# ANALYSIS AND INFORMATION

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# Social Consensus and International Competition

## — A German View —

By
Michael Dauderstädt

Bonn 1983

# Preface

In September 1981, a plain advertisement by the "Deutsche Bank" appeared in the German newspapers in which could be read, under the headline "Competition": "Competitiveness is of essential importance for all enterprises, for all sectors of the economy and for all national enonomies. In the end it determines growth, employment, the price-level, and our position in foreign trade; it is the pre-condition and the prerequisite for the maintenance of our system of social security.
The Federal Republic of Germany owes its prosperity and social peace to the fact that it has been competitive – both nationally and internationally – for more than two decades . . .
Today, too, the German economy also has no reason for pessimism. The loss in competitive strength that has occured can be restored. But to reach this goal we need the consensus of all the parties involved in the economic process – a consensus that is, above all, a recognition that it is our competitiveness which decides the prosperity and material security of the individual and the community."
Long before this advertisement appeared, the Friedrich Ebert Foundation – motivated by a related view of problems – held a colloquium on "Societies in International Competition: Pluralism as a Burden of Economic Efficiency?" (Bonn, October 14, 1981). This discussion focused on the "consensus of all parties involved in the economic process", and as a consequence on the social conditions of international competitiveness.
Is pluralism with its interest groups and its conflicts a burden for efficiency in foreign trade? Can only those societies which direct their economies in a corporative way, by consent, stand up to international competition?
Twelve experts concurred in answering and discussing these questions by submitting papers and contributions, a selection of which is available as No. 101/102 of the series "Analysen". The synopsis presented here is, to a great extent, based on the arguments of the participants. The arrangement, classification, and interpretations of these arguments, however, are solely the responsibility of the author who takes this opportunity to express his thanks, once again, to the experts.

Michael Dauderstädt

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# 1. The New Zero Sum World

Recession, increasing prices for raw-materials, a new international division of labour, and a declining ability of international economic diplomacy to reach a consensus on basic policy issues have turned the international economy into a zero sum world.

International competition is nothing new. And although its effects have always been contested, the general opinion which has prevailed is that up until today they have been predominantly positive. Based principally on classical and neo-classical economic theories, this view sees competition as furthering general prosperity: the world economy is regarded as a non-zero sum game, which generates benefits for all the participating countries (although **how** these benefits have been distributed has been a subject of debate, e.g. in the theory of unequal exchange).

The experience of the 'fifties and 'sixties supported this view. Growth and world trade promoted each other to an extent unparalleled in history. In the process, however, the nation state and the national economy steadily diminished in importance as the cornerstones of the world economy. Foreign trade accounted for an ever-larger share of national economic activity. Transnational enterprises transformed countries into investment sites which, thanks to improved transport and communications, could be reached at steadily falling cost.

The internationalization of the economy and world-wide integration were accompanied by the rise of international policy-making institutions to supervise the flow of benefits derived from the operation of the integrated world economy. At first glance this internationalization would seem to be a necessary and positive development. However, for the individual nations it represents a limitation on their ability to attain national goals. With the increasing embeddedness of national economies in the international economy, the prospect has arisen that any fundamental change in the structural conditions of the world economy might transform **the "openness" of a national economy into a burden,** rather than an asset or opportunity.

The restoration of prosperity and full-employment, stability and growth, would require a certain degree of insulation from world market influences under such circumstances.

As long as the world economy could be regarded as a non-zero sum game, this was not a serious handicap. But the situation has changed. There are three reasons to suspect that nation states today are placed in a different world, a **zero sum world.**

a) **The world recession** has produced a universal dampening of the prospects for growth. If a country hands on an industry to another country, the factors released, in particular labour, will not find sufficient alternative employment opportunities.

b) **The oil-price rise** has brought about a world-wide competition over the distribution of the balance of payments deficits of oil-importing countries, since – as far ahead as anyone can see – the permanent surplus of some oil exporters will correspond to an equally permanent deficit amongst importers, with any individual country only being able to dispose of its share of this deficit at the expense of someone else.

c) The integration of the world economy noted above has created **a virtually unlimited supply of labour in the developing countries** onto a world market established on the basis of the movement of goods and capital. To provide full-employment in a traditional manner for all these people seems utopian. At best the low level of wages which goes hand in hand with the oversupply of labour will lead to high wage labour continually being replaced by low wage labour. The retention of high wage jobs will therefore become a special privilege.

**In this zero sum world the key is internationally competitive production.** Apart from the important, but not crucial, sectors of home goods and services, it is the scope for competitive production which determines the level of prosperity and employment of a country. It is becoming less and less automatic that each country will have the share of competitive production it requires located within its own boundaries. And decreasing competitiveness means less secure access to vital imports, particularly raw materials. Moreover, if raw materials become more expensive – as has been the case with oil – dependence on exports will become even more critical. Competitiveness in export markets may become the key issue of economic policy – perhaps even a matter of national survival. However, in a zero sum world gaining market shares means loss of market shares by less competitive countries. **A policy of exclusive national interest is perforce a beggar-my-neighbour policy.** The machinery of supra-national institutions is increasingly incapable of getting to grips with this fundamental conflict of interest. Unable to share out the costs without commensurate benefits, it cannot offer any remedy. Its failure therefore represents the fourth component of the zero sum world.



## 2. Formulae for Successful Adjustment

*Domestic austerity and export-oriented modernization – these are the conditions for success in the zero sum world.*

Japan is the star example of a country that has been able to make its way in the zero sum world. It exhibits comparatively high growth, low inflation, low unemployment, and high export surpluses. Decisive for this success is the adaptability of the Japanese economy. As with all industrialized countries and all oil-importing nations, Japan had a large balance of payments deficit after the second increase in oil prices (in 1980 c. US $ 10,000 million). However, in contrast to most other deficit countries by 1981 Japan had transformed this into a surplus in excess of US $ 8,000 million – ultimately at the expense of the other industrialized nations.

