Markets over welfare: the consequences of liberalisation and the financial crisis

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Abstract

This thesis considers the 2007/2008 financial crisis as the cause and the catalyst for the establishment of the Eurozone response and the establishment of the European Financial Stability Facility, the European Stability Mechanism, and the expansion of the stability framework in which these operate. The thesis further considers the actions of Germany and France as the main contributors to the establishment of the rescue plan for the Euro. What are the implications of global change for European welfare states in the context of global and Euro Zone crisis? The German and French actions will be considered within a national framework shaping the EU's institutional processes. Germany and France have the ability to shape the state's understanding of its role within political economy and its responsibility to care for the welfare of its population.

These issues are investigated using a most similar case study approach. This approach will be complemented by Susan Strange's theory of structural power applied to Germany and France. This thesis will focus on Germany and France because of their status as Europe's two largest economies and motors of the European integration process. The analysis includes quantitative and qualitative data, which are used to investigate the change in the national conception of the role of the state within the economy and its requirement to provide welfare to its people. This thesis will demonstrate that the German and French states' reconfiguring of state-society relations, leads to the end of the traditional concept of the state. The thesis will also demonstrate that unilateral movement on the side of either Germany or France will likely result in long term adverse political economic consequences for Europe, which can be averted if Germany and France manage to develop and most of all maintain a balanced effort to resolve the Euro crisis.

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Glossary of Terms:

Bündniss90/ Die Grünen	The Liberal and Green party in Germany (Left)
BverG	Bundesverfassungs Gericht/ Constitutional Court
CA	Contrat d'avenir/ Contract for the future
CAE	Contrat d'accès à l'emploi des jeunes/Youth employment contrat
CCE	comité central d'entreprise/Central committee of the company
CCT	convention collective de travail
CDD	contrat de travail à durée déterminée/ Limited work contract
CDI	contrat de travail à durée indéterminée/ Unlimited work contract
CDU	Christlich Demokratische Union Deutschlands/ Christian Democratic Union Germany (Conservative)
CE	conseil d'état/National council
CFT	Confédération française du travail/ French work confederation
CGC	Confédération générale des cadres/ General confederation of white collar workers
CIE	Contract Initiative Emploi
CSS	code de la sécurité sociale/Social Security Law
CSU	Christlich Soziale Union in Bayern/ Christian Social Union of Bavaria (Sister Party Conservative)
ECB	European Central Bank
EFSF	European Financial Stability Framework
EMU	European Monetary Union
ESM	European Stability Mechanism
EU	European Union
EZ	Euro Zone
FConC	Cour constitutionelle/ Constitutional court
FDP	Freie Demokratische Partei Deutschland/ Free Democratic Party Germany (Centre Right)
FO	Force ouvrière/ Worker's Force
FUO	Front ouvrier unique/Single workers front
GG	Grund Gesetz/German Constitution
MEDEF	Mouvement des entreprises de France/ Movement of French enterprises
NAO	négociation annuelle obligatoire/ Annual compulsory negotiation
PCF	Partie Communiste Français (far left)/French Communist Party
PS	Partie socialiste (left)/ Socialist Party
RMI	revenu minimum insertion/Minimum salary for reintegration
RMM	revenu minimum mensuel/ Minimum monthly wage
SGB	Soziales Gesetzbuch/ Social Security Law
SMIC	Salaire minimum interprofessionnel de croissance/ Minimum inter-Professional wage for growth
SMIG	Salaire Minimum Interprofessionel Garanti/Minimum Wage
SPD	Sozialdemokratische Partei Deutschland/ Social Democratic Party Germany (Center Left)

UA	Unité et Action/ Unity and action
UMP	Union pour un mouvement populaire/ The union for a popular movement (right leaning)
WB	World Bank

Chapter 1 Introduction

1.1 Introduction

The neo-liberal capitalist system aims to reduce the presence of the state in economic affairs to a minimum and replace state governance with market forces (i.e. to liberalize the state). The modern state, however, draws its legitimacy from a responsibility of care for its citizens. The 2007/2008 financial crisis was the latest result of the application of the neo-liberal market economic logics, to national economies and the global market, to develop them into a “perfect” neo-liberal economic system, (including the inconsistencies which that system produces). This makes this crisis similar to other economic crises that have resulted from neo-liberal market economics.

The particularity of this crisis derives from the failure of the financial structure of the modern state capitalist system as a result of the establishment of the perfect financial economic system (Crouch 2011). Since the power structure of finance had become global and closely linked to the political and economic structures of nations, its survival had become a political and economic necessity (Crouch 2011). The failure of finance demanded firm and decisive action by the state, which resolved to fiscalise the financial crisis through loans to and nationalisations of financial institutes. This solution, however, had consequences for the Euro Zone, which it was unprepared and unable to deal with due to its power structure at the time. The influence of the financial power structure caused a lack of regulation and supervision, which was encouraged by the neo-liberal concepts imbued within the European Exchange Rate Mechanism, the Maastricht (1992) and subsequent European Union treaties.

Due to the global nature of the financial power structure, this crisis affected all parts of the world. It not only affected the global south but also the richest part of the world; the global north, providing further evidence of the global reach of the neo-liberal economic concepts and their structural power. It caused poverty on a scale unseen in this part of the world for decades. It was worsened by the fact that the European welfare systems that were supposed to alleviate want at the time of the crisis were already at a point that made them unsustainable in the long term for the countries to continue to maintain the way the systems were functioning prior to the crisis.

As this thesis will show, the EU welfare system was part of the Classical/Keynesian economic system, which had global reach before being replaced by neo-liberal concepts of economics. Due to the neo-liberal economic concepts, European states are torn between two choices to resolve this crisis. The first is, maintaining spending and fulfilling their duties towards their citizens as per the social contract, in the face of hostile market logics. The second is, bending to these same logics and instead reducing budgets and consequently welfare provisions in line with market expectations in order to give it the space and the confidence necessary to grow the economy.

The Eurozone response was made more difficult due significant deficiencies within the setup of the Euro common currency, stemming from its constituting Maastricht Treaty, negotiated and pushed forward in great part by Germany and France and their own national concepts of Central Bank (CB) responsibilities. The most glaring problem stemming from the treaty is that the European Central Bank (ECB) is not linked to any one particular country and that the Euro Zone and the European Union are themselves countries in their own right. Hence the value of the Euro currency is not secured by one country but by many with each country having individual levels of debt, individual finances, individual budgets and an individual default potential whose realisation would worsen the crisis.

France and Germany provide excellent examples of countries enacting different solutions to the problem of financial crisis. German actions against this crisis favour reducing debt by reducing state presence within the economy increasing competition in the labour market and reducing welfare benefits; this act privileged the market instead of the state to create growth. France's initial impetus was to stimulate growth through state spending and continued high levels of welfare provision, maintaining strong state involvement focussing largely on influencing labour demand and maintaining purchasing power. While its position has evolved over time and across presidencies, the French government maintains its support towards investment strategies to resolve the current stagnant European economy.

German and French solutions set the trend for other countries to emulate, not least because of their power within the EU institutions. Due to Germany's growing economic power compared to its Euro Zone neighbours (especially France), Germany's influence has grown within the institutions of the

EU Commission, the ECB and the European Stability Mechanism (ESM). These policy-setting institutions, have allowed Germany's solutions to dominate. However, the continuingly low economic performance has given French arguments a boost; that being said, the German government maintains its dominance within this area.

Therefore, if a country finds itself in a situation of potential default within the Euro Zone, they may enter below the umbrella of the ESM and to receive its aid. This entry comes with conditions of austerity attached derived from the structural power of neo-liberal economics, which are set by the European Commission and the ECB with the support of Germany and France.

This thesis argues that this solution is, however, doomed to failure over time. As the data analysed in this thesis will show, state non-intervention is as bad as the state intervening in an overbearing manner. Therefore, allowing the state to remove itself significantly from the guidance or investment within the economy and be replaced by a neo-liberal "free market" is neither sustainable nor an economically successful strategy for long-term economic functioning. The state should follow the mandate that was given to it by previous generations to serve and protect the people before it protects the markets in as much as the neo-liberal economic structure allows. In order to demonstrate the inherent challenges that welfare states face in operating in the Euro Zone, the thesis asks the following question.

1.2 Research Question

What are the implications of global change for European welfare states in the context of global and Euro Zone crisis?

1.3 Research Significance

This thesis considers a chain of events, which had not occurred before in this form in international political economy. Although the 2007/2008 financial crisis follows the pattern of previous crises, this crisis differs from other crises in that it affects the entire financial system. Nations reacted to this 2007/2008 crisis by intervening in the market, which significantly increased the national debt. In the Euro Zone (EZ), this presents a unique and significant problem, since the EZ is comprised of a block of 17 autonomous nations sharing one common currency and are subject to a number of common economic and financial rules, which this crisis has fleshed out further and which the EU and its institutions have begun to enforce more consistently.

The 2007/2008 financial crisis caused a deep economic recession in the Euro Zone countries as well as the fiscalization of the financial debt of national banks. These events caused long-term consequences for national deficits and public (particularly welfare) spending. This thesis will investigate and compare political economies of Germany and France and the international political economies in relation to Europe. The thesis will compare and critique the understanding of public (particularly welfare) spending in Germany and France and their use of "neo-liberal" and "classical liberal" political economic theory in the use and application of that spending. The significance of this comparison focusing on the ideology behind these theories and the actions, which Germany and France have undertaken before the 2007/2008 financial crisis, are based on those political economic theories. Those reforms will in turn guide the course of European responses and reforms to the Euro Zone crisis as far as the prevalent neo-liberal economic concepts within the European institutions allow this.

Because of the financial debt accrued by the banks (before the 2007/2008 financial crisis was too great), many European governments fiscalized (i.e. paid off the private debt of the banks with public funds usually by raising public debt) that debt, to prevent a collapse of the market economy since it was now structurally bound up with the survival of the state. As a result, national deficits soared. In the aftermath of this crisis, economic stagnation set in, and sovereign default among Euro Zone members became a real possibility. The German and French governments heavily influenced the European response to this crisis. This influence was infused by neo-liberal and classical liberal ideology, the structural powers' finance and the powers of France and Germany exerted within the European Institutions (European Council, Council of the European Union, European Commission, European Central Bank, European Stability Mechanism). It resulted in a re-evaluation of public spending and government involvement in the economy at the European level along neo-liberal economic concepts. *This re-evaluation of public (especially welfare) spending, if it continues to remain unchallenged, will determine the spending policies of governments for the coming generation*.

This re-evaluated form of public spending has gained ascendancy within the EU, through the establishment of the ESM, the stability and growth pact and through the agreed tight controls in these contracts. The threat of austerity of countries once under the ESM umbrella also puts pressure on all Euro Zone members to *liberalise* their welfare provisions. These liberalisations bear close resemblance to the reforms instituted in Germany in the late 1990s. The next section will consider the reasoning behind the assertions that are made here.

1.4 Argument

The national concept of welfare is intimately linked with the capitalist political economic ideology, which guides that nation. The EU as a political economic entity has a neo-liberal ideology guiding its processes. The evidence of this can be found in its single market and free trade policies. Member states, particularly Germany and France, also guide the ideological development of the EU by reinforcing the neo-liberal ideology (Germany) or by attempting to change it (France).

The 2007/2008 financial crisis and the setup of the EZ have allowed this neo-liberal EU ideology to be extended to the subjects of national debt, public (particularly welfare) spending and state involvement in national economic activity. This extension of EU authority has taken place under the guidance of Germany. Germany’s national ideology was reformed during the period of 1998-2005, and reflects most closely the current European neo-liberal political economic ideology. France, which has a political economic ideology that has not been reformed in accordance with the neo-liberal concepts prevalent within the EU, does not fit within the current EU neo-liberal ideology. Consequently, it has lost in power and influence at the European institutional level. This neo-liberal re-evaluation of European policy moves towards a scaling back of state interference within the economy through greater budgetary austerity and increased market powers. Particular focus is on welfare, which, due to its close links with economic activity and state interference within that activity, is considered as an impediment to market forces and proper market development.

Therefore, a dominant economic and thereby political influence of German power and German concepts upon the EU institutions will amplify the already latent neo-liberal tendencies of Europe likely resulting in positive economic tendencies and negative political consequences. A dominant economic, and thereby political, influence of France would cause a reverse result. It would likely cause negative economic consequences and positive political consequences. This thesis concludes that the best solution is a combination of both ideological approaches. This involves an appreciation for the welfare of the people while at the same time catering for a number of market demands.

1.5 Theoretical Framework and Method

This thesis uses structuralist theory, power theory, historical analysis, time series analysis and most similar case studies to answer the question posed at the beginning of this thesis:

> What are the implications of global change for European welfare states in the context of global and Euro Zone crisis?

I understand states to be the primary actors within the national and international arena subject to the economic restrictions of the economic framework countries must operate in. The power exercised by the states and by the global economy does not flow directly to the subject it is intended to influence, but does so through an intermediary institution - i.e. through different structures of power (see Lukes 2005 and Galbraith 1983). In this thesis, I will focus on one particular structure.

The main power structure in this thesis, which in my view permeates through the international and national political structure, is the *financial market structure*. Susan Strange's concepts of the structural power of markets (financial markets in particular) on states are used predominantly in this analysis (Strange 1996, 1997, 1998, 1999, 1986, 1970, 1986, 1987, 1988). This power structure shapes all other structures, particularly the national institutional structures such as state intervention and public spending (welfare) and international institutional structures such as the European Union Institutions. In order to provide a better understanding of how the structural power of the markets manages to unfold its powers within the nation or on the global scale, this thesis will consider the works of Colin Crouch (2011) and Kenneth Dyson (2002, 1983). Crouch (2011) therefore considers the industry-state nexus and the influences industries wield within the state. Dyson's (2002, 1983) analysis focuses more closely upon the state tradition, i.e. the manner in which the state negotiates its relationships within industries. Their analysis allows this thesis to understand how the structural power described by Susan Strange can permeate through international and national political structures.

To underscore the global nature of this crisis, this thesis focuses on the run-up and the development of the US financial crisis. This analysis will also serve as an evaluation of the consequences of the unshackled power of financial market structures. It will also demonstrate the German and French responses to the aftermath of the crisis created by that unshackling. Therefore, an additional point that needs consideration is the influence that German and French economic concepts can exert within neoliberal European economic structures, especially since the global capitalist market exerts its pressures on those structures as well.

This entire thesis is defined by a most similar systems analysis (Peters 1998) of France and Germany since both Germany and France share a number of social and economic similarities. Both countries are closely integrated in international institutions as well as sharing a common currency. They are long standing trading partners as well as political partners on the European stage. They are the two biggest economies in Europe. In order to understand the power of Germany and France within the European institutions and the power of Germany and France to shape these institutions, the thesis will undertake two types of analyses. First, a historical analysis of German and French government conceptions of welfare and the state's role in its provision will be provided. This analysis will show both the evolution of the concept of welfare the role of the state in providing that welfare and the state's role in society.

Second, the thesis will consider the economic performance of Germany and France. The timeframe will be the 1950s onward, in order to demonstrate the evolution of both economies. Particular interest will be placed on the time from 1998 to 2014 in Germany. This timeframe comprises the institution of the Hartz reforms, which changed the state's interventionist role within political economy. It also comprised the time when the financial crisis struck Europe. In France, particular interest will be given to the time period from 1981 to 2014. This was the period when, except for the first and the final years of the timeframe analysed, the pace of reforms was more elevated than in the intervening years.

Finally, the last chapter of this thesis will provide a comparative picture of Germany's and France's political economic performances. A comparative investigation of both countries will highlight the political-economic differences and commonalities between the two, which will allow a synthesis to be established of a potential common course of action for the EZ crisis resolution.

1.5.1 Theory of the EU

Another important factor in understanding how Germany and France are able to shape the debate and provide policy direction for European Union institutions is the setup of the EU. It is my argument that within Europe, beginning with the Rome Treaty (Rome Treaty 1957) and coming to realisation in the Maastricht Treaty (Maastricht Treaty 1992), a political economic hegemony was allowed to reign over Europe in the form of French and German cooperation. This Franco-German cooperation was established by the institutional development of the EU and the power it provides to the individual states to shape and approve the political economic direction of Europe (through the European Council and the Council of Ministers (McCarthy 1999, Schmidt 1999, Schneider and Vedel 1999, Rhodes 1999, Bloch-Lainé 1999). It was this Franco-German cooperation that drove the European integration process forward throughout the last half-century (Mazzucelli 1997). The consequent integration process transferred many formerly sovereign powers to European institutions and into the realm of collective decision-making among countries.

To be able to understand the political-economic evolution of welfare over the last 7 years, this thesis will put particular focus on the actions of Germany and France within the Euro Crisis and how the German and French actions are translated and implemented on the European level by European institutions. In the EU decision-making process, the EU Council decides upon a policy direction. Within the Council of Ministers in this context, the finance and economy ministers of the 28 EU members make the decisions in the Council grouping, called Ecofin, (European Commission 2012, 17). This process is complicated by the existence of the Euro, more precisely by the fact that not all 28-member states have the Euro as their currency. Therefore within the Ecofin Council is a separate grouping called the Eurogroup, which determines the *economic* policies of the EZ. The decisions taken by the Eurogroup are then voted on within the Ecofin Council, although only the ministers of the Eurogroup are allowed to vote on those issues (European Commission 2012, 17). The ECB president and the European Commissioner for Economic Affairs are also present during the Eurogroup meetings (European Commission 2012, 17). Therefore, the Eurogroup imposes the austerity policies within other EZ member states. The European Commission and the IMF only play supporting roles in this analysis, despite their position as overseers of the Euro rescue (RIEAS 2011). The ECB is with the Council of Ministers and the European Council, the only institutional player of primary importance as it is the only institution, which can actively participate and influence the markets with its monetary politics. The Commission has only a supervisory role to ensure that the decisions taken by the Eurogroup are followed. This is also because the ECB Chair confers with members of the Council of Ministers and the European Council over economic policy within the Euro Zone as well as being independent.

Therefore, in order for France and Germany, to achieve a certain result, power is exercised through the structures above. These actions in turn are shaped by the power of the neo-liberal ideology on the German and French states' conceptions of state and welfare involvement in the economy. These conceptions are shaped in turn by the global economy and Germany and France's understanding of their role within it (Dyson 2002, Dyson and Wilks 1983). Through the interpretation of that concept, first by Germany and France, and then through them by the European Union, the EZ nations are compelled to implement certain notions of austerity and welfare provision.

The Euro and its framework of rights, responsibilities and duties, were a direct result (Hayat and Farvaque 2012, DeGrauwe 2013) of the negotiations and desires and fears of the respective French and German governments at the time of renegotiation. These negotiations were done within the framework and limitations of the European Union Treaties and European Institutions, which in turn are subject to national bargaining and negotiating in order to bring about a *politically acceptable* solution. Such a solution may not necessarily be a *workable and sustainable solution* from a political economic perspective.

France's reason for wanting the Euro was its desire to put an end to the power the Bundesbank (German Central Bank) (GCB) directives and reasoning had on the French economy. It was also to break the *de facto* German hegemony over EU monetary policy since many currencies (including the

French Franc) were pegged against the Deutschmark (DM). Germany desired the Euro since it was afraid of an overly strong DM, which would mean a greater responsibility of the DM on the international market and, more importantly, the loss of Germany's export advantages because of the strength of its currency (DeGrauwe 2013). Since the Euro was established by common agreement between France and Germany, though with differing reasons, Germany and France remain the two principal powerhouses behind the Euro's continued existence both politically and economically (DeGrauwe 2013).

The reason why I argue that Germany has become the European hegemon over France is because of its stronger economic performance, not only compared to France but to compared to the EU as a whole (and its more enthusiastic espousal of global neo-liberal economic pressures). It allowed Germany to spread its ideological understanding of neo-liberalism to other countries within the Union without effective moderation or countering by France; in fact, the hegemony even operated with the agreement of France (see chapter 7), which the President Sarkozy gave to Chancellor Merkel. With the election of François Hollande, this support has largely been replaced with opposition. However, Germany manages to maintain its ideological influence not only because of the relative lack of power of France but also because of its until recently continued support of German plans (its agreement being the most significant hurdle for Germany to overcome), and because of the fact that the treaties governing the ECB and the monetary power within the Euro Zone are not defined clearly enough.

In addition, the ECB's powers are not wide-ranging enough in order for it to deal with the crisis in a more decisive manner (DeGrauwe 2013; Pasini 2013). The ECB does not have all the powers and rights of a national central bank, and, more importantly, there is no single country backing the currency in question. This leaves a lot of room to manoeuvre for countries like Germany to spread its influence and its doctrines. This point is further amplified by the fact that the ECB was modelled after the Bundesbank (GCB) in its independence, responsibilities (with some exceptions) and ideological direction (DeGrauwe 2013, Pasini 2013). The German Constitutional Court's (BVerfG) decisions on the ESM and the EFSF limiting the German exposure within ESM and by extension the applicability of the ESM EFSF bear witness to the importance of Germany within this process (BVerfG 2012).

Despite its shortcomings, the ECB is also a powerful actor. Its greatest tool thus far is the setting of lending rates across the EZ allowing it to manage economic activity (to a point). Its stated intention to buy unlimited amounts of treasury bonds on the secondary finance market is also a powerful tool (Traynor 2012). However, the question of whether the ECB is legally empowered to do this remains unclear, which is another major weakness. The ECB's power is limited by the unclear formulations of its authority in engaging within the financial markets, leaving uncertainty and possible legal exposure, which would set bad precedents in International Law. In addition, the uncertainty in its authority allows Germany, France as well as other EZ members to block or fight any actions that it deems "wrong".

After presenting the approach taken by the EU, it is important to introduce structural theory since this theory will ultimately be responsible for demonstrating how the crisis in the USA and the EZ has happened. Structural theory will allow this thesis to demonstrate how countries use their power to shape their relationship with the EU and thereby shape the EU itself. This national exercise of power on the EU and the national exercise of power with other countries will shape those interactions.

1.5.2 Structural theory

This section shall investigate Susan Strange's concept of structural power. Strange in her later writing (1999,1998,1997,1996,1995) focussed on state action, market action and the consequences of their interplay. She did so by arguing that states worked with or against each other through the intermediary of the market. She also pointed out that such state influences on the market would also work in reverse, i.e. that the market could influence the state. Crouch (2011) echoes this statement.

Firstly, this thesis starts by defining Susan Strange's concept of structural power. Strange (1996) saw IR (and to some extent IPE theorists) as being fascinated with relational power, which she saw as too narrow a focus for the concept of power. Strange argues that power is not just a direct application of "force" by one agent on another. Relational power in Strange's view implied an active use of power on individuals which is seen by political and social theorists such as John K. Galbraith (1983) and Steven Lukes (2005) as the most inefficient and dangerous use of power as it ignores other forms of power as well as the social relations of power and its consequences. It also implied that power was being used consciously, with a specific (measurable) goal in mind.

Strange (1988, 1996) disagreed with this relational conception of power, arguing that power was far more diversified than was assumed by traditional IR and power theorists such as Kenneth Waltz (1979, 1983, 1986) and Robert Gilpin (1975, 1981, 1987). Strange (1988, 1996) argued that not only was power something that could be measured by how someone else responded to it, power also had other non-measurable effects. Power was exercised by the very presence of an actor within a given situation without the actor engaging in any kind of activity (non-decisions) (Strange 1996). Not only were all the effects of the exercise of "direct" or "indirect" power never completely knowable, but traditional IR only focussed on the exercise of power and the receiver, ignoring any other actors that were involved or were impacted upon by the use of relational power. To Strange (1988), political economic systems have different priorities and the actor who holds that structural power therefore holds the authority to decide what priorities to take. The analysis conducted by Crouch (2011) complements Strange's analysis as he saw that power residing within industries (financial and other) and through their lobbying work, state action or inaction was determined.

The concepts also track closely the concepts of two-dimensional and three-dimensional power developed by Steven Lukes (2005). Lukes (2005) argued that three dimensions of power existed: direct, one-dimensional i.e. relational power; indirect, two-dimensional i.e. power to control the agenda and three-dimensional i.e. conceptual power, the ability to understand the many ways power is exercised through decisions and non-decisions (Lukes 2005, Foucault 1980).

> Complexity, in a word, is inseparable from the study of cause and effect when it comes to outcomes in international political economy (Strange 1996, 28)

To Strange International Political Economy is a complex subject where the cause and the effect of actions are interlinked. The causal link is important in Strange's theory because of the power relations in the power structures in Strange's theory. Strange also points out that causal linkages are complex in international political economy, which can be seen in the argumentation throughout this thesis.

In this sense, Strange's view of power seems to also borrow some of its aspects from Michel Foucault (1980), especially from his ideas of performative power (Foucault 2008, 1984). Power is exercised through the manipulation of the structures of power (Strange 1988).

> The relative power of each party in a relationship is more, or less, if one party is also determining the surrounding structure of the relationship (Strange 1988, 25)

In Strange's (1988) theory, the structures of power were composed of *four primary structures*: the security structure, the production structure, the financial structure and the knowledge structure. It was also composed of four secondary structures: transport systems, trade, energy and welfare (Strange 1988). To Strange, it is only through the control of these structures of power that states or firms are able to shape society. This thesis argues that Germany exerts financial and production control within Europe due to its high production and high financial investment in the EU rescue.

The security structure encompasses the provision of security by one set of individuals towards another set of individuals. The provision of security is a task that largely falls under the authority of the state. The Treaty of Westphalia stated that states had sovereignty over their soil. This included being the sole authority within their country, which means that the state is the only actor allowed to use violence against the populace or against another state (Clausewitz 1922). In neorealist theory, this is one of the main means of diplomacy, as it can be used either as an offensive force or as a deterrent as witnessed during the Cold War (Mearsheimer 2001).

Production is crucial to society for it is the only way in which to satisfy human needs and desires (Cox 1987). The production structure is one of the loci of power of the social formation. Production is the wealth creating apparatus of the state, seeing that production is mainly done by labour; a change in the workforce will inevitably lead to a change in production and therefore change the amount of wealth in the country (Strange 1988). It is thus essential for the dominant social class to be in control of the labour force, or at least have its backing (Cox 1995; 1987).

The knowledge structure (Strange 1988) is the structure that is the least well understood. Knowledge itself is unquantifiable as well as illusive. Although as Strange argued, one cannot quantify knowledge, it is however possible to analyse changes within the knowledge structure. Strange (1988) argued that a change in the type of information, its sophistication and the value judgements that are made about the information all are good indicators of knowledge progress or regress.

The final structure of power is the financial structure. The ability to create credit is crucial to capitalist development, thus the *ability* to *create* and *withhold* credit from others, provides the holder with a great advantage and a large amount of power (i.e. political, economic and social) (Strange 1997). Strange discusses particular arguments on this score (Strange 1986, 1995, 1998): the unshackling of the financial structure has taken away that power from the state and given it to the financial markets instead. This was immensely lucrative for the states as well as for the financial markets. Nevertheless, it also had significant drawbacks, which will be elaborated in Chapter 2. As Crouch (2011) has identified, compliance of states with neo-liberal concepts of financial non-intervention (Strange 1996, 1997, 1998, 1999, 1970, 1986, 1987, 1988) was tremendously lucrative for governments and for people, as it allowed for higher levels of consumption without the use or need of savings due to the easier access to credit.

The creation and/or denial of credit have major implications for society. For example, the variation of credit in circulation has a direct impact on the productive capacity of a firm, a region or a country. The amount of credit circulating in an economy determines the amount of production, as the availability of credit determines the amount of money in circulation at any given time. The resulting inflationary (more credit available) or deflationary (less credit available) pressures directly affect the economic performance of industries within countries as well as their economic and political standing among other nations. This in turn will cause a domino effect, affecting a wide range of different areas such as the country's default potential and its exchange rates. Nations and companies are linked to the value of their currency, but they are also linked to other nations and other companies through that currency (Strange 1988). The interplay of the creation of credit with the non-decisions of states that allow for the use of this provision of credit by the state, reinforces the links of state with industries and further fosters the culture of non-decisions. This in turn created an extremely volatile market (Crouch 2011) (see Chapters 2 and 3).

The following structures are termed *secondary* - not because they lack in importance -but because they are subject to the uses of the four primary structures (Strange 1988). At the time of Strange's writings, the secondary structures were also nationally limited. The states themselves guaranteed the provision of infrastructures in the areas of transport, energy, trade and welfare within their borders. However, with the institution of the Maastricht Treaty, neo-liberal economic principles have also started to enter into traditional areas of nation state influence, as the points enumerated by Strange (1988) will demonstrate. This list is by no means exhaustive; however, Susan Strange's theory was chosen for this thesis in part because of the choice of secondary structures. Strange's choices of secondary structures do provide an excellent example of their dependence upon both the national and international structures, particularly in Europe.

Trade represents the first secondary structure. It is also the most integrated secondary structure within the European Union since free trade forms the cornerstone of the Union's establishment. The trade structure is by far the most politically and economically enmeshed structure on the international structure, as superior bargaining power internationally counts towards the political and economic strengths of a country. Trade is a constant exercise of compromising between certain elements of national security (military and economic) and the opportunity to gain from trade (Strange 1988). Europe has become a free trade zone in its own right with common tariffs and regulations for import and export, which is a textbook requirement of neo-liberal economic theory.

One reason for the complexity of trade stems from its history. As Wallerstein (1974, 1980, 1989) notes, the modern western trade and economic system has been developing since the mid-15th century. From 1600 onwards came a consolidation phase within the world-economy, brought about by the economic stagnation in Europe at the time. The economic stagnation coupled with the appearance of the Dutch hegemon and the economic thinking of mercantilism (defining economics as a zero-sum game) caused struggles between the core and the peripheral European countries to erupt and continue throughout the 1600s (Wallerstein 1980). The hegemonic struggles were eventually won by England, which ushered in the second era of expansion starting around 1730. The era of the British hegemony ended in 1913 (Kindelberger 1986), to be replaced by the USA. Its era of hegemony started in the 1950s and its end is argued to be in the 1970s (Kindelberger 1986) though this date is contested at present (Strange 1999).

The building, maintenance and improvement of the transport system remain a continuing responsibility of the states that set them up. However in the case of Europe, common funds can be allocated to improve transport systems within the member countries through structural adjustment funds (European Commission 2008).

With the continued waves of economic liberalisation following from the Maastricht Treaty, the free flow of capital and goods has already become a reality (Maastricht Treaty 1992). Thus transport systems across the EU have become and continue to become more integrated and they do so across all of the different modes of transport. The best example thereof is the continuing interconnection of the European Rail network, especially between the Benelux countries, France and Germany (European Commission 2008).

The third secondary structure is energy. Since the Industrial Revolution, energy has become essential to the working of any economy, so much so that without energy (including a secure supply thereof), modern large-scale production would be impossible. Modern society has become so energy dependent; energy shortfalls would have disastrous economic as well as political consequences (Strange 1988). However, the influence of EU institutions has also started the process of integrating energy markets within the EU. Whereas energy production priorities are still part of national policy priorities (Germany *energiewende*) (Morris, Pehnt 2013), environmental regulations on a European level already produce a frame of reference for energy production.

Transport, energy and trade, are issue areas where the European Union and its different institutions have started to put forward a common direction. Subsequent treaties have reinforced, refined and communalised many aspects relating to these areas leading to a continued integration of these structures within the policy making of the EU. The only secondary structure where, thus far, there has been no coming together on a European level, and which has therefore remained solidly within the realm of national authority was *national* welfare. This thesis notes that the EU does have a social policy, but it is focused largely on worker protections linked to the protection of the common market.

When talking about welfare it is worth noting that Strange (1988) in her analysis identifies two types of welfare provision: national and international forms of welfare provision. International welfare is a completely separate issue to national welfare and its own separate issue area within European policy. International welfare refers to the transfers of national aid in the form of money, food or other production goods to countries, which cannot afford them by themselves (external redistribution of wealth). This is the reason why the WHO was created (Strange 1988; see Jacobson 1974 on the creation of the WHO).

National welfare is government-sponsored healthcare, unemployment help, education etc. (internal redistribution of wealth). Welfare provides crucial benefits to the state and to industry but especially to its population. Although it kept the peace after the war, its institution was never without its opponents, both on the right and on the left (Offe 1984). Welfare in this thesis refers to national welfare unless expressly stated otherwise.

It is the argument of this thesis that the 2007/2008 financial crisis has changed the nationally independent nature of welfare provision through the establishment of the EFSF and the ESM and the reinforcement of the stability and growth pact. As with all the other secondary power structures investigated by Strange (1988), the welfare structure has also come under the influence of the neo-liberal economic concepts espoused by the EU. This influence has been extended by the economic consequences of the 2007/2008 crisis.

The argument on the right largely follows the logic of thinking analysed in Chapter 2, arguing against an “involuntary” transfer of resources from well-performing individuals to “badly” performing individuals, as well as the market distortion created by state intervention (Offe 1984). The left also has a problem with welfare, as it normalises relations between classes instead of being part of the effort to overthrow the ruling class. However neither side can abandon it, since both left and right profit from it to some extent (Offe 1984).

As Strange (1988) argues, the provision of these services by the state or other non-state actors is only in the rarest of cases motivated by philanthropic reasons. Such provisions, especially in the case of welfare, have underlying political motivations. The fact remains that states used to provide these services to its population for political reasons (Strange 1996). These were in many cases paid for with credit accessed on the international markets. It is this very fact that has caused the welfare authority of nations to be undermined and opened up to pressures to reform from the EU.

1.5.3 Hegemony

Hegemony is an important concept within this thesis. Hegemonic theory informs the understanding of this thesis view of German and French action at the EU level. Hegemony, in this thesis, will be considered as a concept on its own, with which it will not actively engage. It will be considered in this introduction only. Any further mention of hegemony will refer to this explanation.

The fact of the matter is that societies are hierarchical institutions, no matter how much social policy a state is enacting. As was shown in the above section, forms of classification are going far beyond economic distinctions, and involve much more than direct coercion of individuals or other classes in order for the ruling elite to achieve its ends.

> The process of governing entails creating community consent, which relies on the distribution of shares and the hierarchy of places and functions (Rancière 1992, 58-59).

Strange argued that cause and effects of actions of power within a structure were intimately linked within international political economy: it follows that the use of an ideological concept will cause a causal chain, which will not only impact that same concept but also other ideological concepts which may be applied within that structure. It will also impact the economic systems operating within that structure.

> No discourse can be fully established, it is always in conflict with other discourses that define reality differently and set other guidelines for social action (Phillips & Joergensen 2002, 47).

Hegemony (see also Rupert 1995; Overbeek and van der Pijl 1993; Lears 1985; Keohane 2005; and Chompsky and Herman 2002) represents an *ordering principle of competing ideological concepts*. Hegemony is the description of the *act* of consent creation (through force or consensus) as well as the *sustaining* of consensus once consent is created. Hegemony then is an ordering principle whose *physical production*, as well as *symbolic production, creates* consent.

> The political cannot be understood in terms of only one of its attributes; of force or consent. It is both; force and consent, authority and hegemony, violence and 'civilta' (Sassoon 1980, 112).

Consent therefore extends in progressively ever-widening concentric circles from narrow, specialized, and technical groups of intellectuals to popular and mass audiences (Fontana 2008, 95). Since Gramsci argues that civil society is based on material, "manufacturable" objects, i.e. civil society constructs hegemony, therefore hegemony, and by extension consent, can be "manufactured" (Fontana 2008, 96). Hegemony therefore, is constructed within civil society and exercised through the actions of the state (Fontana 2008). These actions then spread this consent throughout the nation. This same principle functions also on the international scale. If Germany is able to construct consent on their political economic course within the EZ, it will be able to slowly implement this consent with the aid of the EU structure within the other member countries.

1.6 Timeframes of (in) action

Before this thesis will start its review of the political/economic evolution of the German and French states over time, and the socio-economic repercussion those evolutions had, it is useful to explain why these particular timeframes were taken and what their significance is for the analysis of this thesis. The time discrepancy between the analysis of the evolution of the conception of the provision of welfare by the German state in Chapter 4 and by the French state in Chapter 6 is about 17 years. Chapter 6 will start its analysis of French reforms in 1981 and Chapter 4 will start its analysis of the German reforms in 1998.

This difference has a very specific reason. Let us consider the trajectories of the two welfare states together. 1981 marks the start of the Mitterrand Presidency, making him the first Socialist President of the Fifth Republic. Mitterrand's ascendency to the presidency marked a turning point in the conceptions of social welfare in France. Mitterrand's conception of social welfare and the role of the state (which will be analysed more closely in the following section) combined socialist ideas with the concept of *dirigisme* established during the de Gaulle Presidency, and has remained the frame of reference for French welfare to date. This understanding has only been reconsidered under the Sarkozy Presidency. During the Sarkozy presidency, significant reforms were discussed and subsequently implemented. These reforms have reduced the power of the unions and have introduced some labour reforms. Their focus, however, was the reduction of inefficiencies in government and other social services through a greater use of the Internet and investment in research and development. The reforms have changed some of the French government's attitudes and *dirigiste* actions, but they have not proposed any fundamental changes to the *dirigiste* concept or to the welfare provisions of the state towards its people. In France, the state continues to be an important political-economic actor.

The German date of analysis begins with the Agenda 2010 reforms of 1998 to 2005. These reforms have completely changed the character of welfare in Germany as well as the state's role in the German political economy. Prior to 1998, the German state's concept was similar to the French concept. It was designed to empower workers and give them an opportunity to realise their worth. The German reforms have redefined that position by redefining the position of the state within the German political economy. This redefinition included the redefinition of the meaning of welfare from a method of empowerment of the unemployed into a form of social workfare for the unemployed. This section shows the most significant divergences in the French and German conceptions. Under the economic pressures of the 1990s and 2000s, the French government reinforced the role of the state creating the *traitement social du chômage* (Teyssier 2011, 513) while Germany decided to reduce the role of the state, creating the "Hartz" laws.

1.7 Chapter outline

Chapter 2 deals with two theories used in political economy which I call "classical liberal" and "neo-liberal" economic theory to make sense of the global economic trends and political action towards those trends. Every other section in this chapter refers back to these two points.

The chapter discusses the concept of freedom in terms of the role of the state in market operations. It touches upon the concept of taxation and welfare provisions and discusses the views of the state that both liberal approaches have. Chapter 2 will therefore investigate the evolution of the concept of welfare from medieval times to 2011. Using the theories of Gøsta Esping-Andersen (1990, 1999) this section will divide the evolution of welfare into early and late welfare provision. The early welfare provision is a piecemeal application of redistribution where the concept is developed and slowly integrated within the realm of the state, creating the state's duty of care for its citizens, which was fully realised with the transition to the late welfare provision. The late welfare provision starts with the establishment of the central provision of welfare by the state and the extension of citizenship rights.

Gøsta Esping-Andersen's typology of the different forms of welfare in Europe will be used to provide the frame of reference for the comparison of the German and French theoretical models. Finally, this thesis will consider how the financial crisis has polarised the concepts of welfare provision and what will be the wider implications for European welfare.

Chapter 3 looks at the consequences of both theoretical and practical financial deregulation. This section looks at the financial structure and the reason for its primary importance to the world economy. This chapter will further discuss the different issues regarding deregulation and the consequences this has on the economy and how it binds the state to the financial sector. This chapter will demonstrate the moral hazard, which the neo-liberal trend of deregulation creates and their consequences. To illustrate this point, this chapter will consider the case of the US 2007/2008 financial crisis for which the biggest contributing factor was moral hazard and deregulation. It will conclude by looking at the effects this crisis had on the economy in Europe and investigate the steps taken by the Euro Zone member countries to combat this crisis. It will investigate the establishment of the ESM and the political and economic consequences this safety mechanism has on the countries within the Euro Zone.

Chapter 4 will investigate the evolution of the concept of welfare provisions in Germany in detail. Chapter 4 looks at how the concept of social security has been redefined from 1998 onwards in line with the neo-liberal reform course of the German government. This Chapter will begin by comparing the social laws of Germany pre- and post- 1998. It will outline their purpose and their impact on the concept of German welfare and the state's role in its provision by analysing the concept of welfare as defined by Schröder and Blair and finalised by the Hartz concept and their subsequent reforms.

Chapter 5 will investigate the socio-economic consequences of the German political economic reforms. This chapter looks at the numbers coming out of Germany and attempts to quantify how the social security changes have changed, quantitatively speaking, the welfare and chances at equality of the German people. It will do so by providing a historical perspective on the German economic performance, including an overview of the historical unemployment rate of Germany starting in the 1950s to 1990 in West Germany and unemployment figures for the reunified Germany from 1991 to 2014.

This chapter will show the evolution of the economy before reunification, the problems after reunification, the economic and social impacts of the reforms as well as the economic and social impacts of the 2007/2008 financial crisis. The final section of this chapter will consider the position in economic terms that Germany has taken up once the European reaction to the crisis was started.

Chapter 6 investigates both the changes in the concept of social security as well as their economic impact of reforms in France. It also assesses the consequences this would have on the other EZ and EU members.

Chapter 6 looks at the constitutional amendments and other decrees establishing wide-ranging rights for workers, amendments which still frame the rights to social security and welfare and the state's role in guaranteeing these rights in general are conceptualised in France. Labour unions form a very important part of society and find their rights secured in the constitution as well. They help regulate work standards on a national and industry level and defend the constitutional rights of the workers to a point where political economic reforms have halted altogether. This chapter will demonstrate how the later reforms by the Sarkozy Presidency have reduced the power of the unions, making them more combative and less willing to compromise.

Chapter 7 will investigate the socio economic consequences of the French political economic stagnation and late reform push. This chapter looks at the numbers coming out of France and attempts to quantify how the political stasis has impacted, quantitatively speaking, the welfare and chances at equality of the French people. It will do so by providing a historical perspective on the French economic performance, including an overview of the historical unemployment rate of France starting in the 1950s and ending in 2014.

This shows that structural unemployment has increased significantly with the two oil crises. 1991-2007 shows a continued fluctuation of unemployment rates as well as other factors reproducing inequality (such as differing access to education healthcare and remuneration practices). 2007-2014 shows that the 2007/2008 financial crisis had severe impacts on the economic performance of France as well as its unemployment numbers.

France is an important member of the ESM with a different philosophy to Germany even though the Sarkozy Presidency had been a supporter of the German austerity course abroad. The economic data for France shows that due to its strong internal consumption the impact of the crisis was milder on France in the early days than on other Euro Zone economies. The potential consequences for the Euro Zone of an expenditure fuelled crisis plan are demonstrated within this chapter.

Chapter 8 compares the different ideologies and spending concepts in Germany and France. Comparing the economic data of France and Germany especially since 1998, it demonstrates that both approaches have their strengths and weaknesses, which if applied on their own will not result in a positive outcome in the medium to long term. The different neo-liberal and classical liberal concepts need to be synthesised so that their strengths can be exploited to the full. What is needed for European growth is not blind austerity, nor is it blind spending. What is needed is a social democratic market reform, which needs to enable long-term research and infrastructure spending along the lines of the Juppé-Rocard Report (2011), as well as targeted spending cuts and a more flexible, German-influenced employment strategy, which does not create a workfare state. There needs to be a balance between incentive and protection, investment and savings.

Chapter 9 provides the conclusion for the thesis. This chapter considers the research undertaken in this thesis and points out its strengths and its weaknesses. It also considers different avenues of research that have not been taken by this thesis, which nonetheless this thesis considers to be worthy of closer analysis in the future. This chapter sums up the arguments made in the previous sections and gives a final conclusion.

Chapter 2 Different liberal economic concepts and the evolution of state welfare conceptions; achievement of equality through different worldviews

2.1 Introduction

This chapter will provide an evaluation of the capitalist concepts of neo-liberalism and classical liberalism and their views on welfare and on the state's role in its provision. The concept of welfare in capitalism is linked to a certain understanding of the concept of freedom of enterprise and freedom of the individual, which in turn is linked, to the national conception of the place of the state in the economy. This chapter will undertake an analysis of the structural power of the classical and neo-liberal concepts within the globalized market economies by investigating their conceptions of the responsibilities and duties of the state as they are related to state welfare.

On the one side, is the moral, economic and political philosophy approach of Adam Smith and John Maynard Keynes. Opposite is the amoral, scientific economic theory of David Ricardo, Friedrich von Hayek, Milton Friedman and Ayn Rand. I investigate these works because they remain the foundational works of the two strands of liberalism (i.e. classical liberalism and Neo-Liberalism), and because current theories do not significantly deviate from those concepts. Ayn Rand's work is used in this analysis to demonstrate an extreme interpretation of the free market idea. This example will allow for an understanding of the full extent of the neo-liberal logic and its consequences for welfare.

Since this thesis investigates the impact of the financial crisis on the conception of social security within Germany and France, in the second part of this chapter, the concepts of welfare provision used primarily in Germany and France and developed by Otto von Bismarck and William Beveridge will be considered. Both systems also provide a match to the economic systems considered in the first section. To achieve this, the theories used within this investigation are those of Gøsta Esping-Andersen, Peter Taylor-Gooby and Christopher Pierson. It should also be pointed out that the definition of welfare investigated in this thesis, is the definition applied within a capitalist social and economic framework as it is applied within *Europe*.

In order to understand *how* states have reached their current level of involvement within welfare and thus within the economy and within society, this thesis will investigate past forms of welfare as I consider those forms to shape future forms of welfare. Thus, the ages of piecemeal social charity set the stage for a more organised social charity during the birth of industrial and democratic societies. This in turn formed the ideological and moral basis of the first welfare systems, which evolved into the welfare states for which Europe continues to be known.

This chapter contends that the state's role in the maintenance and provision of social welfare systems, in their current guise, are the latest result of the changes within the balance of structural power of markets and states. In the on-going struggle of markets to become efficient and perfect exchanges of goods and services on the one side and the state's quest to care for their population by intervening within the neo-liberal economic structure on the other.

Capitalism at its core therefore debates the following questions:

> In order to be free, does the state have to intervene? If so, how much state regulation is necessary until the state constrains the freedom it is trying to protect?

Smith (1904) and Keynes (1936) argued that freedom, equality and balance was not a spontaneous occurrence within capitalism nor was it continuous, or achievable through scientific methods. Smith (1904) and Keynes (1936) therefore argue that government intervention was necessary to enable people to take advantage of these freedoms. Once *balance* and *equality* had been achieved, it needed to be *maintained* through *structures* and *regulations* so that, if the balance were to fail, the rules and regulations set up would help limit the excesses of capitalism created by its own internal inconsistencies and move it back to equilibrium. The state was seen as the place from where structures and regulations could emanate and that would ensure that the balance within the system was maintained and that the highest levels of freedom of the individual and freedom of enterprise were achieved (while keeping disparities in check).

Neo-liberals such as Friedrich von Hayek (1960) and Milton Friedman (1962) answer the question posed above by arguing that the highest possible achievement of freedom, equality and balance, is through individual freedom guaranteed by law. Neo-liberals believe that people should be able to participate in the market as much or as little as they wish in order to *realise their needs and aspirations*. Rand adds to that:

> Freedom is based on the recognition of individual rights, on man's right to exist (and work) for his own sake (Rand 1964, 184).

I see Ayn Rand's (1964) statement to be a succinct but accurate restatement of Adam Smith's (1904) concept of "Self-Interest" as well as an area of common understanding between both liberal approaches. To pursue one's own self-interest within an established legal framework is the neo-liberal epitome of freedom. Having achieved this level of freedom, it allows the mind to flourish, allowing it to develop new ideas, concepts and products that advance human knowledge and human welfare (Fromm 2009). The difference to classical liberals is that neo-liberals do not believe the state is necessary to achieve this balance but that the market can achieve it.

As this chapter will demonstrate, the capitalist system is a system that by design creates and even fosters economic differences since inequality is considered to be an essential drive of economic development within capitalism (Piketty 2014). However, the establishment of (now deeply engrained) welfare systems within Europe designed to reduce and prevent the worst excesses of this inequality was in part a response to the creation of these inequalities. As Offe (1984, 147) points out:

> The welfare state has served as the major peace formula of advanced capitalist democracies for the period following the Second World War.

"Misery generates hate" (Beveridge 1945, title page) is an accurate description of any system of social or economic government, which allows its members to live in wildly differing economic and social circumstances without enough possibility to help people better their socio-economic position.

Although state welfare kept the peace after the war, its institution was never without its opponents, both on the right and on the left. The argument on the right largely follows the neo-liberal logic of thinking, arguing against an "involuntary" transfer of resources from "well" performing individuals to "badly" performing individuals, as well as the market distortion created by state intervention (Offe 1984). However, liberalism cannot answer the question of

> "what comes after to any satisfaction since the complete privatization of the industrial economy is simply inconceivable" (Offe 1984, 153).

The Left also has a problem with welfare, as welfare normalises relations between classes instead of being part of the effort to overthrow the ruling class. Neither side is able or desirous of abandoning it, since both sides profit from welfare to some extent (Offe 1984).

While Germany has long since been the economically strongest EU country, its actions during the 2007/2008 financial crisis have further elevated its position within Europe. This chapter starts this analysis by focussing on the way in which welfare provisions can be analysed. I use the work of Gøsta Esping-Andersen (1999, 1990) and Peter Taylor-Gooby (2001) to complement and flesh out my own understanding of welfare and its application within society. The first part of this section will consider how each new incarnation of welfare carries with it aspects of the position that has come before. The second part of this section analyses how social security evolved through time. To do this, this section is comprised of two parts.

Part one of this section analyses Esping-Andersen’s (1999) concept of social policy from the medieval times through to the early industrial age focussing the analysis by showing the progression of the welfare argument. I will do so by analysing the arguments different thinkers have given in support of social policy over time. Part two of this section analyses Esping-Andersen’s definition of welfare. “Welfare” covers the time from the early industrial age until post-war modernity. This section takes a closer look at the evolution of state-sponsored health and social care and its modern applications. It considers the systems developed by Bismarck and Beveridge, whom I contend, form the basis of two of Esping-Andersen’s welfare models.

I am aware that there are also other versions of welfare provisions most notably in the USA and the Scandinavian countries. However these forms of welfare provision will not be investigated here because they are not relevant to the analysis of the German and French welfare models, nor is there a significant involvement of Scandinavian countries within the Euro Zone (1 of 4 countries is using it). Understanding Beveridge and Bismarck will provide the basis of the German and the French welfare models, the thesis case studies.

Finding an exact time and place where social policy stopped and welfare began goes beyond the scope of this thesis. Hence I use Christopher Pierson’s (1991) concept of determination. Following the industrial revolution, the increase of misery of the population to an unprecedented scale started to transform the piecemeal effort of social charity into a concerted effort of government sponsored programmes of social security designed to ward off the worst troubles created by capitalism. The first such efforts were undertaken in England with the Poor Laws. I will consider the early industrial age as a time of transition between forms of social security and consider the Bismarck reforms as the actual beginning of welfare provisions.

The third part of this chapter will analyse the Bismarck and Beveridge welfare concepts. Both these concepts of welfare can be aligned with either of the two Liberal concepts here analysed. The Bismarck social reforms tend to be favoured by neo-liberals because they function as a very basic survival net that work like an insurance thus working along the same principles as neo-liberal economics.

Friedman (1962), Hayek (1960) and Rand (1966) argue that freedom can only be achieved within a free and unregulated market, where the state is the smallest size possible, only able to enforce and legitimize contracts, with taxation only high enough to pay for that. In this way they argue, everyone is free to participate or not in the market, which in the end brings about the best results for everyone without requiring welfare provisions that would confuse the incentive structure of people and cause market failures.

Classical liberals on the other hand generally favour the Beveridge social reforms because they were the first concrete attempt to provide large-scale state aid to every segment of the population by integrating welfare provision within the classical concept of strong state involvement through high levels of wealth redistribution.

Smith (1904, 2009) and Keynes (1936) argue that freedom needs to be supported by government action in order to promote the positive effects of capitalism and reduce its negative effects. Government action is an essential guarantor of freedom and individual action within which government sponsored welfare performs an essential service, by safeguarding individuals from the worst failures of capitalism.

Post WW2 the Keynesian argument carried the day, establishing the post-war consensus of social security (as mentioned by Offe 1984) upon which the current models of welfare provision are based. The consensus contained a commitment towards comparatively “high” levels of welfare benefits and high levels of employment compared to when these concepts were first introduced at the end of the second to last century and in the middle of the last century (Beveridge 1945).

This section will argue that Keynes' theory provided the economic tools to make the social security concepts of Bismarck and Beveridge sustainable, since both those concepts of social security are predicated on Keynesian type economic concepts. This section will also consider the drawbacks of that economic concept, which will lead this thesis to analyse the actions of Germany and France and their efforts to deal with those problems and the result those actions yielded particularly with the EZ crisis in mind.

This national commitment of welfare provision has come under severe strain since the end of Bretton Woods, but the system of welfare provision continues to remain functional. As Chapter 3 will point out, the 2007-2008 financial crisis and its consequences for Europe left that commitment much weakened in many European States, since the burdens of achieving austerity and the economic pressures are placed largely on social security. This shift in the burden of dealing with the crisis is a direct consequence of the changes within the structural power of the markets and the states. This point will also be further considered in Chapter 3

The European response to the 2007/2008 financial crisis has changed the frame of reference in which European countries can provide welfare to its citizens. The final part of this chapter follows (a) the events, which occurred when the fiscalisation of the debt affected the weakest member states and (b) the reactions of the Germans and the French as well as the British to this event. The reason for Britain's inclusion in this analysis is because Britain is not a member of the Euro Zone and therefore unlike Germany and France, is not bound by regulations imposed within the EZ. However, Britain remains deeply affected by the crisis that occurred within the Euro Zone and by the decisions taken within it to remedy that crisis. This description will aid in understanding the current knowledge of the decision makers at the time and conclusions that were drawn from that knowledge.

2.2 Freedom; capitalism's conduit to prosperity for all

When talking about freedom in liberal theory, one talks about individual freedom. The free individual in liberalism is seen as the greatest innovator within society, continually exploring and inventing new ways to produce efficiently and effectively, i.e. to continually create new markets on which to trade and to *pursue* their *own self-interest*. This freedom, however, is conditional on individuals being free from *coercion*.

> Coercion eliminates an individual as, a thinking and valuing person and makes him a bare tool in the achievement on the ends of another (Hayek 1960, 21; see also Hayek 1962 and Lukes 2005).

As I argued above, to ensure that freedoms can be exercised fully and equally, rules and regulations need to be established to ensure that the exercise of one individual's freedom does not curtail the exercise of another individual's freedom. In capitalism, this task falls to the state, which exists to enforce contracts and, more broadly, rules and regulations set up by the people to manage their interactions and prevent against potential failures by providing welfare to its population.

Coercion, which is the flipside of freedom, is defined by a level of state intervention that is seen in liberal theory as inhibiting the free exercise of self-interest beyond an ideal point. Finding a balance between laws and freedoms, and the validity of majority or minority decisions is what I understand to drive the philosophical debate about *freedom* in liberalism. This definition of coercion is a central aspect of freedom in the liberal argumentation analysed in this thesis. The determination of the adequate level of state intervention necessary to achieve economic growth capable of allowing people to live the lives they wish without having to resort to government aid is the central question within the German and French elaboration of rescue scenarios for the Euro Zone.

