

# Globalisation and National Varieties of Capitalism: The Contested Viability of the ‘German Model’

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*It is often argued that globalisation is eroding differences between national varieties of capitalism and enforcing convergence. This study takes up the debate – triggered by declining economic performance – about the viability of the ‘German model’ of a coordinated market economy, examining the arguments about its alleged seminal transformation over the last decade. It goes on to identify a number of flaws in the literature and questions whether the case for fundamental change in Germany has really been made in a credible and convincing way. In addition, it points to significant elements of continuity in areas such as industrial relations and emphasises the importance of political decisions in determining the fate of national economic models.*

The debate about globalisation and its effects on the capacity of nation states has been very much at the forefront of political science research over the last decade or so.\* At the heart of this debate<sup>1</sup> is the question of whether the process of growing economic integration forces nation states to adopt similar policies – in other words, whether the future is one of convergence, or of continuing diversity.

So far, detailed studies of a variety of policy areas have urged caution with respect to the hypothesis of encompassing convergence and have emphasised more the ‘persistence of national variation’<sup>2</sup> and the ‘diverse responses to common challenges’.<sup>3</sup> However, these studies have looked at state policies. In recent years, a literature has sprung up that looks at national economic systems (or ‘varieties of capitalism’) and addresses the question of convergence or diversity at this level. Will globalisation lead to assimilation in the characteristics of (so far diverse) national economic systems, or will they be able to maintain their independence?

This article addresses this question with respect to the ‘German model’ of capitalism in four steps. First, it gives an overview of the model’s characteristics and development, before briefly outlining the main features of globalisation and the debate about it. The third part discusses the future viability of the ‘German model’, looking both at literatures that proclaim fundamental change as its inescapable fate, and at those that analyse the situation of national economic systems as one of sustainable diversity. The last part draws on examples from recent developments to argue that evidence from the ‘decline hypothesis’ is so far not conclusive: the case needs further consideration.

## THE 'GERMAN MODEL'

The term 'German model' started its life as the 1976 election slogan of the governing Social Democratic Party, and was quickly adopted into social science literature as a convenient shorthand expression for the above all (but not exclusively) economic characteristics of the Federal Republic's system.<sup>4</sup>

The main reason for the model's initial popularity was the same reason for which the SPD adopted the slogan in the first place, namely the comparatively good performance of the Federal Republic's economy in weathering the stormy 1970s (with its multiple shocks of a disintegrating currency system, oil price hikes, ensuing inflationary pressures and rising unemployment) better than most other advanced industrialised economies of a similar size.<sup>5</sup> Even if labour market performance was not stellar (and certainly not as good as the Social Democrats would have wished), it was acceptable; economic growth was average; and inflation performance very good. Compared to countries like the United Kingdom, the United States, Italy and France, Germany performed better. The term 'German model' suggested that other states might be able to learn from the now grown-up country of the 'economic miracle' of the 1950s and early 1960s.

The characteristics of this model were a comparatively prudent fiscal policy, which (partly due to federal structures) did not experiment with Keynesian demand management; a stringent policy of price stability, carried out by a famously independent central bank, the Bundesbank (which did not shrink even from major conflicts with the government of the day); and a very low degree of labour market unrest, leading to low strike rates and thus supporting the low inflation environment.

The challenges of structural change, especially away from historically grown heavy industries, shifted the focus of the model in the 1980s. Here again certain distinctive characteristics were discernible when contrasted with the strategies employed for instance in Thatcherite Britain: namely the emphasis put on coordination and consensus, which were seen as the hallmarks of a system that Rudolf Hilferding had called 'organised capitalism' as early as 1910.<sup>6</sup>

As the Hilferding reference shows, this system has deep historical roots that reach back far beyond the time of the Federal Republic into the second half of the nineteenth century. Alexander Gerschenkron classically described the conditions under which German industry emerged comparatively late: industrialisation took place through heavy industries such as coal and steel, which required high capital investments. These in turn created close connections between large-scale enterprises and banks, resulting in the 'Hausbank' model: 'A German bank, as the saying went, accompanied an industrial enterprise from the cradle to the grave, from establishment to liquidation throughout all the vicissitudes of its existence.'<sup>7</sup> Hans-Ulrich Wehler describes in detail how the cooperation between big corporations and associations created the 'corporativism' of late nineteenth century Germany, how the 'cartel movement' aimed to impose order onto the dynamism (and volatility) of Germany's late industrialisation, and how this encouraged the rise of the 'intervention state' (*Interventionsstaat*).<sup>8</sup>

State support for cartels had disappeared in the Federal Republic with its emphasis on competition (and a powerful Cartel Office to enforce it). However, its 'Social Market Economy' was widely seen as a system in which the role of the market was circumscribed by state and societal forces. This had substantial benefits, as British

economist and political scientist Andrew Shonfield pointed out in his famous book *Modern Capitalism*.<sup>9</sup> He asked why the West European economies had been performing noticeably better since the late 1950s than both the United States and Great Britain, and he focused particularly on the institutional characteristics of the German system. Shonfield concluded that Germany's better economic performance was caused by centralised economic decision making, which, contrary to the French system of indicative planning, was not carried out by the state, but by the private sector. He pointed out that the associations had great influence and were thus able to look after long-term interests, thereby fulfilling 'semi-public' tasks<sup>10</sup> (with banks taking on the role of 'prefects'). This had been the case since German industrialisation, and Shonfield pointed to the re-emergence of the three German 'big banks' in the late 1950s despite the American occupying force's attempts at breaking them up.<sup>11</sup>

