Germany After the Social Democratic Century: The Political Economy of Imbalance

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The end of the social democratic century has marked the beginning of a new era of political and economic imbalance in Europe. These dynamics are visible even in Germany, despite its reputation for stability. This article proposes reorienting the paradigm for research on Germany’s political economy from stability to imbalance in order to help illuminate central causal processes within the country and across the rich democracies. As our review of prominent approaches to the German Model reveals, recent developments have unseated the mechanisms that once balanced competing social forces. Putting contemporary tensions centre stage, we outline three vantage points from which to study political and economic imbalance: the systemic properties of capitalism, multivalent policy feedback, and the organisational foundations of creative adjustment. This conceptual reorientation should equip scholars to use Germany not merely for theorising the roots of stability in the past, but also to employ it as a powerful prism to explain the dynamics of imbalance in the current era.

The social democratic century is over, with both politics and policies shifting significantly across Europe (Dahrendorf 1999). Class-based patterns of group mobilisation have given way to more individualised forms of political contention, and neoliberal makeovers have challenged inherited social democratic policy orientations that once offered an alternative to liberalism. While recent government reforms have improved the rights of some groups and addressed select new social risks, their overall impact has been to deepen, rather than alleviate, political and economic inequalities. Fuelling nativist and welfare chauvinist critiques, these developments have laid the groundwork for the declining legitimacy of established governance arrangements.

Germany is no exception. Though the country’s political economy was viewed through much of the 20th century’s second half as exceptionally stable, with a tendency to balance and serve a multitude of interests across the population, it has more recently
come to display deep imbalances. Its economy now features greater income inequality, with faster growth in the divergence of market-generated incomes than in most of Europe during the early 2000s pushing the pre-tax/transfer Gini coefficient up to that of the United States (OECD 2015). Moreover, in addition to deepening labour market polarisation, the wage share of GDP has fallen to the benefit of capital owners (Haipeter 2017), highlighting both intensifying conflict between winners and losers of structural changes, and reflecting companies’ turn toward value extraction over the reinvestment of profits.

The political realm has similarly become less inclusive, as declining participation in both elections and political parties threatens to hollow out democratic processes (Mair 2013; Schäfer 2013). Furthermore, in line with trends in other countries, the embrace of neoliberal prescriptions by the two centrist catch-all parties has left representative institutions less responsive to popular will (Crouch 2004) and fostered the success of new parties on the margins of the political spectrum, particularly Die Linke on the left and Alternative für Deutschland (AfD) on the right. Finally, domestic realignments have deeply conditioned broader European patterns.

This article outlines three vantage points for exploring the imbalances that have emerged in Germany’s political economy, including their roots and linkages. The broader purpose of this intervention is twofold. First, we seek to better understand the current state of Germany’s political economy as a less orderly and progressively more tension-ridden configuration. Second, we aim to contribute to conceptual progress in the debate over the politics that drive contemporary institutional changes across the rich democracies. Taking a process-oriented approach (Pierson 2004, 174), we strive to demonstrate that German experiences can be of just as much help for illustrating the mechanisms of structural transformation as they have been for the sources of political and economic stability, particularly in the context of welfare state evolution.

We begin our analysis by sketching how recent empirical developments challenge the scholarly paradigm that emphasises Germany’s stability. After showing how existing theories have operated with distinct conceptions of balance in the country’s political economy, we demonstrate that deep contemporary shifts have cast doubt on each of them. A second section puts the emergent imbalances at the centre of the analysis, delineating three crucial entry points for building a more dynamic theoretical perspective on contemporary Germany. The conclusion discusses the changing analytical leverage provided by the German case and suggests ways to make use of it in comparative political economy research.

TOWARD IMBALANCE: CHALLENGES TO THE PARADIGM OF GERMAN STABILITY

Explanations for the stability of postwar Germany have outlined varying rationalisations as to what factors have sustained balance in the country’s political economy. Often, individual scholars have painted quite comprehensive pictures. For instance, studies of Germany’s political economy from the vantage of industrial relations – including those by Markovits (1982; 1986), Streeck (1991; 1997; 2009) and Thelen (1991; 2004; 2014) – are grounded in broad ontologies, displaying an appreciation for the
realities of complex and multiple causalities. Their reliance on a range of approaches to medium-range structural analysis sits in marked – positive – contrast to the narrower grounding of much contemporary comparative political science scholarship.

Yet, to clarify how growing imbalances have challenged scholarly narratives about stability, it is helpful to spell out and contrast the main causal mechanisms that analyses have invoked for Germany’s high degree of productive cooperation among different political groups over time. In turn, we distinguish between different types of arguments that – following distinct theories of action – have stressed the effects of complementary economic institutions on employers’ interests, the impact of interest intermediation structures on labour power, and the influence of institutionalised ideas on policymaking. Elaborated in scholarship on varieties of capitalism, comparative corporatism, and knowledge regimes, these explanations have sometimes been combined. Yet, not only do they tend to focus on different actors – i.e. employers, workers, and public authorities – they also mainly operate at different levels of analysis. While interest-based accounts tend to theorise institutions’ firm-level incentives, power-based narratives usually emphasize the importance of institutions’ effects in sectors, and ideational explanations have predominantly focused on national dynamics. Moreover, each approach relies on different conceptions of balance at the heart of Germany’s political economy (Table 1).