Smith was the first economist to argue that individual freedom was the key to social as well as economic development. Since any state interference would inevitably disturb the "harmonization of individual and social welfare" (Ingham 2008, 10). It is these unique actions, the freedom of individuals to play to their own strengths, that have brought about the division of labour in economics (e.g. the pin factory in book 1 of *The Wealth of Nations* (Smith 1904)). The ability of each person to participate in the economy according to his or her own strengths and ambitions is what drives the technological development of capitalism.

> Individual liberty is a creature of law and does not exist outside any civil society, the rule of law properly understood and consistently applied, is bound to protect individual liberty (Gray 1986, 61)

Hayek takes this a step further by arguing that the free market rewards people according to their actual efforts without regulations distorting or redistributing that reward and thereby making competition unfair (Hayek 1960). Both Smith (1904) and Hayek (1960) however agree that not all things can be regulated by the market system. Sometimes individual liberty has to be interfered with. How much and in what way is a question with which liberalism still struggles.

2.3 Taxation: coercion or necessary redistribution?

A point upon which the discussion between the two competing directions in Liberalism concentrates is the issue of taxation. Taxation is an essential part of the power of the state to finance its actions and perform its duties. Without taxes, there could be no enforcement of laws or contracts and nor could there be a provision of welfare (depending of which concept of welfare is dominant within that society). Though both sides of the Liberal argument agree that some form of taxation is necessary, their conception of what form and what size this taxation should take differs according to the Liberal understanding considered.

2.3.1 Amoral

Rand (1964), Friedman (1970) and Hayek (1960) argue that one of the principal ways in which coercion -as defined in the previous section- is exercised in a capitalist system, is through taxation by the state. Ayn Rand put forward a radical view of taxation and its consequences for economic freedom. Rand (1966) argues that any type of interference in the operation of the free market causes market failures and is to be avoided at all costs. Rand (1964) further argues that the free market principle necessarily extends to the individual. It follows therefore that any taxation of the individual and any sort of majority (or minority) imposed action funded by that taxation (e.g. education, social security, unemployment insurance, *etc.*) is an infringement on the personal liberties of that individual and furthermore, an impediment to the free working of the market (Rand 1964). Friedman (1970) put forward a similar point without using Rand's extreme logic. However, the sentiment Friedman expressed is the same.

> Those who favour the taxes and expenditures in question have failed to persuade a majority of their fellow citizens to be of the like mind and that they are seeking to attain by undemocratic procedures what they cannot attain by democratic procedures. In a free society it is hard for 'evil' people to do 'evil' especially since one man's good is another man's evil (Friedman 1970, 176).

The conclusion that can be reached from these statements is that any form of taxation, which aims at redistributing wealth from one group of people to another is to be opposed as it distorts the processes of the market. It is these processes, which Rand (1964), Hayek (1960) and Friedman (1970) see as more beneficial to society than *forced* redistribution by the state.

> The doctrine of "social responsibility" taken seriously would extend the scope of the political mechanism to every human activity. It does not differ in philosophy from the most explicitly collectivist doctrine. It differs only by professing to believe that collectivist ends can be attained without collectivist means. Social responsibility in capitalism is a fundamentally subversive doctrine in a free society (Friedman 1970, 178).

If Taxes are used for anything other than the enforcement of contracts between people (i.e. establishing and funding social equality programme), it will distort market set wages (the true wage for X labour). This will cause inefficiencies within the market which can lead in extreme cases to market failures; these market failures will cause the inequalities these measures were created to eliminate, instead of giving the market time to deal with the problem.

> The economic value of a man's work is determined, on a free market, by a single principle: by the voluntary consent of those who are willing to trade him their work or products in return. … It represents the recognition of the fact that man is not the property nor the servant of the tribe, that a man works in order to support his own life, that he has to be guided by his own rational self-interest, and if he wants to trade with others, he cannot expect sacrificial victims, i.e. he cannot expect to receive values without trading commensurate values in return (Rand 1966, 26).

Redistributive taxation takes money from well performing individuals and gives it to other individuals who according to the market do not deserve this money, as slow performers did not expend the same effort as the high performers. Therefore, taxes used for the redistribution of wealth, reduce the incentives for people to be at their most productive because their participation will be undervalued, whereas badly performing individuals' participation in the market will be overvalued (Friedman 1970; Hayek 1960). Furthermore, this type of taxation is coercive: they prevent the individual to freely choose what to do with the money they earned and thus negates the incentive to accumulate wealth, thereby invalidating the whole concept of capitalism. Milton Friedman would call this type of redistributive taxation:

> unadulterated socialism, which would undermine the basis of any free society (Friedman 1970, 175).

It bears repeating that neither Friedman, Rand nor Hayek are arguing against the principle of taxation or against all forms of taxation emanating from the state, nor do they argue against all forms of state. A minimum of taxation is something even Rand and Friedman would agree with, since the taxes they would argue for would take the form of fees, paid to the state for making sure the agreed upon rules are followed. Considering this view on taxation, Rand, Friedman and Hayek do not envisage a world of only markets but a world where the state plays a much more reduced role than it does currently; this is a role which reinterprets the current understanding of the social contract between state and society (see Chapter 3 for further explanations of notions of social contract).

2.3.2 Moral

Adam Smith (1904) endorses a wider definition of taxation, as opposed to modern liberal-economist Friedman and market radicals like Rand. Adam Smith’s description of taxation finds similarities in Friedrich v. Hayek’s thoughts on taxation. Considering that Hayek lies firmly within the amoral neo-liberal ideology since his work has formed the basis along which Friedman and Rand have oriented their ideas, Hayek -who comes from the Ricardian (Ricardo 1998) tradition- in turn has taken some of his orientation from Smith. However, that area of agreement between Smith and Hayek is limited to the principle of providing general services necessary for the good functioning of the economy.

Smith (1904) argues that taxes allow the state to provide those services whose costs would outweigh the profits if the services were to be provided by private companies. This wording goes against the central argument provided by Friedman and Rand who see individual freedom as surpassing any other freedoms or desires. Adam Smith (1904) put limits on his altruistic concept of common payment of large projects. Smith (1904) argues that, if taxes need to be levied, taxation should at all times *prioritize personal wealth over and above tax revenues* (Smith 1904). Hayek (1960) echoes that same sentiment; however, Smith (1904, 310-311) goes on to argue, that taxes should be levied uniformly on each subject *to the best of their capacities,* which is an endorsement of the principle of progressive taxation. In my view, this conceptualization of tax is the reverse of the individualistic concept put forward by Hayek, Friedman and Rand.

Hayek does not disagree with Smith on the necessity for the state to provide infrastructure for the economy, nor does he disagree that this infrastructure should be paid for through taxation since Hayek agrees that a pooling of resources is one of the greatest attributes of individuals (Hayek 1960). Hayek argues that the only fair system of taxation -if there has to be one- is one of proportional taxation not of progressive taxation. A standard percentage of taxation levied on all people equally, would automatically cause wealthier people to pay more, as 10% of £100.000 (i.e. £10.000 tax) is more than 10% of £10.000 (i.e. £1.000 tax), without unduly increasing the burden on the rich (Hayek 1960; see also Rawls 1993, 1999). A standard tax rate therefore is more like a fee for services rendered than a tool for achieving an *equal* society, which is the argument made by Rand (1966) and Friedman (1962). Hayek (1960; Kukathas 1989) agrees with Rand and Friedman on the fact that any other redistributive effect that goes beyond providing the necessary infrastructure for a well-functioning economy should not be tolerated.

Hence, Adam Smith (1904) sees the state in a different light to that of Friedman, Hayek and Rand, largely because Smith sees taxation in a different light. Smith's view aligns itself with the common understanding of the nature and duties of state as it is put forward within the social contract (see Chapter 3 for further explanations of notions of social contract). These duties can only be performed adequately if there is an amount of taxation high enough to allow for that performance to be financed. Although the amount of taxes which Smith sees the state using is smaller and more free market oriented, Smith sees within the state an instrument of care for the population and the market which is absent from the concept of Friedman, Hayek and Rand.

Smith's concept of the caring and involved state should once again find relevance in the post WW2 years and through the writings of John Maynard Keynes. His theories of market intervention by the state and the levels of economic growth able to be achieved with a strong state, a well-regulated market and relatively equal distribution of wealth (Keynes 1936) allowed Europe to properly establish and maintain the generous welfare programmes in the first place.

2.4 The State: Night-Watchman or Manager?

The differences between both approaches radiate out from taxation and onto the role of the state and state powers. Since *amoral* and *moral* concepts of Liberalism conceive of the state and its role in society differently, this section will expand on what these differences are as well as introducing the consequences for welfare (further expanded in Chapters 4, 5 and 7) among those differences.

> Competitive capitalism promotes political freedom because it separates economic power from political power and in this way enables one to offset the other (Friedman 1962, 9)

2.4.1 The Manager

Adam Smith, in his seminal work *The Wealth of Nations* (1904), focussed on the economic implications of unregulated individual behaviour. Smith's (1904) analysis demonstrates that, even at the birth of industrial capitalism, theorists did not believe the market to be all-powerful. In fact, Adam Smith pointed out one of the greatest fallacies of the system. Smith contends that individual freedom brings with it the promise of wealth, which causes man to undertake his best and greatest efforts to achieve it. However, the actual attainment of that wealth causes the nullification of those good instincts (Rosenberg 1960). Smith's argument was that the competition between different companies needed to be regulated by laws and by a "gentlemen's agreement" of fair conduct in business. This is what Smith went on to call the "indivisible hand" (Rothschild 1994, 320). Smith's reason for insisting on regulation of the free market stems from Smith's argument that opposed to the self-interested hard worker stood the love of laziness (Rosenberg 1960):

> what are required above all are institutional mechanisms, which compel man in his natural insolence to use the good instrument (Rosenberg 1960, 558).

The state provides such institutional mechanisms. Smith argued for the state, society and the economy to be closely integrated in a way that allowed for individuals to be free but at the same time for the state and society to moderate the inconsistencies and the contradictions that befall the liberal economic system. Adam Smith argued that business was responsible for the wealth effects of its decisions (Kohls and Christensen 2002; Macdonald 2010). A just economy focuses on improving human life, dignity and human rights (Kohls and Christensen 2002) if necessary with the help of the state. The pursuit of wealth is not only to serve the individual but also the society within which he resides (Etzioni 1993).

> Far from assuming a spontaneous identity of interests (in the mere absence of government restrictions) or of being "blind to social conflicts", Smith was obsessed with the urge to go beyond the ordinary market-structure definition of competition and to evaluate the effectiveness of different institutional forms in enforcing this identity (Rosenberg 1960, 559).

A just and well-functioning economy therefore can only be an economy which is integrated within the morals of the society i.e. where industry is not only governed by a motive of profit accumulation but also by a sense of social responsibility. It cannot come from an economy that is governed by a separate morality (Polanyi 2001). In this understanding of economics, the firm is a mere instrument to achieve wealth of all who contributed and not only an immoral instrument of wealth creation for its owners. Smith as well as Keynes (see also Blaug 1990) argues that the free market cannot achieve this state by itself. It is only through the close integration of the market and of institutions that allow the augmentation of the productivity of workers, which in turn allows the free market to become efficient (Persky 1989). This integration of society and the market is facilitated by the state which is aware of the necessary combination of politics and economics, i.e. that has a good understanding of political economy.

John Maynard Keynes also argues for a close integration of the state within society and the market. Keynes (1936) argued that the cases presented by neo-liberal and monetarist economists should not and could not be accepted as general conclusions about how the economy would operate if left to its own devices. Keynes (1936) argued that the market failures were not special circumstances in the real economy but that perfect equilibriums were the actual exception.

> The sort of 'state control' Keynes envisaged was always organizational and not confiscational (Cranston 1978, 112)

Keynes argued that effective supply and especially demand could not be precisely determined, so that the argument that there is a mismatch between the two is mute and therefore a useless analytical tool (Surrey 1988). National economies were in fact in a near constant state of disequilibrium. The equilibrium, which liberal economics argue would be reached by the free market without state intervention, was in fact not a natural occurrence rather than an exception to the rule. The only possible way Keynes (1936) saw to resolve this problem was through specific market intervention by the state, aimed at promoting social justice while at the same time protecting individual freedoms (see also Riesman 1986; Schumpeter 2000).

2.4.2 The Night-Watchman

The more radical economic Liberals like Rand, Hayek and Friedman argue that there is such a thing as a "spontaneous identity of interests", which develops in an unfettered, market; thus there is no reason to intervene (Rand 1966). The belief that a spontaneous identify of interests can arise comes from a different understanding of economics upon which Hayek, Friedman and Rand base themselves. This stems from the theory of David Ricardo.

> It does not assure us of any particular opportunities, but leaves it to us to decide what use we shall make of the circumstances in which we find ourselves (Hayek 1960, 19)

Milton Friedman exemplifies this different conception by arguing that it is the moral responsibility of the firm to increase profits (Friedman 1970). The firm's first duty is to bring profits for its owner's profitability. Firms have no moral right to spend the money that rightfully belongs to the owners. The individual owners on the other hand can spend the money received from the firm any, which way they like (Friedman 1980). Morality, if applied at all should not be applied to either the market or the business, but should in effect be applied to the individuals (Friedman 1970).

Some liberal economists argue that an unfettered free market is the optimal way for the economy to operate: "The free market is its own protector" (Rand 1966, 75), i.e. there is no need for any kind of outside intervention in the operation of market forces. The market, through the laws of supply and demand, Say’s law (Forget 2002) and the self-interest of individuals, will always operate at its most efficient and most effective, any kind of problems in its operation will be minor and after automatic readjustment, the market will continue to function normally. This means that the power and actions of the “free market” are sacrosanct and above question. To Rand, Hayek and Friedman, the market is the ultimate tool for providing any service, and individualism is its driving force.

As Rand (1966) argues, states have no right to sponsor education, as it should be up to the individual to decide what level and type of knowledge is best for him. More importantly, the imposition of a state-structured form of education is tantamount to brainwashing as the state intervenes within the free act of idea creation, thus stunting it because others force individuals into learning patterns. Another example given by Berggren (2003, 205) argues that schools and hospitals are government run monopolies in many countries and are in most cases heavily regulated. This government activity reduces the scope for a dynamic, growth-enhancing market process in which each new business and each new way of doing something can be regarded as an experiment in trying to achieve better consumer satisfaction than existing alternatives (Berggren 2003).

The state in this conception is at best an inconvenience, a monkey wrench in the delicate machinery of the free market, and at worst a coercive force that creates monopolies and inefficiencies through its actions within the market, therefore creating the very inefficiencies that the state intervention was trying to avoid. Any such operation within the market by the state empowers one section of the population and disadvantages another. The only method of empowering all people within society is by allowing the market to run freely (Rand 1966). In this conception, the state should take on the role of Night-Watchman, only intervening when there is no other option and the rest of the time stay in the background and make sure that contracts between people are adhered to. The conclusion this Night-Watchman concept leads to is that the state through its interference within the free market not only distorts market operations, but also creates different classes of people and, worse, destroys the entire human social system built on individual choice (Rand 1966). However, complete non-intervention is not possible since some form of coercion by the state is necessary to prevent coercion within society (Hayek 1960)

> the argument is not an argument against organisation, one of the most powerful tools that human reason can employ, but an argument against all exclusive privileged monopolistic organisation, against the use of coercion to prevent others from trying to do better (Hayek 1960, 37).

Hayek understood that a wholly individualist approach to human creativity was limited to just that individual. Hayek (1960) sees group (e.g. state) action as one of the greatest achievements of people. Hayek understands that the pooling of resources is sometimes necessary for human advancement particularly in highly developed human societies. The point of the individual self-interest which Hayek's theory upholds however stands. The notion that individuals may leave that group at any time if it serves their own self-interest remains valid.

This is the final point of the concept of the Night-Watchman state, which is important to remember. This conception sees the state and society and the economy not integrated but rather loosely associated with one another. Additionally, society itself is considered a loose association of individuals as this last section demonstrated.

2.5 The structural power of neo- and classical- liberalism

As was shown in the previous sections, neo-liberalism and classical liberalism share a set of beliefs which are interpreted using different sets of logics. These logics create different economic concepts and have different structural powers, which were able to establish different economic systems, both of which contain challenges they need to overcome.

The Keynesian model in addition to the points considered later in this chapter had one fatal flaw, namely its propensity towards inflation due to its high labour and social security costs, which in a free market economy would be allowed to adjust itself to a lower level to be able to adapt to the economic climate (Crouch 2011). Its greatest flaw therefore was its inflexible labour and social costs this was, however, necessary to guarantee the stability of the welfare system.

During the 1970s the Keynesian model was rapidly displaced by the neo-liberal model and variations thereof. A laissez-faire policy of automatic adjustments particularly in the production and financial markets quickly rose to dominance displacing with its arrival the nation centric Keynesian power structures with internationally oriented power structures, biased towards industry instead of states (Crouch 2011) (see Chapter 3 for more information). However, this model like the Keynesian model had its own difficulties. The case most relevant to this thesis is the case of the financial industry (see Chapter 3 for more information), which managed to create a perfect market system within which every information was quantified and valued and the price was set by the market itself, according to that information. The issue with that was that the system was too perfect. The fact that these valuations were made in ever-shorter timeframes and buying and selling were also done in very short timeframes, the people doing the trading ignored some of the information available to them in order to buy and sell financial derivatives quicker since greater speed would allow for more trades to be realised and profits to be increased. This meant that if a shock were to hit the system, instead of a gradual balancing of the differences, people would sell as quickly as possible in order not to get left behind, causing a vicious circle of selling to minimize losses in turn causing a full-blown financial meltdown, (Crouch 2011) a crisis which will be considered more closely in Chapter 3.

The first part of this chapter has been dedicated to evaluating two capitalist concepts, which have different notions of the necessity of taxation, the achievement of individual freedom and the responsibility of the state in the management of both taxation and individual freedom, equality and economic stability. Classical liberalism focuses on political and economic methods but had problems with adequately managing inflation. Neo-liberalism focuses on economic methods and due to its profit-centred outlook has inadequately managed expectations causing volatile behaviour and severe crises.

The following section of this chapter will in a first instance investigate the historical evolution of welfare in Europe and the states' role in its provision before investigating the evolution of welfare post industrialisation as well as the European reactions to the financial crisis caused by the global neo-liberal economic model.

2.6 Two phases of Social Security: Social Policy and Welfare

The principle of charity and the early attempts at limiting the power of the king or the state as well as the attempt to create a more just society proved very powerful and have been transposed and transferred within the thoughts of subsequent theorists from Richard Poore (Bishop of Sailsbury) to John Locke. These early advocacies and applications of welfare, which Esping-Andersen (1990) termed Social Security, were initially based on the concept of Christian charity and then slowly evolved into limited rights and corresponding duties throughout the ages. The argument also evolved from individual responsibilities to be charitable to the responsibility of the state to be charitable, which over time evolved into a limited duty of care by the state. This evolution of the duties of the state evolved alongside the reduction of the power of the absolutist state. Over time, a slow but steady transformation occurred. The absolutist state retreated and a democratic, caring state first described by Montesquieu and reiterated by Rousseau in “The Social Contract” (1973) started to emerge, its central reason for being consisted of providing for its population.

2.6.1 Social Policy

During the Medieval Period, the Christian Church was a powerful political entity within Europe. The Christian canon contains within it a duty of care for others. All members of society can only achieve the common welfare and thereby entries into heaven through reciprocal care for each other, i.e. by working all together for the common good. Richard Poore, Bishop of Salisbury (Neederman & Forhan 1993), referencing Plutarch, argued for a duty of care by the ruling towards the ruled. It was the ruler’s responsibility to ensure equity and justice within the land, since a well-governed realm would ensure entrance to paradise after. Ensuring that the many serving masses of a kingdom are cared for and protected in sickness and in health would provide benefits for rulers in this world as well as the next (Neederman & Forhan 1993).

Giles of Rome argued that an expansive middle class was the best way to guarantee a stable and just society, because they fulfilled essential communicative, economic and political duties between the poor and the rich classes. To Giles of Rome, the middle class represented the measured and rational part of a society (Neederman & Forhan 1993). By expanding the middle class he maintained that their measured and rational attitudes would become more widespread, which would aid in the rule of society. It is a, for the time, direct statement for greater equality among people, especially when one considers that Giles of Rome recommended a direct involvement of the state within the process of inheritance, making sure that inheritance of land is done in a manner that spread wealth among the population instead of concentrating it (Neederman & Forhan 1993). This argument defines the concept of social security as a form of government intervention within the economy to bring about greater equality. This is an important point to note as it forms the beginning of the argument that defines the central argument of this thesis, i.e. that the responsibility of the state lays within the care for its citizens and that that can only be achieved through state intervention.

Before considering how a state can intervene, one needs to first consider how a state is being defined. Since this thesis analyses the actions of Germany and France in terms of the 2007/2008 financial crisis, this thesis will focus on their conceptions of the state. While state traditions in France and Germany have developed differently over time, there was some cross-pollination of concepts over time, which did influence some of the conceptions of the state between Germany and France. However, the German and French conceptions of the state remain differentiated. The French conception favours a strong centralised state which cares for and protects its citizens. The German conception sees the state in a more abstract form favouring individual freedom of decision-making and regulation of society by allowing the individual to fulfil its ambitions (Dyson 2009). Both those conceptions of the state will be more closely analysed in Chapter 3, however, either definition allows for a generous and expanded welfare state to achieve the here stated aims.

With the beginning of the Renaissance, the power of the Catholic Church began to fade, and *social laws* began to be passed instead of divine law. Hobbes claimed that, if laws had to be passed, they must be for the benefit of the people. The laws themselves must be restricted in their application so that they keep the people on the right path without restricting their freedom (Hobbes 1996). Hobbes showed his Christian roots when he reasoned that the sovereign was responsible to care for and protect certain vulnerable people who through some type of misfortune are unable to work, and thus are unable to support themselves.

> and whereas many men, by accident inevitable, become unable to maintain themselves by their labour, they ought not to be left to the charity of private persons; but to be provided for, (as far forth as the necessities of nature require,) by the laws of the commonwealth. For as it is uncharitableness in any man, to neglect the impotent; so it is in the sovereign of a commonwealth, not to expose them to the hazard of such uncertain charity (Hobbes 1996, 230).

In order to pay for his concept of “social security”, Hobbes needed to raise taxes. He did so by interfering as little as possible with the people living within a state. To Hobbes a general tax should be as low as possible because all people are equally protected by the state. Although Hobbes was opposed to unnecessary government intervention within society, he did not however hold a purely “laissez-faire” position, as he believed that some government intervention is necessary. This position by Hobbes is very similar to Esping-Andersen’s definition of liberal social welfare. Hobbes’ advocacy of little taxation and little government intervention, only allowing for minimal state help, by securing against the worst of the discrepancies among the population demonstrates his commitment to the liberal ideals.

After the Renaissance, the Enlightenment continued the retreat of divine law and the expansion of societal laws. Charles de Secondat Baron de Montesquieu’s (1977) analysis of the state never specifically engaged with the issue of human welfare. His writings were more concerned with the appropriateness of societal laws to the societies to which they were applied, as his seminal work, *The Spirit of the Laws* (*De l’esprit des lois*) (Montesquieu 1977), points out. However, through his Christian roots, he was a believer and an advocate for the concepts of virtue and “bienfesance” (philanthropy) (Linton 2001, 64, 67). He underscored that, irrespective of the system of rule one lives under, people should attempt to live “virtuous” lives and try to do what is best for others instead of what is best for themselves. This caring for others should be done within limits, as too much charity may make people reliant on it instead of looking for employment (Linton 2001).

In building on these concepts, Montesquieu pointed out that, although those born to nobility had higher life chances than those born to the lower classes and the peasantry, this should not mean that ”lower born people” were any less worthy of social advancement. Montesquieu believed in an organic society where all people (independent of their station and showing promise) had the right to be given a chance to succeed and improve their station. He argued for a meritocratic society in which ability was acknowledged and nurtured (Roche 1998, 540). Montesquieu in effect made the case for social security, i.e. “social equality” and equal opportunity. Even though this is not the point that Montesquieu made explicitly, looking at Montesquieu’s desire to allow people from different classes access to social advancement from a welfare perspective shows Montesquieu’s desire for social equality.

Charles Pinot Duclos and Luc de Clapiers (Marquis de Vauvenargues) later took up this thought and expanded this idea of virtue. They challenged Montesquieu’s concept of organic societies (a structured form of society with people at the top and people at the bottom) and limited meritocratic aid. Duclos and Vauvenargues contended instead that society was made up of homogenous (all people being equal) people who all had the same rights and opportunities and needed to care for and help each other (Linton 2001, Roche 1998).

Rousseau (1973) developed his idea of a “social contract” around the ideas of virtue and a homogenous society developed previously by Montesquieu, Duclos and de Clapiers. Rousseau (1973) focussed the majority of his thought on the concept of social security, as keeping society safe from internal or external threats from other individuals. Rousseau’s thought contains strong libertarian undertones as any other writer during that time. Since he was a strong advocate of equality, Rousseau (1973) acknowledged that there existed forms of inequality that could not be resolved by a free society alone. The state needed to play the role of impartial adjudicator of disputes. The state also needed to enforce equal treatment of people as well as administer equal access to land by people. Since land ownership at the time was still a major cause of inequality, an equal distribution of land was a good way to enact more equal relations among people (Rousseau 1973, 2).

John Locke contended that the state was supposed to help the citizens; it cannot do anything that would be to the detriment of its citizens and if it did, Locke (1993) claimed that the citizens would have the right to rebel against that government and replace it with one that would care for their interests. This statement allows in principle the idea that, if the state or society concluded that helping provide for people was part of the state’s duties, the state had to adhere to the wishes of society.

> in the outmost bounds of it, is limited to the public good for the society. It is a power that hath no other end but preservation, and therefore can never have a right to destroy, enslave, or designedly to impoverish the subject (Locke 1993, 330)

Locke further pointed out that people, who cannot fend for themselves, should be helped and that those who can work but do not need to be forced to work. Locke saw the responsibilities of the state to include social security as a minimal intervention by the government and an enforcement of property rights. Distrustful of government, Locke therefore recommended only a small increase in its powers by having it care for the most vulnerable in society who could not rely on fickle charity to maintain themselves (Locke 1993). Locke's concepts, viewed from the angle of welfare provision, closely resemble the concepts of Hobbes who also argues for little government intervention within the provision of welfare to the people. The difference is that Locke's argument for social security goes a little further in this respect. Locke (1993) argues that people who are able to should be forced to work without being given benefits to deter them from doing so. This again is similar to the position that Germany has taken with the Hartz 4 laws, which would suggest a liberal welfare agenda as the position of Germany. This point will be looked at more closely later in the chapter.

As this historical overview has shown, the concept of welfare and the role of the state have slowly evolved over the centuries. The evolution from piecemeal social policy to a concrete and constant provision of aid by the state to its population also went through a period of evolution. There was an intervening period where the piecemeal efforts of previous ages were consolidated into a single framework. The establishment in Britain of the Poor Laws falls within the characteristics of that intervening period. The Poor Laws were not a significant advance on the road to concerted efforts of welfare provision in terms of the significance of their provisions. The Poor Laws are important to consider since they did set up an initial framework and provided a catalogue of different protections and provisions; this could be considered as an expanded version of social policy undertaken and guaranteed by the state, a centralised and early industrial government. This state guarantee reinforced the notion of the state as a governor of economic activity and protector of the populace from detrimental economic activity. It is the step preceding the establishment of the first welfare state and two steps preceding the establishment of modern welfare provisions, which are much expanded and reinforced from the preceding steps.

The “Poor Laws” were established because the ruling classes feared that, if social and especially economic inequalities within society continued to be left unchecked without even attempting to reduce these inequalities, it might start a second civil war within the country (Bruce 1972).

> The Elizabethan Poor-Law system is a combination of social amelioration and police deterrence that might be said to be the ultimate basis of the welfare state (Bruce 1972, 36)

The Act of 1598, in its policies and decrees, bears close similarities to the recommendations and arguments made by both Thomas Hobbes and John Locke. The “poor laws” were designed to prevent distress where possible and relieve distress where it was not. Furthermore, it was designed to set the poor to work by transferring non-able-bodied poor people to abiding houses, providing tools for able-bodied poor people willing to work and send able-bodied poor people unwilling to work to correction houses to compel them to work (Bruce 1972, 41).

As more and more information became available to British authorities concerning the working conditions within the primary (agricultural) and secondary (industrial) sectors, employment regulations in these sectors were increased and commissions were created to study the long-term effects of these changes (Bruce 1972). In 1890, the Housing Act was enacted, allowing powers to be bestowed on local authorities. This included the authority to demolish buildings the authority judged to be in too bad a condition to live in. Local authorities were also empowered to enact regulations for water and housing management (Bruce 1972). Although new industries were reregulated and out-dated regulations were updated as well as new powers being given to local authorities, this carried with it only a marginal improvement to workers’ working conditions. The reforms changed the role of the state from a passive observer and organiser of charity to an active player within society and the economy, i.e. the state became a political-economic entity.

2.7 Welfare: a variety of opinions

Of the varying welfare systems that exist within Europe, Esping-Andersen (1990) has analysed many different welfare systems. Esping-Andersen's work is in agreement with the work of Pierson that the beginning of welfare can be argued to have started with the introduction by Bismarck of welfare provisions on a national scale and sponsored by the government. This was, however, not the beginning of the concept of welfare in general. That concept is much older and reaches as far back as the medieval period. Once the analysis of the different theoretical and practical welfare applications have been investigated and it has been determined where the German and French systems are placed in this context, I will analyse the evolution of the concept of welfare and its relation to the state.

Peter Taylor-Gooby's (2001) analysis focuses on Esping-Andersen's theory of institutional power and the pressures that institutions can apply to countries to be more competitive on an international level. This institutional pressure becomes stronger if economic circumstances are added to the situation. This is particularly true for Europe, an area where 28 countries are economically and to a certain extent politically integrated.

2.7.1 Welfare: Theory and practice

The structuralist approach contends that the capitalist economic activity created the modern welfare state. In the liberal structuralist view as exposed above (Smith 1904, see also Marx 1974, 1971) and Chapter 3 (Strange 1988, 1996), welfare was a result of a confluence of power relations and economic logic that caused the state to take up the role of welfare provider to maintain the workforce and efficiency within the economy.

The Marxist structuralist (Esping-Andersen 1990) approach argues that the logical inconsistencies and the contradictions of the system as discussed above oblige the capitalist system to create a welfare concept for its workers in order to stave off full-scale revolution. This point was introduced briefly in the introduction of this chapter, making the case that welfare was a way to buy off people by providing for their needs up to a point, thereby reducing the exploitative consequences of capitalism and allowing capital to continue exploiting the people without fear of revolt (Offe 1984).

The institutionalist approach (Polanyi 2001) views welfare from the point of view of democracy and democratic institutions. It takes an empirical view of the matter, which leads it into the areas of citizenship and voting politics (Esping-Andersen 1990). The argument made here revolves around the argument that welfare provision is derived from majority demands. These majorities can take any form and are not limited to class or other similar social formations but can in fact be composed of opposed socio-economic groupings. The central point of the institutional approach is that democratic states are always going to follow majority demands.

The social democratic approach (Esping-Andersen 1990) focuses on the class struggles that determine the levels of welfare. The social democratic approach uses a composite argument of structuralism and institutionalism. The social democratic approach accepts that there is a hegemonic capitalist power structure, which shapes the concepts of welfare. However, it also acknowledges that institutions, i.e. parliaments, have the power to implement their own effective policy solutions which may differ from capitalist ideology (Esping-Andersen 1990). Additionally, the social democratic approach sees welfare as its own power structure, which is congruent with the argument made in Chapter 3. This approach overall fits very well with my own theory of welfare. However, this approach contains a number of problems. Esping-Andersen's (1990) approach overly relies on parliaments instead of third parties such as the EU or other European (and some international) actors to shape welfare regulation. It also assumes a greater unity among conservative than left-wing parties when it comes to agreeing on a path of welfare reform. Both those points are the most salient criticisms made against social democratic theory.

As the substantive chapter on Germany will demonstrate, the political left is no more or less fractured than the political right. In fact it was only through a firmly united leftist political alliance that the German Hartz 4 reforms, as they became known, were implemented. There was also very little opposition on the side of the conservatives and liberals which made the task even easier. The same goes for France. The unity of the French left parties, especially during the years of the Mitterrand administration, shows that there is no compelling evidence to suggest that there are any more significant fractures within the leftist parties than there are in the rightist parties.

This thesis emphasises the structural power of finance and neo-liberal capitalism to effect changes in welfare provision within a country and internationally. Although I agree with the position that changes are being implemented by national authorities, I do not see the state as the sole decision maker in this process but rather as a part of a decision making process, which includes many factors. In the case of France and Germany within Europe, these factors include the EU processes and institutions such as the Council of Ministers and the ECB, and the IMF among others. However, this thesis views France and Germany's guiding ideologies as the primary instigator for changes in policy on the national and international levels.

As pointed out above, the French and German conceptions of the state differ significantly from one another due to their history and philosophical preferences. France is much more heavily influenced by the Latin and Roman world and Germany is influenced more heavily by Greek philosophy. This has as a result created a more centralised state in France. In Germany, it created a more individualistic society with a concept of "auto-limitation" of the state allowing for differences within the state to exist so as to allow people to find the best way for themselves to live (Dyson 2009, 173) (this point will be further developed in Chapters 4 and 6).

Esping-Andersen's (1990) practical analysis of welfare centres on three types of welfare state, which he identified and which follow out from the theories posited above. Esping-Andersen maintains that all welfare systems can be placed in these three types: liberal welfare, social democratic welfare and conservative welfare (Esping-Andersen 1990). The liberal welfare state focuses on market solutions for the provisions of welfare to a large extent, only involving the government as little as possible in these operations. Countries where this is practiced, according to Esping-Andersen (1990), are predominantly Anglo-Saxon.

The Conservative welfare state uses a higher government involvement than the liberal state; this increased involvement centres largely on the family and tries to relieve pressures from the market. It is also the oldest of the three forms of welfare, as it evolved directly out of the imperial times of Bismarck and Napoleon. This type of welfare tends to prioritize social instead of economic ills in contrast to the liberal welfare state, which focuses on economic ills in favour of social ills. Countries considered to be in that section are Germany and

France (Esping-Andersen 1990) among others. The social democratic welfare state is the most generous welfare state of the three since it aims to provide welfare universally for all people within the country and not just those who contribute to the funds. This form of welfare provision Esping-Andersen (1990) associates with Scandinavian countries such as Sweden or Finland.

While I can appreciate Esping-Andersen's decision to put Germany and France in the conservative section, their current systems, especially the one in Germany, have moved away from that position. Furthermore, I maintain that, from the beginning, France never entirely fits within that section. Using Esping-Andersen's terminology, I maintain that Germany now has moved into the liberal welfare section using a conservative framework. The French case is constituted of a combination of factors, which have social democratic overtones within a conservative framework. This thesis substantiates this argument further in Chapters 4 and 6.

2.7.2 Peter Taylor-Gooby

Peter Taylor-Gooby's (2001) analysis takes an institutionalist approach to the issues by considering the abilities of national governments to implement welfare reforms; he does this without foregoing structuralist observations. He acknowledges that national governments are exposed to external international pressures especially in Europe due to the signing of the Maastricht Treaty (1992). The treaty established common rules for competition and common economic policies including rules on national debt and deficits, which impact national welfare provisions. Further more the Maastricht Treaty (1992) seeks to introduce further market liberal concepts into the European economies. The analysis done by Taylor-Goodby takes an economic angle in defence of welfare; focussing on the benefits welfare can bring to the running of an economy. Gooby's (2001) approach looks directly at the effects of changes to welfare provisions. His analysis studies the changes to welfare conceptions of nations due to the continuous integration processes conducted within the EU. His argument was that, given this continued European integration process, institutional pressures would eventually reach a point where an alignment between different national processes of welfare provision would become necessary. This necessity arises due to the common market and the discrepancies in competition created through the different welfare provisions among states. It would also be necessary to reduce undue strains upon different national welfare systems, which are burdened by people from other European countries migrating to countries with better welfare provisions. This in turn would indicate that common sets of reforms would need to happen in Germany and France.

Peter Taylor-Gooby's analysis also has certain shortcomings. For one thing, I am not convinced that an alignment among the different welfare programmes around Europe would have actually worked in a pre-2007/2008 financial crisis environment. Welfare provision forms part of national sovereignty (Strange 1988) and any move to transfer the duties of welfare provision to EU institutions would have required a new EU treaty or the renegotiation of existing treaties. It would also have required a common position on the rules and regulations as well as the size and eligibility criteria governing a European wide provision of welfare. Considering the popular hostility towards the Maastricht Treaty, the European Constitution and the Lisbon Treaty, any undertaking that would have transferred authority for welfare provisions to Europe, would have been met by equal if not more hostility by the national populations as well as their national governments. That being said, the liberalisation of the European economies did have an impact on the welfare concepts of the European nations since companies, to be attracted to settle within a country, required more flexible social security rules as well as a more flexible labour market. German and French governments are excellent examples of different actions and attempts to attract industries to their countries (see Chapter 4-7).

Post 2007-2008 financial crisis, this picture has changed. As Chapter 3 demonstrated, the creation of the EFSF and ESM to deal with the problem of potential default by some of the Euro Nations has opened the door for a further and closer alignment of welfare policies. This alignment of welfare policies is influenced by Germany in the first instance and France in the second instance. Although this alignment is only indirect and still determined by the nations themselves, it has become a reality. Time will tell if it is going to be fully integrated within the EU structure or remains a prerogative of the European nations.

2.7.3 Conclusions of social policy

All welfare is a product of its time: Medieval, Renaissance and Enlightenment Europe were times of absolutist or near absolutist rule, which only truly came to an end after the two world wars. Medieval, Renaissance and Enlightenment thinkers emphasised and encouraged the Christian concept of charity towards others so as to entice some marginal redistribution of wealth towards the lower classes as well as restrain, however little, the exploitative tendencies of the landed and wealthy classes without giving back or further increasing the powers of already powerful states or rulers. This enabled these thinkers to keep government small and at the same time provide some relief to the poorest in society. With the passing of time, especially during the Enlightenment and the Renaissance, states became “less absolutist” as they became slowly ensconced within a body of law. This also transformed the conception of welfare. Welfare changed during these periods from a matter of duty, of Christian charity to a matter of legal responsibility especially on the part of the state. However, these times were still times of absolutist rule, and the powers of the state were left largely unchecked instead of being equipped with modern safeguards against wide ranging abuse of power.

It was, however, the arrival of modernity and industrialisation, which brought a new set of economic developments and new types of government, which could build on the work done during the ages gone by. It was only in the last few centuries that the state has begun to be seen as an apparatus of care and an institution responsible for a well-governed economy and a well cared for population. How these developments affected the concept of social provision and how that impact transformed social provision into welfare provision is the task of the next section.

2.8 Welfare

Christopher Pierson (1991) argues that welfare states are born when states actively try to improve the lot of all people living within its society through three very specific means i.e. the introduction of social insurance, the extension of citizenship and the growth of social expenditure. Once a state actively tries to improve the lot of all people living within its society, the state has taken on the responsibility of care and protection of its people; using the logic and terminology of Rousseau (1973, 1984), the state has entered into a social contract with its population to continue to provide that care. As this section demonstrates, once democratic institutions became more widespread throughout Europe and industrialisation continued to progress, the authoritarian solutions that enforced legitimization of the state became less and less successful and states needed to find a new method of legitimization. The states found that legitimization in the provision of welfare to its population as the Bismarck welfare concept clearly demonstrates. Before this chapter considers the Bismarck welfare concept, it first assesses what is required for a state to be considered as a provider of welfare.

2.8.1 The establishment of Welfare

1. Introduction of social insurance

Chancellor Otto von Bismarck first introduced social insurance in Germany between 1881 and 1889 and was consequently consolidated under the "Reichsversicherungsordung" (RVO) of 1911 (Eurofund 2009). France followed Germany's example, instituting the same social security provisions up to 25 years after Bismarck had initially introduced them (Pierson 1991).

One noteworthy point is that Bismarck's centre-right government undertook those German social security reforms; in contrast, the Hartz reforms reshaping of social security, which included a downsizing of social security provisions, was undertaken by left leaning parties (i.e. SPD and Greens) during their time in government (Schröder, Blair 1998). In France, these reforms were usually undertaken during centre-left, leftist or radical socialist governments during the Third Republic. This shows a different approach towards welfare in both countries. In Germany the establishment of welfare was designed to placate the population by providing a little security and empowerment, in France these reforms were specifically designed to empower the population and to allow them to work without fear of being made redundant. This is also a reason why in France the culture of state *dirigisme* was so strong and, it could be argued, is still applied (see Chapter 6 for further details).

2. Extension of citizenship and the de-pauperization of public welfare.

Once the state decides to introduce universal social insurance and welfare provision, it also needs a way to determine who is eligible to receive those benefits. Hence the state needs to define citizenship for eligibility and reconceptualise welfare as a right and not an extension of charity. The eligibility criteria for welfare in Europe have begun to be much more rigorously defined by the individual nations. The Advocate General of the ECJ has argued that countries may refuse aid payment to people in need of assistance if their sole purpose is to come to the country to receive those benefits (Pop 2014).

The extension of universal male suffrage was introduced in and around the same time the first welfare programmes were introduced. France was the first country in the world to introduce universal male suffrage “in principle” in 1792 and has become an irrevocable part of French elections since 1848 (Vautherot 2008). In the case of Germany, male suffrage was introduced in 1884, the same year that Bismarck also introduced Industrial accident insurance (Pierson 1991). Although the introduction of insurance did not cause the establishment of voting rights in Germany, it does allow for a link to be established between the provision of social security and citizenship rights. Over time, further voting disqualifications were lifted, such as the necessity to own land, pauperism, being female. In 1918 universal suffrage was achieved in Germany followed by France in 1945, 153 years after its original institution (Pierson 1991).

This extension of civil rights had three very important implications for social security. It removes the individuals receiving social benefits out of the category of disdainful and lazy people to take pity on and to be avoided. Since all people now receive, and are entitled to, social security benefits, as well as being entitled to vote, members of every social class can vote on how much welfare is to be provided to the members of society as well as share in its provision. According to John Rawls’ (1999) difference principle and his concept of the veil of ignorance, people who do not know how well off they will be in the future or what may happen to them, will vote to keep welfare provisions at a level that improves the lot of every person especially the poor, since nobody knows if at some point they may be poor themselves. The establishment of welfare also enhances people’s concepts of citizenship as citizens are provided with a safety net enabling them to increase their autonomous spending which in turn will also increase their individual freedoms (Pierson 1991).

It should be pointed out that national social security programmes also put stresses on the social fabric of society as people who are not citizens but still live in those countries are also entitled to part of those benefits. This can lead to an “us and them” mentality, which can be very dangerous as the growth in far right parties in France, the Netherlands and the UK over the last decade demonstrate (Swank, Betz 2003) this has reached a point, that the issue is now taken up by the ECJ (Pop 2014). Third, the introduction of welfare and the extension of citizenship rights to public welfare clearly demonstrate a distinct change in the conception of social welfare. Social welfare is no longer limited to the definition of securing the population against threats from other people. It now also includes making sure people are safe at their workplace and are cared for throughout their life. The state's increased portfolio of care and assorted powers to implement and enforce them cements the state's new reason of existence and for being in power and allowed to rule over the population within its borders.

3. Growth of social expenditure

Measuring growth of social expenditure during the period around the turn of the 20th century is not a precise science, so the numbers in Table 2.1 below should be looked at with caution.

Table 2.1 The growth of social expenditure

	Social Expenditure ≥3% GDP	Social Expenditure ≥5% GDP
Germany	1900	1915
France	1921	1931

(Extract from table 4.4, Pierson 1991, 111)

Table 2.1 shows that in 10-15 years social expenditure grew by 66% (own calculation) in Germany and France. This is a strong indication that those countries were not setting up their own version of the English "Poor Laws" but that these programmes were designed to be a constant part of the social fabric of the country and administered by the state. This is further demonstrated by the continued growth of the welfare budgets in France and Germany between 1940 and 1980 (Pierson 1991, 106-107).

This growth trend of social security has continued into the new millennium. In 2007 the welfare budget settled in at 24.727% of GNP in Germany and at 28.07% of GNP in France (OECD.stat, accessed 2012). This shows that social security budgets have continued to be a part of the social fabric. Considering the size of the budget they take up, they have also become a major staple in the national budget of Germany and France, giving further weight to the argument that the provision of welfare is the reason for being of the state in a democratic society. Because of its longevity and continued importance for the state and society, it is extremely unlikely that social security will ever disappear entirely from national budgets, a point also substantiated by Peter Taylor-Gooby's (2001) research.

2.8.2 Bismarck

Bismarck's system of welfare later consolidated under the "Reichsversicherungsordung" (RVO) of 1911 (Eurofund 2009) was the first "real" system of welfare in the world as well as a matter of political opportunism and an attempt at social peace, rather than a voluntary effort to improve the lot of the population. Bismarck introduced Industrial Accident Insurance, Health Insurance and Pensions, to help the population insure itself against the unforeseen circumstances of life. The social insurance scheme developed by Bismarck has lasted into the modern welfare state with little revision to the type of provisions though with many revisions to the framework within which these processes were conducted. The adaptations and revisions to modern welfare provisions were caused by the particular philosophy of the country applying them. The primary function of these early welfare systems was not to care for the wellbeing of the population. Early welfare systems were an attempt at quelling the rising influence of the socialists and their much more radical socialist demands (DOCOMM 2009). In the case of Germany, it was a pragmatic attempt by Bismarck to quell the rising demands for democratic socialist ideas and at the same time strengthen the monarchy by portraying it in a benevolent and caring light (Eurofund 2009) instead of the imperialist and repressive side, which tends to stand out.

2.8.3 Beveridge

Pierson's definition of the beginning of social security coincides with Bismarck's introduction of social insurance. Thus, over 60 years before the Beveridge report laid out the arguments and the plans for a full package of care for the individual, Germany already had a system in place that provided benefits to its population on the basis of an insurance scheme. William Beveridge's concept for social security, which is the second concept to be considered by this thesis, undoubtedly borrowed some ideas from Bismarck, but Beveridge would significantly expand on them. Beveridge also had different motivations than Bismarck did when Beveridge developed his plan: Beveridge wanted to *empower* the individual *through* welfare, and Bismarck wanted to *placate* the individual *with* welfare. It was likely this sense of empowerment why France used the Beveridge system in conjunction with the Bismarck system to set up its modern welfare state (Chauchard 2010).

The Beverdige Report (1942), compared to the Bismarck reforms, was a much more idealistic concept of welfare with a sincere desire to improve the lot of the general population and not so much a pragmatic solution to growing unrest within the country. Beveridge wrote two reports on the subject of welfare reform. The first one focused on the problems of not having adequate income to preserve one's existence and the issues stemming from that inability. Those issues were: “Want, Disease, Ignorance, Squalor and Idleness” (Beverdige 1942, 6).

At the time that this report was written, Britain had updated and expanded on its Poor Laws established during Elizabethan times, with other types of social insurance. For that time period, these provisions were quite generous, and all were individual programmes, many of which were privately funded. The first Report analysed the number and effects of these individual programmes and concluded that too many inconsistencies and not enough help were provided by the system. Beveridge in this report sets out the general idea for how to reform the welfare sector in Britain and address the issues of Want, Disease, Ignorance, Squalor and Idleness (Beveridge 1942, 6):

> The State in organizing security should not stifle incentive, opportunity, responsibility; in establishing a national minimum, it should leave room and encouragement for voluntary action by each individual to provide more than that minimum for himself and his family (Beveridge 1942, 6-7).

The minimum provided in Beveridge's plan is also there to alleviate want, which for Beveridge is the worst of the five issues that he raises, since want amplified the other issues, causing increased misery. In order to adequately deal with the issue of eliminating want and the other issues, Beveridge attacks the problem from two different but connected paths.

In his first report Beveridge (1942) develops a social security system which is designed to lift people out of poverty i.e. relieve their greatest level of want and in the process reduce the other four issues. This relief is provided by redistributing wealth among the population through the homogenization and universalization (in terms of contributions paid) of the different private social insurances particularly health insurance, pensions and child allowance. It was designed to be as simple and accessible as possible for everyone. Only one tax would be levied on income, which would be supplemented by employer and state contributions, with all members of society having access to it (Beveridge 1942). All aspects of life are being secured for in this document, irrespective of demography, class standing, gender, race, creed, occupation, social standing or education. Beveridge in this report also made it unmistakably clear that this welfare proposal is designed as a safety net (albeit a very generous and soft one) and not a method of supplementing income without participating within working society without a very good reason.

Beveridge's (1942) welfare state takes the form of means-tested altruism. His concept aims to ensure basic sustenance for all by providing adequate help for all members for any length of time necessary. This is provided without *disqualification*; however, certain *qualifications* about its provision need to be made. Beveridge (1942) was aware of the financial outlays necessary to fund this endeavour as well as the myriad of complications associated with such a system (human freedom, human laziness). The way these proposals are funded and conditioned work towards addressing those issues. The funding of welfare is set up in such a way as to share the burden among Employer and Employee and the State within proportion, to discourage abuse, and allow for payments in perpetuity to those who need them if necessary.

The first Beveridge report starts going down the road of a political-economic argument. It analyses the conditions within which people in the UK find themselves and the political-economic consequences those situations may have. The report also provides a first overview of the potential solution to resolve that problem. It is, however, only in his second report that Beveridge develops that point and actively begins to consider the economic requirements for sustaining the welfare plan, which he developed.

The second report focuses on reducing want through employment. Beveridge's second report (Beveridge 1945) goes beyond simple welfare ordinances. Since the welfare system is designed to provide a stopgap measure, albeit indefinitely, for people who are unemployed, for children, women and pensioners, financing of these services cannot only be borne by the state without help. Employment is a substantial and essential part of this welfare system since it is one of its main sources of funding. Beveridge has an acute sense of the interconnectedness of the social and the economic in the same manner that Keynes did. Beveridge argues that, since for social security the responsibility is shared among the state, the employer and the employee, this division of responsibility should also apply to the economic fortunes of the country.

In economic matters, the state has increased responsibility since it falls to the state to ensure high levels of employment providing a buyer's market for employees instead of a supplier's market for employees. This would ensure the continuing and adequate supply of labour for companies to draw upon and would allow the welfare system to run at its most sustainable and most efficient. The section below gives a more detailed explanation as to how this is supposed to be achieved. The management of the state is, however, limited by a number of factors.

All parties to this welfare agreement have responsibilities and rights, just as they do in terms of the economic situation. Although it is the state's responsibility to ensure that companies can operate freely on the market, the state's chief concern is that people are able to work or find work quickly. It is the responsibility of the companies to employ as many people as they are able to and pay them decent wages. It is the responsibility of the people to actively try and find a job as quickly as possible if they are currently unemployed, and to work and pay their dues to social security if they have a job (Beveridge 1945).

Beveridge also foresaw the demographic problem that European countries (Germany in particular, see Chapter 4) are currently facing. Beveridge encouraged childcare funding before pension funding to maintain a generational balance within the contributions system. This recommendation highlights the paternalistic and conservative aspects of this welfare plan. The way this report is descriptive and detailed. Although only a proposition to the UK government, it resembles significantly the principle by which the German Hartz reforms have been instituted.

Both reports are geared towards curing want from society to a point where it is no longer crippling and making the programme responsible as sustainable as possible for as long as possible. In all of the points Beveridge raised, he wrestles with his commitment to individual freedom derived from the neo-liberal concept of non-interference. The result is a mix of social democratic ideas (in terms of provision of welfare) and conservative and liberal ideas in certain aspects of the conditionality of the service. The Beveridge Reports (1942, 1945) try to find a line, which allows Beveridge to profit from the powers of the market fully, by protecting the freedom of the people and at the same time provide some tutelage for industry and individuals alike by way of state interference within the market and within individual decision-making. The result of this struggle is an economic and social principle, which is very close to Keynesian economic theory especially when one considers the notion of active government interference within the market to maintain employment and consumption. However, as opposed to the Keynesian model, which will be analysed next, Beveridge does not preclude the collectivisation of assets and the socialization of the market should it prove to be a better provider of work and eliminator of want.

2.8.4 Keynesian Economics

The current European welfare model is based on classical economics Keynesian variant. The Keynesian idea of welfare is based on economic growth. The Keynesian economic model assumes that the state interventions in the market can lead to full employment as well as non-inflationary growth (Keynes 1936). This point was challenged by the Mundel-Flemming model showing that one could either achieve full employment or low inflation but not both (Carlin & Soskice 2006). This then leads to a welfare structure designed to compensate for weaknesses in that system as Beveridge (1942, 1945) pointed out in his work. In order to keep up the growth of industries, consumption needs to remain at a high level. This welfare system therefore developed welfare benefits to cover any shortfalls in consumption such as unemployment, old age or work accidents.

Because this economic model is designed to maintain economic growth but not to overburden current generations with welfare contributions (as Beveridge (1942, 1945) already pointed out), it also requires a continued and increasing supply of workers, to spread the burden of social welfare contributions among more people and to fill the vacancies created by growing industries. Therefore, for this “generous” model of social welfare to be viable, people need to have a working life of 40-45 years in which they regularly contributed to social security.

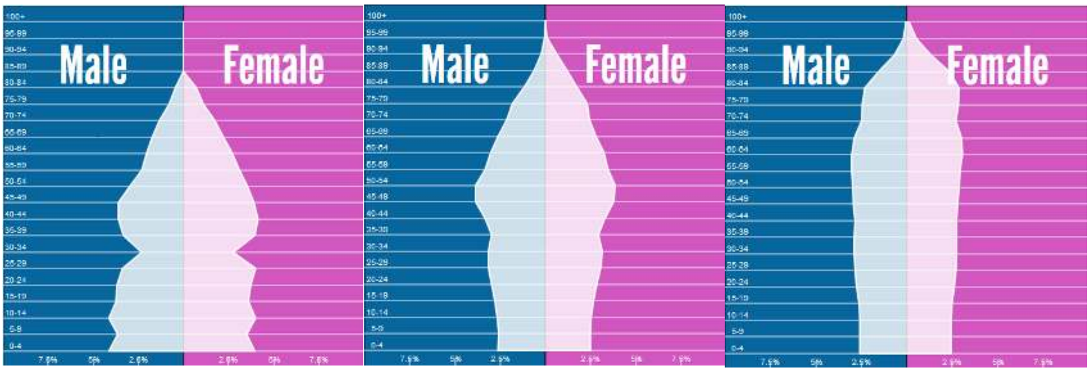
This combination of low unemployment and positive demographic growth would provide a stable system in which people would be secure by maintaining their status until work can once again be re-established (Esping-Anderson 1999). Since industrial society allowed little to no upward movement in terms of employment, i.e. workers were employed for doing the same job their entire career, the welfare state was designed to compensate for that by providing social security and welfare benefits as well as income redistributions through taxation, disposable income of lower income households was increased. Within this system, generational mobility of any kind was not a high priority. Rather, the priority of the system was to make sure that people in their current state were well cared for. While the Keynesian economic concepts have been replaced by neo-liberal economic concepts on the national and international level, the Keynesian welfare state concepts remain in place and will be evaluated within the next part of this chapter.

