

# Germany's iron cage

by François Denord, Rachel Knaebel and Pierre Rimbert

*Le Monde Diplomatique, English Edition, August 2015-10-16*

**Germany adopted the social market system of economic rules separated from political democracy, known as ordoliberalism, after 1945; it was later used as the ideological basis of Europe Union economic policy.**

“If we needed any more proof that referendums present a risk to the proper functioning of modern democracies, this is it,” said *Der Spiegel* on 6 July. The shock that Germans felt at Greece’s loud referendum was the result of a collision between two approaches to economics — and public affairs in general.

The Greek approach reflects a strictly political mode of government. Popular suffrage takes precedence over accounting principles, and an elected government can choose to change the rules. The German approach subordinates government actions to strict observance of an established order. Politicians can do what they like, as long as they follow the rules (which are effectively excluded from democratic discussion). The finance minister, Wolfgang Schäuble, personifies this view. “To him, the rules are God-given,” says his former Greek counterpart Yanis Varoufakis (see [The defeat of Europe](#)).

This little-known German ideology is ordoliberalism. Ordoliberals, like the Anglo-Saxon advocates of laissez-faire, believe the state should not distort the workings of the markets, but they also believe that free competition does not develop spontaneously. The state should establish a legal, technical, social, moral and cultural framework for the markets, and make sure everyone follows the rules.

The history of this free-market interventionism goes back to the turmoil between the two world wars. In 2012 Schäuble said: “I was born in Freiburg, where there’s something called the Freiburg School. It has to do with ordoliberalism, and Walter Eucken” (1). Freiburg is a prosperous city in the Black Forest foothills, close to Strasbourg with its cathedral, and Switzerland with its banks. In this centre of conservatism and Catholicism, the 1929 economic crisis had the same effect as elsewhere in Germany: the Nazis won the 1933 elections with nearly 36% of the vote.

In the last days of the Weimar Republic, three Freiburg academics pondered the future. The economist Walter Eucken (1891-1950) dreamed of giving his discipline a new philosophical basis; the lawyers Franz Böhm (1895-1977) and Hans Grossmann-Doerth (1894-1944) were concerned with monopolies and cartels (2). Together, they developed a research programme based on the idea of order (*Ordnung*), used to mean both an economic “constitution” and a set of rules. They argued that a strong state was needed to neutralise cartels and avoid the escalation of economic war. Eucken wrote: “The state has to consciously shape the structures, the institutional framework, the order, in which the economy functions ... But it [should] not direct the economic process itself” (3).

## Fragile markets

Unlike classic liberals, ordoliberals consider the markets and private property not as products of nature but as human constructs, and therefore fragile. The state must re-establish competition if it is not working. It must also create a favourable environment by training workers, building infrastructure, encouraging people to save, and establishing laws on property, contracts, patents. Between the framework and the process comes money. In *Principles of Economic Policy* (1952) (4), Eucken emphasises the primacy of monetary policy and the need to shield it from political and popular pressure. A good monetary constitution must not only avoid inflation but, “like the competitive order, must be as autonomous as possible.” Otherwise, “ignorance, vulnerability to interest groups and public opinion” would cause those responsible for monetary policy to deviate from the sacred objective of stability.

The little circle of ordoliberalism in Freiburg grew, and soon became known to the outside world. Their work inspired the economists Wilhelm Röpke (1899-1966) and Alexander Rüstow (1885-1963), who added historical and sociological references, and conservatism. These opponents of the Nazi regime felt the main cause of the post-1929 crisis lay not in the economy but in the disintegration of the social order resulting from laissez-faire. Modernity had produced a dehumanised proletariat, a bloated welfare state and an obsession with collectivism. To counter the “revolt of the masses”, Röpke called for a “revolt of the elite”. To restore workers’ lost dignity, he advocated going back to pre-democratic communities that he saw as natural — family, town, church — and eradicating egalitarianism.

By worshipping liberal idols, Rüstow wrote, “we have denied the principle of graduated hierarchy in general, and replaced it with the false and erroneous ideal of equality, and the partial and inadequate ideal of fraternity; for in lesser and greater family alike, more important than the relationship between siblings is the relationship between parent and child, which ensures the succession of generations that maintains the flow of cultural tradition” (5). Röpke and Rüstow, like their friends in Freiburg, had a Christian background and imbued “order” with the sense given to it by St Augustine: a disciplinary rule governing communal life.

