

*International Colloquium*

***ECONOMIC CRISIS AND NEW NATIONALISMS:  
GERMAN POLITICAL ECONOMY AS PERCEIVED BY EUROPEAN PARTNERS***

***German Ordoliberalism and Keynesianism in Historical Perspective***

**HARALD HAGEMANN  
University of Hohenheim, Stuttgart**



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# Outline

1. The birth of *Ordoliberalism* in the deepest crisis 1938-1945
2. *Walter Eucken* and the Freiburg School: Order as a guarantor of freedom
3. *Ludwig Erhard*: the father of the “Wirtschaftswunder” (economic miracle)
4. *Alfred Müller-Armack* and the genesis of the concept of “Soziale Marktwirtschaft” (social market economy)
5. Keynesianism of the Hicks-Samuelson neoclassical synthesis: The role of *Erich Schneider*
6. The high years of *Keynesianism* 1967-1974

## 1. The birth of Ordoliberalism in the deepest crisis 1938-1945 (1)

Whereas the Americans had a decisive influence on the *West German currency reform of June 20, 1948*, and thus on a key aspect of the long-term growth process, their influence on the predominant conception in economic policy after 1945, the social market economy, however, was quite minor. On the contrary, the fundamental ideas of Ordoliberalism, above all those of the Freiburg School under Walter Eucken, originated in the years 1938-1945 in opposition to National Socialism and on the basis of Christian convictions.

## 1. The birth of Ordoliberalism in the deepest crisis 1938-1945 (2)

- The German conceptions of ***Ordnungspolitik*** and ***Soziale Marktwirtschaft*** are a response to the challenges of
  - the Great Depression
  - national socialism and
  - central planning in soviet-type socialism.
- After 1929 economic and political liberalism was in its deepest crisis.

## Walter Eucken (1891-1950) (1)



- Born 17 January 1891 in Jena (his father Rudolf was philosopher and Nobel prize winner in literature)
- PhD in Bonn 1913 and habilitation in Berlin 1921 with Hermann Schumacher (father of Ernst F. Schumacher, the author of “Small is beautiful”)
- 1920 marriage with Edith Erdsiek

## Walter Eucken (1891-1950) (3)

1925 Professor, University of Tübingen

since 1927 Professor University of Freiburg

Eucken's most outstanding student: *Friedrich Lutz*

1933 Opponent to *Martin Heidegger* the philosopher and rector

1940 *Die Grundlagen der Nationalökonomie* (Foundations of Economics), Eucken's opus magnum

9 November 1938 *Reichskristallnacht* (Night of the broken glasses)  
The Nazi pogrom against the Jews leads to the foundation of the *Freiburger Konzil*

1942 co-operation with the *Bekennende Kirche* (Dietrich Bonhoeffer),  
i.e. those members of the protestant church who were in opposition  
against the Nazi system

1942 Essay "Wettbewerb als Grundprinzip der Wirtschaftsverfassung"  
(Competition as a fundamental principle of the economic  
constitution)