2.8.5 Problems with Keynesian Style economics

A key aspect of modern social welfare remains a need for positive (i.e. more births than deaths) or at least a stable (non-negative) demographic evolution. However, as Table 2.2 shows below, demographic changes now indicate that populations get older but not enough new people come into the system to compensate for the increased lifespan of people and the continued provision of social security benefits to those people. As Table 2.2 demonstrates for the period from 1950 to 2015, there will be fewer people born than there will be people who are set to retire within those 65 years. The situation is set to worsen further by 2050. It is argued that this will lead to a shortfall of contributions into the welfare system on which the Keynesian and Beveridge models rely to stay viable. This is an issue that needs much more concerted efforts as the future costs of supporting dependent populations will need to be met by current economic output (Pierson 1991).

Table 2.2 Population Pyramid

Western Europe 1950 | Western Europe 2015 | Western Europe 2050



Source: United Nations 2012a, 2012b, 2012c

That is a demographic problem but there are also analytical ones. Keynesianism as well as Neo-Liberalism treats environmental degradation as an externalizing factor (Araghi 2010). Keynesians do not have a scarcity principle in their economic theory. However, more importantly, neither theory considers entropy or the laws of thermodynamics in their economic models (Kronenberg 2010). Keynesian theories focus on economic growth and full employment; environmental concerns always come second to that. Ecological economists argue that this focus is dangerous:

> … growth is a two-edged sword – it may help reduce unemployment, but it exacerbates environmental problems. The attractiveness of growth-promoting policies should be reconsidered in the light of this, and the distinction between qualitative and quantitative growth should receive more attention … (Kronenberg 2010, 1492)

Economic concerns are paramount over all others, because Keynes desired a comfortable life for all people. Keynes did not desire a lavish life for them. However, a lavish lifestyle is what has developed, due to the focus on continuous production and growth. This growth-based model had other problems than a lavish lifestyle: i.e. environmental and mental and physical degradation. The problems that such a lavish lifestyle brings range from: "stress-related illnesses" (Pierson 1991, 193), such as depression and autoimmune diseases, to "diseases of affluence" (Pierson 1991, 193) such as obesity, diabetes and addictions. It also brings with it health effects related to environmental degradation such as asthma and allergies. Significant concerns also exist about farming and over fishing causing reduced biodiversity. Other concerns include agricultural priorities, focussing on fuel production or cattle raising, which have significant impacts on food availability as well as affordability (Mc Michael, Powels, Butler and Uauy 2007).

A great amount of economic activity remains damaging to the environment, but is also damaging to human health. Unsafe and unhealthy employment conditions result in approximately two million deaths annually as well as causing 8% of worldwide cases of depression, which are related to work stress (Ivanov, Kortum 2007, 2). This demonstrates how essential welfare provision is to an economy, since welfare can mitigate such unhealthy working conditions through the provision of healthcare and other forms of physical and mental support.

2.8.6 Problems with Neo-liberal economics

With the economic downturn of the 1970s the voice of the neo-liberal new right has grown rapidly stronger, as this historic downturn allowed them to comment on the effectiveness of Keynesian theories and quickly replace them. Furthermore, it allowed them to picture the public sphere of welfare and economic interventionism as inefficient and bureaucratic and limiting the freedoms of people living in such systems (Clarke 2004). As much as the economic right ideology would like to see a large-scale scaling back of social welfare provisions, welfare has formed a part of the economic and political system of countries for almost a century now, thereby fully integrating within the economic and social fabric. There is much at stake in those social welfare provisions remaining as and where they are.

> Even those governments most powerfully committed to a reduction of the welfare state have found it to be stubbornly evasive of financial constraint (Pierson 1991, 182).
> The most basic and crucial fact about the modern welfare state is its deep and massive presence in the day-to-day lives of millions of citizens (Pierson 1991, 183).

This is exactly what the neo-liberal system is trying to reverse. Considering that firms argue that they are much better at providing services to people since they are dependent on the service being satisfactory by the customer, or else go out of business, their efforts will always be aimed at improving services in order to maintain their client base (Crouch 2011). Considering that this argument is beginning to find wider acceptance even in public services, it changes the dynamics of the state-firm relationship ever further in favour of the firm and provides ever more structural power to the firm and to its partner international finance. The consequences of this continuing shift in power will be considered in greater detail within the next chapter.

2.9 Conclusion

This chapter undertook the task of demonstrating the different economic and welfare theories that exert influence over structures of power, which are at play within the international political economic arena. This chapter also analysed how the change from one economic concept to another can impact the general understanding of the state within its provision of welfare. Therefore, the second part of this chapter aimed to determine what welfare was, and how it evolved. It did so in order to analyse its importance and thereby the state's importance within the economy and within society.

The Liberal theorists presented here all believe that their economic concepts will achieve the best possible outcome for all participants. Their concepts both base themselves on the idea of freedom; freedom of the individual and freedom of enterprise. However, they draw very different conclusions from those concepts. The neo-liberals use an economic argument, proposing that market freedoms will allow people to be free to choose how to enter and interact within the market while also providing a more effective and efficient service. They argue that market economics can handle all political economic troubles arising within a society. Institutions, which are not subject to market forces, are a disruption to its efficient working.

Classical liberals on the other hand believe that economics is unable to handle all the political and economic aspects by itself and needs help from the state. Their concept of a free economy and free individuals involves government guidance and aid where necessary. Economic processes are guided and regulated to be continuously striving for better products and services. National industries and individuals are aided through subsidies if their economic situation deteriorates.

Neo-Liberal and Classical Liberal concepts therefore have a central concept of the state involving a definition in terms of its responsibilities. Neo-Liberal theory of the state sees it in a much more limited form whereas Classical Liberal theory of the state sees it in a more expanded and active role within society.

This chapter undertook the task of determining what welfare was, how it evolved and the importance of welfare was to economy, society and most of all the state. The social welfare systems have a long legacy and have proven to be resistant (within reason) to changes within the liberal economic thinking and tenacious in their longevity. However, the rapid surge of neo-liberal economic concepts has been able to pose a serious challenge to that resilience.

Welfare has evolved from humble beginnings of the Christian concept of charity within authoritarian states. Welfare has over the centuries continued to evolve out of a charitable duty to a limited legal requirement (in principle). It was only once democratic governments were becoming more common and that industrialisation evolved and progressed further that welfare made its next big evolutionary leap towards a fully state guaranteed and supported provision to help and protect people from capitalist failures.

This move was not done out of pure altruism as Bismarck's actions confirmed but they were rather pragmatic actions by a state which was increasingly struggling to remain relevant in a world that had become increasingly dominated by economic logics. The state's decision of socio-political-economic intervention ensured its continued relevance and support by the population.

Since the days of Bismarck, welfare has integrated so completely within society and has taken up such a large portion of the GNP of a nation that any nation would now be hard pressed to remove it in its entirety as well as be hard pressed to defend that move to their own populations. As these three sections have shown, the provision of welfare is similar among nations; it is however the conditionality of care which changes in different models. The different welfare ideologies analysed above are not perfect. What they do is address the issues, which the social and economic framework within the state creates. The social systems work on a mix of employer, employee and state contributions whose availability is dependent on the system within which they work. However, the ability of these social systems to continue to address all of these capitalist failures has been made much more difficult by the 2007-2008 financial crisis (investigated in Chapter 3) and has provided further opportunities for international finance to acquire structural power.

The following chapters investigate welfare concepts of Germany and France and the reforms or lack thereof undertaken to deal with the economic realities of Germany and in France. In the case of Germany and France, I will demonstrate in the substantive chapters that both systems are variations on the same theme. As already outlined above, Germany and France, have conservative social security systems which frame the provisions provided to the population; however, the *universality* and especially the *conditionality* to receive these benefits varies significantly within the two countries as the following chapters will further show. I argue that Germany, which has reformed its welfare system, now has strong neo-liberal concepts at work within the framework of welfare after Hartz 4 and that France, which has yet to reform its welfare system significantly, has strong social-democratic concepts at work within its own framework of welfare.

This analysis will aid in my argument that Germany and France are through their participation in institutions of the Troika - i.e. the European Commission, the ECB and the IMF, have further committed to the liberal economic principles initially set out in the Maastricht treaty and in the European Exchange Rate Mechanism. They are thereby shaping the austerity conditions which countries under the umbrella of the EFSF and the ESM must apply in order to receive that protection. The following chapter will consider what impact the two different liberal conceptions here analysed have upon finance. It will consider the perils of financial deregulation and introduce the discussion of the impacts of that deregulation on national welfare systems.

Chapter 3 From a financial to a fiscal crisis: the consequences and repercussions of deregulation and unregulated practices.

3.1 The New Crisis

Chapter 2 argued that the balance of structural power between the state and markets has changed, because the classical economic and Keynesian economic concepts have been rapidly replaced by neo-liberal economic concepts. This shift towards the neo-liberal economic concepts constituted a move towards an understanding about the necessity for less state intervention and de-regulation within the markets. This shift in concepts had a significant impact on the welfare conception of states and their role in its provision. The power of states and industries has become subordinated to a certain extent to the power of financial markets. This chapter will investigate how this shift changed the structural power of the financial markets, not only in relation to the state but also in relation to industry.

As Chapter 2 touched upon, neo-liberal economic concepts have created a perfect financial market that holds important structural power within the global market, but at the same time, this perfect financial market is extremely volatile and prone to crisis. As this chapter will show, the foundations for this crisis were laid long before its appearance, and warnings about a potential crisis were voiced long before the crisis. The 2007/2008 crisis happened, because the warnings were not heeded and the relevance of the state within the market was continually reduced, allowing the market to increase its structural power. The first section of this chapter will analyse this process.

Although the reasons for the occurrence of the 2007-2008 financial and economic crisis have been known for some time, the consequences this crisis spawned have not been experienced like this before. The impacts on the concept and provision of EU welfare due to the existence of the Euro and the constitution of the Euro Zone differ from previous crises. With the rapid replacement of Keynesian economic concepts by neo-liberal economic concepts on a global scale (Crouch 2011), the European nations resolved to implement those neo-liberal changes on a European scale. This was achieved by establishing the European Exchange Rate Mechanism (ERM) in a first instance and was built upon, with the establishment of the Maastricht Treaty. These agreements and treaties established the common European currency and set the foundation for the neo-liberal economic concepts to be disseminated throughout Europe (Sapir 2006). While they did not create the convergence that was aspired to when the treaties were initially developed, particularly in terms of national welfare, they did, however, lay the foundations for further enlargement of competencies away from the nation states and towards the European institutions and international markets along neoliberal lines. The second and third section of this chapter will consider the establishment of the new rules and regulations as well as the new European institutions which were spawned by the consequences of this crisis. The final section of this thesis will consider the state traditions of Germany and France to provide an understanding of the German and French receptiveness of these neo-liberal policies.

Since the underlying factors of this crisis are similar to previous crises, the first section in the chapter will provide an analysis of the evolution of the circumstances leading up to the financial crisis. I argue here that Susan Strange's concept of structural power, complemented in places by the work of Colin Crouch (2011), allows for an analysis, which takes account of the neo-liberal pressures upon nations that were exercised through the financial structure. Strange's investigation focuses largely on the regulatory authorities of the financial structure, identifying several instances of moral hazard, which allowed a change in the structures of the financial system. I argue that it was this increase in the instances of moral hazard, which allowed the sequence of events to occur, which caused this financial crisis. In order to support my assertion, I investigate the events that unfolded, which lead to the USA financial crisis in the second section. This provides evidence to my argument that this crisis was caused in large part by the previous changes within the financial structure.

This crisis differs in the size of the collapse and the speculations that caused the collapse. The biggest difference is the existence of the Euro and the Euro Zone, which was infected by this crisis. The cure implemented by the Euro Zone (EZ) countries had wide-ranging consequences for member countries, in particular on their ability to provide welfare. In their efforts to resolve the crisis, the EU has established the EFSF and the ESM and reinforced the rules of the stability and growth pact. The establishment of the EFSF and ESM and the reinforcement of the stability and growth pact allowed Germany to push for austerity budgets to be implemented through the use of its structural power within the Troika and the ESM.

Due to the size and the type of speculation done on the financial market, countries resolved to fiscalize the financial debt accumulated and traded among banks and other financial institutes in order to prevent a complete collapse of the financial system as all parties involved within the economy would suffer the consequences and not just a specific sector. This action set in motion a chain reaction of events culminating in the imposition of austerity within the EZ. Austerity was imposed by the European Council Ecofin led by the major players in Europe and the Euro Zone: Germany and France and supervised by the Troika of, ECB, IMF and European Commission (all institutions that promote neo-liberal economic views). The consequences of austerity created significant pressures for the traditionally held understandings of welfare and especially welfare provision within Europe, the consequences of which will be analysed in Chapter 8.

The financial crisis in the USA was at the origin of the crisis in Europe. The third section accordingly considers the consequences of this crisis. In particular it considers the pressures austerity has put on the understanding and provision of welfare wherefore it will consider the special features of this particular crisis. These features include: the European Common Currency, the Euro Zone and the ESM and EFSF which have powers over providing funding for governments in budgetary difficulties. The powers that these features have can force reforms in other EZ countries for fear of needing the help of the ESM, which would require a much more severe level of austerity.

The application of these powers and their setup have been heavily influenced by state traditions, especially those of Germany and France, which in turn helps define the relationship between the state and industry. Considering the extent of those powers, this thesis will first investigate the German and French state traditions before describing the new powers of the EU more closely.

3.2 How has finance risen to such an important position?

This section analyses how, through inaction and active participation by the state, the financial structure has been allowed to be reformed to such an extent that it allowed the market to become more free but also more volatile and to eventually break down, opening the way for the reconceptualization of welfare on a European level.

> During the 1980's, a hyper-liberal form of capitalism gained ascendency, spreading from America and Britain over much of the world. It is characterised by a liberating of the private sector from state intervention (Cox 1995, 37).

3.2.1 A not so Strange answer

Without political authority, there cannot be a market. Since states are the locus of political authority, states ought to be the main governors of financial activity, Strange and Crouch (2011) focus their analyses on the power relationship between states and markets (Strange 1997, 1995, 1991). In her view, it was the international "non-decisions" (Strange 1986, 31) of economically and most importantly financially developed nations that began the road to the financial crisis. Furthermore, Crouch (2011) argues that the reason these "non-decisions" were taken was because of the industry narrative of neo-liberal economics describing industrial activity as something to be emulated (see also Hartz reforms in Chapter 4). Since industries operate within markets which require them to be efficient and effective, they are able to provide better customer services and do so at lower costs and should therefore be emulated by state. If the state did not emulate these practices, at least then the state should not interfere with the actions of industries lest they would cause inefficiencies.

Non-decisions particularly relevant to the current crisis included not agreeing upon a common provision of credit and the management of debt (Strange 1986). Another non-decision was the non-agreement upon a common standard for handling bad international debts (Strange 1986). A final international non-decision relevant to the financial crisis was the British decision (made by Harold Wilson) to allow London to reopen its international trading markets (Strange 1986).

The USA has on its own also made significant contributions for the increased power of the markets. US financial regulatory companies hold hegemonic positions within the global financial markets. The US has made many *non-decisions* that changed the power relationship not between the states themselves where the US continues to exercise a hegemonic position, but between the states and the market (Strange 1986). While the US remains the world's sole hegemonic nation (in relation to other nations; see Strange 1987), it is the neo-liberal forces *within* the nation that have taken over the agenda setting for the government in economic matters (Strange 1986).

According to Strange (1997), the rise of finance came about through inaction, specifically in terms of the decision by the USA and many of its European allies not to intervene through regulation in the financial markets or within the running of financial actors and institutes even going so far as to dismantle certain financial regulations (see Glass Steagle, Rickards 2012 and Gram-Leach-Bliley Financial Services and Modernisation Act, Crouch 2011). These *non-decisions* had significant consequences on financial markets, effectively transferring structural power and authority *away* from the state and funnelling that power *towards* the financial structure, the financial institutions and its financial actors creating “Finance Capital” (Harvey 2006). The Gram-Leach-Bliley Financial Services and Modernisation Act (Crouch 2011) is particularly troubling in this context since it allowed retail banks to use customer deposits in financial speculation, drastically increasing the financial capital available to traders to speculate with, thereby further fuelling the speculation bubble (Crouch 2011).

It was this governmental *inaction*, which allowed banks and other financial institutions as well national and transnational firms to restructure their operational procedures (Strange 1986, 1998). This concept of *inaction* or *non-intervention* is derived from neo-liberal theory (see Chapter 2), its application opened up the financial markets to new and expanded forms of global financial speculation. It set the foundation for a complex web of hedge markets, currency swaps and an immense number of other tools developed by banks and finance institutes for themselves and for traditional firms and states to capitalise on these new financial markets.

This neo-liberal concept was also applied within macroeconomic thinking and currency regulation. Monetarism argues that freely floating currencies would facilitate automatic and efficient exchange rate adjustments resulting in an efficient currency market which would make pricing more efficient and thereby make markets in general more efficient (Friedman 1956, 1956a, 1991). It would also provide national governments with the ability to (re-) or (de-) value their currency, thereby gaining an additional tool of macro- and microeconomic management (Timmermann and Granger 2004).

For example, with more and more central banks gaining independence from their national governments, these institutes have usually pursued a policy of no or only minimal intervention in the markets. Central banks have stayed clear of any regulation relating to currency trading, merely adjusting money supply to manage growth (though not as heavily as under the Bretton Woods system). The *lack* of intervention by the Central Banks (CB) causes currencies to fluctuate more wildly than if there was intervention (Strange 1997). This created the need for finance managers in the financial as well as the productive sectors to manage their assets so that they would not lose value through currency fluctuations (Strange 1997). This counts especially for transnational companies (TNC).

> The need to swap deposits in different currencies in order to match corporate hedging transactions and to square the books is largely responsible for the growth and size of the interbank market (Strange 1997, 12).
>
> Because of the greater volatility of exchange rates, the Eurocurrency markets became a channel by which any event, which affected an exchange rate, whether that was a change in the trade account, some political event regarded in the market as a plus, or minus for a particular currency was transmitted to the credit markets (Strange 1997, 12).

3.2.2 A moral hazard

Susan Strange (1988) pointed out that the lax nature of government regulation and control of the financial structure on a national and international level resembles more a code of conduct, i.e. company self-regulation, which is applied and perpetuated by the USA instead of specific and enforceable regulation. Further to Strange's analysis, I consider this nature of American regulation to be a moral hazard since it allows companies to engage in risky economic behaviour, which would otherwise not be allowed under state regulation.

The lack of feasible national or international financial market intervention makes the business climate uncertain and difficult. Due to the moral hazard established within this financial framework, risk is no longer known since the risk assessments also fall under the instance of moral hazard. Such uncertainty requires much more capital by firms in order to survive any potential losses from short and long term monetary and interest rate changes (Strange 1997). This uncertainty created hedging services by banks, which in turn allowed risks to be mitigated allowing companies in turn to take more risks, creating instabilities within the system.

The hollowing out of the structure of regulation was a consequence of the transfers of power away from the state towards other state and non-state actors at the local and the supranational level what Palan (2003, 130) termed “race to the bottom”. However, the transfer of power towards the markets is the most relevant one in this situation. The competition among states for access to markets is an intense one, as well as being very lucrative when the access is acquired (Wallerstein 1974, 1980, 1989). Markets, more than any other form of aid, can improve the economic standing of a country (Strange 1991). It is because of this that changes in the attitudes towards regulation resulted in the decisions not to intervene within market operations. Further examples are the decisions made by the USA to give the exchange rate over to automatic market adjustments and no longer act as a lender of last resort (either on the national or international level) as well as its decision not to negotiate with OPEC (Strange 1986, 1995). The reason for this shift, Palan (2003) argues, is that the nature of the state has:

> shifted from so-called demand side to supply side management of the economy, or from the Fordist to the competition state (Palan 2003, 130)

Shifting from demand to supply-side economic management comes at the cost of shifting the state's emphasis from the active engagement in the regulation of the international market to state competition through national deregulation of markets and labour. The desire and need for continuous external sources of finance creates international competition among industrialized and Third World nations to be the most attractive market for investment. This competition in turn causes countries to limit or reduce national regulation of industries. One way to achieve this inflow of investment capital is to provide “attractive” investment opportunities to financial firms. Countries therefore become service providers competing on a global level against other countries. The concept of the citizen has also changed into that of a consumer of governmental services (Palan 2003).

> Consumer-voters are fully mobile and will move to that community where their preference patterns, which are set, are best satisfied (Palan 2003, 159)

To Palan, the nation state in its classical-liberal, interventionist and welfare providing form (see Chapter 3 for further descriptions) is under attack by neo-liberalism, on the one hand through the economic message of individual freedom and development which, redefines society in a more “utilitarian” way (Palan 2003, 161). On the other hand, the classical-liberal state was under attack through the continued drive of globalisation and the increased calls for forms of “global governance” (Palan 2003).

The turn towards a neo-liberal non-interventionist state form also gave birth to a new financial structure, with different limits on financial dealings (Strange 1987; Goodhart 2008). Since the financial sector was left to its own devices, it was free to develop its financial instruments in any way it saw fit. One of the central innovations that came out of this liberalization was "originate to distribute" (Goodhart 2008, 334; Kiff 2007).

> Under this strategy the banks originate loan business, for example in the form of residential mortgages, and then pool baskets of these loans, together in various ways, and securitize and distribute them, so that such loans, changed into new securitized format, leave their balance sheet. So they originate the loans securitize them and then distribute them to various non-bank financial institutions (Goodhart 2008, 334).

Risk therefore changes from an exogenous factor of the capitalist system against which firms secure themselves through the creation of derivatives and becomes a derivative; abstracted, monetized and traded in a circulatory sphere organized by speculative capital (LiPuma & Lee 2006, 417). Risk in the form of a derivative therefore can be traded on a global scale in real time across any type of production. This is a highly profitable and highly powerful market. Since it is entirely removed from the actual business that the firms were in, all these people do is trade shares and this is where the real structural power of finance lies, in the trade of shares not in the owning and value increase of shares (Crouch 2011). This market of risk trading was allowed to develop because of the moral hazard within the regulatory institutions and the ineffectual regulation of national governments.

An example of moral hazard is provided by Strange's analysis of the major global accounting firms. At the time of Strange's (1988) analysis, six accounting firms controlled the financial reporting of FTSE 100 (96%) and FORBES (98%) companies. There now remain only four (Price Waterhouse

Coopers (PWC), Deloitte Touche Thomatsu, Ernst & Young, KPMG), as two of the big six firms merged to become Price Waterhouse Coopers and Arthur Anderson collapsed after the Enron scandal in 2002 (Eisenberg and Macey, 2004). Arthur Anderson which was found to be complicit in the illicit and fraudulent accounting practices of Enron (Eisenberg and Macey, 2004) puts into question not just the independent nature of these accounting firms from the companies they audit. The fact that there are only four companies doing these audits also pulls into question the *competition aspect* for better quality reporting but also the very ability and incentives to *produce* good quality reporting. Finally, these audit firms and their clients are so big that smaller audit firms could not conduct an audit in a timely and accurate manner, even if they were commissioned to do so leaving it by fiat for the big four to do (Strange 1988).

Another good example for a situation of moral hazard created by these lax regulations are the three American international rating agencies -Moodys, Fitch and Standard and Poors (S&P)- that hold an oligopolistic position within the world market (Mathis, McAndrews and Rochet 2009) evaluating and controlling the international performance of credit. For this service, these agencies are being paid by the financial institutes they are supposed to control (Mathis, McAndrews and Rochet 2009). Thus, they not only propagate a US influenced style of financial management and regulation virtually unchecked, but also introduce a significant amount of moral hazard into the financial system.

This moral hazard was the reason why there was such a high amount of speculation on risk that it was undervalued (Goodhart 2008). Due to the pooling of different debts with different risk grades, an adequate risk assessment of the newly created basket of pooled loans becomes increasingly imprecise which leads to an undervaluation and mispricing of traded risk. Mispricing was one of a number of different reasons why this financial crisis was different to other crises.

This continuous undervaluation of risk and the on-going liberalization of the credit market allowed for further development in many sectors directly related to the financial structure, the most important being the almost complete technological revolution that swept through the financial industry (LiPuma and Lee 2005).

The technological revolution and the mispricing of risk caused an increasing development of financial derivatives and derivatives trading, which have become the principal instruments of speculative capital uses in the global marketplace (LiPuma & Lee 2005). The expansion and the variety of these financial derivatives are "only limited by the imagination of financial engineers" (Hull 2006, 175).

It is this combination of liberalisation and the reconceptualization of risk due to its mispricing and technological evolution, which has helped redefine the financial sector as a whole. There is significant discussion about the possibility that the on-going evolution of "finance capital may remake the world in its own image" (LiPuma & Lee 2006, 405; Sassen 2008; Comaroff &Comaroff 2000; Harvey 2005, 2006). Technology is the final ingredient within this culture of moral hazard within the financial crisis. It contributed to the crisis by providing the illusion of infallibility to the traders, who relied blindly on these financial instruments.

> Production's most important product is fast becoming the production of connectivity - the logistics, communication networks, financial instruments and technologies used to aid amplify connectivity (LiPuma & Lee 2005, 407).

Goodhart (2008) identified three major reasons for this mispricing and its consequent increase in speculation. *Low interest* rates throughout the start of the new millennium causing a steady flow of capital from low return destinations such as savings accounts to higher returns destinations such as the stock markets. These low interest rates were combined with *a stable and growing economy*, throughout the 90s and early 2000s. A final important issue is *the assumption by financial institutes that the Federal Reserve will intervene* in case of a widespread financial downturn also termed the “Greenspan Put” (Goodhart 2008, 332). Goodhart does mention the moral hazard created by the deregulation and lack of independence of the control institutes, which I consider to be an important factor in the miss pricing of risk that occurred. The fact that there is no effective separation between the market and its regulators or any kind of final national oversight is in my view a considerable failure, which the market promptly exploited, eventually culminating in the 2007-2008 financial collapse.

3.3 Conclusions form theory

The neo-liberal economic theory investigated above and in Chapter 2 argues that its internal logics are by themselves enough to discipline markets. The many instances of moral hazard demonstrate that this is not so. Self-regulation rather represents forms of moral hazard *especially* in neo-liberal economic theory, creating a unidirectional management of wealth, as financial firms are liable to make enormous profits out of these crises (Strange 1988, Crouch 2011). While Strange openly argued that governmental regulation will always be behind current financial practices (Strange 1997, 86, 1998, 26), Strange's (1997) argument was that governments and international organizations needed to at least establish a *sense* of rule, which financial speculators should adhere to while more broadly applicable rules of conduct were being developed in order to replace the loss of authority of state within financial regulation. These rules of conduct or other forms of restructuring of the financial sector are crucial, as finance is an integral and possibly dominant part of the capitalist and state power structure (Johnson 2010).

As was argued above, deregulation also increases volatility within the market, which, as Strange and other theorists argued, would eventually lead to a collapse of the financial sector. Strange (1997) highlighted different proposals, which in her mind would best tackle the negative consequences of an international financial crisis. In accordance with her view that states could never adequately regulate their financial markets, the proposals by the Brandt Commission (1980), Williamson (1977) and Griffith-Jones and Lipton (1984) do not tackle the underlying problem of financial regulation; they merely try to limit the damages caused by a failure.

Strange (1997) was a supporter of the Brandt Commission’s (1980) proposals, which included an increase in resources and operations of international organizations and their financial independence from classical nation states (Bofinger *et al.*, 2010, EFSF 2014, ESM 2014). The Brandt Commission's proposal, also called for tighter controls of TNCs and reductions in arms sales and defence expenditures.

John Williamson (1977) proposed issuing large amounts of drawing rights thereby addressing the liquidity security issue of some indebted countries, which Williamson (1977) considered a more pressing concern than a country's solvency. The building of large reserves of liquidity would restore confidence in the currency, stabilize it, and consequently lift a country's credit-worthiness. The proposal by Griffith-Jones and Lipton (1984) argues for the necessity of having an international lender of last resort, which could step in to prevent a complete meltdown of the banking system. Considering the age of these proposals, one would be forgiven for thinking that these solutions are not applicable in the market environment of the current crisis.

Even though state regulation is running behind on financial development, some international financial regulation is still being implemented. The most substantive part of government regulation, which is currently enacted, is the Basel 2 Accords. The Basel 2 Accords (signed by all EU members in 2008) state that companies have to have an adequate solvency ratio, be supervised in their financial reporting and show market discipline when trading (Rochet & Décamps, 2004). Additionally to the Basel 2 Accords, the G20 held in Cannes in October, November 2011, has seen countries decide on much more stringent measures of financial regulation. These new measures require for example that the 29 biggest financial institutions (and shadow institutions such as hedge funds) recapitalize their accounts with an additional 1%-2.5% in order to avoid another global financial collapse (MMQ/REUTERS/DPA/DAPD 2011). The Basel 3 accords further increase the capital that banks need to hold in case of an emergency like a financial crisis. The Basel 3 accords also contain further rules on capital liquidity and leverage ratios, which are set to be completed by the EU in 2015 (Basel Committee on Banking Supervision 2014) These current proposals are similar to the proposals by Williamson (1977) and Lipton (1984) 30 and 20 years ago.

That being said, Crouch (2011) further complements Strange's arguments. While Strange argued that government regulation was always lagging behind the innovations created by the banks and financial institutes, Crouch argues that this lagging of regulation on the part of the state is related to the structural power relationship between the state and financial industries, which currently favours financial industries. Thus, Crouch (2011) sees the rate of success of the implementation and particularly the maintenance of the reregulation of the moral hazards was fraught with difficulty.

3.4. The start of the mess

Since the state has retreated from much of its regulatory and investigatory duties in the financial sector, the continued liberalization of the markets has been replaced by self-regulation and by control through other businesses. This in turn has created multiple instances of moral hazard within the financial system. The mispricing caused by moral hazard due to that retreat of the state, as well as the good economic development during the late 1990s and early 2000 nurtured a mood in the markets for a continuous increase in investment. This created a bubble in the financial market, which sooner or later was going to burst, with major negative consequences for the global economy and European welfare systems.

Some examples of other well-known bubbles that burst without state intervention in the market were: the Tulip Mania (1638), the Mississippi Bubble (1720), the South Sea Bubble (1720), the Bull Market Bubble The Great Depression (1929), the Japanese bubble economy (1989), the DOT Com bubble (2001) (MacKay 1856; Julian 2011, Crouch 2011). How bubbles occur and how they can be prevented is matter of a different academic as well as practical debate; there is a large consensus about how they grow. Bubbles grow because assets (be they financial or physical resources) are mispriced (Girdzijauskas, Streimikiene, Cepinskis, Moskaliova, Jurkonyte & Mackevieius 2009; see also Eatwell 2004; Froot & Obstfeld 1991; Garber 1990; Lei & Noussair & Plott, 2001; Smith & Suchanek & Williams 1988; Topol 1991; White, 2006).

The 2007/2008 financial crisis was just such a mispriced asset bubble. The practical consequences of this mispricing will be shown here. Lehman Brothers, a 158-year-old business, heavily active on Wall Street and a major player in the American banking market, officially declared bankruptcy on the 16th of September 2008 (*FT Reporters* 2008). This was the first major financial institution to default on its obligations, sending massive ripple effects through the US financial sector and eventually through the global financial sector and the global economy. This collapse prompted a run on capital as well as a long line of major and minor financial institutions around the world to turn to their governments for aid in settling their debts to avoid the same fate. Governments the world over, have acceded in many cases to those demands to save the system from total collapse. Northern Rock was the first bank in the United

Kingdom to be bailed out in September 2007 and nationalized in February 2008 (BBC 2009c).

This collapse, which sent significant shockwaves through the entire financial system, was the first of many consequences of this financial crisis for which the groundwork was laid long ago (see Strange above). This crisis got truly under way in the second half of 2007 with the collapse of the US housing bubble right on the heels of the collapse of the sub-prime mortgage market (Phillips & Yu 2011). This prompted a run to other asset classes such as commodities or bonds (preferably state bonds) perceived to be safer, which caused speculative bubbles to develop in these assets as well (Phillips & Yu 2011), further worsening the crisis and of particular consequence to Europe as will be shown in the next section.

Those bubbles burst, after investors began to realise the extent of the crisis the system was facing due to sub-prime speculations (Phillips & Yu, 2011) enabled by the hands-off attitude of the states discussed above. The volatility experienced in these markets had an infectious effect on other markets, most notably the currency trade (Melvin & Taylor 2009). It was this on-going volatility throughout the end of 2007 and reaching into 2008, which made investors nervous and caused them to try to move their assets out of high-risk investments. This volatility and insecurity culminated in an orderly collapse (aided by the Federal Reserve of New York) of the investment firm Bear Stearns in March 2008 (Melvin & Taylor 2009, 1321).

This collapse did not help to calm the markets or to stem the tide of the crisis; the crisis in fact continued to worsen. It worsened so much that it caused the collapse of another important American financial institute, Fannie May and Freddie Mac. Fanny May and Freddie Mac were two the giants of the American financial industry (henceforth referred to as F&F), which were Government Sponsored Enterprises (GSEs) tasked with a double mandate to provide low interest mortgages and support affordable housing but were also private companies whose duty lay in providing added value to their shareholders (Wallison & Calmoris 2009).

The F&F situation provides a good example of the problems that Susan Strange pointed out in the analysis above. These two companies were semi-private institutions whose liabilities were backed directly by the US Treasury. Their mission to provide low-cost housing also provided them with a lot of political good will and insurance against *overregulation*, which in turn allowed them to enter into and expand their market-share in the financial markets (Wallison & Calmoris 2009). This expanding market share in turn provided them with more political capital, allowing them to carry on their business as usual. It also created a moral hazard much bigger than the oligopolistic market situation of the rating and audit agencies. F&F's world stopped turning on the 6^{th} of September 2008 when they both had to be fully nationalised because they were no longer able to service their debt. Some estimates put the exposure of both firms at around one trillion dollars (Wallison & Calmoris 2009). Lehman Bros. one of the oldest and most prestigious Wall Street firms followed suit on September $16^{th;}$ Lehman Bros (LB) was not allowed (i.e. through non-intervention of the Federal Reserve and the US Treasury (Melvin & Taylor 2009) to default in an orderly fashion, as was Bear Stearns or F&F. This decision fuelled the fires of crisis even more.

The reason this default was so catastrophic was because of the way LB's speculation and financial trading was structured. For reasons of regulatory arbitrage, sub-prime mortgages were grouped together with prime mortgages in what is known as Mortgage Backed Securities (MBS) consisting of different packages of risk Class A (AAA rated risk) Class B or Mezzanine Level (Goodhart 2008) and Class C or Sub-mezzanine level risk and were traded on the financial market for substantial profit. However, banks needed to securitize those loans before they could distribute them to non-bank financial institutions (Goodhart 2008, 334) known as Structured Investment Vehicles (SIV). The way these MBS were layered and structured should have in principle have been safe from default.

Banks maintain more or less close links with these SIVs to whom they transferred these MBS in order to get them off their balance sheets. This allowed the banks to increase significantly their MBS trading, since technically the MBSs have left their balance sheet. However, since these liabilities only *technically* left the bank balance sheets, banks kept on increasing their leverage past levels that would otherwise be considered safe. Since these SIVs were essentially subsidiaries of banks, the parent banks were also their only way of accessing liquidity to pay out its investors. Liquidity to SIVs was provided by Asset-backed commercial paper (ABCP). Also needed for the proper working of these SIVs was a reasonable certainty that its debts could be paid if ABCPs are no longer able to raise cash for the SIV's. The parent banks that would provide the necessary cash to the institutes provided this guarantee. The closer these SIV's are to their parent banks, the stronger this insurance link is, requiring the parent banks to cover the shortfalls of the SIVs (Goodhart 2008; Melvin &Taylor 2009).

As the crisis in the housing market hit, and its repercussions were reverberating through the economy, investors started more and more frantically to try to get their money out of risky investments. ABCP's were no longer being sold or accepted. The consequent defaults of some of these SIVs have put their parent banks in the position of having to cover their debt. This brought their MBS products back onto their balance sheets, which now had lost a lot of their initial value. This return of valueless assets to their balance sheets amplified the losses of these banks as they added to their accumulated debt through overleveraging, leaving those banks with a limited stack of options. They could either declare bankruptcy or convince the government to step in and allow the banks and financial institutes to carry on with their business; history has shown that the second path was taken.

The option of bankruptcy was an unlikely outcome considering the number of non-decisions which governments have taken to allow the banks to become these centres of wealth creation. The fact that the state allowed the financial institutions to become such centres of wealth creation also caused the moral hazard described above that these acts of wealth creation were subject to. This caused an enormous concentration of wealth within only a very small circle of people. It also created a dependency of the state towards that wealth creation which leaves it with no choice but to make sure that the system remains intact (Crouch 2011).

This path of government intervention coupled with investor flight from riskier assets to “safer” assets such as state bonds would have severe repercussions on national economies and budgets and, most importantly, it would have severe effects on welfare.

> Governments have to make deep cuts of social services, health and education programmes, pension entitlements and social transfers to the poor and unemployed. They have to do this to satisfy the anxieties of the financial markets over the size of public debt, the operators in these markets being the very same people who benefited from the bank rescue, and who have already begun to pay themselves high bonuses- bonuses 'earned' because their operations have been guaranteed against risk by the government spending that created the public debt. (Crouch 2011, 118)

Although Soros does defend the liberal economic notion of the primacy of market decisions over state decisions, he concedes that this ability to react quickly due to their unregulated nature can also make them unstable.

> Markets should be given the greatest possible scope compatible with maintaining economic stability (Soros 2008, 143)

But he also did not absolve regulators of responsibility. The fact remains that if regulators do not comprehend a practice or a derivative then they should not allow it to be used. Furthermore, the regulation of these practices and derivatives should not be left to the financial institutes themselves, as it creates a moral hazard, which leads to the market failures, which could be observed in 2008. However, in order for regulators to be able to do their job, firms *must* provide them with all the information necessary even if that comes at a great cost to the firm (Soros 2008). In this last sentence, Soros demonstrates that his analysis does not take into account any type of structural power relation, and considers the state to have the primacy over the financial market. Strange (1988) and Crouch (2011) have shown that the structural power relations between the state and finance have changed with the application of neo-liberal economic concepts and that their relationship is fraught with moral hazard. Thus this relationship has helped create the crisis which Europe faced at the time.

3.5 The pressures are on …

The previous sections argued that the creation and the burst of this 2007/2008 financial bubble developed along similar lines as previous ones, i.e. through continuous deregulation caused by a retreat of the state out of regulatory and controlling duties. The difference to other bubble crises is that this was a contraction of the entire financial system and not just a part of it. This explains the size of this crisis, its reach and the consequences that stem from it, which are analysed in this section. The pressures put on the welfare state are a particularly important repercussion of this crisis.

As Susan Strange (1988) argued (see introduction), the financial structure has become the most important of the power structures in the international arena because, as was demonstrated in previous sections of this chapter, its ability to create wealth was almost completely unshackled. The analysis above showed that this had as a consequence a staggering increase in wealth for only a very small number of people as well as increasing instability within the financial system, which was fuelled by moral hazard.

What was overlooked at the time the financial system was liberalized were the political-economic repercussions of liberalised finance. Although finance itself is ruled by economic logics, it is still subject to *human* interpretation and the irrationalities that come with that interpretation as well as political action and the irrationalities that come with that. The states, in their attempt to save the system, continue to overlook or ignore the social aspect of finance demonstrated by the mounting pressures on welfare which have only increased with the continuing of the crisis, due to countries like Germany and France which, over time, have subscribed more and more to neo-liberal ideology in their economic policymaking.

The collapsing financial system created a number of pressures on the state, the most important of which was the pressure on welfare. The pressures, which are currently put on welfare, stem from the economic downturn, which automatically increases the number of people who are unemployed due to a contracting economy. Increased unemployment increases the draw on unemployment benefits. This also means that there are fewer people paying into welfare, which automatically puts further strain on the system. As was argued above, weakened economies create further draws on welfare, which in turn increases deficits and makes financial markets uneasy. The welfare system is designed to handle economic and financial crises over short periods of time.

However, as the crisis went on, the economic pressures did not ease off and more importantly, new pressures were added as is shown below. When the crisis reached its highpoint in 2008, there was a concerted global effort to avert the crisis through large-scale intervention in the marketplace by governments spending billions to stabilize the banking system (Propublica 2013). This left the countries with significant debt exposures, since they thought that action had to be taken against the bad debts of the banks. Once the banks were relieved of their debt exposures that are related to the financial bubble, governments needed to enact policies, which once again encouraged banks to start lending and engaging their business of trading those risks on the global market.

3.5.1 …non-Euro countries

In order to provide an effective analysis of the consequences of the financial crisis on the Euro Zone, considering its internal failures, it is necessary to demonstrate the abilities a state external to the EZ and its central bank have compared to the Euro Zone. These abilities are best demonstrated by the UK, which is not a member of the Euro Zone, but is a major European nation with its own independent currency.

Some measures that the UK took were similar to the ones undertaken by the Euro Zone. The neo-liberal ideology, which was investigated in Chapter 2 and used in the analysis of the financial crisis, was also used as a blueprint to restart economic growth in the UK.

Tax increases (VAT in particular), and public sector cuts (much more so than tax increases) became necessary from 2009 to 2013 -according to the Conservative British Chancellor- for long-term economic growth (BBC 2009b). This argument follows precisely the argument made within the previous section as well as the previous chapter. The first budget by Conservative Chancellor George Osborne was a testament to the Conservative election promises, with large budget cuts in the government benefit schemes as well as VAT and tax increases. This was in order to reduce the public deficit to more sustainable levels by 2015-16 and further reductions in public borrowing until 2020 (Hoban 2010).

A measure that was considered by non-Euro countries such as the UK in 2009 was quantitative easing. It was hoped that an increased money supply in the economy would give production a boost and engage banks to lend to each other again thereby stimulating economic output (BBC 2009a). The increased money supply has also an effect on the value of the currency. Greater amounts of money in circulation means the value of the money is lower thereby making goods cheaper in terms of exports, providing a further boost to production. A further advantage of currency devaluation is that the national debt, which is held in the national currency, also becomes less in terms of its value.

3.5.2 …Euro Countries

The European response was different to the UK because, the setup of the EZ, has the economic and monetary tools available (to solve the crisis) split between the Member States and the ECB (DeGrauwe 2013). The individual governments of the Euro Zone are no longer in charge of their monetary policy; that task has been delegated to the ECB with the introduction of the Euro. Hence the ECB coordinates the EU monetary policy for the whole Euro zone area without favouring a particular state. This setup is in large part due to French insistence to limit the power of the Bundesbank (GCB), which up to the start of the Euro had set European monetary policy since many European currencies were pegged against the Deutsche Mark (DM). Germany agreed to French demands but insisted on modelling the ECB operating principles along those of the Bundesbank (GCB) principles of low inflation and national independence (DeGrauwe 2013).

The consequence of this was that the countries affected by the financial crisis were left with a reduced choice of macro-economic tools. Governments could finance their economies through increased tax revenue, a positive Balance of Payments (BoP) sheet, increased Foreign Direct Investment (FDI) or by increasing public debt, or by reducing public spending. Either version or combinations of the four were implemented by every Euro zone country with varying degrees of success and impacts on their economies (Dizard 2008).

An added problem of the Euro Zone is that due to their unique setup the financial crisis also exposed it to speculation about its continued existence (see Hesse 2012), speculation which is encouraged within the neo-liberal economic setup which gives power to traders (Crouch 2011) thriving within a system fraught with moral hazard. This caused further stresses on their finances, since refinancing their debts became more expensive leaving countries with ever fewer tools to spur growth within their countries and leaving the EU with a worsening crisis.

The economies of Portugal, Ireland, Italy, Greece and Spain (PIIGS) were hit hardest by the financial crisis. With varying causes being at the root of their economic woes (Authers 2012), the consequences were the same across all countries. These countries were no longer able to attract or hold on to FDI within their countries because the crisis in their banking sectors and the bank bailouts made those countries ever less attractive for investment. This turned their balance of payments sheet negative and increased their public debt and also increased their GDP to Debt ratio from previous sustainable Maastricht Criteria levels (60% of GDP) to much larger and unsustainable levels (ECB 2012). These actions and the increased debt ratio sucked these countries into a downward spiral of debt, causing an increasing inability of these countries to refinance those debts on the international markets thereby creating a possibility of sovereign default since investors were losing confidence that these countries could honour that debt.

The heavy current debt of the PIIGS and their projected future budget deficits enticed speculation about the possible breakup of the Euro and a reversion to pre-Euro national currencies to prevent an increase in refinancing costs. The legal, and most importantly, the political and economic ramifications of a departure of a nation form the Euro framework would be of a different magnitude. Although the consequences are hard to project since this case has never occurred, any such move could open the floodgates on currency speculations of not only the Euro but also the national currencies, making an already fragile recovery even more fragile, even causing another recession.

This fuelled further speculation on national bond yields for those countries (Dizard 2008), further worsening the crisis. These increased stresses led the major credit rating agencies (Fitch, Moodys and S&P) to downgrade these countries and in many cases put on negative watch, an action, which put further oil on the fire. This confluence of events created a situation where a European solution was not only required, but had become unavoidable.

Sovereign default, although not a common occurrence, has happened many times over the years. In the euro zone, a default becomes a wholly different problem. Every member country economy is tied to the Euro and to the other economies in the Euro zone. This shared currency denies countries the macroeconomic tool of currency management. Countries therefore can no longer try to avoid a default by printing more money and thereby devaluating their currency and their debt. The authority over printing money and monetary policy rests with the ECB and is set by it for all 27 Euro members.

Since the responsibility of the ECB is to keep inflation low, and it is therefore prevented from measures that would make it rise, which would help indebted countries with paying down their debt. The options left to these EZ countries are to pay down their debt on their own, leave the EURO and revert to their own currency and start printing money or finally default. Although in theory this sounds like a compelling argument for these countries, the reality is quite different.

To avoid any scenario that would have to deal with such an eventuality, the European Commission, ECB and the IMF have agreed to aid packages to these countries (chief among which is Greece) in return for stringent demands on deficit reduction. These demands do not leave these countries with much room (if any) to manoeuvre except to force drastic and deep entitlement cuts upon unwilling populations, worsening the recessions as people need to survive with much less income and fewer services than before (Hope and Oakley 2014), causing private defaults or reduced consumption.

3.5.3 …welfare

Since these problems required a European solution, the European Financial Stability Facility (EFSF) was established in June of 2010 (*dpa & Reuters* 2010) and its successor the European Stability Mechanism (ESM), was established at the start of October 2012 (Endres and Faigle 2011). These rescue funds are supposed to help embattled European states from defaulting on their debts. The EFSF and the ESM were established in order to stabilize the financial speculation on the Euro by providing a large buffer of reserve currency. This buffer would allow the EU to provide vulnerable governments with funding; however these mechanisms are offered in exchange for public spending reforms i.e. austerity to prevent further contamination of the Euro zone as well as to stop speculations on sovereign default (Timbeau 2013). This is a quite consequential change within European politics and for European welfare. The establishment of the ESM in essence means an abandonment of national budgetary sovereignty, particularly for the nations under the ESM since their national budgets are financed to some extent by the ESM. Therefore, in order to receive funding and avoid default, these countries have to comply with the budgetary prescriptions of the European Council of the Eurogroup, which are enforced by the Troika of EU Commission, IMF and ECB. The country with the greatest influence within the ESM and the Troika is Germany as its greatest contributor, before France and the Benelux countries (Endres and Faigle 2011). The ESM funding comes with its heavy austerity prescriptions, which tend to focus on the reduction of government services, in accordance to neo-liberal doctrine.

This re-conception of national budgetary sovereignty however also goes beyond the countries directly affected by it. The ESM also changes the budgetary decisions of other countries, which want to avoid to being placed under the austerity prescriptions of the Troika. The “Six-Pack” rules and the “Treaty on Stability Coordination and Governance” complete the new financial framework within which all EZ member countries have to work within as well as those who whish to join the EZ at some point.

Hence the chief contributor countries to the ESM like Germany and to lesser extent France have the ability to influence, to a much greater extent than at any other time, the budgetary priorities of other EU countries by exercising their structural powers through the Troika, the ESM and other European institutions.

The establishment of the EFSF and ESM and the economic requirements that were attached to it, were the result of a political-economic necessity and were nowhere particularly popular. The German government, the ruling CDU/CSU in particular, suffered a heavy political backlash, which came remarkably from *within* the ranks of the ruling CDU/CSU where party members challenged the constitutionality of the EFSF and ESM (BVerfG 2012). Their challenge failed since the German Constitutional Court (BVerfG) declared the EFSF and the ESM as constitutional on the 12.09.2012 only limiting the German contributions to the stability mechanisms (BVerfG, 2012). This backlash is remarkable since it signals that Chancellor Angela Merkel did not have the full backing of her own party when she decided to embark upon this project. This backlash would also go some way to explain why Chancellor Merkel holds on to the austerity course so determinedly.

The CDU/CSU is well aware of the economic burdens of helping a country out of debt (see the history of German reunification that was accomplished by the CDU/CSU and Helmut Kohl). The CDU/CSU saw itself paying again for other people’s mistakes (participation of Germany in the EFSF is the largest of all Euro-Members (Endres and Faigle 2011)) without enough assurances that the measures imposed on the countries will be adhered to. The fears grew so high within the party and outside, that calls, especially in Bavaria, grew louder for an end to the German involvement in the ESM. The Bavarian “Freien

Wähler" campaigned heavily against any further involvement in the ESM. Their party leader, the grandson of Konrad Adenauer (first West-German chancellor), has used that issue to campaign for a seat in the Bundestag (Fischhaber 2012) for which elections were held in October 2013. The French government also resisted the course of the "austerity focused Germans", though the French Government did agree that some austerity measures need to be implemented.

3.6 The tradition of the state; Germany and France

As was previously argued, the German and French states are central components of European Union development and evolution. This evolution stems from a negotiated consensus developed out of two different conceptions of the state, therefore the conceptions will be analysed here. This analysis will also be helpful in determining which state conception has had greater influence on the development of these actions.

Whereas the French government favoured a centrally controlled EU, Germany favoured a federal system (Reuters 2010). This cultural attitude is also reflected within their state conception. However Germany and France also share a number of common understandings.

> There is above all, an abhorrence of inconsistency and a passion for synthesis and systematization (Dyson 2009, 158).

This would explain why the French and German governments continue their cooperation with each other on the topic of the European financial and economic crisis, although both countries are openly at odds when it comes to the implementation of ways to resolve it.

What differentiates both countries are their religious influences. Whereas Germany has a more Protestant heritage (see also Weber 2002), putting stock into the belief of emancipation of individuals (Dyson 2009, 158), France on the other hand is a much more Catholic influenced country where individualism is often related to selfishness and to the submission to a central authority.

The French governments from de Gaulle to Chirac did not believe in smaller government but historically saw government as a paramount piece of a well-regulated society and economy. It was only under President Sarkozy that the French government's attitude changed and France began to embrace a small government oriented stance, like that of the governments of the reunited

Germany beginning with the Schröder governments and leading into the Merkel governments (Lhaïk 2010).

With the election of François Hollande to the French presidency, this stance has once more changed as France has tried to take up the mantle of providing a different perspective on resolving the current European crisis other than using austerity to do it. The French and German state traditions on the subject of the manner in which this crisis should be resolved are also divergent. The German concept of the state is a remote and self-limiting authority imposing and implementing laws in such a way as to allow people a maximum amount of freedom to find what is best for themselves. The expansion of the SGP with the six-pack and two-pack rules as well as the establishment of the ESM with conditions is an example of those principles. The French concept of the state favours a more paternalistic approach where the state can help shape and guide society. This is exemplified in the French *dirigiste* model (see Chapter 6) and the return to the argument of European investment within industry.

The reason, however, that the German government has more success with its approach is due to the close fit between the basic German principles of the state and the neo-liberal economic agenda. The German concept of the state providing fertile ground for the neo-liberal economic concept to develop.

Considering these divergences, French and German governments are agreed in principle on the methods necessary to ensure the success of the EFSF and the reduction of public deficits of Euro countries (dpa/Reuters 2010). Another reason for this close if not always agreed co-operation between France and Germany is their agreement that the Euro will and must survive this crisis (AFP 2011b).

3.7 The European way of managing the financial sector

The 2007/2008 financial crisis caused a number of significant challenges to Europe and the Euro Zone. Not only did it cause a contraction of the European Economy, it also brought into question the solvency of states and the sustainability of “high” levels of debt. As this chapter demonstrated, financial crisis, low economic performance and high levels of national debt are intimately linked to welfare and to the ability of the state to provide it. As was demonstrated in point 3.3 a number of older concepts, designed to keep finance in check were being reconsidered on the international level. The EU and the EZ went even further in their attempts to defuse the crisis potential of the financial market. The EU and the EZ introduced four concrete measures to combat the economic downturn and rebuild financial confidence.

Before any of these new measures were introduced the “Stability and Growth Pact” was designed to ensure the stability of the Euro currency. Since this pact was not consistently applied (see Germany and France breach Maastricht criteria (Feldman 2003)) further rules needed to be established to strengthen the pact.

The first measure that is considered here is the European Financial Stability Facility (see EFSF framework agreement 2010) which was later transformed into the European Stability Mechanism (ESM). Both of these programmes implemented the principle of increasing currency availability so that countries, if they could no longer get new liquidity from the markets because of increased interest payments, they could still get liquidity from the EFSF while they were getting their finances in order and return to the capital markets (Bofinger *et al.*, 2010 and EFSF 2014, ESM 2014).

To deal adequately with these problems, and avoid for EZ countries to even having to require ESM aid, the EU has also instituted in 2011 a “six-pack” of rules strengthening the “Stability and Growth Pact”. The six-pack of rules included the institution of stricter regulations and macro-economic financial controls, which applies to all EU member countries except the UK. These rules demand that a country should not overstep a debt limit of 60% of GDP in addition to the limit of 3% of GDP increase of annual sovereign debt. Should a Euro member country be in breach of one or both of these provisions, an Excessive Deficit Procedure (EDP) will be implemented, to force the country to adhere to these rules or make efforts to adhere to them in the near future (European Commission 2013).

A third measure was the institution of the Treaty on Stability, Coordination and Governance (TSCG). This was another measure designed to run alongside the Growth and Stability Pact and the Six-Pack. The TSCG applies to all Euro Zone members and will apply to any EU member state which will join the Euro Zone. Non-EZ members have the option to apply TSCG rules but they are not required to do so. Its supervision and enforcement capacities are even larger than the one of the Six-Pack. The TSCG rules require national debt limits in terms of GDP to be integrated within the constitution of a country. The treaty also allows the ECJ to implement fines if they refuse to do so (European Commission 2013).

The institutions of the EFSF and the ESM and the “Six-Pack” rules and the TSCG were aimed at regulating national budgets. In terms of banking regulation, further safeguards were established in the form of a Banking Union. This regulation of national debt and re-indebtment was designed to avoid new attacks on the solvency of states and by extension reduce the threat of the Euro’s collapse.

The term Banking Union combines a number of different rules, regulations and institutions, which the EU and the EZ have decided to institute, to reduce the crisis potential of the banks (European Commission 2012b) (European Commission 2014a).