In the late 1980s and early 1990s the United States was in the throes of a 'decline' debate, fuelled by Japanese economic success, and then slid into a recession; a similar fate befell the United Kingdom. At the same time, Germany seemed to shoulder the economic burdens of unification with relative ease, displaying remarkable growth figures while maintaining low inflation and even reducing unemployment. As a result the 'German model' was seen as something to be emulated abroad: the British journalist Will Hutton recommended the German system for curing the ills of British 'short-termism' and landed an unexpected bestseller.<sup>12</sup>

A more sophisticated (if compared with Hutton, less popular) appraisal of the German system's advantages was produced by Harvard Business School economist Michael Porter. He described the US economic system as marked by deficiencies in the allocation of investment capital – both between and within firms.<sup>13</sup> This constituted a comparative disadvantage, putting at risk the long-term US growth rate. Porter argued that – compared with the German and Japanese economic systems – the US system put too much weight on short-term considerations, which worked as a disincentive for investment in 'intangible assets' – like worker training and re-training, research and development, organisational development, and stable supplier relations that were becoming ever more important for competitiveness.

The main reason, according to Porter, was the fluidity of US capital. Capital was provided primarily by institutional investors with broadly diversified portfolios, and these investors were above all interested in short-term performance. They lacked incentives to obtain inside information about firms, e.g. through seats on a company's board. Accordingly, they lacked influence over firm decisions. Quick portfolio changes were attractive if a company's performance suffered temporarily. German and Japanese systems, however, were setting incentives for 'dedicated' capital, which helped create stable investor relations and a long-term investment and planning horizon for firms.

Admiration for the German case was based upon its performance – not on an intellectual appreciation of a theoretical kind, for there was no coherent theoretical argument behind it. However, just as Hutton and Porter were writing their praises, the German model's performance declined: the Bundesbank applied the brakes to monetary policy in a drastic way, which to a substantial degree was an expression of the conflict over the strategy for the economic handling of German unification. Germany slipped into a deep recession, unemployment shot up, growth dwindled, and the once-coveted 'German model' seemed to have lost its shine in an age dominated by globalisation.

## GLOBALISATION, CONVERGENCE AND DIVERSITY

The debate about globalisation has had a very prominent place in both academic and popular discussions over the last decade or so. At its core lies uncertainty over the future fate of the nation state. In the face of growing economic interdependence, would national democracies still be able to determine their own fate, or would they be steered by the power of anonymous markets?

This should not have come as much of a surprise as market economies were becoming ever more closely intertwined. Indeed, this process had been going on for quite some time, but it was the end of state communism and the Cold War that made it particularly evident. Trade had been growing more quickly than GDP for quite some time, and as a result of this greater openness countries became more vulnerable to external economic shocks and influences. Foreign direct investment grew substantially, again increasing the influence that events abroad and multinational firms had over domestic affairs. Liberalised financial markets underwent revolutionary developments, with volumes in certain instruments – particularly so-called derivatives – skyrocketing in only a few years. A good example is the 50-fold increase in currency markets turnover between 1980 and 1995, which reduced central bank reserves to a *quantité négligeable*, symbolising the reduction of state capacities for intervention.<sup>14</sup>

The academic debate about globalisation – a growth industry for many years – focused on the question of whether increased interdependence would enforce increased convergence of policies or whether it would have no such effect. From a theoretical point of view, the answer was unclear.

Scholars favouring the former position argued that governments competed for mobile capital that was seeking the highest net return. This would lead to an international equalisation of net yields and consequently to tax competition between countries seeking to offer the best conditions for business.<sup>15</sup> Competition, however, would not be limited to taxation alone, but extend to labour market, social and environmental regulations – which all have an effect on the expected return on capital – and lead to an equalisation here as well. Since capital was the most mobile factor, it could most easily threaten with exit and thus force government policy to adapt to its wishes.<sup>16</sup> As this process would happen everywhere, convergence of policy would be the result.

Another group of scholars drew the opposite conclusion, based on theoretical arguments that had been developed about path dependence by the institutional and transaction cost schools of economic theory.<sup>17</sup> They argued that specific national characteristics, such as differences in national policy styles or in institutional arrangements, would display a high degree of stability and persistence. These positions found support from scholars of institutional practice who argued that '[i]nstitutions are not simply reflections of current exogenous forces or micro-behaviour and motives. They embed historical experience into rules, routines, and forms that persist beyond the historical moment and condition'.<sup>18</sup>

The academic debate about state capacity under conditions of globalisation has so far arrived at rather cautionary results about the amount of convergence and has emphasised the high degree of diversity in the reactions to common challenges.<sup>19</sup> But public political discourse does not follow the often meandering paths of detailed scholarly argument. In many countries the debate about globalisation was

instrumentalised politically and used to push through economic policy reforms. The public 'discursive construction' of globalisation emphasised the need for change and delimited conceptions of what is economically 'possible' towards an agenda dominated by neo-liberal recipes.<sup>20</sup> The focus on restrictions was meant to galvanise support for reforms. Within the German system the gloomy perspective outlined in the previous section led to the conviction expressed by the then chairman of the Bundesverband der deutschen Industrie, Olaf Henkel: 'Nobody wants our model anymore.'<sup>21</sup>

#### THE DEBATE ABOUT THE VIABILITY OF THE 'GERMAN MODEL'

##### *The Decline Hypothesis*

Prognostications of decline were echoed in the scholarly literature. One book title saw the German model moving from being a 'role-model to being a phase-out model'.<sup>22</sup> All in all, an extensive academic literature has sprung up over the last couple of years on the decline of the German model. Notable contributions have especially been made by present or former members of the Cologne Max-Planck-Institute for the Study of Societies, which is why one could perhaps label this position the 'Cologne decline hypothesis'. In brief, it states that changes in constitutive areas of the German system are undermining the latter's functionality and complementarity. Because these changes are 'uncoordinated',<sup>23</sup> they have to have negative consequences, resulting in the 'winding up of Deutschland AG', to quote the subtitle of another book.<sup>24</sup>

Even more radical statements have been made by American corporate law experts: in an influential and much discussed article, two lawyers from Yale and Harvard Law Schools declare nothing less than 'The End of History for Corporate Law'.<sup>25</sup> The US system, they assert, has established itself as the normative role model, and alternative models like the German one had failed.

