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German Thatcherism

The structural and historic limits to making Germany more "Anglo-Saxon."

BY JONATHAN HOFFMAN

The lessons of the Thatcher era—which brought deregulation, privatization, and a reduction in the powers of the trade unions to the United Kingdom some twenty years ago—have not been lost on other countries. Europe in general and Germany in particular have been attentive pupils. Europe's Lisbon Agenda aims to boost growth via the classic Thatcherite methods of deregulation and greater economic flexibility. It stands in sharp contrast with previous European initiatives, such as the Social Chapter adopted during the era of former EU President Jacques Delors at the 1989 Madrid Economic Summit.

Moreover, Germany has adopted a radical program of economic liberalization. Agenda 2010 includes tax reform, cuts in pensions and entitlements for the unemployed, and an increase in the minimum size of a business in order for it to be subject to the laws on the conduct of dismissals. In some respects, Germany has gone even further than the United Kingdom. For example, beginning this year the public pension in Germany is numerically linked to the dependency ratio. If there are more old people in the population, pension payments will fall automatically. Almost all countries

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NATO

The Iron Lady: *The lessons of the* **Margaret Thatcher** *era—which brought deregulation, privatization, and a reduction in the powers of the trade unions to the United Kingdom some twenty years ago—have not been lost on other countries. Europe in general and Germany in particular have been attentive pupils.*

face the same pensions "time bomb" as Germany, but to the best of my knowledge no other country has made this direct linkage.

It is also the case that global economic trends are amplifying and reinforcing the German reforms. For example, Baroness Thatcher curtailed the powers of trade unions and successfully resisted the miners' strike in 1984–85. But in Germany, the move within the economy away from industry, which is highly unionized, and toward services, which are much less so, has substantially reduced trade union membership. Since 1998, the membership of the DGB national union federation has declined by nearly 12 percent to 7.7 million. In the summer of 2003, IG Metall—Germany's largest trade union—admitted defeat in an industrial dispute for the first time since 1954. The four-week strike, in eastern Germany, was in support of a three-hour cut in the work week to thirty-five hours, the same as in western Germany. But many workers ignored the call to strike because orders had fallen and unemployment in the east had risen to 19 percent. Another example is the length of the work week, which is rapidly increasing to forty hours from thirty-five. The cause is not Thatcherite legislation. Rather, it is the reservoir of cheap labor within the European Union, in Poland, the Czech and Slovak Republics, and Hungary, to which German companies can easily shift production if local labor costs fail to fall.

DO THEY KNOW HOW MUCH HAS CHANGED?

Those who are most vocal in urging further Thatcherite policies on Germany—they have been called the "Anglo-Saxon triumphalists"—often do not seem to realize how much has already changed. They place the blame for global imbalances on Europe, omitting any mention of the huge U.S. current account deficit or the heavy undervaluation of some Asian currencies.

Such expressions of "Anglo-Saxon triumphalism" have drawn some robust responses. For example, the United Kingdom's EU Commissioner Peter Mandelson used his first public appearance as Commissioner to criticize what he called "exaggerated gloating." "Today Britain seems to offer its own distinctive model of economic success [and] I'm proud of the country's economic record and achievement," he said. "But let's have no exaggerated gloating about that." He warned of the risks in adopting the Anglo-Saxon model wholesale: "We do need more American-style dynamism in Europe but without emulating the raw divisions of America's more polarized society."

Those who urge further Anglo-Saxon policies on Germany are vulnerable to other criticisms, too.

The first is that "one size does not fit all." In other words, there are limits in transferring the Anglo-Saxon model to non-Anglo-Saxon economies. One obvious difference in the case of Germany is that relations between the government and the trade unions remain good. They have certainly not deteriorated to the same extent as was the case in the United Kingdom in the 1980s. For the sake of the economy, Margaret Thatcher had no choice but to confront Arthur Scargill's National Union of Mineworkers

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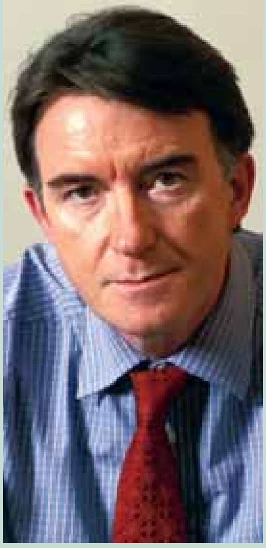