The nature of the zero sum world dictates that the prosperity of the more competitive countries is paid for by the job losses and payment deficits of their rivals. This imposes a clear limit on the number of countries in the world which can enjoy economic success. How many Japans can the world accommodate? Who would import all their exports?

However, this is not the point at issue. Although one might not share the optimism of conservative economic policy that an export-oriented mercantilist strategy (contraction of the home market and an "offensive" modernization policy) would not damage one's neighbours, but rather benefit the world as a whole, no country dare afford not to pursue such a policy if it wants to avoid falling victim to the mercantilists. The byword therefore becomes – competitiveness at any price, even at the expense of third parties.

Which factors, then, determine the international competitiveness of a country, and how can they be positively influenced?

The position of a country in the world economy depends, in the first instance, on factors which cannot be politically influenced – or at least not in the short term: its industrial structure, the availability of natural resources, the skill of its labour force.
Nobody would expect Libya to produce a revolutionary new mini-computer, or Germany to come up with a glut of aluminium. Nevertheless, this historical endowment is only the basis on which each and every country has to maintain and develop its competitiveness. This applies especially to the industrialized countries, whose exports for the most part consist of manufactured goods, and which have very few natural competitive advantages. This is the sector on which the present study concentrates. **Countries have two ways of becoming competitive in the manufactured goods' sector:**

- **through low-costs in the field of price-sensitive products** – with austerity policy aiming to reduce wage costs and taxes in order to lower the burden on industry.
- **through quality, specialization, high technology, and reliability in the field of "quality"-sensitive products** – where competitiveness is achieved and maintained by modernization of the economy.

The following takes a closer look at these factors and the policies aimed at achieving them.

a) **Austerity policy**
Stabilizing, possibly even lowering, wage rates and the proportion of GNP accounted for by the state has several important consequences for a country's foreign trade position:

- It lowers home demand and hence the demand for imports. This reduces pressure on the balance of payments though at the cost of a (temporary) decrease in growth and employment.
- The reduction in the financial pressures on industry (lower wages, lower taxes) may increase competitiveness by creating a price-advantage. If prices do not fall by as much as costs, higher profits increase the incentives and opportunities for investment. Thus new income and employment may be created.

However, these two effects may, in turn, be negated by other consequences of the same policy. In a system of flexible exchange rates a fall in imports and increase in exports will bring about a rise in the foreign exchange value of the currency, wiping out any price advantages gained elsewhere. Moreover, revaluation and devaluation have a stronger impact than reductions or increases in domestic costs. There is therefore a temptation to obtain price advantages through devaluations rather than



the application of incomes or austerity policies, which inevitably generate conflict. Between Autumn 1979 and Summer 1981 the D-Mark lost about 30% of its value compared to the US Dollar, with corresponding positive effects on international competitiveness in the price-sensitive sector. A similar reduction in costs via wage or tax reductions would have been unimaginable.
Nevertheless, a dynamic consideration reveals that a policy aiming at competitiveness cannot rely on the devaluation approach. Devaluation increases the prices of imported goods, in particular oil. This, in turn, generates pressures on costs that may lead to a vicious circle of inflation and devaluation. Moreover, in a system of fluctuating exchange rates, the foreign exchange value of a currency depends on many influences. A relatively high level of interest rates, earnings from the export of raw materials and political factors may, for example, cause a currency to be revalued even though the movement of domestic prices and industrial competitiveness might necessitate a devaluation. Because of this relative independence of exchange rates, the more direct approach to lowering costs seems to be the more reliable route to reach international competitiveness.
All this however only effects prices, and therefore competitiveness exclusively in the price-sensitive sector. But this is not the direction in which the long term opportunities for a high wage country are to be found. Its advantage lies rather in the capacity to offer goods which are attractive to purchasers despite high unit klabour costs. This is the object of the modernization policy outlined immediately below. However, austerity has an important role in an overall modernization policy far surpassing its immediate impact on prices. Cutting costs improves the return on capital and therefore helps to finance the investments which lie at the heart of a policy of modernization. Consequently, **austerity policy** is not so much an isolated measure to create competitiveness - which is anyway only a short term effect, endangered by revaluation tendencies - but rather **prepares and supports the modernization policy** that aims at long-term competitiveness.

b) **Modernization Policy**
**Permanent structural change is the motto of the modernization policy.** The economy must constantly adjust the range of goods it offers to world demand. It must be able to diagnose, anticipate and promote growth-contributing factors. Technological advantages, high quality, reliable delivery and service make markets safe from price competition. Productivity increases even if high wage and material costs prevail, protect against less efficient competition. To reach this aim continous investments and innovations in new product lines and new production processes as well as continuous investments in the organizational efficiency and the qualification of labour are essential.

However, the structural change has two sides: productive new plants and new lines of production put burdens on old, less productive ones. **Booming industries face declining ones.** On the one hand, this has effects on foreign trade: if the increasing exports of the competitive, modern industries strengthen the foreign exchange value of the currency, the weak parts of the economy are exposed to stiffer price competition since their products become more expensive compared to foreign products. On the other hand, modern and traditional industries compete for factors of production. In times of underemployment this may be no reason for concern, but in bottleneck sectors (e.g. skilled labour) it puts the weaker enterprises under strain. Conversely, traditional industries may tie up resources and thus impede modernization. This is particularly valid if weaker industries are protected by trade barriers and subsidies, thereby burdening the remaining economy with higher prices and higher taxes.