The main arguments for decline and failure can be summarised as follows:

- In corporate governance the so-called market for corporate control has undergone wide-ranging change since the mid-1990s, above all in corporate strategy, especially in the financial sector. The focus is now on shareholder value, barriers for takeovers have been scrapped and cross-shareholdings largely abolished. Systematic disposal of 'super-ordinated' linkages has led to a 'decline of organised capitalism' or at least its 'disorganisation'.<sup>26</sup>
- In industrial relations, a substantial weakening of associational strength has occurred, both on the trade union and on the employer side. Streeck and Hassel talk of the 'crumbling pillars of social partnership', which has developed from an asset of the German system into a liability.<sup>27</sup> The reason is that both associations and the state are now too weak to push through their own preferred strategies, but still strong enough to block other strategies. As a result, collective bargaining has turned into a policy oriented towards the interests of labour market insiders, but incapable of contributing to the solution of labour market problems, especially high unemployment – as the failure of the 'Alliance for Jobs' negotiations made abundantly clear.

- In the financial system banks have undertaken a change of strategy away from the ‘Hausbank’ model towards one focusing on investment banking. They have divested their shareholdings in non-financial firms, because of emerging conflicts of interest.<sup>28</sup> Investment banking promises bigger profit, which is why banks sold their investments in corporations and gave up seats on supervisory boards. In the case of Deutsche Bank, in 1996 it held the chair of the supervisory board on no less than 29 of Germany’s top 100 corporations. Only two years later, this number had shrunk to 17, and in 2001 the bank declared in its corporate guidelines that it would no longer seek any chairmanships on supervisory boards.<sup>29</sup> The banks, in other words, have also shifted to an exclusive focus on shareholder value.
- Political reforms supported this development. In 1998, the *KonTraG* bill (*Gesetz zur Kontrolle und Transparenz im Unternehmensbereich*) was supported by all parties on the floor of the Bundestag. Strikingly it was originally an initiative of the Social Democrats when still in opposition. Joint criticism from the political left and the political right of the ‘power of the banks’<sup>30</sup> meant that ‘Deutschland AG’ no longer enjoyed any support in parliament. In 2001, budgetary changes resulted in the abolition of capital gains taxation for sales of corporate investments. This measure provided a clear incentive to divest the cross-shareholdings and block-holdings that had been characteristic of Deutschland AG.
- The ‘end of history for corporate law’ is predicted by two leading American authors, who argue that an international convergence towards a model exclusively oriented towards shareholder interests is not only inescapable and has already widely taken place but is also preferable. They suggest calling this model the ‘standard model’ forthwith and ascribe this worldwide convergence to the failure of alternatives, such as the ‘labour-oriented model’ (as they call Germany with its co-determination), and the ‘state-oriented model’, which includes France and Japan. In their view, bad economic performance and the end of socialism had eliminated the latter model; the conflict of interest between capital and labour (and the unrest springing from it) had rendered the German model uncompetitive.

Both authors exclusively use corporate law literature for their sweeping assessment. They might profit from a more interdisciplinary approach and a visit to a social science library – where they would likely not only discover foreign trade statistics instructive with a view to German competitiveness, but also a literature on ‘varieties of capitalism’ and the persistent differences between national economic models – which implicitly puts question marks behind the hypothesis of the decline of the ‘Rhenish model’ – and even more the hypothesis about ‘the end of history’.

### *National Models of Capitalism and their Persistence*

At the same time as domestic popularity of the ‘German model’ was waning and the discussion about globalisation – and the convergence that it would bring – took off in academic journals and in political commentary, a new literature argued in favour of the persistence of ‘varieties of capitalism’. In this literature the ‘German model’ played a prominent role.

The literature on national models of capitalism is complex and multi-faceted. However, two things are of particular interest: this literature is truly interdisciplinary with contributions from sociologists, economists and political scientists; and it

illustrates a growing differentiation of concepts and an active debate. As a consequence, this area of academic investigation has over the last decade grown from more journalistic beginnings into a branch of systematic empirical and theoretically well-founded social science research.

The French economist and then President of Assurances Générales de France (AGF), Michel Albert, began the debate about classifying market economies with his book *Capitalism against Capitalism*. It is probably no coincidence that the debate started briefly after the demise of Communism, when market economies had won a resounding victory over planned economies.<sup>31</sup> Albert distinguished between a 'Rhenish' and a 'neo-American' model of market economy, and left no doubt which of the two he preferred. On grounds of superior economic and social performance, he considered the 'Rhenish' model (of which the German model is the most prominent expression) preferable and advocated its adoption for France. His book undoubtedly hit a nerve and became popular very quickly as well as translated into many languages. It often still serves as a reference point for the debate, as the term 'Rhenish capitalism' demonstrates.