Banking union regroups under its auspices a single supervision mechanism, a single resolution mechanism and a single rulebook (European Commission 2014b). The single supervisory mechanism (SSM) provides the ECB with the authority to directly supervise the workings of any of the Banks of the participating countries. The ECB will directly monitor the three largest banks in each participating member country while the national central banks together with national supervision authorities will supervise all the other banks within the country (European Commission 2014a).

The single rulebook provides a common set of banking rules across all Euro Zone member states and all other participating sates. One of the biggest points implemented by the single rulebook is the operationalisation of the Basel 3 regulations investigated above as well as new banking rules and transparency of trading. To aid the different countries in their adaption of their banking rules to the ones set out in the single rulebook the European Banking Authority (EBA) was established (European Commission 2014a).

The quite severe case of Greek sovereign debt and its risk of sovereign default bring into the public discussion the necessity of international bankruptcy law and an international bankruptcy court (Hilgers 2003) *to prevent excesses* (Soros 2008, 142). The single resolution mechanism is the European answer to this problem, by providing a single set of rules, through which, failing banks can either be restructured or go bankrupt in an orderly fashion and in a way that doesn’t put the burden on taxpayer but rather on the private sector.

Another proposal, which has seen a recent resurgence within discussions at the European level, is the proposal by Griffith-Jones and Lipton (1984). They argue for the necessity of having an international lender of last resort. This role is still quite limited and still faces significant opposition regionally in Europe, especially from Germany, mostly because the competences of the ECB are not exactly defined within this area (DeGrauwe 2013, Schadler 2012). The Federal Reserve Bank (Fed) in the USA has already taken on this role, and the European Central Bank (ECB) has followed suit - though grudgingly and within a limited scope until the ECB's competencies within this area have been clarified and agreed upon (Frieda 2012; Schadler 2012; Wolf 2012), especially in terms of the ECB buying Greek debt.

All of these new measures, particularly the ones implemented by the EU, show a commitment to greater fiscal responsibility on the part of the national governments, providing a definite frame of reference for the countries to do business in. This is a clear demonstration of the structural power of the EU as a governing body and the structural power of Germany (achieved due to the close fit between the German state concept and the neo-liberal economic concept) as member of that body. It remains to be seen if the European Union's or the member state's structural power will prevail against the power of the financial institutions and the international business community. Considering that both those organisations managed to get regulation reduced and the fact that the national states are dependent upon the financial benefits the previous system has provided them, one should be cautious to consider these rules to provide a lasting solution (see also Crouch 2011).

While the austerity argument still faces criticism and pushback within the Euro Zone and increasingly from business and academia (see Krugman 2012), there have been some positive results in 2014. Ireland (SIR/dpa 2013), Portugal (Coelho 2014), and Spain (ESM 2014), have all left the ESM rescue fund in 2014. Unemployment data from Spain shows a marked drop in unemployment for the second quarter of 2014. The Spanish economy created almost half a million new jobs (402,500) in the second quarter. This is a very big achievement and a demonstration that the Spanish economy has moved to a more solid footing, a point which is further underlined by its ability to leave the ESM and start paying back its loans early (ESM 2014). However, even with this marked drop, unemployment remains high in Spain, and, according to Focus

Economics (2014), the level of unemployment for 2014 is expected to remain at 25%. If the unemployment rate continues to remain at 25% for 2014, it would be further evidence that a focus on austerity without some form of investment is counterproductive and does not allow for countries to achieve economic growth of the type necessary to permanently reduce unemployment and thus increase tax incomes. The reduction in unemployment did show that application of austerity with the help of the ESM did allow the country to make changes to its economy and make it more competitive for the future.

3.8 Conclusion

This chapter argued that there was a retreat of the state in terms of financial regulation and control, which had as a consequence a change in the state’s ability to provide welfare. This chapter analysed the continued change of the financial structure towards a neo-liberal concept of deregulation and reduced state interference since the end of Bretton Woods.

This analysis used the work of Susan Strange whose analysis of the structural power of state-market relations was the best suited for this analysis. She concluded that the retreat of the state changed the power relationship between the state and the market to such an extent that structural power now resides with the market and not with the state. This is a result of the neo-liberal reforms that were enacted within the financial sector since the end of Bretton Woods, which neo-liberal theory (as pointed out in Chapter 2) sees as essential for market growth and an efficient running of the market.

The analysis of the deregulations and the change of structural power towards the financial structure formed the first section of this chapter. This section demonstrated that a retreat of the state did cause an increase in wealth for financial institutes but at the same time, it also created its own internal inconsistencies, responsible for the eventual (near) collapse of the financial system.

The second part of this chapter looked at the consequences of those changes in terms of the moral hazard that this liberalisation of the financial market created. It further analysed the consequences of this moral hazard, which it argued was a contributing factor in the 2007/2008 financial crisis, the repercussions of which caused Euro Zone states to redefine its duties towards welfare and reconsider its welfare provisions.

The retreat of the state from its regulatory and investigatory duties was followed by a quick and large expansion of the financial market, financial services and of financial assets. This expansion was no longer managed externally by the state, but internally either by the financial institutes or by external audit companies that the financial institutions paid for their evaluation. This internalisation of its own surveillance caused the moral hazard, which would eventually lead to the 2007-2008 financial crisis and the changes to welfare.

The moral hazard in the financial sector created mispricing of speculative assets, which created speculative bubbles that burst in 2007. The mispriced risk and the expanded financial trading through the financial instruments created to deal in this risk overleveraged the banks using over and above sustainable levels, causing their bankruptcy. The consequences of these bubble bursts and the bankruptcies had profound effects on Europe and the Euro Zone.

From the consequences of the deregulation followed the particular consequences for the Euro Zone. The consequences for the Euro Zone relate to the fractured nature of the financial and economic responsibilities within the Euro Zone as well as the fractured nature of the Euro Zone country performance throughout the crisis. Bond yields were increased on some Euro Zone countries because their debt levels rose at a pace that worried investors who demanded higher yields on their bond purchases, further worsening the debt problems of these countries. The countries were weakened to such an extent that a common solution to the problem was the only possible alternative, to end the debt spiral and the speculations on sovereign debt.

Before looking at the consensus the EU drew from this, this thesis analysed the concept of the state on a national level to understand how this response to the crisis was developed. The EFSF and the ESM were created to guard against the effects of speculation. These funds established a financing mechanism for countries to have access to fresh funds if they could not get them on the financial markets. These funds were linked to neo-liberal austerity conditions (such as public sector reform) which countries had to fulfil to receive the money.

The funds of the EFSF and the ESM were supplemented by new European budget rules and regulations such as the Single Supervisory Mechanism (SSM) and the Treaty on Stability, Coordination and Governance (TSCG). The SSM was designed to implement the new Basel 3 rules on bank liquidity. The TSCG on the other hand was designed to complement and reinforce the existing financial regulation established with the development of the Euro. All of these regulatory frameworks were designed to keep national deficits and borrowing at sustainable levels, so that countries would not again get into a position where they would have to come under the protection of the ESM. In addition the Single Resolution Mechanism the Single Deposit Protection and the Banking union (which form part of the SSM), were designed to reregulate banking activities in order to avoid payment shortages due to insufficient liquidity of the banks.

These conditions were elaborated by the European Council of the Eurogroup and IMF of whom France and Germany were significant members and enforced by the Troika of ECB, European Commission, and IMF allotting them a lot of influence in the elaboration of these prescriptions both countries tried to put forward their own view of welfare reform. The power of Germany and France and their different understandings of welfare will be analysed more closely in the following chapters.

Chapter 4 Social Security the German Way

4.1 Introduction

This chapter analyses what happens when a government reinterprets the role of the state within the political-economic makeup of a country; particularly its role in the provision of social security, including its understanding of welfare, in response to the application of structural power of a global neo-liberal economic concept through international organisations.

In this chapter, the case of Germany is analysed. This chapter examines how the newly elected centre left SPD/Green 1998 German government, with an eye towards adapting the German economy to the demands of the globalised free market (and its intermediaries), redefined the state's role to be in the provision of social welfare as agreed upon within the Maastricht Treaty (1992) and the ESM (2013). This chapter also considers how this redefinition of welfare evolved over time, which institutions were involved in shaping that definition as well as how much of this definition was transformed into law.

Shortly after their election to the Bundestag in 1998, the SPD/Green coalition set about to undertake the most substantial reform of the German social security model since its establishment by Bismarck. The ruling coalition and the media dubbed the ensuing legislation the "agenda 2010" (Blum 2008). The "agenda 2010" is an umbrella term used to describe a number of reforms to the pension, health, unemployment and accident insurance schemes as well as education reform and other social reforms, such as family policy and labour market policies. This agenda 2010 reform was the end result of different national and supranational pressures to enact structural reforms in the German economy as well as an internal reconceptualising of the political-economic setup and duties by German industry, banks and the German state.

This analysis demonstrates that the 1998 elected SPD/Green government reversed the original position of the German state on social security and economic management. The evolution of the idea of the state as an active participant and carer of society, (see Chapter 2) demonstrated that the most important development in the provision of welfare came about with the advent of industrialization. It was during that period that the state redefined its *raison d'être* by making welfare provision a substantial part of its responsibility; the state thus became a socio-political-economic entity. This analysis will help in understanding the German state’s reasoning as well as the pressures to which it was exposed, leading to the state’s withdrawal from those political-economic positions of social care and market influence. Its move towards a smaller state with more market freedom and individual empowerment could be considered as a continuation of the trend of economic and particularly financial liberalisation on the national level, which Susan Strange analysed on the international level in her research (see Chapter 3). The manner in which the German state has gone about changing the welfare provisions within Germany also show the increased power of industry within the determination of the state welfare provisions, which in turn shows the changed power relations between the state and the global market. It also shows the philosophical overlap the German state tradition has with the neo-liberal economic concept used.

The implementation of the German welfare reforms has changed the state’s conception of its role within welfare provision. This re-conception had positive effects on the German unemployment rate and made the labour market more attractive for firms as well as making firms themselves more profitable. This re-conception also had positive effects on the German economy and the German budget (see Chapter 5), which is why the German government has firmly embraced austerity conceptions on the European level. This analysis will therefore also help in understanding the German support for austerity demands for countries applying for protection under the ESM framework thereby expanding upon the work done in Chapter 3.

In order to provide a clear overview of the evolution of the German position, this analysis first investigates the legislative structure of the German welfare law; knowing the constitutional and legal framework is important to understanding how these reforms were implemented.

Secondly, this chapter will conduct an analysis of the German business model before the implementation of the Agenda 2010 reforms in order to better understand the significance of the Agenda 2010 changes and the extent to which those changes have caused a paradigm shift in the understanding of the concept of the state as a provider of welfare and as a member of the political-economic framework of the nation. It furthermore investigates the circumstances which allowed such a substantial change of concept to be implemented.

The third section of this chapter will lead on from this investigation of the circumstances that put pressure on Germany to reform its socio-political-economic structure. The third section will investigate how the redefined concept of welfare, which evolved from the early proposals by the SPD, was first transformed into a commission report to then be implemented within German law under the name of "Hartz" laws and how those reforms changed the power structure regulating the relationship between the state and the market.

Finally, this chapter will investigate the extent of these changes through a critique of the reforms from both the left and right spectrum of Germany experts. This will not only provide an overview of the size of the reductions in the state involvement within the provision of welfare and the potential social consequences thereof.

4.2 Soziales Gesetzbuch (SGB)

Before going into an in-depth analysis of the new social agenda, we need an analysis of the legal points that allowed such an extensive reshaping of the social contract to take place. The points introduced here form the legal basis and regulations of welfare within Germany. It is important to note that these regulations form part of the German general legal code and is not enshrined within the constitution as is the case in France (see Chapter 6). This fact greatly simplifies the process of changing these laws.

The social contract, defined as a duty to provide care for its population, as analysed in Chapter 2, is laid out differently within Germany. The German constitution "Grund Gesetz" (GG) (own translation) is not explicit about the sort of care that needs to be provided by the state. The duty and the right to welfare are inferred within the German constitution in the Articles 20 and 28 of the GG. These articles provide the basis of the German welfare concept. They are framed by other constitutional articles i.e. Articles 2, 9, 11, 12 and 14 (Bundesministerium der Justizt und für Verbraucherschutz 1949), which effectively prohibit a centrally planned economy. Also significant are Articles 14, 15, 20 and 28 (Bundesministerium der Justizt und für Verbraucherschutz 1949): they provide an argument for the duty of care by the state for its population in terms of welfare provision and in terms of industrial regulation (Lampert 1992). These "vague" positions in the German constitution according to the BverG only determine that the government cannot remain a neutral arbiter between society and the market but needs to actively engage with both the market and society in the way the state sees fit but, which is in line with the articles enumerated above (Lampert 1992, 98).

In order to allow the State to intervene within society and the market, it needs a legal framework within which it can do so. Since the GG does not contain specific articles on social security, the “Soziales Gesetz Buch” (SGB) (the Social Code, own translation) takes on those duties. However, the SGB does not benefit from special constitutional protections and hence, changes to the SBG can be made by normal parliamentary procedures. This however means that any of the twelve SGB books (§ SGB I 2014, §SGB II 2014, §SGB III 2014, §SGB IV 2014, §SGB V 2014, §SGB VI 2014, §SGB VII 2014, §SGB VIII 2014, §SGB IX 2014, §SGB X 2014, §SGB XI 2014, § SGB XII 2014, Wasmund 2013) can be reduced or expanded as the government sees fit.

> § 1 Tasks of the Social Code
> (1) The law of the Social Code shall aim at helping to achieve social justice and to shape social and educational aids. It should help:
> - to secure a humane lifestyle
> - achieve equal opportunities for the free development of individual personalities, especially for younger people, and to protect and promote the family
> - the acquisition of livelihood through a freely chosen employment and to help avert or compensate for special (great) burdens of life, by helping the individuals to help themselves.
> (Wasmund 2013) (own translation)
>
> (2) The law of the SGB is also intended to aid in the fulfilment of the tasks as set out in paragraph 1, by making sure that essential social services and timely and adequate facilities are available. (Wasmund 2013) (own translation)

This wording provides the state with only a very general framework of social responsibilities. Though interpretations of the exact meaning of the text vary, the formulation, because of its vagueness, provides the state with a lot of leeway on the action or inaction it chooses to take in its provision of welfare. This vagueness provides two further advantages to the legislator.

On the one hand, §1 of the SGB falls within the wording of the German constitution allowing for legal implementation of social security laws to be passed by parliament and enacted on a national scale (triumph of the federal (Bund) over the individual (Länder) German States), though the principles of §1 are not reproduced within the constitution (Lilge 2012). This makes social security in Germany an entitlement framed within the guidelines of §1 *backed by the constitution*. This entitlement is however not legally binding, i.e. the constitution does not directly specify a right to social security (Lilge 2012). This is problematic because it leaves legislation of social security, which has severe generational impacts, subject to short-term law making (Ligle 2012). This is especially problematic if one considers that Germany plays host to an ever-aging population. Laws passed for short-term economic benefit will eventually have significant bearings on the quality of life of older generations.

On the other hand, the vagueness of §1 allows for a more or less generous understanding of the provisions of social security, which allow Germany to adapt more quickly and more easily to changes in the international markets and their international power structure if it chooses to do so. It was these vague guidelines that made the rapid implementation of the "Agenda 2010" legislation possible (Ligle 2012).

4.3 The German Business model before Agenda 2010

In the "pre-Agenda 2010" definition of the social security framework, the aid provided to the population was considered more of an increase or an addition to the "self-help" performed by the population at work or trying to find work. The previous German socio-economic model (Rhineland capitalism, Dyson 2002, 174) shared some common traits with the French dirigiste model (analysed in Chapter 6), in the sense that in Germany as in France, government involvement within the economy and particularly within industry was much greater and employee involvement within the company was also a lot stronger. As the "pre-Agenda 2010" definition was much more integrated within the economic life of the country, the welfare model of Germany combined with the managed economy of the German "bank-industry nexus" (Dyson and Wilks 1983; Esser, Fach and Dyson 1983; Dyson 2002) allowed the German economy to grow and develop throughout the post WW2 years up until the 1980s when the classical nation-centric economic theories like Keynesianism were being rapidly replaced by a global neo-liberal economic concept.

The Agenda 2010 definition of welfare and economic cooperation was modelled along such a neo-liberal economic concept, which in Germany is called *ordoliberalism* (Dyson 2002, 174) this concept was much more globally oriented: i.e. the ordoliberal economic concept attempted to make all aspects of the German economy able to compete internationally; the results of these efforts culminated in the establishment of the Hartz laws analysed below. Generally speaking, this economic concept and the subsequent reforms which it has spawned, has moved the German welfare provision more toward a *quid pro quo* arrangement where people are provided with social security benefits in return for working or trying to find work (Ligle 2012).

Due to this spread of neo-liberal economic concepts on a global scale, banks and particularly industries in Germany have become much more dependent on international markets and the evolutions on international markets. The state itself has also come under much higher pressure by international institutions, with increased structural powers, the EU in particular since the signature of the Maastricht Treaty and the agreement on the ESM, to become more market friendly and to reduce its presence within the political-economic structure of the nation. Therefore the following two sections will consider in turn the previous social setup and the economic setup of Germany to be able to more adequately assess the changes that the Hartz reforms brought with them as well as the structural consequences of those changes.

4.3.1 German Welfare before Agenda 2010

The state saw the market and its role in the market and in society in an almost opposite way before the Agenda 2010 reforms were implemented as the following section shows. Before the Agenda 2010 reforms were implemented, welfare was considered to be a tool of empowerment for the people instead of a stopgap measure on their way to another job or out of an unforeseen circumstance of life.

> One of the essential tasks of the work- and social order is to ensure that the person in its guise as production factor of the economy does not get diminished to an instrument of the economy, but that in the exercise of the economic activity rights of the personality are secured and encouraged; e.g. it is the duty of the work and social order that the health, the human dignity and the rights to express one's personality are protected and promoted (Lampert 1992, 216).

The state sees itself here as a political economic agent, keeping in balance the forces of the market and the ability of individuals to participate in it (Dyson 2002). This is further underlined by the old German employment policies. Those policies were designed around a demand economy where there were more jobs available than there were people looking for employment (Lampert 1992). The Employment Agency directives further underline this. These directives create an Employment Agency designed as a consultative body, where people can receive training and advice over labour market developments and receive unemployment benefits in case of unemployment, so as to provide them with the best possible tools to get an appropriate job and to be adequately rewarded (Lampert 1992). This protection and care for labour is further underscored by the old German unemployment compensation policy.

In Germany, people who become unemployed are eligible for two types of unemployment benefit. They initially receive *Arbeitslosenunterstützung* (Unemployment Support) of 63% to 68% of the salary they received before becoming unemployed for a maximum of 312 Days (Lampert 1992). Thereafter they can apply for another unemployment benefit, the *Arbeitslosenhilfe* (Unemployment Aid) of 56% to 58% of the salary they received before they became unemployed (Lampert 1992). This is done so that the unemployed have a certain amount of protection from the market environment. This protection will allow them to look for job opportunities which fit better with their qualifications and which would allow for a greater fulfilment of the person taking on that job, instead of having to settle for the first job that is available. This also meant that the willingness to work, which is a prerequisite of the eligibility of either of those benefits, was a necessary but not a required component of receiving those funds (Lampert 1992).

The German employment agency furthermore incorporated other points into their operating mandate to get as many people as possible into work. These points include financial aid for retraining in the form of loans, or payment of living expenses (Lampert 1992, 236). These points also include the maintenance and funding of short term or part time employment for the elderly and for people engaged in works for the public good. The employment agency is a central part of the government’s commitment to full employment (Lampert 1992).

This is only a sample of the institutions and of the concept of welfare in Germany before the Agenda 2010 reforms. This sample, however, does provide an overview of the amount of time and money that was being made available to the unemployed in terms of the time people have worked. The fact that the state is prepared to pay unemployed workers between 50% and 65% of their previous salary shows a strong commitment of the German state to take care of the German workforce (Lampert 1992). Their retraining programs and the financial aid provided to people to enter such programs is further evidence of the amount of energy and wealth that was expended in enabling people to re-enter the employment market. It is also evidence of a more balanced power structure where the state has much more control and is able to more effectively negotiate the power of industry, finance and labour. However, it also underlines the structural problem of the inflexibility of the labour market as was pointed out in Chapter 2.

As the following section shows, the new centre left government of Social Democrats and Greens reversed these concepts changing the Rhineland concept to an ordoliberal concept. This was followed by a re-evaluation of the concept of care. The German government re-evaluated its generous concept of care to a more restrictive concept of care, taking away much of the independence of the people of employable age and increasing the independence of the firms. This is a paradigm shift from its previous position of care towards the people as well as its previous industrial policy.

4.3.2 German Industrial policy

The “social market economy” (Dyson 1983, 30) is an expression of the German concept of welfare and the concept of social responsibility of both the German state and of German industry. The previous German economic organisation was designed as a partnership between industry, the workers and the state. In case of economic failure, the state, industry and workers came together to negotiate a *supportable* distribution of the costs of economic failure for all parties involved (Dyson 1983). This was done because during the time before the agenda 2010 particular the time called, by the French, “the glorious 30” (i.e. the thirty years of economic growth after WW2), industry in Germany felt a *social responsibility* not only to itself and its profit margins but to the workers and the economy within which it acted. This conception was also shared by the other social partners particularly the state as the previous section demonstrated by providing political support to the workers through social financing (Dyson 1983).

The previous section it was demonstrated that the state provided a great number of benefits to the workers in order to empower them to find adequate employment as well as continue to participate within the economy while they were looking for employment. This same concept was also employed by the state in relation with German industry.

> In short, corporation law and the law of insolvency rest on a concept of the firm as a community of interests and reject a strictly contractual notion of employment. (Dyson 1983, 33)

German law recognises the importance of industry within the economy and privileges its survival over the rights of the creditors, in the sense that it provides possibilities for industry to reorganise its workings so as to become solvable or in the worst case be able to provide satisfaction to as many parties concerned as possible should it fail (Dyson 1983).

However, in contrast to the services provided to the workers, the German state only provides the legal framework for industries while leaving the resolution of the crisis to “the bank-industry nexus” (Dyson 1983, 41). The relationship between state and industry in Germany should be considered more as a strategic alliance which profits both parties.

Within this phase of economic development, industry (pre-agenda 2010), finance, society and the state were closely connected. The German crisis resolution mechanism the “bank-industry nexus” (Esser, Fach and Dyson, 1983, 110) was also the motor of the German economy. Banks in Germany are universal banks ((i.e. banks that combine commercial and investment services) (Esser, Fach and Dyson 1983, Dyson 2002)), these banks would provide financing to industry and thereby retain shares or part ownership of industries allowing them to exert direct influence over the direction a firm was taking. Banks during that period used long-term evaluations with the aim of providing for healthy and continued industry growth as well as targeted investment (Esser, Fach and Dyson 1983, Dyson 2002).

This allowed them to enter into a close cooperation with the firms as well as with employees and with the state. It also allowed them to provide accurate and considered investment advice to investors since these banks were also operating within the international markets. However, this universality of the banks while having been a tremendous asset to the German economy it was also a conduit through which changes in structural power on the international arena could be translated into domestic pressures. The proximity of German banks to German industry further increased those pressures.

Several events within the past 50 years have put pressure on the close connection between industry banks and society. Firstly, the actions and inactions by the USA and European nations in the regulation of the financial institutions and financial markets described in the previous chapter provided the framework for the power balance between the different parties to become lopsided. Secondly, the oil shocks of the 1980s and the German reunification of the 1990s put further pressure on the relationship. Finally, the increased structural power of the European institutions (see the Maastricht Treaty) and the progress made on the EMU, required a more liberalised market and less state intervention to allow for closer European integration. All of these points significantly contributed for this arrangement to be seen as too sluggish to deal with crises quickly and decisively.

It was also seen as a hindrance to further European economic integration (Dyson 2002). The agenda 2010 is the German governments reaction to these pressures towards greater industry independence and a greater market presence in state operations and industry-labour relations. Additionally, the EMU implementation in 1998 has added further stresses, which will be considered in the following section.

4.3.3 The EMU and its impact on the German Model

So far the position of the state and of industry has been investigated. This section will consider the importance of banks within the German model, specifically the Bundesbank since the Bundesbank was the model upon which the European Central Bank has been modelled.

The Bundesbank was a centrepiece of the German economic policy during the post-war years and into the 1980s and 1990s (Dyson 2002). The Bundesbank maintained a low level of inflation within Germany and a stable "Deutsche Mark" at a level that supported the German export of goods manufactured in Germany. The stability and predictability of the monetary strategy of the Bundesbank led to its principles being overtaken by the European Monetary Union (EMU) in its establishment of the European Central Bank (ECB) (Dyson 2002).

The independence of the Bundesbank in setting German monetary policy came to an end with the entry into force of the EMU. No longer independent or empowered to enact monetary policy. This is now being done by the governor of the ECB in consultation with the other national governors. Therefore the Bundesbank is no longer able to fine-tune its monetary policy to the needs of the German economy as monetary policy is now set to achieve the best results in the entire euro zone (Dyson 2002).

Not only did the EMU bring with it the Euro but also convergence criteria and rules and regulations, which Germany as well as the other Euro members now have to adhere to in order to keep the Euro a stable currency. This package of rules and regulations was the final straw that sealed the German road to reform of its social-political-economic setup. Germany was now not only under pressure by internationalized markets to reform but also from the institutions of the European Union. With the signing of the Maastricht Treaty and the establishment of the EMU the EU gained further powers and influence, further changing the balance of structural power between nation states and European Union.

4.4 The becoming of the Agenda 2010 and the Hartz laws

This section analyses the evolution of the new nature of the concept of social security in Germany. In the first part, it assesses along which socio-political-economic principles the conceptions of social security are shaped and how these principles have been translated into law. This and the following sections also show that these reforms constitute not only a significant change from the traditional social framework, which was in effect before these reforms were undertaken, they also constitute a significant change in the relations between industry, state and labour. This is a significant departure from the old norms as these norms were closely integrated and were designed for a greater burden sharing. It will be demonstrated that the new understanding of social security has changed from a classical-liberal political economic concept to a neo-liberal market centric concept changing the structural power distribution within the country. The second part of this section will consider in detail the Commission report, which drafted the policy recommendations, which the SPD/Green government then transposed into law under the name of “Hartz Laws”.

4.4.1 Party Manifesto

After 16 years in office, the CDU/CSU and FDP coalition was voted out of office in 1998. In October 1998, Gerhard Schröder became the new German Chancellor. At an extraordinary party conference on the 17th April 1998, the SPD approved their party manifesto, their governing document for the coming legislative period entitled “Arbeit, Innovation und Gerechtigkeit: SPD Programm für die Bundestagswhal 1998” (Work Innovation and Fairness: SPD manifesto for the federal election 1998, hereafter referred too as the *SPD manifesto*) (Vorstand der SPD 1998). This document forms part of the ideological basis of the “Agenda 2010”, which would become the most expansive and in-depth change in social security provisions in the history of the German state since Bismarck’s introduction of social security in 1883.

This programme was a political document, therefore it should be considered with a certain amount of caution. Nonetheless, this document raises several important points that should be noted as they address the demands made by the EU institutions with regards to the liberalisation of the German economy. This is the SPD’s initial attempt at dealing with the increasing number of problems and pressures that Germany was exposed to since the oil shocks in the 1980s. This is also the SPD’s initial attempt at recapturing the structural power that it lost due to the crisis as well as due to the increased power of the EU with the enactment of the EMU and the signing of the Maastricht Treaty.

The SPD manifesto defines the politics of the SPD as: “Die neue Mitte”, *the new middle* (own translation) (Vorstand der SPD 1998). It thereby lays claim to all forms of centrist politics, which this SPD manifesto goes some way to demonstrate. It focuses on the economy and on employment as the central themes of its governing efforts. The SPD manifesto also provides the central theme in the SPDs understanding of the state’s provision of social security. This move by the SPD to put at the centre of its governing ethos a labour market and economic reform designed to make Germany more competitive on the international markets (Vorstand der SPD 1998) has important neo-liberal economic theory undertones. I would characterise the old German social state and economy as heavily influenced by Keynesian economics. Judging by the direction this manifesto is taking, the SPD manifesto moves decisively into the direction of neo-liberal orthodoxy. However, in doing so it does try to retain some Keynesian elements. It was the aim of the SPD, though particularly its leader Gerhard Schröder, to find an effective balance of neo-liberal and Keynesian ideas with this manifesto, in order to help tackle an increasingly globalized economy within which Germany had to survive.

The manifesto tries, as a rule, to increase efficiencies through *a reduction of bureaucracy*, *increased flexibility in the labour market*, *reduced taxes* and *fewer industrial regulations*, with all available savings being diverted into funds to expand funding in education. This is a good example of the changing power structure between the state and the market that Strange pointed out earlier. The SPD manifesto tires to accommodate the demands of the market in a way that doesn't have overly negative repercussions on German society. It argues that equal access and advancement across all forms of education and science provides a better way of achieving equality than direct governmental efforts. The manifesto's focus is on human capital instead of real capital (Vorstand der SPD 1998, 16-17).

The central focus of the SPD manifesto is employment (Vorstand der SPD 1998, 18). Employment to the SPD is the lynchpin on which the economy and the success of Germany in Europe and the world depend. The answer the SPD manifesto finds to the question of how to increase employment while balancing the traditional concepts of social security with modern market processes has several parts.

First, the manifesto wants to enable internal consumption, thereby boosting domestic production and taking away the focus on the exports of goods. This is a Keynesian effort of boosting job growth through economic expansion. However, the realisation of that effort shares more aspects of neo-liberal than Keynesian economic principles. The idea was to expand the economy through helping the middle class with tax reductions, (Vorstand der SPD 1998, 15). A reduction of the tax burden across the board with a special emphasis on the lower income classes, in the name of a more fair tax system would, so goes the argument, incite increased consumption (Vorstand der SPD 1998, 20). This attempt at increasing job opportunities involved efforts to increase employment and private consumption and included a push to improve the situation for businesses, especially SME's through the tax reductions (including payroll taxes) and reductions of bureaucracy (Vorstand der SPD 1998, 21).

Second, the manifesto wants to reinvigorate the labour market to be able to respond to the rapidly changing economic landscape. Therefore, the SPD manifesto linked and conditioned social security provisions closely to employment by redefining the duties of the state. The SPD manifesto no longer considered the state as *a carer* for the disenfranchised but as *a helper* of the disenfranchised to lift himself or herself up. This is a central point, which is going to be carried through every further evolution of the redefinition of the state and form the basis of the Hartz laws. It also demonstrates Strange's (1988, 1996) point about the continued decrease of power of the state, which in this case is no longer willing to provide unconditional support to its citizens. This all follows from a changed understanding of the conception of social security analysed in section 1 of the SGB above. This change is defined in this manifesto in the following way: "Arbeit finanzieren statt Arbeitslosigkeit bezahlen" (finance work instead of paying for the unemployed) (own translation, Vorstand der SPD 1998, 22).

Another pillar of the SPD's efforts to reduce unemployment was to define a strategy that would ensure that young people in particular could find work as quickly as possible and not spend a lot of time on the unemployment line. One proposal of the SPD manifesto was to make working hours more flexible, even reduce working time, in order to allow other people to get a job even if it was only part time (Vorstand der SPD 1998, 19). This proposal aimed to help those who have lost their employment or have just graduated school or university and are trying to find employment (a similar concept was also implemented in France, see Chapter 7).

This increased flexibility of the working conditions was aimed at making it easier for young people to enter the jobs market. Irrespective of one's age or work experience, personal responsibility was a key point in the new government narrative on welfare. One further way to fund the expansion of the education and job opportunities for young people was supposed to be financed via reduced unemployment contributions to young people, which, as a double function, was serving as further incentive to the young to find work quickly (Vorstand der manifesto 1998).

In their attempt to finance or to incentivize work, the SPD in its manifesto also put forward a very Marxist-influenced concept. The manifesto proposed the workers' ownership of the means of production by giving each worker a stake in the company they work in. Though not as drastic as Marx's' (1974) original concept, the principle remains the same. Another Marxist inspired issue was the SPD's opposition to wage dumping which in their manifesto they condemned very strongly (Vorstand der SPD 1998, 23). This condemnation does feel somewhat empty, however, when one considers that one of the first labour market reforms passed concerned mini-jobs (400-800 EUR) (BMAS, 2011) and the Hartz4 reform (Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt, Bundestag 2003) required people to take the first job offered irrespective of the pay.

Third, reducing public debt remains an issue of great importance to the SPD and methods to reduce that debt have been put forward in the SPD manifesto. The necessity for a balanced state budget and reduced levels of debt would help keep investor confidence as well as government bond sales high and the yields on these bonds quite low (Vorstand der SPD 1998). This is the first time that a link between balanced budgets and low interest on government bonds is made by the new German government. This link, however, will become a very important argument to the German government in 2010 when austerity prescriptions were introduced to receive aid under the EFSF and later the ESM. This link would become even more important to the German response to critiques of other Euro Zone countries that austerity was bad for their economies. One of the reasons for the German government's maintenance of these austerity prescriptions will be considered below.

Public debt again was linked to work and a performing and expanding economy. In the German argument, taxes can be lowered for all people and the budget balanced, if there is economic growth and low unemployment (Vorstand der SPD 1998). Economic growth means more income for the state and low unemployment means that the state can tax more people even though it lowers the overall level of taxes. Having more people employed also means less social security expenditures for unemployment benefits and other benefits in kind, further reducing the financial burden of the state.

It should though be noted that at the time of this manifesto, the main thrust aimed at financing these tax cuts was by way of closing down tax loopholes and special deductions and through a tougher crackdown on tax fraud (Vorstand der SPD 1998, 28). These tax reductions for private citizens needed to be paid for with a reduction of state expenses, which was part of a financial restructuring effort aimed at reducing overall public debt (Vorstand der SPD 1998, 30), of which higher levels of employment were an essential part. The focus on reducing the public debt is, as this document shows, not a new or recent discussion within the German government. However, as this document also shows, the social democratic way of deficit reduction initially consisted of finding a balance between stimulating the economy and reducing public spending.

These changes in the conception of social security provisions are indicative of a greater move towards market orthodoxy by the state. This is again concurrent with Strange's (1996) argument that the state is ceding more responsibilities to the market. The SPD manifesto attempts that move in a very ambiguous way. It holds on to the traditional conception and role of the state's social apparatus by arguing that a well-functioning economy requires well-functioning social services whose provision allow for risks to be reduced and more easily calculated. Those services are only allowed to intervene so far that people are still able to think creatively, come up with innovative ideas, and therefore participate fully within the economy. The goal of a modern social state should be to *encourage personal responsibility and innovation instead of taking a paternalist role* (Vorstand der SPD 1998, 37).

This thought argues that the market should be allowed to work freely and thereby efficiently directing the economy. The state and its social apparatus should only be there to complement the market and ensure a flexible and vibrant effective labour market with a readily available labour supply. The result was a desire to have the state and its social apparatus take a much more reduced role in society and focus on ensuring true market growth. This desire by the SPD draws the manifesto into making an assertion, which closely resembles - indeed paraphrases –John Locke (see Chapter 4, section 4.3.1) where he argued that people who were able to work but did not, should be forced to do so by laws designed to encourage production and increase employment (Locke 1993). This manifesto echoes that statement.

> ... we will ensure that for those social welfare recipients who decline available employment without a valid reason, the existing statutory provisions for termination of welfare payments will be enforced. (Vorstand der SPD 1998, 38)

One of the biggest issues that were being pointed out in this manifesto was the generational repercussion of the pensions system. The SPD pointed out in their manifesto that there was a problem within the current concept of pensions. As Chapter 2 demonstrated, the system requires a greater number of people coming into the system than people who are taking out of it. This system also requires people to provide 40 years of contributions to the system before they can get their pensions. This system according to the manifesto has begun to come under severe strain, since many people may not earn enough to pay those contributions. These people may be self-employed, unemployed or have had breaks (periods of non-payment) in their contributions making them fall short of the 40 years required to get their full contributions (Vorstand der SPD 1998, 39-40). The problem is acute since, the retirement age had already been raised by the previous government to 65 years (Lampert 1992) to compensate for the shortfall in funds.

The SPD solution is in keeping with the solutions proposed by the manifesto so far. The SPD manifesto attempted to adapt the Keynesian pension model as defined above to the socio-economic reality of the time. This was done within the confines and with the help of the other principles already established - i.e. a reduction of social services, and a general increase in the working population. An increasing working population would plug the hole in the contributions for current recipients but would not entirely address the generational deficits (see Chapter 2, Table 2.2). Other options, which the SPD manifesto was exploring included an increase in the retirement age by two years (raising the retirement age to 67), which would lower the overall contributions to be paid out and increase the amount of contributions paid back in and make the pension fund viable for longer (Vorstand der SPD 1998, 40). Further avenues that were being pursued by the Vorstand der SPD in this manifesto (1998) were: an increase in private pension contributions as well as corporate pension schemes, taking further strain off the public pension system making it available for longer.

Healthcare is the final component of social security that this manifesto looks at. Here again, a restructuring was proposed using market forces, by introducing more competition into the health sector. Other proposals include improving communications among doctors, collectivizing costly medical technologies as well as introducing stricter household budgets for hospitals.

These proposals aim at reducing the overall costs and inefficiencies of the healthcare system, improving services for people (Vorstand der SPD 1998, 41). A further benefit of reducing costs for people is that they also reduce the cost of healthcare for the state.

The SPD manifesto is a very important document, as it defined the political and socio-economic ideology, which was driving the SPD's decision-making during their time in office. This manifesto also served as the ideological and policy basis for the "Agenda 2010" social security reform proposal passed by the Bundestag from 1999 to 2005. This reform defines social security practices by the German government to this day.

This SPD manifesto moves the German state action further down a neo-liberal path than it was on before. It also started the process of liberalization of the German economy. The SPD manifesto in its propositions addressed many of the points which the EU through their new found power through the EMU treaty demanded (Dyson 2002), the SPD manifesto still tried to temper those structural forces and direct them to serve a social democratic agenda along the lines of the one that was developed in the post-WW2 era and described in the previous section. It can be considered as an attempt to reinvigorate the "Model Germany" (Esser, Fach and Dyson 1983, 102) with quicker response times and greater flexibility. The SPD manifesto also shortly precedes the publication of a position paper written by Gerhard Schröder and Tony Blair, which will be analysed next.

4.4.2 The Third Way

Gerhard Schröder and Tony Blair in June 1998 published a document entitled "Europe: The Third Way/Die Neue Mitte" (Schröder, Blair 1998, 1), wherein they propose a new socio-economic agenda for Europe's social democrats. This document is important for several reasons. On the one hand, this document shows that both Tony Blair and Gerhard Schröder have similar conceptions of the world in which they live in and what social democracy represents within that world. The fact that this document was co-written by Schröder suggest a strong personal connection to the ideals proposed in the SPD manifesto, which was approved only a few months before this text was published.

The most notable point for this thesis is the explicit nature of the vision of Tony Blair and Gerhard Schröder in this text. On the one hand, there are the much more explicit and “enthusiastic” espousals of neo-liberal ideas and concepts and, on the other hand, there is the categorical denial of any concrete affiliation to neo-liberal ideology all the while reframing the social democratic conception of social security and social welfare along neo-liberal lines. In their efforts to find ways to improve the jobs market and employment, Schröder and Blair dismantle Keynesian conceptions of the proper setup of the economy and of society. One of the key ideas in their efforts to improve employment prospects is flexibility particularly of the labour market. This could suggest a Gramscian strategy of building up a competing (in this case neo-liberal) ideology within an existing (in this case social democratic) ideology (Sassoon 1980). The Examples of this include:

> The promotion of social justice was sometimes confused with the imposition of equality of outcome. …. (Schröder and Blair 1998, 3)

> The means of achieving social justice became identified with ever-higher levels of public spending regardless of what they achieved or the impact of these taxes required to fund it on competitiveness, employment and living standards. Decent public services are a vital concern for social democrats, but social conscience cannot be measured by the level of public expenditure. … (Schröder and Blair 1998, 3)

> The belief that the state should address damaging market failures all too often led to a disproportionate expansion of the government’s reach and bureaucracy that went with it. … (Schröder and Blair 1998, 3)

> Too often rights were elevated above responsibilities, but the responsibility of the individual to his or her family, neighbourhood and society cannot be offloaded on to the state. …. (Schröder and Blair 1998, 3)

> The ability of national governments to fine-tune the economy in order to secure growth and jobs has been exaggerated. The importance of individual and business enterprise to the creation of wealth has been undervalued. The weaknesses of markets have been overstated and their strengths underestimated. (Schröder and Blair 1998, 3)

> Ideas of what is ‘left-wing’ should never become an ideological straightjacket. (Schröder and Blair 1998, 3)

This document as well as the SPD party manifesto's focus on jobs and job creation; all other aspects engaged with in this document are linked in some way to job creation.

As was argued above, the lines of neo-liberal ideology are drawn more clearly in this work. This comes especially to the fore in Blair and Schröder's interpretation of the adequate size of government of which the previous quotes have provided some indication. They argue that government has now reached its highest extent in terms of its capacity to spend money and mitigate any structural weaknesses in the economy (a point, which is at least partially disproven by the 2008 financial crisis government interventions). They further argue that the state indiscriminately throwing money at issues is inefficient and unnecessary. Any programme that does not provide value for money should therefore be reduced or cut entirely (Schröder and Blair 1998).

> The state should not row but steer: not so much control, as challenge (Schröder and Blair 1998, 4).

It is followed by claims of greater quality control of the state bureaucracy and a general reduction of the bureaucratic hurdles businesses are required to surmount (Schröder and Blair 1998). All in all, this statement argues that the role of the state in society and within the economy needs to be redefined in accordance with the new realities of more powerful markets and greater competition between states.

Although Blair and Schröder denounce neo-liberal laissez-faire doctrines as out-dated, they equally denounce classical liberal state interventionist theories. The way that Schröder and Blair (1998) attempt a melding of the two liberal approaches is through a much greater emphasis on market powers as the regulating force in the economy. The state plays only a complementary role in this worldview.

Further evidence of Schröder and Blair's neo-liberal bias is demonstrated by their advocacy of lower taxes for low-income households and corporations to incentivise growth as well as their argument that hard work, and not social welfare, would make people better off (Schröder and Blair 1998).

The most significant and contentious programme of theirs was to increase employment through "welfare to work programmes" (Schröder and Blair 1998, 7) and reductions in social security contributions by both employees and employers which were supposed to stimulate consumption with employees and production and hiring with employers. These proposals feed directly into another policy proposed of theirs, again linked to job creation i.e. the promotion of SME's. Allowing SME's to flourish through the reduction of corporate taxes and non-payroll taxes as well as reduced red tape in their argumentation would be a motor for employment and economic growth (Schröder and Blair 1998).

While they argue that laissez-faire economics are out-dated, Schröder and Blair (1998) do emphasise a greater need for deregulation. They contend that the changing nature of work from industrial production to directly consumed knowledge-based services requires a new way of thinking especially by the state. Stringent and over regulation would hamper a knowledge-based economy in its development (Schröder and Blair 1998, 8).

> Companies must have room to manoeuvre … they must not be gagged by rules and regulations (Schröder and Blair 1998, 7)

Proper education and training during youth would enable a much quicker and effective start to the working life and a much smaller probability of requiring government aid as well as making the labour market in Germany and the UK more attractive and flexible. What aid the government *is* spending, is designed to improve economic growth and implementing the changes to the social structures (Schröder and Blair 1998). The principle of investing in the teaching and training of its youth does have some Keynesian connotations to it.

A final policy priority for Schröder and Blair (1998) are deficit reductions. This policy area is also the one which shows their most centrist and pragmatic positions. They agree with the Keynesian principles of government that intervention through deficit spending is necessary during times of economic contraction. They disagree with the idea that government should continue its intervention once growth picks up again, as such interventions would distort market signals and shelter any "structural weaknesses" that state intervention compensated for during the downturn (Schröder and Blair 1998, 10).

All in all, it can be argued that, although Schröder and Blair do not completely espouse the neo-liberal laissez-faire attitude, this document and the policy proposals contained within it do give the impression that although their solutions are pragmatic, they do favour more neo-liberal ideas than they do Keynesian ideas of government. This is again demonstrated by one of the final passages in the document:

> Change inevitably destroys some jobs, but it creates others (Schröder and Blair 1998, 11)

This is reminiscent of Joseph Schumpeter's concept of creative destruction (Schumpeter 2000). The different points that have been raised above, demonstrate that Schröder and Blair have taken a pragmatic approach to the market forces. It is true that there are some policy initiatives that come straight out of neo-liberal logic, though there are some points that go back to more traditional social democratic concerns. The entire work holds true to its pragmatic nature and tries to keep the social framework intact but at the same time reducing the presence of the social framework in society in order to incentivize individual action and effort.

The establishment of the EMU and the signing of the Maastricht Treaty were the European response to the global economic pressures of neo-liberalism. The contents of this document are the conclusions that were reached by Blair and Schröder in their effort to adapt a social democratic ideology to the structural power exercised by the neo-liberal economic concepts exerted on the international arena, which have put reform pressures on the European Union.

4.4.3 The State of the Nation

The pragmatism that was displayed by Blair and Schröder in their position paper was once again displayed in Gerhard Schröder's state of the nation address. The speech also displayed a resolve to finish implementing the reforms, which he and the SPD considered necessary to address the structural problems of the German economy, which the global market required. By 2003 Gerhard Schröder and his party had managed to implement many of the points raised by Schröder and Blair in their position paper in the form of the Agenda 2010 reforms. Gerhard Schröder's address on the state of the nation in 2003 was dedicated in its entirety to the Agenda 2010 reforms, to allow him to take a stand in support of the necessity of those reforms.

This state of the nation address was on the 14th of March 2003, three and a half (3.5) months after the first three of the four Hartz laws were implemented on the 1st of January 2003. The Hartz IV laws were implemented on the 1st of January 2005. In this state of the nation address, he defended the reform course of the SPD/Green government as an overdue and necessary step in a more globalized and competitive global environment (Schröder 2003).

This is a direct reference to the fact that the German government has responded to the changes within the international power structures towards a more liberal and finance oriented economy with less state intervention more market freedoms and a more flexible labour market.

The speech repeated references about a more flexible workforce, a greater investment in education, lower government spending and an overall greater share of generalized burden sharing as well as much more stringent benefit schemes as advocated in the SPD manifesto and the co-authored position paper of Gerhard Schröder and Tony Blair. In this speech, Schröder (2003) touts the achievements already accomplished as well as vowing to continue the reforms (see next section for a full analysis of the Hartz reforms). Although steadfast on the legislations passed by his government, Schröder does try to put a more humane face on the reforms in this speech.

> Solidarity, the protection of vulnerable people and the hedging against unforeseen risks are not only a constitutional mandate. It is my firm conviction that they form the foundation of our social order (Schröder 2003, 9).

Schröder in his speech not only touted the achievements of the Agenda 2010 reforms, he also engaged with the opposition to these reforms. He argued that, although some may consider these reforms harsh or unfair, considering the economic state of Germany at the time, these reforms were necessary for the greater good of the German society.

> Of course there is no enthusiasm regarding these reforms. Surely, that cannot be otherwise, and I really did not expect anything else. Occasionally, there are measures that need to be undertaken which do not prompt any enthusiasm, not with me either by the way. Nevertheless, they are necessary (Schröder 2003, 10).

This speech was much less infused with economic rhetoric or demands than the SPD manifesto and the Third Way Paper were. The speech was laden with attempts to justify and explain the impacts these reforms would have on the German economy. The speech also demonstrated that the SPD was committed to the reform path it had embarked upon. The document contained many references of the points put forward in both the SPD manifesto and the Third Way Paper, which correlates with the initial assessments made that the SPD/Green coalition was in fact able to pass significant reforms during its tenure as the ruling party of the Federal government.

4.5 From the Hartz Commission to the Hartz Laws

The previous section took a closer look at the ideological statements made by the SPD as well as by its leader Gerhard Schröder. The section also considered the reasons behind these statements, i.e. the 1980s oil crises and the growing structural power of the markets, the 1990s German reunification effort and the increased structural powers of the EU through the implementation of the Euro and the following closer integration of the European economies. The 2003 State of the Nation served to demonstrate that many of the policy proposals that were put forward in either the SPD manifesto or the Third Way paper were enacted in some form or another. This section analyses the process that transformed the abstract policy proposals into actual laws by considering why the Hartz Commission was established and what the policy recommendations of that commission were.

To this end this section will analyse the setup and the decision process within the Hartz Commission. With the increased structural power of the finance and industry, due to the changed economic framework and the changed economic narrative, depicting market forces as more competent at organizing economic activity than states (Crouch 2011 see Chapter 2 and Chapter 3), its setup was biased to favour industry and bank representation. This section argues that the proposals by the Hartz Commission based themselves on the proposals made within the SPD manifesto and the "Third Way" paper but were changed within the commission to further increase the structural power of industry and banks than was proposed by the SPD manifesto and the "Third Way" paper thereby fundamentally changing the socio-political-economic framework of the country. The implementation of these Commission proposals into law demonstrate the German government's fundamentally self-limiting state tradition and its consequent acceptance of these reform proposals as well as demonstrate the influence that neo-liberal structural power already holds within Germany.

Finally this section explores the Hartz Laws, which were based on the Commission's recommendations, as well as the changes these laws brought to the legal framework of welfare provision.

4.5.1 Establishment of the Hartz Commission

In 2002, a “Vermittlungsskandal” (“placement scandal” - own translation)) (Siefken 2006, 375), in which the Federal Labour Office (FLO) was accused of falsifying employment statistics, provided a political opportunity to the SPD to try and introduce reforms that would not have passed through parliament at other times. The establishment of a commission was not part of a long-term plan by the SPD/Green government. It was a short-term arrangement allowing them to keep the unemployment issue current and linked to the scandal (Siefken 2006; Hinrichs 2007).

> Their mission was not to present an all-encompassing concept for job creation. Their mission was; to support the creation of jobs through a more efficient labour market politics (Jann and Schmid 2004, 4).

The “Kommission Moderne Dienstleistungen am Arbeitsmarkt” (“Commission for Modern Services in The Labour Market”, own translation, Hartz 2002), the Hartz Commission for short, was composed of 15 people, including business leaders, labour union members and government representatives. Their primary mission was to redesign the Federal Labour Office (FLO). The Hartz Commission was composed of various people, most of whom did not have any close ties to the SPD. The Commission hosted a majority of private sector leaders (7 of 15) (i.e. Peter Hartz being the CEO of “Volks Wagen” (VW) and leader of the Commission) it contained only 2 politicians and 2 social scientists as well as 2 union and employer representatives and 1 Federal Labour Office (FLO) representative. This composition was a break from a traditional tripartite commission, which was composed in equal numbers of business representatives, government mediators and employee representatives, who are traditionally appointed in these situations (Siefken 2006). This is a move away from a traditional setup of such a commission by biasing the membership of the commission in favour of industry. It changes the balance of the power structure within the commission and will create results that will favour industry instead of being an equitable agreement among all the parties.

Another unconventional trait of the Commission was that much of its deliberations were done under little to no public scrutiny (this is similar to traditional business meetings who, as opposed to traditional government meeting are not subject to public scrutiny (Crouch 2011)), at least not for the first four months of its existence. The SPD/Green government did not make a big deal about the nomination or the start of the Commission's deliberations. The Commissioners also agreed (amongst themselves) not to speak to the press about their deliberations. This relative anonymity embraced by both government and Commission was broken only after the exclusive interview of Peter Hartz with *Der Spiegel* in June 2002. After that interview was published, all deliberations by the Committee were made in the public light and discussed openly (Siefken 2006).

Siefken (2006) shows (through interviews with members of the Commission as well as others close to the Commission and partaking in the discussions) that there was no formal structure to the Commission. Although decisions were taken unanimously and chiefly through the efforts of the Commission leader Peter Hartz, who held many smaller group meetings with Commission members. All members of the Commission were regularly updated over the progress of the discussions and were sent extracts of decisions, which were then discussed in the larger circle of the entire Commission.

As the two researchers Werner Jann & Günter Schmid (2004, 5) were part of the Commission, they reported their observations of the interior workings of the commission, which will be analysed below. In its attempt to deal with the problem of transforming the FLO that was set before them, the Commission oriented itself on three "scientific truths":

1. Every strategy for unemployment reduction has to primarily tackle long-term unemployment
2. Studies show that the easiest way to combat long-term unemployment is to tackle it before it becomes long-term.
3. Employment agencies are much more successful when they are in direct contact with employers. (Jann & Günter Schmid 2004, 3)

The investigations into the Commission procedures and set up (Siefken 2006, Jann & Schmidt 2004) show that the members of the Commission felt a sense of duty towards Germany and its people to come up with a document that could be helpful for their future well-being. This sense of duty combined with the growing independence from the government who appointed it and an expanding issue area. The Commission decided to take on this expansion in order to better tackle the task it was initially assigned (Siefken 2006; Jann and Schmid 2004).

> The members of the commission saw themselves mainly as an idea factory, with neither the request to formulate; fully thought out law proposals, nor the self-evident understanding to formulate scientifically based truths (Siefken, 2006, 381).

“Moderne Dienstleistungen am Arbeitsmarkt” (Modern Services on the Employment Market, own translation, Hartz 2002, Legnaro 2006) is a document, which was written in conversational German, using a large amount of management jargon and management style. It shows that the primary goal of this Commission was not to present law proposals but rather provide ideas for the government. The greatest efforts have been made in the presentation of this report, which is designed to be catchy and engaging; the content itself, however, does not have a clear or cohesive structure (Siefken 2006).

There are further concerns about the quality of the report. Considering the fact that the Commission was only in existence for 6 months, it was quickly assembled and therefore is liable to not have had time to go over and finalise a clear and easily applicable plan, which indeed was not the case. In addition, the atypical configuration of the Commission, with regards to other such commissions, the closed appointment procedure and the mere 2 months, which faced an intensive scrutiny by the media of the Commission’s, work. The scrutiny raised questions about its legitimacy and the competency by which these proposals were worked out (Siefken 2006).

The primary mission of the Hartz Commission was to redesign the FLO. Their task was to enable the FLO to be better able to get people to work. The Commission soon realised that, in order to reform the FLO, it also had to find ways to reinvigorate the jobs market, making it more flexible and more competitive. At the end of their deliberations, the Hartz Commission had developed a set of proposals.

4.5.2 The Commission proposals

The conclusions and changes to the SGB, which the Commission presented, bore close similarity to the changes proposed by the SPD manifesto of 1998. The Commission report for instance copies and builds upon the SPD’s idea of a reduction and restructuring of the social and unemployment assistance payments to people out of work. The SPD slogan “Arbeit finanzieren statt Arbeitslosigkeit bezahlen” (“finance work instead of paying for unemployment", own translation, Vorstand der SPD 1998, 22) is a leitmotif to the Commission's proposal whose slogan was "Fördern und Fordern" ("to foster and require", own translation) (Deutscher Bundestag, Viertes gesetz für moderne dienstleistungen am arbeitsmarkt, 2003, Article 1, Kapitel 1) which also became the first chapter of the Hartz IV reform bill (Deutscher Bundestag,Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2956).

