Over the past two decades the concept of a ‘German model’ of economic organization and production has been debated hotly. In the 1980s this model was, for the most part, viewed positively, largely because German export and labour market performance was significantly better than the Organization for Economic Co-operation and Development (OECD) average. For social democrats and trade unionists the model was particularly attractive because it seemed to demonstrate that strong unions and works councils, high wages and good working conditions were not incompatible with low unemployment and economic competitiveness. Even a number of mainstream economists and management consultants became enamoured of the German model and argued for its adoption in less-well performing countries.

Most academic work attempting to understand the German model at that time attributed economic success to a particular linkage between institutions and a production system capable of creating products which were competitive with mass produced goods on world markets. For Piore & Sabel (1984), Germany’s regional economies such as Baden-Württemberg, which were dominated by small and medium-sized firms, proved fruitful ground for flexible specialization, a strategy based on intra-firm co-operation in the production of small batches of high quality goods. For Kern & Schumann (1986) the elaborate training system and co-operative industrial relations allowed for the introduction of new production concepts in traditional manufacturing sectors such as automobiles, machine tools and chemicals. These concepts, which involved a departure from the Taylorist principles underlying mass production, were based on exploiting the possibilities of new, flexible machinery by delegating more responsibilities to skilled manual workers.

In a number of publications, Streeck (1989; 1992) and Sorge & Streeck (1988) have argued that high wages and dismissal protection create constraints which are beneficial for employers, in the sense that they are forced to focus on their long-term interests rather than to respond to short-term market shocks. These constraints have helped German firms such as Volkswagen shift away from mass production to diversified Quality Production (‘DQP’), which combines the use of modern machinery with a
craft-like focus on customized and small-batch production by skilled workers. Germany’s export success with this type of production and ability to pay high wages was based on the fact that consumers in world markets were willing to pay a premium for goods which had higher quality and corresponded more closely to their particular needs. Finally, another strand of research argued that Germany’s bank-based financial system was better able to provide cheap and ‘patient’ capital to industry than the stock-market based systems in the UK and the USA, which focused on short-term results and demanded high dividend payouts (Dertouzos et al. 1989; Porter 1992). Interestingly enough, some of these authors tried to extend the analysis beyond Germany and develop a more general theory of institutions and types of production which could be applied to a large number of national cases.¹

In the 1990s, however, this virtuous link between institutions, production regimes and economic competitiveness appeared to weaken, and criticism of the German model grew both domestically and abroad. The main driving factor here was the dramatic slide in economic performance relative to other OECD countries. The USA and UK in particular enjoyed strong economic growth and a reduction in unemployment throughout the decade. Germany, in contrast, suffered its worst post-war recession in the early 1990s and has had problems bringing unemployment down below the 9 percent rate since then. Some commentators have argued that much of this deterioration is attributable to the burdens of German re-unification and the tight monetary policy followed in the run-up to the Euro (Carlin & Soskice 1997; Casper & Vitols 1997). The fact that export performance has, if anything, improved is further evidence for the competitiveness of Germany. Nevertheless, it cannot be denied that the German model appears to have lost much of its shine, and even some of its staunchest supporters are questioning its viability (Herrigel 1996; Kern 1996; Streeck 1996). In part based on a neo-liberal critique of the inflexibility and inefficiency of the institutions that were supposedly responsible for economic success in the 1980s, the social democratic-green government elected in 1998 has undertaken efforts to reform the labour market, welfare state and financial system in Germany.

What explains this drastic shift in perceptions towards the German model? Is there, in fact, a single model applicable to a wide range of industries, particularly outside the core of export-orientated traditional manufacturing? What has happened to this model in the recent past, given the reform efforts of the government and the changing domestic and international strategies of companies? At the suggestion of the editors of *Competition and Change*, a number of researchers based at or affiliated with the Social Science Research Center Berlin (WZB) and the Max Planck Institute for the Study of Sciences in Cologne were brought together at a workshop in June 2003 to discuss these issues. The papers presented at this workshop developed into the core of this thematic issue. Not surprisingly, these researchers, who for the most part specialize on different aspects of Germany’s institutions or in specific sectors, have a number of disagreements, particularly on the depth of change in and future direction of the German model. Nevertheless, something like a consensus appears to emerge from the papers on a number of key points.

