The vulnerability of an export champion - Upheaval in the German employment model

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INTRODUCTION

The current crisis has given a blow to all existing "varieties of capitalism" (Hall and Soskice 2001) whose stability has already been subject to an intensifying debate over the past few years (Coates 2005; Streeck and Thelen 2005; Hancké *et al.* 2007). Distinctive flagships of both "liberal" and "coordinated" market economies such as the UK and Germany have been hit with similar vigour. The German case may be particularly surprising in this respect as over the past few years, Germany has given the picture of regained economic dynamism as a revitalized export champion which appeared to be hit by the financial crisis from abroad, and whose economic success over the past few years was not based on the speculative bubble which gave rise to the current turmoil in the world economy. Contrary to these widespread perceptions, the present paper highlights the contradictory nature of contemporary German capitalism, in particular the making of an increasing vulnerability of its employment model, i.e. the institutions which shape the employment relationship. It is based, within the framework of a comparative EU funded project (www.dynamoproject.eu), on qualitative research into the "dynamics of national employment models" in nine European countries (Bosch *et al.* 2009, Lehndorff *et al.* 2009). While the latter publication draws a more comprehensive picture of the interaction of a wide array of institutions within the process of upheaval in the German employment model, the present paper is focused on the importance of the industrial relations system to this change.

THE PRIME YEARS OF THE GERMAN MODEL

For most of the 1960s to 80s, the Federal Republic of Germany was regarded both at home and abroad as one of the countries that had been particularly successful in combining economic growth and social equality. Twenty years ago, on the verge of its prime, the essence of the 'German model' could be characterised as a combination of economic dynamism and low social inequality. The high value approach adopted by German manufacturing industry, fostered by long-term relationships within capital and between capital and labour, benefited the wider German society through generalising institutions such as the collective bargaining system, labour law and the welfare state.

The industrial relations system as one key pillar of the model was characterised by sector-wide collective agreements which were concluded between strong trade unions and employers' associations. As a result, the only way firms, including the export-oriented manufacturing sector, could obtain competitive advantages was by improving quality and efficiency. For this reason, specialisation in high-quality, high-value products became a question of survival at an early stage. Works councils provided a separate channel of workers' interest representation, based on general elections within establishments. The division of labour between these works councils with their codetermination rights with regard to hiring, dismissals, training, or overtime work on the one hand, and the unions on the other, constituted the institutional basis of a 'conflictual partnership' (Müller-Jentsch 1991) between labour and capital.

Both in the self-perception of major actors in Germany and in the analysis of scholars interested in the distinctive features of this exemplar of 'Rhenish capitalism' (Albert 1992), the institutions in the manufacturing sector were assumed to represent the whole of the system. True, the implicit assumption that the institutions and configurations of actors observed in manufacturing were typical of the system as a whole did have a certain validity until well into the 1980s. This becomes clear if the economy is divided into three segments, which can be designated ‘production’ (including manufacturing, construction, research and development, financial and other business services), ‘consumption and distribution’ (including trade, hotels and restaurants, transport, telecommunications) and ‘provision’ (including public administration, utilities, education, health and other social services) respectively. The links between these segments, and within each of them, were particularly strong (Table 1).

Table 1: Regulation of the segments of the German employment model in the 1980s

Area of regulation	Segments: Production	Consumption and distribution	Provision
Governance	Stable ownership by banks / “patient capital”	State ownership of public transport and utilities	State ownership or strong regulation by the state
Industrial Relations	Industry–wide collective bargaining Co-determination laws Extension of collective agreements Pattern wage agreements Predominance of collectively agreed sector standards over firm-level agreements		
Training	Dual system of vocational training		
Employment	Decommodification through employment protection in labour law Labour market policy and public tenders respected collectively agreed wages High unemployment benefits, active labour market policy concentrated on retraining and workcreation schemes		
Welfare system	Decommodification through mandatory welfare system (health, old age, accident, unemployment) Welfare system oriented to male breadwinner (income splitting taxation, subsidies for marginal part-time jobs, derived entitlements in health and old age insurance schemes, half-day school and cash benefits for children instead of childcare provision)		

Source: own representation

At the beginning of the present crisis, however, after more than a decade of turmoil, the German model was characterised by a dynamic manufacturing industry amidst institutional and social disintegration. Important elements of its core institutions have either been changed gradually but substantially or are suffering a lack of support from major actors and have become subject to controversy.

