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The state and the economy: Germany

How to restart the engine?

BERLIN

European governments are taking over ever-larger parts of the economy. In the first of two articles, we examine the debate in Germany

FOR German leaders nowadays, Rüsselsheim is an obligatory destination. Frank-Walter Steinmeier, the foreign minister who is campaigning to become chancellor in September, showed up last month. His mission: to reassure workers at Opel, an ailing carmaker based in Rüsselsheim, that the government will fight for their jobs. "Opel must live!" cried the normally circumspect minister before a crowd of 10,000 people. The chancellor, Angela Merkel, who hopes to be re-elected, plans a pilgrimage later this month.

Sorting out Opel's fate has become the most pressing question in German politics. The company is part of the German arm of America's nearly-bankrupt General Motors, which says it needs €3.3 billion ($4.2 billion) to survive. Mr Steinmeier's Social Democratic Party (SPD), and members of the conservative Christian Democratic Union (CDU) whose constituents include most of Opel's 29,000 workers, want to rescue the company at almost any cost.

On the other side are economic liberals who fear that the state is already taking over too much of the economy. Some worry that Germany risks becoming something of a socialist state—"East Germany lite", in the words of Guido Westerwelle, head of the opposition Free Democratic Party (FDP).

Germany's post-war prosperity (first in West Germany, then haltingly across the country after reunification) was founded partly on the notion of *Ordnungspolitik*, whereby the state referees the market without seeking to control it. It would intervene in some areas, for instance to prevent monopolies, but stay out of other domains, such as setting wage levels. This arrangement largely succeeded in making a success of Germany's "social market economy". To the dismay of economic liberals, however, the "grand coalition" government, in which Ms Merkel's CDU is yoked to the SPD, had been chipping away at *Ordnungspolitik* even before the crisis, for example by introducing minimum wages in some sectors.

Now it is going further. The government plans to spend €80 billion to stimulate demand and has made €500 billion available to rescue banks. It has created a €100 billion "Germany Economy Fund" to provide credit and loan guarantees to non-financial companies, perhaps including Opel. And it is proposing a law that would let the government expropriate failing banks as a last resort.

Few doubt that the banking system needed rescuing. But the risks of bailing out industrial firms are "much more severe", says Justus Haucap, head of the Monopolies Commission, which advises the government. These include distorting competition, weakening healthier companies and preserving outmoded methods of production. The costs could mire the government in large debts; the worry may be not that the state will become too powerful, but that it will become severely weakened. "The growing fear that the bail-out state will be overburdened could decide the election," commented a recent editorial in *Frankfurter Allgemeine*, a conservative newspaper.

That said, there are fewer purists in politics these days. Even Mr Westerwelle's FDP concedes that aid to industrial firms may sometimes be warranted. The fights are over nuances: what sort of aid, to which firms and under what conditions? The government's policy, officially at least, is that only firms that are in trouble through no fault of their own and have credible plans for recovery will qualify for aid, and then only in the form of loans or guarantees.

Opel so far has failed these tests. It has been losing market share for years and may be too small to survive in an industry plagued by overcapacity. The economy minister, Karl-Theodor zu Guttenberg, says Opel's 184-page survival plan still leaves many questions unanswered. Waiting in the wings is the equally undeserving Schaeffler, a car-parts manufacturer which borrowed €11 billion to buy a larger rival, Continental (see page 68).

The crisis is polarising politics. The SPD is gaining in the polls, thanks in part to its advocacy of state intervention, which appeals to its core voters. At the same time, the unabashedly free-market FDP is enjoying record ratings of 15% or more.

The CDU is caught in a pincer and is be- ▸▸

ing split. Roland Koch and Jürgen Rüttgers, the CDU premiers of Hesse and North Rhine-Westphalia, would contemplate temporary state ownership of Opel to save factories in their states.

The chancellor has not sided with them, but nor has she vigorously opposed them. That angers the party's liberal wing, which grumbles that she is too ready to follow the lead of the left-leaning SPD on company bail-outs and bank takeovers. "We have to avoid giving the impression that the CDU is the party of nationalisation," says Gunther Oettinger, Baden-Württemberg's premier.

Ms Merkel, who grew up in East Germany, is unlikely to wish for the return of state control of the economy. "At the end of this process we can go back to the old contours of the social market economy," she says. The interventions in the economy so far have been limited. The Germany Economy Fund runs out next year (though its guarantees will linger). The bank-expropriation bill leaves the government just enough time to take over one bank, Hypo Real Estate, into which it has already pumped more than €100 billion.