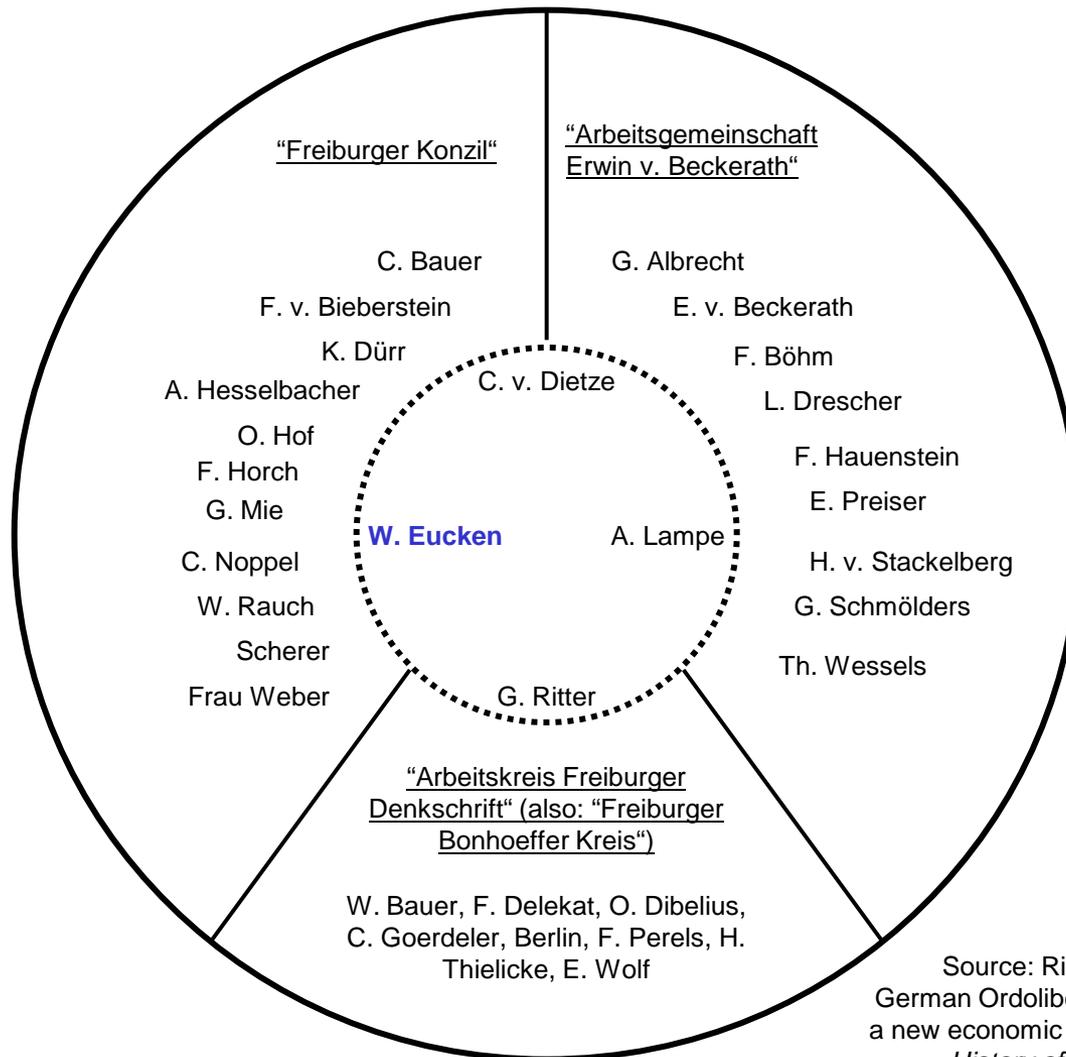
## Walter Eucken (1891-1950) (2)

1923 “*Critical considerations of the German monetary problem*”

Against the background of the *German hyperinflation* Eucken distanced himself from the research tradition of the German historical school in which he had grown up, and put forward a penetrating criticism of the balance-of-payments theory. The *primacy of monetary (and currency) stability* later became a key constituent principle in *German Ordoliberalism*, alongside the fundamental principle of the economic constitution, that is, the functioning price mechanism of perfect competition – the “Freiburg Imperative” – deeply affecting the monetary policies of the *Bundesbank*.

- **US American trauma**  
*Great Depression, with mass unemployment and deflation*
- **German trauma**
  - *Hyperinflation* in Germany and Austria after WWI leading to a currency reform at the end of 1923, far-reaching expropriation of money wealth owners
  - historical background of the writings of *Mises* and *Hayek*
  - atypical statement: “*better 5% inflation than 5% unemployment*” (Helmut Schmidt 1972):
- **Trauma:** morbid condition of the body produced by a wound or injury – (psychology:) emotional shock

# The Freiburg Circles



Source: Rieter/Schmolz (1993) – „The ideas of German Ordoliberalism 1938-45: pointing the way to a new economic order“, *The European Journal of the History of Economic Thought*, 1(1), S. 87-114.

## 2. Walter Eucken and the Freiburg School (1)

20 July 1944 attempt to kill Hitler

→ Eucken interrogated by the Gestapo, but in contrast to Constantin von Dietze, Adolf Lampe and Gerhard Ritter not put into prison.

Eucken (1940), “Wissenschaft im Stile Schmollers”  
(*Weltwirtschaftliches Archiv*)

In this article Eucken criticizes the historical blindness of an exaggerated idea of progress which animates to make the present (1940!) to the measure of historical development and Schmoller’s statement that it is the right of the stronger and better to celebrate victory. Reference to great crimes in history (Bartholomäus night) and radical differences between power and ethical values.