CRISIS AND UPHEAVAL

The first cracks in the German employment model became visible at the end of the ‘golden age’ of post-war capitalism. In key areas of manufacturing, growth prospects were increasingly restricted by the intense competition in world markets, in particular from Japan, where quality and diversity were delivered at much lower cost than in Germany. The need to respond through radical innovations in work organisation designed to make better use of the potential of skilled workers was widely neglected. What made things even worse was the delay in developing the service sector as a counterweight to the diminishing potential for employment growth in manufacturing. As in many other Western industrialised countries, there emerged influential calls for a radical market or neo-liberal approach. Although the neo-liberal critics of the German employment system were unable to achieve welfare state cutbacks on the scale they were demanding, at the same time its defenders were equally unable to initiate a new wave of reforms that could have brought the known strengths of the German system into play more effectively. It was not until German unification that the balance of power changed substantially.

The economic shock of the 1:1 conversion of the East German currency into Deutschmarks turned large swathes of the East German economy uncompetitive over night. A process of extensive deindustrialisation got under way within a very short period of time. Given the high level of unemployment, East-Germany turned into a "dependency" or "transfer economy" (Hickel and Priewe 1994), imposing a rapidly increasing strain on public and social security budgets that helped to undermine the trust in the viability of the German social security system in large parts of the published opinion. Furthermore, the only institution whose transfer from West to East Germany failed was the collective bargaining system. In the course of the rapid privatisation process, it became obvious that this crucial element of the old German model had not taken root in the Eastern part of the country. While it was primarily the large West German manufacturing companies that stuck to industry-level bargaining, these were small in number compared to the small and medium-sized West German outsourced subsidiaries and home-grown small East German firms, the bulk of which either left the employers' associations or did not join them in the first place.

Thus the shock of German unification and its economic and political consequences triggered a rapid change in the political climate. The political and economic elites, along with key opinion formers, now shared the belief that the only way of solving Germany's problems was to adopt the harsh prescriptions of neo-liberalism. These were held to include restricting the earnings of the vast majority of workers, cutting back on welfare state benefits and government expenditure as a share of GDP, and deregulating the labour market, giving priority to company-level arrangements geared to undercut industry-wide collective agreements. The prevailing wisdom among mainstream politicians – more or less explicitly stated – was that the main pillars of the German model, and in particular the welfare state and the 'conflictual partnership' of the industrial relations system, had to be weakened if the economic dynamic was to be strengthened and employment increased.

Until the beginning of the second half of the present decade the German employment model had been changed substantially. The long-term strategic planning and cooperation that marked the old 'Germany plc' and that were key characteristics of the entire German employment system had been being pushed backby a concern with short-term returns. The change in corporate governance was being driven by two developments in particular: the increasing importance of the financial markets and shareholder value in the production segment and the privatisation of publicly-owned enterprises and their organisational principles in the consumption and provision segments. Both trends had been provided with powerful tailwind by various government initiatives.