The rise of ordoliberalism was part of a vast international renewal of liberal thought in the 1930s — neoliberalism. In this context, the ordos opposed those nostalgic for laissez-faire — Ludwig von Mises and his disciple Friedrich Hayek — who, Rüstow complained, “found nothing to criticise or to change in traditional liberalism.”

Ordoliberalism had few representatives in Nazi Germany, though some were on the regime’s economic panels, including Ludwig Erhard (1897-1977) and Alfred Müller-Armack (1901-78), who first met in 1941 through “a collaboration between light industry and the Nazi state” (6). A newborn ordoliberalism, notes economist François Bilger, was forced into hiding: “Röpke and Rüstow were forced to go into exile when the National Socialist regime came to power; the others were able to continue teaching ... only because they gave up voicing all their thoughts” (7).

## Post-war intervention

The fall of the Nazi regime heralded their triumph. In West Germany — unlike France, Italy or the UK — reconstruction was based on liberal and free-market rather than social-democratic principles. The US, as the most influential occupying power, prevented the nationalisation of industry that the majority hoped for (8), but eased the transition to an open economy as the ideal recipient for its exports, and granted its new ally a 50% reduction of its external debt (9).

These conditions favoured the establishment from 1948-9 onwards of a system that blended ordoliberalism with Christian doctrine to produce a “social market economy”. This sounds good, but the adjective is deceptive. “Its social character,” said Alfred Müller-Armack (who coined the phrase) in 1948, “lies in the fact that it is able to offer a great variety of consumer goods at prices that consumers can help to determine through demand” (10). A range of measures compensated for the inequalities of the competitive model: a social insurance system inherited from Bismarck, income tax, social housing, support for small businesses. “Social” as used in this context is a reminder that a market economy only works if the state builds a society to match. Post-war Germany was a laboratory for neoliberalism, and its head was Ludwig Erhard, economic administration director in the US and British-occupied zone (Bizonia), economy minister under Konrad Adenauer (1949-63) and then chancellor (1963-6). Most of the structural reforms associated with Germany’s economic miracle were introduced under Erhard (who converted to ordoliberalism during the war), especially the removal of price controls and the introduction of the Deutschmark in 1948, which Germans remember as a new beginning.

Erhard, who was responsible for privatisations and for opening Germany up to free trade, summarised his work: “Just as the referee does not take part in the game, the state is not allowed on to the field. In every good football match there is a constant: the game is governed by precise rules. What I aim to do with my liberal policies is to set the rules of the game.” The introduction of joint management in industry, in 1951-2, was forced on him by Adenauer and the trade unions, who saw it as making up for wage stagnation.

In line with Eucken's principles, Erhard was reluctant to intervene to alleviate economic downturns. Hans Tietmeyer, former president of the Bundesbank (Germany's central bank), wrote that Erhard feared that focusing on full employment to the detriment of all other objectives would reduce monetary stability and individual responsibility (11). Ordoliberalism reached its high point in 1957 when Erhard introduced decisive laws making the Bundesbank politically independent, and against restraints on competition. Monetary stability and undistorted competition: "In this social market economy model, these two policies escape the usual democratic debate," writes Christophe Strassel (12).

## **The ideology's unexpected success**

An economy minister can't act alone, and from 1948 Erhard surrounded himself with ordoliberal experts such as Böhm, Eucken and Müller-Armack. There were many on the Bizone scientific council, and the economy ministry became their sole preserve. Ordoliberalism had support in many other quarters: the periodical *Ordo*, first published in 1948; the Community of Action for the Social Market Economy, a lobby set up in 1953 to promote ordoliberalism — its work frequently appeared in the *Frankfurter Allgemeine Zeitung*; and Die Waage (The Scales), an association of Catholic industrialists which financed campaigns to influence public opinion ahead of legislative elections (13).

But it was in the Bundestag that ordoliberalism achieved its most unexpected success. With its concept of a social market economy and slogan of "Prosperity for All", it allowed the new Christian Democratic Union (CDU) party to move into Social Democrat territory. In 1949 the CDU announced its ambition to build a society in which order would be achieved through "freedom and honouring the promises embodied in a social market economy through genuine competition and curbs on monopolies" (14).

Some intellectuals in the Social Democratic Party (SPD) were charmed by this siren song. In 1955 Karl Schiller published *Socialism and Competition*, containing the slogan "As much competition as possible, as much planning as necessary". This was taken up by the SPD in 1959 when, at the party conference, a majority of delegates recognised private ownership of the means of production and a market economy as beneficial — a major ideological turning point.