The decline of industries that are no longer competitive, could be accepted more easily if the expected job losses were low. However, it is uncertain whether the growth in the more productive industries can create sufficient new employment. Because of their high productivity and high capital intensity, this growth would have to be very pronounced. This, however, is rather unlikely in the zero sum world.
Whatever combination of austerity and modernization a country may pursue, there are some **central conditions** to be complied with, **so as to succeed in the zero sum world:**

- **distributive discipline** contributes to the financing of investments for modernization even though it is no reliable support in international price competition;
- business and labour as well as regional and national authorities must accept that **industries which are no longer competitive are slimmed down or faded out;**
- **industry must invest in competitive production.** But it is precisely the unwillingness of other groups to accept the necessary sacrifices which is blamed for the current weak tendency to invest. This refers to demands for wages and welfare state benefits as well as to the resistance against ecological and/or social consequences of new technologies (c.f. chapter 8).

The ability of the political and economic system of a society to distribute disadvantages on social groups is decreasing. Reduced possibilities of financial compensation and uncertain expectations concerning the future advantages to be gained by present "moderation" limit the scope for compromise. **The zero sum world as environment creates national zero sum societies.**



# 3. The Inner Life of the Zero Sum Society

> *Modernization and stability depend on the society's capacity for distributing costs and burdens promptly and without disruptive conflicts.*

The internal structure of the political-administrative system, of the society and the relations between state and society determine how efficiently, i.e. how fast and with how little cost, dis-benefits can be distributed. These structures therefore contribute fundamentally to the position of a country in the world economy.
All big industrialized societies have different inner lives and social arrangements. Social science has developed numerous and contradictory typologies of societies. Whereas a rough classification would – following the "official" self-characterization – designate the Federal Republic of Germany or Austria as pluralistic states – in counterposition to totalitarian ones – one school of sociological thought regards all Western industrialized societies as more or less **corporative** (the term "neo-corporatism" is often used to distinguish this notion from the earlier concept of corporatism meaning fascism, for instance). Without going any further into this debate, a clear distinction seems to be justified between societies based on the degree of corporative interest mediation:

- **relatively strongly corporative democracies: France, Japan, Federal Germany, Sweden, Austria, Switzerland.**
- **less corporative democracies: the USA, Great Britain.**

Japan, and pre-1981 France occupy a special position among the countries of the first group in that workers and their organizations play a subordinate role in these corporative systems. In France this situation has changed with the advent of the Socialist government.
How can we distingusih between the systems of interest mediation in the strong and less strong corporative societies? Simplified to the extreme: by the extent to which the settlement of distributive conflicts

in the widest sense is left to the market and market power of groups. Whereas legalization and state mediation are of great importance in the highly corporative societies, state and interest groups are less entangled in the liberal systems, and the interest associations themselves are often less representative (e.g. possibly because of their lower degree of organization).
In addition to this rough division to the degree of "corporativity", the structure of state and unions or business associations is of importance for the functioning of the zero sum society, whereby the following dimensions may be distinguished:

- **the internal structure of the state,** as regards both the traditional division of power and the coordination of the individual policies of the executive;
- **the relation between the state and the interest groups;**
- **the relation among various interest groups,** in particular between labour and capital;
- **the structure within the interest groups,** especially the relation between the national (central) organization and the one on the sectoral and firm level.

The internal structure of the state and the interest associations influence their ability to execute certain functions externally. Thus, for instance, the federative structure of a state or an elaborated system of "checks and balances" may differentiate or delay the effects of government policy. Or: only a trade union structure organizing all workers and employees of one firm into one union, is able to meet the employer as representative of the whole working force.
These specific strengths and weaknesses of an organizational structure also determine how conducive it is to facilitating modernization and economic adjustment and hence to strengthening the country's international competitiveness. The role of organizational structures becomes particularly clear if one looks at the examples of the "successful" industrialized nations, Germany and Japan.



# 4. "Japan Inc." versus "The German Model"

*Corporative democracies with a relatively balanced distribution of income have been particularly successful in international comparison.*

Competition in the zero sum world increasingly compares whole societies and their ability to create the right preconditions for international competitiveness. An analysis of social structures in terms of their adaptation to this competition would seem to indicate that a highly corporative system, such as Japan, seems to offer exactly what is required to achieve international competitiveness. Though differing fundamentally from the Japanese "Model", the Federal Republic of Germany also tallies with this pattern as "The German Model" (Modell Deutschland) – that is, **a successful export giant resting on a smoothly functioning and corporatively managed modernization.** The fact that Japan is even more flexible and efficient in this respect may be attributable to its "better" – that is, more markedly corporative – structure.
Considered in terms of the four dimensions sketched out above, **corporatism in Japan** can be seen as follows:

1. **Institutionally, Japan's industrial policy is concentrated** in the Ministry for International Trade and Industry (MITI), responsible for coordinating, planning and implementing measures relating to policies on trade, competition, subsidy, research, and technology. In other countries these policy areas are institutionally divided and as a result their management is often uncoordinated, and even counterproductive.
2. This organization of state industrial policy facilitates the creation of effective **mechanisms for establishing consensus.** In Japan these **focus on the relation between government and big business,** though there are a number of important advisory bodies for economic policy which are tripartite in nature (government, capital, labour). Within the

framework of this consensus formation those partial strategies are worked out which, taken as a whole, represent Japan's policy of modernization. Such a modernization effort in an industrial subsector is guaranteed and supported by research policy, trade and competition policy and frequently leads to production which is highly competitive on the world market. The weak representation of trade unions in the Japanese corporative system is not reflected in conflicts outside the system of consensus formation, as is the case, for example, in the less corporative British system. The main reason for this is to be found in the relative weakness of the trade unions. This weakness is based on the unique dualism of Japanese society with its traditional and modern sector (c.f. 4.).