- The attempts of researchers in the 1980s to characterize the German economy in terms of one type of production system, while laudable, appear to have been taken too literally in the description of reality in academic discussions. Although elements of increased training and the upgrading of products can be found in many if not most industries in the 1980s, the analyses regarding flexible specialization, new production concepts and DQP tended to focus on specific industries or even companies. The degree of homogeneity of institutions and production strategies across and even within industries is, thus, less pronounced than some researchers applying these paradigms have claimed.
In the 1990s there has been an important and undeniable shift in the behaviour of some key actors, including both companies and political parties. Many companies, including those that were exemplary of the German model, have modified or even abandoned the production strategies they pursued in the 1980s. One aspect of this is the increasing internationalization of companies in order to exploit the comparative advantages of different production locations and to reduce vulnerability to shocks such as changes in the exchange rate. Another aspect of this is the shift in demands made on the state and support for different aspects of the institutional infrastructure.

The increased influence of the Anglo-American model on companies and in politics cannot be denied. Perhaps the strongest example of this is the attempts to reform the financial system and corporate governance to strengthen the stock market and company performance. At the head of this movement have been a number of large companies such as the Deutsche Bank, Daimler Benz (now DaimlerChrysler) and Hoechst (now a part of Aventis). Nevertheless, it is a mistake to generalize from these cases to the whole private sector. German companies are quite divided between ‘Anglophiles’ and ‘traditionalists’, and it has been quite difficult to form consensus on important reform issues.

Although there have been important changes in key institutions in Germany, such as the financial system and the labour market, the debates on ‘divergence versus convergence’ have not advanced our understanding of the process of change very far. Important continuities persist within the German system, and concepts like incremental change, path dependence and the adaptation of foreign and international practices to local conditions are more useful for understanding this process of change and transformation.

The individual contributions to this thematic issue develop these points in much greater detail, looking at changes in Germany from a variety of angles. The first perspective focuses on elements of the institutional infrastructure in Germany, including financial markets, corporate governance, the labour market and venture capital. A second perspective looks at changes from the point of view of specific sectors, including the automobile industry, discount grocers and software. A final perspective examines the behaviour of German companies abroad and whether the ‘German model’ is being exported.

The article by Höpner and Krempel makes the strongest argument for deep change in the German model. It focuses on what has been called ‘Deutschland AG’ in Germany, i.e. the close shareholding and boardroom links between most large companies in Germany. The authors argue that these close links played an important role in history, particularly in helping companies overcome economic crises and in protecting companies from hostile takeovers (particularly from foreign companies). Nevertheless, Deutschland AG is not an invariable ‘genetic’ part of the German institutional infrastructure. It emerged in a series of waves starting in the industrialization period as a result of both the self-interest of companies and the active support of the state. The contrast with the USA, where state policy at an early stage was directed against cartels and collusion rather than encouraging it, could not be more stark.

The analysis of the build-up of the inter-company links in Deutschland AG helps lay the groundwork for the argument that the network is dissolving, with serious consequences for company behaviour. On the one hand a number of key actors, particularly the large banks and insurance companies at the centre of the network, have lost interest in maintaining the large shareholdings and dispatching representatives to company boards. The large banks in particular wish to shift away from corporate lending activities to the potentially more lucrative area of investment banking. Close links with companies are a disadvantage in this area, particularly when trying to avoid the conflicts of interest which may arise
during hostile takeovers. On the other hand the social democratic party, the dominant party in the government coalition that took power in 1998, is also interested in dissolving the network and has passed legislation encouraging this process. As a result the density of the network has decreased substantially since 1996. The authors suggest that the increased threat of hostile takeovers has an undeniable effect on company behaviour in Germany.

The second article in this issue, by Sigurt Vitols, starts from these changes in ownership as given and focuses on their implications for corporate governance and company behaviour. The corporate governance literature, particularly that written by microeconomists, has generally analysed countries in terms of two models of corporate governance: the shareholder or ‘outsider’ model found in countries such as the USA and UK, and the stakeholder or ‘insider’ model found in countries such as Germany and Japan. The predominance of this two-model approach has forced participants in the debate on the nature of change in corporate governance systems to take the position that countries must choose between one or another of the systems (‘convergence or divergence’).