This modernisation would not have been possible if raw ordoliberalism had been imposed on German society. The social market economy was a blend of Eucken (the accounting principles devised in Freiburg) and Bismarck (the social welfare system established in the late 19th century). Erhard's resignation in 1966 signalled a "social" reorientation, accentuated when Willy Brandt became chancellor in 1969. Keynesian measures were added: medium-term planning, wage hikes, the expansion of joint management, investment in education and healthcare. In the 1970s and 80s West Germany put together a model that proclaimed its loyalty to the social market economy but incorporated a dose of classic interventionism.

A change of government in 1982 gave Christian Democrat chancellor Helmut Kohl the opportunity to end this phase. The ideological scales had tipped, and the aim was now to restore budgetary equilibrium. But the cost of German reunification prevented any return to ordoliberal fundamentals during the 1990s. It fell to Social Democrat Gerhard Schröder, chancellor from 1998, to restore the order of the 1950s through large-scale labour market deregulation and a weakening of social welfare. These measures have been confirmed by Angela Merkel, who stated in January 2014: "The social market economy has always been more than an economic system, because it is an economic and social order that combines economic power with social justice. The social market economy is our compass, because its principles are timeless."

## **'I am an ordoliberal, but I'm leftwing'**

Eighty years after its foundation, ordoliberalism is perpetuated in Germany by institutions such as the Cartel Office, the Monopolies Commission, which advises the government on competition issues, and the Stability Council, established in 2010 to ensure that the golden rule of zero deficit is observed, at federal level as well as by the Länder. But it also infuses politico-economic debate in Germany, a shared cultural background that everyone interprets as they see fit.

From the conservatives and liberals to the SPD and Alliance '90/The Greens, via Alternative für Deutschland (Alternative for Germany, whose co-founder, Joachim Strabatty, was Müller-Armack's assistant at the University of Cologne), German political parties have many of Eucken's heirs in their ranks. All accuse their rivals of misinterpreting ordoliberalism. "I am an ordoliberal, but I'm leftwing," says Gerhard Schick, a Green Party member of the Bundestag since 2005, who used to work at the Walter Eucken Institute. He does not consider himself "neoliberal in any way. We Greens all believe in the social market economy, though we would add the word ecological. I agree with the ordoliberal view of market control. And I think it's important that the state should set rules to ensure that competition works."

Over the years, varieties of ordoliberalism have emerged that are to some extent interventionist. "It isn't a hard and fast doctrine," says Ralf Fücks, current president of the influential Heinrich Böll Foundation, affiliated with the Green Party. The ordoliberal principle of responsibility can be used to justify not only the regulation of financial markets and eco-taxes, but also a rejection of European debt mutualisation. "Ordoliberalism is a third way between laissez-faire and state socialism. To the Greens, it's a particularly attractive position, which allows us to distance ourselves both from the traditional left and from neoliberalism."

Herbert Schui, a far-left Die Linke member of the Bundestag from 2005 to 2010, emphasises that "the social market economy is a lure. It was created after the war to divert people away from socialist ideas. It works so well that even some people on the left have fallen into the trap." It represents a flexible, yet legitimate standard, since it is associated with the idea of renewal, like Gaullism in France. The German Trade Union Federation (DGB) adopted the social market economy in 1996. Its founding programme, unchanged since then, claims that "the social market economy has produced a high level of material prosperity" and represents "a great ... step forward in the fight against unfettered capitalism," but admits it "does not prevent mass unemployment or the wasting of resources, and has not led to social equality."

## Seen as a liberal market economy

Though part of the German left sees ordoliberalism as a form of interventionism that can be used to oppose neoliberalism, employers associate it with a strictly liberal market economy. A number of organisations sharing this second vision act as a sounding board for ordoliberal thought. Initiative New Social Market Economy, a thinktank formerly headed by Tietmeyer, is campaigning against public support for renewable energy, inheritance tax and the new minimum wage, introduced early this year. The Community of Action for the Social Market Economy is still going after 60 years. The Jena Alliance for the Renewal of the Social Market Economy awards an annual prize for innovation in ordoliberalism, while the Kronberger Kreis, a circle of economists backed by a market economy foundation, claims to supply governments with "thinking on which to base vital reforms". Ordoliberalism even has support within the Church, from Reinhard Marx, archbishop of Munich.