3. **The relation between capital and labour in Japan is characterized by a strong orientation to the individual company.** This orientation, while not excluding negotiations at national level, assigns relatively little importance to collective bargaining between trade unions and employers' associations. Crucial wage policy decisions are taken at company level, and numerous other issues (productivity, new technologies etc.) are likewise the object of the establishment of consensus at the workplace. The success of Japanese firms in achieving modernization is attributed to this combination of company wage-bargaining (high percentage of remuneration paid as bonuses) and company employment-, promotion- (seniority principle, life-time employment), and productivity-policies, without any great resistance on the part of labour.

4. The internal organization of the two important socio-economic groups – capital and labour – is characterized by a structural feature of Japanese society already noted above: **the dualism of the traditional and modern sector.** Whereas the traditional sector produces primarily for the home market with low productivity, high labour intensity, and mostly in small and medium-sized firms, the modern sector is made up of large export-oriented and competitive companies. At the same time the traditional sector complements the modern sector in a number of respects. Through subcontracting it provides the modern sector with cheap inputs based on low wages and low profits (accompanied by low productivity). It also assumes a buffer role as far as employment is concerned, allowing big companies to maintain a stable number of jobs despite changing economic conditions:

   - This dualism also characterizes the trade unions. Having a strong company bias, they show a high degree of organization in the modern sector and a low degree in the fragmented traditional sector. The large firms with a close cooperation between company trade unions and management give worker representation an importance that becomes visible in (material) advantages for the workers. This important role of the trade unions, in turn, guarantees high membership figures. However, the weakness of worker representation in the small and medium-sized firms leaves the trade unions with very little influence at sectoral and national level.
   - The internal structure of private enterprises is marked, on the one hand, by the dualism already mentioned and, on the other, by big company groupings, the "zaibatsus". Both these structural elements have rendered a high contribution to the success of the modern sector, which is so admired abroad: the small and medium-sized firms by their cheap and flexible supplies; the "zaibatsu" by the provision of finance for investment and by various other kinds of support for a member firm. It is the "zaibatsu" financing which has led to the high portion of outside capital, typical for Japanese companies.

Even though **Japan's institutional and social structure appears very conducive to international competitiveness,** its transferability is doubtful and questionable. After all, these structures are shaped by cultural traditions and by histories which differ sharply from country to country. Nevertheless, the case of Japan concretely reveals the functional requirements of international competitiveness, already indicated on a more general level above (p. 1): distributive discipline, the determined adaptation of a competitive modern structure of production and in its wake the demise of old, less productive industries. The latter, however, occurs less often in the form of closures and dismissals but rather through efficient re-organization and re-allocation of resources.

With her much more strongly represented trade unions, the Federal Republic of Germany seems to reach a similar economic performance, with a comparable corporative structure. For the analysts of the **"German Model"** she appears as a society in which government, capital, and labour closely cooperate. In economically depressed regions and sectors the measures necessary for modernization including the unavoidable allocation of disadvantages to certain groups, are carried out largely by consensus. **At the level of firms and plants** such consensus is reached within the framework of a legally established **co-determination.** In general, one can say there is something like a **"productivity coalition" between business and trade unions,** based on the advantages it carries for all who participate, including labour, to the detriment of those remaining "outside". The critics of the "German Model", therefore, speak of a trend towards **"social segregation".** The unions themselves prefer to consider their cooperation as forced upon them by necessity. Since business has a fundamental advantage within the market economy, it is a matter of protecting workers from a worsening of their position, the unions say.

And yet, the attitude of the German trade unions is very cooperative, if compared internationally, to the advantage of the competitiveness of German industry and to the advantage of those who maintain their jobs in the competitive core-sector.

**The relation between state and capital,** however, is more difficult. German investors do not respond all that readily to incentives provided by government. This may have to do with the quality of economic policy. In contrast to Japan, for instance, governmental activities related to **industrial policy** in a wider sense are **relatively uncoordinated,** even fragmented, in the Federal Republic of Germany. Individual measures are often counterproductive insofar as they only have protective effects and do not constitute an incentive for competitive production (e.g. subsidies as compared to credits). Some subsidizing bodies and/or policies have led to such a close entanglement of the state bureaucracies and business sectors that the latter have virtually lost the ability to survive in the market on their own.

The last mentioned aspect of modernization, i.e. the readiness of industry to penetrate into new growth sectors, has a decisive effect on the foreign trade position of a country (c.f. chapter 7). The following considerations will focus, however, on the relation between labour and capital and on the likelihood that this relation will lead to a consensus on how to distribute social costs and thereby reduce conflict. Such consensus, which is of particular importance in times of dis-investment and structural change, apparently also increases the willingness of enterpreneurs to modernize. On the other hand, if changes in production or shutdowns are delayed, complicated, or made more expensive by workers, enterprises are all the more inclined to hang on to existing production and to ask for subsidies from the state.

The acceptance of modernization by labour and labour organizations in Japan and the Federal Republic of Germany certainly has had its costs, too: costs that partly had to be borne by the workers themselves, for instance in the form of job-losses, and partly by the enterprises, e.g. in the form of redundancy payments and schemes for dismissed workers ("social plans"). But the costs were lower and productivity increases higher than, for instance, in the less corporative societies, such as the U.S.A. and Great Britain. The hard line and the provocative attitude of the trade unions has been singled out as the reason behind Great Britain's slow progress in modernization and its lack of international competitiveness in particular. Similarly, in the U.S.A. it has been claimed that "feather-bedding" of workers has made traditional industrial locations less and less attractive.

The comparison of the two "export models" Japan and the Federal Republic of Germany with the two big Anglo-saxon industrialized nations suggest that the formers' corporatism has a lot to do with their economic success. The same holds true for the comparison between the two



successful countries. It seems to have been easier in Japan to involve workers and employees in the interest and in the policy of the enterprise as well as to involve the enterprises in sectoral, even national strategies. On the other hand, Germany's position has been characterized, especially in times of recession, by an emphasis on particularistic interests and by missing trust between labour, capital and government. Is it a higher degree of corporatism which is (and would have been) needed? Is this the key to more international competitiveness?