The argument made in the article is that this framework is too rigid for doing justice to the situation in Germany. It is true that banks have reduced their shareholdings, as Höpner and Krempel have shown. However, it is incorrect to claim that this trend has led to the exit of other stakeholders from the stakeholder coalition influencing German firms, including large strategic shareholders (such as founders/families, other companies and the state). Thus, it appears that institutional investors, such as mutual funds and pension funds, are being drawn into a modified stakeholder coalition surrounding firms, rather than driving out other stakeholders. The article goes on to discuss a number of variables that indicate that German companies have adopted a more ‘moderate’ form of shareholder value than the variant practiced in the USA and UK. This reflects the continuing influence of the traditional stakeholders, despite increased pressure from institutional investors.

The article by Katrin Vitols takes a look at one of the key areas for reform in Germany, namely the labour market, which has been based on corporatist regulation (i.e. state-supported collective representation of interests through employers’ associations and trade unions). As discussed at the beginning of this introduction, a number of political economists have argued that the type of high quality production undertaken in Germany is dependent upon (at least some parts of) the highly regulated labour market. At a minimum, the training system, under which almost two thirds of young Germans complete an official apprenticeship programme of up to 3½ years, has been seen as a crucial for helping upgrade skills on a broad basis. In contrast with industrial relations systems based on fragmented and/or political trade unions, the German industrial relations system is based on a balance between plant-level works councils and sectoral-based trade unions. Although labour representatives in this system have been, for the most part, pragmatic and co-operative, nevertheless it has been based on defending the standard employment relationship, i.e. full-time work with an unlimited contract, performed mainly by men.

However, the predominance of the standard employment relation has come under increasing attack for being too rigid and costly, thereby allegedly contributing to the problem of stubbornly high unemployment. One solution proposed, which has widespread support, is to encourage the use of non-standard employment, such as temporary agency work. In fact the social democratic-green government, which came into power at the federal level in 1998, has taken a position in favour of encouraging temporary agency work and other forms of non-standard employment. However, an attempt to get the social partners to agree to reforms in the context of the tripartite Alliance for Jobs, Training and Competitiveness failed. Subsequently, the government established an independent Commission (the ‘Hartz Commission’), which developed a far-reaching agenda to transform not only the Federal Labour Exchange but also the substantive regulation of
temporary agency work. The failure of the Alliance for Jobs, and the passage of legislation on the basis of recommendations by the Hartz Commission, have led to claims that the corporatist governance of the labour market is dead. However, the article argues that, although corporatist institutions face difficulties in agreeing radical reforms, the government’s insistence that collective bargaining be extended to the temporary help sector shows that corporatist governance continues to play a useful and important role in Germany. The fact that the ‘German model’ of social partnership has been extended to cover an important form of non-standard work is indicative of the resiliency of this model for the future.

In the fourth article Engelhardt analyses a major attempt at transforming Germany’s manufacturing-based ‘old economy’ through public programmes to stimulate venture capital and the creation of the ‘Neuer Markt’, a special stock market segment modelled in part on the US Nasdaq. Although more than 300 companies listed on the Neuer Markt during its brief existence (from 1997–2003), many of these backed by venture capital, the experiment cannot be characterized as a success. Reasons for this include the public scandals and the crash in stock market prices which eventually forced the Frankfurt Stock Exchange to close the Neuer Markt. However, a more fundamental reason in the long term is that these efforts did not appear to encourage the emergence on a large scale of the type of entrepreneurial companies that one finds in the new emerging industries in places like Silicon Valley.

This conclusion is based on an examination of the approximately one hundred software companies that listed on the Neuer Markt. First of all, the companies that were successful tended to display a number of characteristics typical of Germany’s Mittelstand (the traditional SME [small and medium size enterprise] sector) and were active in established software sectors, rather than in radically innovating sectors such as internet software. Secondly, econometric analysis of these companies shows that German venture capital firms were not able to select software companies that performed significantly better than other listed companies. Engelhard leaves unanswered the question of whether this is attributable to the inexperience of German venture capitalists or due to the inherent hostility of the institutional environment to radical innovation on the Silicon Valley model. Nevertheless the conclusion regarding the difficulties of fundamentally transforming Germany’s industrial structure is a striking argument for continuity.