Stop Gloating

Expressions of "Anglo-Saxon triumphalism" have drawn some robust responses. For example, the United Kingdom's EU Commissioner **Peter Mandelson** [right] used his first public appearance as Commissioner to criticize what he called "exaggerated gloating." "Today Britain seems to offer its own distinctive model of economic success [and] I'm proud over the country's economic record and achievement," he said. "But let's have no exaggerated gloating about that." He warned of the risks in adopting the Anglo-Saxon model wholesale: "We do need more American-style dynamism in Europe but without emulating the raw divisions of America's more polarized society."

—J. Hoffman

in the 1984 miners' strike, and the NGA print union in 1986–87 in the News International dispute over the introduction of new technology.

The second is that in their anxiety to squeeze Germany into the Anglo-Saxon mold, they forget the important aspects of Germany's constitution—included for valid historical reasons—which mean that the model can be only partly valid. Especially important here are the large size of the trade unions and the power of the Länder, the sixteen provinces into which Germany is divided. Both were deliberate features of the new post-WWII constitution, drawn up by Ludwig Erhard and others. They were designed to prevent or at worst neutralize a second Hitler. The pre-war fragmentation of workers was one of the main reasons it was impossible to form a united front against the Nazis, and the framers of Germany's new constitution reasoned that strong trade unions would prevent that paralysis being repeated. Also, the Länder were given substantial powers in order to make the federal government as weak as possible, reducing the damage that could be done by any future tyrant.

Germany's higher output per hour is due to its higher human capital and greater physical capital per hour worked.

Both large trade unions and a weak federal government make structural reform more difficult. For example, there have been a number of cases where the Länder have blocked privatization (e.g., Lufthansa, blocked by Bavaria). And the deliberately weak center is a very expensive way of doing things, with each Land having its own parliament, police force, publicly funded party system, and the right to its own broadcasting system. Some two-thirds of national bills require the approval of the state premiers sitting in the Bundesrat.

UNEMPLOYMENT AND INCOME INEQUALITY: TWO SIDES OF THE SAME COIN

In their rush to dress Germany in Anglo-Saxon clothes, the "triumphalists" miss other important points. For example, they often observe how much lower unemployment is in the United Kingdom. Indeed, German unemployment is more than double that in the United Kingdom: 9.9 percent (November 2004) versus 4.5 percent (September) (under the International Labour Organization's "searching for work and available to work" definition).

However, high German unemployment is a sign of a problem which also exists in the United Kingdom, but manifests itself in a different way. That problem is one of unskilled workers. In Germany, unskilled workers are unemployed, but in the United Kingdom they are likely to be "working poor." Income distribution in the United Kingdom has been consistently more unequal than in Germany. Which is better, higher unemployment or more unequal pay? It's impossible to say. It's a political judgment, to be decided at the ballot box.

It is also the case that Thatcherism did not solve the unemployment problem, though it did create jobs. Over the period 1982–90, for example, on average 9.7 percent of British workers were unemployed.

The "triumphalists" also tend to forget the size of the burden of absorbing eastern Germany. Reunited Germany has successfully absorbed 18 million people from the impov-

Qualifications held in the workforce, 1998 (percentages)

	At least degree	At least "A-level"	At least "good GCSE"	Skills index (UK=100)
Germany	22	74	83	109
France	23	45	73	103
United Kingdom	24	36	55	100
United States*	22	29	50	97

Source: The Skills Audit (1996), published by the Department for Education and Employment and the Cabinet Office.
Note: Economically active population aged 16–65 (for women in the United Kingdom, 16–59). For information on equivalencies for qualifications, see Annex 1.
*U.S. results are for 1994.

erished ex-Communist east. Although the burden of bringing standards of living in the east up to those in the west still absorbs about 5 percent of GDP each year, Germany's economy has still grown by 23 percent since reunification in October 1990.

DAS ÜBERTREFFEN?