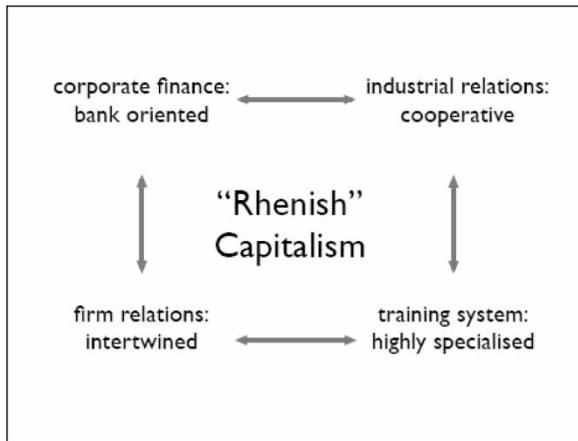
In the following years the analysis was broadened and substantiated with a focus on questions of firm organisation, alternative disciplinary mechanisms and problems of agency in the economic literature.<sup>32</sup> The publication of the edited volume *Varieties of Capitalism*<sup>33</sup> by Hall and Soskice was a milestone, not only because it provided it with a name (at least in political science), but primarily because it provided a sophisticated theoretical grounding. Building on theories from the economics of information and institutional approaches, Hall and Soskice placed the firm in the centre of their analysis. They distinguished two types of market economies: 'coordinated' (comprising such countries as Germany, Sweden, Switzerland, the Netherlands and Japan), and 'liberal' (the Anglo-Saxon countries: USA, United Kingdom, Canada, Australia and New Zealand). Their model was the first to emphasise the complementarity of the constituent partial systems (finance, industrial relations, training, inter-firm relations) for the performance of the system as a whole, distilling from that their hypothesis of 'comparative institutional advantage'. From this hypothesis it follows that convergence should be unlikely, as it would require forgoing existing comparative advantages. Their volume applies the approach to a wide variety of policy areas, ranging from labour market and corporate governance to employers' preferences in social policy, in a way that combines theoretical and empirical inquiry.

More recent contributions add the dimension of discourse<sup>34</sup> and extend the number of countries analysed as well as the number of varieties.<sup>35</sup> But the most important point in this literature is that it finds strong evidence in favour of the existence and persistence of different national economic models – or 'varieties of capitalism' – even if a precise typology of these different systems is still not agreed.

This literature would analyse the German economic system as the interaction of four sub-systems (see Figure 1):

- A system of financing enterprises that can be labelled 'bank-oriented' and provides long-term capital (also described as 'patient capital'). In exchange, banks which provide this capital obtain influence on the business – often via seats on the supervisory board. The stock market – in contrast to the American model – plays only a minor role in corporate finance.

FIGURE 1  
THE COMPONENTS OF THE 'RHENISH CAPITALISM' MODEL



- The system of labour relations is characterised by a strong element of cooperation, which to a large part rests on the comparatively strong role of associations. One result is a high degree of employment protection, which in turn leads to comparatively long periods of employment tenure.
- The system of training combines general and firm-specific skills, which are often highly specialised.
- Relationships between firms are often characterised by an element of cooperation as well as competition, for example when agreeing on standards, where associations play an important role. Cross-shareholdings help to stabilise long-term supplier relations, and interlocking directorships enable firms to gain detailed inside information about each other even without wide-ranging publicity rules.

In short, the German economic system relies to a considerable extent on non-market forms of coordination and strong 'networks'. The constituent parts do not exist independent of each other – in fact, it is only through their functional interaction and their complementarity that they form a system or a 'model':

- 'Patient capital' (which does not have to vie to maximise profit on a quarterly basis) enables businesses to credibly commit to a high degree of employment security, which in turn makes acquiring and investing in firm-specific skills rational for both employees and employers – since they do not have to be afraid of 'sunk investments'.
- Training standards that are the result of cooperation between firms add to this model, because they increase the likelihood of finding suitable employment in the industry (for the employees) and of finding suitably qualified labour (for the firms). In addition, such cooperation makes it possible to obtain inside information about the performance of firms, which means that the correction mechanism of 'hostile takeovers' in the case of failure (which is so typical of the American system)

becomes as unnecessary as it is unlikely because of the prevalence of cross-shareholdings (which are the root cause for the nickname Deutschland AG – Germany, Inc. – that has been given to the system). Safety from takeover bids, in turn, enables firms to take a long-term view of business development, which again is required for the 'patient capital' and its long time horizons (see Figure 1 for a graphic depiction of the system and its interaction).

An economic system characterised by these features will not exclusively focus on the interests of the owners, but take into account the interests of all stakeholders, such as employees, suppliers, customers and society as a whole. It is particularly well equipped for competition in the area of 'diversified quality production', which means incremental improvements in high-quality products with little price competition.<sup>36</sup>

#### CONTINUITY AND CHANGE IN THE GERMAN ECONOMIC SYSTEM

Does the flourishing literature on 'varieties of capitalism' and their persistent difference imply that the 'Cologne decline hypothesis' is wrong? Perhaps not, though I would argue that at least two criticisms can be made concerning the stability and robustness of their results.

- Many of the conclusions are based on the behaviour (and changing behaviour) of a select group of big enterprises (such as Deutsche Bank, Allianz and – in the case of hostile takeovers – Mannesmann). However, these firms are not typical of the German economy, where the 'Hausbank' relationship is still central to many small and medium-sized enterprises. Indeed, this *Mittelstand* (firms below 500 employees and with a turnover of less than €50 million) comprises a relatively bigger share of the German economy than in Britain or the United States. It accounts for around 70% of employment and about half of gross value production of the enterprise sector.
- More importantly, the results are based on a period of observation that is in many respects an exception rather than the rule – namely the years of the last stock market bubble of the late 1990s and early 2000s. This period has now given way to normalisation. A crucial test will be whether the results will be confirmed during more normal times.

