

II. The Dynamics of European National Employment Models

Changes in the System or Change of System? The National Employment Model of Germany

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Abstract

The controversial assessments of the German employment model in the literature are generally based on analyses focused on individual pillars of the model, such as the production system, or the welfare state. The present paper suggests an alternative view that takes into account the interactions between various elements of the employment model. We argue that, by the implementation of what we call a German variety of lean production, the competitiveness of the manufacturing industry has been boosted over the last few years. In contrast to earlier decades, however, the success of the export machine does not entail a more general employment dynamic. That is, the cranks between manufacturing and the rest of the employment system have been damaged substantially. Most importantly, over the last two decades consecutive governments have reduced the state's anchor role for the whole of the employment model and the potentials for its revitalization. The major reasons for this drawback include the conservation of the male breadwinner-focused structure of the welfare state and a fundamental shift in government economic and social policy priorities in the aftermath of the German unification.

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The Need for a Review

For a long time the Federal Republic of Germany was regarded both at home and abroad as one of the countries that had been particularly successful in combining economic growth and social equalization. For many economists and social scientists, Germany was—or is—the exemplar of “Rhenish capitalism” (Albert 1996) or “negotiated capitalism” (Coates 2000), which by virtue of the “beneficial constraints” (Streeck 1997) imposed on German capital by strong labour unions and institutions was said to be superior in the long run to the U.S. example of a less-regulated market economy. Thus, authors such as Hall and Soskice (2001) highlight the ability of the German employment system, as a market economy coordinated at industry level, to obtain competitive advantages in the international division of labor. These conditions have fostered the development of a system of “diversified quality production” (Streeck 1992), which in turn powers the entire employment system.

However, since the historic turning point of 1989–90, when Germany was united, and the arrival of the high unemployment levels that have persisted ever since, opinions on the German employment model have been divided. Whereas in major parts of the Anglo-Saxon literature in particular the emphasis continues to be put on the “coordinated” nature of German capitalism as a basis for “comparative institutional advantages” (Hall and Soskice 2001), some German authors tend to maintain the stagnation-gear character of the system. It is the build of the welfare state in particular that is attracting the criticism of these authors, as it allegedly drives up labor costs and hence impedes employment growth in the service sector, particularly in the low-wage sectors.

In fact, the German employment model is in upheaval. For a better understanding of the reasons, however, we go beyond the prevailing approaches in two respects. First, our analysis goes beyond manufacturing, which has been the focus of most of the investigations of the German employment model carried out to date. There is a need to include the other major areas of employment in an economy in which services account for the greater share of activity. In particular, the significance of the welfare state is not revealed until the employment model is examined in its entirety and not just in terms of manufacturing industry. Second, and unlike most analyses of institutional change, we place the role of politics and policy at the heart of our analysis. Far from strengthening the existing institutions, the economic and employment policies adopted by governments of various stripes and other influential actors have served only to undermine them through a combination of deregulation and a restrictive budgetary policy. The political and economic conditions under which Germany was united have had a decisive influence on this issue.

Beyond Manufacturing

Despite considerable differences of emphasis within the extensive international literature on the German employment model in its prime years, most studies agree in the conclusion—namely, that strong institutions would serve to establish relationships of trust among the key actors, which in turn would provide the foundation for long-term corporate strategies. This long-term approach would pay off in an economy that specializes in high-quality products and at the same time has high levels of productivity. This would produce the economic basis for the social equalization through high wages and good social security on which German corporatism is based.

According to these analyses, the essence of the “German model” ultimately lay—or lies—in the fact that the high added value generated by the country’s high-skill, high-quality manufacturing (and exporting) sector benefits the whole of German society by being redistributed through generalizing institutions such as the collective bargaining system, labor law, and the welfare state. It was only through this interaction that the German model’s characteristic combination of economic dynamism and low social inequality could be achieved.

Given the growing literature on the crisis of the German model over the 1990s, it was not until very recently that the striking contradiction between the allegedly “rigid labour market” and “petrified welfare state,” on the one hand, and the success of German firms on the world markets on the other have received much attention. As the *Financial Times* of London put it (Benoit 2006), the “‘sick man’ is a picture of health.” In fact, when it comes to the German *production* model in manufacturing, the radical move toward a German variant of lean production is certainly, besides the policy of wage moderation, the most important explanation for the revival of German exports and the high average profitability of German manufacturing companies.

In earlier analyses of the German employment model it was implicitly assumed with some degree of justification that the production model—namely, the manufacturing sector and the structures and configurations of actors observed therein—could be taken to represent the entire system. However, the grounds for this assumption have faded over the last two decades. One obvious reason for the declining importance of manufacturing industry within the employment system is the quantitative shift that has taken place between and within the three employment segments (see table 1).

Even more important than the shifts in quantitative importance are the institutional changes. The links and cranks that held the system together in its prime years have been weakened substantially (see table 2).