## 2. Walter Eucken and the Freiburg School (2)

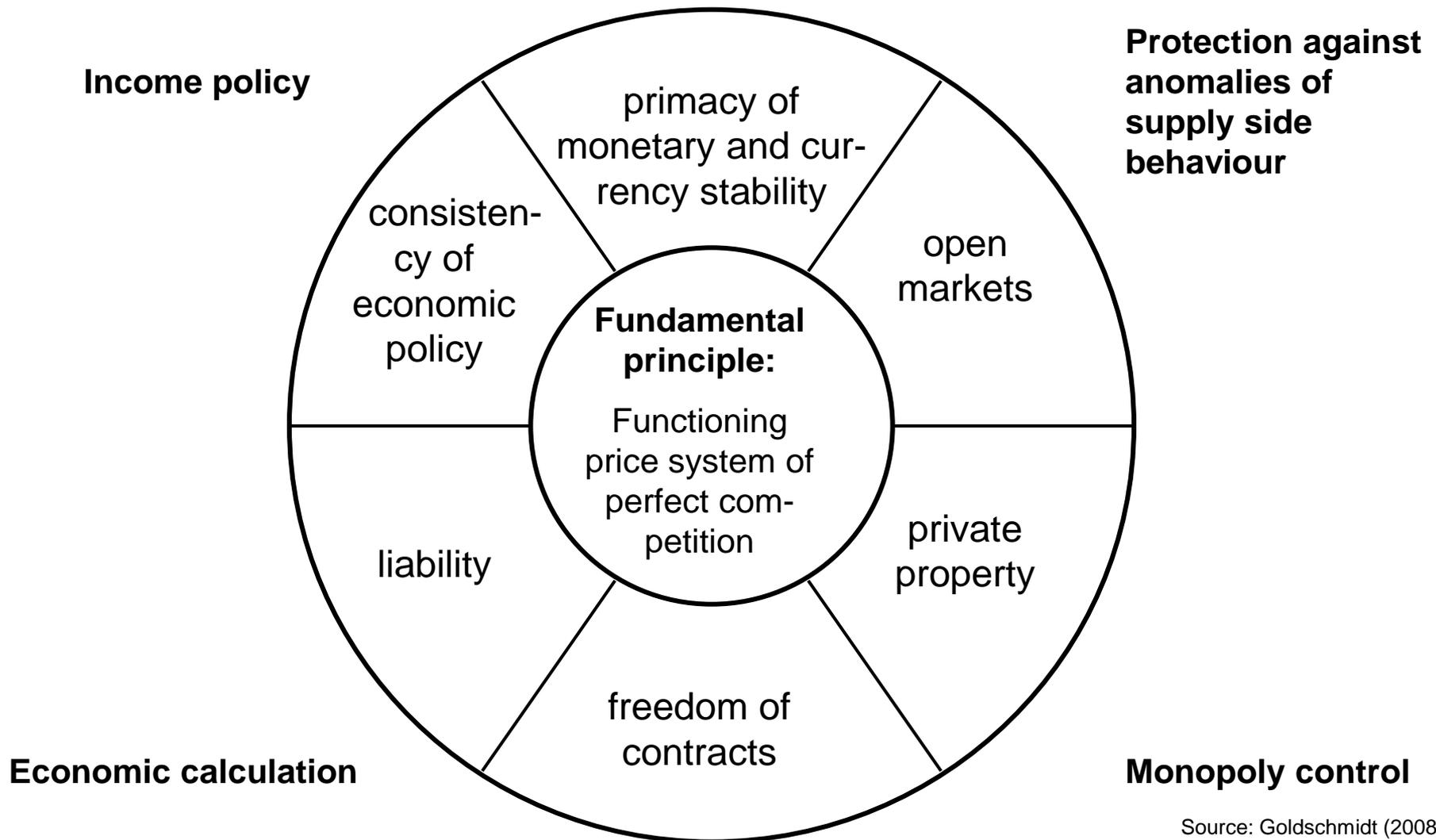
- **Constituent principles:**
  - Fundamental principle of the economic constitution: functioning price mechanism of full competition (“*Freiburg Imperative*”)
  - Primacy of monetary (and currency) stability
  - Free market entry (open markets)
  - Private property<sup>(\*)</sup>
  - Freedom of contract
  - Full liability (2010/11: higher own capital quota for banks)
  - Consistency of economic policy (against discretionary interventionism)

(\*) “Private property *may* lead to grievances, collective property *must* do so.” (1952: 317). Rejection of socialism and a centrally planned economy.