The Commission's report fleshes out some of the measures necessary for the implementation of a more flexible jobs market, as well as the measures linked to the restructuring of social benefit programmes, such as unemployment benefits, which were proposed in the 1998 SPD manifesto. The Commission report proposes to transform the Federal Labour office (FLO), a government agency, into the Federal Employment Agency (FEA), a partially privatized agency, with corporate structures and independent agencies spread across the country. The partial privatization of the FLO was supposed to add an element of competition and flexibility into the agency. The decentralization was an effort aimed at improving the services provided by these agencies by giving the different FLO agencies a measure of authority letting them focus on the region within which they are located and allocate funds as they see fit (Hartz 2002).

The restated aim of transforming the FLO into the FEA is to reduce long-term unemployment and to get people quickly back into work if they ever fall out of work (Hartz 2002). In order to do that, the Commission proposes further restructuring of the local agencies into specialized jobcentres, with the sole purpose of getting people back to work. Any activity that does not directly relate to that task should be outsourced to private subsidiaries. *This reduction of bureaucratic tasks should further reduce the time it takes for people to get referred into new jobs*.

There will be a greater focus on personal responsibility and personal initiative. Information on employers and job vacancies will be made more widely available. This is a clear move by the Commission down a neo-liberal redesign of the social services that the state provides. These proposals also change the structural power of the labour market away from people and towards industry, allowing for an easier method to obtain skilled labour and to adapt more quickly to changes in economic performance by lowering employment protections.

People will be required to register with the jobcentres as soon as they have been made redundant or as soon as they know that they will be made redundant. If they do not, they will face reductions in their unemployment benefits for each day they fail to report their redundancy. Any refusal of a job offered will have to be substantiated by reasonable proof. If that proof cannot be provided, the person will face a suspension of his/her benefits (Hartz 2002).

> The reasonableness of an offer will be judged by the material, geographical, functional and social criteria and consequently implemented in connection with voluntariness and duties (Hartz 2002, 24)

Priority in job placements and greater leniency towards refusals of those offers and consequent contributions will be given to people who have a responsibility towards dependents. On the flipside, young singles will receive far less leniency towards refusals of job offers as well as facing a greater expectancy of job mobility. Having restructured the eligibility clauses of benefits, the Hartz Commission also restructured the benefits that fulfilling these clauses would provide. This restructuring meant that people, depending on their status with the job-centre, would be entitled to one of three types of payments.

> a) Arbeitslosengeld 1 (“Dole1”, own translation): Dole 1, is the original unemployment pay, which is being paid out according to current regulations.
> b) Arbeitslosengeld 2 (Dole2, own translation): Dole 2, is a tax funded benefit covering a person’s basic living expenses including social security contributions once Dole1 has been exhausted or the conditions for its payment have been breached.
> c) Sozialgeld (“welfare pay”, own translation): Welfare pay will correspond to the social entitlements of the unemployed and will be managed by the social welfare office. (Hartz 2002, 27)

These changed measures in the payment of unemployment benefits are aimed at taking better account of individual living conditions. Thus, people have the option of de-registering from the job-centres, thereby no longer getting help to find a job as well as no longer being eligible to receive unemployment benefits.

Further cost reductions were proposed by the Commission through the introduction of data cards designed to further reduce administrative costs, as well as simplifying the calculation of benefits to the unemployed (Hartz 2002, 27). Another concept of the Commission was a “*Beschäftigungsbilanz*” (employment balance sheet, own translation). The companies (on a voluntary basis) would keep balance sheets that would show the hires and fires of the company. If a company had a positive balance sheet it would get a bonus from the unemployment office, if it had a negative balance it would forfeit the bonus (Hartz 2002, 28).

Another project of the Commission was the creation of Personal Service Agencies (PSA) (Hartz 2002, 29). These companies are supposed to provide services to ease the entry of people into work by providing services to other companies in the hope that these people will be taken over by the companies as permanent employees (Jobs with the PSA's are subject to the same pains and penalties as other jobs offered by the FEA).

Getting people back to work needs a more precise interpretation of work: it means getting people back into *taxable* work. Focussing on the issue of clandestine employment therefore is a significant issue that needs to be resolved if the state wants to increase the taxable salaries to which it has access. The solution of the Commission to reduce clandestine employment was through the creation of "Ich-AG" and "Familien-AG" as well as the creation of Mini-Jobs (Hartz 2002).

"Ich-AG"'s and "Familien-AG" are designed to be a stepping-stone towards self-employment for people who are clandestinely employed. These AG's benefit from FEA grants equal to Dole and welfare contributions for the first three years since their setup, as well as being granted a flat-rate tax of 10% on their earnings up to a limit of 25000 Euros (Hartz 2002, 30).

Mini jobs are designed to cover the remaining clandestine domestic work, which does not fall under the purview of the "Ich-" or the "Family-AG". Mini jobs can earn up to 500 Euros and are subject to social security contributions at a flat rate of 10% (Hartz 2002, 30). Originally designed by the Hartz Commission only to be used in private household situations, Mini Jobs (and the Mini Job salary) have now been allowed to be proposed in an expanded range of jobs. This increase in the amount of jobs that are allowed to be proposed as Mini Jobs and the pay this includes is causing significant concerns (Werner, Schmid 2004).

Further technocratic aspects include the coordination of local initiatives and the complementing of those initiatives with company requirements. The jobcentres will be designed to serve as a conduit between the communes and the *Länder* in order to be able to better respond to the companies' job requirements (Hartz 2002, 31). Another technocratic aspect includes hiring incentives, where companies are provided with a financing package in the form of a loan for each worker hired if they take onto their payroll the job floaters provided to them by the FEA (Hartz 2002, 33). Using these measures, the Commission expected to get up to 2 million people back into work (best-case scenario). This return to work would potentially save the German government up to 19.6 billion Euros in benefit payments (Hartz 2002, 33).

The SPD/Green government's establishment of the Hartz Commission could be compared to the non-decisions critiqued by Strange (1998, 1986) in Chapter 3 where instances of non- or deregulation have allowed the financial market to expand and develop in ways the states were no longer able to control effectively. Even though the situations compared here are of a different scale, the principle is the same.

Considering the importance of industry within the German socio-political-economic makeup a strong presence of industry leaders within the Hartz Commission was not surprising. The Commission therefore was able to present a reform plan which would certainly help German industry, however, at the same time also departed from the close connection between industry state and labour. It can be argued that the reason why industry has suggested these reforms was because of the close connection of banking and industry which, in order to attract more investment, needed to demonstrate higher profits and better returns for investors.

The German government on the other hand was not blameless in this. It was the German government that allowed businesses and therefore the market to develop and design a reform for a sector of the political economy that without effective state intervention was liable to instances of moral hazard (see Chapter 3). While the content of the Hartz laws has modelled itself along the neo liberal proposals initially set up by the SPD manifesto, the Hartz proposal has been much more infused by neo-liberal concepts and neo-liberal thinking. The Hartz laws are further evidence of that.

4.6 The Hartz Laws

The SPD/Green coalition set up the Hartz Commission at the end of their first term in office, on the 22nd of February 1998. The Hartz Commission proposals investigated above had a profound impact on the laws that were enacted by the SPD government during their second term in office. The coalition government vowed to implement into law 100% of the recommendations of the Commission (Schröder 2003), although only about 30% of the Hartz Commission recommendations have been directly transposed (Werner, Schmid 2004)

The four laws entitled: „Gesetz für moderne Dienstleistungen am Arbeitsmarkt“ (Laws for modern services in the labour market (own translation)) more commonly known as the Hartz I-IV laws, were named after the name of the Commission that proposed these reforms. These social security and labour market reforms were subsequently implemented in three instalments (Verein für soziales Leben e.V 2011).

4.6.1 The first Hartz law

*Hartz 1 (*Deutscher Bundestag Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002) provided the general framework for the Commission proposals. The Hartz 1 law made the first move in reframing the conception of the caring state towards a more expecting state. These laws consequently moved towards more market-oriented principles of recruitment practices and service outsourcing to cheaper service providers as well as increasing expectations towards the unemployed to engage more actively with the search for a new job, instead of overly relying on unemployment benefits (Deutscher Bundestag Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4608).

The Hartz 1 laws created the Personal-Service-Agentur (PSA) providing it with structures and governing bodies as well as defining its rights and responsibilities towards jobseekers as well as the rights and responsibilities of the FLO towards the PSA. It also introduced the requirement for the unemployed or soon to be unemployed to register immediately with the “Arbeitsamt” (unemployment office), or face a reduction of their unemployment benefits. It defined the instances within which a person may see their benefits reduced in case of non-compliance with that directive (Deutscher Bundestag, Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4609). It also set the amount by which those benefits would be reduced as well as the timescale within which they would be paid out (Deutscher Bundestag, Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002 4612-46).

The Hartz 1 laws also provide a legal framework and conditions of availability for the Commission's proposal to provide people with the ability to seek further education or training through payment of the registration fees as well as childcare, housing and commuting subsidies. These payments are conditioned on the attendance of the person at the classes as well as the demonstration of progress and the successful completion of the course (Deutscher Bundestag, Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4610-4612).

Another proposal of the Commission, which was transposed into law, was the proposal for performance-linked pay for the employees of the "Arbeitsagenturen" (employment agencies, own translation) in an effort to increase the efficiency of the agencies and the number of people put back into work (Deutscher Bundestag, Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4614).

The Hartz 1 law (Deutscher Bundestag, Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002), implemented the reforms that were a combination of administrative changes designed to lead the way for the more substantial reforms of the second but especially the third and fourth Hartz reform laws. What can be pointed out, however, about the Hartz 1 laws is that it provides a good overview of the kind of neo-liberal concepts the following Hartz laws will contain.

4.6.2 The second Hartz law

Hartz 2 (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002) provided the legal framework for the "Ich-" and "Familien-AG" as well as for the Mini jobs. Because of these changes, it also contains changes to the social security contribution laws, as well as the social financing laws (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4621). The "Ich-" and "Family-AG" was created within law just as it was proposed by the Commission. Providing aid to these one-man/one-family firms in the form of unemployment and social security benefits up to an income limit of 25000 Euro on the condition that the people can make a case for their continued provision. The aid is limited to three years after the founding of the AG as was proposed by the Commission

(Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4622).

The mini jobs were made into law with special emphasis on the social security contributions that these jobs would hold. Mini jobs can pay a maximum of 400 Euros per month, which are free from taxes, and can reach up to 800 Euros (through a combination of mini jobs), still remaining tax-free. If, however, the income regularly exceeds 800 Euro, the income will be taxed along standard rates (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4623).

The Commission designed the Mini job provisions to be used in domestic work and not necessarily as a general method of employment. People who employed a house helper were now required to submit papers for the employed help as well as allow social security contributions to be deducted from the wage. Though the pension insurance is not paid into the same pot as for regular earners, it is held with the "Bundesknappschaft". The same goes for health insurance contributions, which go to the Bundesverischerungsanstalt ("Federal Insurance Institution", translation leo.org) instead of the health insurance companies (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4623-4625). Although, on request, they can be dispensed from paying health insurance contributions (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4626) pension insurance contributions remain mandatory.

Additionally, changes to the tax code undertaken by the Hartz 2 Laws are designed to make registering domestic aides by the employers more attractive, as such; employees if registered can apply for a tax deduction of up to 510 Euros (Deutscher Bundestag, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, 4631). Most of the more significant and controversial changes in the social security laws were introduced with the Hartz3 and Hartz4 laws, which remain a controversial topic in Germany.

The reforms contained within the Hartz2 laws continued on the same neo-liberal trajectory than the Hartz1 reform by introducing two new forms of low-income employment allowing that sector to increase substantially with negative effects for German society (see Chapter 6 for further analysis). This I would also consider to be a first example of a negative social consequence of the German government’s inaction in allowing the Hartz Commission to develop social policy.

4.6.3 The third Hartz law

Hartz3 (i.e. Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt) tackled some of the more significant changes of the Hartz Commission’s social security reform. Hartz3 transformed the “Bundesarbeitsamt” (the Federal Employment Office, (own translation), a government body, into the “Bundesagentur für Arbeit” (“the Federal Employment Agency”, own translation) a private employment agency funded by the government. With that transformation came also a redefinition of its purpose and its responsibilities. The constitution of the FEA defined its hierarchy, its internal workings, and appointment processes as well as the legal standing of its employees. The FEA’s constitution also defined its socio-economic purview, and its data protection requirements were comprised within the Hartz3 laws.

Of particular interest here is the fact that the FEA has become a semi-private organization. It has a “Verwaltungsrat*”* (board of directors, own translation) and an administrative committee in each branch but the different government ministries remain the final authority with regards to decisions relating to budgets or administrative disputes as well as approving the FEA’s by-laws (see also Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2875-2883; Hartz 2002 85-86).

Furthermore, to aid in the FEA’s efforts to get people into employment, the FEA was authorised to outsource some of the jobseekers to third party job agencies. Jobseekers may even request to be transferred to a third party if the FEA fails to find a job within 6 months (Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2854-2855). Hartz3 also fleshes out some more the financial aids that the unemployed can request. Such as the “Überbrückungsgeld” (tie-over allowance, own translation) for someone who becomes self-employed (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2856).

Hartz3 refines some of the regulations introduced in Hartz1 and Hartz2, concerning the availability of unemployment benefits. Hartz3 does so in the first instance by defining what falls into the category of unemployment and what does not. It furthermore defines actions that this unemployed person must take or must be willing to take if provided with the opportunity by the FEA or a third party (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2857-2859). The amount of unemployment pay is also precisely regulated within this text. The text formulates the time span of earning along which the unemployment pay is measured, what is included in its measurements and what conditions exist for its further payment. It also includes the regulations for the taxation of those payments, as social security, solidarity and income tax are deducted from the unemployment pay (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2859-2861). The payments of unemployment benefits and pay may be suspended for up to 12 weeks if the jobseeker does not comply with the rules and regulations set forth above. The amount of time that the suspension will last may diminish depending on the circumstances of the suspension (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2861-2862). The period of suspension of services was meant to motivate the recipient to participate actively within the search for employment. It was not meant to be unduly harsh on a person's circumstances or cause any undue economic harm to the person.

Hartz3 also introduced a scheme where companies would receive aid in case of a firm restructuring that results in redundancies of employees. The firm receives this funding only if it undertakes (and demonstrates) efforts to "transfer" people into other employments. This funding includes payments to workers who will lose their jobs due to that restructuring. This should be done within precise boundaries, putting strict requirements on the employer and on the employee to enable the later to re-enter into gainful employment; otherwise the former will see the payments get suspended. The law furthermore puts separate rules and regulations into effect for disabled and severely disabled people, as well as endowing the FAE with the power to change those conditions on a case-to-case basis (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2866-2868).

Another point of interest in this Hartz3 law, is its emphasis on job-procurement measures (*Arbeitsbeschaffungsmaßnehen,* own translation) especially for the long-term unemployed, in order to get them back into a fulltime job in the medium to long run (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2868). To that effect, Hartz3 also introduced financial incentives for companies to hire unemployed workers of up to 1300 Euros if they have higher education qualifications and up to 900 Euros for unqualified workers. These incentives were increased and prolonged if the workers were over 55 years old or had disabilities (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2868-2869).

The Hartz3 Laws also significantly increased the requirements as well as the authority of supervision of the FEA towards both the employer and the employee. The employee is now required to submit proof of successful progression at work or at the education facility, which the FEA is funding. The FEA itself may visit the company to verify said progress. The FEA was also given authority to visit the companies, which employ temporary workers as well as view their books and their evaluations of the worker. This authority further extends towards third party agencies to the extent that they were responsible for the placement of the temporary worker (Deutscher Bundestag, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, 2870-2874).

The Hartz3 laws were the first changes of the social framework that directly impacted the German people. The Hartz3 law was the first half of the reform package that impacted the state's relation with its citizens and redefined the state's duty of care and the citizen's duty to care for himself. The measures comprised within the Hartz3 reform still contain some social democratic principles like the work procurement measures. I would consider the Hartz3 reform to be as far as the reforms would have gone had the SPD manifesto been applied.

4.6.4 The fourth Hartz law

Hartz4, which was being implemented throughout 2005, the last year of the Schröder government, was the most controversial of the Hartz laws. The Hartz4 laws implemented some of the central themes of the SPD manifesto, the Third Way document and Schröder's state of the nation address. This specifically refers to the implementation of Dole1 and Dole 2 as well as toughening the existing regulations on workplace rights and redundancy securities as well as tougher requirements on the use of personal wealth to secure a decent living.

Hartz4 unambiguously redefined the new stance by the German government towards their provision of social security. The concept of “fördern and fordern”, although present in the other Hartz laws, enacts more draconian measures than the previous laws. Although effecting changes in the majority of SGB’s, the Hartz4 laws focus particularly on the SGB II, basic care for the unemployed. In 11 chapters the Hartz4 law modifies the previously existing rules and regulations concerning basic care provided to the unemployed (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a).

Throughout the different SGB’s the term “Arbeitslosenhilfe” (“unemployment help”, own translation) is being replaced with “Leistungen zur Sicherung des Lebensunterhalts nach dem Zweiten Buch Sozialegesetzbuch” (“services regarding the securing of the personal livelihood according to the SGB II”, own translation) (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a). Chapter 1 of the Hartz4 laws is emblematic of this changed conception.

> The basic insurance for the unemployed shall strengthen the personal responsibility of the unemployed and their dependents and contribute to their ability to take care of their own wellbeing independently of the basic insurance. (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2956)

This statement in and of itself seems a quite reasonable statement to make. However, the paragraphs that follow in this chapter strike a much more stern tone. Hartz4 requires that all people within the household who require aid need to use every legal way to achieve their own financial survival before any aid is granted. If a job cannot be found by the jobseeker within a reasonable timeframe, the jobseeker is required, in order to continue to receive basic coverage, to take any “reasonable” job offered by the employment agency or a third party. Any and every effort should be made to get people back to work before benefits are to be paid out with special priority being given to unemployed youth (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2956).

> Contributions towards the sustaining of a living wage can only be provided as far as the financial aid necessary cannot be provided through another source (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2957).

Only in special cases, where non-payment would cause severe and undue burden on the claimant, can benefits be continued to be paid out without equivalent effort. However, these payments will take the form of a loan to be paid back later (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2958). The definition of what constitutes a need for basic benefits remains broadly defined but is complemented by previous definitions in the Hartz1-3 laws.

The point that caused the greatest discussions, and with good reason, is the definition of reasonableness. The only exceptions for a job to be a reasonable proposition are, if:

The person is physically, mentally or morally unable to do it.

1. If a job would prevent him to return to his previous line of work which was particularly taxing.
2. If the job would imperil the education of a child below 3 years old. Children of 3 and above should be given priority access to day-care centres.
3. If the job would endanger the care of a dependant who cannot be cared for by other means.
4. Any other important reason that would prevent a person from taking the job (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2958).

These exceptions *do not* include:

1. If the job offered is not in the area of competence of the person.
2. If the job tasks are below the qualifications of the person.
3. If the job proposed is further away than the previous job.
4. If the job benefits and pay are lower than in a previous employment (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2958).

Though many of these points are reasonable requirements on their own, the combination of these points does indicate callousness towards personal circumstances as well as a devaluation of individual competencies for the sake of employment and cost reduction. The efforts in cost reduction are particularly obvious looking at the further conditions the German state poses on the payment of those basic benefits. People were required to dig into their personal wealth (if there is any) in order to pay for their own upkeep. Having said that people will not be asked to sell their homes or other valuable assets as long as their sale will put undue burden on the persons (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2959).

Hartz4 is not all about the reduction of payments: it also further expands upon prior strategies and principles for getting people back to work. It is reminiscent of neo-liberal politics since each jobless person is required to sign a contract with the jobcentres defining the services being rendered to him as well as the requirements imposed on him in return (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a, 2560).

A further point of contention in this Hartz4 law was the definition of what Dole2 actually comprised. In Hartz1-3, Dole2 was defined as a reduced version of the standard Dole1 payments but not time limited as Dole1. Dole2 varies in its amount and coverage depending on the earnings of people to whom it is paid to supplement any requirements that the employment cannot fulfil (Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003a 2961-2963). This was made even more contentious by the fact that Dole2, which already was a scaled back version of Dole1, was allowed to be scaled back even further by up to 30% of the total amount received by Dole2 (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt). These measures where designed as another incentive to people who are unemployed to conform to the conditions set by the job agencies.

I consider non-decisions by the German government to allow the Hartz Commission to reform the framework of the state relationship with its population to be a contributing factor within the creation of the Hartz4 reforms. Without the intervention of the German state, in fact with the aid of the German state (since it passed the laws enforcing these proposals) market forces were able to strongly influence the state’s own reconceptualization of its own understanding of its role within society.

4.7 The Good the Bad and the Ugly

With a socio-economic reshaping of this magnitude, it is unsurprising that there were a host of differing opinions on the necessity and validity of this new regulation. Considering the size of the reforms and the speed with which they were done, there are a number of points that are of particular importance in the analysis of the Hartz laws. This section analyses how the German establishment has perceived these changes to the social security system. This section will evaluate what the qualitative impacts of the Hartz reforms were before analysing in the following chapter what the quantitative impacts were.

The German government, led by the SPD/Green coalition, in their second term in office vowed to enact into law every point that was raised by the Hartz Commission; in reality about two thirds of the proposals were enacted or were being prepared for enactment (Siefken 2006, 386). Considering the close connection of industry, labour, state and banks, whose connection enabled the economic growth during the 1950s until the 1980s, the major changes to such deep socially embedded programmes such as welfare and unemployment benefits, brought with them significant opposition within the political and social arenas. The price paid by the 2nd Schröder government was its premature end. Leftist theorists argue that the Agenda 2010 was a market- based legalisation of poverty (Osiander 2010; Schmidt 2008, 166) and that there is an argument to be made that the reforms were not as market-oriented as is often argued.

The combination of the unemployment and the social aid into Dole2 and the reduction of the payments from Dole1 were a significant step in helping reduce unemployment in Germany (Osiander 2010; Blum 2008; Horn & Logeay 2008; Hinrichs 2007) since it helped the state in a number of ways. On the one hand, it significantly reduced the state's unemployment costs. On the other hand, the reform allowed the state to simplify the procedure to get any kind of unemployment benefit. To this, one needs to add the changes in the dismissal protection, limits to social aid and reasonableness of offered employments (Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt – Viertes Gesetz für Moderne Dienstleistungen am Arbeitsmarkt 2002-2003; Blum 2008). However, bureaucracy was not reduced by as much as expected since the government still tries to determine how much (or how little) wealth a person needs to continue to live a humane life. Furthermore, considering the reforms that were implemented with the Hartz laws, the government needs to maintain a large staff, tasked with investigating to what extent people are deserving of government aid with respect to the tasks and jobs they are fulfilling.

One of the criticisms, which were levelled against the Agenda 2010 at the time by the political left, was that it was unfair towards those people who have paid into social insurance, in this case unemployment insurance, for their entire working life in order to only get a "mere" 12-18 months in return. This argument is commonly countered by the argument that, as insurance, unemployment insurance is not meant to be a savings plan for people to fall back on. It provides a cushion against hardship for the time a person is out of work and is looking for new work (Franz 2008). Furthermore, the agenda redefined what it meant to be unemployed to both people out of work and people still in work. With the changes to the concepts of what was an acceptable job (Hinrichs 2007) and the expansion of low income jobs (Franz 2008) put new stresses on the working population.

> … about three fifths of former unemployment assistance recipients can be regarded as 'losers', in particular those who had high earnings before becoming unemployed, whose spouse/partner has full-time employment or who live as singles. Winners include lone parents and those who lived on low unemployment (assistance) benefits and failed to claim additional social assistance to which they were entitled. (Hinrichs 2007, 227)

The low-income job element is a particularly troubling element of the Hartz reforms. Low income mini jobs and other types of low income jobs designed by the Hartz laws could potentially undermine those employed positions that normally would be paid at the standard industry wage level. One of the ways this undermining is achieved is through government intervention. By adding Dole2 to the pay of someone whose employment does not pay enough for him to survive on that salary alone, the salaries that companies have to pay are artificially lowered. A consequence of these downwards job pressures are the reinvigorated calls by the left for a countrywide minimum wage, which would prevent these types of government sponsored low income jobs (Osiander 2010).

Mini Jobs create downward pressures on salaries. This is manifested in the reduced bargaining power of employees (Horn & Logeay 2008), especially at the low qualification end of the jobs market, whose wages are above that of a mini-job but have similar qualifications to those Mini Jobbers. These Mini Jobs make everybody worse off since they force people to work for very little money and force other people to accept lower wages or risk being replaced by a person taking a Mini Job (Franz 2008, Jann & Schmidt 2004). Studies (Osiander 2010) show that, due to the liberalisation of the labour market, people in both east and west Germany have been willing to suffer a wage cut or start with a much lower salary than before these reforms have been instituted (Osiander 2010). This is also one of the reasons why wage flexibility especially at the lower earnings (unskilled labour) end of the scale has increased (see

Chapter 6), which in turn also increased the number of people who earn much less than the national median wage (Hinrichs 2007).

Furthermore, these downward pressures on incomes tend to be asymmetrical. These pressures are biggest with people who have few to no qualifications and lowest with people who are highly qualified. This increased flexibility in wages has its advantages for the economy but nevertheless has severe effects on the people in society. These wage pressures tend to create a vicious circle of low wage employments, and continued low levels of qualifications throughout several generations (Osiander 2010).

Economic discussions help illustrate this point. The discussion follows the line of argumentation already investigated in Chapter 2. Market liberals and monetarists argue that reduced payroll costs would increase profits, which would spur production as well as greater hiring, thereby increasing growth (Friedman 1962, 1991). However, this logic does not address the issue of the level of pay people receive, nor does it take account of the fact that that level of pay may not be enough to sustain that person. Nor, finally, does it take a wider view of the issues related to income disparity such as quality of life or social advancement or the greater concentration of income at the top.

Keynesians and classical liberals partly address this problem of low wages. They do agree with the logic of the argument that lower wages stimulate growth and consumption. Keynesians and classical liberals do, however, point out that such low wage levels would be of much more benefit to a small economy with no significant internal market. Keynesians argue that in a large economy with a significant internal market, downward pressures on wages would compromise the internal consumption of that nation and with it any ability to sustain or further increase economic growth because of the reduced buying power of the population. Therefore, Keynesians argue for compensating measures to be taken to relieve these pressures (Horn & Logeay 2008).

Social security, which was another big part of the Agenda 2010, was successful in implementing an increase in the pensionable age. As of 2012 the pensionable age is increased to 67 years (hen/dpa/ddp/AP 2007) as has been pointed out above, this increase in the pension age is only the latest increase since in 2001 the pension age had already been raised to 65 years (Lampert 1992)

Though designed to reduce unemployment, the redesign of the FLO into the FEA has meant that the government also put more responsibility into the FEA's hands. Providing it with a managerial structure of governance for its day-to-day activities (Hinrichs 2007, 222) as well as more service-oriented structure, this was supposed to help get people back into work. This change of the FLO into the FEA is an excellent example of the application of the neo-liberal narrative. Since private companies are more efficient than government institutions because they are incentivised by market success and customer satisfaction, a privatized employment office would be more successful at placing people (Crouch 2011). This recasting of the FLO into the FEA with its new structures was also a way to redefine the work that it does. It is no longer there to *care for* the unemployed but to *manage* unemployment. Since the FEA now has to an extent become a private agency following the changes made to its working structure, it now has to conform to targets; if it does not, then it is fined.

These negative incentives are imposed on the agency and its local offices if they do not meet their targets of getting people back to work. These fines are essentially equating efforts to success, which is not always causally linked since it may involve a variety of causal variables. There usually are also structural problems to be considered. This is especially true for the long-term unemployed. Because of the negative incentives as well as the multitude of issues with long-term unemployment, it has become more attractive as well as more cost effective for FEA offices to forsake concerted efforts for the long-term unemployed and pay the 10.000 Euro fine to the unemployed before transferring them to the Dole2 system. This is what is known as "Aussteuerung" (Legnaro 2006, Zimmerman 2008). This is especially tragic since the long-term unemployed are *the* target group, which the Hartz laws tried to reduce. Thus the incentive structure established to ensure that the problem of long-term unemployment is tackled actually has the opposite effect and ensures that the issue remains unresolved by making it cheaper to pay for long-term unemployment instead of paying for reintegration into the jobs market.

4.8 Conclusion

This chapter provided an analysis of the political-economic situation in Germany before, during and after the Agenda 2010 reform package. This reform agenda saw the implementation of social security and unemployment reforms through the implementation of the Hartz laws. Before any analysis of the economic and social repercussions of the Hartz laws was undertaken, this chapter looked at the German constitutional legal framework, which allowed these laws to be enacted in the first place.

The German constitution (GG) provides the people with the *entitlement of* social security but not with a *right to* social security. The text was written with enough vagueness to allow the legislator to define social security as well as the requirements necessary to receive it in a manner that suited the economic situation of the time and could range from a near fully communist- to a near fully market-oriented economy. The constitutional points which deal with the question of social security contributions are based on the self-limiting government tradition established in Germany (Dyson 2009), which allows the government a flexible definition of what it may consider to constitute a provision of care to its working and unemployed population depending on the economic situation of the country. The only explicit safeguards are that the government is not allowed to provide no measure of care whatsoever, or take over complete control over all socio-political-economic activities. This should be considered as a great achievement in foresight since it enabled legislators to adapt social security legislations to the economic times the country faces.

Additional to the constitution, the 13 SGBs provide the concrete framework for the different provisions the people were entitled to. They also help specify under what circumstances what types of benefits can and should be provided to people. It was the vagueness of the constitution on the issue of welfare and social care that allowed these 13 SGB's, which allowed the SPD/Green government to significantly modify the existing social security and unemployment laws with by the Hartz laws.

Before the Hartz reforms were enacted, the duties of the German state were constituted of duties of care towards its population, its working population in particular. The pre-Hartz era used classical economic tradition of demand side economics, and used in the Beveridge plan to manage unemployment and attempt to get people back to work. The pre-Hartz policies empowered employed as well as unemployed people equally.

While the motor of the German economy lay within the “Bank-Industry nexus” (Dyson 1983, 141), the German state also empowered industry by providing a legal environment that protected industries from bankruptcy and allowed them the opportunity to enact restructuring programs to resolve their issues.

The German state helped maintain an equal burden sharing framework, by helping the employed maintain their bargaining power and the power of the labour unions, and the state helped the unemployed by offering re-education courses, loans and advice on labour market trends as well as offering help to people who want to start their own business. The most important portion of the help provided to the unemployed by the German state was the provision of unemployment aid and unemployment help, which empowered the unemployed to look for jobs that suited them in terms of pay, qualification and (to a certain extent) fulfilment. The German state also provided help to its industry and maintained close links to unions and industry to provide a platform for discussion and negotiation in case crises arose.

Considering these labour empowerment policies, the Hartz reforms which were very deep cutting reforms of the labour market and significant unemployment benefit reductions that were instigated by the SDP, which has strong ties to unions and other worker organizations, came as a surprise for many people.

This chapter suggested that the decision of the SPD not to continue developing their concept for reform, which they had begun with the 1998 SPD manifesto, was due to the structural pressures of the neo-liberal economic concept. This change of the reforms where instigated by the structures of industry which were using the neo-liberal argument to discredit the notion of an efficient state service provision. This allowed the industry to put forward a reform proposal since the German state tradition included a self-limiting state to allow for individual actions to find the best solution. The global economic setup and the EU institutions further reinforced these neo-liberal notions and gave them further structure.

Instead of continuing to develop its re-conception of the state’s duties, the Hartz Commission was tasked with that duty. The plan by the Hartz Commission was in many instances based on the SPD manifesto as well as original ideas developed by the Commission itself. These ideas shift the tone of the reforms further to the right of the political and economic spectrum and further in line with neo-liberal orthodoxy. This becomes especially apparent when one, looks at the language of the laws introduced by the SPD/Green government.

The most significant law enacted by the Agenda 2010 combined different unemployment and social benefits into two different payments of Dole 1 and Dole 2; Dole 1 running for up to 18 months and Dole 2 running indefinitely but providing far fewer benefits than the social insurance that came before it. This has been one of the main points designed by the Commission and enacted into law by the SPD/Greens to reduce long-term unemployment.

With this restructuring of the unemployment benefits, also came incentives to get more people on benefits back into work. These incentives included, aside from a now finite amount of time someone was allowed to receive full unemployment benefits, the redefinition of what work is acceptable for people to be doing regarding their qualifications. The restructuring of the incentives for work also includes the restructuring of the Unemployment Office into the Unemployment Agency designed to providing better services to the unemployed. The restructuring also reduced the amounts of wealth people are allowed to own before they receive benefits. It furthermore includes incentives for setting up individual businesses as well as creating new types of low paid and contribution free work.

All of these incentives (positive and negative) follow from the leitmotif “fördern und fordern” (Deutscher Bundestag, Viertes gesetz für moderne dienstleistungen am arbeitsmarkt, 2003, Article 1, Kapitel 1). This concept is in and of itself not a bad principle since it implies rewards for services rendered, however, the way this concept was applied into law especially with regards to the reduced contributions, the lowered free amounts and the liberal interpretation of the concept of “acceptable work” does leave these Agenda 2010 reforms open for criticisms regarding the unequal relationship between the rewards received and the rewards rendered. All of these actions promote a conclusion arguing that *employed as well as unemployed people are now no longer at the centre of the economic process but are now conceived of as just another part of the economic processes* whose expansion is of primary importance and not the workers who achieve that progress. Thus, workers are being sanctioned if they do not show enough efforts in their search for new employment thereby becoming a drag on the economy.

This puts an undue burden onto the unemployed and employed alike, increasing the pressures on both of those parties to become more efficient in their tasks and do so with less bargaining power than before the reforms. This provides further weight to the notion that these reforms are an example of the changes in structural power between the state and the markets. As pointed out in Chapters 2 and 3 the German government with the application of these reforms has ceded to the pressures of neo-liberal ideology.

In the way it was enacted in Germany, the principle of “fördern und fordern” (Deutscher Bundestag, Viertes Gesetz für Moderne Dienstleistungen am Arbeitsmarkt, 2003, Article 1, Kapitel 1), though having seemingly positive effects on the economy (see Chapter 5), did have negative effects on the social makeup of society as the final section pointed out (see also Chapter 5). The negative effects of these changes in the laws and organizational principles created with these reforms were to the disadvantage of the working population - in particular to the poorer segments of society. That this effect was deliberate is doubtful; however, the effects are nonetheless real.

The Hartz reforms were the result of a pragmatic attempted to align two different economic conceptions with one another in order to enable markets to operate more effectively. However the problem with that concept is that the German state failed to keep control over the entire process as it allowed market forces to influence the shape of the reforms. Had the German government kept greater control over the reform process the reforms might have had more balanced socio-economic results. The positive economic consequences of these reforms were the validation of the German argument for austerity conditions to be imposed on struggling Euro Zone countries. These reforms have changed the way the role of the government is viewed in Germany since it presided over a paradigm shift in the provision of services to the workforce and redrawing the balance of power in favour of industry and banks.

The German Hartz reforms are a very good example of austerity-based reforms. The following chapter analyses, using quantitative data, what affect exactly these reforms had on the German economy. This analysis provides the explanation as to why the German government so stubbornly holds onto its austerity conceptions.

Chapter 5 The Hartz reforms: socio-economic consequences for Germany and an argument for European austerity?

5.1 Introduction

In this chapter I provide empirical evidence to my argument that the Hartz reforms the German government implemented between 2001 and 2005, were a form of austerity. This form of austerity was implemented, as explained in Chapter 4, in response to the evolution of the international market and the changes in structural power in the national and international sphere. As the previous chapters demonstrated, Germany is along with France one of the major economies within the Euro Zone. The German government is also the EZ's most important advocate for austerity.

As it was described in the previous chapter, the changes in structural power, which have changed the power relationship between the market and the state, have created a large amount of pressure upon the state to liberalise its processes and become more open to market influences. This was a process that proceeded through a number of phases such as the agreement on Monetary Union or the signing of the Maastricht treaty, whose economic impacts will be analysed in this chapter.

The first section of this chapter will consider the evolution of the German economy from the 1950s to 2005, focussing particularly on the unemployment rate and the economic performance of Germany. This is done in order to investigate the performance of the German economic system (see Chapter 4) up to that point i.e. before the Hartz reforms, to function within the international economy. This will provide an overview of why the SPD considered a reform of the concept of the state and of welfare to be necessary. This section will also consider how the social differences among Germans have developed during that time by considering the evolution of the income and the evolution of the risk of poverty before the Hartz reforms were implemented.

Within this first time period analysed, the second section will give particular focus on the years between 1991 and 2007, as it was in the beginning of the 1990s that East and West Germany became unified once again and that the EMU treaty was signed, which put two distinct types of pressure on the German socio-political-economic system. The second section of this chapter analyses the changed circumstances of Germany's reunification (from 1991-

2007) and the signature and application of the EMU treaty, in order to provide a more precise overview of the economic situation that prompted the reforms of the SPD/Green government (1998-2005).

The third section of this chapter will investigate the period of 2005 to 2013, this chapter will consider the trends within unemployment, GDP growth and other economic indicators to try and discern the socioeconomic impact that the Hartz reforms have had in Germany. This data allows the thesis to determine that the German economy has improved over that period, however, how much of this improvement can be attributed to the Hartz reforms cannot with certainty be ascertained. The analysis of this time period will also consider if the Hartz reforms have impacted positively or negatively upon the social trends in Germany.

This evaluation is complicated by the fact that Germany went through an economic upturn during the period of 2004 until 2008 when the global economic crisis engulfed Germany. Additionally any negative effects of these reforms would also be masked by the recession. Economic recession as a rule drags down every economic and social indicator. This period also makes a determination of the effects of the Hartz reforms on the employment market especially difficult, distinguishing between jobs created because of economic growth or by reform.

This analysis will show that the economic impacts of the Hartz reforms have allowed Germany to weather the 2007/2008 financial crisis and have helped Germany to become the best performing economy in Europe. Coupled with its alignment towards neo-liberal policies provides it with increased structural power over other EU and EZ members. Since these reforms were in alignment with neoliberal economic thinking, German structural power was able to further expand within the European power structure.

Because of the 2007/2008 crisis, Europe is now faced with a sovereign debt (fiscal) crisis and low (or lower) growth figures for the EU as a whole (Heitmeyer 2012). Therefore, in the final section, this analysis will consider the German investment within the Euro rescue the EFSF and the ESM, whose conditions on the receipt of those aides have been translated as an imposition of austerity by Germany upon other members of the Euro Zone. One of the reasons for that logic stems from a further avenue of structural power, which the European reaction to the crisis has opened, namely to set the conditions and requisites that a country must adhere to in order to be given that funding. It is because of the economic success of the Hartz reforms, which allowed Germany to weather the 2007/2008 financial crisis that the German government holds on to the austerity argument, which is imposed on countries under the protection of the EFSF and the ESM.

As this analysis will use data sets to evaluate the performance of the German economy throughout a period of time that has seen a number of social reforms as well as economic boom and bust cycles, data for this period of time is still relatively recent and subject to change as this analysis progresses.

Due to the complexity of the question set in this thesis, a large number of factors need to be considered in the analysis. Therefore, this thesis has decided to use a number of different data sets provided by different international institutions. These institutions include the World Bank, the IMF, the WHO, EROSTAT and the OECD. It also includes the German national statistics office DESTATIS and the Poverty and Wealth report compiled by the German government.

The SPD published a “Poverty and Wealth Report” (own translation) during their first term. To this day there are four of those reports written, providing an overview of the German economy and of society. The first report was published in 2001; the second in 2005, the third in 2008 and the fourth was being completed in 2012 (a copy of a draft (17.09.2012) is used in this analysis). This report is a political document and, as a recent article in the German *Der Spiegel (Janssen 2013)* shows, is not safe from tampering. The version of the report from November 2012 no longer contains some of the more negative evaluations of the statistics collected in this report, which were still contained in the September draft (here analysed). This thesis uses the statistics contained within these documents as independent researchers and institutes have developed these statistics. This thesis only utilises the government evaluations as a comparison and basis for discussion. This analysis will furthermore rely on data, which uses the new OECD scale, and not the old OECD scale (OECD 2013c), to ensure consistency across the study.

> OECD equivalence scale. This assigns a value of 1 to the first household member, of 0.7 to each additional adult and of 0.5 to each child. This scale (also called the “Oxford scale”) was mentioned by the OECD (1982) for possible use in countries that have not established their own equivalence scale. This scale is sometimes called the “old OECD scale”. (OECD 2013c, 174)

> OECD-modified scale (here referred to as new OECD scale own addition). After having used the “old OECD scale” in the 80s and the earlier 90s, in the late 90s Eurostat adopted the so-called “OECD-modified equivalence scale”. This scale, first proposed by Haagenars et al. (1994), assigns a value of 1 to the household head, of 0.5 to each additional adult member, and of 0.3 to each child. (OECD 2013c, 174)

Using this many different data sources may lead to some of the data not being 100% verifiable with other data sources used. However, these are all well regarded international institutions, which use these same statistics in their own models, wherefore this thesis is confident that the data provided by them is accurate. Therefore, if multiple statistics demonstrate the same trend, it will be considered by this thesis as accurate even if the numbers themselves do not match. The conclusions reached in this thesis will be based on these numbers.

This chapter concludes its analysis of the consequences of German austerity by investigating how much Germany has actually invested within the ESM and the EFSF to demonstrate how powerful Germany is within these institutions. This will help in the determination of how much heft Germany has and how likely it would be that Germany’s demands are being acceded to in terms of austerity implementation.

5.2 Germany in the 20th Century

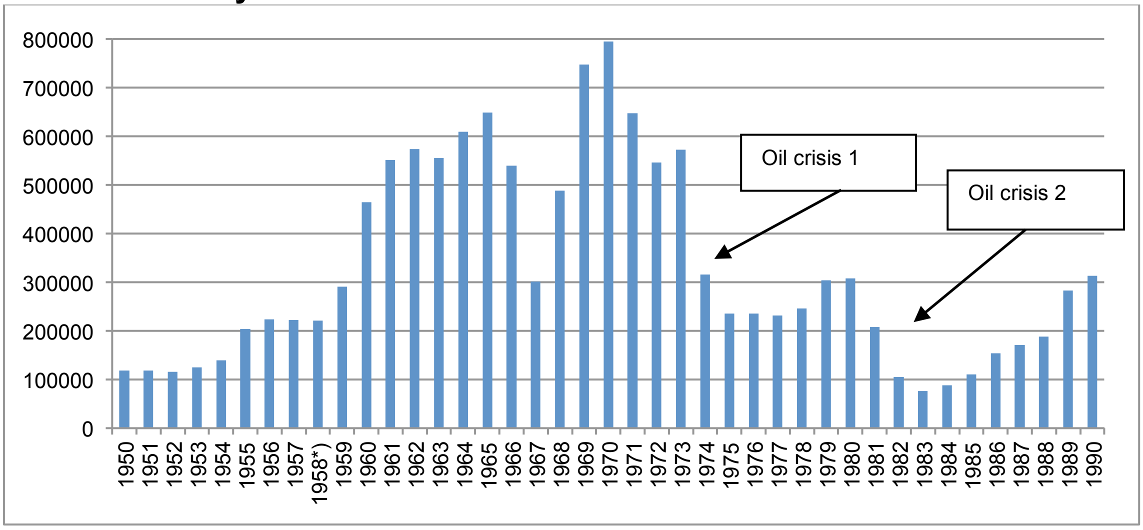
Germany is a nation with a turbulent past. The scars given and received from their involvement in the two world wars of the previous century define its modern history. Germany’s actions and reactions on many national and international issues are to this day informed by those consequences.

5.2.1 Germany between 1950 and 2005

After WW2, France, the UK, the USA and the USSR occupied Germany. It was eventually divided into East and West by the superpowers at the time, the USA and the USSR, once their ideological differences became too pronounced. This division claimed thousands of lives over the 40 years of German separation and it was only after the reunification of Germany that its painful past found some measure of closure. Throughout the time East and West were separated, West Germany witnessed an unprecedented level of growth in wealth, economic output and living standards for large sections of its population as the Keynesian system that was used in Germany spread the accumulated wealth throughout society in a more or less even fashion.

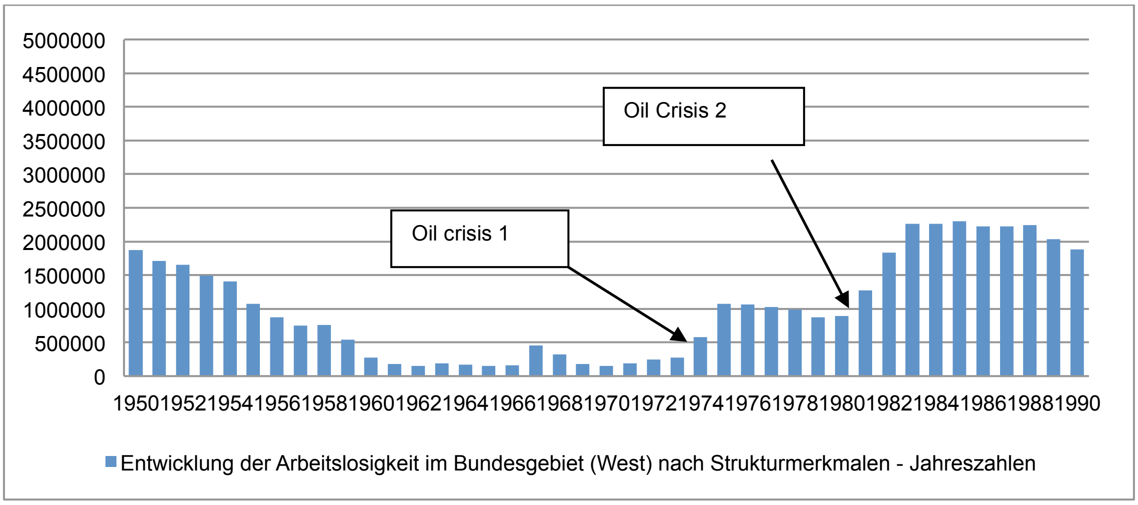
However, the 1970s saw this period of growth come to an end. The oil crisis of the 70s caused significant economic losses around the world. With the drastic rise in oil prices, many industries that benefitted from cheap energy prices, allowing for larger production quantities and consequently cheaper goods, were forced to decrease production or increase prices. Other industries, which relied on oil as a primary or secondary resource in their production process, faced that same problem. Global output diminished, through reduced demand (i.e. an increase in price) or through reduced supply (i.e. reduction of the quantity produced) or a combination of both factors. A further consequence of the increased oil prices was a contraction of the jobs market and a sizable increase in the number of unemployed people (see Table 5.1 & 5.2). This in turn resulted in an important increase in the provision of unemployment benefits and other types of welfare, which had to be paid for through increased borrowing and causing accelerated inflation.

Table 5.1 Payroll Jobs between 1950 and 1990 - Annual Numbers



1958*) addition of the Saarland to Germany
Bundesagentur für Arbeit (October 2012 data) accessed 14 11.2012 (own calculations and annotations

Table 5.2 Evolution of the Unemployment rate in West Germany - Annual Numbers

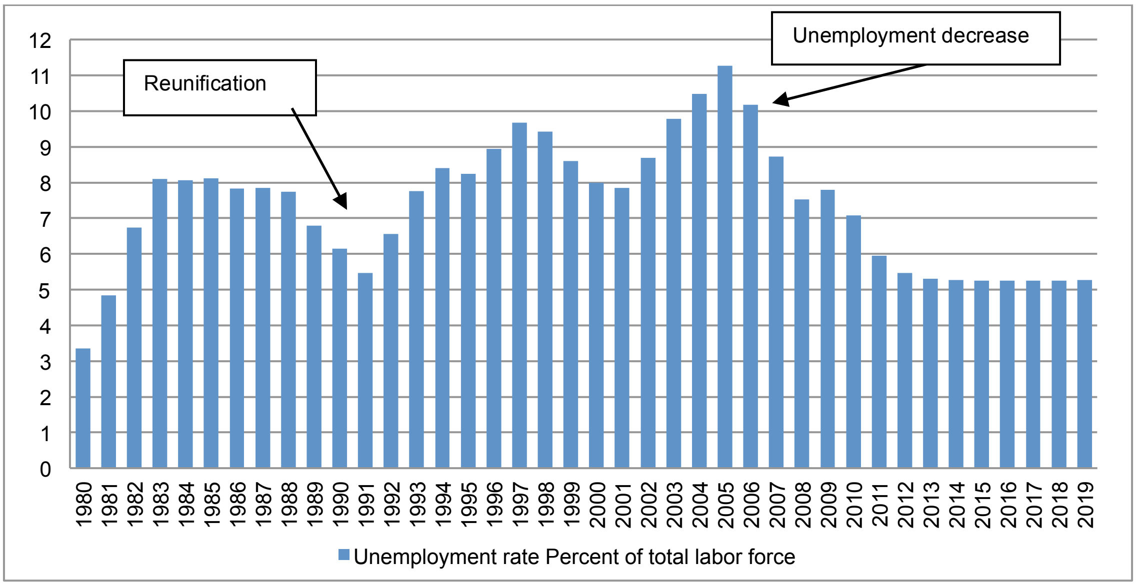


Bundesagentur für Arbeit (October 2012 data) accessed 14 11.2012 (own calculations and annotations)

The oil crisis was a major contributing factor to the global economic recession, which started in the late 70s and became an acute crisis in the early to mid-80s. As was argued in Chapter 3 the crisis was not managed by the USA or the EU, which would have been within their power to do. This failure to intervene as argued in Chapter 3 allowed the market to gain in power and responsibility in managing the international economy. The oil crisis was also the first serious challenge to the established socio-political-economic system within Germany.

As Tables 5.1 & 5.2 show, after a slight fluctuation in the unemployment rate between 1976 and 1980, the number of people without employment (in West Germany) more than doubled between 1980-1984 in real terms and increased by almost the same amount in nominal terms (see Table 5.3). After a marked decline of unemployment in the final years of the 1980s, the unemployment rate started to climb again to new heights throughout the 90s after the reunification of Germany.

Table 5.3 Unemployment rate (% of Labour force: Germany 1980-2019)



IMF time series data: Monetary Fund, World Economic Outlook Database, October 2014 (accessed 16.10.2014)

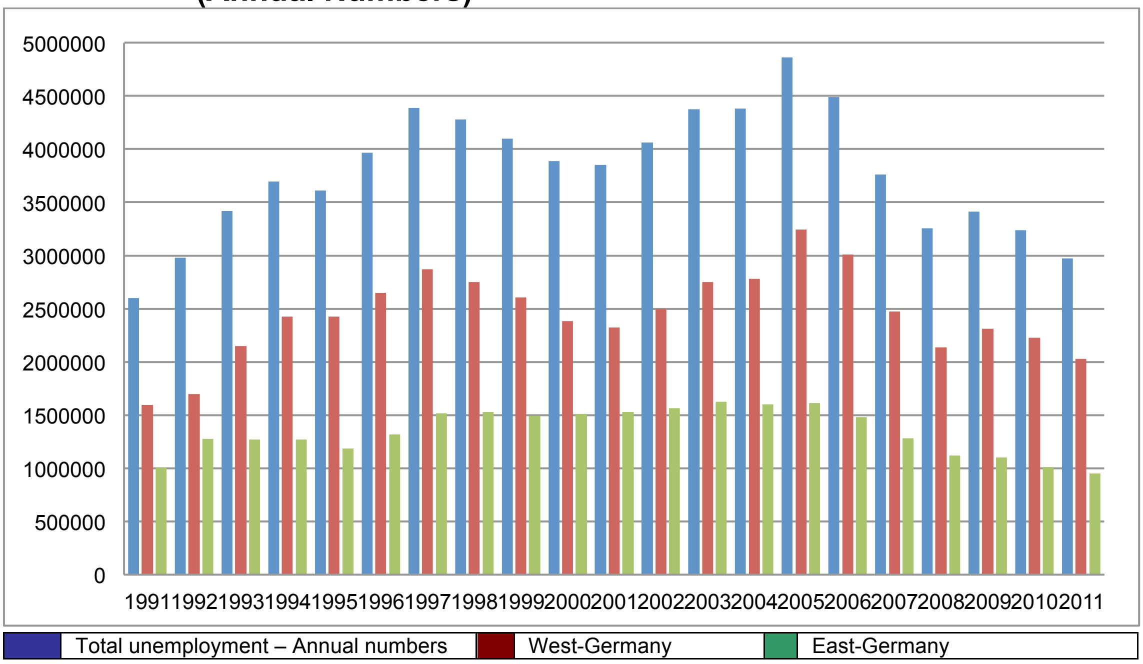
5.2.2 Germany between 1991 and 2007

At the end of the 1980s and the start of the 1990s, West Germany achieved reunification with East Germany. The processes of reintegration of the East and West German states lasted throughout the 1990s and into the early 2000s and came with significant economic costs for West Germany. Since East Germany was occupied by and had aligned with the Soviet bloc, East Germany, suffered from an underdeveloped economy and underdeveloped infrastructure. From 1991 to 1997, unemployment almost doubled to an unprecedented level of almost 10% in 1997. Tables 5.3 & 5.4 show the increase in unemployment in Germany after 1991 due to the addition of the unemployed from East Germany to the statistics of the unified German Federal Republic.

Both the oil crisis and the German reunification put significant pressures on the German economy. These pressures might have been reduced if the state had reformed the labour market to allow greater flexibility in employment conditions. As Tables 5.3 and 5.4 also show, this increase in unemployment was not a temporary increase linked to economic performance but was a structural problem, as unemployment remained high throughout the 1990s and early 2000s. If data from Table 5.5 is added, one can see that the fluctuations in the West German unemployment rate almost exactly match those of the number of employments provided, shown in Table 5.5. This shows that Western markets were more responsive to upturns than Eastern markets, which required continued investment in the form of unemployment assistance causing a continuously high economic burden to the federal government.

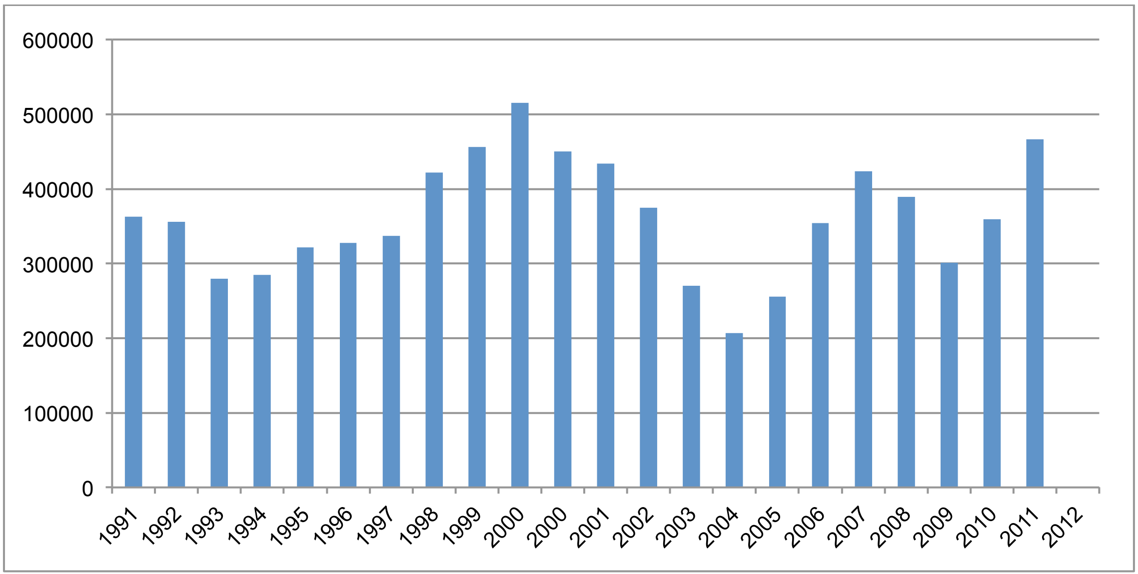
The greater variance in the unemployment numbers also underscores the different economic systems within which East and West Germany were operating until the 1990s. The numbers for West Germany show a variation of the level of unemployment commensurate with economic performance. This data does suggest greater flexibility within the West German employment market. This in turn is suggestive of a more important neo-liberal influence within Western Germany. However, the combination of an economic slowdown and a German state unable or unwilling to adapt to that situation by further liberalising its socio-political-economic structure, caused a stagnant economy and an increasingly worsening labour market. This resulted in a high rate of unemployment throughout the 90s and early 00s.