And even though annual German growth has been slower than that in the United Kingdom since 1993, production per hour worked remains much higher. GDP per hour in Germany in 2003 was 2.7 percent above the EU-15 average, while in the United Kingdom it was 11 percent below. That is, output per hour in the United Kingdom was 13 percent below that in Germany. With hours in many plants drifting back up to forty hours per week from thirty-five, it should not be long before the gap in productivity per person is closed (in 2003 GDP per employed person in the United Kingdom was just 0.6 percent above that in Germany, whereas average annual hours, at 1,707, were 18.2 percent more in the United Kingdom).

Remember the excitement in Italy when per capita GDP overtook that of the United Kingdom? It was called Il Sorpasso—but it didn't last. Now we could get das Übertreffen!

GERMANY'S BETTER HUMAN CAPITAL

Germany's higher output per hour is due to its higher human capital and greater physical capital. One study estimates the United Kingdom's physical capital per hour worked is 37 percent below Germany's. For human capital, the same study estimates that nearly half the difference between British and German output per worker can be put down to differences in literacy and numeracy. Germany's vocational education remains well ahead of the United Kingdom's.
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Which is better, higher unemployment or more unequal pay? It's impossible to say. It's a political judgment, to be decided at the ballot box.

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As Alfred Marshall, one of the founders of the economics profession, commented (*Industry and Trade*, 1919) "All the world has much to learn from German methods of education."

There has long been a legal obligation in Germany for all under the age of eighteen who are not enrolled in full-time education to attend part-time vocational training. But in the United Kingdom, such training is voluntary. Ten years ago a series of studies (by some/all of Prais, Bierhoff, Jarvis, Steedman and Wagner) was published by the National Institute for Economic and Social Research in the United Kingdom, comparing workforces in the United Kingdom and Germany. In one year—1985—the researchers found that the numbers qualifying in engineering and technology in Germany was double, at the master's level; 50 percent higher at the bachelor's level; 50 percent higher at the technician level; and more than three times as high at the craftsman level. They commented (NIER, May 1993): "When compared with the Continent it is the lack of training to craftsman-level—rather than a lack of University graduates—that forms the principal deficiency in Britain's education and training system … there seems little doubt that the Continental approach to practical subjects at secondary schools remains more successful in preparing pupils of average and below-average attainment for subsequent specialized vocational training and for the practicalities of life." All in all, they found (Prais, NIER, November 1981) that 60 percent of the German workforce had intermediate vocational qualifications, double the 30 percent of the United Kingdom. The better qualifications of the German workforce are also detailed in the accompanying chart.

There are limits to the extent to which Germany can become more "Anglo-Saxon."

ANGLO-SAXON LESSONS FOR THE RHINELAND

So do the "triumphalists" make any valid points? Are there remaining aspects of the Anglo-Saxon economies which Germany should emulate?

There are. For one thing, the European Central Bank is less transparent than the Bank of England and the U.S. Federal Reserve in one important respect: it does not produce minutes. The risks of doing so, in terms of increasing pressure on Council members to vote according to national and not pan-European considerations, are far outweighed by the potential gains due to greater transparency.

The pre-war fragmentation of workers was one of the main reasons it was impossible to form a united front against the Nazis.

For another, the Stability and Growth Pact needs reforming in the direction of the United Kingdom's "Golden Rule," which makes the distinction between current and capital spending.

And the power of the Länder is an obstacle to necessary reforms, e.g., privatization. It is surely time to move towards a directly elected upper house, as in other European countries, and away from an upper house comprising Länder representatives (the Länder representatives are never going to vote against themselves, as was shown in the collapse just before Christmas of the attempt at political reform). The sanctions regime of the Stability and Growth Pact is currently under question, but if it is resuscitated, it would be sensible for the Länder to share in any financial penalty that is levied on Germany.

Finally, corporate governance needs reforming in an Anglo-Saxon direction, notably to dilute or even terminate the Mitbestimmung system, by which all companies with over five hundred employees must have one-third representation on their supervisory boards.

Possibly the main lesson for Germany from Thatcherism is that reforms can take time to produce results. Some of the Thatcher reforms took years to bear fruit, partly because in the United Kingdom, macroeconomic stability was not achieved until well into the 1990s.

Structural reform in Germany is very much in the interests of other European economies. But there are limits to the extent to which Germany can become more "Anglo-Saxon." These limits derive from Germany's unique history which has shaped its institutions and from political choices. Attempts to squeeze Germany into a mold that does not fit properly will inevitably fail. ◆