## 2. Walter Eucken and the Freiburg School (3)

- **Regulating Principles:**
  - Monopoly controls
  - Income policy
  - Corrections of external effects
  - Corrections of abnormal supply behaviour. In the case of an increase in labour supply induced by a reduction of wages, Eucken recommended *setting a minimal wage*.
- In the competitive order Eucken conceived, the *state* plays a substantially stronger role than in Hayek (who came from Chicago to Freiburg in 1961). This is particularly visible in the *regulating principles*. Full competition requires a strong democratic state who has primacy over the economy. It is evident that Eucken stands in the German tradition of *Staatswissenschaften*.

## 2. Walter Eucken and the Freiburg School (4)



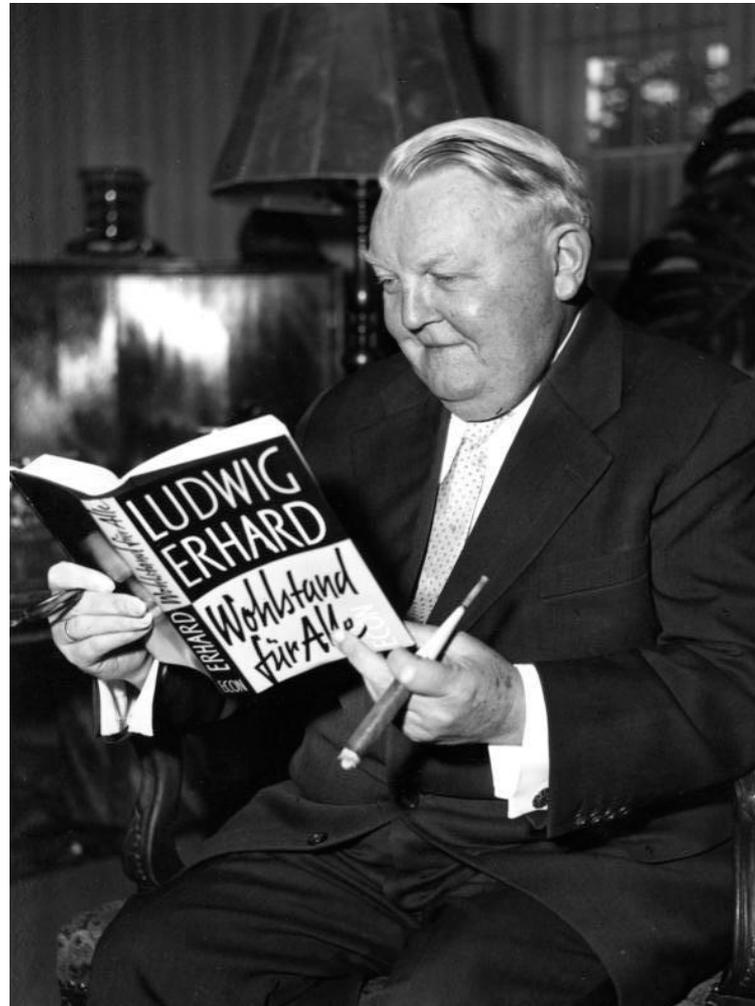
Source: Goldschmidt (2008).

## 2. Walter Eucken and the Freiburg School (5)

- since 1947 economic policy adviser of Ludwig Erhard
- 1947 Invitation by Hayek to the constituting meeting of the Mont Pelerin Society
- 1947 Report “Konzernentflechtung und Konzernauflösung”
- 1948 new journal ORDO – yearbook for the order of economy and society (together with Franz Böhm)
- 20 March 1950 Eucken dies during a lecture series at the LSE
- 1952 *Grundsätze der Wirtschaftspolitik* (Foundations of economic policy)