## 5. The "neo-liberal" Challenge . . .

> *In the new zero sum world liberal societies that allow the market more freedom, have an austerity advantage.*

So far, the corporative factor seems to have made an essential contribution to economic efficiency. It is associated with a relatively equitable distribution of income, which distinguishes Japan and Germany from the United Kingdom and from the United States, where income is more concentrated. Social consensus, as a result of a corporativist organization of society, seems to be one of the keys to international competitiveness.
However, the zero sum world may have switched the lock. If international competitive growth can only be achieved – at least for some time – by re-distributing costs and burdens, the chances for a corporative solution which has always been based on distributing benefits, have greatly been diminished. The pressure on the corporatist consensus model is not only exerted by the fact that there is less to distribute. Above all, this pressure derives from the fact that in other societies, above all in Great Britain and in the U.S.A., the issue of distribution is solved more quickly.
The growing ability of these societies to allocate costs in the zero sum setting has been the consequence of a switch to a markedly liberal-conservative, anti-trade-union policy. This move to the right can be considered a direct consequence of the former system of industrial relations and its poor productivity results. The British example has begun to show now the first signs of success in form of a clear rise in productivity – at the price of massive recession and unemployment. This rise is all the more significant as it took place under conditions of idle capacities, which, as a rule, are more likely to bring about a decline in productivity because of diminishing "economies of scale".
The liberal policy of the government and the depression, accompanied by relatively slight corporative involvement, i.e. legalization and institutionalization of the relations between state, labour, and capital have



quickly restored the market its "rights". **There is no corporatist compensation for labour's loss of market power due to recession. This in turn imposes discipline on labour.** A decreasing frequency of strikes and the rise in productivity are the welcome consequences for the enterprises.
On the political level this process is supported by a deliberate attempt to remove any remaining traditional disruptive power held by the trade unions. In Great Britain this happens primarily by legislative initiatives: in the U.S.A. the reaction of the government on the strike of the air traffic controllers (PATCO) was a clear step into this direction. Moreover, this economic and political strategy creates a psychological climate reducing the determination of the workers and their organizations to resist. The strength of this policy lies in the rapid disintegration of non-competitive industries which leads to an increase in overall productivity by forcing marginal suppliers out of the market. Its weakness is the enormous price that has to be paid for it. Industrial production and employment fall dramatically. This is accompanied by a decline in demand which is further weakened by a reduction of state expenditure and social services. Thus, there is a clear disincentive to invest as far as sales on the home market are concerned. It counteracts the incentives which the liberal model otherwise provides, especially with regard to distribution. The British example in particular seems to prove that these incentives on their own do not produce growth. Even supply-side policy obviously needs demand so as to produce supply.
But on the other hand, a mere stabilization of demand does not create growth either, and certainly no competitive growth. It is the capacity to modernize which plays the key role. The price to be paid for this capacity, is much higher for the corporative models than for the neo-liberal models. This is particularly valid for Germany and similar countries, such as Austria, Sweden, etc. In Japan, the situation is different due to the relative weakness of the trade unions and other factors mentioned above which are specific to Japan.
Structural change, first of all meaning the slimming down of industries which are no longer competitive, costs more time and money in this case since processes clearly encrusted in the corporative structure have to be observed. However, these very differences to the competing "liberal" societies may be the deciding factors in international competition.

A slowdown of change, which has the pleasant anti-cyclical effect of stabilizing demand, may end up simply boosting imports, thus providing a handy compensation to the liberal competitors for their own, decreasing home markets. The balancing mechanism of flexible exchange rates reduces this danger (the development of the Pound and the Dollar has, for various reasons, impaired the competitiveness of the British and American exports), but it certainly will not eliminate it, especially not in the longer run.

**Seen world-wide, the success of this "liberal" policy, i.e. its enforced adoption by other countries, would lead to a general recession, but also to an increase in productivity.** In the long run, both effects may curb inflation – but not necessarily so, considering the market power of the big suppliers. Yet, only if increasing productivity is turned into an additional demand, can there be a lasting new impetus to economic growth.



## 6. . . . and How to Meet It

*In the short run, corporative democracies can compete with liberal austerity only by advantages in modernization and by special social compromises which have to be secured by long-term guarantees.*

Workers and their organizations in particular have to face up to the question of how to meet the neo-liberal challenge, especially in those corporatively oriented democracies in which the trade unions are of major political importance, i.e. Austria, Germany, Sweden and more recently France, though hardly Japan. Basically, this liberal challenge is nothing but an especially rapid and hard-lined adjustment to the "zero sum" world, as outlined in the first chapter, but which has the effect of exacerbating this zero sum quality by bringing about an additional reduction in world-wide demand and by increasing competitive pressures.

More to give a complete picture than to present feasible solutions, we briefly deal below with two possible direct responses to this pressure **as far as foreign trade is concerned:**

a) **an internationally coordinated effort to accelerate world-wide economic growth:** such a "global Keynesianism" approach is to be found in the proposals of the Brandt Commission, among others. Not unexpectedly, this initiative for a world-wide reflation of demand through the transfer of resources to poor countries is supported by the international trade union organizations. However, equally obviously, such an initiative has no prospects of implementation by governments as long as major countries pursue a diametrically opposed policy of national adjustment via neo-liberalism.

b) **national protectionism:** parrying the pressure of foreign competition by means of customs tariffs and other trade barriers, or of subsidizing domestic suppliers may have greater chances of being implemented but also has considerable drawbacks: in the long run it lowers pro-

ductivity and competitiveness at the expense of consumers and tax payers, that is, workers themselves.
Moreover, it gives rise to the danger of retaliation which could hit an export-dependent country such as the Federal Republic of Germany very hard. World-wide, the consequences would be a strengthening of recessionary and contractive tendencies.

