p. 99)
<b>Current account balance</b>	3.2 %	Balance of all exports and imports of goods as a percentage of GDP (source: International Monetary Fund: World Economic Outlook 10/2009, p. 187)
<b>Employment rate 2008</b>	70.7 % (59.7 %)	Proportion of persons of working age (figure for women given in brackets) aged 15–64 out of the whole population (source: Eurostat)
<b>Unemployment rate 2008</b>	4.0 %	Proportion of unemployed persons in the working age population (source: Eurostat)
<b>Income inequality in terms of the Gini coefficient</b>	24.9 %	Ratio indicating the unequal distribution of income; 100% = maximum inequality (source: Human Development Report 2009, p. 195)
<b>Women's incomes in comparison to men's incomes</b>	45 %	Percentage of women's incomes in comparison to those of men (source: Human Development Index 2009, p. 186)
<b>Poverty Index 2009</b>	11.6 %	The Poverty Index is composed of various indicators (including life expectancy, literacy rate and access to health care); 0 = minimum poverty, 100 = maximum poverty (source: Human Development Report 2009, p. 180)
<b>Unionisation rate 2007</b>	18.3 %	Proportion of the working age population organised in trade unions (source: OECD)

## 6.5. Sweden

*Erik Gurgsdies*

*Full employment  
with a »solidarity  
based wage policy«*

### **The Rehn-Meidner Model**

Swedish economic policy is based on the so-called Rehn-Meidner model, named after two trade union economists Gösta Rehn and Rudolf Meidner. In 1951, they developed a general economic model which was designed to reconcile full employment with a »solidarity based wage policy«, but without triggering inflationary processes.

The fundamental idea was that permanent full employment cannot be achieved by generally high aggregate demand, whether generated by favourable development of the global economy or by national economic stimulus programmes. Since individual economic branches also grow at different rates, continuously high aggregate demand leads rapidly to the formation of bottlenecks. In order to be able to maintain growth in the face of that sectors in which bottlenecks have developed seek to woo workers away from other sectors. With full employment this can be achieved only by bidding up wages, leading to price increases in these sectors. As a consequence, in order to compensate for losses in purchasing power, wages rise in the other branches, which results in price increases across the board and thus inflation in the national economy.

### **Solidarity wage policy**

To make matters worse, from the end of the Second World War the Swedish trade unions pursued a so-called »solidarity wage policy«. This had two principal aims. First, it aspired to applying the principle of »equal pay for equal work« and was based on the development of average labour productivity. Second, the wage gap between different kinds of work was generally to be reduced. The condition for achieving these goals was the prioritisation of central wage negotiations at the expense of lower levels.

In order to prevent the gains ensuing from a »solidarity wage policy« from being lost to inflation the Rehn-Meidner model recommended a tight public finance policy which keeps aggregate demand in check by means of budget surpluses.

This economic policy concept puts low-productivity companies on the defensive in two ways: first, they are confronted with sales problems when demand is

*Advantages and  
disadvantages of the  
Rehn-Meidner model*

*Pressure on low-pro-  
ductivity companies*

only moderate due to their poor cost and price structure; second, the »solidarity wage policy« exacerbates their already difficult situation with regard to costs and competitiveness in that it gives rise to wage demands in all branches and at all companies in step with average labour productivity.

In direct contrast, the situation favours high-productivity companies in two ways: first, they are confronted by ample demand on account of their good cost base and favourable prices; second, wage settlements are deliberately tailored to average productivity thereby creating a certain room to manoeuvre as a result of high productivity. In this way these companies receive a capital boost for the creation of high-productivity jobs.

Low-productivity companies and their employees lose out as a result of the restrictive public finance policy and the »solidarity wage policy«. The resulting unemployment is not regarded defensively as a public problem, however, but proactively as a matter requiring public action. A constantly expanded and refined »selective labour market policy« was therefore developed. By means of extensive training activities and mobility assistance strenuous efforts were made to qualify the unemployed, as well as persons entering the labour market or returning to it after a break, for productive and well-paid jobs.

Under the Rehn-Meidner model, then, restrictive fiscal policy, »solidarity wage policy« and »selective labour market policy« are directed towards the constant renewal and structural adjustment of the Swedish economy. Since the 1960s this model has – sometimes more, sometimes less – provided the guidelines of Swedish economic policy. Overall, the Swedish economic model has been characterised by a »conceptual coherence [unity] and political acceptance which comparable countries have barely approximated«, as Fritz W. Scharpf remarked in 1987 on the basis of a comparison of social democratic economic policy in Germany, the UK, Austria and Sweden (Scharpf 1987: 119). This judgement also holds today. With its small domestic market of less than ten million inhabitants Sweden has managed, despite the upheavals of globalisation, not only to maintain a keenly competitive economy in the global market but to intensify its trade in goods and – more recently – provision of services. Exports now account for half of GNP.

*More productive companies are favoured*

*Unemployment is understood proactively as a task requiring public action*

*High level of acceptance of the Swedish model*

*Not dependent on  
the capital market*

## **Financing system and ownership structure**

Corporate financing comprises a number of elements in Sweden. Financing is based first and foremost on a distinctive system of house banks. There are also elements of equity financing, but with the peculiarity that cross-holding of shares is common among Swedish companies. A key characteristic of corporate financing in Sweden, therefore, is a long-term outlook. The Swedish financing system resembles the one which was long known in Germany under the name »Rhine capitalism«.

*Avoidance of  
educational  
dead-ends*

## **Training system**

In Sweden, it was recognised early on that in a globalised economy the most important »raw material« of a competitive economy is education. Swedish vocational training takes place in upper secondary school (between the ages of 16 and 20). Virtually all students engage in it voluntarily. Besides the academic route, there are 14 national programmes which offer specific vocational training.

A basic principle of Swedish education policy is that educational dead-ends should be avoided as far as possible. To that end, specific vocational training is supplemented to a considerable extent with more general education and vocational qualifications are combined with the higher education entrance qualification. In 2006, the pass rate for the school leaving certificate, for example, was 94.6 per cent.

Also characteristic of the Swedish education and training system are the many opportunities for recurrent training throughout working life. As we have already seen, the goal of Swedish economic and employment policy is not the protection of existing workplaces, but rather enabling people to take up productive and thus the most competitive jobs within the framework of international competition. In the education and training system, therefore, general and specific training are combined for the whole population.

## **Labour relations**

When it became evident that the Social Democrats would not be ousted from government for the foreseeable future the employers accepted the trade unions as full-fledged negotiation partners in the so-called Saltsjöbaden Agreement of 1938.

*Trade unions and  
employers on an  
equal footing*

The Agreement meant that the state would be kept out of labour market regulation as much as possible. This remained the case for the next 30 years or so. The

labour market was peaceful and wage development was controlled centrally via wage agreements. There was virtually no labour market legislation.

This period of cooperation was followed by one of confrontation from the beginning of the 1970s up to 1998. The central wage negotiation system progressively came apart. In particular as a result of the constraints imposed by the Stability and Growth Pact in the wake of EU accession it became clear to both sides that the wage negotiation system would have to be established on a new basis. Prompted by the Social Democratic government the most important industrial trade unions and employers concluded the so-called »Industry Agreement« (Industrins samarbetsavtal) in 1998.

The Industry Agreement is based on the following pillars: first, a set of rules aimed at minimising the periods during which there is no agreement and thus likely to lead to conflict. For this reason negotiations on the next agreement must commence before the expiry of the existing one. Second, publically appointed non-partisan arbitrators are involved to influence negotiations in the direction of agreements in accordance with EU norms. Finally, the idea that the export-oriented private sector should have a wage-guiding function was revived. Substantial portions of the Industry Agreement were later adopted for the public sector.

Trade unions are in a very strong position in Sweden and the organisation rate is high, at 70 per cent. In that context it is perfectly natural that enterprise codetermination should be organised by the trade unions. German duplication in the form of autonomous works councils is unknown in Sweden.

Codetermination at company level – again in contrast to Germany – is not institutionalised by law. In Sweden the path taken was to grant the trade unions negotiation rights over all kinds of codetermination issues. In conflicts arising from codetermination there is a right to strike even while collective (wage) agreements are in force.