### 3. Ludwig Erhard: the father of the “Wirtschaftswunder” (1)

#### Ludwig Erhard (1897-1977)



Bundesarchiv, B 148 Bild-F04204-0003  
Foto: Adman, Bonn 1.25. Januar 1967

### 3. Ludwig Erhard: the father of the “Wirtschaftswunder” (2)

- 4 February 1897 born in Fürth (near Nuremberg; also hometown of Henry Kissinger)
- 1929 PhD with Franz Oppenheimer, Goethe University Frankfurt
- 1942 lost his position as Director/Editor, Institute for final goods, Nuremberg
- 1944 War financing and debt consolidation
- October 1945 Minister of Economics, Bavaria
- 20 May 1946 *Colm-Dodge-Goldsmith plan* for the liquidation of war financing and the financial rehabilitation of Germany / key role of Gerhard Colm (!)
- 1947 Honorary professor, University of Munich
  - Chairman “Sonderstelle Geld und Kredit” (Money and Credit)
  - Secret group of experts to prepare the currency reform

### 3. Ludwig Erhard: the father of the “Wirtschaftswunder” (3)

- March 1948 *Wirtschaftsrat* (Committee of economic experts elected from the members of the German regional parliaments) nominates Erhard as the Director “*Verwaltung für Wirtschaft des Vereinigten Wirtschaftsgebietes*”
- 20 June 1948 Currency reform in West Germany  
fundamental *internal* liberalisation in the trilateral (American/British/French) zone
- 23 May 1949 *Grundgesetz* (new democratic German constitution)
- Erhard is elected member of the first German *Bundestag* (constituency Ulm/Heidenheim)
- 20 September 1949 to 1963 Minister of Economics
- 16 October 1963 Erhard succeeds Konrad Adenauer as Bundeskanzler (Chancellor)
- 1 December 1966 Resignation in the German recession  
1<sup>st</sup> Grand Coalition forms the new government:  
Willy Brandt, Vice Chancellor and Minister for Foreign Affairs  
Karl Schiller, Minister of Economics

### 3. Ludwig Erhard: the father of the “Wirtschaftswunder” (4)

23 May 1949 The German *Grundgesetz* does not fix a concrete economic order. However, in Art. 14 it guarantees private property and mentions the social responsibility deriving therefrom. Art. 20,1 refers to the *Sozialstaatsprinzip*, i.e. the obligation of the state to form a social order.

1958 *Gesetz gegen Wettbewerbsbeschränkungen*  
(law against restrictions of competition)

1961 *Außenwirtschaftsgesetz*  
external liberalisation as a legal norm  
since Germany's entry into the European Economic Union in 1958 domestic firms are in competition with firms from European member countries

### 3. Ludwig Erhard: the father of the “Wirtschaftswunder” (5)

- 1957 *Wohlstand für Alle* (Welfare for everybody)
- Conviction that a market policy should always be adapted to the existing social relations
- Social market economy as a goal of economic order  
A market economy in which *monetary/price stability* and *full employment* co-exist!
- Discussion  
“Vater des deutschen Wirtschaftswunders”  
(father of the German economic miracle)  
versus  
*Reconstruction period*

## 4. Alfred Müller-Armack and the genesis of “Soziale Marktwirtschaft” (1)

### Alfred Müller-Armack (1901-1978)



## 4. Alfred Müller-Armack and the genesis of “Soziale Marktwirtschaft” (2)

28 June 1901 born in Essen (father director at Krupp)

1923 PhD

1926 Habilitation, University of Cologne  
“Economic Theory of Cultural Policy”

1932 *Economic laws of capitalism*

1938-50 University of Münster  
Professor for Economics and cultural sociology

1950 Professor and director, Institute of Economic Policy,  
University of Cologne

1952 Director, Dept. 1 – Economic Policy, German Ministry of  
Economics

1958 Secretary for European Affairs

1963 With Erhard becoming Chancellor, Müller-Armack resigned  
from his role in the Ministry of Economics

## 4. Alfred Müller-Armack and the genesis of “Soziale Marktwirtschaft” (3)

### 1941 *Genealogie der Wirtschaftsstile*

Of great importance for the genesis of the concept of the *social market economy*. Müller-Armack regards the economic process as a complement to the cultural and ethical development of societies. Openness of the competitive order for social questions

### 1946/47 *Wirtschaftslenkung und Marktwirtschaft*

The first work in which the concept of a social market economy which is based on ethical values is developed. Fundamental values of *liberty* and *social justice* as maxims.

## 4. Alfred Müller-Armack and the genesis of “Soziale Marktwirtschaft” (4)

The *Theory of the Social Market Economy* was developed as a *synthesis of liberalism, Christian social doctrines and a liberal socialism* (“freiheitlicher Sozialismus”). It was regarded as a “*midway*” between capitalism (which shortly after WWII was still discredited by the Great Depression) and socialism. Müller-Armack: “It would be a calamitous error to give the task of creating a final social order to the automatism of the market”

vs. *Hayek*: “A social market economy is a socialist market economy!”