**Complementary Institutions and Employer Interests**

The best-known perspective on German stability today is the varieties of capitalism school (VoC), which has arguably become hegemonic in comparative political economy scholarship. VoC relies on the German case to conceptualise the ideal type of a coordinated market economy (CME), contrasted with the ideal type of a liberal market economy (LME) modelled on the United States (Hall and Soskice 2001). Borrowing from institutional economics, each ideal type’s national institutional system is theorised in terms of the economic complementarity of its individual parts, i.e. the positive returns that any one particular institution receives from neighbouring institutions, with respect to companies’ chosen competitive strategies. According to VoC, the web of market-based institutions in LMEs provides quick adjustments that support

| Explanation based on | Balance between | Examples |
|----------------------|----------------|----------|
| Company interests    | 1) corporate strategies and institutional system  
                        2) long-term interests of investors and workers | Hall and Soskice 2001; Estevez-Abe, Iversen, and Soskice 2001; Mares 2003 |
| Relative class power | 1) relative power of employees and employers  
                        2) reach of democratic and market forces | Katzenstein 1987; Streeck 1991; Müller-Jentsch 1991; Thelen 1991 |
| Institutionalised ideas | 1) principles of Ordoliberalism and social insurance  
                             2) state and society | Markovits 1982; Maier 1987; Carlin 1994; Vail 2018 |
company strategies relying on both low cost and radical innovation. CMEs, in contrast, allow for employers’ non-market coordination in providing specific assets, like patient capital and workers’ non-transferable skills. Firms in CMEs are thereby able to base investment decisions on longer time horizons, adopting high-road strategies and pursuing incremental innovation.

Viewed through this lens, Germany’s institutions are characterised by two kinds of balance. First, in line with conceptions of rational-choice institutionalism, each ideal type is in equilibrium by virtue of company strategies and institutional structures sustaining one another. Given their past investments in competitive strategies, and market successes associated with comparative institutional advantages, German companies should be committed to defending institutions’ ability to provide collective goods, even if these institutions constrain managerial autonomy through employment protections and require substantial corporate co-financing of skill investments and unemployment benefits (Estevez-Abe, Iversen, and Soskice 2001; Mares 2003). Second, with respect to balancing the interests of companies’ stakeholders, CMEs like Germany should deliver for both investors and workers over the long term. Each group similarly benefits from company decisions made on the basis of extended time horizons, which allow investments that take time to generate returns to go ahead, and which tend to offer lower volatility. For a significant share of workers, moreover, these strategies should also mean higher wages due to incentives to invest in skills.

This explanation has provided a compelling justification of German stability. Many institutions in Germany clearly showed a strong affinity to one another and offered positive externalities that allowed their co-existence to produce beneficial outcomes for both employers and labour (Deeg 2007). Stability in one sphere of the economy seemed to reinforce stability in another. For instance, given that firms could rely on domestic banks and a dense network of other German firms for financing, managers were insulated from the financial market pressure for short-term gains typical of Anglo-American economies. Corporate governance practices focussed on accommodating the interests of various stakeholder groups, rather than merely those of shareholders, thereby enabling peaceful labour relations that reduced the risks associated with long-term investments in physical or human capital (Höpner 2005).

Yet, starting in the early 2000s, a raft of reforms has cast doubt on VoC conceptions of institutional complementarities and employer interests. The financial sector in particular has experienced a far-reaching liberalisation that has strengthened market forces and threatens to marginalise non-market coordination in Germany’s economic governance (Beyer and Höpner 2003; Streeck and Thelen 2005). For instance, cross-shareholding by companies, in particular insurance companies and banks, has been unwound, and legal defences against corporate takeovers have been relaxed. Companies have thus become far more exposed to financial markets and activist investors pursuing short-term value maximisation. Major private banks have shifted toward investment banking (though frequently rather unsuccessfully as we now know), and private equity firms and hedge funds have become increasingly active in the country. These increases in investor power sit uneasily with inherited stakeholder-focussed corporate governance regulation, industrial relations, and human resource management.
The increasing inequality of incomes, along with the pressures on labour standards mentioned above, is evidence of liberalisation in the realm of employment as well, which goes against arguments about superior social outcomes in CMEs. Research has documented how wage levels in services have fallen ever further behind those in manufacturing, while even wage increases in manufacturing now lag behind productivity improvements (Hassel 2014; Baccaro and Benassi 2017). Although the past few years have witnessed stronger wage growth, the bottom 40 percent of the income distribution have yet to recover financially from their losses in the early 2000s (Haipeter 2017). In particular, generations born after 1975 have experienced income polarisation, pointing to companies’ resetting of conditions offered for labour market entrants (BMAS 2017). Moreover, workers are increasingly employed in non-standard forms, often in part-time positions across various services, and on temporary agency contracts in manufacturing. Yet, as the fissuring of workplace relations and declines in job quality indicate, these features are merely part of broader phenomena associated with companies’ vertical disintegration through outsourcing of non-core activities to multiple tiers of suppliers (Doellgast 2009; Vidal 2013).