There is evidence of a rollback of some of the developments of the bubble period and of substantial stability in other areas. Hence it remains unclear whether the changes that undoubtedly take place in Germany really hit the core of the systemic functionality of the German economic model and will ultimately cause it to fail. So far, it seems, that case has not (yet?) been made.

Restrictions of space do not allow me here to embark upon a fully fledged empirical test of the various symptoms of the 'decline hypothesis'. They will be covered in more detail in the contributions by Lütz (for the financial sector) and Menz (for labour market reform) in this volume. But in this section I will put forward a couple of observations that would seem to question the hypothesis of systemic change and support the notion of considerable stability at the core of the German system. I will make four

points in this respect: one about macroeconomic problems; one about a continuing culture of cooperation; one about evidence for reversal of bubble-period strategies, and one about the importance of political decisions.

While there is no doubt about the weakness of recent macroeconomic performance in Germany, it seems curious that macro-level factors are never used to explain this weakness. As a consequence, the whole malaise of low growth rates and high unemployment is attributed exclusively to microeconomic problems, particularly in the labour market, and the failure to reform those decisively. This is mistaken. There have been substantial macroeconomic disadvantages for the German economy from the introduction of European Monetary Union which contribute to the negative performance.<sup>37</sup> Two disadvantages stand out: Germany lost its privilege of the lowest benchmark rate of interest on government bonds (which sets the floor for the national interest rate); and Germany, traditionally a low inflation economy, now has one of the highest real interest rates in the Euro Zone. The reason for the first problem – the loss of a comparative advantage – is that other Euro Zone countries' long-term interest rates converged on the German rate in the run-up to EMU. The reason for the latter problem is that the ECB only sets the nominal rate of interest for the Euro Zone as a whole. A Euro Zone country with a (comparatively) low rate of inflation, in this case Germany, has consequently a higher real rate of interest than one with a higher rate of inflation. One can only speculate about the reasons for the absence of these facts from public policy discourse in Germany: a fear of further increasing public discontent with the euro would be an obvious candidate; not wanting to distract from the perceived need for domestic reform would be another.

Examining the debate about transformation of the German model, Carola Frege has rightly argued that significant change would be instantiated by change in the traditionally cooperative attitudes in industrial relations.<sup>38</sup> She finds no evidence for that in the surveys that she conducted with trade union officials. In a similar vein, evidence from recent events in collective bargaining also seems to demonstrate a continuing culture of cooperation that produces results without major conflict – in spite of the organisational weakening of both trade union and employers' associations. The cases of Volkswagen, Siemens and DaimlerChrysler in 2004 have all seen painful concessions from trade unions in response to substantial cost-cutting demands from management without major conflict or confrontation. Other examples of continuing cooperative attitudes would be IG Metall joining forces with the metal industry employers in setting up a pension scheme<sup>39</sup> or an agreement between the big German banks to coordinate their ratings for the Mittelstand and thus facilitate lending for that crucial sector of the German economy.<sup>40</sup> If cooperation is at the heart of the 'coordinated market economy' model, then the aforementioned examples would seem to point to significant continuity.

Less continuity is apparent in some of the purportedly seismic shifts in company and particularly bank strategy. Listing German companies on the New York Stock Exchange (NYSE) and shifting bank strategy away from retail banking and towards investment banking seemed to be all the rage in the late 1990s. But not any longer: the 'big' German banks, such as Deutsche Bank (which was accused by *The Economist* of behaving like a 'giant hedge fund'<sup>41</sup>), have pledged to cut down on investment banking and try to win new customers in the retail market. The reason is that

income from the retail market is more stable than from investment banking – and that, without such stability, analysts will downgrade the banks, with ultimately negative effects for capitalisation, making them a potential takeover target.<sup>42</sup> Similarly, many German companies discovered that the costs of a listing on the NYSE can easily outweigh the benefits. Therefore, many of them try to de-list – only to find that this is a difficult process.<sup>43</sup>

Finally, it is important not to underestimate the importance of political decisions (as opposed to market decisions) in determining the future viability of national economic systems. Here – in addition to the national level – the European level plays an increasingly important role. Whether and how successfully respective interests influence decisions on that level is of crucial importance. One area of corporate governance regulation demonstrates how influence on political decisions can be used to 'defend' features of the 'German model': The German stock market has a low degree of capitalisation, which means that German corporations are comparatively cheap to buy if foreign shares are used as a currency. A German firm listed on the stock market is rated at only a quarter of a comparable British firm per unit of turnover and at only a sixth per employee.<sup>44</sup> The reason for this divergence is that while a British firm exclusively focuses on profitability, for a German firm profitability is only one goal among several others, such as turnover, market share and employment. What makes a German firm strong in product markets thus weakens it in the market for corporate control.

The European Commission's attempt, driven by the desire for capital market integration, to harmonise the rules for corporate takeover, was accordingly a threat to the German system. It had been on the Commission's agenda since the early 1990s and was the subject of intense negotiations. In 2001, the Commission launched a draft directive – based on British rules – which included the abolition of all defence mechanisms against takeovers (such as restricted voting rights for shares, 'golden shares' or multiple voting rights for certain classes of shares).<sup>45</sup> The German government fought against this proposal, but was voted down three times in the European Council of Ministers by a margin of 14:1. However, a massive political mobilisation ultimately led to a close defeat of the proposal in the European Parliament. Further consultations followed, and in December 2003 the Italian Presidency proposed a compromise in which all regulations concerning defence mechanisms for takeovers were made optional for member countries – an almost complete reversal of the original proposal. The Commission consequently vehemently opposed this compromise, but – in view of the Council's unanimous position – was no longer able to withdraw its original proposal.