1974 *Genealogie der Sozialen Marktwirtschaft*

Synthesis of the foundations and concepts of the social market economy

## 5. Neoclassic Synthesis: Erich Schneider (1900-1970)



- *Theory vs. Policy*
- *Theory*: early dominance of the neoclassical synthesis (until today)  
central role of Erich Schneider (who had done his habilitation with Schumpeter at Bonn)
- *Policy*: early dominance of Ordoliberalism (social market economy)  
Keynesianism came relatively late in international comparison (Karl Schiller 1966) and lasted less than a decade (1974/5 switch to supply side policies)

## 5. Neoclassic Synthesis: Erich Schneider (1900-1970)

At German universities the *Keynesianism of the Hicks–Samuelson neoclassical synthesis* had become the dominant position since the late 1950s. This can largely be attributed to **Erich Schneider**, whose three-volume Introduction into Economic Theory, originally published in 1946–52, became the dominant textbook in the 1950s and 1960s, going through many editions. Schneider became Professor in Aarhus in 1936, came back from Denmark in 1946 to become professor in Kiel, where he also directed the Institute of World Economics from 1961–9 (when he was succeeded by Herbert Giersch). From 1963 to 1966 Schneider was *chairman of the Verein für Socialpolitik*, which had been re-founded in 1948. When the influential *Theoretical Committee* was re-established shortly afterwards, Schneider exercised his power as chairman in the direction of *a more mathematically oriented approach*, which at the beginning had to overcome strong resistance (Schefold, 2004).

## 6. The high years of Keynesianism 1967-1974 (1)

Until the recession of 1966–7, however, **economic policy** was still dominated by **ordoliberal ideas**. As a consequence, *Ludwig Erhard*, who had been a successful Minister of Economics from 1949 to 1963, lost his job as Chancellor in December 1966, when the first ‘Grand Coalition’ of Christian and Social Democrats was formed. With the Social Democrats' entry into government and the ratification of the *Stability and Growth Act* in *June 1967*, **Keynesianism gained a relatively late admission into Germany**. According to Article 1 of the Act, the federal and state governments have to respect the requirement of macroeconomic equilibrium in their economic and financial policy measures which have to be taken in a way that they contribute, within the scope of a market economy, to simultaneously achieve *stability of the price level, a high level of employment, and external equilibrium* together with *steady and appropriate growth*.

These *four macroeconomic goals* appeared in the statutes of the German Council of Economic Advisers (CEA), which was founded in August 1963 and from autumn 1964 presented its annual report. The German council differs from the American in being an external and independent committee for policy consultation rather than part of the government.

## 6. Keynesian economic policy in Germany: Karl Schiller (1911-1994)



## 6. The high years of Keynesianism 1967-1974 (2)

In the public eye **Karl Schiller's** term of office as economics minister from the end of 1966 to the summer 1972 is remembered as the *heyday of Keynesian economic policy in Germany*. This is due to Schiller's remarkable ability to coin phrases such as '*Globalsteuerung*' ('macroeconomic demand management'), and his charismatic interpretation of economic policy which contributed to a widespread belief in the government's management power of macro variables, before the first oil price shock and the new phenomenon of stagflation shook that confidence. However, it should not be overlooked that *Schiller* had always followed **a synthesis of Keynesianism and ordoliberal ideas**. This is expressed most clearly in his influential article on economic policy in the *Handwörterbuch der Sozialwissenschaften* (Handbook of Social Sciences) (Schiller, 1962), in which he formulated his famous credo: '*competition to the extent possible, planning to the extent necessary*', with 'planning' understood in the sense of Keynesian demand management.

## 6. The high years of Keynesianism 1967-1974 (3)

Through his homage to *Eucken*, that is, in *supplementing process policy with Ordnungspolitik*, Keynesian policies took on a distinctly German tinge. This came against the background of discrediting the interventionist policies of the Nazi period, policies that were being pursued in Stalinist East Germany, and the need to safeguard the market economy against *Marxist policies* that were *finally given up by the Social Democratic Party (SPD)* only in its *Godesberg programme adopted in 1959*. In line with Giersch and the majority of the CEA, Schiller also advocated flexible exchange rates in the final years of the Bretton Woods system and in debates in the German 1969 election campaign when currency flexibility was heavily opposed by the Christian Democrats and the German export industry. The strong revaluation of the Deutschmark thereafter contributed to a dampening of inflation in Germany.