Finally, contrary to the expectations of VoC theorising, employers are lobbying hard to further liberalise institutions (Kinderman 2017). They have also reduced domestic investments while increasing both dividends and share buybacks. These changing uses of profits appear to follow American companies’ abandonment of ‘retain and invest’ strategies in favour of ‘downsize and distribute’ practices (Lazonick 2015; Immenkötter 2017; Belabed, Theobald, and van Treeck 2018). In turn, VoC’s reading of an institutional equilibrium has become hard to sustain, and arguments about a better balance between economic growth and social welfare in CMEs have lost much of their former punch. In response, VoC analyses of contemporary Germany have begun to engage with the politics of institutional change, an endeavour that has required clearer distinctions between static theoretical ideal types and evolving individual cases, and has generated interest in identifying the mechanisms of transformation behind complex empirical developments (e.g. Hall and Thelen 2009; Thelen 2014) – themes that we take up below.

Interest Intermediation and Labour Power

A second narrative on German stability has revolved around the intermediation of diverse interests in labour-capital relations, stressing how organisations’ strength and the multiplicity of veto points have sustained cooperative – even consensual – decision-making through corporatist networks (Lehmbruch 1984). Predating VoC, this second approach is less deterministic in character. For instance, the apparent fit of different elements in Germany’s economic governance infrastructure is conceptualised in more open-ended terms that emphasise deep historical roots, as well as the role of labour power and its facilitation of cross-class concertation (Ornston and Schulze-Cleven 2015). Again, one can speak about two kinds of balance: first, between the relative power of employers and employees as the two core industrial relations parties, and, second, between the respective reach of democratic and market forces. Together, these two types of balance ensured the ‘primacy of politics’ over the economy associated with postwar social democracy (Berman 2006).
Analyses in this stream of research acknowledge that German employers have often benefited from constraints entailed by institutions that protect workers. Manufacturing firms, for instance, were pushed into a competitive high-wage and high-productivity strategy of ‘diversified quality production,’ which helped them avoid competing on price in commodity markets (Streeck 1991). While employers would have preferred freer markets and managerial autonomy, the constant threat of open conflict with labour long prevented any movement in that direction.

In the workplace, co-determination through works councils and labour representation on supervisory boards provided for ‘confictual partnership’ (Konfliktpartnerschaft), enabled by both managers and workers having access to tools that they could use for productive cooperation or turn into resources for defection (Müller-Jentsch 1991). Employers chose cooperation with labour because they were not confident that they would win in open conflict, just as labour recognised its inherent dependence on capital (Korpi 2006). The same dynamic also produced policies of détente at the sectoral level between unions and employer associations (Streeck and Hassel 2003). Moreover, in formal politics, a long-standing alliance between unions and the Social Democrats (SPD) ensured that capital’s interests would be balanced here as well (Smith 1981). This multi-level character of the interest intermediation system gave it stability. If capital, say, were to get the upper hand in national policy, labour would punish it at the sectoral level (Thelen 1991).

The state did not pose much of a threat to these mutually reinforcing arrangements, given that it simply did not seem to have the capacity to align and marshal its disorganised units against a highly organised civil society (Katzenstein 1987). Thus, although the German economy’s performance had declined by the turn of the century, with employers increasingly exercising the exit option offered by growing capital mobility and the opening of markets in the former Eastern Bloc, a plethora of veto points appeared to prohibit unilateral government initiatives akin to Thatcherite reforms in Britain or more progressive concerted reform in the shadow of state threats as in other European countries (Streeck and Trampusch 2005). Both scholars and policymakers found the German polity to be gridlocked, unable to address the problem of ever-rising non-wage labour costs, which were held responsible for growing unemployment. The social partners continued to use welfare corporatism to offload their adjustment costs onto social insurance schemes by, for instance, sending workers into early retirement (Ebbinghaus 2006). Nonetheless, state representatives seemed resigned to repeatedly increasing public subsidies for social insurance to keep non-wage labour costs below the symbolic rate of 40 percent, although this came at the price of growing public indebtedness.

With the benefit of hindsight, we know that the Social Democrats’ neoliberal turn with the Agenda 2010 and Hartz labour market reforms came to cut this Gordian knot. While successful in attracting centrist swing voters and extending the life of Schroder’s Red-Green coalition government, this strategic reorientation had far-reaching consequences. Not only did it sever many of the party’s links with the union movement and accelerate the SPD’s transformation into what some have called a ‘cartel’ party (Jacoby and Behrens 2016; Walter 2018), it also spurred the fragmentation of the German party system, with West German unionists playing a key role in the formation of Die Linke and union members moving toward support for the AfD at rates
above overall averages in the population (Schwander and Manow 2017; DGB Bundesvorstand 2017). This has precluded any medium-term chances of forming a centre-left government.