## CONCLUSION

This essay cannot deliver a definitive verdict on the viability of the 'German model'. By examining the controversy about the viability of 'Rhenish capitalism' and challenging the 'decline hypothesis' with the recent literature on the persistence of differences between national economic models, it demonstrates that, while changes are taking place in the German economic model, evidence for fundamental and long-term change is so far not strong. At the same time it would be unwise to presume an unchangeable stability of the German model.

However, though there are challenges and change, it remains unclear whether such change will affect the core of the German model and disable the positive complementarity of its sub-systems – its ‘comparative institutional advantage’. As noted above, in July 2004 the management at DaimlerChrysler demanded cost cuts in the order of €500 million per year and an agreement was reached within a week, combining cuts for employees with long-term employment guarantees. This example seems to support the conclusion that patterns of interaction and exchange may be very deeply entrenched and not be affected by a decline in organisational strength on both sides of industry – even though theoretical considerations would lead one to expect less cooperation and growing radicalisation as a result of less ‘encompassing’ organisations.<sup>46</sup> As Thelen has pointed out, it is not only the trade unions that keep the system alive, but also employers, and for good reasons.<sup>47</sup>

The conclusion that the German system is changing, but not undergoing systemic change, is also supported by recent management studies and economics literature.<sup>48</sup> In addition, the Anglo-Saxon system may lose some of its shine – not only because of obvious system failures like Enron or WorldCom, but also because recent academic studies have raised serious question marks about whether the Anglo-Saxon system really works as it is supposed to work – particularly the nexus between corporate governance and economic performance.<sup>49</sup>

If the Anglo-Saxon model should lose the hegemony that it undoubtedly possessed in public and academic discourse at least since the mid-1990s,<sup>50</sup> German businessmen, as well as politicians and the general public, would have to awaken from the comfortable gloominess into which they have settled recently and assess their economic system more objectively. They will then most likely find that economic systems are far less at the complete mercy of anonymous markets than is often assumed in public discourse about globalisation, for many important decisions concerning economic systems are political decisions. Both the *KonTraG* and European takeover decisions have demonstrated this importance of the political dimension. Whether features that can be defended will be defended depends ultimately on political will and skill. The German political system is a very complex environment in this respect.

#### NOTES

\*For helpful comments to earlier versions of this paper I am grateful to the participants of the workshop on ‘The Politics of Economic Reform in Germany’ at the University of Cardiff, 16–17 September 2004, and the participants of the conference on ‘Die Politische Ökonomie der Europäischen Wirtschafts- und Währungsunion’, hosted by the Political Economy section of the German Political Science Association at the Max Planck Institute for the Study of Societies in Cologne, 3–4 December 2004. I have also benefited from detailed comments by the editors of this volume and from Martin Höpner and André Nilsen. I am grateful for all advice, even if occasionally I chose not to follow it. This article was finished during my time as a visiting fellow at the Social Science Research Centre in Berlin (WZB) to which I extend my gratitude.

1. For an introductory overview of the debate see Andreas Busch, ‘Unpacking the Globalization Debate: Approaches, Evidence and Data’, in Colin Hay and David Marsh (eds.), *Demystifying Globalization* (Basingstoke: Macmillan, 2000), pp.21–48.
2. Colin Hay, ‘Contemporary Capitalism, Globalization, Regionalization and the Persistence of National Variation’, *Review of International Studies* 26/4 (2000), pp.509–31.
3. Fritz W. Scharpf and Vivien A. Schmidt (eds.), *Welfare and Work in the Open Economy. Volume II: Diverse Responses to Common Challenges* (Oxford: Oxford University Press, 2000).