### **Relations between companies**

Not only the trade unions, but also the employers' associations have a high organisation rate in Sweden. Strong partners on both sides was one of the main reasons for the success of the abovementioned agreements between employers and trade unions. Also characteristic of Sweden are the strong cross-holdings of

companies. Besides market relationships, finally, there are also numerous business information networks, for example, with regard to the provision of company capital, but also for the purpose of technology transfer within the framework of cooperation between companies.

### **Evaluation**

Of all the countries examined in this book Sweden comes closest to the ideal-type of the coordinated market economy. The Swedish economy is characterised by the fact that employers and employees cooperate intensively in wage formation; both labour market actors are involved in the public provision of vocational training; and corporate financing comprises a mixture of house banks, enterprise cross-holdings and business information networks in the provision of company capital. These information networks for the purpose of technology transfer are also used in the establishment of cooperation between firms.

Sweden is remarkable because its coordinated economic system and strong welfare state have enabled it to combine high economic growth, a fair distribution of wealth and low unemployment. In comparison to the USA, Great Britain, Germany and Japan, then, Sweden corresponds most closely to the demands of social democracy.

*Close to the ideal-type of a coordinated market economy*

Sweden		
<b>GDP per capita 2008</b>	30,100 €	GDP per capita in terms of purchasing power standards (PPS); 1 PPS corresponds to the purchasing power of 1 euro (EU27 average) (source: Eurostat)
<b>Average economic growth 1990–2007</b>	2.3 %	Average annual economic growth per capita at constant prices (source: Human Development Index 2009, p. 195)
<b>National debt 2008</b>	38.0 %	National debt as a percentage of GDP (source: Bundesministerium für Finanzen, Monatsbericht 12/2009, p. 99)
<b>Current account balance</b>	7.8 %	Balance of all exports and imports of goods as a percentage of GDP (source: International Monetary Fund: World Economic Outlook 10/2009, p. 187)
<b>Employment rate 2008</b>	74.3 % (71.8 %)	Proportion of persons of working age (figure for women given in brackets) aged 15–64 out of the whole population (source: Eurostat)
<b>Unemployment rate 2008</b>	6.2 %	Proportion of unemployed persons in the working age population (source: Eurostat)
<b>Income inequality in terms of the Gini coefficient</b>	25 %	Ratio indicating the unequal distribution of income; 100 % = maximum inequality (source: Human Development Report 2009, p. 195)
<b>Women's incomes in comparison to men's incomes</b>	67 %	Percentage of women's incomes in comparison to those of men (source: Human Development Index 2009, p. 186)
<b>Poverty Index 2009</b>	6.0 %	The Poverty Index is composed of various indicators (including life expectancy, literacy rate and access to health care); 0 = minimum poverty, 100 = maximum poverty (source: Human Development Report 2009, p. 180)
<b>Unionisation rate 2007</b>	70.8 %	Proportion of the working age population organised in trade unions (source: OECD)

## 7. ECONOMIC POLICIES: PRACTICAL EXAMPLES

Social psychologist Kurt Lewin is supposed to have remarked that »nothing is as practical [in the sense of ›handy‹] as a good theory«. In order to clarify the practical relevance of theories presented in the foregoing chapters to issues of economics and social democracy practical instances have been referred to throughout.

In this concluding chapter these references are supplemented by practical examples from a number of controversial policy fields. The idea is to make clear how the core values of social democracy are reflected in everyday economic policy and how their economic policy principles can be brought to bear.

In this series of readers there is no separate volume on labour market policy since for social democracy this is a key policy area and so addressed in every volume. Admittedly, labour market policy has particular importance in the present volume on »the economy and social democracy«. For this purpose two practical examples are presented, »decent work« and »minimum wages«.

The contributions presented here encompass a wide variety of authors with different points of view. The examples cannot provide conclusive answers to constantly changing circumstances, but rather constitute an attempt to present ideas and make the reader think.

### **In this chapter the practical examples address:**

- environmental industrial policy: how lead markets can be established, with government help, which promote innovation, growth and employment;
- the state budget: the circumstances under which government borrowing makes sense with regard to investment policy;
- privatisation: its advantages, how it should be organised in policy terms and in what cases it should be avoided;
- decent work and codetermination: they are interwoven and matters of key concern for social democracy;
- minimum wages: necessary to curb precarious employment, but also in response to gender issues.

## 7.1. Environmental Industrial Policy: Growth Policy for a Sustainable Future<sup>14</sup>

*Peter Franz, Florian Mayer and Stefan Tidow*

The environment will be a key driver in twenty-first century economies. Demand for energy and raw materials has grown enormously in recent years and this will continue. Over the next four decades the number of people on Earth will increase from its current six billion to around nine billion. The number of those living in industrialised societies will triple over the same period to around four billion people. As a consequence, the demand for industrially manufactured consumer products will increase enormously. According to estimates, in Brazil, Russia, India and China (the so-called BRIC countries) alone over the coming three years the size of the middle class, which both has money to spend and is eager to spend it, will double. However, the raw materials of our planet are just as limited as the areas which can be built on or cultivated. Air and water are precious resources. Energy, too, is far from inexhaustible – certainly that obtained from conventional sources, which still accounts for the bulk of the energy we use.

In short, economic and environmental challenges are becoming ever more closely intertwined. The time is over when the environment and the economy could still be regarded as entirely distinct. What the environment dictates will increasingly become economically necessary and not only from a national economic standpoint but also at the enterprise level. For example, Sir Nicholas Stern, former Chief Economist of the World Bank, estimates the economic costs of unchecked climate change at up to 20 per cent of global GDP.

This change in the relationship between the economy and the environment has direct consequences for politics. Exaggerating only a little, one might say that environmental policy is increasingly becoming economic policy. The strategy of environmental industrial policy takes account of this development and draws the consequence that energy and resources have become a key economic, environmental and social issue, both at national and global level.

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<sup>14</sup> Further information on the close links between the environment and the economy can be found in the Green Economy Report first published in 2009 by the German Ministry of the Environment and the Federal Environment Agency: [www.umweltwirtschaftsbericht.de](http://www.umweltwirtschaftsbericht.de)

► Sustainable growth policy is becoming part of the innovation, growth and employment agenda

Environmental industrial policy links an economic-environmental modernisation strategy for more sustainability with an environmental-economic specialisation strategy. This is no mere ideological answer to the challenges of our time, but rather marks out a pragmatic and target-oriented path.

Basically, it concerns two things. First, we have to restructure the economy on a sustainable basis. This is a matter of the structures of production and revolves around energy and resource efficiency. This includes not only more efficient use, but a changeover to renewable raw materials. Not only can fuel be produced from biomass, but also plastic and modern materials. Needless to say, in terms of energy policy it also involves making better use of renewable energy sources, such as sun, wind, water, geothermal energy and biomass and fully exploiting its potential. Long term, there is simply no alternative. Only in this way will we be able to break out of the structural dilemma of limited raw materials and increasing demand and to decouple growth from resource consumption. However, the purpose of environmental industrial policy is not confined to this changeover, but – second – concerns the optimal use of the opportunities made available in this way for the economy. The very fact that throughout the world energy is becoming more expensive and raw materials scarcer endows green technologies with enormous potential, making them really and truly the lead market of the future. Efficient technologies and environmental technologies are becoming key technologies.

Management consultants estimate that the global market for environmental technology is already worth around 1,000 billion euros. By 2020, according to prognoses, that will have more than doubled, to 2,000 billion euros. Germany is already the principal global exporter of environmental goods and global market leader in many areas of technology. This stands the country in good stead to profit from green markets in the future, assuming it manages to remain at the technological cutting edge. However, as experience shows, that is largely dependent on the pursuit of an ambitious environmental policy which is becoming a driver of modernisation by imposing stiff requirements on production processes and products.