Fragmentation in electoral politics reflects and reinforces a growing imbalance of power as employers gain the upper hand over labour. Pushed by increasingly critical and no longer captive employers, and underwritten by a progressively more activist state, contemporary Germany has broken with the tradition of consensus rule (Vail 2003). Policymakers have liberalised political decision-making, such as in the administration of federal employment policy, where social partners’ roles in economic governance have been marginalised (Trampusch 2009; Hassel and Schiller 2010). Often, liberalisation also entailed increasing the scope of market allocation, a turn that labour had become too weak to prevent. With union membership levels down, collective bargaining coverage declining, and public opinion clearly favouring reforms, Germany’s institutions did not provide labour with enough power to block these changes.

In the process, Germany has experienced significant welfare state retrenchment. For example, pathways to early retirement have been overhauled, mirroring trends in other countries (Trampusch 2005; Schmitt and Starke 2016). Given that employers have been able to avoid some of the institutional constraints that once aligned their interests with labour’s, they have become more able to shift the costs of adjustment onto workers (Paster 2018). Employers have, for instance, actively used less restrictive employment regulation to push down wage levels at the bottom of the labour market. Workers had little recourse against such offensives, as they were effectively locked in by public policies’ reorientation to activation and ‘welfare through work’ approaches, featuring reductions in passive benefits, curtailments of eligibility, and expanded opportunities to top-up market wages with public funds. In the workplace, moreover, institutions that once supported worker voice have been converted into instruments of managerial discretion and labour control (Jackson 2005; Baccaro and Howell 2017a).

Importantly, the decline of labour power has not been uniform across levels of governance. Works councils have become far more important, displaying a significant degree of institutional entrepreneurship as unions have been weakened, and many employers have turned their backs on their associations in response to the loss of a credible labour threat (Crouch 2005; Silvia and Schroeder 2007). In some scenarios, this dynamic has contributed to re-embedding markets at the level of the firm, a trend that has provided relative stability in larger manufacturing companies (Jackson and Sorge 2012; Sorge and Streeck 2018). Yet, this shift in the primary locus of labour power to the company-level has had broader consequences because it sharpens the long-standing risk of workers putting company interests before those of class solidarity, long referred to as the threat of Betriebsegoismus (Streeck 1984). Already, the character of co-determination has significantly changed, morphing into ‘partnership without conflict’ in core manufacturing firms, and ‘conflict without partnership’ in services companies where collective bargaining coverage is marginal and workers’ defences against employer discretion are limited to antagonistic collective action (Streeck 2016a).

These company-level trends have, in turn, been taken up by research that extends original VoC analyses by adopting a power-distributional approach. Invoking theories of insider-outsider cleavages and studies of labour market segmentation from the 1980s, this line of work theorises a cross-class coalition between manufacturing employers and
their core workers, which has channelled liberalisation into the dualisation of employment conditions and social protection. The resulting reform pathway is thus distinct from deregulation in Anglo-American contexts and embedded flexibilisation across the Nordic countries (Hassel 2014; Thelen 2014).

The debate over the significance of current changes is ongoing, given that evidence for dualisation is mixed and turns strongly on the particular conceptualisation of institutional change. Some indicators point to a general erosion of labour protections and a broad shift of economic risks to both middle-class and working-poor families akin to trends in the United States (Hacker 2008; Clasen and Goerne 2011). There is also little agreement among scholars on the politics driving these changes, not least on the question of the role played by unions. Some evidence points to labour moving toward strategic renewal (Benassi and Dorigatti 2015; Rothstein 2019), as predicted by theories on different phases of collective action (Offe and Wiesenthal 1980). Yet, whatever the specific disagreement might be, the general tenor of most analyses is that contemporary Germany has been experiencing capitalism’s reassertion over its 20th-century democratic limits (Streeck 2009).

Institutionalised Ideas and Policymaking

Scholarship on the role of ideas has been the third major strand of inquiry into the relative stability of the German model and its social market economy (Soziale Markt- wirtschaft), which its intellectual father, Alfred Müller-Armack, once defined as an irenic formula to connect the principles of market freedom and social accommodation. Scholarship on Germany’s institutionally supported normative legacies and the knowledge regime associated with them has traced how the country’s universe of political discourse has long emphasised the importance of restricting public policies to indirect, rule-guided state interventions (Maier 1987; Campbell and Pedersen 2014; Schulze-Cleven and Timo Weishaupt 2015). According to debates among academic experts in Germany, these self-imposed limits on government action uphold an appropriate market order (Ordnung) and social justice (Gerechtigkeit) by reducing uncertainty, sustaining competition, and facilitating the self-organisation of society.