Balance of payments of the Federal Republic of Germany\*, 1978-2011  
 (in million DEM up until 1998, in million EUR since 1999)

year	current account balance		capital account balance	
1978	+ 18 034		+ 5 788	
1979	- 10 096		+ 9 643	
1980	- 24 250		+ 30	
1981	- 7 195		+ 7 654	
1982	+ 14 305		+ 2 542	
1983	+ 14 410		- 17 566	
1984	+ 30 627		- 36 261	
1985	+ 54 226		- 53 373	
1986	+ 88 214		- 76 783	
1987	+ 83 864		- 40 282	
1988	+ 92 585		- 122 721	
1989	+ 104 112		- 110 286	
1990 <sup>1</sup>	+ 73 021		- 89 497	
1991	- 40 182	demand pull	+ 12 715	high interest rate
1992	- 35 438		+ 16 574	
1993	- 31 450		+ 43 448	
1994	- 49 418		+ 60 708	
1995	- 42 363		+ 50 117	
1996	- 21 086		+ 24 290	
1997	- 17 336		+ 6 671	
1998	- 28 696		+ 25 683	

Balance of payments of the Federal Republic of Germany\*, 1978-2011  
 (in million DEM up until 1998, in million EUR since 1999)

year	current account balance	capital account balance
1999	- 25 834	- 10 396
2000	- 35 459	+ 34 187
2001	- 12	- 11 794
2002	+ 42 669	- 38 448
2003	+ 40 525	- 61 758
2004	+ 102 368	- 122 984
2005	+ 112 591	- 129 635
2006	+ 144 739	- 175 474
2007	+ 180 914	- 210 151
2008	+ 153 633	- 173 910
2009	+ 140 558	- 155 440
2010	+ 150 668	- 147 439
2011	+ 147 652	- 161 937

\*) Including the former GDR since July 1990.

Source: Deutsche Bundesbank, Monatsbericht Juni 2012

Current account of the Federal Republic of Germany\*, 1978-2011  
(in million DEM up until 1998, in million EUR since 1999)

year	current account balance	foreign trade	services	income	current transfer
1989	+ 104 112	+ 130 469	- 18 445	+ 26 872	- 34 784
1990 <sup>1</sup>	+ 73 021	+ 101 549	- 26 118	+ 32 859	- 35 269
1991	- 40 182	+ 19 095	- 30 724	+ 29 260	- 57 812
1992	- 35 438	+ 32 230	- 44 983	+ 28 481	- 51 167
1993	- 31 450	+ 57 187	- 52 549	+ 19 095	- 55 083
1994	- 49 418	+ 70 444	- 62 803	+ 2 393	- 59 451
1995	- 42 363	+ 81 109	- 63 985	- 3 975	- 55 413
1996	- 21 086	+ 93 597	- 64 743	+ 1 052	- 50 991
1997	- 17 336	+ 108 592	- 68 692	- 4 740	- 52 496
1998	- 28 695	+ 118 053	- 75 053	- 18 635	- 53 061