In the absence of these two escape routes, any individual country simply has to come to terms with the neo-liberal challenge in the zero sum world. Industry demands – above all from its own micro-economic standpoint – a copy of the policies being pursued in competitor nations: greater labour-market flexibility through reductions in social "featherbeds", and other institutional barriers; concessions to business in distribution policy at the expense of the state and wage-earners; the removal of "investment barriers" at the expense of the environment and other long-term security considerations (nuclear waste disposal, arms exports etc.). The trade unions will also be inclined to put up resistance, especially on the distribution and social policy front, to defend existing levels (of redistribution).
Even if successful, both parties will have to reckon with counter-productive side-effects over the longer run: accession to the demands of companies might intensify the recession, as can already be seen in the United States and the United Kingdom, and would inevitably be detrimental to large sections of industry. At best, the trade unions might manage to secure the status of those who remain in employment despite increasing competition, that is, those either employed in industries not exposed to international competition, or in internationally competitive firms. But if there is a general decline in the country's competitiveness and a weakening propensity of enterprises to invest, recession and growing unemployment will be unavoidable.
This stand-off between labour and capital could constitute the basis for a social partnership typical of corporatism. However, two factors oppose such a development:

a) in contrast to previous coalitions, above all the classic "productivity coalitions", **this time there are no benefits to be distributed – only costs:**

b) the stand-off is asymmetric. Unless the trade unions decide, against all tradition, to make a risky attempt at an offensive to change the political system, they will be fighting with their backs to the wall. Companies, however, have access to the neo-liberal option as an alternative, without and/or against the trade unions, following the British or the American example. Although this possibility will not increase their readiness to make concessions, on the other hand it will not extinguish it completely, since the political as well as the economic price of a long conflict or dispute must certainly not be underestimated.



If we assume that labour and business are prepared – albeit hesitantly – to create a new "coalition", the question arises as to the possible guarantees for the maintenance of the terms of the coalition. After all, it involves the (voluntary) acceptance of (social) costs in order to prevent even higher costs, whilst prospects for eventual benefits remain very uncertain. Therefore the weaker partners, especially the trade unions, will insist on a guarantee which will make the sacrifice worthwhile.

The guarantees are all the more problematic since,
- because of its market power, capital can, if necessary, largely enforce the desired behaviour of workers, whereas this is scarcely a feasible option for the unions;
- the internal guarantees for compliance are stronger amongst the trade unions, especially in view of the bad economic situation: agreements on wages and working conditions are binding for all workers: it is unusual for the employees of an individual firm to step out of line;
- the internal guarantees on the capital side are rather weak: if losses force a firm to dismiss staff or close down, other firms can only step in to a very limited extent.

**The guarantees must** therefore **be established at a political level.** Following trade union ideas these could consist in economic and social councils whose powers would embrace at least a partial redistribution and democratization of economic power, paralleling the pattern of political democracy. In a more modest deviation from present institutional realities, they may be found in a national economic policy conducted by a strong government which has the confidence of both capital and labour, and which would not hesitate to apply sanctions if necessary. But in the absence of a last-resort policy of controls on the international movement of capital and trade, such a government would only have limited possibilities for imposing sanctions on companies.
Irrespective of whether the one or the other form of guarantees is desirable, one thing is certain: **without guarantees,** and that means first of all, guarantees for workers and employees because of the asymmetry of the market power, **a scenario of costly conflicts would be inevitable.**

# 7. How to Get Business to Invest

*Neither the carrot nor the stick are reliable means for involving business in a national policy of competitiveness and burden-sharing.*

**The central problem of economic policy-making is less that of involving labour but rather that of involving capital.** The trade unions have the unpleasant choice between diminishing competitiveness and unemployment on the one hand, and full competitiveness accompanied by job-losses and wages-cuts on the other. As a consequence, they find that they are virtually forced to cooperate. Capital has the option of shifting to the international investment markets or pushing the neo-liberal alternative. It is no accident, then, that the state sees its main task as motivating enterprises to invest by improving the general business climate through the offer of subsidies and other measures. The privilege of production on home territory has to be maintained, and the attractiveness of the location (Federal Republic of Germany) to be preserved.
A large number of subsidizing agencies have the task of "getting business to invest". Support is provided for research and development through regional and competition policy. Infra-structure is made available. The labour force is trained. And yet business still seems reluctant to invest.

Why?

Two different answers are offered.

a) **Wrong incentive pattern**
The tendency to invest and modernize is impaired by a faulty economic policy. High interest rates induce capital to invest in securities rather than high risk ventures. Research projects carried out by big companies and financed by government grants do not stimulate initiatives to develop new products and technologies in line with market requirements. Small and medium-sized firms are hopelessly disadvantaged from the start, even though they are possibly intrinsically more aggressive and adaptable.



Indiscriminate subsidies reduce the tendency and necessity for firms to earn the counter-value to state-supported investments on the market.
A policy which shifts the responsibility for economic success back onto business would recommend itself under such circumstances. Assistance should certainly be offered to establish the necessary preconditions for competitive production, such as the provision of finance, access to basic scientific knowledge etc., but in order for this to promote the type of competition which benefits the customer and exerts permanent pressure for adjustment and modernization, these offers must be general in character. More stringent regulations, e.g. on the environment, would then act as a further incentive for innovation and are no excuse for subsidies or unexecuted investments. The survival of industries in a market in which tough requirements, standards and controls are the norm – not least enforced by the state – will generate greater competitiveness in particular on foreign markets where similar requirements will be demanded sooner or later (for example, on environmental standards). The motor vehicle industry is a good case in point: Sweden's manufacturers were very early to adapt to strict safety regulations, and those in Japan and Europe to relatively high fuel prices – adjustments that later paid off for both sets of suppliers in the US market.

b) **Obstacles to investment**
Consumer and environmental protection, political considerations, interventions into the market – these are, according to industry, the major obstacles to investment, competitiveness and growth. The state is held responsible for additional pressure on costs and cost-incurring delays to decisions, which slow down the necessary adjustment process and set up competitive disadvantages vis-a-vis the less encumbered countries.
In the broader sense, the social framework, the rigidity of wage settlements, and other distribution problems are included in the obstacles to investment. In particular, the growing tax burden is claimed to divest the entrepreneur of the fruits of his efforts, and thereby kill off his motivation.