Table 5.4 Evolution of the Unemployment rate in Germany (Annual Numbers)



Bundesagentur für Arbeit (October 2012 data) accessed 14 11.2012 (own calculations)

Table 5.5 Reported openings from 1991 until 2011 (Annual Numbers)



Bundesagentur für Arbeit (November 2012 data (accessed 14.11.2012) (own calculations)

In the years from 1993 to 1998, the median German income increased by 200DM from 1527DM to 1727DM. The median income in West Germany increased from 1651DM to 1822DM whereas the East German median income increased from 1178DM to 1435DM (see Table 5.6). This does show that a convergence of incomes has happened over this time as the median income difference between East Germany and the median German income has almost halved over these 5 years. This is a testament to the continuing efforts of integration of both east and west during that time. The constant unemployment rate in East Germany does, however, show that this imported West German employment model without any type of reform of the East German labour market caused an increase in the contributions the federal government had to pay.

The data thus far suggests that both events had a significant impact on the German political-economic model. While West Germany may have been able to adapt to the economic changes East Germany was unable to do so at the same rate. The result was that the German government needed to spend a significant amount of its resources over the following years to maintain its social security commitments. This was the point where the German state took notice and re-evaluated its presence within the economy. This provided access to the neo-liberal concepts in the guise of industry and EU influence within the German state's re-evaluation of its standing within society.

Table 5.6 Alternative Poverty limits (in DM/Month) 1973 until 1998

	1973	1978	1983	1988	1993 [1]			1998 [1]		
	West Germany only				West	East	Total	West	East	Total
	New OECD-Scale									
50% / mean [2]	592	808	1.040	1.176	1.557	1.057	1.458	1.707	1.295	1.628
50% / median	527	722	939	1.060	1.376	982	1.273	1.519	1.196	1.439
60% / mean	710	970	1.248	1.411	1.868	1.268	1.749	2.048	1.553	1.953
60% / median	632	866	1.127	1.272	1.651	1.178	1.527	1.822	1.435	1.727

Source: Hauser. R. und Becker. I.: Einkommenserteilung im Querschnitt und im Zeitverlauf 1973 bis 1998

1. 1993 and 1998 the values in the sections "West" and "Ost" relate to the mean within that section. The section "Total" relates to the mean for all of Germany
2. mean: arithmetical mean

Deutscher Bundestag (Extract from table Alternative Armutsgrenzen in (DM / Monat) 1973 bis 1998) (2001, 38)

Table 5.7 Alternative Poverty Averages (in %) 1973 to 1998

	1993		1998		1993			1998		
	West	East	West	East	Total	West	East	Total	West	East
	Respective mean for east and west [1]				Complete German averages [2]					
	New OECD scale									
50% / mean[3]	9,7	2,9	10,6	4,8	9,6	7,6	17,9	10,2	9,1	14,7
50% / median	6,2	1,8	7,1	2,9	5,6	4,7	9,3	6,2	5,6	8,5
60% / mean	18,6	9,1	18,9	11,9	19,0	14,8	36,2	18,7	16,3	28,9
60% / median	12,0	6,1	13,1	8,4	**(11,7)**	9,1	**(22,0)**	**(12,5)**	11,0	**(18,7)**

Source: Hauser. R. und Becker. I.: Einkommenserteilung im Querschnitt und im Zeitverlauf 1973 bis 1998

1. The particular middle values: the middle values are the ones of the particular parts of the country
2. Complete German middle values: the particular distributions of the part of the country as well as the general division middle values will be measured on the middle for all of Germany
3. Middle: arithmetical middle

Deutscher Bundestag (Extract from table Alternative Armutsquoten (in v. H.) 1973 bis 1998) (2001, 39)

Table 5.7 shows that another effect of the reunification and the export of the West German employment model to East Germany did have a serious impact on the poverty rates in the East. Although overall poverty for Germany increased from 1993 to 1998 by **0.8%** (own calculations from brackets), the East German poverty rate fell by **3.3%** (own calculations from brackets). Although there was no discernible effect in employment ratios during that time, the people who were employed did earn more and were able to move out of poverty.

Despite this positive picture, Table 5.8 demonstrates that starting in 1978, the share of the growth in income grows ever smaller for the bottom decile of the population. In 1978 their share consisted of 0.46% of this increase, in 1998 their share was only 0.39%. *This does demonstrate that before the election of the SPD in 1998, the size of the economic inequalities between people was becoming greater even though the federal government was* *spending large sums of money trying to level the playing field between east and west as well as trying to get people out of unemployment.*

The fact that inequalities became greater even though the government was spending more funds on the unemployed and on social security provided a good argument for the state to re-evaluate its social security commitments. The following tables will demonstrate the social distribution of the social security provisions by the state during that time.

Table 5.8 Net Equivalent Income, nominal and real 1973 to 1998 (in DM/Month)

Year	New OECD scale					
	Arithmetical mean		Bottom decile		Share	Price index 1995 = 100
	Nominal	Real	Nominal	Real		
1973	1.183	2.459,46	544,18	1.131,35	0,46	0,481
1978	1.616	2.671,07	743,36	1.228,69	0,46	0,605
1983	2.080	2.711,86	873,60	1.138,98	0,42	0,767
1988	2.351	2.891,76	963,91	1.185,62	0,41	0,813
1993	3.113	3.249,48	1.245,20	1.299,79	0,40	0,958
1998	3.414	3.279,54	1.331,46	1.279,02	0,39	1,041
Increase from 1973 to 1998 (in %)	188,59%	33,34%	144,67%	13,05%		

Source: Hauser, R. und Becker, I: Einkommensverteilung im Querschnitt und im Zeitverlauf 1973 bis 1998 sowie eigene Berechnungen
1 Share of the bottom Decile of the Total net equivalent income
Deutscher Bundestag (Extract from table Nettoäquivalenzeinkommen nominal und real 1973 bis 1998 (in DM/Monat) (2001, 40)

Table 5.9 Number of people receiving on-going income support at the end of 1998

Percentage of Recipients **- Share of the recipients of social aid of the respective population in% -**	
Men	3,2
Women	3,8
Germans	3,0
Foreigners	9,1
Children (under 18 years)	6,8
Older people (65 and older)	1,3
Old Federal Republic	3,7
New federal states and East Berlin	2,7
Total of people receiving income support	3,5

Source: Statistisches Bundesamt, Sozialhilfestatistik
Deutscher Bundestag (Extract from table Empfängerquoten laufender Hilfe zum Lebensunterhalt am Jahresende 1998) (2001, 70)

Table 5.9 shows that in 1998 the total number of people receiving income support was 3.5% and that of those 3.5 %, looking at the first three columns of Table 5.9 the recipients were in large majority foreign nationals, female and under the age of 18 living in West Germany. This statistic suggests that foreign nationals who have come to Germany usually are employed in low cost jobs.

Table 5.10 Earnings status of recipients of income support aged between 15 to 64 years of age in Germany for the end of the Year 1998

Employment status		Shares in %	Count
Employed (8,4%)	Full-time	3,9	69 000
	Part-time	4,5	79 000
Unemployed (40,2%)	With right to work benefits	16,1	285 000
	Without right to work benefits	24,0	424 000
Not gainfully employed (51,4%) Because of	Training and advanced training	6,1	108 000
	Domestic Bound	15,7	276 000
	Illness	7,7	136 000
	Age	1,6	29 000
	Other reasons	20,4	360 000
Overall		100,00	1 766 000

Source: Statistisches Bundesamt
Deutscher Bundestag (Copy of the table Erwerbsstatus der Empfänger/-innen von Hilfe zum Lebensunterhalt in Alter von 15 bis 64 Jahren in Deutschland zum Jahresende 1998) (2001, 71)

Table 5.10 shows that people who relied most heavily on income support were people who were “unemployed” making up 40.2% or people who did not work for other reasons with 51.4%. Of the people who were not working, the single biggest reason given was because they needed to stay at home with 15.7%. What these statistics also show is a largely traditional society, where there is only 1 breadwinner and the partner is staying at home. The other part of the statistics show that low educated people are in the greatest danger of being unemployed and thus also at the greatest risk of poverty. The mini-job reform from Hartz 4 was designed to tackle that problem. Table 5.10 also shows that less than 10% of all people who were employed either full-time or part-time required income support. This statistic demonstrates an effective balance of pay and prices within the society.

Tables 5.11 and 5.12 provide a more precise breakdown of the distribution of social benefits among the population. Table 5.11 shows that people with little or no scholarly achievement lead the table on benefits (brackets). Approximately 50% of people who have a lower technical education degree receive income support, compared to only 18.6% of those who have a higher technical education degree and 8.4% and 8.2% of those people who have a full high school diploma or other equivalent degree. The only surprising number is the 13.3% of the people with no diploma, which this thesis expected to be leading this statistic. Considering that on average the people most likely to require income support are people with lower education, the highest percentage of people on income support should by that logic be people with no degree, however, these are much lower than the two subsequent degree levels.

The figures in Table 5.12 are more in line with expectations of income support. They show the large majority (90%) of people with no or only a basic work qualification requiring income support. Of these people, 55% are women. These statistics lead me to conclude that the lower the qualification of an individual, the higher the risk of his being unemployed and living in poverty.

Table 5.11 Social aid recipients and highest scholarly achievement 1998

School leaving certificate	People reliant on income support December 1998*		Population in April 1998*	
	Quantity	Percentage	Quantity	Percentage
No school graduation	143.575	**(13,3%)**	1.315.000	2,6%
Primary school	556.495	51,5%	22.621.000	44,7%
Secondary school or equivalent	200.782	18,6%	15.426.000	30,5%
Bachelor degree	91.637	8,4%	10.904.000	21,6%
Other scholarly degree	88.210	8,2%	309.000	0,6%
Together	1.080.699	100,0%	50.575.000	100,0%
Still in training	107.949	X	2.992.000	X
School degree unknown	577.766	X	2.075.000	X
Altogether	**1.766.414**	X	**55.642.000**	X

X Table section locked because indication not of use
* In the Age of 15 to 64 years of age outside of facilities
Source: Statistisches Bundesdamt, Sozailhilfestatistik und Mikrozensus sowie eigene Berechnungen
Deutscher Bundestag (Copy of the table Sozialhilfebezug und höchster Schulabschluss 1998) (2001, 72)

Table 5.12 Social aid and highest work qualification 1998

Training qualification	People reliant on income support 12/1998*		included therein % of		Population April 1998*	
	Amount	%	Men	Women	Amount	%
No training qualification	606.166	52,8	49,6	55,0	7.165.000	20,0
Vocational school diploma	427.389	37,2	40,2	35,1	19.926.000	55,6
Master craftsman diploma	21.325	1,9	1,9	1,8	3.379.000	9,4
Bachelor diploma	40.399	3,5	3,8	3,3	5.390.000	15,0
Other diploma	53.781	4,6	4,5	4,8	-	X
Together	1.149.060	100,0	100,0	100,0	35.860.000	100,0
Still in professional training	22.996	X	40,3	59,7	-	-
Highest professional diploma Unknown	594.358	X	41,4	58,6	-	-
Together	1.766.414	X	41,3	58,7	35.860.000	-

- No information available
X Table locked, because description not meaningful
* In the age of 15 to 64 years outside of institutions
Source: Statistisches Bundesamt, Sozialhilfestatistik und Mikrozensus, sowie eigene Berechnungen
Deutscher Bundestag (Copy of the table Sozialhilfebezug und höchster beruflicher Abschluss 1998) (2001, 72)

According to the poverty and wealth report (Deutscher Bundestag 2001, 48) since 1973, the number of people who require income support from the state has quadrupled until 1998 in West Germany and doubled in East Germany. This thesis agrees with the conclusion of the report that these increased numbers have to do with the lack scholarly achievement as well as professional qualifications available to students. Tables 5.13 and 5.20a and 5.20b show that children and single parents are the most disadvantaged by this evolution.

Table 5.13 shows that, although incomes for families have increased from 1993 to 1998, single parents have seen a dramatic decrease (-4.6% in own brackets last column) in their household income in West Germany and the lowest rise in incomes among the different groups in East Germany **4.9%** (own calculation) lower than the next lowest family group. Table 5.20a and 5.20b shows that children of single parents have the highest risk of sliding into poverty and form also the biggest block of people already living in poverty (first two columns on the left). These tables show that the social system in place was over time less effective at distributing the wealth among the population providing further arguments in favour of reforming the system to the political parties in particular the SPD.

Table 5.13 Household income of couples and single parents with kids under 18 Results of the EVS 1993 and 1st semester 1998

Family Type	Average income earning 1993	Average income earning 1998 1st semester 1998	Changes
		Old federal Republic	
Families with one child	6 050 DM	6 066 DM	+ 0,3%
Families with two children	6 712 DM	6 868 DM	+2,3%
Families with three children	6 924 DM	7 586 DM	+9,6%
Single parents	3 469 DM	3 311 DM	(-4,6%)
		New federal states	
Families with one child	4 302 DM	5 113 DM	+18,8%
Families with two children	4 634 DM	5 435 DM	+17,3%
Families with three children	4 779 DM	6 288 DM	+31,6%
Single parents	2 407 DM	2 705 DM	+12,4%

Source: Eigene Zusammenstellung aus Quinke. H. u. a.: Entwicklung der Familieneinkommen in den 90er-Jahren Deutscher Bundestag (Copy of the table Haushaltsnettoeinkommen von Paaren und allein Erziehenden mit Kindern unter 18 Jahren Ergebnisse der EVS 1993 und 1. Halbjahr 1998) (2001, 86)

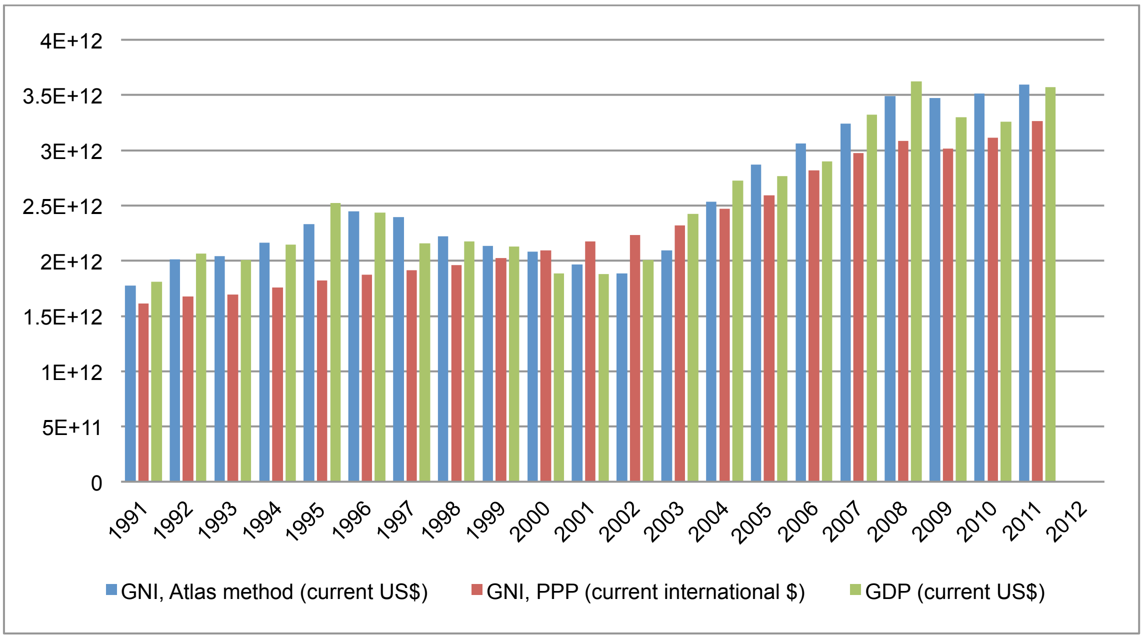
Unemployment remained above 8% from 97-99 and dipped under 8% for 2000-2001, only to increase again to new levels throughout the first half of the 2000s, reaching a new high in 2005 of 11.2% (see Tables 5.3 & 5.4).

Table 5.4 demonstrates the variations in the unemployment rate and shows that the unemployment rate in the East has remained steady from 1997 to 2005. Hence, all the addition of East Germany did, regarding the unemployment rate, was to increase the overall number of unemployed in Germany. It also showed that the East German employment market was not as receptive to the stimuli of the market or to the measures the state has taken to get people back into work (see Chapter 4). This would suggest that traditional measures for employment reduction weren't working or weren't having the desired effects. Thus a new tactic to deal with the high number of unemployed needed to be found. This was especially so since the high number of unemployed were a significant drain on the state's financial resources.

Previous reductions in unemployment proceeded at a slower pace than the reduction from 2005 onwards (see Tables 5.3 & 5.4) and were usually undone by economic contractions, as was the case in 2001 (see Tables 5.3 & 5.4). *After 2005 however, both East- and West-German unemployment rates started decreasing (significantly) to levels close to those between 1991 and 1992.* Although this alone does not provide a conclusive notion that the Hartz reforms have had any impact on the labour market, especially considering that

Table 5.5 shows an increase in available job places from 2004 to 2007. This increase in jobs may also have been caused by the renewed economic growth starting in 2002 after 7 years of declining GDP (see Table 5.14).

Table 5.14 Economic Growth Indicators



World Bank Data on 11.2012 (own calculations)

Although this data shows fluctuating employment markets throughout the late 1990s and early 2000s one cannot speak of fluctuating evolutions in the differences in income and opportunities for all citizens. As Table 5.14, 5.15 and 5.3 show, the differences between rich and poor have only continued to increase between 1995 and 2007. Tables 5.14 and 5.15 show the evolution of the GINI coefficient has been negative from 1993 to 2005; this shows that the inequalities between people have been increasing and not decreasing. The GINI coefficient has increased its difference between 1998 and 2003 by 2.7%, which, in 5 years, is quite a large increase in social differences. This equates to an average annual increase of approx. 0.5% in inequality. From 2002 to 2005, there has been a slowdown in the increase in inequality down from 2.7 to 2.0%.

Table 5.15 gives clear evidence that the income distribution between the different income groups has developed in a negative way for at least 50% of the population. The half of the population with the least income has suffered a reduction of its share of the revenues through salaries by a cumulative 1.9% (own calculation from own brackets in Table 5.15) while the top 30% of the income earners have increased their share by approx. 1.7% (own calculation form brackets). These differing accumulations are widening the income gap between rich and poor by 3.6% (own calculation from brackets) over 3 years, which is a significant change in income equality.

Table 5.15 Development and Spread of Income according to different levels and areas 1998 & 2003

	Germany		West Germany		East Germany	
	1998	2003	1998	2003	1998	2003
Gross Income from employed persons [1]						
a) all recipients						
Arithmetical Middle in Euro/Month	25.955	27.493	27.191	28.747	20.556	21.950
Median in Euro/Month	25.128	25.692	27.004	27.630	20.724	20.738
Gini-Coefficient	0,396	0,423	0,397	0,422	0,357	0,403
b) of the full-time employed						
Arithmetical Middle in Euro/Month	33.832	37.601	36.236	40.089	24.648	27.889
Median in Euro/Month	31.824	34.776	33.860	36.744	23.749	25.970
Gini-Coefficient	0,271	0,283	0,257	0,270	0,264	0,285
Market equivalent income of the population [2]						
Arithmetical Middle in Euro/Month	1.762	1.864	1.872	1.968	1.282	1.403
Median in Euro/Month	1.591	1.619	1.701	1.718	1.162	1.190
Gini-Coefficient	0,449	0,472	0,436	0,461	0,482	0,509
Net equivalent income of the population [3]						
Arithmetical Middle in Euro/Month	1.541	1.740	1.607	1.803	1.254	1.462
Median in Euro/Month	1.375	1.564	1.445	1.624	1.182	1.335
Gini-Coefficient	0,255	0,257	0,257	0,258	0,211	0,226

1. Including employer contributions to the social security contributions and assumed social contributions of officials
2. Sum of all the market incomes in the Household (Gross Income from employed persons, from self-employment and from assets including the rent value of the property that privately used) divided by the equivalent weighting of the Household members according to the New OECD-Scale
3. Household net income (Market income including running transfers minus required contributions to social security (employee and employer contributions and assumed contributions of officials) and taxes divided by the sum of the equivalent weights of the household members according to the new OECD scale

Source: EVS, jeweils Halbjahresergebnisse, Berechnungen von Hauser/Becker 2005
Deutscher Bundestag (Copy of the table Entwicklung und Verteilung der Einkommen nach verschiedenen Ebenen und Gebieten 1998 und 2003) (2005, 44)

Table 5.16 Distribution of real Gross Income[1] from employment from Employees total

Germany	**2002**	**2003**	**2004**	**2005**
Arithmetical Middle	24.873	24.563	23.987	23.684
Median	21.857	21.531	20.438	20.089
Gini-Coefficient	0,433	0,441	0,448	0,453
Share of Low Income [1]				
Total	35,5	36,5	36,8	36,4
Men	23,7	24,6	25,6	24,8
Women	47,9	48,5	48,1	47,7
Percentage of Gross Income from wage earners in Deciles [2]				
1. Decile	0,7	0,6	0,6	0,5
2. Decile	1,7	1,6	1,6	1,6
3. Decile	3,6	3,3	3,0	2,9
4. Decile	5,8	5,5	5,3	5,3
5. Decile	7,8	7,7	7,5	7,4
6. Decile	9,9	9,8	9,8	9,8
7. Decile	11,6	11,7	11,9	11,8
8. Decile	14,3	14,3	14,3	14,4
9. Decile	17,1	17,5	17,8	17,8
10. Decile	27,7	27,9	28,2	28,4

Source: SOEP

1. Income in prices in 2000
2. Low income border: 2/3 of the median

Deutscher Bundestag (Copy of the table Verteilung der realen Bruttoeinkommen aus unselbständiger Arbeit der Arbeitnehmer/-innen insgesamt) (2008, 13)

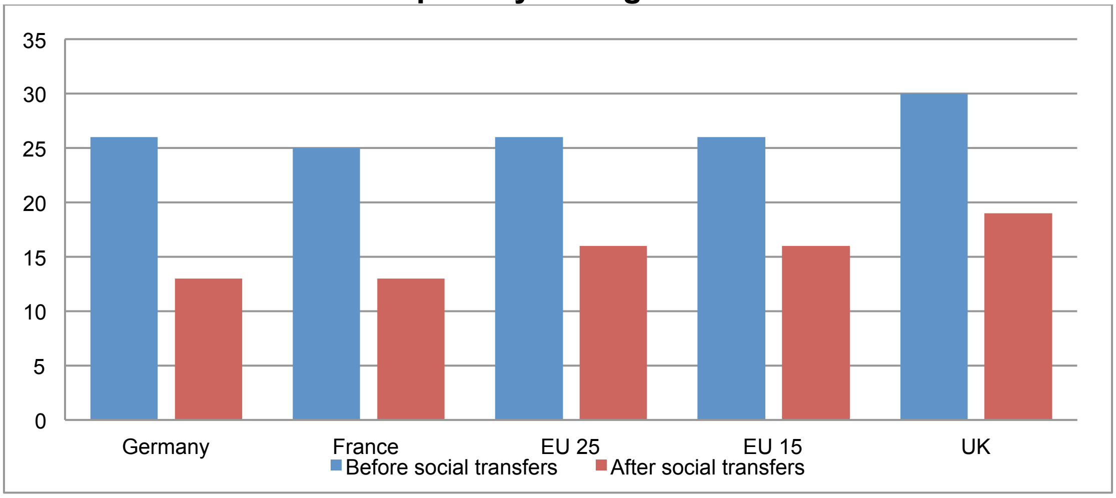
The consequences from the increased inequality present a varied picture. As demonstrated in Table 5.17, the groups at greatest risk of poverty are still the unemployed, whose risk of poverty has increased by 7.8% (own calculation) to 40.9% between 1998 and 2003, closely followed by single parent households whose risk of poverty has remained at 35.4%. It is also noteworthy that the gap between men and women has narrowed by approximately 1%. Although both are more likely to slide into poverty than in 1998, their chances are now more equal about doing so. Additionally, the likelihood of almost all age groups to slide into poverty has increased. The group with the highest likelihood of poverty is the age group of 16 to 24 years whose likelihood of being poor has increased by 4.2%, the second biggest increase in the rise of poverty.

Table 5.17 Group specific risk of poverty[1)] in % in Germany according to gender, age, employment and household type

Section of the population	New OECD-Scale	
	1998	2003
Differentiation by Gender		
Men	10,7	12,6
Women	13,3	14,4
Differentiation by Age		
Until 15 years	13,8	15,0
16 to 24 years	14,9	19,1
25 to 49 years	11,5	13,5
50 to 64 years	9,7	11,5
65 years and older	13,3	11,4
Differentiation by Income status [2)]		
Self-employed	11,2	9,3
Employee	5,7	7,1
Unemployed	33,1	40,9
Pensioner	12,2	11,8
People in one-person households		
Total	22,4	22,8
Men	20,3	22,5
Women	23,5	23,0
People in households with Children [3)]		
Single parents	35,4	35,4
2 families with child(ren)	10,8	11,6
Poverty risk quote altogether	12,1	13,5

(1) Poverty risk border 60% of the Median of the currently running and available equivalent incomes
(2) Only people from 16 years on
(3) Children: people below the age of 16 as well as people between 16 and 24, as long as they are not working and at least one parent lives in the household
Source: EVS, jeweils Halbjahresergebnisse, nach Berechnungen von Hauser/Becker 2005
Deutscher Bundestag (extract from table Gruppenspezifische Armustrisikoquoten in Prozent in Deutschland nach Geschlecht, Alter, Erwerbsstatus und Haushaltstypen (2005, 46).

Table 5.18 Reduction of poverty through social transfers 2005



Source: EU-SILC 2006
Deutscher Bundestag (Extract of table Reduktion des Armutsrisikos durch Sozialtransfers 2005) (2008, 18).

Table 5.18 shows that after social transfers, Germany is in line with the European average of countries whose people are at risk of poverty. After social transfers people are 50% less likely to go into poverty. With the social transfers, this was one of the lowest rates of poverty risk in the EU in 2005.

Table 5.19 reinforces the observations made above and shows that the amounts of people who are in need of aid have increased in real terms by about 230,000 from 2005 to 2007. Whereas unemployed people in need of aid have dropped from 2005 to 2007 (see Table 5.3), the amount of people in 400 EUR jobs or other forms of state sponsored employment who are now in need of government aid has gone up (see Table 5.19, People in employment starting 400 Euro Gross/Month). This was to some extent intended by the SPD government who wanted to reduce the amount of aid it had to pay to the unemployed (see previous chapter), which this project has succeeded in doing. Single parent households have been worst affected by these changes (see Table 5.19, Single parents). The group of people who saw the lowest rise in government aid was the people of 25 and younger.

Table 5.19 Structure of the employable aid seekers from 15 years onwards in thousand

Employable people in need of aid	2005	2006	Juni 2007
Total	**4.980**	**5.390**	**5.310**
People looking for or being employed who require aid (eHb)	3.400	3.800	3.460
Unemployed	2.770	2.820	2.420
People in employment starting 400 Euro Gross/Month	373	543	587
Included within, employed people with 800 Euro Gross/Month[1]	-	-	374
Procedure participants[2]	305	474	499
People remaining in eHB	1.580	1.590	1.850
For information only:			
Under 25 years	1.030	1.120	1.050
Single parents[3]	474	584	663
Foreigners	958	1.010	981

1. From the balance of the basic security and employment statistic in 2005 and 2006 (only social security paying employees) and basic security statistic in 2007 (all employees), therefore in the elapsed time not directly comparable, includes approximately 50000 unemployed.
2. Average stock without one off provisions and advancement of dependent employment; from 2006 with Information of accredited municipal mediums
3. With children below 18years, comparison over time only with limited meaning

Source: Bundesagentur für Arbeit
Deutscher Bundestag (Copy of the table Struktur der erwerbsfähigen Hilfebedürftigen ab 15 Jahren in Tausend) (2008, 73)

To sum up, the two major trends of the period analysed above are the reunification of Germany and the subsequent increase in unemployment that occurred with that reunification. The period of 1950 to 2007 also demonstrated that a trend of growing inequalities between the different income classes and the different household compositions in Germany has occurred. This trend became especially apparent in the late 1990s and early 2000s. When wealth started to become more concentrated with the wealthy. Single parent households, children and people in low-income jobs were the worst affected by this trend. This sector of low-income jobs saw a particularly large growth with the institution of the Hartz laws.

5.2.3 Germany between 2005 and 2014

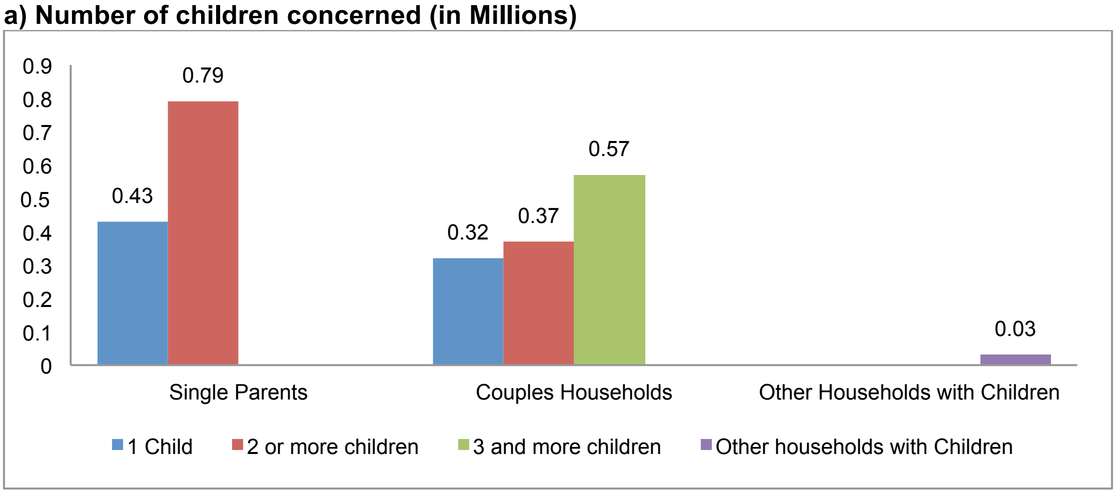
In 2005, the German unemployment rate starts to go down significantly, returning to approximately 1991 levels by 2011 (see Table 5.3). The slight increase in unemployment in 2009 can be explained by the financial crisis and the global economic downturn resulting in a severe economic contraction (*a recession*) in the three last quarters in 2008 and the first quarter in 2009 with economic growth recovering in the final three quarters of 2009 (see Tables 5.6 & 5.7).

Tables 5.3 to 5.7 do not provide a clear picture of the impact of the Hartz reforms upon the German economy. An impact can be inferred from the fact that unemployment has begun to go down consistently since 2005 and that there have been no major fluctuations within the unemployment rate after 2005 unlike after 1991 or 2001 when the unemployment rate started to climb again once it had gone down. Gross Domestic Product (GDP) and Gross National Income (GNI) have also seen an above average increases compared to the last increase which further strengthens the case for a positive impact of the Hartz reforms on the German economy. It is these types of trends, which the German government would use to back up its claim that austerity measures are good for the national economy.

Although the economic impacts of the Hartz reforms, from what can be asserted by this analysis have had a positive effect upon the German economy, the social effects tell a different story. The social effects of the Hartz reform can be established more easily since changes in the social payments can be, in many cases, directly analysed, as will be demonstrated below.

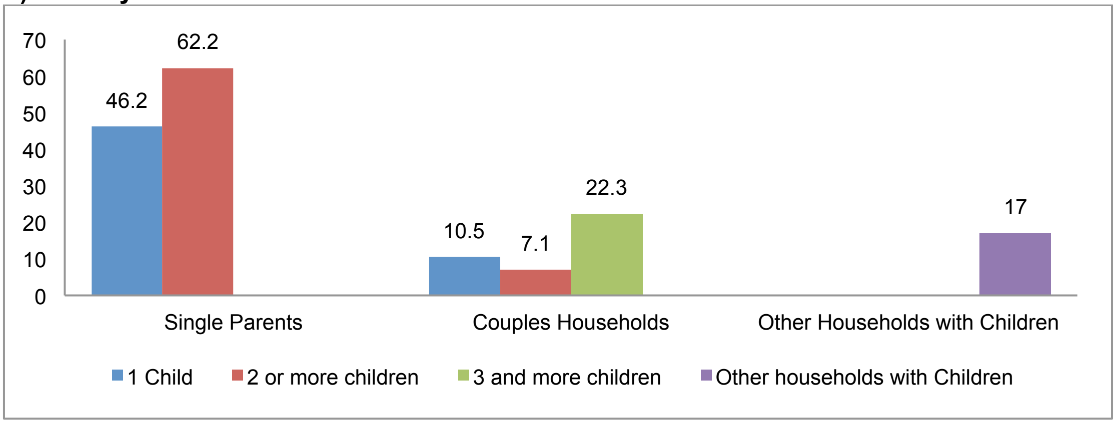
As is demonstrated in Table 5.20a and 5.20b, the more kids a family has, the more likely they are to live in poverty. This is especially so, if the children are raised in single parent households. A child born to a single parent is four times more likely to slide into poverty. Two or more children are almost 10 times more likely to slide into poverty. This is yet another distressing statistic demonstrating the, large gaps between people in Germany.

Table 5.20 Children at risk of poverty according to family type in 2010
a) Number of children concerned (in Millions)



Source: SOEP 2010, Berechnungen von Prognos auf Basis von Einkommen aus dem Jahr 2009
Deutscher Bundestag (Extract of table Armutsrisikoquote von Kindern in Deutschland nach Familientypen, 2010) (2012, 107)

b) Poverty risk in %



Source: SOEP 2010, Berechnungen von Prognos auf Basis von Einkommen aus dem Jahr 2009
Deutscher Bundestag (Extract of table Armutsrisikoquote von Kindern in Deutschland nach Familientypen, 2010) (2012, 107) (2012, 107)

Table 5.21 Household income with DOLE2 / Social Funding

Applicant	Normal requirements	Cost of Housing[1]	Household Income
Single	374	283	**657**
(Married) Couple	674	358	**1.032**
Single Parent (1 child, 4 years)	728	378	**1.106**
Single Parent (2 children 4 under 12 years)	979	435	**1.414**
(Married) Couple (1 child, 4 years)	893	474	**1.367**
(Married) Couple (2 children 4 under 12 years)	1.144	547	**1.691**
(Married) Couple (3 children 4 under 12, 15 years)	1.431	610	**2.041**

These examples illustrate how the household income is composed following basic insurance for employment seekers.
1) Average appropriate running costs for housing and heating (July 2011, Source: Analysereports, SGBII, Nov. 2011, Seite 55)

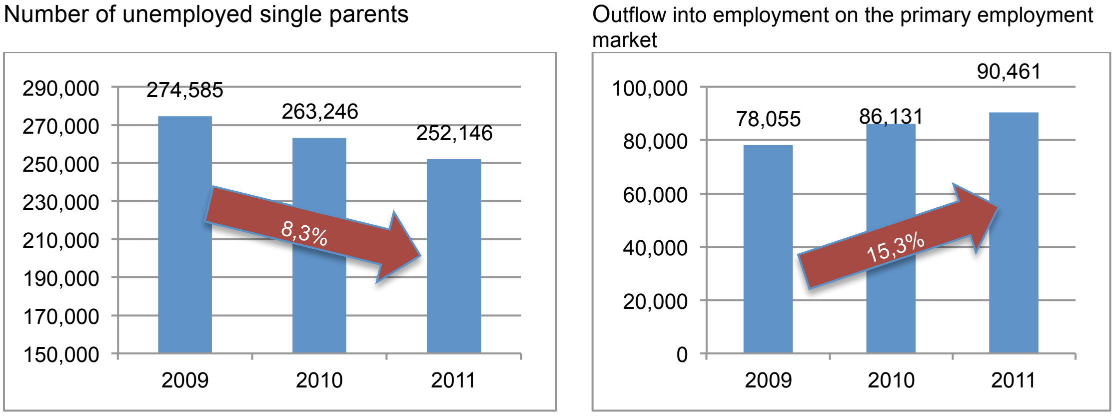
1. Standing of the normal requirement from 01.01.2012. Normal requirement for single parents including additional requirement awards

Deutscher Bundestag (Copy of the table: Haushaltseinkommen mit ALG II/Sozialgeld) (2012, 115)

One of the reasons for this increase in the likelihood of poverty is the fact that DOLE2, which provides for only basic sustenance in case of unemployment, is particularly disadvantageous to certain groups. This is especially true of the single parent. If the single parent is the sole household provider, DOLE2 payments are at a low sustainable level with only 1106 Euros of household income a month including the “Cost of Housing” (see Table 5.21), if one considers, that the German median income in 2009 was 1566.42 Euros a month (Statistisches Bundesamt 2014).

Table 5.21 shows that being a single parent and out of work in Germany virtually guarantees poverty. As Table 5.22 shows, this situation has improved from 2009 to 2011; the level of unemployed single parents has reduced by 8.3%, which is a significant reduction.

Table 5.22 Labour market evolution of single parents in SBG2



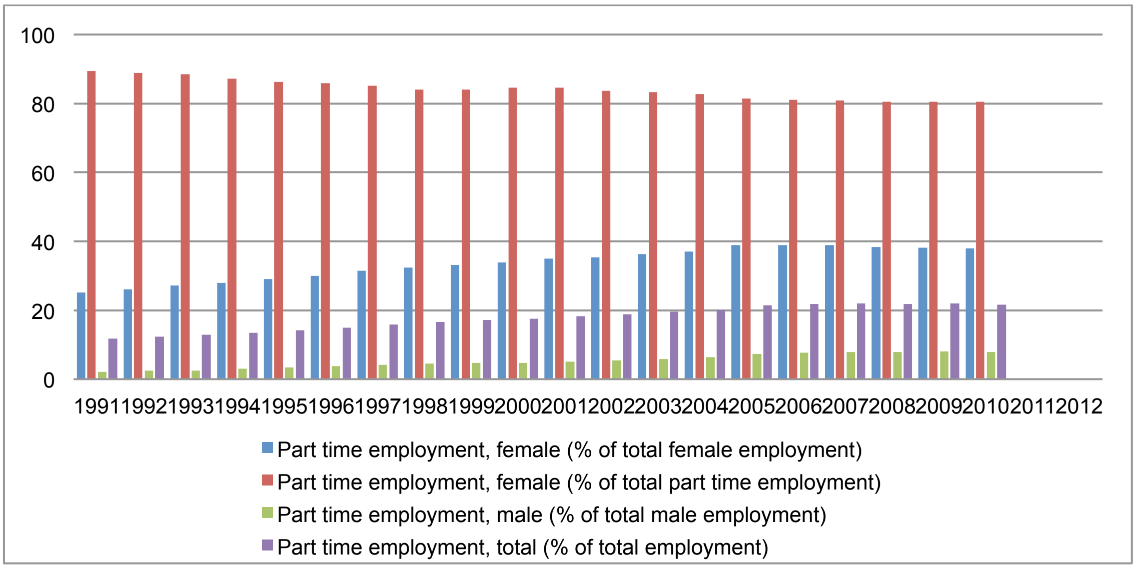
Source: Statisik der Bundesagentur für Arbeit
Deutscher Bundestag (2012, 158) (extract of the table Arbeitsmarktentwicklung bei Alleinerziehenden in Rechtskreis SGB II)

Furthermore, since 2009 there has also been a 15% increase in the number of single parents who have returned to the primary employment market (Table 5.22, right table), which is an encouraging sign that poverty may be reduced for many people in the medium term. However, it only remains an encouraging sign, since those statistics do not provide an idea of the level of pay of these jobs.

Except for greater movement on the lower end of the income scale, other labour-related statistics show merely continuing trends, which have been going on since at least 1991 (Egeler 2012). Part-time employment is a good example of that. Part-time employment has been continually increasing since 1991 and then has been stagnating at approximately 22% of total employment (see Table 5.23). During that same time, female part-time employment has decreased as part of total employment. However, female part-time employment has increased as part of total female employment (see Table 5.23) during that same time-period. This would confirm the data regarding labour force participation (see Table 5.24), which shows that more and more women have entered employment since the 1990s. It also shows an unbroken and growing trend of female part-time employment as part of total female employment although their overall participation in part-time employment seems to be decreasing.

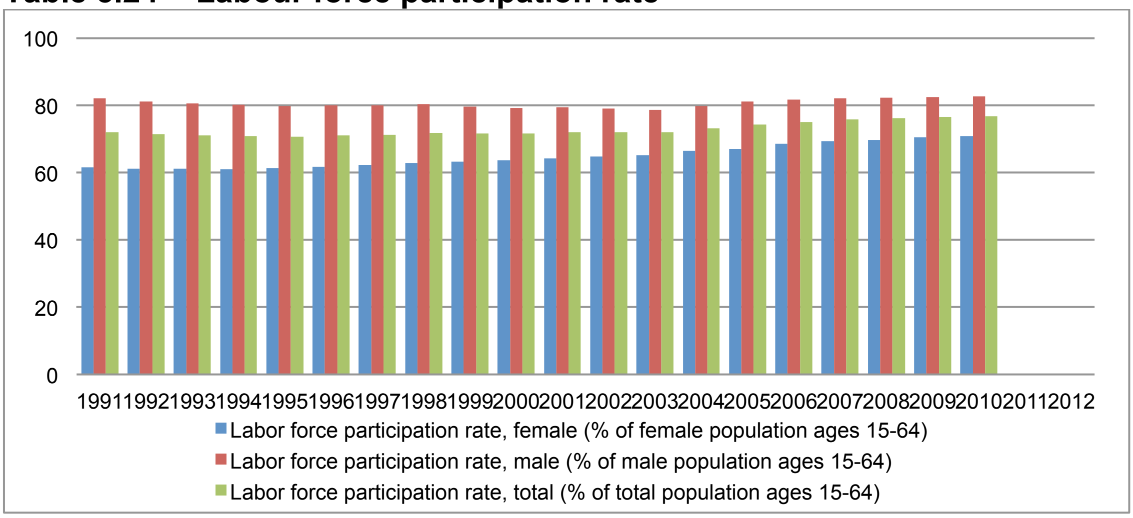
The previous chapter pointed out that the non-decisions of the German government that allowed the Hartz commission and with them the market forces to influence substantially the reforms of the State conception of its role in society. The resulting Hartz reforms created, among others, a number of new types of employment. This was seen as a very positive and necessary reform by the Department of Statistics (DoS) as it vitalized the employment market (Egler 2012), as it was designed to. This would also explain the decrease in Female part-time employment. This analysis is supported by WB numbers (2012), which show an increase in self-employment of approximately 1.0% from 2003 onwards; males whose increase was on average 1.5% since 2003 largely led the increase. However, as these numbers begin to show, the result of these reforms in terms of impact on employment were mixed if not negligible.

Table 5.23 Part Time Employment



World Bank Data on 11.2012 (own calculations)

Table 5.24 Labour force participation rate



World Bank Data on 11.2012 (own calculations)

The positive economic effects of these new types of employment coupled with the increase in traditional part-time employment can be seen in Table 5.7 in the increased production and the increased GDP numbers since 2005. Part of this increase could be attributed to the growing number of cheap and well-trained people that were “forced” into the labour market due to the Hartz4 reform of the DOLE payments into DOLE1 and DOLE2 as well as the rules and regulations governing its availability to people. This allowed companies to hire more labour cheaply and produce at more globally competitive prices raising profits and thereby GDP.

The embrace of the neo-liberal market and profit oriented worldview that was adopted by the German government helped in raising the attractiveness of Germany as a place of business. However, as the statistics will further show, it did not help in the spreading of wealth but rather in its concentration, which in turn further fuelled the structural power of the neo-liberal market concept. This embrace of the neo-liberal concept and the economic success Germany enjoyed because of that move also earned itself more structural power within the EU institutions particularly those dealing with the maintenance of the single market and the EMU. Their organisation is as was pointed out in Chapter 2 designed to reinforce neo-liberal concepts within its member states. This gives further credence to the argument of the German government that austerity prescriptions are good for the economy.

Table 5.25 and 5.26 consider a further point, which has been left unconsidered thus far. “In work” poverty has become the all-important factor to consider when studying employment statistics in Germany. As Table 5.25 shows, there has been a marked increase in the amount people who earn next to or on the poverty level (i.e. >60% of the median income), so even the fact that one has a job may not be enough to guarantee a life without poverty.

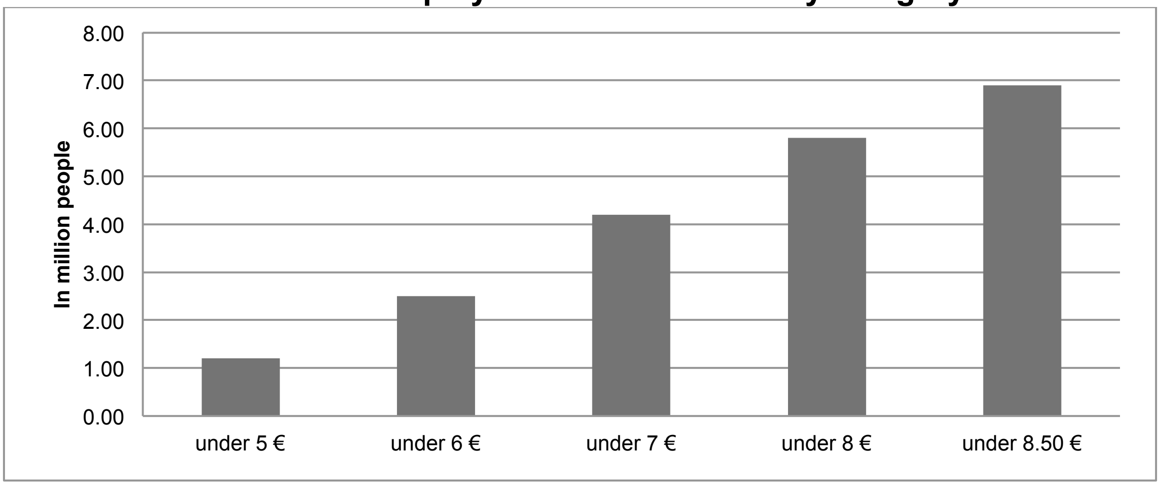
Table 5.25 In Work Poverty (A.9)

Indicator Income year	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Poverty risk rate[1] of employees[2]												
Total	5,9	6,9	6,7	7,1	7,4	7,7	8,3	8,1	7,5	7,8	8,6	8,7
Men	5,6	6,2	5,7	5,9	6,4	6,6	7,3	7,3	7,0	6,9	7,4	7,7
Women	6,2	7,7	8,0	8,4	8,6	9,0	9,5	9,1	8,1	8,7	9,9	9,8
Differentiation by age												
18 to 24 years	15,2	17,8	14,7	16,2	16,2	22,1	23,3	17,3	18,8	19,0	21,1	18,9
25 to 49 years	2,1	4,1	4,3	2,9	4,3	4,1	4,6	4,1	5,1	5,4	6,2	7,7
50 to 64 years	10,4	10,6	5,4	9,5	9,9	9,7	9,4	8,7	9,8	3,0	8,1	4,2
Differentiation by type of employment												
Full time	3,0	2,9	2,8	3,2	3,1	3,2	3,7	3,7	3,0	3,8	3,7	3,7
Part time	11,4	14,4	13,8	13,6	14,7	14,8	15,9	15,3	14,9	14,6	16,3	16,5

1 Equivalent weighted Household net income (new OECD-Skale) <60% of the Median income of all people
2 People are classified as employed, if they worked for more than 6 months in the year

Source: Berechnungen im BMAS auf Basis SOEP 2010
Deutscher Bundestag (Copy of table: In work poverty (A.9)) (2012, 475)

Table 5.26 Extent of the employment in the low salary category 2010



4,0%	7,4%	12,0%	16.7%	19,9%

Including School children, Students, Retirees and employees with a second employment
Shares: For all employed in %
Source: Institut für Arbeit und Qualifikation auf Basis des SOEP
Deutscher Bundestag (Extract of table Umfang der Beschäftigung in Niedriglohnbereich 2010, absolute Schwellenwerte) (2012, 327)

The German statistical office Destasis (DoS) calculated an average minimum wage for the whole of Germany, as Germany did not have a minimum wage. This changed on the 3rd July 2014 when the Bundestag approved the introduction of a minimum wage level to enter into force on the 1st of January 2015 (euractive.de, Reuters 2014).

This explains why there is a large spread in hourly salary even at the lower end of the income curve (Egeler 2012) (see also Table 5.26). It would also provide an explanation as to the increase in the number of people at risk of poverty even though they are earning a salary. This is particularly striking since the number of people who are earning low wages has increased steadily over the past 20 years (see Table 5.27). The greatest expansion therein was in secondary employment (i.e. people having a second job), which has increased by 50% between 2005 and 2011 (see Table 5.27). This is further confirmation that the wages many people are receiving for a job is no longer enough to provide for their needs, which is why they need to take on a second job. It remains to be seen if the implementation of a national minimum wage will manage to reduce the spread of the hourly income, considering that the implementation of the minimum wage will be staggered over two years and will include exceptions for certain sectors (euractive.de, Reuters 2014).

The DoS notes that, since 2006, asymmetrical employment (i.e. employment that does not fall under the definition of a standard employment contract, which here means full term employment of more than 20 hours a week and is not considered to be a temporary or low wage job) has remained stagnant, only increasing slightly from 25.0% in 2006 to 25.4% in 2010 (Egeler 2012). The largest share of asymmetrically employed workers lies in low skilled jobs such as replacement workers in part-time employment comprising 50.7% of that workforce. The higher the skill level, the lower the participation rates of the asymmetrically employed, so that in leadership positions only 9.1% are asymmetrically employed.

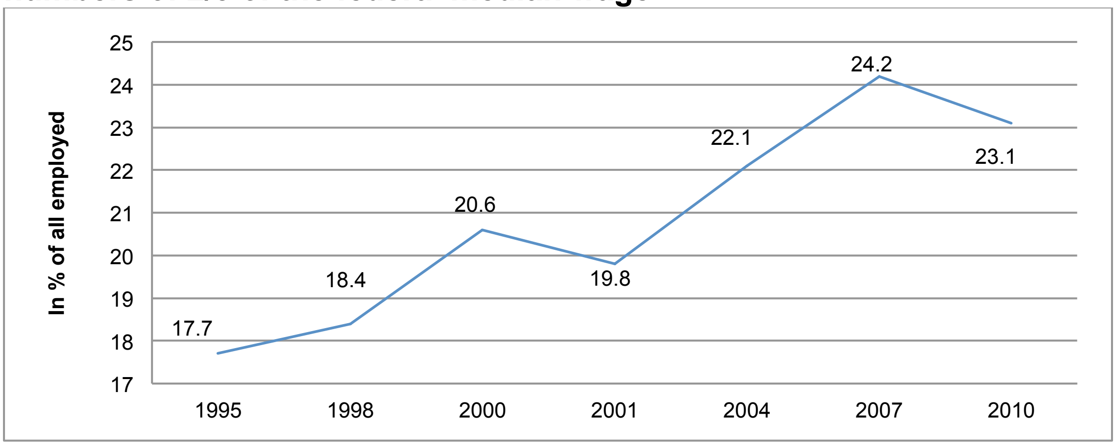
The DoS finds further evolutions of this sort throughout the economy. Whereas in 2001 the top 10% earned 3.33 times as much as the bottom 10%, in 2006 this number grew to 3.45 times the amount in 2010 (Statistisches Bundesamt 2012, 17). This number represents a **3.6%** (own calculation) increase in the earnings difference between rich and poor. If the evolution of the median household income is added, one can see that the median income in Germany has increased from its 2006 level of 9.90EUR to 10.36EUR in 2010 (a **4.6%** increase, own calculation). The proportion of people who earn less than the median income also increased by **1.9%** (own calculation), which is a strong indicator that the discrepancies between rich and poor in Germany are becoming broader as well as deeper instead of becoming smaller. A point, which is given more force considering that the earnings differences between middle- and low-income classes has increased by **2.23%** (own calculation) and the difference between middle- and high-income classes have increased by **0.53%** (own calculation) (Statistisches Bundesamt 2012).

These numbers confirm the initial statement made above that the chasm between rich and poor is getting greater, to the benefit of the economy and Germany's structural power, within it and within EU institutions, and at the expense of the very poor who are left furthest behind. This concurs with the evaluation made by Crouch (2011). He argues that the growth and stability of the system is due to its increased polarization of the poor and the rich as well as the continued financial and economic exploitation of the poor (Crouch 2011).

The DoS argues that this is a continuing trend that has been developing for years and therefore is not directly related to the Hartz reforms (Statistisches Bundesamt 2012, (companion to Egeler 2012)). If one considers the evolution of this widening income gap, one can argue that the failure of the Hartz reforms to reduce this earnings difference is a failure of its stated aims to reduce inequality in Germany by using market liberalisation concepts (see Chapter 4). This failure becomes even more evident when one considers that low income jobs and temporary work have increased between 2006 and 2010 from 18.7% to 20.6%, a majority of whom are atypically employed (Statistisches Bundesamt 2012, (companion to Egeler 2012)).