One element of the social market economy, Ordoliberalism, has roots that reach back to writings by Walter Eucken and his associates published before World War II. Yearning for political stability in the face of Weimar’s turbulence and hoping for more economic competition than that offered by increasingly cartelised markets, Ordoliberals called for a strong state to anchor the economy by providing the necessary legal and institutional framework to exercise economic freedom. This has included enforcing contracts and liabilities, curbing concentrations of market power, and guaranteeing free market entry, as well as ensuring monetary stability (Allen 1989). Ordoliberalism rose to prominence when German authorities abolished price controls against the advice of the Allies in June 1948, a step that has become widely perceived as the foundation for the country’s Wirtschaftswunder. Subsequently, ordoliberal principles were enshrined in the 1957 law providing the basis for West German competition policy.

Yet, Ordoliberalism never became truly hegemonic, due to the widely shared desire to limit state power after the experience of Nazi authoritarianism and the perceived need for state-society cooperation to rebuild the country. Instead, ordoliberal elements came to be combined with a commitment to corporatist social insurance, which similarly
emphasised the importance of principled over discretionary government policies (Manow 1997). Core features of social insurance, such as a close link between contributions and benefits, as well as associational governance, had normative roots in Catholic social ethics and were first introduced as public policy by Bismarck during the 1880s in the service of stabilising monarchical rule. Following World War II, these principles fit well with the governing Christian Democrats’ emphases on subsidiarity, maintaining the status of male breadwinners, and collective rights over individual rights.

The Social Democrats and labour unions eventually accepted the orientation toward a social market economy, but in doing so they reimagined core tenets in line with Müller-Armack’s insistence that changing circumstances require the system to evolve dynamically. The social-liberal coalition of the late 1960s and 1970s placed a stronger emphasis on Keynesian demand management and expanded equal co-determination on supervisory boards beyond the coal and steel industries. Yet despite these reforms, the commitment to a robust competition policy remained strong, as the creation of the Economics Ministry’s *Monopolkommission* in 1973 indicates. By 1976, the SPD campaigned in the federal election with an active defence of its version of *Modell Deutschland*. Moreover, in subsequent decades, expanded co-determination has come to be widely accepted even by many conservatives whose faith in Ordoliberalism had originally made them sceptical (Kommission Mitbestimmung 1998; Müller-Jentsch 2008).

While rationalisations of Germany’s social market economy were never ideologically pure, and were even somewhat incoherent (Vail 2018), the self-limiting policies launched under its label have arguably played a strong role in sustaining Germany’s impressive postwar performance (Carlin 1994; Streeck 1997; Beck and Kotz 2017). They also provided a third conception of two types of balance at the heart of Germany’s political economy, one between the principles of Ordoliberalism and social insurance, and one between the state and society. Yet, recent developments have called this narrative of stability into question, just as in the cases of the other two addressed above.

Social policymaking has increasingly turned its back on the ideas that once guided the social insurance welfare state (Palier 2010), with the *Hartz* reforms in particular reconceiving citizens’ rights and responsibilities. The push for the long-term unemployed to become self-employed in the spirit of an *Ich-AG*, as well as the lowering of standard unemployment benefits with respect to generosity, duration, and eligibility criteria, reflect increased public expectations of individuals’ ability to adapt to market forces. Not only have regular unemployment benefits been cut to one year, standards for reasonable rejections of job offers (*Zumutbarkeitskriterien*) have been tightened. Pay below collective bargaining levels, long commutes to work, and mismatches with educational credentials are no longer considered hindrances that unemployed individuals can invoke to legitimise resistance to connecting with their ‘entrepreneurial self’ (Bröckling 2007). Germany now appears to be another example of a ‘triple integration’ in the regulation of unemployment risk cross-nationally, featuring benefit homogenisation, risk re-categorisation, and activation (Clasen and Clegg 2012).

Moreover, even where traditional ordoliberal economic ideas continue to be prominently invoked by German policymakers, such as in Germany’s positions on managing Europe’s Economic and Monetary Union (EMU), these ideas are far from determinate (Jacoby 2014). Given Germany’s size and power, it is reasonable for the country to develop template policies to be adopted beyond its borders (Dyson and Padgett...
2005), as it did with respect to European competition law, the independence of the European Central Bank, and the Stability and Growth Pact, as well as national ‘debt brakes’ more recently. But many of Germany’s positions have exhibited self-interested double standards rather than principled action. Not only was Germany one of the first countries to break the fiscal deficit rules it had pushed for in the European Union, it also did so without consequences.

Whether one perceives Germany as reluctant to exercise hegemony in Europe or not (Paterson 2011), it is hard to deny that it does so, without always providing broader benefits. Examples of such narrowly self-interested action include German leaders’ successful advocacy for the interests of German banks in limiting their exposure to foreign default risks and the government’s support for domestic car manufacturers’ opposition to stricter European emission rules. Moreover, Germany’s EMU-enabled, export-based compensation for weak wage-based or investment-driven demand at home looks a lot like beggar-thy-neighbour free riding. After all, in contrast to 19th-century Britain and the United States during the immediate postwar era, Germany has repeatedly resisted financing the collective goods needed for stable cross-national cooperation as it celebrated record current account surpluses that climbed beyond eight percent of GDP (Matthijs and Blyth 2011).