Thus, a new perspective on German employment as a whole is needed. In

TABLE 1
The Quantitative Shifts in Employment Between and
Within Employment Segments, 1985 to 2004

Employment Segments	1985	1995	2004
Production	50.8	47.5	45.1
Manufacturing Industry	35.6	27.6	24.9
Business Services	7.6	10.2	13.1
Consumption/Distribution	24.0	24.3	23.9
Provision	25.1	28.3	31.0
Public Service	9.1	9.1	8.1
Education	4.4	5.3	5.8
Health	5.4	8.9	11.6

Source: European Labour Force Survey, special tabulation.

Note: Share of employees in the various manufacturing and service sectors in total dependent employment (%).

what follows, we give a rough and brief account of what we think could be a fresh look at the main features of change and crisis in the German employment model. In doing so we will pay particular attention to the prime importance of political choice.

The Key Role of Government Policy for Break-Up or Revitalization

For more than ten years the specter of the downfall of the German employment model has repeatedly been conjured up. Mainstream economists at the Organization for Economic Co-operation and Development (OECD), the European Central Bank (ECB), and in German universities, as well as many of the social scientists who had previously regarded the institutional constraints on capital as the reason for the particular effectiveness of German capitalism that made it a counter-model to the less regulated U.S. form of capitalism, have all agreed that the price that has to be paid for setting in motion a new employment dynamic in Germany is a weakening of social equalization. Our analysis of the upheavals currently taking place in the German employment model diverges from this assessment in many regards.

First, far too little attention has been paid to the impressive regenerative capacities of the high-skill, high-quality productive system that makes up the productive core of the German employment system. The most striking illustrations of these regenerative capacities are the successes achieved by German companies in their export markets. Although globalization is one of the favored explanations for the decrepitude of the German employment system, challenges such as the international reorganization of value-added chains or even the increased price competition in global markets for high-quality goods

are clearly being met so successfully by firms that German manufacturing industry is actually one of the winners from globalization rather than a loser. The development of a German form of lean production, which has benefited from the specialist qualifications of large swaths of the German labor force, is not the only reason for these economic successes. This restructuring of production systems is also linked to a marked shift within organizations and among employees toward greater flexibility and customer orientation, which has set new standards that will have to be adopted in many parts of the private and public service sector.

Second, however, cracks have begun to appear in the foundations of the skill-based, high-quality productive system, putting its very survival in jeopardy. There are structural and political reasons for this. On the one hand, the trend toward the “financialization” of capitalism is squeezing out the “patient capital”—even in Germany capital is impatient. The increasing short-term nature of corporate decision making is undermining institutions, such as the vocational training and industrial relations system, that rely on long-term strategic considerations and trust relationships. Policy makers are not only not countering this trend but are actually encouraging and supporting it. The underinvestment in education and training, from the provision of care for younger children to further vocational training, and the deregulation strategies being pursued at the national and EU levels are having particularly destabilizing effects on an employment model that draws its strength from its human resources.

Third, even if the foundations of the high-skill, high-quality manufacturing system can be successfully shored up and stabilized, it will no longer be sufficient—in contrast to previous decades—to give renewed impetus to the employment system as a whole. Despite the important position of manufacturing industry in the German employment system, the vast majority of workers have for a long time been employed in service activities. In order to boost employment growth in the service sector, there needs to be an increase in both investment and demand, the impetus for which, beyond the manufacturing sector, would have to come from German consumers as well as from government investment. One particularly urgent requirement in this regard is a reshaping of the welfare state in order to provide support for the increasing number of women entering the labor market. At the same time, if the expansion and improvement of childcare, education, and other care services were to be accelerated, major new areas of employment would be opened up. To date, however, instead of clear priorities being set in favor of a state-initiated strategy of service sector development, considerable resources continue to be devoted to subsidizing the traditional single or main (male) breadwinner model. The lack of will or ability to modernize the taxation and social security

TABLE 2
Changes in the German Employment Model by Employment Segments

	Production	Consumption and Distribution	Provision
Governance	<p>Changes in ownership structures and role of banking system and increasing importance of shareholder value orientation</p> <p>Challenges to ties between high- and low-added-value segments of the production chain</p> <p>Outsourcing of business services into areas with weaker regulatory standards</p>	<p>Privatization of post/telecom and parts of public transport</p> <p>Stock market orientation of German Railways AG (plc.)</p> <p>Increasing importance of tendering in local transport</p> <p>Pressure on labor costs in low-price-oriented competition in distributive services</p>	<p>Privatization trend in health and elderly care</p> <p>Cost-cutting pressures in health and elderly care in conjunction with governance strategies borrowed from private businesses</p> <p>Staffing cutbacks in public services and clash over collective agreements</p>
Industrial Relations	<p>Industry-wide collective bargaining in manufacturing maintained but traded against decentralization and growing number of derogations</p> <p>Agreement on fundamental reform of status and pay in metalworking</p> <p>East-West gap in coverage and binding character of collective bargaining</p> <p>Challenges to predominance of collectively agreed standards over firm agreements in various manufacturing and service industries</p> <p>Demise of extension of collective agreements except for construction</p>	<p>Industry-wide bargaining in distributive services maintained but on the edge</p>	<p>Major reform of pay and status structures in public services</p> <p>But break-up of association of public employers</p>

TABLE 2 (cont.)