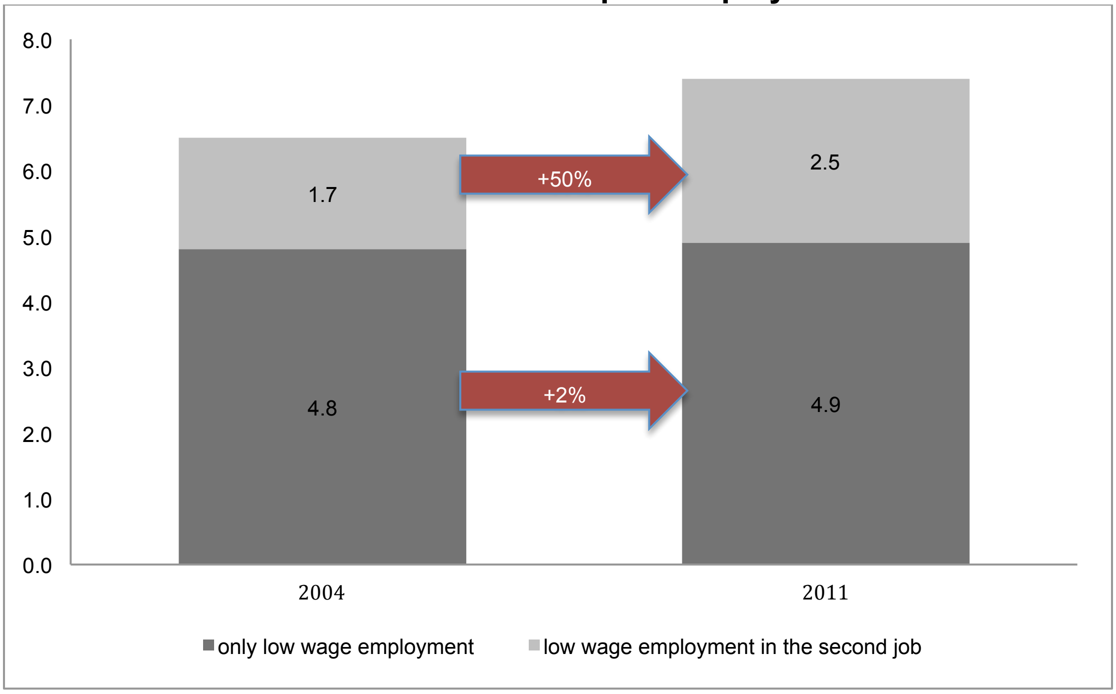
However, it can also be argued that the Hartz laws have been successful in the reinforcement of the continued polarization of the wealthy and the poor, by providing further freedoms of the firms and industries while restricting the freedoms of the workers, as they are put under ever growing pressures to perform and care for their own wellbeing.

Table 5.27 Extent and evolution of the share of low-income jobs relative numbers of 2/3 of the federal median wage



Including pupils, students, retirees and employees with secondary employment. For the year 2010 was the marginal value for an hourly wage at 9,15 Euro.
Source: Institut für Arbeit und Qualifikation auf Basis des SOEP
Deutscher Bundestag (Extract of table Umfang und Entwicklung des Anteils der Niedriglohnbeschäftigung, relative Schwellenwert von zwei Dritteln des bundesweiten Medianlohns (2012, 328)

Table 5.28 Evolution of low paid employment



Deutscher Bundestag (2012, 332)

Table 5.29 Self-assessment of the income situation in Germany

With the current income levels we can…	2002	2004	2006	2008	2010
live comfortably	30,4	29,1	24,8	30,5	34,0
manage	56,1	53,2	57,0	55,1	50,8
manage adequately	86,4	82,3	81,8	85,7	84,7
live on only with difficulty	10,9	13,8	13,7	10,7	11,9
live on with great difficulty	2,7	3,9	4,5	3,6	3,3
subsist with difficulty	13,6	17,7	18,2	14,3	15,3

Data in percent
Source: Institut für Sozialfoschung und Gesellschaftspolitik auf Basis European Social Survey
Deutscher Bundestag (Copy of table Selbstbewertung der Einkommenssituation, Deutschland) (2012, 316)

The Destatis research further underlines the fact that the chasm between rich and poor has been continually increasing for the time from 2001 to 2010 that this thesis has been evaluating (Statistisches Bundesamt 2012). Table 5.29 shows how the German people themselves see their own situation. It shows that fewer and fewer people have been living comfortably between 2002 and 2006, a period which was mainly a time of economic growth. This trend has changed in 2008-2010, which again showed a marked increase in happiness about the income situation. This increase is likely linked to the economic recession.

Interestingly it is only the upper income groups that have increased their opinion of what they can do with their income during that time. The lower income groups have all increased in their opinion that the salary they earn they can “live on only with difficulty”, “live on with great difficulty”, “subsist with difficulty” to manage with the income they are provided with by their employers. This statement is concurrent to the research conducted within this section, which demonstrates that the Hartz reforms, though having helped with economic recovery, have also failed to help with the reduction of wage inequalities. The Hartz reforms, as this chapter showed, have even further increased these inequalities.

Table 5.30 shows that the income distribution has continued in a negative way for 60% percent of the working population where as the top 30% have been able to increase their incomes, the top 10% having been most successful in that regard. At the same time, one can argue that a 0.7% increase in income for the top 10% and a 1% increase in the difference between the bottom and the top 10% over 5 years is a marked slowdown compared to the increases in income inequality at the start of the analysis conducted here.

Table 5.30 Distribution of the Net income in 2003 and 2008

Year	Decile										Gini-Coefficient
	1	2	3	4	5	6	7	8	9	10	
	Share (%) of Volume of Net equivalent income										
2003	3,9	5,5	6,5	7,5	8,4	9,4	10,5	12,0	14,3	22,0	0,267
2008	3,6	5,1	6,3	7,3	8,3	9,3	10,5	12,2	14,7	22,7	0,284

Source: EVS: Statistisches Bundesamt
Shares in % of the Volume of the Net equivalent income
Deutscher Bundestag (Exract from table Verteilung der Nettoäquivalenzeinkommen 2003 und 2008 (2012, 318)

Table 5.31 shows that the inequality between rich and poor did slow down slightly but still has had as a result the accumulation of more than half of all earnings going to the top 10%. In contrast only about 1% of all earnings are going to the bottom 50% of the lower income households.

Table 5.31 Income distribution

	EVS Income and consumption control sample			**SOEP**[1)] Socio economic panels	
Indicator / Year	**1998**	**2003**	**2008**	**2002**	**2007**
Distribution of the net income to the top 10% of households	44,7%	49,4%	52,9%	57,4%	57,1%
Distribution of the net income of the bottom 50% of households	3,7%	2,6%	1,2%	1,4%	1,2%
Gini-Coefficient	0,674	0,713	0,748	0,761	0,766

1. Including company and tangible assets

Source: Statistisches Bundesamt und Berechnungen im BMAS auf Basis SOEP 2010
Deutscher Bundestag (Copy of the table: Vermögensverteilung (Q.1)) (2012, 461)

A consequence of these low incomes and the negative income distribution is an increased likelihood of illness, as Table 5.32 demonstrates. Whereas the percentages of health risks have remained steady for those earning 150% or more than the median income, that is not the case for those earning less than 60% of the median income, whose number of illnesses has increased by 30% over six years. This is a clear indication of a relationship between income and health and the impacts that low income can have on an individual's health.

Table 5.32 Health impediments according to income

Income positions [2]	Men [1]							
	2004		2006		2008		2010	
	%	OR	%	OR	%	OR	%	OR
<60%	**9,2**	**3,0**	**8,8**	**4,1**	**10,5**	**0,8**	**12,7**	**4,1**
60<150%	**6,4**	**1,8**	**6,8**	**2,7**	**6,0**	**3,3**	**6,9**	**1,6**
>=150%	**3,3**	**Ref.**	**2,8**	**Ref.**	**1,8**	**Ref.**	**3,5**	**Ref.**
Total	**6,1**		**6,1**		**5,6**		**6,2**	
Income positions [2]	**Women [1]**							
	2004		**2006**		**2008**		**2010**	
	%	**OR**	**%**	**OR**	**%**	**OR**	**%**	**OR**
<60%	**9,8**	**1,2**	**11,4**	**1,8**	**11,2**	**2,8**	**13,4**	**2,8**
60<150%	**9,1**	**1,2**	**8,4**	**1,2**	**7,6**	**1,7**	**7,9**	**1,7**
>=150%	**6,4**	**Ref.**	**6,3**	**Ref.**	**4,2**	**Ref.**	**4,0**	**Ref.**
Total	**8,7**		**8,6**		**7,5**		**8,1**	

%= Occurrence in %; OR= age adjusted Odds Ratio determined through binary logistic regressions; 95%= confidence intervals of the OR; Ref= reference category

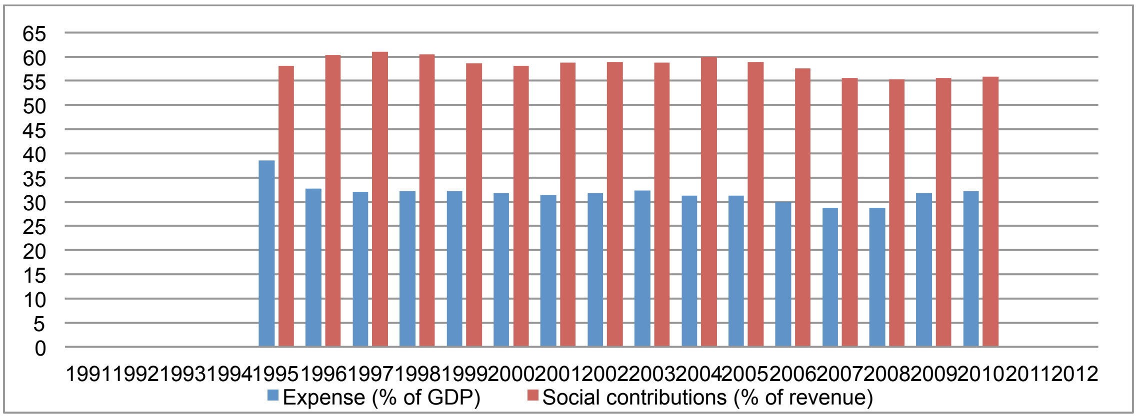
1. The indicator describes the share of men and women, who would describe their general level of health as "less good or bad" and are limited in at least 3of5, predetermined areas "strong", "often" or "always". Taken into account are limitations because of physical difficulties in taking the stairs, or in executing taxing physical activities, through psychological or emotional problems during regular activities and limitations because of physical or psychological problems during social activities
2. Relative income positions: under 60%, 60-150% and 150% and above Net equivalent income related to the societal median

Source: Berechnungen des RKI Berlin auf Basis SOEP
Deutscher Bundestag (Copy of the table Gesundheitlicher Beeinträchtigung nach Einkommensposition A.3) (2012, 462)

"Social contributions" held steady from 1995 to 2004 (see Table 5.33) but subsequently dropped by 5% between 2004 and 2007 after which they continued to remain steady. This noticeable reduction in social contributions as well as the timing of these reductions, (which did not happen during the previous growth cycle) do provide weight to the argument that the Hartz reforms, if not the cause of these reductions, were at least responsible for their steep decline and continued lower level of healthcare expenditure.

The same goes for the "expenses" that also noticed a slight reduction during that time. However, "expenses" got once again increased in 2009, which would agree with a response to the global recession (see Table 5.33).

Table 5.33 Social Contributions and Expenses (% of GDP)

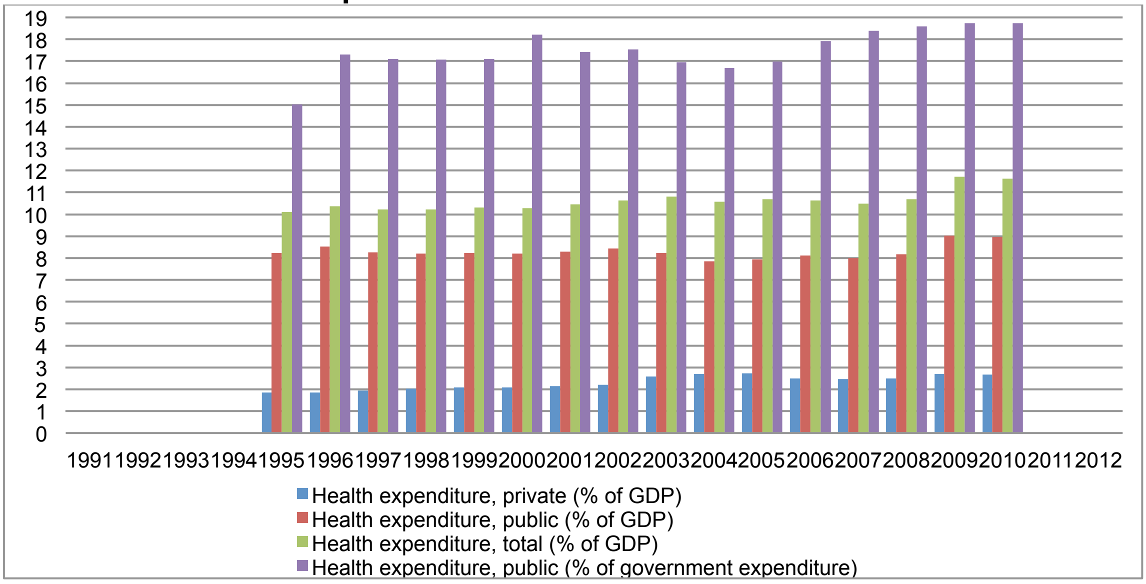


World Bank Data on 11.2012 (own calculations)

Having said this, if one looks at the figures for the German health expenditure, a mixture of data is the result. Private healthcare expenditure has only varied within 1% of GDP in the 15 years of which data is available (see Table 5.34). The same goes for public healthcare expenditure: this did not vary much more than 1% until 2009 and 2010. This increase is likely due to the global recession as the increased spending was used to offset the loss in productivity and spending on healthcare by individuals and companies as well as to reduce any adverse impacts on the poorer segments of the population; this continued until 2010 at least (see Table 5.35). Any further payments would confirm if this was just a temporary incidence due to the recession or if it was a genuine increase in healthcare contributions.

Health expenditure as a portion of government expenditure, however, varied considerably more over the time period than the other health expenditures. These variations might be explained if it was considered that health expenditure as part of government expenditure is ascertained through different values. Taking into account the quasi-cyclical 5 year fluctuations (1995-1999 and 2000-2004) (see Table 5.34) 2005 and onwards do break with this established pattern (at least in the two previous cycles). It does so right from the start in 2005 and increasing by almost 2% by 2007 and then remaining steady at that level. This increase in health expenditure in 2005 does indicate that this increase was not a response to the recession, but was independent of it.

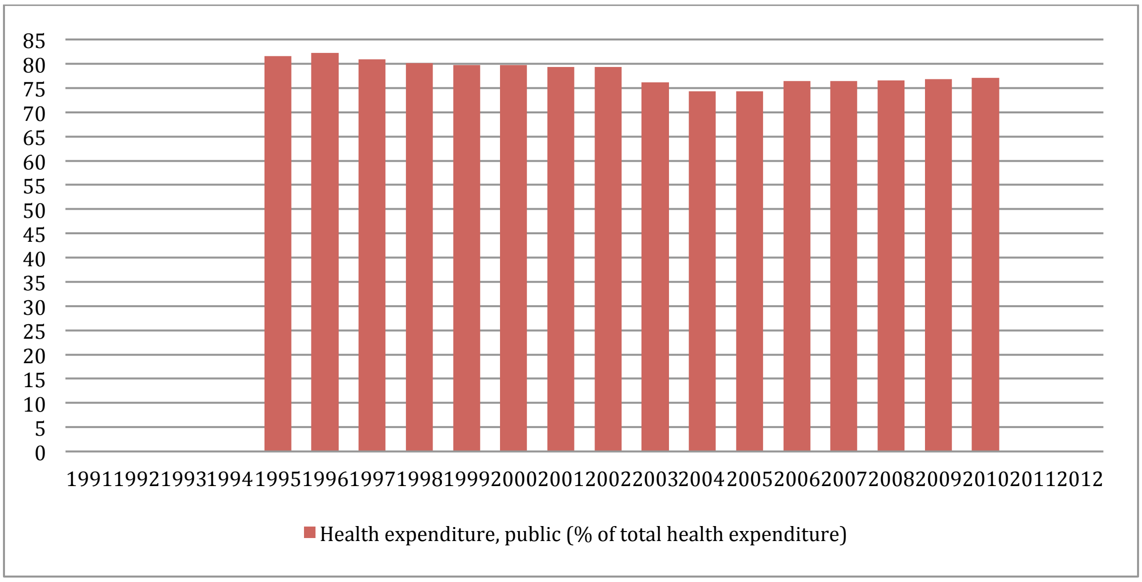
Table 5.34 Health Expenditure



World Bank Data on 11.2012 (own calculations)

This data is, however, not as clear-cut as one would expect. Looking at Table 5.35 shows that public health expenditure (% of total health expenditure) has gone down 5% from 2003 onwards and has remained at that level ever since, even though public health expenditure ((% of government expenditure) (purple)) (Table 5.34) has gone up as part of government expenditure. Considering that healthcare spending in terms of government spending has increased (Table 5.34) but healthcare spending itself has been reduced, it would lead to the conclusion that overall government spending has been reduced but healthcare spending has been given a greater share of the remaining spending though not increased enough to offset all of the cuts.

Table 5.35 Health expenditure, public (% of total health expenditure)



World Bank Data on 11.2012 (own calculations)

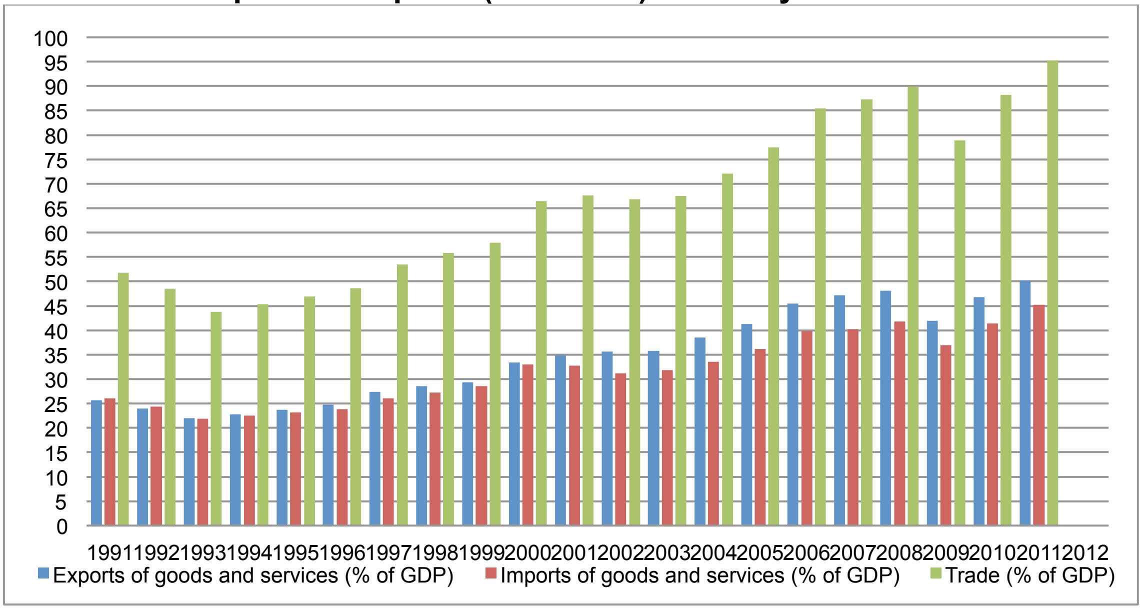
5.3 Germany: the burden of success and reform

The previous section demonstrated that the Hartz reforms have had a variety of consequences on the German economy and on German society. From the data presented in this chapter and the analysis undertaken, it can be inferred that the Hartz reforms were a contributing factor in increasing German competitiveness. By increasing the demands the state made on its population, including allowing its population to be exposed to a greater extent to market forces, is in keeping with the changing concepts of classical and neo-liberal economics as well as in keeping with the state tradition of the self-limiting state (Crouch 2011, Dyson 2009). As was argued in the previous chapter, these reforms institutionalised neo-liberal concepts and reduced the importance of the state in the economy as well as in society. These actions helped increase the labour supply in Germany, particularly within the lower income jobs market and the secondary jobs market. This allowed firms to hire more people and produce more goods and services as well as achieving higher profits. Simultaneously, these actions allowed for a greater polarization of society, which as Crouch (2011) argued was a by-product of the neo-liberal economic concept.

This section will consider how the implementation of the Hartz reforms and the move towards a more neo-liberal socio-political-economic state structure helped Germany increase its own structural power within the EU by harnessing the structural power of the neo-liberal economic structure. Therefore this chapter will focus in its penultimate section on another set of economic performance indicators namely Germany’s trade as percentage of GDP as well as its levels of pay and the most recent GDP growth figures. This section will also consider the German state’s borrowing projections and the most recent budget estimates. This is another good indicator of how the Hartz reforms and their neo-liberal concepts have impacted Germany. They pinpoint how exactly the German government intends to finance itself and more importantly, what it intends to finance over the coming years. These finance projections will be strongly influenced by the concepts behind the Hartz reforms, i.e. smaller government, less spending and more income.

If one wants to understand how the German economy has fared through the 2007/2008 crisis, one needs the German export data, since exports are one of Germany’s most important sources of income. Table 5.36 shows that since 1995 trade has grown in importance in the German economy on a scale that leaves the German economy almost completely dependent on its ability to trade with other nations. Table 5.37 also shows that the German economy has had a permanent trade surplus since 1994. This trade surplus also carried through the economic crisis of 2007/2008, which would have helped the German economy to get through the crisis without increasing the German deficit.

Table 5.36 Imports & Exports (% of GDP) Germany



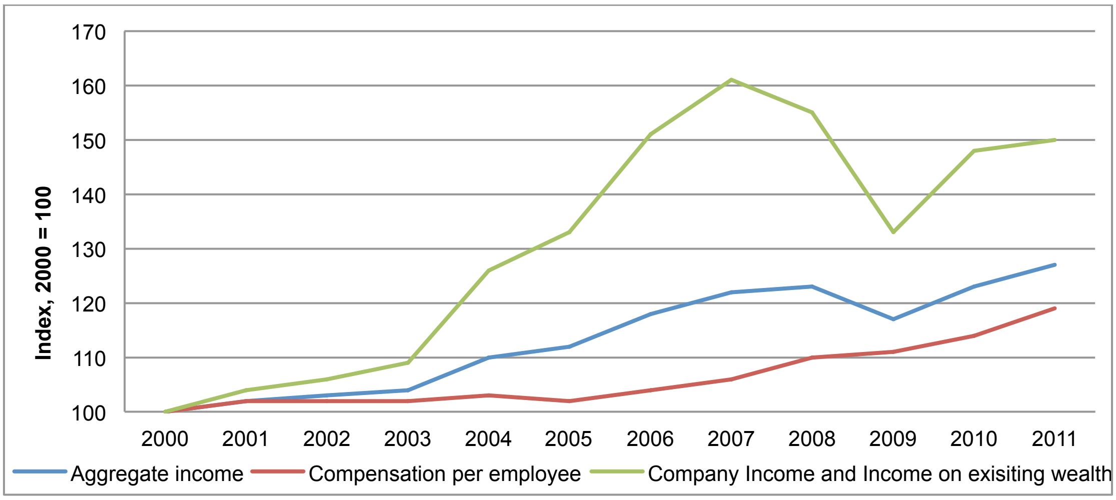
World Bank Data on 11.2012 (own calculations)

Since 1993, Germany has become a net export nation. Although imports and exports were closely matched throughout the 90s, after 2000 a significant gap opened up between exports and imports, with exports constituting 50% of the country's GDP in 2011. Considering that the global market is run on neo-liberal economic principles, the importance of trade within the German economy, a strong and competitive production sector is necessary to maintain these exports. The implementation of the Hartz reforms had a positive impact on production in Germany by enabling it to compete more easily in the global markets due to the reduced labour costs, which the Hartz laws made possible. It also made attracting funding easier further bolstering German production, since it implemented neo-liberal economic principles. This shows that the Hartz reforms contributed to the increase in exposure to the international market of the German state and the German economy. They did so by contributing to greater international competitiveness as well as more forcefully embracing the structural power, which the neo-liberal economic system provides at the expense of the Keynesian system.

In 2013, 69% of German exports continue to go to other European countries (57% going to EU members). Only 16% are going to Asia, 12% to America, and 2% to Africa and 0,9% to Oceania (DESTATIS 2014). This breakdown of the German exports shows how Europe centric its exports are and therefore it is vital that the other European countries recover from that crisis quickly to stave off a contracted reduction of German exports. This is a particularly important point since the German government considers the best way for the other EZ countries to recover is by applying their austerity prescriptions so that these countries can grow again and once again consume German products. The issue with that argument is, however, that the Hartz reforms have done nothing to bolster internal consumption particularly at the lower end of the income scale, as this chapter showed, incomes of only the upper income brackets have improved and those of the lower income brackets have been reduced, resulting in a reduced consumption on a national level.

It is this focus on European exports that makes the German austerity position so counterintuitive especially since it was this export expansion which helped increase the income of German business (green), the German workers (Red) and German Society in general (Blue) (see Table 5.37). What is interesting about this table, is that one can see a significant decrease in the profits of German industries since 2007 and a much flatter growth indicator for 2011 as compared to the rate of growth even just before the financial crisis (2006-2007) when it levelled off slightly as compared to previous years (2005-2006 and 2003-2004). This flattening could indicate a reduction in the sales by German companies nationally and internationally which would concur with the reduced demand within Europe, which was already showing slow growth (Table 5.38) due to the financial crisis. The austerity prescriptions imposed, on over indebted countries as well as on better performing countries, would only worsen or at least prolong this trend of low growth.

Table 5.37 Evolution of the Popular Income and its components, 2000-2011



Source: Statistisches Bundesamt, Volkswirtschaftliche Gesamtrechnung, Datenstand: Märtz 2011
Deutscher Bundestag (Copy of table Entwicklung des Volkseinkommens und seiner Komponenten, 2000-2001) (2012, 47)

A further point to be noted is the fact that pay continued to rise from 2005 onwards, stagnating in 2008-2009 and then continuing to rise from 2009 onwards. The rise in pay (Table 5.36 blue line, middle one on the graph) would go some way in explaining the economic recovery of Germany after the crash. The increase in income suggests an increase in internal consumption, which would replace to a degree the reduction of exports. However, this statistic does not consider the distribution of that income and therefore does not demonstrate who actually benefited from this increase in pay. The continued expansion of poverty coupled with the increase in income would suggest a continued widening of the inequality within society and a concentration of the wealth and incomes at top. The labour reforms instituted by the Hartz laws back up this assertion.

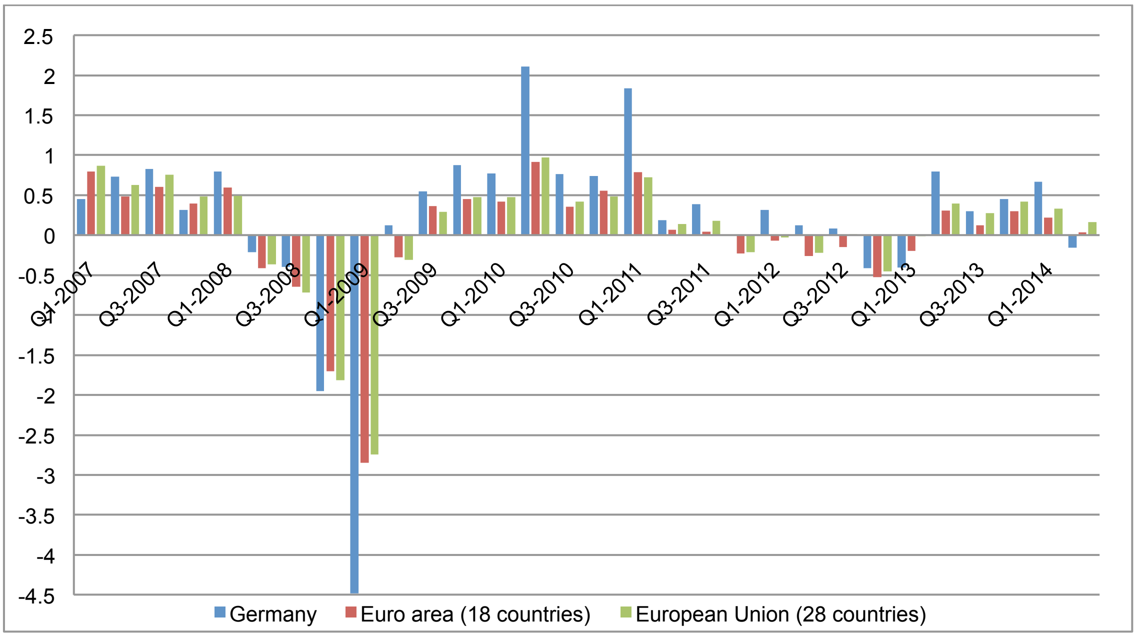
Table 5.6 and Table 5.7 show how deep the economic crisis was. In Q2 of 2008, Germany entered a recession, which continued until Q1 of 2009 where the German economy registered a -4% (negative) growth in GDP, the highest contraction of the German economy during the recession. The four quarters of recession caused a combined economic contraction of approximately 7% of GDP. Germany managed to come out of the recession after 4 quarters of negative growth, even though the recession continues in other EU countries such as Greece, which in 2011 had a negative growth of -6.9% (IMF World economic outlook 2012, 53), recession has continued until 2013 where the Greek GDP was reduced another -3.9%. 2014 and 2015 are projected to be the first years of positive growth for Greece (IMF World economic outlook 2014, 50)

Germany's recovery, in comparison, has been "good" throughout the last three quarters of 2009 and 2010 (considering the severity of the recession). Germany managed to deliver 7 quarters of growth above 0.5%, Q2 2010 even showing a strong growth of approx. 2.2%. In 2011, this strong growth continued with a growth of 3.1% of GDP. However, since Q2 2011 economic growth has not been over 0.5% of GDP, which does mark a slowing of the economic activity in Germany. Table 5.38 further shows that after Q1 of 2011 German growth has been lacklustre turning negative in Q4 of 2012 and Q1 of 2013. After Q1 of 2011 German growth has not managed to break the 1% mark of economic growth. This is a particularly troubling statistic from the economically most powerful country in Europe. While throughout 2013 German economic performance has recovered, Q2 of 2014 once again showed negative growth, which leads to the conclusion that the imposition of austerity in the EZ countries has an impact upon the consumption behaviour of these economies impacting the German economy in turn.

On the other hand, from 2005 Germany saw a 1% annual reduction in unemployment until the recession of 2008 and 2009 when it began to stagnate. In 2011 the unemployment rate settled at approx. 6% and is projected to remain at that level. This reduction in unemployment provides a strong argument for a positive relationship between the effects of the Hartz reforms and their contribution towards the reduction of unemployment during that time. The IMF projects unemployment to remain at this level (with a variation of 0.1-0.3%) until 2016 (see Table 5.3). This gives further credence to the assertion that the Hartz reforms did have a measurable impact on the German labour market since there was no significant stability in the unemployment rate for almost 30 years since every economic upturn or downturn caused the unemployment rate to fluctuate (see Tables 5.2, 5.3, 5.4). If the IMF projections were correct, this would further solidify the positive relationship between the Hartz reforms and the reduced unemployment rate. Although it is still a bit early to tell, the combination of all of these statistics shows that the Hartz reforms do seem to have had a some impact on the labour market which does seem to have gotten to grips with some of the issues the reforms were supposed to get under control. The positive effects of this reduced number of people being unemployed become especially important considering German economic prospects as well as the growth prospects of the EU.

The IMF shows European growth to be lacklustre with growth for the whole EU area for 2013 to be 0.5% of GDP and at -0,4% of GDP growth for the EZ, while projected growth is more optimistic with a projected average level of growth of approx. 1.7% EU wide and approx. 1% EZ growth. Considering that Germany's 2013 growth is on par with the EU average, German growth is not projected to surpass EU wide growth, which means that Germany as well as the EU in general remains in a precarious situation, which needs to be closely monitored (IMF World economic outlook 2014, 50).

Table 5.38 Gross domestic product - expenditure approach (Germany, Euro Zone, European Union)



GPSA: Growth rate compared to previous quarter, seasonally adjusted
OECD 2014b Stat Extracts

Taking into account the economic performances of other EU countries, Germany remains a strong player on the national and international scene. As the German department of statistics (DoS) revealed in its "Verdienststrukturerhebung" (earnings report (own translation)), the German economy continues to develop positively even though it is caught up in a global economic crisis (Egeler 2012, 1). This confirms the data above, showing slow but positive growth above the average growth rate in the rest of the EZ and on par with Europe.

This economic data shows a fragile European recovery close to stagnation. Therefore, a situation of the sovereign debt crisis of the PIIGS countries causing enormous socioeconomic problems in the Euro Zone including in Germany, where the financial markets started speculating against, not only a sovereign default of individual countries but also started speculating against the collapse of the common currency as a whole (Radcliffe 2011) needed to be avoided.

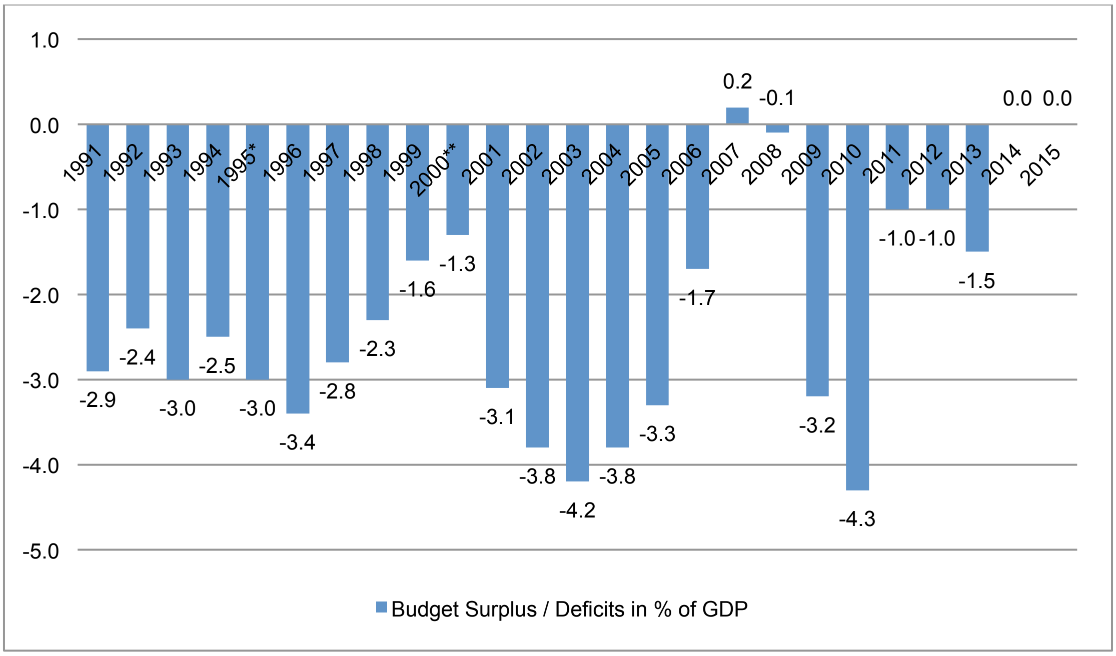
As was pointed out in Chapters 2 and 3 of this thesis, the consequences of such an event which were caused by the changed economic concepts now in power in global economics and the changed relationship between the state and industry. This caused the non-decisions taken by the governments over time and the increase in structural power of the neo-liberal market ideology. This in turn allowed the countries to accumulate this large amount of debt in the first place, which has been disastrous for the EZ and all of its members. This same neo-liberal concept now required countries to maintain a balanced budget and economy in order for the financial industry to be able to continue to do their trading in an effective manner (Couch 2011).

A rescue plan was therefore devised in the form of the EFSF and later the ESM to secure the EZ members from such an event and to allow Greece, Ireland Spain, Italy and Portugal who had come close to default to get their economic house in order. In order to create a new stable financial framework for the Euro, the access to the rescue funds by any country including the ones already in trouble required them to apply austerity prescriptions following the German example, since Germany as was demonstrated throughout this thesis, had already successfully implemented neo-liberal reforms and was able to participate fully on the global stage (individually or as part of the EU). The size of Germany’s economy and, its role as the biggest contributor to the European budget as well as to the stability mechanisms (the EFSF and ESM, 27% of the total contributions) further increased German and by consequence neo-liberal economic influence within these frameworks.

The German government, in its attempt to balance its budget, is well aware of what happened to other European countries now in trouble. It also does not want to repeat their mistake nor does it want to relive its own period of contraction hence its insistence upon the austerity measures (see Chapter 4). As Table 5.39 demonstrates, throughout the 1990s the German state increased its borrowing by an annual average of 2.5%. After 2003 the annual level of borrowing begins to go down, even managing to achieve a surplus between 2007 and 2008. After the initial shock of the 2007/2008 crisis had passed, the German government managed to keep the increase of sovereign debt to about

1% from 2011 onwards. This to my mind shows a strong influence of the Hartz reforms and the austerity concept.

Table 5.39 Outgoings, Income and net state borrowing 1991-2015



Source: Destasis and the Federal finance minister
* Without the wealth transfers after the takeover of the debts of the privatization agency and the building firms of the GDR. Including this effect, the total state deficit added up to 9.5% of GDP
** Without UMTS incomes. Including this effect, the national budget showed an excess of 1.1% of GDP
Source: Nationales Reformprogramm 2012 (BMF: Bitte aktualisierte Zahlen als Excel-Datei bereitstellen)
Deutscher Bundestag (2012, 52)

If one considers the budgets for 2013, 2014 and the proposed budget for 2015, one can distinguish a continued commitment to deficit reduction within the German government. This is particularly true for the proposed 2015 budget, which aims at achieving a balanced budget. This aim was already stated in Table 5.38. The German government empowered the ministry of finance to contract debt up to a maximum of 6,5 Billion Euros for the fiscal period of 2014 and true to its aim to not contract any new debts as of 2015 (Bundestag June 2014, Bundestag August 2014). Should this law project be accepted in its current form, it would mean that the non-contraction of debt would become a legal requirement for the German government.

This is a potentially significant problem considering that the German economic growth projections while positive, remain very low, and neither are the growth projections of the other European countries providing any further encouragement (IMF World Economic Outlook 2014, 50).

In addition, the income projections for the 2014 and 2015 budget project show an increased income of approximately 7 billion Euros through taxes for 2014 (Bundestag 2014, June) and another increase of approximately 10 billion Euros for 2015 (Bundestag 2014, August). This increase in state income I find highly unlikely considering the German economic growth projections. Furthermore, the designed savings in the 2014 budget are primarily geared towards reductions in investment, which foresee a reduction of approximately 8 billion Euros in investments within the different ministries (Bundestag 2014, June). The 2015 budget once more contains an increase in investment of approximately 1 billion Euros for 2015 (Bundestag 2014, August). However, this does not signal a new effort at funding a recovery considering the size of the cuts in investment in 2014.

5.4 Conclusion

The German economy has performed better than other European economies during and after the 2007/2008 financial crisis. Its growth projections are better than the growth projections for the rest of Europe. The price German society is paying for this growth, however, does give cause for concern. Based on the data analysis in this chapter, this thesis was unable to establish a clear pattern that would unambiguously demonstrate the effects of the social and economic reforms enacted by the SPD/Green government by the end of 2005.

However, some conclusions can be proposed. The most direct impact that the reforms have had so far was on the lower income job market. However, the long-term implications of these reforms for German society and to a lesser extent to the German economy are not yet foreseeable, particularly since the 2014 elected CDU/SPD government is moving to change parts of the welfare programme enacted by the SPD/Green government. Through the introduction of the 400 Euro jobs and the restructuring of the unemployment benefits into DOLE1 and DOLE 2, the Hartz reforms have revitalized the German market and spurred hiring, production and economic growth as well as bringing the German budget back into line with EMU and Maastricht (SGP) criteria which have been supplemented recently by further rules and regulations (see Chapter 3). The continuous and continued reduction in unemployment in both east and west and the continued maintenance of the EMU and Maastricht criteria on economic stability and debt is a further testament to the success of these reforms in economic terms.

This thesis further concludes that the German government, at the time it enacted these reforms, was mindful that they were necessary to rejuvenate the employment market and put the German economy back on a path of growth. The SPD/Green government, however, failed to follow through on a systematic change that would affect abilities to re-enter work at all levels of income and employment instead of just the lower income band. These reforms had, as a consequence, a unilateral liberalization of the labour market, which actually had a negative effect in terms of social cohesion and upward mobility.

Reduced inequality, which the SPD/Green government had vowed to tackle (in part through empowerment of the individual) has not been realised. Although there are now more people employed than before, their average earnings have gone down. These negative effects especially affect single parents and children. The number of people whose pay is unable to provide them with sustenance has increased, as has the likelihood of them remaining in, or sliding into, poverty. One way that neo-liberalism provides for people in these circumstances is a greater financial participation in the financial market or an increase in private debt in order to finance individual expenditure, which the financial market can once again use to trade upon and further increase their profits.

These reforms did have a positive effect on German economic performance and on the German state budget, transforming Germany once again into Europe’s strongest economy, allowing Germany to regain much of the structural power which it had lost to the EU institutions in the 1990s with the creation of the EMU and the convergence criteria as well as the globalization of the economy and the neo-liberal ideology which it included.

This being said, this chapter also showed a mixed international picture. The economic success of these reforms, which enabled Germany to weather the 2007/2008 crisis have left Germany with an increased reliance on its export sector. The majority of Germany’s exports continue to go to Europe and the USA where the crisis continues to rage.

The establishment of the EFSF and the ESM were designed to calm the markets and allow the EZ countries to resolve the crisis raging within it. Germany, as one of the biggest contributors to those programmes, was able to strongly influence the direction these institutions would take. The economic successes the Hartz reforms helped achieve, have provided the German state with an excellent argument in support of their solution of austerity to resolve the EZ crisis. According to neo-liberal market logic, which Germany has espoused, the crisis needs to be solved through internal adjustments such as reduced spending and increased national income. This can be achieved by increasing personal responsibility and reducing the role of the state in welfare provision thereby “forcing” people to work and providing the industries with cheap labour allowing industries to produce more and make larger profits thereby helping revitalise the economy and help it grow.

The neo-liberal logic is against using monetary policy to influence inflation or by using large spending programmes which according to their logic and to traditional neo-liberal logic would do nothing to revitalise the economy since it would be unable to get rid of its structural problems.

Considering the 2014 budget and the proposed 2015 budget which no longer includes any borrowing on the national level at all, the German government seems to have firmly embraced that position. This is particularly so since it plans to save 10 billion Euros in investment in 2014, leaving the market ample room to potentially expand within that room that the state has left. Considering the weak German growth and the weak state of European and global growth, this thesis makes the judgment that, the increase in tax revenue that the German government expects for the year 2014 and 2015 to be overly optimistic. It would also point out that the current German emphasis on debt reduction and adherence to the convergence criteria are not in keeping with future growth.

The trajectory Germany is currently on will only further widen the gap between rich and poor, not narrow it. Current economic data suggests that it will also hurt future growth not only in Germany but also in the rest of Europe. A single-minded pursuit of deficit reduction and liberalization of employment holds many dangers that the German government is either not aware of or has decided to ignore. This attitude poses many dangers for the economic and social stability of Germany in the medium and long run. The German government should consider a less headstrong attitude towards different economic theories and principles, particularly public spending and higher inflation levels. Their insistence on low inflation levels has the potential to turn into deflation (Kwasniewski 2013) and the hording of money by consumers and consequently less consumption. Public spending, as Keynes already argued in Chapter 2, is an ideal way for the government to foster domestic consumption, which is something that is still lacking in Germany and considering its high reliance on exports would be a welcome diversification of its economy. Some impulses have been set in that regard with the implementation of the minimum wage, which should foster internal consumption.

What is also an option is the increase in private debt within all segments of the population to compensate for the reduction of salaries and the reduction in welfare. However, this option would only further empower financial markets and potentially create yet another unstable situation. Considering the reforms undertaken which were analysed in Chapter 4 the repeat of such a crisis in the same way would be unlikely for now, another such crisis may have worse impacts than the impacts that were experienced by the most recent crisis. This point will be further considered in Chapter 8 of this thesis.

Chapter 6 Social Security the French Way

6.1 Introduction

This chapter analyses what happens when a state tries to maintain its model of welfare despite economic recessions and global economic pressures. This chapter focuses on the case of France. France, as a nation, has a long history of social movements and social upheaval as well as of strong central leadership, which left a distinctive mark on French society (Dyson 2009). The French dirigiste tradition of government intervention is diametrically opposed to the free market, non-interventionist framework, which Strange and Crouch pointed out in their analysis, is spreading around the world and with the implementation of the Maastricht Treaty and the Economic and Monetary Union (EMU), this liberalisation has also come to Europe.

Currently in its Fifth Republic since the overthrow of the French Monarchy, Marxist and socialist principles have evolved and have been eroded over time but their principles have endured in French politics and continue to influence and shape French social and political thought. This socialist influence is shown in the French national motto: *Liberté*, *Egalité*, *Fraternité* (liberty, equality, brotherhood/togetherness, own translation).

This analysis will help understand the French position within the European neo-liberal framework and its opposition towards the German support of neo-liberal concepts and austerity demands aimed at pleasing the market and investors by putting financial discipline before economic growth programmes and European wide affirmative action against unemployment. This chapter will analyse the French government's opposition to the German government's austerity demands towards countries applying for protection under the ESM framework from a historical and constitutional perspective.

The French state's sense of care for its citizens is deeply engrained within its traditions as well as within French constitutional law. Both have helped shape all welfare legislation since WW2 and, with it, the conceptions and expectations of the French citizenry. Social and labour market reforms of the scale and scope undertaken by the German government would be very difficult to do as they run opposite to the state's very understanding of its role in society. This chapter demonstrates how the French state has gone about defining that duty of care; Chapter 7 will demonstrate the different contributions and payments that have been made by society and the state to discharge this duty.

This chapter begins its analysis by investigating the French state tradition and the French constitution as well as other constitutional documents, which are the basis and provide the framework for all social security legislation in France. This is done to provide a first sense of the type of government action that is produced on a political-economic level in France. In order to present the best way by which these documents have shaped the French understanding of social security and welfare, their analysis will be divided into their areas of influence, i.e. *Droit Social* (social law, own translation) and *Droit de la sécurité sociale*, (social security law, own translation). The former is a term, which is used to describe all laws governing internal and external firm relations and contributions to social security and their levels of people in work (i.e. an amalgamation of labour and work legislation). The *Droit de la sécurité sociale* governs all other aspects of social security, their health insurance, unemployment insurance *etc*. completing the set of legislation governing social security. Both these laws will be investigated in this chapter.

In order to appreciate the reasons for a lack of reforms of French welfare and social security further even in the face of changing economic circumstances and understanding of the workings of the economy within the French government, it is necessary to understand the French labour unions and understand their position and influence within the socio-political-economic framework of the country. French unions occupy a special place in French society, due in part to their mention in the French constitution, making them a mainstay of French economics and French society. The voice and power of the unions still resonates deeply within French society and with the French government.

The final and most substantial section of this chapter investigates the French concept of social security and welfare and investigates any changing conceptions of welfare and social security within the French government. The subsequent governments of the Fifth Republic have more or less successfully adapted and applied dirigiste strategies to deal with national as well as global challenges. Although, all governments have shaped French regulations in one way or another before or since the Presidency of François Mitterrand, it was his presidency that instituted the first major changes to social security since the end of WW2 (Mitterrand 1981). These changes heavily favoured the French working population and the subsequent governments of Jacques Chirac and Nicolas Sarkozy have continued to govern under that framework and left welfare and social security regulation largely untouched for a long time. Neo-liberal economic reforms along the lines outlined within the agreement on EMU and the Maastricht treaty have only been instituted slowly and at a high political cost, due to their challenge of the core of the French state nature. It was only beginning with the Presidency of Nicolas Sarkozy and the 2007/2008 financial crisis that the “dirigsite” position came to its limit of adaptability under significant pressure from the global markets and reforms of labour markets and government interventions began. This implementation began with the commissioning of a report for French growth outlining the reform priorities for the government. This report was followed by a second report for growth right after the financial crisis hit Europe. Both these reports epitomize the French effort to maintain their dirigiste positions in the face of global pressures by adapting their concept of an interventionist welfare state to modern times.

This chapter will also demonstrate that the slow course of reforms has influenced France’s political-economic standing within Europe since France did not follow quickly the European trend towards greater market freedom and a more market oriented economic policy, by implementing reforms, turning over government responsibility to the market. French slow implementation of austerity was another aspect of the slow progress of neo-liberal economic reforms. Chapter 7 will consider the economic impacts of a dirigiste report by Alain Juppé and Michel Rocard, which challenged the austerity orthodoxy in many ways.

6.2 State traditions and the constitutional rights to work and social security

As opposed to Germany, the French state is strongly influenced by its Catholic heritage and their concept of a centralised state designed to repress individual action and help guide society for the good of all. This aspect of centralised power was combined with both catholic as well as roman concepts of a centralised state, which have survived until today. One could argue that the forming of the fourth republic has even reinstituted a Caesar type figure at the head of the state in the form of the President.

The influence of Catholicism can be further seen within the notion of care, which is deeply embedded within the French state tradition. The catholic doctrine has influenced a notion of a:

> …'unified' self which realized freedom and goodness through its sociability, openness and generous character (Dyson 2009, 172)

The points introduced above are largely responsible for the conceptions of law and the state analysed here below.

The right to work and to social security is guaranteed by law and by the constitution in ample form. The Preamble to the Constitution of the Fourth Republic of the 27th October 1946 in eight of eighteen points enumerates the rights of the workers and the duties of the state (Carcassonne 2011). This Preamble to the French Constitution is considered to be a part of the constitution, proven by the French constitutional court whose rulings often refer to the preamble with regard to welfare decisions (Carcassonne 2011).

While welfare provisions are now fully integrated within the French constitution and French law, this process was started as far back as the Third Republic. The preamble to the constitution of the Fifth Republic was written for the constitution of the Third Republic and copied to the constitution of the Fifth Republic upon its creation. The preamble to the constitution of the Third Republic was created since the French State decided that it wanted to:

> …integrate the working class within society, rather than letting it continue a marginal existence, with the challenges to social stability that presented (Gaudu 2008, 396).

This discussion was very much in keeping with the state tradition of the integrality of society analysed above. The French state tradition sees it as its duty to bring all groups within society under the leadership of the state so as to provide all with equal access and thereby provide them the freedom of self-realisation.

6.2.1 Labour Law

Labour law in France is an umbrella term of the "Droit social" and the "Droit du travail" (labour law and employment law) (Troper 2008). The points enumerated below form part of the preamble to the constitution of 1946 combined with the French constitution and the French human rights charter, these documents form the basis (both ideological and legal) of all French welfare law.

> 5. Everyone has the right/duty to work and the right to get a job) (No one can be harassed in their work or their employment because of their origins, their opinions, or of their beliefs (own translation) (Carcassonne 2011, 428).

This sentence, as Carcassonne (2011, 428) notes, is interpreted by the French constitutional court (FCconC.) as first and foremost constituting a moral duty for the worker. It also constitutes a right of the worker, creating the obligation for the state to provide the circumstances within which all people can find work. Failing that, *it is the duty of the state to provide people with assistance during their time of unemployment*. It should further be added that the moral duty to work does not allow for the non-payment of the Revenue Minimal d' Integration (RMI) (Income for people who are unemployed) if no attempt is made at finding work (Carcassonne 2011).

> 6. Every man can defend his rights and his interests through union action and join any union, which he wishes to be part of. (own translation) (Carcassonne 2011, 429)
> 7. The choice to strike can only be exercised within the framework of the law that regulates it (own translation) (Carcassonne 2011, 430)

Both these points allow for unionization and strike action. While on strike, strikers must respect the laws regulating strike action. These laws are not allowed to infringe upon the character and impact of the action, the strike is supposed to achieve (Carcassonne 2011, 429-430).

> 8. Every worker participates through their delegates in the collective determination of the work conditions as well as the running of the companies. (own translation) (Carcassonne 2011, 430-431).

This point gives quite wide-ranging powers to the legislator to define conditions and rules of work in whichever way he sees fit, although preventing the employer from instigating a wide-ranging repeal of workers' benefits. (Carcassonne 2011, 430-431). Additionally to this rule, legislation has been instituted to have *unions and labour organizations consulted in matters concerning employment and welfare* (Matignon 1936). Point eight has also made possible the establishment of the workers councils. These councils play an important role in administering the relations between employer and employees in a firm; they also provide a check on employer power.

> 9. Every good or company whose resource exploitation or management or market share acquires the characteristics of a national public service or a monopoly, must become the property of the collective (own translation) Carcassonne 2011, 431).

Article 9 is used principally to hinder or prevent the privatisation of companies (Carcassonne 2011, 431). They also made possible the nationalisations of various industries during the early days of the Mitterrand era (see section 6.4.2).

The points enumerated so far do demonstrate a heavy socialist and communist presence influencing the writing of this preamble. This is unsurprising considering that French communists held a lot of sway in the 4th Republic due to their involvement in the fight against the Nazi occupation of France in WW2. It is a further testament to their influence that this preamble was attached to the constitution of the Fifth Republic.

Although designed to empower workers, which this text undoubtedly does, some of these points have lately been re-interpreted in such a way as to provide a bigger room for manoeuvre to the state in its labour and social security regulations (Attali 2008 and 2010). At the same time, the way in which this text is worded, clearly demonstrates that French legislation principally favours workers and workers' rights.

6.2.2 Social Security Law

> 10. The nation ensures that the conditions necessary for the development of the individual and the family are met (own translation) (Carcassonne 2011, 432).
> 11. The nation guarantees to all, especially to the child, the mother and to the old workers, the protection of health, material security, rest and leisure. Every human being, who due to their age, their physical or mental state, their economic situation, finds themselves incapable to work, has the right to receive from the collective the means by which to ensure an adequate existence. (own translation) (Carcassonne 2011, 432).

Points 10 and 11 provide the legal basis upon which all social security legislation "droit de la sécurité sociale" is based. It also enshrined it within the social fabric of the French state. The constitution does not permit there to be no welfare state. However, it does allow changes to it, which replace or change provisions as long as they provide the same results without diminishing the benefits received to individuals and society (Carcassonne 2011, 432). This is a double edged sword for governments, as it essentially allows it to change social security institutions to adapt to changing circumstances, but does not allow them to substantially reduce them without any adequate replacement. This also allows in principle the option to the state to replace the state provided service with a market provided service, as long as that service does not disadvantage the French population. This means that in France, convention dictates that social security is essentially open to greater protections but is closed to reduce protection even if circumstances might demand it.

The points enumerated so far, also demonstrate an essential point of the makeup of French welfare upon which the French population and the French government are unwilling to compromise, even with European pressures towards austerity and a greater openness towards the market. This unwillingness is further demonstrated in France’s recent Presidential Election of the Socialist François Hollande who vowed to renegotiate austerity (Fouquet & Deen, 2012) for France as well as on a European scale (Duch-Guillot, 2013).

> 13. The nation guarantees the equal access of the child and the adult to education, formation and culture. The organization of free and secular public education to all levels of education is a duty of the state. (own translation) (Carcassonne 2011, 433-434).

Point 13 has the same effect as Points 10 and 11 though focusing on education instead of welfare. Since it is a duty of the state to provide free education to its population, it is understood that free education is going to continue to be a permanent fixture within the budget and the duties of the state. A further anchor of social security in French Society was the "ordonnance du 4 octobre 1945". This ordinance aimed to

> take away the insecurity of tomorrow, which creates in the workers a feeling of inferiority, which is the real basis of the profound division of classes (own translation) (Badel 2007, 14)

Although not a constitutional amendment, it remains in law to date and provides the principal basis for the different types of social insurance provided by the state and the private sector. These points are also demonstrating a heavily communist influenced language, which stems again from the great influence the French communists yielded in French politics at that time.