It may be a surprise, or not, but both these answers share the view that the market is the source of innovation and investment. And both consider the effectiveness of this source to be prejudiced by state activities.

**Both would like to reinstate the power of market forces, the latter though as carrot, the former as stick.**

Whereas in the one view the market no longer offers sufficient profitable opportunities, the others see the pressure of competition weakened by state protection and monopolization. Accordingly, different cures are suggested.
In fact, it is justifiable to ask why a policy geared to a Darwinist view of the market would not prove salutary. Any so-called obstacle to investment can also be seen as a pressure or a stimulus. If nuclear power is unacceptable for political reasons, the quickest and most flexible in offering competitive alternatives will succeed in the struggle for (economic) survival.
Anyone subsidizing the retention of an outmoded option will be blocking adjustment. That the sum of feasible options – that is, the market – should be determined politically is nothing new. It happens in other spheres too (armaments, trade with the East etc.).
**The stick of adjustment pressures does not work if those who refuse to adjust are simultaneously offered the carrot.** As long as there appear to be better prospects for removing the political barriers to certain profitable ventures, adjustments will not be made. Even investments which are clearly profitable will be held back. Clear political limits within which economic rationality (as a carrot as well as a stick) is allowed to work seem to offer the solution.
How does this solution look in the zero sum world?
How narrowly can the political conditions be set within which industry has to adapt?
It is the **choice of dosage** which is crucial. For instance, if the nuclear power option is precluded by a political decision, and the market and industry set the datum of higher energy prices, within ten years, in theory, one could have an energy sector with a high share of alternative energy sources and a range of energy-saving investments in the energy consuming industries. Successful adjustment, then, will allow only the most flexible and most innovative firms to survive.
The zero sum world, however, makes a version different from this ideal development more likely: high energy prices will reduce the competitiveness of energy-intensive industries, e.g. chemicals, and make other locations more attractive such as France with its large-scale nuclear programme. Other countries will get the production and the employment.
**Therefore, if the state reduces the breathing space of firms too much in the zero sum world, it will not encourage the survival of those most able to adjust, but will drive all those out of the country who feel that the costs of adjustment are too high.** The stick of competitive pressure, therefore, must be applied with care; a generous allowance of the carrot is advisable.



# 8. Who Pays for the Carrot?

*A one-sided shift of social costs onto marginal groups in society, onto the environment, and onto the future may seem tempting, but it produces serious dangers that neo-liberal systems will find hard to escape.*

The zero sum character of the world economy obliges the observer to fall back on the old question of how to distribute the social costs. If obstacles to investment, like environmental and consumer protection, block modernization and adjustment and prevent a new productivity coalition between labour and capital, these obstacles and the related costs and burdens have to be removed. But what is to be understood by removal? In many cases it means transferring burdens to the environment, to marginal groups, to the future. **The carrot that is supposed to entice the enterprises to invest and to secure economic growth in the home country, has to be paid for by other sectors of the zero sum society.** Rises in productivity will be achieved by externalizing the costs if higher yields are at the expense of nature and of humanity.
Capital and labour, which will benefit from such externalization of costs, constitute a powerful productivity coalition for the protection and development of favourable production conditions at home. Just as companies expect distributive discipline from the trade unions, both in turn expect social discipline from the remaining quarters of society, from the marginal groups that oppose a **redistribution of costs and benefits in favour of the sectors engaged in international competition.** Here, too, the Japanese example gives the clue. On the one hand, the dual economic structure burdens the costs of adjustment on the small and medium-sized firms. On the other hand, this country is notorious for having neglected for too long the external effects of rapid growth. The poor housing situation and the precarious state of the environment are typical for the industrialized country with the highest concentration of production (gross domestic product per area).

However, the Japanese example does not only show that rises in productivity and competitiveness have to be paid for by other sectors of the national economy and by the environment. It demonstrates, moreover, **a further and even more frightening danger:**
**It may not be possible to stop this development,** not even with the best of will. Japan has tried to do so with its economic plans for 1967 and 1970. After years of unprecedented growth both plans focused on the development of the welfare state. Social development was supposed to complement and safeguard the economic development. The oil price shock of 1973 brought an end to these hopes. The new emphasis on social development had to give way to economic growth and competitiveness again.