But the most influential voice of ordoliberalism is the Council of Economic Experts, founded by Erhard in 1963 to advise the government. Only one of its five members, Peter Bofinger, is a Keynesian: "No matter what the topic, it's four to one against me." His colleagues see themselves as pragmatic: "We see the good points of ordoliberalism, but when you look closely, it's a mixed bag," says Lars Feld, president of the Walter Eucken Institute. "Ordoliberalism does not necessarily mean austerity. In 2008 my colleague Clemens Fuest and I recommended the government to introduce a major stimulus package to help relaunch the economy after the financial crisis. But, we added, 'if you fear that these measures will affect your terms for refinancing on the markets, then you should introduce a control on borrowing'" — the fiscal golden rule. The government followed both recommendations to the letter. Economist and ordoliberalism expert Ralf Ptak says: "As a German, I can't understand how my country can be so rigid in its economic thinking."

Besides its bastardised application in Germany, ordoliberal ideology has been infused, in a pure state, into the structures of the European Union. Jens Weidmann, president of the Bundesbank admits that "the entire Maastricht framework reflects key ordoliberal and social market economy principles" (15). With its call for the "sustainable development of Europe based on balanced economic growth and price

stability, [and] a highly competitive social market economy”, article 2, paragraph 3 of the 2007 Lisbon Treaty sounds as if borrowed from a speech by Erhard.

Not without reason: most of the Germans who helped establish the Common Market in the 1950s, including Müller-Armack, who helped negotiate the treaty, Walter Hallstein, first European Commission president (1958-67), and Hans von der Groeben, competition commissioner (1958-67), were followers of Eucken. The senior officials of European institutions, not then as important as they are today, reproduced at Community level the strategy of Erhard’s Council of Economic Experts: they concentrated on setting up a legal framework for competition and monetary stability, which the major powers regarded as a secondary priority during the cold war.

Yet their triumph was not unassailable. During the 1950s, the European project was built around two distinct doctrinal approaches. The French approach — centred on intervention and planning — created large areas of exception to competition (the common agricultural policy and national champion policy) through subsidies. It saw a common market as a protection from global free trade. The German ordoliberal approach urged its partners not just to establish a single market but to work for the removal of customs barriers throughout the free world. As early as 1956, Erhard was advocating the establishment of a transatlantic free trade area.

### **‘Divided between building Europe and social justice’**

The French approach dominated in the 1960s and 70s, but did not survive the deregulation of international trade, which demanded budgetary rigour and competitiveness. France effectively surrendered in 1983, when François Mitterrand decided to keep the franc tied to the European Monetary System and to Germany, going back on his election promise to break with them. This obliged the French left to implement an austerity plan symbolically comparable to the one Alexis Tsipras was forced to approve in July. Mitterrand said in 1983: “I am divided between two ambitions: building Europe, and building social justice” (16). Tsipras faced a similar choice, though the pressure on Mitterrand from German chancellor Helmut Kohl and his own economy minister, Jacques Delors, was certainly less than that on Tsipras.

Twenty-five years after the fall of the Berlin Wall, ordoliberal doctrine still prevails among the senior officials of the EU Directorate-General for Competition, and has inspired many commissioners, including Belgium’s Karel van Miert and Italy’s Mario Monti. But the greatest stronghold of ordoliberalism is in Frankfurt. The current president of the European Central Bank, Mario Draghi, says: “It is worth recalling that the monetary constitution of the ECB is firmly grounded in the principles of ordoliberalism” (17). In its workings, in its independence from democratic institutions and in its key mission of maintaining price stability, the ECB copies the Bundesbank. In 2003 the French newspaper *Les Echos* applauded the ECB’s incoming president Jean-Claude Trichet as “the most authentic representative of the spirit, and also the practice, of the Bundesbank, from its creation in 1949 to the enthronement of the euro” — though he was a Frenchman and educated at the Ecole Nationale d’Administration in Paris.

In Europe, the decline of popular sovereignty has revealed the cold efficiency of the automatic pilot systems patiently installed by the EU and the ECB: the settings are removed from democratic intervention by the Maastricht treaty (the 3% limit on budget deficits) and the adoption, in 2012, of Germany’s golden rule limiting the size of member states’ budget deficits (the European fiscal compact).

Ten days after the Greek referendum, Hans-Werner Sinn, Germany’s most influential economist, adviser to the finance minister and inflexible representative of orthodoxy said: “The European crisis cannot be resolved with Keynesian measures. That’s not specially a matter of ordoliberalism, it’s just economic sense.” Eucken’s framework has become an iron cage.