Germany has prescribed austerity and restraint for Europe, while at the same time undertaking extensive fiscal stimulus packages at home.

by Blog Admin

The eurozone crisis is one of the most significant challenges EU policymakers have yet faced. **Waltraud Schelkle** *examines Germany's reaction to the crisis, finding that while Germany proposed economic self-restraint in 2008, it also embarked on a policy of domestic fiscal stimulus to the welfare system and car industry that amounted to 3 per cent of GDP. She argues that hard times can often lead to a delicate balance being struck between the presentation of policies to the electorate on the one hand, and the need to balance the needs of interest groups on the other: what she terms the 'dual politics of policymaking'.*

Times are hard for economic policymaking. A financial crisis of unprecedented scope shattered politicians' beliefs in the received economic wisdom that had informed two decades of continuous reform. Ever since the demise of pump-priming Keynesianism in the late 1970s, governments have tried to reduce their involvement in the direct provision of goods and services. The project of European integration was revived in the mid-1980s and became a major force in redefining what national government should and could do when intervening in markets. Yet, in 2008-2009, the international financial system would have collapsed if public authorities had remained faithful to the various hands-tying innovations instead of giving monetary and fiscal life support to banks and governments.

The German response to the financial crisis in Europe since 2008 is of interest not least because the government plays a key role for the EU's concerted effort to combat recession and a meltdown of euro bond markets. This allows us to understand why the European Union presents such a contradictory image in its crisis management, namely of indecisiveness and hyperactivity, of timidity and hyperbole.

The irony to be explored is that what the German government stated publicly, and at the EU level categorically, fitted the stereotype of ordoliberal Germany but this was the opposite of what it practiced at home. The German Chancellor Angela Merkel proposed self-restraint and principled collective action only where absolutely necessary. In practice, the German government topped up the in-built stabilisers with a sizeable subsidy to encourage labour hoarding by firms and generous demand-side policies for the car industry, undeterred by considerable spillovers that also stabilised demand for its European neighbours to the East.

German Bundesministerium der Finanzen in Berlin Credit: Manuel Martin (Creative Commons BY)

In contrast to the then French President Sarkozy, Angela Merkel did not give any speech that can be called grand. In fact, those speeches that the press considered to be significant and formally important – in parliament or to an annual party conference – were criticised as missed opportunities across the political spectrum. She was short and specific on the subject of Europein her first crisis speech in 2008, arguing that there are two ways in which national and European crisis management should *not* be linked. First, she criticised the Irish way of protecting only domestic banks and discriminating against those from other member states. Second, she distanced herself from a proposal by President Sarkozy for a European sovereign wealth fund that would protect European firms against takeovers. It was never created because theUK was also opposed and the European Commission skeptical of its protectionist air.

The German government at the time, a Grand Coalition between Christian and Social Democrats, did not show such self-restraint in practice. The flagship of the German stimulus package, initiated by the Social Democrats, became a short-time work programme that was made more generous in terms of duration for workers (up to 24 months for 2009, 18 months for 2010) and relief from social security contributions for employers (50 per cent). By comparison, France also had a short-term work programme but limited in duration to 6 weeks at a time and a maximum of 600 hours per year, i.e. the equivalent of about 4.5 months. The German programme could be extended by an ordinance of the federal employment minister and did not require parliamentary approval, as the Social Democratic minister in charge noted publicly. The Employment Agency paid 60 per cent (67 per cent for parents) of the net wage lost due to short-time work. Participation exploded from about 50,000 in May 2008 to 1.5 million workers in May 2009, maintaining an estimated equivalent of 500,000 full-time jobs, keeping unemployment at a stable level despite a deep drop in GDP.

Germany also extended support through a more generous cash-for-clunkers programme than France. The car-scrapping scheme paid a so-called 'environmental premium' of €2,500 for the acquisition of a new, cleaner car that replaced a car at least nine years old, no matter where it had been produced. This stabilised production in other countries as well because the import share in the value of cars is considerably higher than for the average of consumer goods. For sure, the government was also tempted by protectionism, except that it would never admit to blatant patriotic interference. The government allegedly conditioned credit guarantees for a third party's takeover of Opel from General Motors on the maintenance of national production capacities. Backed byBelgium,Spainand theUK, member states that saw their Opel plants under threat, the Commission undermined German protectionism by invoking EU state aid rules.

The outcome was one of the biggest fiscal stabilisation efforts in the EU. The net effect of fiscal stimulus (deficit-increasing) measures amounted to 3.0 per cent of German GDP over 2008-2010 (by comparison, the stimulus in France amounted to 0.6 per cent only). The automatic stabilisers accounted for an additional boost to the economy of 4.2 per cent of German GDP (of 3.4 per cent in France, data based on OECD and EUROMOD). High tax revenues in an economy growing at over 3 per cent in 2010-11 allowed Germany to reduce its deficit under the 'excessive deficit' threshold of the Stability Pact.

What kind of politics can explain this difference between political presentation and effective policymaking (which a detailed comparison could show is the reverse image of France under Sarkozy)? A combination of electoral and interest group politics is arguably the answer. Hard times, in the sense of an economic and intellectual crisis, are indeed times of very visible politics, even when policymakers choose to present themselves as merely responding to economic imperatives. The public presentation of policies must speak to constituencies and pivotal groups of voters, by communicating a credible ideological stance or by conveying competence in solving their problems. Actual policies must accept that certain economic actors can make or break a policy, interest groups with veto power have to be satisfied, and redistributive effects of problem-solving may be undesirable. This discrepancy is a constant source of frustration for voters and has contributed to the popular cynicism that democratic politics is inherently hypocritical.

The dual politics of policymaking in hard times has arguably wider significance for the political economy of crisis management in capitalist democracies. The lack of a grand narrative about the role of the political fitted the German government's strategy of responding to economic needs with a display of the popular politics of restraint. German political elites instinctively favour a cautious approach, possibly because the rhetoric of a strong state is taboo, but also in order to avoid overstretching state capacities. So the government chose to be pushed into decisive state intervention rather than to engage in it proactively. Even if it had not worked out so well, Merkel could have stated that she never pretended to save the market from itself. The problem with this strategy is that policymakers are always behind the curve because they restrain their capacity for intervention and thus become driven by market forces.

The fallout from the eurozone crisis is a case in point. The German Chancellor wanted EU political decision-making to manage and contain economic interdependence. But the disciplinarian approach led to more interdependence in economic terms because markets remain unstable. The reforms of economic governance have also increased interdependence in political terms. The corresponding reflex of responding to every economic imbalance with ever more intrusive intervention in national budgetary processes politicises conflicts over economic adjustment in an unintended way.

The politicisation of the EU has not been accompanied by an increase in the capacity for macroeconomic policymaking. The lesson from Germany's crisis management is that the popular politics of restraint needs an effective policy of stabilisation. Hence, a Europe Union emulating German crisis management can deliver neither economic stabilisation nor political legitimacy.

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Note: This article gives the views of the author, and not the position of EUROPP – European Politics and Policy, nor of the London School of Economics.

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About the author

Waltraud Schelkle – *LSE European Institute*

Waltraud Schelkle is a Senior Lecturer in Political Economy at the European Institute of the London School of Economics. Furthermore, she is an Adjunct Professor of Economics at the Economics Department of the Free University of Berlin. Previously, Schelkle worked as a development economist at the prestigious German Institute of Development inBerlin. She is particularly interested in the political economy of European integration.

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