The zero sum world has made this constraint the permanent companion of all countries – not only of Japan. Growth and competitiveness can be achieved by externalizing social costs. The rises in productivity and the lower costs achieved that way will, however, force the competitors to take similar steps. **In the zero sum world every country improves the competitive conditions for its enterprises with "the carrot" of irresponsibility towards the environment and the future.** But since an international harmonization of competitive conditions is just as unrealistic as global Keynesianism, adjustment means always adjustment to lower standards. For instance, countries which still have a "pollution capacity" can offer a more favourable industrial location.
On the other hand, social costs can hardly be re-internalized any more. Should growing external effects make themselves felt socially and politically, then foreign trade constraints make internalization impossible or too expensive, as in the case of Japan. Even increasing pressure on the political and social climate has to be put up with so as not to prejudice international competitiveness. If a country has "only delayed" social development for the time being in order to avoid a decline in competitiveness, it must realize that "delayed" now means "abandoned", unless it wants to fall behind again, since the country's own policy of externalizing social costs will have forced its competitors to adopt the same policy in the meantime. These may have lowered their standards in environmental protection and are now just as competitive. Insofar, as they are all adjusting downwards, one after the other, all countries end up finding it impossible to adjust upwards at a later stage for fear of losing their competitiveness.
**What remains unresolved is how far – nationally and internationally – the payment of social costs can be deferred into the future.** The sum due (whenever it has to be paid) is growing with every year that passes. And the charges are piling up like a mass of earth in front of a bulldozer: the time will come when the load is too big to fit into the bulldozer's blade – and may even bring it to a dead-stop. However, the corporative system is notably lacking in advocates of the prompt consideration and internalization of social costs before the problems get out of hand. What predominates are the interests of the "productivity coalition" in the removal of "investment barriers".
These massive interests in the maintenance and expansion of productivity and the equally massive constraints of the zero sum world pressing in the same direction are, however, opposed by other interests and exigencies:

- the dangerous practice of delaying solutions in favour of short-term cost reductions may come to a dramatic and costly end.
- the interest in parrying social costs (i.e. in a cleaner environment, less stress etc.) rises in step with productivity and income.
- with a fast increase in productivity the social basis of the productivity coalition will tend to diminish, since fewer and fewer workers produce more and more goods and services.
- therefore, the political power and influence of the marginal groups will gain in importance in democratic societies, even though they are not widely represented in the institutional system.
- finally, the reduction of social costs itself may become a growth sector providing an important contribution to employment and competitiveness.

**The more the zero sum world forces social costs to be externalized, the more the pressure of interests and of problems which are pushed aside in the process will grow too.** Environmental catastrophes and small political groups can tip the scales in the often very evenly balanced party democracies and may force a turn around in certain cases. However, such a re-internalization of the costs of growth would have to be secured at the foreign trade front by protectionism and a partial de-linking from the world market. It remains questionable whether a concerted international effort can preempt such developments. Growing concern, e.g. about environmental pollution, has brought about some success (institutions, agreements, etc.) in the past, but as in the case of a reflation by redistribution, the chances of reaching a global policy are decreasing in this area, too.
First hints as to the solution of this conflict will be given by those countries that have up to now massively externalized their social costs in favour of their international competitiveness. Thus, many critics of Japanese society, for instance, are waiting for the pendulum to swing back to more social development. Whether, when, and how this swing will take place, depends on the foreign trade situation which has already prevented it once before.
If a balanced development of the economy without deep social conflicts is considered desirable, it seems reasonable that social costs should be internalized and that the various interests should be mediated through appropriate political arrangements (institutions). In this case, the same

holds as in the classic productivity coalition: temporary sacrifices may be necessary in order to finance and implement productive restructuring on a long-term basis. All groups which have to bear sacrifices, however, must be given guarantees that these sacrifices will bear fruit at a later stage. Such economic or political guarantees do not only have to include the labour force and its organizations but also those who have to bear the social costs and those who represent them, since the long-term guarantee of stability – and hence competitiveness – requires that the environment and other social interests and not simply jobs and wages, have to be attended to.



## 9. Synopsis: Bleak Perspectives

The zero sum world demands a simultaneous double redistribution of an attractive and internationally competitive industrial location:

- Profits are to be increased at the expense of wages in order to finance modernization and structural changes and to keep job losses to a minimum.
- Employers and workers form a productivity coalition which defends its position at the expense of the natural and the social environment.

The pressure of these demands is increased by the radical adjustment of those countries (U.S.A. and Great Britain) that pursue the neo-liberal strategy of effecting redistribution through the market. This reduces the stabilizing influence of the welfare state and organized interest groups on demand and social costs.

Corporatively organized democracies thus have to face increased adjustment pressure. In former times, their ability to implement structural changes and modernization quickly and without disruptive conflicts by involving the groups affected, has given them an advantage in productivity and competitiveness. This favourable position meant, moreover, that incomes could be distributed more equitably.

In particular, Japan and the Federal Republic of Germany have developed (different) organizational patterns that make state, capital, and labour cooperate to the advantage of international competitiveness even though short-term disadvantages have to be put up with. The internal structure of the administration as well as of the interest groups (at the firm, sectoral, regional, and national level) furthered consensus and adjustment. Thereby Japan was even more successful because of her dual economy and better cooperation between state and enterprises.

The zero sum world, however, has altered a key aspect of the corporative way of managing adjustment: the volume of profits and jobs respectively to be distributed, has drastically shrunk and is uncertain for the future, too. Therefore, the redistributions mentioned at the beginning require sacrifices to be made by certain groups without any great prospects of compensating rewards now or in future.

Moreover, both kinds of redistribution have dangerous side-effects: the reduction of wages and incomes lowers demand, and the continued externalizing of social costs may have disastrous effects in the long run. On top of it, their positive effect on international competitiveness disappears to the extent that other countries pursue the same kind of policy. For lack of a global economic policy, an international race into redistribution (of both kinds) cannot be put under control. Therefore, each country can but try to stay as competitive as possible until the accumulating negative effects enforce politically a change of course (on a global scale). Such a change will – at least in its first stage – take the form of independent national measures of a protectionist nature.
In order to minimize the sacrifices to this point and in order not to destroy the basis for long-term solutions, those who lose out on both kinds of redistribution must be compensated with structural and institutional guarantees. Only by institutionally involving those who have to bear the sacrifices, can the necessary redistribution take place without costly social conflict. In the long run, this paves the way back to a socio-economic order whose continued neglect, for the sake of international competitiveness, will seriously endanger the basis of the whole system.



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