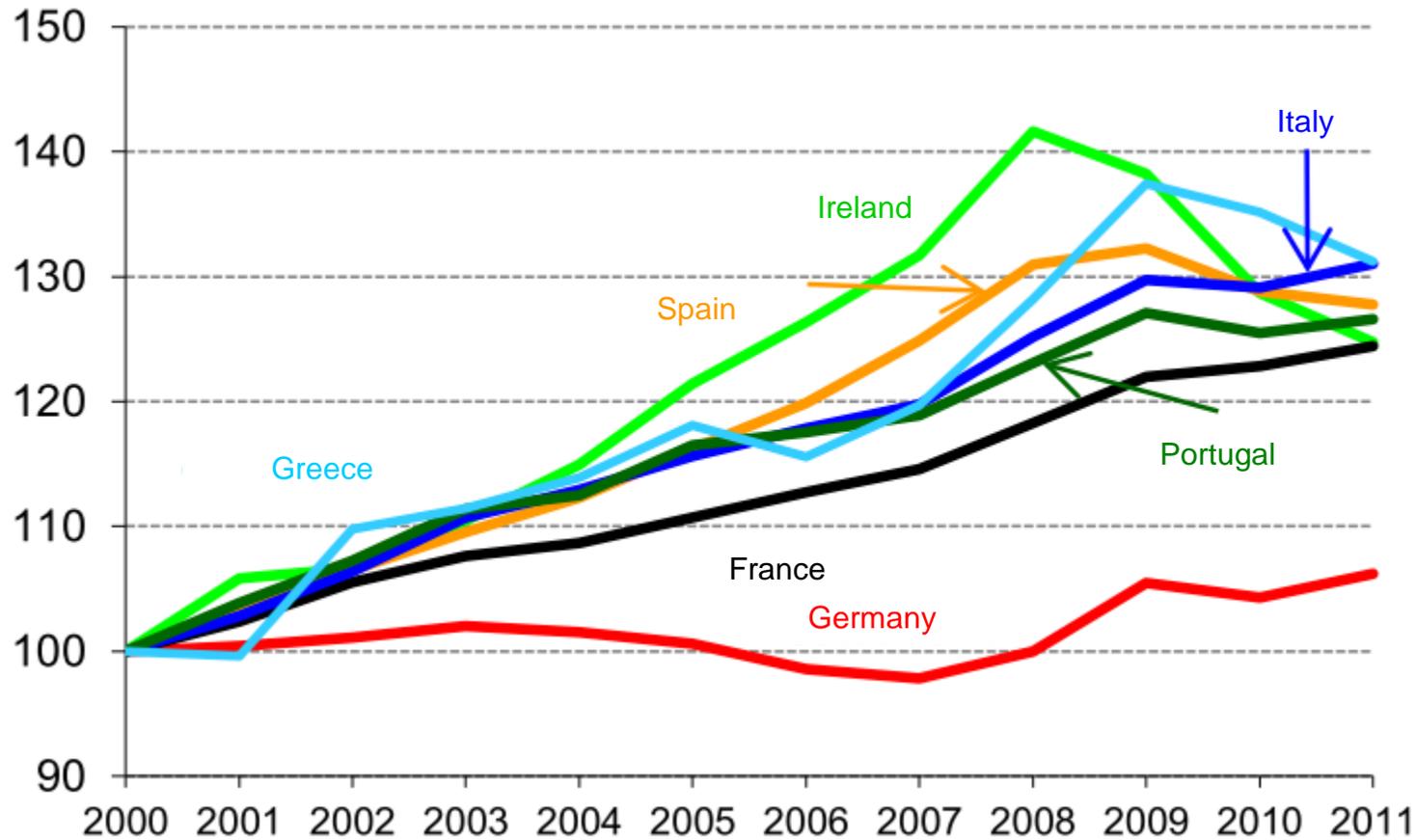
Current account of the Federal Republic of Germany\*, 1978-2011  
(in million DEM up until 1998, in million EUR since 1999)

year	current account balance	foreign trade	services	income	current transfer
1999	- 25 834	+ 57 058	- 46 035	- 12 457	- 24 401
2000	- 35 459	+ 50 057	- 49 006	- 8 670	- 27 840
2001	- 12	+ 88 075	- 49 862	- 11 533	- 26 692
2002	+ 42 669	+ 124 236	- 35 728	- 18 888	- 26 951
2003	+ 40 525	+ 118 773	- 34 506	- 15 677	- 28 064
2004	+ 102 368	+ 139 626	- 29 375	+ 19 681	- 27 564
2005	+ 112 591	+ 144 122	- 27 401	+ 24 391	- 28 522
2006	+ 144 739	+ 146 160	- 17 346	+ 44 460	- 28 536
2007	+ 180 914	+ 185 532	- 14 852	+ 42 918	- 32 685
2008	+ 153 633	+ 164 669	- 10 258	+ 32 379	- 33 157
2009	+ 140 558	+ 123 645	- 8 049	+ 58 120	- 33 158
2010	+ 150 668	+ 143 250	- 4 258	+ 49 864	- 38 187
2011	+ 147 652	+ 139 232	- 6 494	+ 48 415	- 33 501

\*) Including the former GDR since July 1990.

Source: Deutsche Bundesbank, Monatsbericht Juni 2012

# 6. Unit labour costs in the euro area, 2000 = 100



Source: IMK Report 71/2012