Where does this leave theorising on the German model, and what are the lessons for comparative inquiry from Germany’s evolution? As the above review has highlighted, Germany has adapted to the new global environment while holding on to – and in some cases even doubling down on – long-standing strengths. Yet the existing paradigm of stability has become ever harder to maintain. Prosperity has become less widely shared, centrifugal forces are operating in the political system, and the long-term viability of Germany’s post-Fordist growth model seems questionable. Whether viewed through the lens of actors’ interests, power, or ideas, Germany’s political economy appears increasingly ‘unhinged’ (Baccaro and Howell 2017b), having lost economic, political, and social anchors that once gave it impressive coherence. The next section outlines promising elements for a more dynamic theoretical perspective on Germany that can guide scholars in exploring the recomposition of the country’s political economy.

PROCESSES OF RECOMPOSITION: A DYNAMIC PERSPECTIVE ON GERMAN POLITICAL ECONOMY

Drawing on recent interventions by leading scholars, we discuss the systemic properties of capitalism, the multivalent character of policy feedback, and the organisational foundations of creative institutional adjustments as vantage points for examining the political dynamics governing imbalance in contemporary Germany. Whether as pillars of new theoretical schemes or simply ingredients, these analytical angles offer a powerful conceptual repertoire. In contrast to the approaches reviewed in the preceding section, a framework centred on imbalance allows for studying Germany not as a neat system, but as an inherently unstable configuration-in-motion. Moreover, examining the country’s political economy from these vantage points sharpens accounts of institutional recomposition by conceiving of institutional change as continuous rather than restricted to short periods of disruption.
Systemic Properties of Capitalism

Many analysts have moved away from studying Germany through economists’ non-political concepts, such as non-market coordination in support of voluntary exchange relationships. Instead, they have come to view it in more sociological terms as a particular historically constituted capitalist social formation that also encompasses an increasingly polarised society (Streeck 2009; Baccaro and Howell 2017a). Frequently, scholars have done so in the name of researching what unites rather than divides countries during an era of increasing financialisation, secular stagnation, and deep challenges to collective action.

Classic theorists of capitalist development – from Marx and Weber to Schumpeter and Polanyi – all provide ample opportunities and are united in their recognition of capitalism’s constant evolution and inherent imbalances. Three properties of contemporary capitalism – the dynamics of capitalist expansion, the exhaustion of public authorities’ mechanisms of social compensation, and the accumulation of social power – deserve particular attention.

**Capitalist expansion.** Conceptions of capitalism are united by their emphasis on the system’s propensity for expansion, with ‘restless’ agents entrepreneurially pushing up against the established social order as they search for new profit opportunities by expanding the scope of markets, commoditising more of the life world, and relying on individual contracts to govern a greater share of social relations (Streeck 2011). Without sufficient counteracting mechanisms for shoring up collectively constituted institutions, this behaviour not only leaves market orders inherently unstable, it also incessantly (re-)shapes social collectivities in their image (Vergesellschaftung).

This functional logic of capitalist organisation operates independently of any particular individual, and its systemic effects are clearly visible in contemporary Germany and across Europe (Streeck 2014). From the global production networks implied by corporations’ vertical disintegration to ‘activating’ labour policy reforms, markets have become ever more central to political and social organisation – both across societies and within them (Rosa, Lessenich, and Dörre 2015). With neoliberal discourses – whether framed in terms of meritocracy, employability, or self-realisation – emphasising the optimising decisions made by supposedly autonomous individuals, citizens are increasingly treated as sellers and consumers, with previous conceptions of the public good falling by the wayside (Streeck 2016b).

**Exhaustion of social compensation.** The social policies that public authorities use to buffer democratic citizens from markets’ harshest effects have long been important for stabilising societies, yet welfare states’ inherited approaches appear increasingly unable to mediate tensions between capitalism and democracy (Habermas 1973; Offe 2006). Governments’ growing reliance on financial markets has been a particularly important constraint. Easily expressed in rising debt-to-GDP ratios, including a doubling in Germany every two decades, this structural dependence has grown as policymakers encountered difficulties in tax collection under conditions of increased capital mobility, and turned to debt-financing expenditures instead (Streeck 2014).

Policymakers across countries have responded by reimagining institutions, hoping to simultaneously address fiscal challenges and new social risks as they embraced international discourses on human capital building through social investment and lifelong...
learning. But these experiments have usually failed to yield reliable answers to the re-emerging social question. In parallel with growing ‘segmentalism’ in Germany’s vocational education system (Thelen and Busemeyer 2012), the expansion of higher education has nurtured rising inequalities (Schulze-Cleven and Olson 2017), both of which are likely to undermine social mobility (Wehler 2013). German policymakers also embraced income subsidies as a way to increase employment while ensuring living standards. Yet, underlining the experimental character of polices, they soon grew wary of high costs and incentivising dumping-level pay, and eventually introduced a minimum wage instead (Mabbett 2016).