Environmental industrial policy will also lead to a closer intermeshing of these two dimensions. For that purpose the state must formulate demanding goals

and establish the right framework, functioning as a pioneer and pointing the way forward, but also leading the way when necessary. Although the market is increasingly responding to the changed realities, it is still too slow in many instances. So far, it has failed to anticipate both the challenges and the opportunities satisfactorily. And if we take seriously what science is telling us about climate change we have only a few years in which to carry out the momentous change of course that is so necessary. Too little time, certainly, to waste on inconsequential debates about regulation and general principles. What is needed is a pragmatic mix of different policy instruments and approaches and the intelligent intermeshing of environmental and innovation policy within the framework of state and market failure. To that end, governments must utilise a wide variety of policy and economic instruments in such a way that innovations are initiated, eco-efficient technologies are applied, impetus is given to an energy- and resource-efficient restructuring of both economy and society and, at the same time, growth and employment are stimulated.

### ► Principles of environmental industrial policy

Characteristic of the environmental industrial policy approach is its combination of a variety of aspects:

1. Demand- and supply-side instruments must be intelligently combined. Frequently, demand- and supply-oriented policies are presented as irreconcilable opposites. However, innovation research shows that the best way of nurturing and bringing to the market innovative technologies is to ensure the interaction of a good supply-policy framework and activating demand. But this only occurs if policy takes account of both the supply and the demand sides.
2. Calculable framework conditions are just as important as ambitious targets. Companies must know where they stand. For that reason policy must not be arbitrary. However, planning certainty should not lead companies to rest on their laurels or to fail to take up the »challenge of the future«. Competitors never sleep. The rising Asian economies in particular are crowding into world markets. Ambitious goals which are long term and predictable are an important component of a policy which balances plannability and dynamism. Another example is the so-called »top runner« approach which orients itself towards the state-of-the-art technology. Companies can only be asked, therefore, to do what is practicable and realisable – but complacency is not an option.

3. Prices must »tell the truth« without undermining competitiveness. Prices are important measures of scarcity which should no longer blind us to the environmental truth. The internalisation of external costs and functioning markets are crucial pivots of an environmental industrial policy. Factoring in the »true costs« remains difficult in practice, for example, through the failure to take them into consideration in international competition or the difficulty involved in calculating costs that will only arise in the future.

4. Research must not be technology-specific and, at the same time, deliberately foster progress and lay down beacons. No one can know today which technologies will win out in the future. This is why policy must avoid being technology-specific and not put all its eggs in one basket. A policy of »technology forcing« sets ambitious targets but does not provide strategies for finding technological solutions to reach these targets. On the other hand, there are particular lines of technology which the market alone does not develop but which promise much in terms of problem-solving potential. Government research and technology policy must also take these into account by instigating experimental pilot projects and lighthouse projects with symbolic power.

5. Horizontal approaches and sectoral policies must complement one another. The framework must be established in such a way that it sets the entire economy on a course of environmental innovation. This is not merely a question of environmental policy regulation but also of competition, taxation and economic policy. This also requires efficient, modern and environmentally-friendly infrastructure and well qualified workers. This horizontal dimension is crucial. But there will always be areas in which structural change must be accelerated on a sectoral basis. This involves fostering key technologies and industries in a targeted fashion, because otherwise it will not be possible to break out of decrepit and entrenched market structures or ensure that long-term strategic interests play a role in international competition; furthermore, technological leaps forward cannot be produced solely by means of careful management of framework conditions.

A resource-oriented restructuring of industrial society needs not only innovative entrepreneurs and a pioneering state. It also needs workers with decent jobs and who »do a good job«, as well as active consumers who set in motion significant modernisation impulses »from the bottom up« by means of their demand. Finally, what is needed is no less than a »New Deal« for all those concerned in

order to meet the challenges of a world in transformation and to pursue an environmental-economic modernisation strategy.

The political and economic arena has changed considerably. It is clear that economy and environment are more interlinked than ever and that a Germany that wishes to establish itself as a sustainable business location needs environmentally- and socially-friendly industrial production with sustainable products and services, well qualified workers and good training. Environmental industrial policy will set the course in this direction.

## 7.2. Budget Policy: What We Owe Germany

*Michael Dauderstädt<sup>15</sup>*

Germany's national debt is currently running at over 1.5 billion euros. Servicing it will devour a considerable portion of tax revenues or require going further into debt. Allegedly, it imposes a burden on future generations who will have to pay down these debts. The so-called »debt brake« has been put forward as a way of stopping this increase in the national debt in its tracks. This idea chimes with the basic outlook underlying the European Stability and Growth Pact, which also assumes that long term – that is, over the economic cycle – there should not be significant new debt. However, a smart finance policy should also include, besides paying down the debt, the option of an active economic policy aimed at renovation and investment. It should not impede it.

Politically and economically, two dimensions of the national debt should be distinguished: the deficit arising as a consequence of economic factors and long-term debt incurred in the financing of growth-promoting investment. For most economists, both dimensions are essential, although their extent is controversial.

### ➤ Growth through Debt?

In economic downturns state revenues contract, while spending – in particular, on unemployment benefit – increases. The deficit which, as a result, arises from this, stabilises demand which would otherwise fall. Most modern approaches to

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<sup>15</sup> This is an abridged version of the August 2007 WISODirekt publication »Was wir Deutschland schulden« (What we owe Germany) revised in light of the financial market crisis of 2008

consolidation consider these automatic stabilisers to be very useful. In Germany, the 1967 law on stability and growth envisages such an anti-cyclical budgetary policy, although in the event a pro-cyclical policy was implemented.<sup>16</sup> In recessions, finance policy has often reacted to the growing deficit with panic austerity measures, which served only to deepen and prolong the suffering. In economic upturns, by contrast, no consolidation efforts were made, as a result of which total indebtedness increased.

An active economic policy should manage public spending in such a way that it has an anti-cyclical effect. Ideally, spending would be increased in a recession, even if the deficit and the national debt grow, in order to compensate for weaker private sector demand. From a cyclical standpoint it does not matter whether this involves state investment or consumption, although the growth effect is more sustainable in the case of investment. In boom periods, spending should be reduced in order to counteract overheating and to consolidate the budget.

In Germany, before the introduction of the debt brake, the Constitution laid down that government borrowing should be used solely to finance investment. This expressed the view that the burden of financing spending whose benefits would be spread out over a long period should not be imposed in a single budgetary year. More broadly, what benefits future generations should not be financed solely by the current population. This transfers to the state budget the logic of a private household or a company, which incur debt in order to finance investment, yield future earnings or reduce costs (for example, building or purchasing a house which brings in future rental income or saves rental costs).

In the case of states, however, this logic is more complex. What increases its future revenues or reduces its spending? Ultimately, all measures which increase growth contribute to revenue increases. This includes much more than what is covered by the notion of »capital investment«. Expenditure to avoid future spending should count as investment (for example, immunisation programmes).

But in what circumstances does borrowing make sense? All growth processes are credit- and thus debt-financed, if not by the state, then by the private sector. Current income only suffices to purchase current production. Additional production

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<sup>16</sup> At least, this is the damning verdict of Solow/Wyplosz (2007).

requires borrowing to finance the necessary additional investment the proceeds of which, ideally – in other words, without hoarding or saving on the part of the drawer of income – then make possible the sale of the additional production. If households and companies – for example, due to pessimism induced by a recession – do not borrow the need for growth dictates that the state step into the breach. Conversely, during periods of expansionary optimism – like the one in the USA up until 2007 – lending can exceed possible growth in the real economy.

In this system monetary policy is tasked with restricting borrowing to realistic levels. Excessive debt – regardless of whether it is incurred by the state, companies or households – leads to asset price bubbles or inflationary demand which does not bring forth real volume growth but predominantly price increases in the face of stagnant supply.

#### ► How much debt is too much?

But how high should the debt mountain be? Many periods of growth, not least the most recent one experienced by the world economy, end in debt crises, although it is usually not states but overshooting financial markets which are involved. It was not always obvious whether asset prices, which generally increased in tandem – real estate, shares and so on – arose from realistic yield expectations or speculative exuberance. Ultimately, the real economy, through its productivity gains and idle factors of production, determines how much room to manoeuvre is left in the system. Inflation and the balance of payments are important indicators in this respect. People are generally wise after the event (for example, the Asian Crisis of 1997, the dot.com bubble in 2000 and the financial crisis in autumn 2008), but who would choke off a lovely boom which creates jobs and incomes only because prices are rising a bit and the balance of payments is in the red?