A planned constitutional amendment would bar states from running deficits and would limit federal budget deficits to 0.35% of GDP, beginning in 2016. As the economy recovers, this should ensure that public spending will shrink as a share of GDP, says Michael Eilfort of the liberal Market Economy Foundation in Berlin. For now the government's plan is to return to *Ordnungspolitik* once the crisis has passed. But if it deepens, is there a Plan B? ■

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The state and the economy: France

Back in the driving seat

PARIS

The return of dirigisme

IN ONE respect, at least, the global downturn is welcome in France: it has legitimised economic interventionism in the land where Louis XIV's finance minister, Jean-Baptiste Colbert, invented it under the term *dirigisme*. "The main feature of this crisis", declared President Nicolas Sarkozy recently, with more than a hint of satisfaction, "is the return of the state, the end of the ideology of public powerlessness."

The government's recent €6 billion ($7.6 billion) rescue of Renault and PSA Peugeot Citroën, two carmakers, captures the French political mood. It prompted little debate over whether the state should bail out car manufacturers with public money, or even whether such state aid would distort competition. Such arguments were left to the European Commission, as well as to central and eastern Europeans livid at protectionist comments made by Mr Sarkozy, who suggested last month that it was "not justified" for a French carmaker to build a factory in the Czech Republic in order to sell cars in France. At home, though, barely a voice was raised to recall that the freedom for companies to do this is enshrined in Europe's single-market laws.

Instead French politicians, from the left and the right, have urged Mr Sarkozy to do even more to protect French jobs, keep factories open and curb bosses' pay. The car industry directly employs 700,000 people in France, and 2.5m indirectly. With unemployment already at 8.3%, and global car sales collapsing, the French are particularly worried about job losses and stagnant pay. Unions have called for another day of strikes and protests on March 19th; the latest day of action in January drew 1m-2.5m people onto the streets across France.

This is why Mr Sarkozy tried so hard to tie state aid for the car industry to a promise to keep production at home. "We could not have explained to the French that we were spending money on companies but not saving jobs in France," says one minister. After meetings with car bosses, Mr Sarkozy announced triumphantly in February that he had got his way. Both Renault and PSA, he claimed, had given "a commitment" not to close any factories for the duration of the state loans, and to "do everything" to avoid layoffs. But Neelie Kroes, the EU competition commissioner, demanded a written promise that the aid would not be linked to any measures limiting carmakers' freedom in the single market, now or in the future. With that guarantee in her pocket, she gave the go-ahead.

French politicians consider as given a strong role for the state. If anything, the policies regarded in Brussels as protectionist are in France considered too liberal. Voices on the left charge that Mr Sarkozy has ceded too much to Brussels over the car industry. Even before the slump, economic liberals were a discrete species in the French political ecosystem, dominated by the traditional big beasts of the Gaullist right and the Socialist left. The anti-capitalist hard-left is enjoying fresh popularity. A recent *Paris Match* poll suggested that the three far-left political parties, a mix of communists and Trotskyites, would together grab 16% of the vote at the upcoming elections to the European Parliament—more than the centrist party of François Bayrou.

Indeed, many in France have found renewed pride in their statist system. *Le Monde* noted in a recent article that, "In the crisis, the French model, formerly knocked, is finding favour once more," and argued that "France is better equipped than the United States or some of its European partners to deal with the recession because its model limits social damage." François Fillon, the centre-right prime minister, has praised the virtues of *dirigisme* in building high-speed trains and developing nuclear energy. The new creed has notably raised the stock of Henri Guaino, Mr Sarkozy's speechwriter and a long-standing advocate of state intervention.

Even Christine Lagarde, the free-market finance minister, points out that the heavy state now has its advantages. In 2007 public spending accounted for 52% of GDP in France compared with 45% in Britain and 44% in Germany. This may have held back the economy in boom times; but, with its welfare cushion, it helps to keep it afloat in recession. Once denounced for running a high budget deficit, France now has one which, at 5.5% of GDP forecast by the IMF for 2009, is well below that of Britain (7.2%) and the United States (12%).

During his election campaign, ironically, Mr Sarkozy had called for reforms to the French model which, he said, produced less growth and more unemployment than elsewhere in Europe. The recession took hold just as he launched measures to trim the civil service, stiffen competition, cut red tape and loosen the labour market. Now he is under pressure to ease off.

Yet in the long run, many of those policies are needed. "The French economy and, above all, the French consumer appear to be relatively resilient in the presence of shocks," wrote Carlos Caceres, an economist at Morgan Stanley, in a research paper this week. "However, this resilience stems mostly from structural rigidities—in particular labour-market rigidities—which prevent the economy from adjusting rapidly, and therefore can come at the cost of a more protracted downturn." ■