In the next article Jürgens re-examines the strategies of automobile companies in Germany since the 1980s. This is significant since the automobile industry was considered by many to be the flagship sector for the German model of production. The article outlines a much broader and differentiated understanding of the industry than is found in many accounts. First of all, DQP was not explicitly and, in fact, only partially and gradually implemented by the automobile producers in the 1980s. Although training efforts were expanded massively and the proportion of skilled workers in the workforce increased dramatically, these efforts were actually undertaken in anticipation of the extensive use of fully automated, computer-integrated manufacturing (CIM), rather than on the type of skilled-worker based neo-craft production emphasized by Piore & Sable, Kern & Schumann and Sorge & Streeck. When CIM proved not to work, a reversion was made to assembly line techniques rather than to the type of worker-based experiments in production undertaken in places like Sweden. Secondly, the number of models and model variants expanded only gradually over the 1980s, rather than showing a quantum leap that one would expect with the introduction of a fully new production paradigm. DQP thus only partially explains the situation in the automobile industry in that decade.

Similarly, the strategies of automobile producers since the crisis of the early 1990s can neither be explained as a full acceptance or the total rejection of DQP principles. Instead, an
emphasis on high training efforts and a high skill level is combined with a number of other initiatives, including outsourcing more production to suppliers, spreading the value chain to lower-cost production locations, such as Eastern Europe and boosting the use of white collar workers, particularly in research and development. Although the automobile producers successfully adapted to the early 1990s crisis and have expanded their share of world markets, one cannot say that this was the result of finding a 'successful formula' for production. Rather, car companies must continually experiment with new practices, each of which are only one of a number of components in an integrated strategy. Furthermore, the fit between national institutions and company strategies is not as tight as some would argue.

An analysis by Wortmann of a sector rarely studied by advocates of the German model – discount grocery stores – provides a further channel to the idea that there is a tight fight between national institutions and successful competitive strategies. The type of labour relations and product strategies in grocery retailing deviate quite substantially from the stylized German model based mainly on the manufacturing experience. Unions and works councils are only weakly represented in the sector and workers generally do not complete an apprenticeship. In contrast with the DQP strategy, the product policy of the discount grocers, particularly the hard discounters like Aldi, is to offer a limited range of goods with little or no service. Nevertheless the hard discounters have been highly successful both in Germany and abroad and have been expanding market share. It is, thus, clear that DQP is not the only strategy that German companies can pursue successfully.

Furthermore, the discount grocers emerge from another set of institutions which can also be considered very German, namely the ownership structure and set of regulations supporting the Mittelstand (i.e. family-owned SMEs, in many cases in the context of a purchasing or marketing co-operative). The emergence of companies like Aldi must also be seen in the context of industry-specific actions, many of which have unintended consequences. In this case the development of discount grocers was encouraged by spatial regulations designed to protect traditional Mittelstand stores from competition by suburban superstores.

In the final article Dörrenbächer tackles the important question of the effect of the internationalization of German companies. One aspect of this is the employment effects of internationalization within Germany. Although it is frequently claimed that the inflexibility and highly regulated nature of the German production location has led to the mass export of jobs, Dörrenbächer claims that there is little or no evidence for this view. Rather, according to his estimates, the number of jobs exported abroad have been insignificant compared to the massive rise in unemployment in the past two decades.

Regarding the behaviour of German companies abroad, however, the article is less optimistic regarding the resiliency of the German model. In a study of direct investments in Hungary, Dörrenbächer finds that German companies are exporting their production model completely or almost completely. However, the system of labour relations is being exported only very selectively. The implication of this is that, even if the production model is successful, there is little chance that the German system of social partnership will be exported abroad through the behaviour of German companies alone.

All in all the articles provide a detailed examination of developments in German institutions and sectors and, thus, contribute to the debate on the existence and future directions of the German model. One the one hand the idea of a ‘national model’ as an ideal type is supported as a useful tool for analysis. On the other hand these ideal types should not be confused with the real structure of economies. Above and beyond this, however, the issue attempts to shed some light on the complex process of change in countries, an endeavour we hope we have, at least to some extent, succeeded in.
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Notes

1 Although appearing much later, Hall and Soskice (2001) have taken this line of reasoning the furthest and argued that that there are two types of advanced capitalism. Germany is exemplary of co-ordinated market capitalism, which involves a high degree of co-operation between firms, while the USA and UK are paradigmatic of liberal market capitalism, which is governed much more by markets.

References