Regardless of the extent of current net borrowing, whether for reasons of economic stimulus or to finance public investment, many are disturbed by the absolute size of the accumulated debt. This restricts the state's room to manoeuvre since it has to spend a considerable portion of its revenues on debt servicing, which can swell up painfully with rising interest rates. Public debt represents, on top of that, a redistribution in favour of capital owners who have lend money to the state and whose interest income is paid out of the taxes predominantly levied on wage earners. Finally – to cite the argument brought forward most frequently – it imposes a burden on our children, the future generations.

### ➤ A poor future versus a rich present?

But does this indebtedness really harm future generations? Although often rolled out, this thesis is too sweeping. The next generation inherits the claims as well as the debts. Public debt does not affect the total sharing of the burden between the generations, but rather its distribution within the next generation. Set against all the taxpayers who will be responsible for paying down the debt are the creditors, in other words, those who have lent the state money.

The extent of the burden that the state and the taxpayers will have to bear over the long term as a result of a particular level of indebtedness essentially depends on the relationship between interest rates and nominal growth. If the economy grows more quickly than the interest rate the relative weight of public debt – as a proportion of GDP – will fall. Such periods of relief were the rule in the long growth phase between 1950 and 1975, but their frequency has since diminished. However, this circumstance also shows that a policy of high interest rates primarily benefits capital owners. High interest rates increase or stabilise at least the relative value of their claims.

If the current generation wants to do something for the prosperity of the next it should not accumulate financial asset claims whose real returns must be generated by the next generation for the inheritors of the claims. It should rather take measures which increase the next generation's productivity. This includes investment in infrastructure and education, research and development. If non-consumption is expedient it should be in the form of resource preservation since rising resource costs – including, for example, flood protection – reduce productivity. If – in particular against the background of unequal distribution – richer households save, but without real investment being made, this can lead to dangerous, unsustainable asset bubbles.

As a country Germany cannot pass on prosperity to the future within its own economy by piling up claims – assets – any more than it can shift poverty into the future by piling up debts. This is possible only if debts are incurred abroad or claims are amassed vis-à-vis foreign countries. Foreign debts may railroad us into having in future to export more than we import in order to service creditors. Foreign claims, such as Germany has build up in recent years, can go up in smoke or be marked down strongly in a financial market crisis, as many investors learned to their cost in 2008. But in Germany export surpluses are regarded not as a burden but as an aim (also of economic policy).

### ► Public thrift but private exuberance?

In all of this ultimately it makes no difference whether the debts belong to the government or companies and households. Although only public debt counts as a burden (or a vice) in Germany the accumulation of private debts – primarily by companies – is regarded as a virtue. In this way, the next generation inherits not only 1.5 trillion euros in low risk public debt, but also 2.5 trillion euros of potentially insecure corporate debt.

The fact that private debts were long regarded as less problematic contributed not least to the wave of privatisations of formerly public sectors such as the post, telecommunications, the railways and motorways. Their borrowing is now regarded not as alarming public debt but as welcome private investment. In this respect, too, redistribution will take place only within the next generation. But this time it is not the taxpayers who must pay the interest on public debt but consumers and – it must be repeated – employees who are supposed to increase profitability through prices (for example, rent) and wage restraint. But even for the private sector real prosperity consists of rising real productivity.

We therefore owe Germany the courage to incur the debts necessary for long-term sustainable growth. This is served by investment in tangible assets, health, education, research and human capital. The much-praised accumulation of foreign claims by means of export surpluses or against future generations of Germans by means of funded »provisions« is only worth what future generations both at home and abroad are able to obtain due to investment today. Apart from »unsocial« redistribution to the benefit of investors their yield cannot be higher than the growth rates of the national economy itself.

## 7.3. Risks and Opportunities of Privatisation

Simon Vaut

The privatisation of public property is a controversial economic policy issue which revolves around the question of the relationship between the state and the private economy. The heated debate on the privatisation of German Railways illustrates clearly that much more is at issue than individual political decisions, including fundamental ideas about public welfare, so-called »services of general interest« and the tasks of the state. The fact that opinions for and against rail privatisation cut right across the SPD suggests that there are no simple answers to the question of the relationship between the private economy and the state for Social Democrats but rather that complex consideration is required.

A detailed presentation of privatisations worldwide has been undertaken in an investigation headed by academic and politician Ernst Ulrich von Weizsäcker of the Club of Rome<sup>17</sup> in the book *Limits of Privatisation*. The following remarks are based mainly on this report.

The Club of Rome argues in its report against the extreme positions of an uncritical pro-privatisation ideology, on the one hand, and an uncritical trust in the state, which would like to see as much as possible in public ownership, on the other. A subtler middle way which, in accordance with the needs of a given sector, relies on private actors, public-private partnerships or state provision, however, is fraught with caveats. Various forms of privatisation and actor constellations are possible:

- State-owned companies are in competition with private companies, but remain in public ownership: for example, Deutsche Bahn, which was a public limited company in federal ownership from 1994 until its part privatisation, is increasingly exposed to competition with other providers.
- Outsourcing of tasks: this means that the state hands over certain tasks to private providers and buys them in. The Federal Printing Office is one example of this. However, it was bought back from private operation after a few years on security grounds.

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<sup>17</sup> The Club of Rome is an international organisation of scientists and scholars concerned with social and economic issues. The Club of Rome came to prominence with the publication in 1972 of the study »The Limits of Growth«, in which it put population growth, environmental pollution and the depletion of raw materials reserves onto the agenda. It had a decisive influence on the environmental movement.

- Public-private partnerships (PPP): cooperative solutions by means of which state and private actors work together.
- Full privatisation: complete disposal of public assets so that the state can henceforth have only a regulatory influence on market developments.

The relationship between state governance and economic freedom, between security and innovation must be constantly reassessed. General conditions can change over time: the privatisation and liberalisation of the telecommunications sector continues to be regarded as a positive instance of privatisation. Prices have fallen sharply as a result of privatisation, innovation in the sector has increased and the proceeds of privatisation have put money into the public coffers. This development was conditional on different providers being able to offer their services on the existing telephone network, which became technically possible only at the end of the twentieth century. Previously, privatisation would not have led to more competition, because a state monopoly would merely have been replaced by a private monopoly.

The pendulum swings back and forth between state and private over time. In the nineteenth and twentieth centuries states increasingly took responsibility and the public spending ratio increased significantly almost everywhere. Everything from telecommunications through energy generation to branches of industry, such as steel production and car manufacturing, were in public ownership in the past, which have now been partly or wholly privatised. In the past quarter-century the pendulum has swung decisively in the direction of the private economy.

But what were the precursors of this development? At the international level, the World Bank and the International Monetary Fund (IMF), within the framework of the so-called Washington Consensus, played a major role. Its economic policy guidelines called for the rolling back of the state and led to a global wave of deregulation and privatisation. According to Nobel Prize winner and former World Bank Chief Economist Joseph Stiglitz (Stiglitz 2002: 78–81), if in the 1980s and 1990s someone had taught a parrot to say »privatisation« the advice of the World Bank and the IMF would have been largely superfluous. The problem with the Washington Consensus, according to Stiglitz, was that it regarded privatisation as an end in itself instead of examining in detail which sectors were suitable

for it and under what circumstances and what constellations of actors would be needed in order to attain more sustainable growth and fairer distribution and provision. The effects of privatisation depend on the economic sector in which it is implemented and the prevailing conditions: privatisation can therefore succeed in one country, but fail in another in the same sector.

The following factors are particularly important for the outcome of privatisation:

- Is competition feasible in the sector or would the state monopoly merely be substituted by a private one? Especially in so-called network industries this is only partly possible; for example, in rail traffic on a given line possible competition is severely constrained. It is simply unprofitable to construct railway lines side by side and trains can hardly overtake one another on the same track. Other network industries include performance-based providers, such as water, gas and electricity. If privatisation is implemented, providers must be regulated in such a way that they cannot abuse their market power.
- Is there a danger that some consumers will be excluded from important goods and services? For example, people in remote areas might be denied a postal service or people who find it hard to make ends meet might be cut off from the electricity grid.
- Does the state have a particular security interest? The German Federal Printing Office was taken back into public ownership after full privatisation because the documents it produced and the data it managed were considered too sensitive.