In the labour market, too, major structural changes had taken place as a result of persistently high levels of unemployment. As in many other countries, precarious employment relationships such as agency and temporary work and fixed-term employment have increased over the fairly long term. One German particularity, however, is the boom in marginal part-time jobs for which the German tax and social security system offers considerable incentives (so-called mini-jobs). This segment now accounts for around one fifth of all employees and has made a considerable contribution in recent years to the development of a low-wage sector (Bosch and Kalina 2008). The increase in precarious employment relationships and the dynamic of the low-wage sector were given a decisive boost by the labour market reforms introduced by the SPD-Green coalition government, the core purpose of which was to increase the pressure on the unemployed to accept job offers. This was to be achieved by simultaneously reducing benefit levels and strengthening controls and sanctions. This shift of emphasis applies to the centrepiece of these labour market reforms, namely the restriction of entitlement to unemployment benefit to one year. Anyone remaining unemployed for more than a year now receives a means-tested flat-rate benefit roughly equivalent to what used to be known as social assistance. As there is no entitlement to this flat-rate benefit until personal savings above a defined threshold have been spent, people who may have paid insurance contributions for 30 or even 40 years will lose the bulk of their savings as a result. Thus, for the long-term unemployed, the income-linkage principle of the German unemployment regime has been replaced by a means-tested poverty relief principle, which represents a paradigmatic shift within the German welfare regime (Knuth 2007).

Finally, the government's drive to consolidate the national budget and reduce non-wage labour costs gave rise to various 'welfare state reforms'. Unemployment was causing the number of benefit recipients to rise relative to the number of people paying contributions, the austerity policy was reducing the scope for benefits funded out of taxation and the reductions in social security contributions that are regarded as a necessary part of economic policy mean that revenue flows were also reduced. One example of this approach was the pension reform which cut pension benefits while fostering individual savings. At the same time, and despite the financial squeeze, the conservative nature of the welfare state (Esping-Andersen 1999) is being reproduced by ongoing financial support for the male breadwinner family.

Thus, government policy had fostered "a hardening of the division between the core labour system in the advanced sector of the economy and the 'outsider' labour system with a less supportive welfare state and weaker protective labour market institutions in low skill sectors" (Carlin and Soskice 2007: 3). But the dualism has gone far beyond sectors: it includes fragmentations within sectors, including the export industries, and increased job insecurity within the core labour system itself. The links and interdependencies that held the system together in its prime years have been substantially weakened (Table 2).

Table 2: Changes in the German employment model by employment segments

<table>
<tr><th></th><th>Production</th><th>Consumption / Distribution</th><th>Provision</th></tr>
<tr><td>Governance</td><td>Changes in ownership structures and role of banking system and increasing importance of shareholder value orientation
Challenges to links between high- and low-added-value segments of the production chain
Outsourcing of business services into areas with weaker regulatory standards</td><td>Privatisation of post/telecoms and parts of public transport
German Railways AG (plc) floated on stock market
Increasing importance of tendering in local transport
Pressure on labour costs through low-price competition in distributive services</td><td>Privatisation trend in health and elderly care
Cost cutting pressures in health and elderlycare in conjunction with governance strategies borrowed from private businesses
Staffing cutbacks in public services and clash over collective agreements</td></tr>
<tr><td rowspan="2">Industrial relations</td><td>Industry-wide collective bargaining in manufacturing maintained but traded against decentralisation and growing number of derogations
Agreement on fundamental reform of status and pay in metal and engineering sector</td><td>Industry-wide bargaining in largest private service industry (retail trade) 'on the point of collapse'</td><td>Break-up of association of public employers
Major reform of pay and employee status structures in public services</td></tr>
<tr><td colspan="3">East-West gap in coverage and binding character of collective bargaining
Challenges to predominance of collectively agreed sector standards over firm-level agreements in various manufacturing and service industries
Demise of extension of collective agreements except for construction</td></tr>
<tr><td>Training</td><td colspan="3">Dual System of vocational training modernised but increasing reluctance to provide vocational training among employers in some industries</td></tr>
<tr><td>Employment</td><td colspan="3">Persistent decommodification of labour through employment protection in labour law but blurring of standards at fringes of labour market
Improved opportunities for electing works councils in smaller establishments
Labour market reforms drive jobseekers into low wage jobs far below collectively agreed wages
Public tenders do not always respect collectively agreed wage rates</td></tr>
<tr><td>Welfare system</td><td colspan="3">Persistent decommodification of labour through extensive social security coverage but cuts in benefits
Continuing male breadwinner orientation of tax / social security system in spite of gradually improved child care provision and modernised parental allowance
Subsidies for marginal part-time work extended</td></tr>
</table>

