

Ageing Model

Herbert Giersch, Karl-Heinz Paqué and Holger Schmieding, The Fading Miracle: Four Decades of Market Economy in Germany (revised edition), Cambridge University Press, Cambridge, 1994

Reviewed by James Cox

THEY order, said I, this matter better in France.' So observed Lawrence Sterne in 1768. Policy-makers in fairly small and isolated economies such as Australia and New Zealand naturally keep an eye on developments overseas. Equally natural is the hope that somewhere there is the good model: the economy whose example we should follow because they have got it right.

International organisations such as the OECD have done a good deal of work to develop economic statistics that can be compared between countries. It is now quite easy to learn how Australia compares with other countries in terms of unemployment, inflation and economic growth. But such comparisons, important though they are, can take us only so far. They describe the results of the choices made by private and governmental agents but not the habits of mind, institutional arrangements and debates about policy that lead different countries to take different courses of action. One must therefore welcome the appearance of a series, titled 'Cambridge Surveys in Economic Policies and Institutions', which aims to enable readers to 'grasp the influence of economic ideas on the real economy' by 'examining policies in a detailed yet accessible manner'. *The Fading Miracle* is a member of this series.

Germany has often been considered to be the good model because of its low inflation and large current-account surpluses, and because it is an exporter of high-quality manufactured products. The authors, however, offer a more sceptical assessment. By the late 1980s,

there was no longer any doubt that the German miracle had faded away in every relevant respect and that, economically, West Germany had become 'just another part of Europe', with its fair share in all positive and negative characteristics of the old continent. In terms of its stability orientation — both fiscal and monetary — it remained ahead of most other EC countries, although the difference had greatly narrowed in recent years; also, the unemployment balance looked slightly better than elsewhere, though by itself clearly not satisfactory. Yet in terms of growth dynamics, West Germany had become a laggard and was widely perceived as remaining so for quite a while. (p.275)

Prospects for economic growth in Germany have, so the authors believe, improved somewhat since the late 1980s because of a higher rate of return on capital, some

modest supply-side reforms, the completion of the EC's single market and the opportunities provided by the integration of East Germany in particular and (perhaps) Eastern Europe more generally into the wider European economy.

The authors' account has three main aspects: a description of economic events in Germany from the misery of the post-war period to the problems of reunification in the 1990s; a synopsis of German debates about economic policy and a description of the institutional context within which these debates took place; and (most controversially) an interpretation of the fading miracle in terms of free-market economics.

The chronicle of economic events is coherent and cogent, and superbly done. Considerable attention is paid to developments in Germany's external trade and international transactions as well as to domestic developments. As so often when reading historical accounts, I was struck by how easily events could have turned out differently. Two examples must suffice. Germany might have followed democratic socialist rather than free-market economic policies in 1948 but for a number of unexpected events that brought Ludwig Erhard into office. And the German government might have had the chance to deregulate agriculture in 1948 but decided instead to implement complex programs for stabilising domestic prices. High levels of support for German farmers were then carried forward into the EC's Common Agricultural Policy.

The presentation of the economic debates and the institutional setting in which they take place makes the important point that these have not remained unchanged. Of particular importance was West Germany's unilateral liberalisation of its external trade during the 1950s; the evolution of European institutions and a common external tariff for the European community from the 1960s; and German reunification from 1989. At times an Australian reader can only wonder at the civility of German economic debate. For example, the West German parliament passed a law in 1963 to establish an independent Council of Economic Experts. 'Unlike its American counterpart . . . it was designed as an advisory board independent of the government, so that a critical attitude towards the prevailing policy did not constitute a violation of its duties'. Moreover, 'Karl Schiller — Minister of Economics from late 1966 and himself a prominent economics professor — was ready to engage in a long standing constructive dialogue with the Council of Economic Experts' (p.39). An independent central bank was established by the Allies in 1948 against the wishes of many German experts.

The authors address a larger question in conjunction with their discussion of events and institutions. They argue that:

Not only the miracle, but also the fading of the miracle provides important lessons. Corporatism and bureaucracy are strong forces, leading potentially everywhere to a politicisation of economic life. For a while, they may held back or brought into the service of rapid market growth where people or the public can be made to believe that distributional quarrels will close growth opportunities to the detriment of all, eventually leading to a zero-

sum society. But politicians, bureaucrats and leaders of corporatist organisations have too short and too partial a view to meet the concerns of market-oriented economists. Not doubt, the narrow interests of the practitioners of the corporatist system will often gain the upper hand, so that the economy is bound to slow down under the impact of mounting regulations, and higher taxes, rising costs and shrinking profit margins. (pp.xi-ii)

Whereas West Germany enjoyed faster economic growth than France, Italy and the United Kingdom during the 1950s, the German growth rate was below those other countries' during the 1980s. The true German miracle occurred during the 1950s when the economy was able successfully to absorb a supply of well-trained surplus labour. Expansion of the economy was assisted by trade liberalisation (which reduced inflationary pressures and enhanced the supply potential of the economy) and by a surprising degree of wage restraint by unions. By the mid 1970s, 'supply-side conditions had drastically worsened because of a wage revolution, an oil price hike and a creeping but sustained government growth. Thus, a good part of the temporary stagflation and chronic lack of growth which followed may have had their roots in earlier times' (p.163). These factors, and high real interest rates, resulted in a slow pace of capital formation after 1973. By the 1980s the German economy was required to adjust to increased competition from newly industrialised countries. Such adjustment was made more difficult by protectionism, worsening industrial relations, subsidies to ailing industries, undue regulation of the service sector and a fairly rigid labour market.

There was, as the authors point out, no shortage of warnings at the time by pessimists about the possible adverse consequences of these developments for German economic growth. It is, however, not possible to prove that things would have gone better for the German economy had different policies been followed; all one can do is to observe the historical record. The authors' large theme is therefore likely to remain controversial. Nevertheless, they have, I believe, succeeded in providing from the free-market perspective a coherent account of the causes both of rapid economic growth in West Germany during the 1950s and of the subsequent slowdown. It remains to be seen whether an equally sophisticated account can be provided from another perspective, such as a Marxist one. If such an account does exist, the authors do not mention it.

Finally, what can the Australian or New Zealand reader learn from this account of debates and developments far away? Clearly, Germany occupies a different place from Australia and New Zealand in the international division of labour. Nevertheless, beneath the surface success, the Germans are learning to deal with problems that are not so very different from our own. Although there is no German model which, if followed, will guarantee success, the efforts of Germans to address their economic problems will continue to deserve our sympathetic attention.

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