The results of privatisation and nationalisation are mixed. They depend heavily on the sector concerned and policy design. In the report »The Limits of Privatisation« case studies of privatisations in Germany and other countries are studied and evaluated. There is a wide spectrum of positive and negative results. In what follows we shall first present the established positive effects, and then the risks of privatisation, based on the analysis of the Club of Rome.

When privatisation brings it about that competition arises in a sector, as a rule that leads to an enhanced customer orientation. Private companies in competi-

tion with one another depend on satisfied customers and have to be innovative and efficient to remain in the market. Telecommunications exemplifies a sector in which competition between private companies has led to innovation and market expansion, which would be inconceivable for a state monopoly. State-owned companies which do not find themselves in a competitive situation tend to operate more cost-intensively and are less open to innovation. Cost reductions and better quality service, however, are not inevitable. Private companies tend to ignore customers from whom they cannot make a profit: in other words, they incline towards »cherry-picking«. Examples of this are people living in remote areas to whom postal delivery is not cost-effective.

Privatisation makes sense if the state lacks the resources for investment and private (international) investors are willing to make capital available. This is frequently the case in poorer countries where services of general interest – such as water supply – are sometimes given to private investors. Provision tends to improve, however, only for those able to pay and thus can exacerbate inequalities.

A problem frequently encountered with privatisation is weak investment rules: under pressure of circumstances a state inexperienced in privatisation can end up with sales conditions which are to its own detriment. Faced with experienced international concerns former communist countries in particular were frequently led into unrealistic price and quality provisions. Thus in the transforming states of Central and Eastern Europe, for example, energy companies were sold well below their value.

We have already mentioned the problems that can ensue when inadequate competition prevails and private monopolies form, for example, in the case of network industries – water supply, electricity grid – where no alternative is feasible. This leads neither to innovation nor price benefits. Private monopolies are generally more disadvantageous than state monopolies.

Another danger is the displacement of risks and external costs. After sale to a private investor it can happen that revenue risks are shifted onto the state. This happens, for example, when external operating costs, such as environmental effects, are imposed on the state, while the profits remain in private hands. One example of this is the operating costs of atomic energy.

Another potential problem with private investors is their neglect of the long term and disregard for sustained quality which in some instances has led to the decline of infrastructure previously maintained by public means. A familiar example is the British railway system. After privatisation, investors neglected the rail network, resulting in serious accidents. The network had to be re-nationalised.

Often privatisation is implemented primarily for fiscal reasons: the revenues are to be used to take care of budgetary shortfalls. This can have a positive effect in other policy areas. The city of Dresden, for example, sold its housing stock of 100,000 dwellings and as a result is the only large German city which is debt-free. The 80 million euros annual saving which previously had to be raised to meet interest payments can be invested – minus the difference between rents and maintenance costs – in other areas, such as education.

The Club of Rome provides a checklist for privatisation. First, the reasons for privatisation should be publicly debated in order to ensure that privatisation is not implemented merely as an end in itself.

- There should be a robust regulatory framework with clear targets for investors.
- Privatisation should not be implemented on ideological grounds in relation to services that the state could just as well provide.
- There should be democratic control by means of supervisory authorities.
- Where the state is no longer an owner it should exercise influence on the market via regulation.
- Public goods and services of general interest should be subject to particular safeguards: privatisation of these goods must be carried out with special care.
- There should be a social charter for the vulnerable: this is exemplified by the city of Dresden which linked the sale of its housing stock to special protective rights for tenants.
- Privatisation announcements should be transparent and fair.
- It should be examined whether a third way, between public and private, might be possible in the form of public-private partnerships or cooperatives.

## 7.4. Decent Work and Codetermination: The Policy of Decent Work

*Wolfgang Schroeder*

Every society has its own understanding of work. There are also diverse views about work, including what counts as decent work. How is work organised today? What will work be like in the future? What is the significance of work in our lives and for social cohesion? Is polarisation in terms of precarious<sup>18</sup> employment with low pay and frustrating working conditions, on the one hand, and well paid and satisfying work situations, on the other, a passing phenomenon? Or are we witnessing the advent of a malignant development? These are pressing concerns. Unless they are addressed both individual and societal plans for the future cannot be developed. The voices of those preaching the doctrine of the »end of work« are becoming fainter. They argued that modern society was outgrowing gainful employment and that full employment was no longer an option. This idea can be refuted on the basis, for example, of the Scandinavian countries which combine a high employment rate and high social standards. In Germany, too, after years of stagnation it has been possible to reduce unemployment. At the same time, however, worries are widespread about a »flexibilised hyper working society«. Even if productivity gains mean that today less labour is needed to produce a much larger GNP than, for example, 40 years ago, this is only one aspect of the debate on the transformation of work.

### ➤ Changes in Work Organisation

Even if the organisation of gainful employment is the subject of broad public debate only during particular phases and in certain situations it nevertheless defines the daily routine of employees. Industrial work was closely interwoven with work on production lines or work at the mercy of machines. Although so-called Taylorist work organisation, which was characterised by machines, control and standards – in other words, by the »scientific« planning of work – did not affect everyone, it not only exerted a decisive effect on society as a whole, but also on life after work. Also, the history of the labour movement, in particular trade unions, cannot be understood without taking account of Taylorist work organisation and large concerns.

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18 »Precarious« comes from the Latin *precarius*, meaning »obtained through entreaty or prayer« (hence dependent on another's will) or »insecure«

From the 1980s Taylorism was joined by a second innovative production model, known as »Toyotism«.<sup>19</sup> This production model – named after the at that time new form of work organisation based on team work practised at car manufacturer Toyota – had the aim, among other things, of overcoming the disadvantages associated with a rigid division of labour and facilitating the tighter integration of workers with more extensive skills. One aspect of this, which chimed with one of the main objectives of trade union management policy, was the humanising of work: linked to this were improved working conditions combining quality of work and life, preserving health and boosting social wealth.

Car factories were the main centres of innovation in terms of work organisation. One major impulse was given by new forms of team work in the Swedish Volvo factories. The development of new forms of autonomous or partly autonomous team work at the beginning of the 1980s and new ideas about production were closely linked to this key industry. Partly autonomous team work brought together hopes of a more varied, more interesting and more demanding – in terms of the skills utilised – work situation in which employees would have more scope for individually shaping their work quota and participating in the relevant decision-making. It seemed that team work would come to symbolise the new world of work and that the individual would gain a new status in cooperative groups.

To the extent that standardised assembly-line work – Taylorism – reached its limits a debate commenced on how working conditions might be improved. In the development towards partly autonomous team work this converged with the model of »decent work«. By international comparison, in Germany this process was quite widely diffused, leading many to talk of a German »special path« whose qualitative dimension was based on the foundations of skilled work and dual vocational training developed in Taylorism. In this way, a certain harmony was achieved between humanisation and rationalisation, which in turn constitutes a

**Taylorism** goes back to Frederick Taylor (1856–1915). His goal was to organise work as efficiently as possible. In his view, workers operate on the same principles as machines and he tried to structure work processes in terms of mechanistic assembly-line production.

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<sup>19</sup> Named after the production model of the car maker Toyota, which tried to combine the productivity characteristic of mass production with the quality characteristic of workshop production.

productive basis for the project of flexible specialisation in export-oriented industries. Since the mid-1990s, however, the future of this specific form of industrial work has come into doubt because economic and financial constraints, on the one hand, and contradictory developments in team work, on the other hand, have called its efficiency and acceptance into question.

Disillusionment has set in. Team work has expanded, but the expectations it generated with regard to a far-reaching humanisation of the world of work have not been realised. On the contrary, opportunities for employees to organise their own work have once again been reduced in many areas in favour of more standardisation. Consequently, different work regimes are competing with one another in industry today to achieve the highest productivity.