4. To give a few examples out of many: the 'German model' (or 'model Germany') features in Fritz Scharpf's comparative analysis of Social Democratic economic policy in the 1970s, Fritz W. Scharpf, *Sozialdemokratische Krisenpolitik in Europa. Das 'Modell Deutschland' im Vergleich* (Frankfurt am Main, New York: Campus, 1987); in Karl-Heinz Paqué's description of the long-term challenges to Germany's labour market, Karl-Heinz Paqué, 'Unemployment and the Crisis of the German Model: A Long-Term Interpretation', in Herbert Giersch (ed.), *Fighting Europe's Unemployment in the 1990s* (New York: Springer, 1995); in Kathleen Thelen's insights about the persistence of employers' interests in cooperative relations with trade unions, Kathleen Thelen, 'Why German Employers Cannot Bring Themselves to Dismantle the German Model', in Torben Iversen; Jonas Pontusson and David Soskice (eds.), *Unions, Employers, and Central Banks: Macroeconomic Coordination and Institutional Change in Social Market Economies* (Cambridge: Cambridge University Press, 2000), pp.138–69; and in Helmut Wiesenthal's description of the political system's institutional conservatism, Helmut Wiesenthal, 'German Unification and "Model Germany": An Adventure in Institutional Conservatism', *West European Politics* 26/4 (2000), pp.37–58.
5. See Scharpf, 'Sozialdemokratische Krisenpolitik in Europa' for a detailed description.
6. Rudolf Hilferding, *Das Finanzkapital. Eine Studie über die jüngste Entwicklung des Kapitalismus* (Wien: Verlag der Wiener Volksbuchhandlung, 1910).
7. Alexander Gerschenkron, *Economic Backwardness in Historical Perspective. A Book of Essays* (Cambridge, MA: Harvard University Press, 1966), p.14.
8. Hans-Ulrich Wehler, *Deutsche Gesellschaftsgeschichte. Band 3: Von der 'Deutschen Doppelrevolution' bis zum Beginn des Ersten Weltkrieges: 1849–1914* (München: Beck, 1995), pp.662–80.
9. Andrew Shonfield, *Modern Capitalism. The Changing Balance of Public and Private Power* (London: Oxford University Press, 1965).
10. For the concept of 'parapublic institutions', in which associations play an important role, and which are considered a characteristic of the German political system, see Peter Katzenstein, *Policy and Politics in West Germany. The Growth of a Semisovereign State* (Philadelphia: Temple University Press, 1987) and Andreas Busch, 'Shock-Absorbers Under Stress: Parapublic Institutions and the Double Challenges of German Unification and European Integration', in Simon Green and William E. Paterson (eds.), *Governance in Contemporary Germany: The Semisovereign State Revisited* (Cambridge: Cambridge University Press, 2005), pp. 94–114.
11. On the latter episode see for example Andreas Busch, *Staat und Globalisierung. Das Politikfeld Bankenregulierung im internationalen Vergleich* (Wiesbaden: Westdeutscher Verlag, 2003), chapter 5.1; and Manfred Pohl, 'Die Entstehung und Entwicklung des Universalbankensystems seit der Mitte des 19. Jahrhunderts', in Norbert Kloten and Johann Heinrich von Stein (eds.), *Geld-, Bank- und Börsenwesen. Ein Handbuch* (Stuttgart: Schäffer-Poeschel, 39th edn. 1993), pp.187–93.
12. Will Hutton, *The State We're In* (London: Vintage, 1996).
13. Michael E. Porter, *Capital Choices: Changing the Ways America Invests in Industry* (Washington, DC: Council on Competitiveness, 1992) and Michael E. Porter, 'Capital Disadvantage: America's Failing Capital Investment System', *Harvard Business Review* (Sept.–Oct. 1992), pp.65–82.
14. For more detailed empirical information about globalisation see e.g. Paul Hirst and Grahame Thompson, *Globalization in Question. The International Economy and the Possibilities of Governance* (Cambridge: Polity, 1996); Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, DC: Institute for International Economics, 1997); David Held, Anthony McGrew, David Goldblatt and Jonathan Perraton, *Global Transformations. Politics, Economics and Culture* (Cambridge: Polity, 1999); Busch, 'Unpacking the Globalization Debate'; OECD, *Measuring Globalisation. The Role of Multinationals in OECD Economies, Vol. 1: Manufacturing Sector; Vol. 2: Services* (Paris: OECD, 2001).
15. A survey of the respective economic literature can be found in e.g. Günther G. Schulze and Heinrich W. Ursprung, 'Globalisierung contra Nationalstaat? Ein Überblick über die empirische Evidenz', in Andreas Busch and Thomas Plümper (eds.), *Nationaler Staat und internationale Wirtschaft. Anmerkungen zum Thema Globalisierung* (Baden-Baden: Nomos, 1999), pp.41–89.
16. Jeffrey A. Frieden and Ronald Rogowski, 'The Impact of the International Economy on National Policies: An Analytical Overview', in Robert O. Keohane and Helen V. Milner (eds.), *Internationalization and Domestic Politics* (New York/Cambridge: Cambridge University Press, 1996), pp.25–47.
17. Douglass C. North, *Institutions, Institutional Change and Economic Performance* (Cambridge/New York: Cambridge University Press, 1990); Oliver E. Williamson, 'Transaction Cost Economics and Organization Theory', in Neil J. Smelser and Richard Swedberg (eds.), *The Handbook of Economic Sociology* (Princeton: Princeton University Press, 1994), pp.76–107.
18. James G. March and Johan P. Olsen, *Rediscovering Institutions. The Organizational Basis of Politics* (New York: Free Press, 1989), p.167.
19. See the quotes at the beginning of the article as well as Busch, *Staat und Globalisierung* for a more extensive review of recent results.