Source: Own representation

INDUSTRIAL RELATIONS IN THE PROCESS OF FRAGMENTATION

The turn of the political tide proved to be particularly harmful for the trade unions. They lost significant numbers of members and a considerable part of their influence, which drove trade union density from about 29 per cent in 1995 to roughly 20 per cent in 2004, which is below the EU-25 average (European Commission 2009). Within a very short period of time, the unions found themselves cornered. On the one hand the government and central bank refused to countenance any expansionary macroeconomic strategy to address high unemployment rates and sluggish growth in both parts of the country. On the other hand they also faced an onslaught on their control at the workplace, with a fierce cost-cutting approach from big business intent on regaining their international export leadership and an increasingly beleaguered system of collective bargaining in both parts of the country. Symptomatically, from 1997 to 2006 real compensation per employee rose by no more than 0.7 per cent per year, which is among the lowest rates in the EU (European Economy 2007).

The most striking indicator of the upheavals in the industrial relations system is the decline in coverage by collective agreements, triggered by the declining membership of the employers' associations which is indissolubly linked with the haemorrhaging of members from the trade unions. In 2006, 63 per cent of German employees were covered by collective agreements, out of which 54 per cent were industry-wide and 9 per cent firm-level agreements. From 1998 to 2006, the share of employees covered by collective agreements dropped from 76 per cent to 65 per cent in Western Germany, and from 63 per cent to 54 per cent in Eastern Germany. As small firms are underrepresented in the employers' associations, the shares of firms covered by collective agreements in 2006 are much lower, namely 40 per cent in Western and 24 per cent in Eastern Germany (Bispinck 2008).

It is not only coverage by collective agreements that is diminishing, but also their power to shape the regulation of working conditions. Decentralised bargaining which, in the prime years of the German model, used to yield extra pay beyond industry standards, has crossed the divide and has lead to the payment of wage increases below those agreed at sector level. As trade unions have taken major efforts to increase internal coordination and to intensify their activity at the work place, the momentum of decentralized concession bargaining has slowed down while the overall erosion of the collective bargaining system has not so far been stopped (Haipeter 2009; see also the paper of Haipeter at the present conference).

Differences in pay and working conditions between industries and segments are growing. Union influence is highest in industries exposed to globalisation pressures, and much weaker in industries dependent solely on the internal market or public budgets. While the collective bargaining actors in the core manufacturing industries have managed to agree wage increases slightly above inflation rates, real wages in large areas of the public and private service sectors are stagnating or even falling, due largely to the blocking of negotiations over long periods, for example in retail. Moreover, in growing low-wage sectors, such as food processing, there are virtually no associations on either side in a position to negotiate and powerful capital groups in outsourcing markets such as call centres and former monopoly markets such as mail services are actively fostering competition based on low wages. Between 1996 and 2004, average labour costs in the private service sector dropped from 83 per cent to 78 per cent of those in manufacturing, which is the largest gap among EU countries (Horn *et al.* 2007). With real wages stagnating in manufacturing and falling in parts of the service sector, both the wage moderation in core areas of the collective bargaining system and the crisis of that system in large areas of the service sector contributed to the decline in Germany's unit labour costs relative to the Euro area by almost 10 per cent between 1999 and 2006, as computed by the ECB (2007: 64).