This ongoing reconﬁguration has left states with a more activist role in regulating class relations, whether in sponsoring institutional liberalisation across the economy or providing new counter-measures to offset markets’ consequences (Howell 2016). It has also lowered the redistributive effect of taxes and transfers – down by more than ten percent in Germany during the new century’s ﬁrst decade (Fratzscher 2016, 204–5). Subject to the policy-sponsored acceleration of life, contemporary life courses’ new uncertainties, and individuals’ greater accountability for potential failures, populations report feeling more unanchored and drained (Sennett 2000; Ehrenberg 2010). At the same time, policy reforms have failed to stabilise the economy for the long term. For instance, at the macro level, Europe’s contractionary macroeconomic stance threatens the ﬁscal health of the trading partners that Germany depends on (Johnston and Regan 2016; Scharpf 2018). Moreover, ongoing political resistance to activist policies domestically has increased divisions among sectors, which cannot be compensated for by the successes of German ﬁrms abroad (Carlin and Soskice 2009).

**Accumulation of social power.** A concentration in the distribution of social power is central to these broader dynamics. Focussed on long-term processes of wealth accumulation, analysts of capitalism emphasise shifts in groups’ relative material power and their effects on the strength of oligarchic tendencies across political systems. Germany’s distribution of wealth is much closer to the distribution of wealth in the United States in terms of inequality than often thought. In the Eurozone, it is the most unequal and exhibits the lowest median wealth (Fratzscher 2016, 39–44). The drivers for this are complex, but the legacy of socialism in the East, low rates of home ownership country-wide, and the existence of many – and often large – privately-held Mittelstand businesses are some of the most important factors. Moreover, in line with other rich democracies, Germany’s net private wealth has grown as a share of national income over the past half-century – effectively doubling from above two-hundred to above four-hundred percent – while net public assets have dwindled from above one-hundred percent to low positive shares (Piketty 2014, 144). Processes of privatisation and ﬁnancialisation have strongly supported this striking divergence (Krippner 2005), with returns on capital tending to be higher the greater the capital endowments, given opportunities for lower relative transactions costs and more aggressive portfolio allocations with longer investment horizons.

Crucially, the rich tend to use their material power to safeguard their wealth, including the implicit income possibilities it provides (Winters 2011). A rapidly growing ‘wealth defence’ industry – including law ﬁrms and accounting ﬁrms, insurance companies, and banks, as well as lobbyists and think tanks – provides services to reduce tax loads through avoidance schemes or political interventions (Winters 2017, 193).
In Germany, this industry’s efforts have paid off in falling tax rates for many forms of income, including wages and capital gains. Moreover, the private wealth tax was last levied in 1996. Corporate taxes were lowered, so much so that public authorities failed to collect any during 2001, and corporate tax receipts’ recent five percent share of total tax receipts significantly lags the OECD average of nine percent (OECD 2018). Assessments of inheritance tax have become regressive over time due to special rules for family-owned businesses. While the scope for some exceptions for privately held firms was narrowed in 2016 after the Constitutional Court declared their broad use unconstitutional, key provisions remain in place. Contemporary inheritance flows arguably have significant systemic effects. Not only did the annual value of bequests and gifts increase from two percent in 1960 to above ten percent of GDP in 2010, but inherited wealth as a share of private wealth also grew, from below a quarter in 1980 to roughly half in 2010 (Alvaredo, Garbinti, and Piketty 2017, 252–53).

Across countries, non-financial institutions have also become more central to the accumulation of social power as more realms of the social world are subject to capitalist expansion. In higher education, for instance, ‘world-class’ universities confer status credentials with global scope and frequently extend privilege from one generation to the next (Schulze-Cleven et al. 2017). Crucially, rich individuals’ propensity to deploy status-protecting services underwrites effective class-based collective action even without much explicit coordination.

**Multivalent Policy Feedback**

Appreciating how these systemic features of capitalism play out in any particular institutional context turns on recognising the role of policy feedback. During the past couple of decades, political scientists have emphasised the self-reinforcing properties of institutions, with positive feedback creating strong path dependencies. In the language of economics, institutional systems were seen to provide increasing returns that effectively locked in particular approaches to politics (Pierson 2000). Yet policy feedback is multivalent, and also includes self-undermining processes that can negatively affect institutional endurance (Jacobs and Weaver 2015; Dixon 2018). For instance, rather than merely providing complementarities through positive externalities, German and European institutions have long included negative side effects. Crucially, across Europe, the ratio of negative to positive externalities appears to have grown over time. Institutional constraints that once were beneficial to Germany seem increasingly to be undercutting the sustainability of policymakers’ responses to new challenges (Streeck 2009; Schulze-Cleven 2018).