20. Colin Hay and Ben Rosamond, 'Globalisation, European Integration and the Discursive Construction of Economic Imperatives', in *Journal of European Public Policy* 9/2 (2002), pp.147–67. See also Tom Conley, 'Globalisation and the Politics of Persuasion and Coercion', *Australian Journal of Social Issues* 39/2 (2004), pp.183–200.
21. Interview in *Die Zeit*, 9 May 1997, p.19, quoted after Roland Czada, 'Reformloser Wandel. Stabilität und Anpassung in politischen Akteursystem der Bundesrepublik', in Thomas Ellwein and Everhard Holtmann (eds.), *50 Jahre Bundesrepublik Deutschland [PVS Sonderheft 30/1999]* (Opladen/Wiesbaden: Westdeutscher Verlag, 1999), pp.397–412.
22. Jürgen Beyer (ed.), *Vom Zukunfts- zum Auslaufmodell? Die deutsche Wirtschaftsordnung im Wandel* (Wiesbaden: Westdeutscher Verlag, 2003).
23. Jürgen Beyer, 'Einleitung: Unkoordinierte Modellpflege am koordinierten deutschen Modell', in Beyer (ed.), *Vom Zukunfts- zum Auslaufmodell?*, p.11.
24. Wolfgang Streeck and Martin Höpner (eds.), *Alle Macht dem Markt? Fallstudien zur Abwicklung der Deutschland AG* (Frankfurt/Main/New York: Campus, 2003).
25. Henry Hansmann and Reinier Kraakman, 'The End of History for Corporate Law', in Jeffrey N. Gordon and Mark J. Roe (eds.), *Convergence and Persistence in Corporate Governance* (Cambridge: Cambridge University Press, 2004), pp.33–68. (First published in *Georgetown Law Journal*, 89 (Jan. 2001), pp.439–67).
26. Martin Höpner, *Der Organisierte Kapitalismus in Deutschland und sein Niedergang. Unternehmenskontrolle und Arbeitsbeziehungen im Wandel* (Wiesbaden: Verlag für Sozialwissenschaften, 2004), pp.300–321.
27. Wolfgang Streeck and Anke Hassel, 'The Crumbling Pillars of Social Partnership', *West European Politics* 26/4 (2003), pp.101–24.
28. This had become very clear on the occasion of the attempted hostile takeover of Thyssen by Krupp in 1997, when Deutsche Bank advised the 'attacker' Krupp while simultaneously holding a seat on the supervisory board of 'victim' Thyssen.
29. Jürgen Beyer and Martin Höpner, 'Corporate Governance and the Disintegration of Organised Capitalism in the 1990s', *West European Politics* 26/4 (2003). [Special issue on 'Germany: Beyond the Stable State', ed. by Herbert Kitschelt and Wolfgang Streeck].
30. For the historical roots of this criticism and precedents for such cross-party coalitions regarding the 'power of the banks' see Busch, *Staat und Globalisierung*, pp.108–9 and 134–5.
31. Michel Albert, *Capitalism against Capitalism* (London: Whurr, 1993).
32. Pieter W. Moerland, 'Alternative Disciplinary Mechanisms in Different Corporate Systems', *Journal of Economic Behavior and Organization* 26 (1995), pp.17–34; H.W. De Jong, 'European Capitalism: Between Freedom and Social Justice', *Review of Industrial Organization* 10 (1995), pp.399–419.
33. Peter A. Hall and David Soskice (eds.), *Varieties of Capitalism. The Institutional Foundations of Comparative Advantage* (Oxford/New York: Oxford University Press, 2001).
34. Viven A. Schmidt, *The Futures of European Capitalism* (Oxford: Oxford University Press, 2002).
35. Bruno Amable, *The Diversity of Modern Capitalism* (Oxford: Oxford University Press, 2003).
36. Wolfgang Streeck, 'On Institutional Conditions of Diversified Quality Production', in Egon Matzner and Wolfgang Streeck (eds.), *Beyond Keynesianism: The Socio-Economics of Production and Full Employment* (Aldershot: Elgar, 1991), pp.21–61.
37. Focusing on problems here does not mean to deny that there have been substantial benefits as well. The fact that the D-Mark does not alone have to shoulder the recent violent exchange rate fluctuations of the US dollar is only the most readily evident.
38. Carola M. Frege, 'Transforming German Workplace Relations: Quo Vadis Cooperation?', *Economic and Industrial Democracy* 24/3 (2003), pp.317–47.
39. Christine Trampusch, 'Vom Klassenkampf zur Riesterrente. Die Mitbestimmung und der Wandel der Interessen von Gewerkschaften und Arbeitgeberverbänden an der betrieblichen und tariflichen Sozialpolitik', *Zeitschrift für Sozialreform* 50/3 (2004), pp.223–54.
40. *Süddeutsche Zeitung*, 9 Dec. 2004, p.34.
41. *The Economist*, 28 Aug. 2004, pp.65f.
42. *Süddeutsche Zeitung*, 18 Sept. 2004, p.19.
43. *Süddeutsche Zeitung*, 21 Sept. 2004, p.27 and 16 Nov. 2004, p.34.
44. Martin Höpner and Gregory Jackson, 'An Emerging Market for Corporate Control? The Mannesmann Takeover and German Corporate Governance', *MPIfG Discussion Papers*, Vol. 01/4 (Köln: Max-Planck-Institut für Gesellschaftsforschung, 2001).
45. On the case of the EU takeover directive, see e.g. Erik Berglöv and Mike Burkart, 'European Takeover Regulation', *Economic Policy* 18/1 (2003), pp.171–213; Lucian Cernat, 'The Emerging European Corporate Governance Model: Anglo-Saxon, Continental, or still the Century of Diversity?', *Journal of European Public Policy* 11/1 (2004), pp.147–66.

46. Mancur Olson, *The Logic of Collective Action Public Goods and the Theory of Groups* (Cambridge, MA: Harvard University Press, 1965).
47. Thelen, 'Why German Employers Cannot Bring Themselves to Dismantle the German Model'.
48. See for example Marc Goergen, Miguel C. Manjon and Luc Renneboog, 'Recent Developments in German Corporate Governance', *Finance Working Paper*, Vol.41 (Brussels: European Corporate Governance Institute, 2004); Andreas Hackethal, Reinhard H. Schmidt and Marcel Tyrell, 'Corporate Governance in Germany: Transition to a Modern Capital-Market-Based System?', *Journal of Institutional and Theoretical Economics* 159 (2003), pp.664–74; Eva Terberger, 'The German Financial System: Great Institutional Change and Little Effect?', *Journal of Institutional and Theoretical Economics* 159 (2003), pp.707–16. Considering the small, but detectable normative bias the latter two authors have in favour of an Anglo-Saxon style system (a 'modern' system, as the first authors put it, while the second writes about 'limited success of German reforms'), these assessments are particularly interesting.
49. See Mary A. O'Sullivan, *Contests for Corporate Control. Corporate Governance and Economic Performance in the United States and Germany* (Oxford/New York: Oxford University Press, 2000); Marco Becht, Patrick Bolton and Ailsa Röell, 'Corporate Governance and Control', in George Constantinidis, Milton Harris and René Stulz (eds.), *Handbook of the Economics of Finance* (Amsterdam/London: Elsevier/North-Holland, 2003), section 7.1.
50. It should be noted that already Albert spoke of the 'star quality', 'excitement' and 'charm' of the neo-American model, which he contrasted with its inferior performance. Albert, *Capitalism against Capitalism*, p.10.