Given the crisis affecting both the trade unions and the employers' associations, the lack of institutional defences in the German industrial relations systems against outsiders intent on undercutting collectively-agreed labour standards becomes decisive. Even worse, the scant defences that once existed have been demolished by political intervention. Firstly, at the instigation of the employers' associations, the state has virtually given up using its power to declare collective pay agreements generally binding. Secondly, the privatisation of publicly-owned companies and competitive tendering for public services have given rise to competition between companies bound by collective agreements and those not so bound. Thirdly, as a result of budgetary pressures, bargaining structures in the remaining areas of the public sector are becoming fragmented. It is only recently and in a very limited number of industries that minimum wages have been extended by the Federal Ministry of Labour, while the introduction of a general statutory minimum wage remains, for the time being, a highly controversial issue in public debates. In consequence, wage dispersion in Germany, which had started to increase in the 1980s at the upper end of the wage scale, increased at the lower end in the course of the 1990s and is now above the EU average and approaching the UK rate (OECD 2007).

EXPORT CHAMPIONSHIP AMIDST INSTITUTIONAL AND SOCIAL DISINTEGRATION

The nature of the changes in the German employment model can no longer be captured by focusing solely on the export-driven manufacturing industries. German companies' success in their export markets, which was reflected in the all-time record net contribution exports made to GDP in 2008, has brought the contradictory nature of the new German employment model increasingly under the spotlight. It is true that the high-skill, high-quality productive system at the heart of the German employment system has exhibited impressive regenerative capacities. The development of a German form of lean production, which has benefited from the specialist qualifications of large parts of the labour force, and the restructuring and internationalisation of the value-added chain have contributed to this revitalisation of the export machine.

However, this renewed success model has proved to be vulnerable in several respects. It has exposed the German economy not just to the ups, but equally to the downs of its export markets which make it part of those EU countries which are suffering most from the current crisis. Further, the process of corporate 'slimming down' is not sustainable in the long run, given its inherent risks for human resources, flexibility and innovation potentials. A third fundamental problem is the way in which the export machine is embedded in the other sectors of the economy. One key aspect here is the pressure on labour costs, on which business attention has been increasingly focused. The radical restructuring of the production model has been closely intertwined with the exploitation of increasingly fragmented labour relations. The labour input to high value production has become heterogeneous, and now includes larger shares of precarious labour. The labour market reforms of past years have added to the rise in social inequality and to a widespread perception of job insecurity, while tax reforms have limited government's capacities to compensate for the weakening of employment growth potential beyond the export machine.

This fragmentation, in turn, has become the Achilles heel of the employment model as a whole. In contrast to the prime years of the German model, the basic mechanisms for disseminating the benefits of export success throughout the wider economy and society, which were rooted in the industrial relations system and the welfare state, have been damaged or partially dismantled. Stagnating wages and increasing shares of low-wage and precarious employment provided a weak basis for domestic growth.

The trend towards the 'financialisation' of capitalism tended to squeeze out 'patient capital'. This change in the economic structure has created a strategic challenge for policy makers; the less corporate governance structures encourage the leading actors to adopt behaviour oriented to the long term, the more important counterweights in labour market and welfare state institutions become, at national and, above all, supranational level.

It was already before the current crisis evolved that German policymakers were faced with challenges that are difficult to meet. Is the state to invest more heavily in social services and, in doing so, will it, both as regulator and employer, establish the basic conditions determining the extent and quality of provision or will they seek to gain public acceptance for a growing polarisation in provision between good services for the few and poor services and poor working conditions for the many? If the collective bargaining system becomes fragile and the associations themselves lack the power to renew the system on a country-wide basis, is the state to introduce a national minimum wage, or leave it to the self-regenerating forces of the actors in collective bargaining to prevent an even further expansion of the low-wage sector entailing a boost in poor relief?

It is fair to assume that today's dual and interlocking crises of the financial system and the world economy put an enormous additional pressure on major actors to resolve these problems of the German employment model. It is not only that the search for a new balance between government action and the self-organising forces in the industrial relations system will be essential for fighting back the increasing social inequality. At the end of the day, the success or failure of trade union revitalisation will prove to be the crucial factor behind the emergence of this new balance.

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