With the waning of large-scale industrial production another type of work is increasingly taking centre-stage in the public debate: flexible, knowledge-oriented work in services. It is often assumed that individuals in this area have more autonomy. It is true that they do not work in large workplaces, but in small ones and are much more responsible for the results of their work. However, this kind of work goes hand in hand with the demise of established working time practices. And instead of working time being reduced people talk of »work without end«. For example, in the age of e-mail and mobile telephones many employees are expected to be constantly available outside working hours, even in contravention of the law. In the debate on the risks and opportunities characteristic of this development workers' qualifications play a decisive role when independence comes into question. On the risk side, the focus is on new forms of stress, burn-out syndrome (mental exhaustion due to work), the all-embracing demands imposed by work and the resulting contradictions in terms of quality of life improvements.

In recent years there has been much discussion about whether a new type of worker has come into being who, as »entrepolyee« (see below) is also responsible for his own employability. This highlights a process of development leading from the proletarian wage labourer through the vocational employee to the »entrepreneurialised entrepolyee«. The characteristics of these »entrepolyees«, who under market-like conditions to some extent organise their own work in accordance with the specific needs of the company, are defined in terms of three dimensions in particular: (i) individualised qualifications, (ii) systematic

self-control with regard to work and (iii) the danger of self-exploitation under precarious conditions with regard to social security. Since the »entreployee« is a social construct that corresponds to a new stage in the development of the market-based economy the sociologists Voß and Pongratz – who coined this expression – describe a new set of power relations within companies: »The contradiction between capital and labour in capitalist enterprises does not disappear with the type of the entreployee, but is transformed into a structural contradiction between entrepreneurs of different kinds« (Voß/Pongratz 2003: 32). Even if, as critics have rightly objected, this type is by no means dominant in the world of work the characteristics identified here are already widespread.

The biggest challenge for a »decent work« policy at present is the greatly increasing number of precarious employees. Particularly problematic in this respect is the fact that it is becoming more and more difficult to get out of this mode of employment. For social democracy decent work is important primarily in two respects for the individuals concerned. First, low quality work must be humanised. Second, those who work under such circumstances must be helped to get out of them again in order to develop themselves.

#### ➤ Codetermination: Actors and Procedures

With the declining significance of industrial work new demands are being imposed on those involved in promoting the policy of decent work. Alongside employers' and employees' organisations and the state, enterprise-level actors constitute the third pillar of the German mode of a negotiated policy of decent work. Their bargaining concerned central issues related to working conditions into the 1980s within the framework of standards negotiated industry-wide or implemented by the state. To that extent, a social system formed at enterprise level in Germany oriented towards industry-level regulation but without following it slavishly. The German model permits a wide range of different practices and forms of exchange at enterprise level. To be sure, they are subject to particular framework conditions. For example, the management has to take into account the interests of the staff and the works council on personnel policy questions, as well as the guidelines of industry-wide bodies, such as the provisions of collective agreements and government regulation. On the other hand, the works council has to combine its activities as representative of the employees' interests with a responsibility for company productivity and results. The model of

enterprise codetermination and cooperation is succinctly expressed in the Works Constitution Act: »The employer and the works council shall work together in a spirit of mutual trust having regard to the applicable collective agreements and in co-operation with the trade unions and employers' associations represented in the establishment for the good of the employees and of the establishment« (§2 section 1 Works Constitution Act).

The model of interest representation in Germany formally separates works councils and trade unions. Works council members do not have to be members of a trade union and trade unions do not have a direct and automatic influence on works councils. Given this formal separation it is one of the greatest achievements of the German model that an insurmountable rivalry has not developed between works councils and trade unions but rather day-to-day cooperation. For six decades, more than 70 per cent of all works council members are also trade union members and do outstanding voluntary work in trade unions. While the works council operates as a »border« institution (Fürstenberg 2000 [1958]), between the workforce, the management and the trade union, the workplace management has to perform a delicate balancing act in relation to the workforce, the works council and the decisive interests and requirements of central management and the employers' association. Clashes of interest between works council and management are dealt with on the basis of established procedures. Open conflict is unusual. Where distributional or organisational disputes do arise external actors are often involved. Works council and management are the most important ground-level actors in the arena assigned to them. They have a different legal basis and their power resources are usually unequal, so that industrial relations are generally not characterised by encounters between actors of equal strength. Workplace actors do not have discretionary rights with regard to collective bargaining, which instead lie at industry level, complying with an institutional pattern which has developed over time and which, to date, has fostered a mode of cooperation whose most important components can be categorised primarily as political and economic, respectively.

### ➤ Challenges for Codetermination

The model of the division of labour based on workplace codetermination via works councils, partial involvement in economic decision-making through employees' workplace representatives and also full-time trade unionists in supervisory boards is currently facing new challenges.

**1. The forces binding together the actors of codetermination are dis-integrating.** The acceptance of the industry-wide level of decision-making in labour policy matters by the workplace level by no means goes without saying, but instead is the expression of ways of doing things that have developed over time and of the current political balance of power. The fact is that where managements see an opportunity to go their own way with regard to collective bargaining without jeopardising peace in the workplace or productivity they will sometimes try it. In recent years, indeed, this has been happening more and more frequently. For Social Democrats it goes without saying that it is not the issue whether employees' participation is »beneficial« or not: rather it is a legally attested fundamental right which is not up for negotiation under any circumstances.

It is crucial for the legitimacy and acceptance of industry-wide policymaking that workplace actors can see that their views and interests are being taken into account at confederation level. As a rule, representative organisations are dependent on this if they are to achieve a high degree of loyalty and the ability to make and keep commitments with regard to their members. Tradition has been an important binding force shaping the political dimension of industrial relations. However, in the past 20 years this has suffered a precipitous decline. For decades in the majority of German workplaces there was a tried-and-tested division of tasks, never seriously called into question, passed down from generation to generation. These cultural-traditional binding forces between confederations and workplace actors seem to be losing influence: since the 1980s it has been observable that the power of confederations to set norms has been diminishing. Management and works councils are increasingly going their own way, publicly expressing their discontent with regard to the decisions of industry-wide organisations and refusing to comply.

**2. The works council is the contact partner and interest representative of all employees.** One major challenge is the joint representation of the interests of both core and peripheral employees: corporate employment structures have changed dramatically in recent years. The number of temporary workers, part-time workers and agency workers has increased enormously. This is a potential source of conflict in the workplace, confronting workplace codetermination with major problems concerning mediation and solidarity: the works council represents a constantly changing workforce, which sometimes gives rise

to extraordinary problems when it comes to representing the interests of poorly protected groups of employees with the same success as the regular workforce.

**3. The codetermination model is confronted by diverging forms of corporate responsibility.** When the Works Constitution Act (Betriebsverfassungsgesetz) came into force workplace decision-makers were also generally those taking the economic risk. Codetermination by the works council was restricted to workplace organisation and personnel issues. But it was usually also possible to discuss economic decisions and, in some instances, to ameliorate their effects. However, as a result of internationalisation and the separation of ownership and management, economic decision-making may be against the interests not only of the workforce, but even of the workplace, without workplace actors having the opportunity to exert any influence on these decisions as they are being made. It is sometimes possible for the works council to alleviate the effects of decision-making by negotiation, but the development and »financial market oriented control« of companies have presented the codetermination model with new problems.

**4. The internationalisation of companies requires the internationalisation of codetermination .** One of the principal arguments put forward to justify lowering the standard of working conditions is competition between business locations, and all too frequently between different units of the same company. For example, orders for new car models may be announced throughout the company and competition between workplaces instigated in order to bring about reductions in wage costs and employer's social contributions. However, the first displays of solidarity in such circumstances have occurred, for example, between different General Motors plants in Europe when the central management threatened to close individual European plants. European works councils represent the first important supranational institution, and their powers have already been seriously tested. Nevertheless, further improvements with regard to employees' rights are needed here in order to allow employees' representatives a say in decision-making on an equal footing. Another arena for codetermination made available by international provision is the European company (SE). Also in this respect strategies and ideas need to be developed to take advantage of the opportunities and minimise the risks. The logic is simple. In order to ensure codetermination rights enhanced European cooperation is needed, with the inclusion of a range of actors and levels. To the extent that this is done, the more satisfying the results will be.

