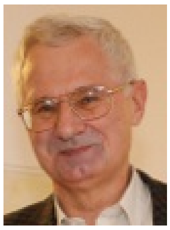
The institutional foundations of the German economy explain why it has handled the economic crisis more effectively than other European states.

by Blog Admin

Germany's economy has experienced a transition from the 'sick man of Europe' after unification in 1990, to becoming a relative 'winner' during the current economic crisis. **Gregory Jackson and Arndt Sorge** *argue that while explanations for economic performance typically focus on macroeconomic and fiscal policies, the evolution of institutions within a state can also be highly significant. The institutional changes which have occurred within Germany since the end of the 1970s go some way toward explaining why the country has managed to deal with the crisis more successfully than other states.*



In dealing with the post-2007 economic crises, both academics and politicians have focused on causes and solutions using macroeconomic and fiscal policies. We argue that more attention is needed on the wider institutional foundations of the productive economy, and how these might generate economic stability and sustainable growth. Such institutions are ultimately more important than controlling the floodgates of macro aggregates. Here the German experience may be highly instructive given its economic strength in export manufacturing and strong development of institutional coordination across different spheres of the economy. To better understand how Germany's 'non-liberal' capitalism worked in the context of the crisis, we looked at the long-term evidence for institutional change during the same period when neo-liberal policies first took hold in the USA and Britain until the resulting economic crisis (1979 to 2009). We concentrate on changes in financial markets, corporate governance, employment and industrial relations, and training and skill formation.

In Germany, changes in finance, the emergence of shareholder-value management styles, declining coverage of collective bargaining, and certain educational reforms all point towards a type of convergence, set in motion by both institutional imitation and supranational regulation. But within this broad tend toward more liberal and market-oriented institutions; we also observe a simultaneous continuity in non-market forms of coordination. For example, while shareholder value capitalism has made major inroads into publicly quoted enterprises, the climate of industrial relations has retained strong elements of cooperation. Employee representatives on supervisory boards have smoothed this development, rather than being crushed by it. Employers and politicians have moved to scale down codetermination in large enterprises, but have not succeeded despite the governing center-right coalition. A new exchange for small joint-stock companies (Neuer Markt) was established but subsequently crumbled again. Industry level collective bargaining has very much come under pressure, but nevertheless, the coordination and solidarity in wage negotiations helped maintain unit labour productivity and the competitiveness of enterprises.

Much political economy literature on institutions has been side-tracked by a half-full or half-empty debate about change, rather than developing historical analysis of how continuity and change condition one another. We distinguish 'proximate institutions' as specific, normative and tangible norms governing economic action in a particular domain and 'background institutions' as more fundamental and less specific and formalised (e.g. general assumptions about trust or distrust, cooperation or competition, as applying to roughly circumscribed situations). Institutional continuity is subject to the dialectics between concrete, specific and tangible 'proximate institutions' at the surface of the institutional landscape, and 'background institutions' at deeper levels. The bedrock of more inert institutional continuity shapes the direction and precise content of institutional change. A 'metatradition' of institutional continuity exists that in no way contradicts substantial institutional change. Even radical institutional change always involves a recombination of the 'new' with the 'old' institutions in creative, original and often surprising ways. We add to this that 'new' proximate institutions may be complemented and amalgamated with institutional innovation that draws on resources and capacities embodied by 'old' institutions.

Three dynamics have different effects with regard to institutional convergence and divergence across countries or between diffusing global practices and local institutions:

1) International trends stemming from supranational government (such as the EU) or quasi-government (e.g. the normative importance of US stock exchanges, the OECD or International Accounting Standards) clearly produce some convergence. These institutional rules are mostly of a market-liberalising variety most visible in new codes of practice and international regulation.

2) The socio-political situation of each country creates differentiated contingencies and temporalities that shape institutional change. This effect works towards divergence-within-convergence. The German case suggests that political contingencies cannot be read directly off the strength of left or right political parties, or formal rules of the political system. The selective adoption, differential implementation and complex effects of liberalisation requires looking at historical processes.

3) Inertial bedrock of background institutions (i.e. basic structures, beliefs and habitualised dispositions) is often invoked by collective actors as a resource and applied to deal with change coming from the international scene and affecting significant change in proximate institutions. This dynamic asserts the specificity, or divergence, of proximate institutions.

Corporate governance shows the clearest convergence effects in Germany, notably in financial and accounting standards, in the dissolving of share cross-ownership, and in the taking-on-board of EU directives or other international rules on take-overs, financial markets and corporate governance. Here international laws and standards had the most direct impact. On the other hand, existing institutions of codetermination have also proved to be resilient; they shaped how these imported practices are framed and understood in practice—an institutional compromise between conflicting value rational logics.

The second effect, of divergence within convergence, is exemplified by increases in enterprise level bargaining and declining union strength, together with the renewed use of these tools for both enterprise competitiveness and socio-political aspirations. Distinctive contingencies for Germany are visible: Unification led to problems of industrial wage bargaining and competitiveness in view of rapidly rising wage and non-wage labour costs; the subsequent effect of this crisis was to alert the social partners and governments to non-wage labour costs and bring back wage restraint. While Germany is not immune to trends of widening inequality as an effect of liberalisation, firms have retained a core long-term labour force with high skills.

The third effect, the assertion of institutional continuities, is visible in adherence to codetermination despite political pressures and reduced union strength, in the disappearance of the Neuer Markt after its initial success, and in the renaissance of wage restraint in aid of competitiveness, export performance and limiting the public sector financial burden.

Altogether, from being a relative winner after the crises following the demise of Bretton Woods in 1972, through turning into a timid adopter of neoliberalism and being styled as the 'sick man of Europe' after unification, Germany again became a relative winner after 2007, by enabling itself competitively to supply the goods that world demand will buy.

This is a summary of the article: G. Jackson and A. Sorge, The trajectory of institutional change in Germany, 1979-2009 Journal of European Public Policy 19 (8): 1146-1167.

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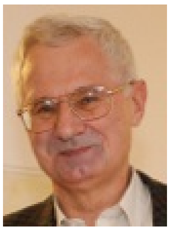

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