Moreover, just as positive externalities across spheres can shore up a system’s stability, instability from negative externalities in one realm may destabilise others through feedback spirals, underwriting vicious circles and accelerating institutional change. For example, weakened unions are less capable of enforcing labour regulations, which encourages employers to exercise greater discretion and, in turn, further weakens unions. Importantly, feedback dynamics are not restricted to the realm of interests as emphasised in VoC conceptions, but also affect the distribution of power and actors’ ideational orientations. This leaves them central to the causal processes that variously challenge or shore up the class solidarities necessary to keep precarious working conditions in check (Doellgast, Lillie, and Pulignano 2018).
Organisational Foundations of Creative Adjustments

In ever-changing capitalism, organisations provide important resources for democratically embedding markets, whether as sites of conflict or as collective agents that construct political coalitions within and across classes (Herrigel 2015). At this point in time, scholars’ refinement of VoC frameworks cannot quite capture these crucial functions of organisations. Recent research has emphasised how national institutional constraints provide incentives and power resources for particular cross-class coalitions in the politics of liberalisation, as well as how actors’ constant testing of institutional limits contributes to the evolution of institutions (Hall and Thelen 2009; Thelen 2014). Yet, an organisation-centric perspective provides a threefold extension. First, it emphasises that actors operate in environments of overlapping structural constraints, so that they not only engage domestic political institutions but those of global capitalism as well (Streeck 2016b; Schulze-Cleven 2017). Second, because this multiplicity of institutional structures prevents any one particular institution from shaping the outlines of collective actors, the boundaries of organisations play an important role in structuring political conflict. Third, collective actors’ experimentation with institutions is a product of strategic interactions between them, which is obscured by merely focussing on one actor alone.

The shift in perspective advocated in this section – taking capitalism, policy feedback, and organisations seriously – allows analysts to appreciate both the openness and the complexity of collective action under contemporary conditions. While capitalists may exert their power despite – or even by virtue of – their disorganisation and potential collective inaction (Offe and Wiesenthal 1980; Woll 2014), opposition to market rule needs to have a collective dimension, which can take many organisational forms and engage different channels of influence. Facing deep uncertainty, actors’ ideas and reflexivity are central to innovation, as they seek to learn from their experiences in political conflict and entrepreneurially develop creative strategies (Blyth 2002; Berk, Galvan, and Hattam 2013). In turn, while many old strategies used by labour unions are as exhausted as those used by state authorities, workers and citizens have joined public officials and corporate managers to reconfigure organisations (Herrigel 2015; Le Gales and King 2017). In the process, the makeup of collective actors and their patterns of mobilisation have shifted to better represent the interests of white-collar workers and to fit the conditions of the growing gig economy (Rothstein 2019).

CONCLUSION: FROM GERMANY AS MODEL TO GERMANY AS PRISM

This article has argued that changes in institutions and practices have given rise to a political economy of imbalance in Germany. Breaking from the paradigm of stability, Modell Deutschland of decades past no longer exists, with contemporary institutional arrangements exhibiting far less coherence than equilibrium-based accounts once suggested. As companies, public authorities, and large parts of the citizenry came to embrace neoliberal approaches to tackling the economic and political challenges of post-Fordist capitalism, their actions have reduced the scope for Germany to serve as an alternative model to Anglo-Saxon short-termism. At the same time, however, they
turned the country into a productive prism for understanding processes of institutional transformation that operate cross-nationally.

Going forward, political economists can draw inspiration from historical research that refined first-generation theories of modernisation by closely engaging the political economic processes during German industrialisation. As historians delved into the German case and uncovered important commonalities with other European countries, they not only came to question the paradigm of Germany as an outlier in its path to modernity (Sonderweg), but also to highlight the inadequacy of all-too-rosy readings of bourgeois revolutions in Britain and France (Blackbourn and Eley 1984). These efforts produced a far better understanding of cross-national transformations through tighter conceptualisations of causal mechanisms (Berman 2001).

In the contemporary period, the analytical challenge is similar. Imbalances have increased in Germany as well as in other countries. Yet the rise of imbalances in Germany is particularly visible against the country’s record of stability. Much can be gained from delving more deeply into the German experience and using the findings to develop a more dynamic theory on wealthy countries’ diverging evolution since the social democratic century (Deeg and Jackson 2007).

To effectively tap into this potential, analysts will need to choose the appropriate comparative perspective. Most research on political economy today engages ‘juxtapositional’ comparisons, with scholars studying the same, or at least outwardly similar, narrowly defined phenomena and causal processes across time or geographies, often using quantitative analysis. While this approach seems to provide precision, it is also conceptually conservative and can limit the scope for revising existing explanations. ‘Perspectival’ research – anchoring comparisons of ostensibly dissimilar cases in broader categories that require the analyst to invest in conceptual innovation and properly contextualise individual cases to identify a common core (Schaffer 2019) – will likely make better use of Germany’s recent experiences for understanding contemporary cross-national transformations. Indeed, much of the most effective juxtapositional work has long relied – and will continue to rely – on the results of perspectival inquiries.

These points are echoed in recent defences of comparative area studies that emphasise the need for detailed knowledge of at least one case to formulate valid categories and make progress in theorising long-term global developments (Ahram, Köllner, and Sil 2018). Few countries have received as much focussed attention in comparative political economy as Germany. As capitalism enters a new phase in the 21st century, we can build on this wealth of existing research by training our theoretical lens once again on Germany to develop tools for understanding the next stage of economic and political development.

**DISCLOSURE STATEMENT**

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