## 7.5. The Debate on Minimum Wages

Claudia Weinkopf<sup>20</sup>

Is the growing significance of low wages a problem requiring political action or a necessary aspect of an effective strategy for reducing unemployment? This is a controversial issue in Germany. Although several studies in recent years have largely concurred that the extent of low wages in Germany is already considerable (see, for example, Schäfer 2003; Rhein/Gartner/Krug 2005; Goebel/Krause/Schupp 2005; Eichhorst et al. 2005) there continue to be demands for a further extension of low wage employment and even sporadic calls for the »introduction« of low wage jobs.<sup>21</sup>

Recently, the debate has shifted to consider the question of whether it is the (sole) task of the state to supplement low wages to ensure that they guarantee households subsistence or whether minimum thresholds are needed at the level of collective bargaining or on a statutory basis to ensure that wages cannot be forced further and further down. In what follows, the validity of some of the arguments frequently adduced pro and contra low or minimum wages is examined and a commentary provided from a gender perspective.

One argument frequently put forward in favour of low wage jobs is that they can provide a springboard to better paid employment. However, the results of a number of recent studies on this issue are sobering: so-called »upward mobility« from low paid jobs has decreased significantly in Germany in recent years (see Rhein/Gartner/Krug 2005). This is confirmed by an evaluation carried out by the Institut für Arbeit und Qualifikation (IAQ) of data from the Bundesagentur für

20 A virtually identical version of this section was published under the title »Die politische Debatte über Niedrig- und Mindestlöhne – aus der Gender-Perspektive kommentiert« (The political debate on low and minimum wages – with a commentary from a gender perspective) as part of the article »Niedrig und Mindestlöhne. Eine Analyse aus der Gender-Perspektive« (Low and minimum wages. An analysis from a gender perspective), in: Friederike Maier and Angela Fiedler (eds) (2008), *Verfestigte Schief lagen. Ökonomische Analysen zum Geschlechterverhältnis* (Entrenched problems. Economic analyses of gender relations), Berlin. We would like to thank the publisher Edition Sigma and the author for their permission to reproduce the text here.

21 Useful references are difficult to find in this connection. In most of the relevant publications demands for more low wage employment are hedged with qualifications to a greater or lesser extent. For example, there is talk of a need for greater wage dispersion, for the possibility of more competitive wages for low or unskilled labour, for the restoration of the so-called »Lohnabstandsgebot« (the principle that social security benefits must be significantly lower than wages) or for the closing of »gaps in service provision« in comparison to the USA. To give an example, the Annual Report 2006/2007 of the Council of Experts states: »In the service sector, many employment opportunities are opening up, as the experiences of other countries – for example, the USA – show. However, in the past numerous jobs have disappeared in the low paid service sector as a result of excessively high wage costs« (Sachverständigenrat 2006: 370).

Arbeit (BA), in which we examined the extent to which full-time employees who in 1998 received wages below the low wage threshold had succeeded by 2003 in moving on to higher paid employment (above the low wage threshold). On average, 34.4 per cent – in other words, one-third of those in gainful employment in 2003 – had managed this. The proportion of those who had been able to obtain a better paid job varied considerably in terms of type of employee: best performing were young people (under 25 years of age: 62.3 per cent), those with good qualifications (academic degree: 53.6 per cent) and men (50.4 per cent). Among women, however, only just over one-quarter had managed to escape from the low wage sector (27.1 per cent) (Bosch/Kalina 2007: 45).

The issue of low wage jobs is also extremely controversial from a social policy standpoint: while some argue that income from full-time work should be sufficient to ensure an independent livelihood and that poverty for someone with a full-time job is not acceptable, others point out that low wage employment does not necessarily lead to poverty. Another view is that low wage workers are predominantly persons seeking additional income (see, for example, Brenke/Eichhorst 2007). Both standpoints also imply that low wages for women do not matter so much. Among the advocates of minimum wages, too, the focus is on a male breadwinner who, despite working full time – and also overtime – does not earn enough to feed his family. In this view, the situation appears to be less serious for women: if so many women work part-time or take mini-jobs, surely – at least this is the widespread belief – they are working primarily for »pin money« and thus, despite the low wages, are not affected by poverty because they have a husband or partner who earns more.

Such views are correct to the extent that indeed not all low wage workers are affected by poverty because there may be several incomes in a given household, putting household income overall above the poverty threshold. In fact, unemployment or inactivity are the main causes of poverty, with low wages playing only a partial role. Having said that, the number of poor persons working in the low wage sector even at the end of the 1990s was 41 per cent, in comparison to the EU average of 37 per cent (Marlier/Ponthieux 2000). Furthermore, the insinuation that women on low wages generally enjoy the protection of a solvent household appears questionable: according to an analysis by Becker (2006a) – although it concerns only full-time employees – the rate of women on low wages living in households below the poverty threshold, at 19 per cent, is only a little

lower than in the case of men on low wages (22 per cent). Looking at the problem solely in terms of the household also leaves out of account that social security entitlements, such as for pensions or unemployment benefit, are related to the level of one's own income. It is also important to note that the support of a partner is not guaranteed to last forever. Unemployment, separation or divorce can change things overnight and permanently.

It is often argued against the introduction of a statutory minimum wage that low wages indicate low productivity and thus lower wage limits set by government would lead to job losses. In particular, the job opportunities of the low qualified would be seriously affected in this way. However, in Germany low wages by no means affect predominantly the low qualified. Around three-quarters of low wage workers in Germany have completed vocational training or even have an academic degree. The employment effects of minimum wages are also highly contentious. In the UK, large-scale job losses were expected by some with the introduction of the minimum wage in 1999, but in the event employment has increased significantly in recent years despite substantial increases in the minimum wage (Bosch/Weinkopf 2006a). In the USA, more than 650 economists (including five Nobel Prize winners) called for a substantial increase in the minimum wage there in 2006 (Economic Policy Institute 2006).

Such differences of opinion are still not really represented in the German economics community. The vast majority of German professors of economics take the view that minimum wages per se would have negative employment effects. For example, Wolfgang Franz, President of the Zentrum für Europäische Wirtschaftsforschung (ZEW), stated in a press release of 12 April 2005 that: »On no other issue is there so much agreement among economists as on the subject of the damaging effects of minimum wages« (cited in Schulten 2005: 190).

The Vereinigung der Bayerischen Wirtschaft (Bavarian Business Association) (2006: 7), with reference to experiences with statutory minimum wages in other countries, argued along similar lines: »There are no reports of positive effects on the labour market«. <sup>22</sup>

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22 It was also (falsely) asserted that the minimum wage in the UK and Ireland does not apply to »the low qualified« (Vereinigung der Bayerischen Wirtschaft 2006: 8). In fact, in the UK a somewhat lower minimum wage (the so-called »development rate«) can be paid for induction periods of up to six months while training is being given (see Bosch/Weinkopf 2006b: 36f). However, this by no means represents a general exception for the low qualified.

In fact, the employment effects of minimum wages have by no means been established in the literature and the available studies come to widely varying conclusions (see Bosch/Weinkopf 2006b). For example, the US Council of Economic Advisers (the US counterpart of the German *Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung* [Council of Economic Advisers]) stated in its annual report to the President in 1999: »The weight of evidence suggests that modest increases in the minimum wage have had little or no effect on employment« (cited in Schulten 2005: 198).

A report by Bofinger et al. (2006) states: »Since empirical studies do not present a uniform picture one cannot assume that minimum wages are in general harmful to employment. At least, this is the case as long as they are kept at a reasonable level.«

In our view, two other important arguments speak in favour of the introduction of a statutory minimum wage in Germany: the prevention of wage dumping, which in Germany is growing, and – closely linked to that – the increasing subsidisation of low incomes within the framework of social assistance. The rising share of low wages in Germany indicates that the collective bargaining system, which long protected minimum standards at branch level, no longer provides effective protection against low and very low wages. The binding effect of collective agreements is declining in both eastern and western Germany, but agreed wages are also sometimes very low (see Deutscher Bundestag 2004).