	Production	Consumption and Distribution	Provision
Training	Dual system of vocational training modernized but increasing reluctance to provide vocational training amongst employers in some industries		
Employment	Persistent decommmodification of labor through labor law but blurring of boundaries at fringes of labor market Improved opportunities for electing works councils in smaller establishments Labor market policy drives jobseekers into low wage jobs far below collectively agreed wages Public tenders do not always respect collectively agreed upon wage rates		
Welfare system	Persistent decommmodification of labor through extensive social security coverage but cuts in benefits Continuing male breadwinner orientation in spite of improved conditions for combination of part-time work with parental benefits Subsidies for marginal part-time work extended		

systems in this respect is placing considerable financial restrictions on recent attempts to improve childcare provision and is increasing the cost pressures on the statutory old age and health insurance schemes, which are then shifted on to the insured.

Fourth, the failure to invest in areas such as education and childcare that are important for the future is also a reaction to government indebtedness, which increased sharply in the 1990s. German unification and the way in which it was implemented, both economically and politically, was an important factor that paved the way to this state of affairs. In the wake of this economic shock and the attendant change in the political climate, the German employment system became caught up in a vicious circle of stagnation and austerity. The persistently high levels of unemployment are undermining the financial and political basis of the institutional structure. The low economic growth rates and the shifting of risk from the statutory social insurance schemes to private households are exacerbating the distribution problems. The government's room to maneuver has been further restricted by its tax-cutting policy. Since German unification the structural problems of the German employment model have become ever more acute, and German policy makers are particularly constrained by the restrictive requirements and conditions forced on them by the Economic and Monetary Union (EMU) stability criteria and, especially, ECB policy, which takes absolutely no responsibility whatsoever for employment growth. However, these "constraints" have also arisen out of the choices made by German policy makers. Today, they act as a self-made straitjacket.

Fifth, the vicious circle of stagnation and austerity in which German economic policy is now caught up, the persistent stagnation of real incomes, the cutbacks in social security benefits, the weakening of industrial relations and, not least, the failure to invest in the future have all contributed to the development in the German labor market of increasingly extensive areas of precarious employment and even poverty around the dynamic productive core of the employment system. Social inequality is on the rise and the long-established pillars—the welfare state and the industrial relations system—are increasingly unable to prop up the employment system as a whole. The labor market reforms of past years are playing a particularly important role in this regard, with possible long-term consequences, since they are bringing the extensive, vocationally qualified middle segment of the German labor market, which until now was the most vital resource available to the German employment system, face to face with new social risks of considerable magnitude. Furthermore, they are damaging the further vocational training system. Nor should it be forgotten that Germany is one of the few EU member states that has not sought, through the introduction of a legal minimum wage, to counter

the emergence of a “working poor” segment on the ever-widening margins of the labor market.

It is clear from the brief summary of the contradictions in the German employment model what a decisive role government policy has played in the situation that has developed. Through the provision of infrastructure, the organization of social equalization, and in its capacity as employer, the state plays a key role in the employment system; in all these areas, it has been working to destabilize that system, whether through its own passivity or the initiatives it has taken. However, the state would also be a key player in any revitalization of the employment system since it is unlikely that the crucial actors will be encouraged by the new economic governance structures to adopt long-term strategies of their own accord. Consequently, it is all the more important to put in place new and stronger counterweights outside of these governance structures—in the education and research infrastructure, the welfare state, and labor market institutions—in order to reduce the influence of the new short-term strategies.

All in all, the picture at the beginning of the new century is one of an employment system that is becoming increasingly fragmented. Unemployment remains at a high level, particularly in eastern Germany but also in large areas of western Germany. Social differentiation within the employment segments is increasing, while the equalizing links between the employment segments are becoming weaker. The long-established combination of skill-based, high-quality manufacturing and social equalization has been seriously undermined. The fragmentation of the employment system is further reinforced by the east-west gap within Germany. There is a risk that eastern Germany will become the country’s “mezzogiorno,” in which large swaths of the territory suffer from emigration, impoverishment, and dangerous political instability.

It only took a few years for the problems of the German employment system to come to a head. It will take considerably longer to put the system back on its feet. At least the same amount of energy will have to be expended on stabilizing and renewing the employment model as has been spent to date on dismantling it.

Note

1. The present paper is a shorter version of our national report for the EU project on the “Dynamics of National Employment Models” (DYNAMO). See Bosch et al. (2005) for the more detailed bibliography included therein.

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