In 2006, according to our calculations, around 5.5 million workers earned less than 7.50 euros gross per hour, which is what the trade unions were at that time demanding for a statutory minimum wage. Just under two-thirds of them were women, making up 19.8 per cent of all women workers in Germany. About 1.9 million employees received less than five euros (Kalina/Weinkopf 2008). This represents about 33 per cent of the average hourly wage in Germany. The workers concerned therefore earn even less than is permissible in the USA, where the national minimum wage – which in any case is merely symbolic by international comparison – lies at around this level (and, furthermore, is soon to be increased significantly).

In the EU, 20 out of the 27 member states have a statutory minimum wage and the other countries have mechanisms which provide for much more binding col-

lective agreements than in Germany. Countries such as France, the Netherlands, the UK, Belgium, Luxembourg and Ireland had minimum wages in autumn 2007 ranging from around 8 euros to over 9 euros.

Even in the employers' camp, which traditionally – with the exception of the construction industry – has rejected state interference in wage setting, there are now demands for minimum standards to prevent wage dumping, which is on the increase. Particularly active in this respect are the associations from the commercial cleaning and temporary work sectors – in other words, two branches with very different proportions of women among the employees. The commercial cleaning sector was recently subsumed under the Posted Workers Act, which means that collective agreements are generally binding and also apply to foreign providers. Two of the three major employers' federations in the temporary work sector are demanding branch-wide minimum wage regulations in order to curtail increasing wage dumping and to ensure that foreign companies, which in future could enter the German market in a big way, are obliged to comply with minimum standards by being made subject to the Posted Workers Act (for more details, see Weinkopf 2006).

A further argument for a statutory minimum wage is related to financing the welfare state: companies in Germany have so far been able to depend on the state to take up the slack with regard to low wages, for example, through supplementary entitlements to so-called »basic jobseeker's allowance« (*Arbeitslosengeld II* – the basic benefit for the unemployed), if household needs cannot be met from members' incomes. In October 2006, according to the Federal Employment Agency, 20.9 per cent of all working-age people in need of assistance were employees entitled to supplementary benefit (1.117 million out of 5.339 million). The majority of those entitled to such »top-up« payments were employees liable for social insurance contributions (11.3 per cent of all those in need of assistance or 601,533 persons). A total of 440,055 persons (8.3 per cent of all those receiving basic social benefits) were even in full-time employment. The proportion of women among employed recipients of basic social benefits represented 48.4 per cent of those liable for social insurance contributions and 55.1 per cent of those in marginal employment (mini-jobs). According to a study by Becker (2006b) significantly more people are entitled to additional benefits but have not as yet made a claim. The introduction of a statutory minimum wage would not render state subsidisation of low incomes superfluous in every

instance since, besides low hourly wages, short-time working and household size also play a role, but it would undoubtedly significantly reduce the financial cost of such »combination wages« (*Kombilöhnen*) and prevent the burden arising due to wage cuts from being shifted onto the state.

It is often assumed that the recipients of basic social benefits in marginal employment (mini-jobs) »optimise« the combination of transfer payments and earned income: in other words, they make sure that what they earn does not go above the social contribution threshold (»stealth jobs« – see Grabowsky et al. 2006). However, this does not take into account that the increase in mini-jobs is also due to changed company personnel strategies; it cannot be assumed that employees take these jobs of their own free will. In commercial cleaning, for example, part-time and full-time jobs liable to social contributions are reserved primarily for supervisory staff (Hieming et al. 2005; Jaehrling/Weinkopf 2006). To that extent, it appears questionable whether this could be changed by altering the level of earned income permissible with regard to basic social benefits in favour of higher paid jobs, as Bofinger et al. (2006), for example, have proposed. Persons with low additional income (see IMK-WSI-Arbeitskreis Kombilohn 2007) would be substantially worse off, with women disproportionately affected.

All in all, we think that there is much to be said for the view that binding minimum standards are necessary with regard to wages. Among the different variants which could, in principle, be adopted, the introduction of a statutory minimum wage would be the best solution from a women's perspective because in that way a binding lower limit would be established for all areas of employment. Minimum wages laid down in collective agreements are not a viable alternative, but at best supplementary because the requisite conditions for a declaration that they are generally binding and for their inclusion in the Posted Workers Act exist only in a few branches. Typical low wage sectors with a high proportion of women tend not to be covered by collective agreements.

There is no denying that a statutory minimum wage alone would not automatically enable women to secure their livelihood independently. Even a wage of 7.50 euros an hour – or the 8.50 euros an hour currently demanded by the trade unions – is often not sufficient for that, especially because a considerable proportion of women in Germany are in part-time or mini-jobs.

## 8. CARRY ON THINKING

The *Social Democracy Readers* series provides a compass with which to explore the basic questions of social democracy and reference points in the various policy areas. But they are not intended to provide – nor could they – eternally valid answers. The path of social democracy – both as an idea and as political action – must be constantly scrutinised, adapted and reconsidered if it is to be pursued successfully.

This summary is also a continuation of that and thus amounts primarily to an invitation to carry on thinking about the issues presented: what would make a good social democratic economic policy and what challenges face social democracy in the twenty-first century?

At present, the main challenge of a social democratic economic policy concerns how to strike a new balance between state and market. The German Social Democratic Party's Hamburg Programme provides significant impetus in this respect:

*»For us, the market is a necessary instrument and superior to other forms of economic coordination. However, when left to regulate itself the market is both socially and environmentally blind. It is unable spontaneously to provide public goods in sufficient quantities. If the market is to be able to have a positive effect it requires regulation by a state able to impose sanctions, effective laws and fairer ways of setting prices.« (Hamburg Programme 2007: 17)*

Social democracy must develop itself constantly in the face of new challenges. If it keeps in mind what it really stands for and maintains a clear view of reality this will not be a problem.

This applies equally to a social democratic economic policy. The aim of this volume is to show that a distinct social democratic economic policy approach can be derived from the core values of social democracy, embodied in the UN covenants on fundamental rights. This represents a compass for a modern, value-oriented economic policy based on the principles of growth, social equality and sustainability.

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**Further Reading:**  
*The website of the Akademie für Soziale Demokratie provides selected further reading (with commentary): [www.fes-soziale-demokratie.de/materialien](http://www.fes-soziale-demokratie.de/materialien)*

*Current economic policy studies and analyses are to be found in the publications of the Friedrich-Ebert-Stiftung's Department of Economic and Social Policy: [www.fes.de/wiso](http://www.fes.de/wiso)*

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## Further reading:



*More background, texts and materials on the values and roots of social democracy are provided by the module »Social Democracy« of the Friedrich-Ebert-Stiftung's der OnlineAkademie: [www.fes-online-akademie.de](http://www.fes-online-akademie.de)*

*An introduction to all important issues related to economics and economic news is provided by »Das Wirtschaftslexikon. Begriffe. Zahlen. Zusammenhänge« by Volker Happe, Gustav Horn and Kim Otto (see p. 20).*

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## Twelve key terms

### 1. Equality

(p. 77, p. 144 ff.)

### 2. Globalisation

(p. 52 ff., p. 103 ff.)

### 3. Fundamental rights

(p. 59 ff.)

### 4. Core values

(p. 56 ff.)

### 5. Decent work

(p. 13, p. 137 ff.)

### 6. Capitalism

(p. 19 ff., p. 25 ff., p. 30 ff., p. 43 ff., p. 47 ff.)

### 7. Market economy

(p. 43 ff., p. 47 ff., p. 50 ff.)

### 8. Minimum wage

(p. 144 ff.)

### 9. Codetermination

(p. 40 ff., p. 78, p. 137 ff.)

### 10. Sustainability

(p. 70 ff.)

### 11. Social equality

(p. 67 ff.)

### 12. Growth

(p. 66 ff.)

## REACTIONS TO THE 1st GERMAN EDITION

*»An informative book. Reader 2 is well worth reading. It is not intended expressly for that purpose but it is just what we need in this era of rampant financial capitalism. Value-oriented economic policy is the topic of the book and what it calls for. It is about a politics – that of social democracy – in which people are the centre of attention. A politics whose aim is prosperity for all at a high level and which it makes achievable and also permanent – economically successful, environmentally rational, socially stable and fair. A compass for the way forward.«*

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