These constitutional preambles and ordinances follow the state tradition here analysed and demonstrate that the French state was always intended to be a major part of the political-economic activity of the country. This tradition of direct influence by the French government in the French economy was called *Dirigisme* (direction giving (own translation) (Hall, 1986).

6.2.3 The particularities of the French style of government

In France, the office of the President of France and the office of the Prime Minister (PM of France) are by design closely integrated and interlinked. In most democratic systems, the President (the executive branch) is seen as a figurehead and is limited to a representative role and the exercise of executive power (i.e. signing Decrees into Law). Presidents usually are not elected directly by the people but through a vote in the national legislative chambers (Germany and Italy are examples). In France the office of the President is the most powerful in the political position in government. The president appoints the prime minister who then can form a government; the President cannot dismiss the PM but can ask for his resignation (Troper 2008).

A check on the powers of the President is that most of his legislative powers require the cooperation with a parliamentary majority, the PM or a counter signature by a minister depending on the issue (Troper 2008, 23), which does give the executive a certain independence from the legislative.

Initially the President was elected for a seven-year term and the National Assembly (Assemblée Nationale) was elected for a five-year term. This made it possible for the party, which holds the majority in the national assembly, to be different from the party from which the president was elected (Torper 2008). This case is called a *cohabitation* (living together, own translation) where the president appoints a prime minister who would be able to command a governable majority in the assembly. Together, the President and the Prime minister form a cabinet, though theoretically the naming of ministers is the prerogative of the PM (Troper 2008). *Cohabitation,* as the name would suggest, was a system designed by de Gaulle to eliminate as far as possible political division. More often than not, however, this organization of government has caused a political standstill (for example, the Mitterrand and Chirac cohabitation) - the very thing de Gaulle had tried to avoid.

During *cohabitation*, the President continues to preside over the weekly meetings of the council of ministers (Sirinelli, 2013). Since the President needs to rely on the assembly, the PM or other ministers to exercise the full breadth of his influence and powers, which are now controlled by the opposing party, his influence is reduced and that of the PM amplified. However, the President is never entirely powerless as he traditionally holds the prerogative over the foreign affairs agenda (Troper 2008, 24). Depending on the size of the majority in the national assembly, the PM may go the road of the decree, which does not have to be voted on in the Assembly but needs to be signed by the President. Other than laws passed by both houses of government, the President can refuse to sign decrees, providing him a further avenue of influence (Teyssier 2011).

6.3 The State and Labour unions

The reason for the power of the labour unions is due to the power and influence that the communists and the left in general held within the fourth republic, this allowed them to substantially shape work regulation for generation to come.

6.3.1 The French business model: A dirigiste tradition

Charles de Gaulle as he formed the Fifth Republic used France's state centric tradition to create or at least reinforce a sense of French unity and, implicitly, a tacit acceptance by the French of the policies of its government (Sirinelli 2013). The planned economy was a logical development of this state-led principle.

> By "providing an image of a growing economy within which production would be guaranteed to find "outlets", the initial plans according to P. Massé, have played well their roles of "reducers of uncertainty". (own translation) (Caron 1995, 272)

The planning of the French economy was also quite helpful in aiding the French economy transition from a closed to an open economic system (Caron 1995, 272) at least initially. This "French style" of government by giving direction to the economy has remained a staple of French government. Although, as Holmes (1992) (see also Teyssier 2011 and Hall 1986) correctly argues, the amount of power the French government can use to influence industry and the economy has often been overstated (mostly by the French government), particularly since the advent of the neo-liberal global economy. One of the reasons for that fact is that before the Mitterrand presidency, when the European idea was still developing and states and economies were still much more insulated from the global market forces, French *dirigisme* was mostly without structure and consistent rationale except for trying to maintain failing industries afloat (Green 1983, Dyson 1983). As Strange (1998, 1997, 1996) pointed out, the liberalisation of the global markets enabled through continued non-decisions by major institutions and nations, has created a global economy (a global financial economy in particular), which it is impossible to control particularly for a single country. France was no exception. The gradual opening of the French economy to the global markets and further participation of France within the European project of political and economic integration (meaning trade liberalisation and harmonisation of practices and greater economic rigour) brought with it a more concerted effort to direct the economy and develop a real strategy to ensure that French industries were given the opportunity to compete in the global market. A good example of such a difficulty is the Mitterrand Presidency. During his Presidency, the French government realised that the powers of government were more limited than it had thought and needed to be applied more strategically (Green 1983, Dyson 1983).

Although, the constitutional points enumerated above, do prescribe a large state presence within French society. French *dirigisme* has, however, suffered significant pressures from globalising economic forces particularly from European Union legislation to continue to liberalise its economy and reduce the state influence exerted onto the economy. These have significantly circumscribed the state's power to manage exterior and interior market processes (Teyssier 2011).

The French government under Mitterrand had fewer powers to compensate for external impacts on the French economy than the governments under de Gaulle for example. This was so because France had worked with Germany on a closer political economic integration of the European economies culminating in the establishment of the EMU and the Maastricht Treaty. The establishment of that treaty made the French economy more open and more dependent on the global economy (Howarth 2002). The French government nevertheless remains an important arbitrator for internal impacts, in particular as a regulator and adjudicator of labour law, alongside labour unions.

The French government sets industry regulation and environmental legislation as well as maintaining close links to industry without exerting direct influence upon it. Many corporate CEO's of French companies graduate from the same schools as French government officials thereby creating social links between government and industry. Labour unions also take advantage of these links to aid in their labour negotiations, making the state a nexus of economic activity (Suleiman 1978).

6.3.2 Labour unions

State influence in industry and on labour is much greater in France than in Germany. One of the reasons for this is the close ties between the state and French corporate management as mentioned in the previous section. Due to this "intimacy" between the state and corporate France, unions,

> instead of saving money so as to be able to afford strikes, French Unionists relied on their ability to influence the state to create better conditions for workers (Gaudu 2008, 396).

This level of intimacy between Labour once again demonstrates the central role the state plays within the French political economy. It was reached through the signing of the “Accords Mattignion” of 1936 (Ministère du Traviail 1936). These Accords created the legal requirement for laws relating to employment to be passed only with labour union consent.

> Collective Bargaining is a Labour Union monopoly. Apart from small exceptions, employers cannot negotiate collective agreements with other workers' representatives, such as the elected workers councils (Gaudu 2008, 409).

In 1950 aided by the PCF (French Communist Party), a law was voted reaffirming the necessity for unions to sign collective agreements. Only the most senior unions with the greatest membership, the highest number of dues paid, the greatest experience and biggest patriotic attitude during the war were allowed to sign these contracts as representatives of the workers (Gaudu 2008 and Mouriaux 2013). These accords also established the minimum wage: the "salaire minimum interprofessionnel garanti" (SMIG) (Mouriaux 2013, 19-20).

> These collective bargains are generally done on the industry level binding all companies of that industry to that bargain. However, for issues relating to social security or unemployment benefits bargains are often struck on the national level (Gaudu 2008, 399).

Unions, while sharing the same struggle and the same principles as the PCF, always made a point of being independent of politics or at least appear to be independent of it (Mouriaux 2013) so as not to lose credibility with their members as well as allowing impartial negotiations with other political parties. Irrespective of the independence, or appearance thereof, of the French unions, the ascension of François Mitterrand to the French Presidency saw union expectations for more powers and influence rise. Mitterrand met those expectations but the results were contrary to the unions' expectations.

On the one hand, Mitterrand's Presidency did provide unions with more powers. The Lois Auroux (Noblecourt 2012) provided the unions with power to shape working conditions, negotiate for working time and salaries in the firms, reinforced rights of the unions within the firms and finally allowed the workers to express themselves on the conditions within the firm (Noblecourt 2012), but, on the other hand, the attribution of these powers made them lose a lot of their influence and members, so much so that by 1985 labour unions had lost as many as half of the members they had at the height of their power (Mouriaux 2013, 80).

This loss of power consequently affected the unions' ability to function in the way they had up until that point. The reduced number of members meant a shortage of dues, resulting in a reduction in the number of initiatives that the unions could pursue effectively. Consequently, efforts to achieve equality of men and women in the workplace were progressively reduced, as were the efforts to achieve equality for immigrants. The ecological ambitions of the unions also fell victim to their reduced funds. Because of the lower incomes the unions now faced, they focussed all of their efforts on job protection (Mouriaux 2013) and a greater emphasis on national strike action.

Coming into the new millennium, unions remain unable to attract new members, which also leave them unable to achieve deals satisfactory for all parties concerned in the labour negotiations since government policy can only go so far to accommodate labour unions since the French government also has to be mindful of external pressures. This incommensurability of their positions caused an increasing number of “accords minoritaires” (minority collective bargains, own translation) to be signed throughout the first decade of the 2000s. This effectively means that accords were established on a case-by-case basis between the state, industry and specific unions (Mouriaux 2013). These minority accords allowed the French government to transpose into law new social and economic reforms, which go against union beliefs (Mouriaux 2013).

In 2008 the system, which defined labour union involvement within the collective bargaining process between the state, the labour unions, and industry, was reformed (at the recommendation of the 2008 Commission for Growth Report - see the last section of this chapter). This reform was done with the help of a collection of workers unions (CFDT, CGT) and employers’ associations (MEDEF, CGPME) to reflect the new realities of reduced union membership as well as a more adaptable work force capable of reaching agreements more quickly. It was signed into law in 2008, in an effort to revitalise the social dialogue among the three negotiating parties (State, Employers and Unions). For collective agreements to be effective now, the agreement still needs to be signed by representative unions, however, the definition of how representative a union has to be, has been reduced to having a presence in a sufficient number of industrial sectors. Collective agreements now count as accepted if unions representing 30% of the workforce sign it and if there is no opposition of unions representing more than 50% of the workforce (Mouriaux 2013, 106).

This reform was a blow to union power since this reform substantially simplified the procedure required by the government to introduce new labour reforms economy wide. It reduced union bargaining powers and increased those of the state and employers, which in turn allowed for greater liberalisation efforts to be instituted (in principle). After the financial crisis had hit France and the first reforms of the Sarkozy government were starting to be implemented, all the major and recognised labour unions put out a common set of proposals on how to engage with the financial crisis. Their main concern was the security of employment and retirement provisions. The text put forward five points, which the unions argued the state should embrace.

1. Give priorities to the maintaining of employment in a context of economic crisis.
2. Wage policies: improve purchasing power, reduction of inequalities
3. Orient economic dependency towards employment and purchasing power
4. Preserve and improve collective rights
5. Regulate the international financial sphere

(own translation) (la déclaration commune des syndicats de salariés, 2009)

Although these demands follow the line of argument that could be expected from labour unions, the unions put qualifications on some of those statements. The unions do not demand guarantees against redundancies but a commitment by the government to minimise them. Their demands prioritize worker protection at the expense of an internationally expansive economic policy, which would require either pay decreases or increased redundancies (i.e. labour liberalisation).

Throughout the Fifth Republic, unions and industries lived under governments that favoured one side or other. The following section investigates the tenures of three presidencies whose decisions have had significant impacts on the French economy and on French society.

6.4 The EMU and its impact on the French model

The EMU first began with the Exchange Rate Mechanism, which was created a few years after the collapse of the Bretton Woods System and fixed the European currencies exchange rate margins in preparation for the establishment of the EMU. France joining the ERM and the EMU meant a drastic change to the French economic and monetary policy towards a more market-oriented system that is more open for competition and foreign investment. This was a move that France did not take voluntarily. Considering the loss of competitiveness and increasing inflation (see Chapter 2, 3, 7), France was compelled into action.

While the integration within the EMU has opened some new markets for French goods, the progress of liberalisation of the French economy has been slow. The French legal system as well as the French labour unions as considered in the sections above pose a number of socio-political restrictions on the French government do to so. The French state, considering its history of directing economic progress, was also reluctant to cede more economic power and centralised control (Dyson 2009) to the market and to allow access to the French financial market and French industries in order to finance public and private sector projects (Howarth 2002). The liberalization of the economy and particularly of the financial industry brought the French state and its economy added income as well as added pressures.

The adherence to EMU rules translates into adherence to German principles of sound money and low inflation in order to be able to attract the foreign investments, which the opening of the French financial market allowed for companies and the state to access a great number of funds to finance its projects. However, this means that government debt needs to be brought under control and its increases can no longer be equalled out by currency devaluations (Howarth 2002).

This, only further fuels the French distrust of globalisation and liberal market practices, which is why the French adherence to the EMU is publicly sold by the state as a way to enhance French competitiveness by harnessing the free market powers with French *dirigisme* thereby securing the French social model (Howarth 2002). The French state defined its liberalisation and greater use of neo-liberal concepts as helping the dirigiste method to be more viable within the economic surroundings. This definition will find its limits once the dirigiste method can no longer be adapted and the neo-liberal concepts will have to be embraced even further.

The French state also saw its participation within the EMU as a way to curb German power within the rulemaking for the EMS and the Maastricht treaty. The French state attempted to do on the European level what it was attempting on the national level i.e. to harness economic activity on a European scale by allowing for some austerity or as it was then called rigour but also trying to provide some leeway on its application as well as to create programmes for investment in the European economy (Howarth 2002).

The French commitment to the EMU shifted the power relations not only between the French state and the European institutions but also between different sections of the French government itself. The French state's move towards the EMU empowered the conservative liberals in the French state by reinforcing the influence of the treasury and the influence of the Bank of France (Howarth 2002, 147). However, even with this increased amount of influence the EU has, progress in this area was and continues to be slow due to the legal framework within which France has to operate and the popular aversion to such reforms as well as the subsequent political reticence towards such reforms.

What helped to reduce the French reluctance to integrate its economy with the other European economies was the opportunity to once again become a player on the world stage. This next section will consider the political process within France to establish how and why this progress has been so slow.

6.5 The Years of Mitterrand and Chirac

These four presidencies were the first ones to have to actively engaged with the concept of a neo-liberal global market and negotiate its pressures upon the French economy and the French state.

6.5.1 Mitterrand

The election of François Mitterrand in 1981 sounded the final death of the Gaullist regime, which established the Fifth French republic. Mitterrand became the first Socialist President of the republic, and expectations were high within the Parti Socialiste (Socialist Party) (PS) and in the Parti Communiste Français (French Communist Party) (PCF), that François Mitterrand would put France on a path towards socialism (Sirinelli 2013, Teyssier 2011). After being elected President, Mitterrand used the powers of the Presidency to dissolve the Assembly triggering new elections in 1981 that the Socialists won convincingly, providing them with a majority in the National Assembly and providing Mitterrand with the full breadth of power in the office of the President (Sirinelli 2013, Teyssier 2012).

True to the socialist doctrine, their economic argument was one of redistribution both of wealth and of workload. Based on Keynesian principles and French state traditions, government influence over the economy was increased (Teyssier 2012). These reforms represented a countermovement to the neo-liberal advance and the social reforms, which were implemented in the UK under Thatcher and in the USA under Reagan (Teyssier 2012). 39 of the 110 propositions enumerated by Mitterrand during the 1981 campaign related directly to the economy. They all follow not only a socialist logic but also a Keynesian economic logic.

> 16 - A programme of great public works, from construction of social housing and collective equipment (crèches, school restaurants, housing for children) will be engaged starting from the second semester 1981 (own translation) (Mitterrand 1981)
> 18 - 150000 places will be created in the public service and social sectors in order to improve working conditions and capacities (in health, education, Mail, and Telecommunication, etc…). 60000 places of collective use will be made available to associations and local collectives. (Own translation) (Mitterrand 1981)

These first two points give a good example of the Keynesian logic of public works and expanded state employment to reduce unemployment and stimulate internal growth. They also provide a good example of the *dirigiste* tradition of the French state, focussing on state-led impulses to the economy.

> 20 - The franc will be defended against speculative attacks. The industrial and agricultural development combined with energy savings will make growth less dependent on imports. Until 1990, foreign trade will be reduced to less than 20% of GDP. (own translation) (Mitterrand 1981)

Defence of national interests such as defence of the Franc and the increased self-sufficiency of France has Gaullist attributes on the face of it, but it is a further aspect of the dirigiste tradition of economic control by the French state. It is also a point, which would later demonstrate the limits of the state powers when it comes to changing international economic trends.

> 21 - The public sector will be increased through the nationalisation of the nine industrial groups, of the iron industry and the defence industry and the spaces financed by public funds, as designed in the Communist Party Programme and the Socialist Party Programme (own translation) (Mitterrand 1981)

This is a purely ideological statement. There is no real economic necessity for a complete nationalisation of industries. It does, however, provide yet another good example of the dirigiste tradition, as well as a plain text application of the constructional preamble allowing/requiring for such nationalisations as well as fitting squarely within the communist tradition.

> 23 - The working day will be progressively reduced to 35 hours after negotiations between the social partners. The fifth team will be instituted in the annoying jobs. A fifth paid week of paid holiday will be instituted for all. (own translation) (Mitterrand 1981)

> The acquisition by the state of the big enterprises dominating the key sectors of the economy will allow for better planning and rationalising of industrial activity and will allow for an in-depth modernisation of the French economic structures by improving their competitiveness. The "new public sector" needs to be the tip of the spear of the new political economy (own translation) (Mauroy in Teyssier 2012, 382-383).

This point combines both political dogma and economic reasoning. The logic behind it is very simple. By reducing the working week and retirement age, the government provides more space for new people as well as young people to enter the jobs market, thereby reducing unemployment and strengthening consumption. This is a demand-economic proposition as was suggested within the second Beveridge plan (see Chapter 3).

> 35 - Direct taxation will be reduced for the low-income earners and increased for the large earners to reduce income differences. The tax credit will be deleted (own translation) (Mitterrand 1981).

This is again a combination of political dogma and economic reasoning though not as solid an economic reasoning than in the previous point. It is a sound strategy to encourage increased consumption of goods. Reducing the taxes on low earning incomes will leave more income for consumption. The increase in taxation on the higher earning incomes will, for one, offset the reduction in tax income from low earners but will also impact less on consumption since consumption of high earners will be less affected by the tax increase than a low-income earner would.

These are just some of the points enumerated by the Mitterrand plan, but they do show a clear train of thought in their attempts to stimulate the economy. Aside from the political action plans, it is an earnest attempt at creating an economic boost by bolstering employment and internal consumption. All of the points enumerated above had been implemented or started early in Mitterrand's presidency. The 39-hour week was introduced with the pension at 60. The tax on the rich and the nationalisations all were made in the first 3 years of his presidency (Teyssier 2012).

The dogmatic stance of these reforms as well as their wording demonstrates the strong force that the French Communist Party still was on the left at the time (Teyssier 2012). Without them, Mitterrand would not have been elected; hence a quick show of good will towards them was required. The appeasement of the left and far left, though politically necessary, came at a high cost, especially since these reforms came after the first and second oil crises. Whereas the more moderate actions taken from Keynesian theory were designed to reverse or at least to mitigate the effects of this crisis by increasing employment and bolstering consumption, the more radical reforms put great pressure on the budget. An example of that can be seen in point 20 (which can be seen as a response to the first oil shock) where a greater independence of outside energy sources was being proposed.

The idea of the French government was simple, one could go as far as to say too simple, since the solutions focussed on internal changes to the economy without being mindful of the influence and the power of the global market had on the national French economy (and vice versa) (Strange 1988, 1995). The French government's concept of economic stimulus consisted of an increase in jobs (through creation of public sector jobs and the reduction of working hours and the reduction of the pension age) and a more equalised income system. The government could increase domestic consumption, thereby boosting domestic growth and weathering the global economic downturn created by the first oil crisis without causing undue burden to society (Teyssier 2012).

With the second oil crisis in 1979 also came another economic global economic crisis. Worldwide energy prices soared, consumption on a global level declined and debts, especially national public debt, started to rise. France did not come through this crisis unscathed: France's public debt soared and the French economy started contracting significantly in 1982. As opposed to the Gaullist principles of independence and self-reliance, which would have meant protectionist measures, and a continued devaluation of the Franc and a conditioned increase in inflation, to manage the level of French debt and to allow the French economy room to grow again, the Socialist government of Mitterrand was pro-European integration. Mitterrand decided not to abandon the project of European integration, which was started with the ERM in 1979, by not devaluating the Franc and instead implementing reforms and new taxes to get the deficit and inflation under control. Mitterrand's commitment was further demonstrated by his future willingness to support the project of monetary union (the EMU) (Teyssier 2012). This goes by way of trying to preserve the social model by increasing the weight of the French economy in the world through EU integration. It could also be argued that the French state thought it would be easier to try and shape the neo-liberal economic concept on the European state before trying it on the world scale.

This embrace of European economic integration required the French government to start liberalising the French economy, proceed to a significant cut of the level of inflation as well as a reduction of the state debt. This decision meant that economic restructuring measures had to be taken (Sirinelli 2013). The French government therefore embarked on deeply unpopular measures. The French government raised taxes to increase government revenues and let energy prices rise significantly to reduce French national expenditure in order to pay France's debts. The government also enacted an obligatory loan (to the government) by people who pay more than 5000 Francs in Taxes (Vaslin 2013). Protectionist measures were also instituted and consumption of French products was encouraged to try and reverse the negative balance of payment evolution that came about through the oil crisis (Teyssier 2011; Hardy 2011).

After the resignation of Pierre Mauroy, Laurent Fabius became the new Prime Minister in 1984 and continued this course of reform (Hardy 2011). Fabius, more so than his predecessor, attempted to open up the French economy to the global market. Fabius argued for a more modernized Socialist Party that should not be as beholden to socialist dogmatic principles. According to Fabius, the Socialist Party should strike a more moderate economic course, more in tune with economic reality than with Socialist dogma (Teyssier 2011). This stance although preceding that of Schröder in Germany is reminiscent of these same arguments. It also showed that some politicians on the left could sense the wider implications (see Chapters 2 and 3) of the neo-liberal global economy.

Fabius during his tenure as Prime Minister started a programme of deregulation of the financial industry. As discussed in Chapter 2, Strange argued that (see also Crouch 2011), this act of deregulation, which not only occurred in France but also all over the western World, made the first step that, would lead to the 2007/2008 financial crisis.

Fabius also started to cede governmental control of nationally owned industries making the idea of free enterprise a popular concept. Although largely reversing only some of the more leftist campaign promises of the Mitterrand campaign, it does constitute a reversal of the initial narrative of the

Mitterrand government. These actions were a step forward in the economic convergence process upon which Germany and France had set upon and which would culminate in the establishment of the EMU and the Maastricht Treaty, institutionalising neo-liberal economic concepts on the European level. All the while, France maintained the notion that this new economic model could be directed in the same way than the previous classical economic model.

In 1986, after the national assembly elections, the centre right politician Jacques Chirac became the new Prime Minister of France under Socialist President Mitterrand. It was the first cohabitation of the Fifth Republic, which would last for two years.

The Chirac government socio-economic plan built upon the plan by Laurent Fabius and rested on the liberal concepts of free enterprise and reduced social contributions (Teyssier 2011; Sirnielli 2013). The French government was now committed to the political-economic integration process that was happening in Europe with economic and political competencies slowly moving from national authority to the European institutions. The Chirac government took a distinctly more confrontational line with the President than did Laurent Fabius even though the National Assembly elections only secured Chirac a narrow majority. Because of the confrontational line Chirac took with Mitterrand, the fact that Chirac only had a narrow majority in the Assembly and the fact that the social reforms Chirac proposed were much too liberal for Mitterrand, no reforms were made in the areas of working time or retirement age or on the 5th week of paid holiday (Teyssier 2011).

Therefore, Chirac attempted to enact the more far-reaching liberal reforms by executive decree (ordonnance) under article 38 (Carcassonne 2011) of the constitution by vote of cabinet. The President has a constitutional obligation to sign laws voted on by the Assembly (under article 13), but this obligation does not apply to decrees voted on by the council of ministers (Teyssier 2011). Thus, any kind of far-reaching liberal social or labour reforms were abandoned as they would not pass the narrow majority in the Assembly and would not be signed by the President through executive decree. The only major social and economic reform that was passed during those two years was the repeal of the income tax for the rich (Teyssier 2011).

In 1988's Presidential election, Mitterrand beat Jacques Chirac. To avoid another "cohabitation" with a right leaning party, Mitterrand dissolved the National Assembly and called for new elections in the National Assembly. The Socialists won these elections and François Mitterrand disposed again of a Socialist government, this time under Prime Minister Michel Rocard (Teyssier 2011).

After having secured the stability of his second term in office, François Mitterrand and his government returned to the path of socialism, upon which they had embarked upon in Mitterrand's first term although with a more pragmatic approach since Mitterrand committed France to a path of closer political-economic integration within Europe. The most noteworthy legislative achievements of this government were: the reintroduction of the tax on the rich (which was abolished under the Premiership of Jacques Chirac) and, most importantly, the establishment of the Revenu Minimal d'Insertion (RMI) (Teyssier 2012)

The RMI is a payment available to all people residing in France with not enough income or resources to live on minimum wage (Loi n88-1088). It is based on point 11 of the preamble to the constitution, arguing for the necessary funds to be provided to maintain their existence for those people who (due to age, physical or mental state or their economic situation) are unable to work. This is an important law to consider, as it aptly demonstrates the state's embrace of its caring role for society as well as the state's admission that full employment is no longer a possible scenario.

The RMI is a payment that is available to

> each person residing in France of whom the resources, …, are insufficient to reach the level of the minimum wage, …, and who is 25 years of age or older, or assumes the care of one or more children born or to be born, and who engages to participate in the actions or activities defined by this law necessary to his social or professional habilitation, has a right to the RMI under conditions defined in this law (own translation) (loi n88-1088 article 2, 1988) This benefit programme is funded by the state (own translation) (loi n88-1088 article 5, 1988)

The calculation of the size of the RMI includes all personal wealth of the individual in question. However, this excludes other aid payments such as housing benefits (loi n88-1088 article 9, 1988). The respective local agencies have to provide an annual evaluation of the "insertion" measures. They are tasked with evaluating what areas of support for the RMI beneficiaries need to be expanded or redeveloped, including further education for the people tasked to help those needing "insertion" into society. They are also responsible for harmonising all efforts concerning the RMI and its beneficiaries. Article 42-5 is of particular interest to this thesis.

> the reintegration offered to the beneficiaries of the RMI and defined with them can take one of the following guises:
> Actions of evaluation, orientation and remobilisation
> Actions of public interest or work with or without public aid
> Actions permitting the recipients to recover or develop their social autonomy, to participate with an appropriate level of social aid, in family and civic life as well as the social life of the town and to participate in various activities especially leisure, cultural and sporting activities.
> Actions permitting to provide access to housing, relocation or improvement of the home
> Actions or workshops designed to acquire or improve professional skills, the knowledge and the mastery of tradecraft and capacities of reintegration in the profession. Possibly within the framework of conventions with firms or with training institutes for improving professional skills
> Actions aimed at facilitating access to health care, the healthcare needs cannot be in themselves part of the RMI.
> (own translation) (loi n88-1088 article 42-5, 1988)

To care for the individuals in society was what this state conceived its role to be. The whole of this article established the need for support towards reintegration of the individual into society. As Carcassonne (2011) points out in his constitutional evaluation, there is no explicit mention of a duty to work but therein is contained a moral duty of care by the state, which has developed into the concept of "traitement social du chômage" (social treatment of unemployment) (Teyssier 2012, 513). It is out of this concept that the RMI law has evolved. This concept of the social treatment of unemployment points to a significant and severe problem in France. As was stressed above, the introduction of the RMI is a concession by the government that it is unable to provide jobs for all the people looking for one. It is also an indirect admission of failure of the concept of *dirigisme* since the state through its guidance of the economy is unable to provide full employment.

The state's decisions therefore to care for the unemployed through providing them with an income to allow them to participate in society is commensurate with the French Socialist perspective as well as the French constitution on the state's duty of care. It is this logic, which is still present in

French governmental thinking, and it continues to influence to some extent the thinking of the French government in terms of its opposition to the austerity prescriptions included in the ESM conditions for aid to be awarded to countries in need.

6.5.2 Chirac

In the 1995 presidential election, which François Mitterrand decided not to contest, Jacques Chirac won and became President of the Republic. The first government under President Chirac was a centre right one under the leadership of PM Alain Juppé (Teyssier 2012). Their initial economic policy ran along the same lines as the previous governments' under the Presidency of François Mitterrand. President Chirac wanted to reduce the social rift between rich and poor as well as continue to use dirigiste policies to do so. At this time the EMU was already established and with it the stability and growth pact (see Chapter 3) had come into force. Member countries now had to conform to stricter budget rules and keep the annual debt increase to 3% of GDP (Howarth 2002, 162). This means that the budget deficit to GDP ratio was not allowed to exceed 3%. The idea to reduce the social rift was therefore to be achieved through more centre-right policies of liberalisation. To this end, a new form of contract was established, the *Contrat Initiative Emploi* (CIE) (Contract to incentivize employment, own translation) and the *Contrat d'accès à l'emploi des jeunes* (CAE) (Contract to aid in youth employment, own translation) (Teyssier 2012). The purpose of these contracts was to provide incentives for companies to hire more people by taking on some of the costs of the newly employed (Pôle emploi, 15.03.2013).

The CIE and CAE contracts are good examples of the French centre right's efforts to tackle its problem of "*traitement social du chômage*" (Teyssier 2012, 513) (social treatment of unemployment). The solution of the Chirac government was to offer companies to pay for part of the costs of employing more workers, in order to give them a chance to get some experience and either get taken-on definitely by that company or get some experience so as to make it easier to find another job after this one ended.

Even though the state would have to spend funds on paying some of the social security contributions of the employer, this solution would reduce social expenditure, as it would get more people into work thereby raise the tax income of the state and reduce the state's RMI payments

The most radical reform that the Chirac government tried to pass was the Plan Juppé designed to reduce contributions to social security by employers and begin a pension reform. The Plan Juppé also wanted:

> *- Progressive institution of universal health insurance coverage, including the special regimes*
> *- Elongation of payment times from 37.5 to 40 annuities for public sector employees, as was the case since 1993 in the private sector*
> *- Freeze and taxation of family allowances including increasing the health contributions for people in retirement and people out of work*
> *- Increase of the amounts not covered by health insurance*
> *- And finally a constitutional amendment, requiring a Parliamentary annual law for the financing of social security, which determines the objectives and the progression of the expenses of social security. (own translation) (Assemblée Nationale 1995, accessed 15.04.2013)*

This attempt at reform would ultimately end in a watered-down version of the initial proposals due to massive strikes and popular dissent (Teyssier 2012). Although having parliamentary support, Juppé did not have popular support for the measures and strikes were organised by the FO, the CGFT and other organisations. They were the worst strikes since 1968 and caused great consternation within the government. Parliamentary support evaporated and the reforms had to be put through by legislative decrees (loi no95-1348, 1995) but in a more reduced form (Teyssier 2012).

The reforms implemented by the first Chirac government demonstrate that the goals of the government to care for its population have remained unchanged but the methods by which this is to be achieved have changed in accordance with the pressures of liberalisation which the EMU and the Maastricht treaties have created. As these reform proposals show, they were a reaction to a fiscal reality and an attempt by the French government to once again engage in demand-side economic policy making. The reforms proposed in the Juppé Plan are quite far-reaching in their consequences and effects, considering the French constitutional safeguards and the power of the unions.

This “crisis” created by the Juppé reforms contributed to an electoral reversal during the National Assembly elections in 1997 bringing the Socialists back into power in the National Assembly and beginning the second cohabitation of the fifth Republic, this time between Jacques Chirac and Lionel Jospin (Teyssier 2012).

The biggest undertaking achieved within that period of cohabitation, in terms of welfare, was the introduction of the 35-hour week initially proposed in the 101 points campaign document of Francois Mitterrand. The 35-hour week expands on the principle of managing unemployment by creating more employment. “L*’assainissment de l’economie au service de l’emploi”* (Teyssier 2012, 579) (the reconditioning of the economy to serve employment), the concept of reducing employment time was first introduced by Mitterrand during his first term when retirement age was reduced to 60 years and working time reduced to 39 hours.

This reduction of working time was designed with a number of employment incentives. If a company increased its workforce by 6% due to the reduction in working time, the company would receive a benefit. The state would take-on a part of the employer’s social security contributions the company ordinarily would have to pay. This amount would be increased if the company reduced working time further than the 35 hours weekly (15% reduction) and increased its staff by 10% from its current total. The same also holds if the company decided to lay-off people but reduced these layoffs by 6% for the standard reduction and 10% with a 15% reduction in working time for the extended reduction. The additional hiring or avoided redundancies have to stay in place for at least two years to benefit from these reductions. These payments by the state can be made for up to five years. A further increase in state grants will be given if the majority of people hired are young or have a disability. Specific grants are also given to companies whose workforce works close to or at minimum wage (SMIC) (Loi dite Aubry no 98-461 du 13 juin 1998).

Although the idea of working time reduction was introduced by Mitterrand, the argument provided by the Socialists in this instance was slightly different but with the same effective result. French Socialists at the time understood work to be something to be shared or distributed. Thus, redistributing work meant reducing unemployment and restarting the economy (Teyssier 2011, 713) (*l’assainissment de l’economie “au service de l’emploi”*

(Teyssier 2011, 579)). The idea of a social nature of work and a social nature of economic activity remains the same with Mitterrand and Chirac, as does their focus on internal consumption for the sake of international competitiveness and exports (Rifkin 1997).

The 2002 election of the National Assembly during the final term of Jacques Chirac saw the return of the centre right as well as a return of a more liberal reform course. As with the last attempts at reform, large protests were once again rolling up against these reform attempts. The resulting reforms did not significantly change the essence of the social security provisions. They were a step towards a more sustainable social security system but fall short of a full reform.

The Retirement reform (Loi n 2003-775, 2003) implemented in 2003 by the Chirac government reaffirms the commitment of the French state towards their retiring population and the principle of the generational transfer system upon which the pension system is based (Article 1) (Loi n2003-775, 2003). The state also engaged itself to guarantee a retirement wage of at least 85% of the SMIC (minimum wage) to all retirees.

The three points created in this law which are of note, were the creation of a "Commission de garantie des retraites" (Commission for a Guarantee to Pensions, own translation). It was tasked with administering the pension scheme in order to optimally utilize its available resources (Article 5) (Loi n2003-775, 2003). The Commission was also given the responsibility to advise the French government on the continued measures necessary to guarantee the sustainability of the system. This included advice on the annual revalorisations of the amounts of pension payments, since these had now been linked into the annual vote on the state's finance requirements, which have been established in the previous reform by Alain Juppé (Loi n2003-775, 2003).

The second important point to note is that the retirement age at 60 years was left untouched by these reforms (Teyssier 2011, 768). So, in order to take some of the pressure of the national retirement scheme, a third important point was established, i.e. a private pension scheme was created alongside the national one (Title 4). This private pension scheme included tax incentives aimed at making the scheme as attractive to as many people as possible.

This reform, managed to institute small changes to the retirement process in France in order to make the system more sustainable. It fell however short of the change that may have increased its sustainability for longer like it was in Germany where the retirement age was increased to 67 years (see Chapter 5). This reform is emblematic of the type of reform torpor that has beset France even if France has a united (no-cohabitation) government. This torpor helped the French *dirigiste* concept by reinforcing existing decision-making structures. This torpor has aided in the protection of the “traditional” French social model and helped limit the impacts of the global neo-liberal pressures. The French state has never changed its understanding of its role in the economy and of its role as a provider of care. The French concept of *dirigisme* has remained a powerful idea throughout all the Presidencies of the fifth Republic - especially during and after the Presidency of François Mitterrand.

Although the EMU and the European economic integration project have put pressures on the French state to open and reform its economy along the liberal concepts investigated throughout this thesis, the French government has withstood these pressures to a more or less greater extent. The government was able to stall these changes either through acquiescing to the neo-liberal demands in some way or by stalling or loosening the requirements (Howarth 2002). The 2007/2008 financial crisis has been the first serious challenge to that process. The analysis of Nicolas Sarkozy’s Presidency will illuminate how much of a challenge the crisis was and if that challenge changed anything in the concept of *dirigisme* and how the crisis defined France’s role in the prescription of austerity to other Euro Zone countries.

6.6 Sarkozy

The election of Nicolas Sarkozy would prove to be a big change for the French economy as well as for French society. Since Sarkozy and his centre right party achieved victory in the Presidential and in the National Assembly elections, President Sarkozy was able to use the full range powers available to his office, which he would use to implement a number of social reforms (Teyssier 2011). The Presidency of Nicolas Sarkozy was a controversial one for a number of reasons. The reasons that are of interest to this thesis relate to the social reforms, which he undertook during his Presidency. They are of particular interest since they are the most far-reaching reforms that have been enacted since the Mitterrand reforms 25 years prior.

6.6.1 Sarkozy and the TEPA law

The Law "en faveur du Travail, de l'Emploi et du Pouvoir d'Achat" (Loi n 2007-1223, 2007) (favouring work, employment and purchasing power, own translation), was a first attempt at reform and at a revitalizing of the French economy, which the French government worked on by implementing market liberalisation on their terms. The TEPA law reformed the regulation on working hours. It did so in such a way as to make overtime, tax and contribution free in order to make it more attractive for employers and employees to work longer hours (Article 1, Loi n 2007-1223, 2007). This law also helps businesses get around the 35-hour working week without creating too many more costs for the companies.

The law was voted on and passed shortly before the Commission for French Growth was created. However, much of the content of the law goes in the direction proposed by the report of the "commission pour la liberation de la croissance française" (Commission for French Growth, own translation).

The TEPA law also significantly reduced inheritance tax for all those who stand to inherit (Article 8, Loi n 2007-1223, 2007). It reduced the top tax bracket from 60% to 50% and simplified the system of tax deductions (Article 8, Loi n 2007-1223, 2007). Furthermore, the TEPA law reduced the tax burden on companies by reducing the tax on capital, especially for small and medium businesses (Article 16 Loi n 2007-1223, 2007). This law also introduced a trial period for the "revenue de solidarité active" (RSA) (income for active solidarity, own translation), which was designed as a more stringent and conditional version of the RMI, which was instituted in 1988. The reform of the RMI is another example of the attempt by the French government to liberalise its economy on its own terms, which is in essence, as was pointed out at the beginning of this chapter, a dirigiste effort at economic liberalisation.

The reforms of the TEPA law showed that the Sarkozy government was willing to move away from the traditionally held stance by the French government that it would care for its population along the lines of the "traitement social du chômage" (Teyssier 2011, 513). The tax reductions and the "provisional" establishment of the RSA are a signal that the French state was willing to retreat from its position within the economy and let the market take on more responsibility.

6.6.2 A Proposal for Reform (part 1)

The "commission pour la liberation de la croissance française" (Commission for French Growth, own translation) was a commission established by President Sarkozy in 2007 with the aim, as the name of the Commission suggests, to provide a template for economic growth to the government. It should be noted that these reform proposals were all made with the French constitutional limitations in mind. The resulting report put forward 316 points of reform necessary to revitalise the French economy. This more than tripled the number of reform points, by comparison to what Mitterrand proposed in his paper in the 1981 Presidential election. The number of reforms proposed as well as the way in which this report is worded transmits the necessity and urgency for reform. The report also stresses the necessity for compromise by emphasising the non-partisan nature of the report, going as far as to note it in the report's first sentence.

> This is neither a report nor a study but a manual for urgent and foundational reforms. It is neither partisan nor bipartisan: it is non-partisan (own translation) (Attali 2008, 5)

The non-partisan nature of the report is further underlined by the fact that this report urges the government irrespective of party in power to enact all 316 reforms and not just select whichever proposal is politically convenient for them. These reforms need a concerted effort by the government spanning at least two legislative periods (Attali 2008). This statement is an implicit suggestion to maintain the Sarkozy government for at least another term. The report explicitly links GDP growth to wellbeing of all types, making it a necessary condition for social justice, thus further reinforcing both the idea that neo-liberal economies can be used to complement and improve upon *dirigisme* and reinforcing the idea that neo-liberal economies can be controlled in the first place. This, however, runs counter to the whole idea of neo-liberal economics.

> Becoming wealthy is not a scandal but being poor is (own translation) (Attali 2008, 6)

The link between increasing GDP and increasing social justice is, in principle, compatible with the traditional views of the responsibilities of the French state. The difference is, as will be pointed out in this chapter, that this report doesn't necessarily see the state as the guarantor of the GDP and social justice increase. This notion goes some way towards the same type of reconceptualization of the role of the state that was undertaken by Germany with the exception that this report has not been opened up to as much market influence as the Hartz report in Germany had. The French government had maintained its influence within the creation of this report.

The report does point out the fact that there had not been a thorough economic and social reform in over 20 years, causing the dialogue to atrophy and long held positions between the social partners (state, unions and industry) to harden instead of improving and revitalising networking and cooperation (Attali 2008, 6). The report also pointed to the large French budget deficits and the necessity to bring those under control since the money (taxes) spent servicing French debt could be put to better use financing social programmes. The report points out that reining-in the public debt should be a paramount concern of the state. The level of growth of the debt at the time would mean that the debt would grow to become 130% of GDP by 2020, putting undue burdens on future generations and causing a greater polarisation of the middle classes (Attali 2008, 10). This is a direct reference to the continued troubles of the French state to stay within the debt limits set by the European stability mechanism, which France had continuously exceeded for the 4 preceding years (Table 7.19, 7.20, 8.9). It is also a tacit acquiescence to the power of the market and the necessity for the French economy to submit to its requirements in order to secure investment and future growth.

> Strong economic growth is available to all in France. … It requires tolerance, an appetite for risk and success, the respect of failure, a loyalty to the nation and to future generations, self-confidence and confidence in others (Attali 2008, 10).
>
> More economic growth will bring with it concrete advantages for every Frenchman, which it will be the prerogative of each political majority to distribute according to their own ideas (own translation) (Attali 2008, 10)

This paragraph frames the issue of reform and economic growth using principles from both right and left French political parties. The first quotation wants to reduce the influence of the state by fostering an appetite for risk. That quotation at the same time wants the state to remain a significant staple of the economy by wanting to respect failure. The writers frame their report as the only option for the future of sustainable economic growth and social equality in France, the rewards of which will be distributed according to the wishes of the party in power.

> The main action that needs to be taken however lies with the French themselves who will have to want change and share a desire for the future, to learn more, to adapt to work more and better, to create, to share and dare. (own translation; Atalli 2008, 11).

The report in the first pages essentially concludes that stalling tactics are no longer working and that the French state needs to meaningfully engage with the global neo-liberal economic framework. This paragraph addresses itself to the many demonstrations that have sprung up over the last years against welfare and labour reform attempts. The report puts the responsibility and the blame of failure on the shoulders of the population; the French themselves need to start taking responsibility for their fate in the economy. This is a major step away from the concept of *dirigisme*. The report seeks to empower the individual to go out into the labour market and compete with others for work instead of waiting for the state to intervene on their behalf.

> Our project has one obsession: that all benefit, especially those who are being excluded today. (own translation) (Atalli 2008, 12)

The Report tries to provide a sensible solution to the French economic problem by providing concrete reform proposals and framing them in a way that leaves no alternative to it. It also calls all parties including the French population and other social actors (unions and employers) to action, to engage in constructive discussions designed to benefit the largest possible section of the population.

The substance of the Report addresses a panoply of different issues, starting with education. The Report argues for a thorough reform of the entire school system. It starts by arguing for more skills to be taught in primary education, to better prepare children for higher education or the labour market.

A closer orientation to the requirements of the labour market is also recommended by the Report.

It further argues for more funds and authority to be given to universities to be able to provide better higher education. It would also attract more research and talent to France for which, well-funded and highly quoted universities are a prerequisite (Attali 2008); this includes also attracting more foreign students to French universities by e.g. expanding the Erasmus programme (Attali 2008, 171).

These education reforms are designed to reduce inefficiencies in education while avoiding layoffs where possible and simultaneously introducing elements of competition and market forces into the system. The report focuses the priorities of education to cater more to the requirements of the labour market and the economy by changing the curriculum to better suit the needs of the economy and by trying to attract research and development into France (Attali 2008). The first reform is quite dirigiste because the state sets the scholarly curriculum. Setting it to suit the needs of the industries in France requires a close relationship between state and industry. The attraction of research and development to France is less of a dirigiste effort since that is mostly left to the market and the universities.

The Report also advocated reforms to SME (small to medium enterprise) regulation and support structures. These reforms propose a simplification of start-up rules and accounting practices for SMEs in order to make it easier for people to start small businesses as well as make it easier for such companies to get advice and business guidance. The reforms would also make it easier for SMEs to get funding and be active on the stock market (Attali 2008, 50).

Although not an example of *dirigisme* this reform proposal is an example of the efforts of the report to make the French economy more flexible and vibrant, not by reducing the size or the actions of the state but by making those actions more efficient and faster. Another such example in this report is its promotion of a greater use of the Internet to achieve greater economies of scale and greater gains in efficiency. The report considers the development of high-speed internet and the creative industries that it spawns to be a motor for future growth and efficiency, also through a closer integration of the internet with France’s European partners (Attali 2008).

The business related reform proposals this report provides are aimed primarily at reducing unemployment by making France a generally more attractive place for businesses and people to come and settle in or to visit. One of the ways to attract new business to France is by labour market and labour union reforms (Attali 2003, 105). This means that the rights and responsibilities of unions and Workers Councils need to be reformed and adapted to the new realities of Globalisation (see section on unions above for details about the reform). This labour market reform included calls for continued efforts at encouraging youth employment and most significantly an increase of the retirement age. At the same time the report inspires companies to make redundancies the very last resort (Attali 2008).

This is a significant proposal in the sense that this proposal considers a redefinition of the roles of the social partners in labour negotiations towards a more market oriented principle, thereby reducing the importance of the state and the importance of the unions. However, the Report stresses that these liberalisations of the labour market and the economy should not prevent the state from caring for the unemployed and the most vulnerable among the population. The state should continue to provide them support and foster cohesion among the different social, economic and ethnic groups and enable them to become productive members of society (Attali 2008).

The reforms proposed in this report would move the French economy further towards a neo-liberal economic system, as defined in Chapter 2, than any other reforms proposed by previous French governments. Another good example of this move is seen in the paragraph below. What also comes out of this report is that with the reform proposals analysed above, once a liberal reform is proposed the report also tries to compensate any negative repercussions of that proposal with state action. The result is that the French state no longer has such a large directing role in the French economy, and that its role is directed more towards fixing any issues that a market oriented French economy might encounter thus in a way, making the French subject to the market, as is desired by neo-liberal theory.

Another recommendation of the report was to make financial regulation and taxation more attractive, enabling French businesses to compete internationally as well as enticing foreign financial business to settle in Paris. Along that same principle companies, although relieved of a great chunk of the burden of regulation, should nevertheless be made to comply with the rules that are in effect, to insure a smooth running of the economy (Attali 2008, 95-96).

The final section of recommendations by the Commission focuses on the French budget deficit, which has remained at high levels for at least 30 years and whose growth had to be curbed, not only to continue to attract business to France but also to comply with Maastricht and EMU rules and bring them into line with market operations (Crouch 2011). These budget reforms were supposed to allow the state apparatus to be slimmed down and made more efficient without compromising the state's ability and duty of care.

These budget reductions would reduce the cost of health and social benefits by reforming the French social security system, focussing on the expansion of preventive care and standard care facilities as well as a greater focus on disease research (Attali 2008). The report also recommended increasing efficiency and reducing overheads by outsourcing specific tasks to outside contractors awarding the contracts to those that upheld the highest standards. Further reductions could be achieved by consolidating administrative services especially for social housing and development (Attali 2008).

This last example of the report's proposals is another good example of the neo-liberal direction this report is taking as it argues for cost saving measures and outsourcing to be implemented. It also shows again the report's desire to keep the state as part of the economic process to ensure that the constitutional provisions of France are respected, while at the same time slimming the sate apparatus down.

The report's recommendations were limited just as the previous reforms; legally by the French Constitution and philosophically by French state traditions. As was determined in the first section of this chapter, the French constitution has very specific guidelines and rules on how many social provisions and how much national care can be reduced by, before they breach constitutional provisions. However, this report went a long way towards identifying inefficiencies and possibilities for improvement and complementing those possibilities with reformed social, welfare and labour provisions that lay within the borders set by the constitution but still moved it further towards a more liberalised economy. It endeavoured to make the French economy more productive while maintaining as much as possible the labour standards and the current French system of state care and support. Throughout this report it becomes plain that this report was written within a strong dirigiste influenced frame of thought, trying to introduce reforms at a high pace, but also making sure that those reforms do not entirely apply market demands but also revalorise the state as an active member of the economic process. These reform proposals try to achieve the same effect on the French economy than the Mitterrand decision had on the economy in 1982. The proposals here would shift the balance of power further towards the market and subjugate the authority of the French state further to that of the European institutions, international companies and the concept of neo-liberalism generally, while still trying to keep the authority of the French state intact on a national scale.

6.6.3 Sarkozy and the 2008 reforms

The publishing of the Commission Report in January 2008 did have some impact on French politics. In the second year of Nicolas Sarkozy's presidency, a number of economic reforms were enacted into law.

The law "portant renovation de le démocracie sociale et réforme du temps de travail (1)" (loi n 2008-789, 2008, law relating to the renovation of social democracy and reform of the working time) reformed the statutes of the French Labour unions (see section 7.3.2). It set new and more favourable conditions for the government to pass and enact social and workplace reforms (Article 8, loi n 2008-789, 2008) as well as setting new transparency and audit rules for the unions to abide by (Article 10, loi n 2008-789). For France, this constituted a significant change of its internal balance of power. It saw the unions lose some of theirs and government gain some which would allow it to cede some of that power in turn onto the market and to industries operating within the French territory.

It also introduced further liberalisations to the working time as an extension to the ones already instituted in the TEPA law (loi n 2007-1223, 2007). A further reform changed the RMI into the RSA (loi n 2008-1249, 2008) (revenue de solidarité active). This reform was designed to make the RMI more jobs oriented. It did so by strengthening the requirements to find employment. It linked the receipt of the RSA with a job support package aimed at helping people get back into work. It also tightened the availability of these benefits to a more select group of people in France most notably the French themselves leaving out non-Europeans or its former colonial possessions. It also implemented higher wealth- and benefit- caps onto the calculation of the RSA to reduce state expenditure on it. The RSA was designed in particular to complement incomes of low-income households or single parents without leaving those without employment aside (loi n2008-1249, 2008). The implementation of the RSA is a good example of a law applying the recommendations of the Commission report. The RSA was designed to act as incentive for people to work yet still provide security for people who have not yet found any work. The RSA is a good example of the move by the French government to start down the path of workforce liberalisation, which is one part of the economic liberalisation. The RMI reform creating the RSA could be considered as a copy of the Hartz reform in Germany that also tried to incentivise people to go and look for work.

The last reform package, which the Sarkozy government implemented before the 2007/2008 financial crisis started impacting the French economy, was the “loi de modernisation de l’économie (1)” (loi n 2008-776, 2008, economic modernisation law (own translation)). The application of this law was the biggest attempt by the government to apply the propositions of the Commission for Growth.

This law was designed to liberalise the French economy by promoting personal enterprise and the financial sector. In the first section entitled: “Mobiliser les Entreprenneurs” (Title 1, loi n 2008-776, 2008) this law aims to promote entrepreneurial spirit by simplifying the rules and regulations surrounding independent individual contractors (Chapter 1, loi n 2008-776, 2008). It supports the creation of SMEs (Title 1, Chapter 2, loi n 2008-776, 2008), through the modernisation of the commercial housing law (Baux Commerciaux) (Title 1, Chapter 3, loi n 2008-776, 2008) and the simplification of the running of SME’s (Title 1, Chapter 4, loi n 2008-776, 2008).

This law aims at reducing state influence by simplifying and accelerating procedures as well as reducing barriers to entry so that more people can quickly set up new firms. It could be argued that it is also a reduction of dirigiste policies since the state is no longer as involved in the creation of SME’s as before.

The second section entitled: “Mobiliser la Concurrence comme nouveau Levier de Croissance” (mobilise the competition as a new motor of growth, own translation) (Title 2, loi n 2008-776, 2008), takes up the challenge of increasing and developing the competitiveness of French industries. It does so in a first instance by strengthening consumer protection (Title 2 Chapter 1, loi n 2008-776, 2008) and reforming sales practices (Title 2, Chapter 2, loi n 2008-776, 2008). This law furthermore created a competition authority (Title 2, Chapter 3, loi n 2008-776, 2008) charged with ensuring fair competition on a national, European and international scale. To do so, this law also allows the state to take action via “ordonnances” to strengthen competition rules and regulations as well as the competition authority in their ability to enforce competition and prosecute anti-competitive behaviour (Title 2, Chapter 3, Article 97, loi n 2008-776, 2008). This part of the law, however, is actually reinforcing the dirigiste aspects of the French state by creating new services, which are supposed to monitor and manage economic activity so as to make it more competitive as well as strengthening the competition framework.

The third section entitled “Mobiliser l’attractivité au service de la croissance” (Titre 3, loi n 2008-776, 2008, mobilise the attractiveness of France in service of growth (own translation)). This law aims to achieve this through the widespread availability of high-speed Internet (Title 3, Chapter 1, loi n 2008-776, 2008). The reform of company tax as well other rules and regulations of FDI and company regulation in order to make it more attractive for companies to move to France (Title 3, Chapter 2, loi n 2008-776, 2008). The reform to the rules and regulations of the FDI specifically include the desire to attract private funds to France designed for research and development (Title 3, Chapter 4, loi n 2008-776, 2008). These reforms further include reforms to the French intellectual property law (Title 3, Chapter 3, loi n 2008-776, 2008). The final reform this law promulgates is the reform of the French financial sector. Article 152 (loi n 2008-776, 2008) allows the government:

> To, by way of ‘ordonnances’ in the conditions defined by article 38 of the Constitution, take decisions in the legal domain necessary to the modernisation of the legal framework of the financial market place (own translation) (Title 4, Chapter 4, Article 152, loi n 2008-776, 2008).

The reforms investigated above form only a small part of the total number of the recommended reforms that were passed by the Sarkozy government. These reforms have allowed the French economy to become more liberal, but the French legal code continues to retain in many instances (see Article 152 above also Chapter 1-3 in Title 2) a quite dirigiste character. The laws enacted liberalise the economy on one side and increase state involvement on the other side. The French state seems to be uncomfortable with a consistent line of liberal market reform. As these points showed, the unions, even weakened, continue to wield a lot of influence within the industry, the state and the economy. The liberalisation and simplification of SME rules and regulations is another significant effort at making the economy more open and more responsive, while also slowly diluting the French dirigiste tradition only to increase the control and the regulation of competition. It should also be noted that neither the report nor the laws that followed have taken on any significant measures except for the transformation of the RMI into the RSA to change the welfare provisions of the French population and the proposed outsourcing of some healthcare jobs to the private sector in the report.

This gives further credence to the notion that the French government is not comfortable with a reduction of the role of the state within the economy. The French government, as was shown above, continues to struggle with the neo-liberal concepts, which it has decided to espouse when it signed the Maastricht Treaty and committed to the EMU. The history of the French government with the EMU and the closer socio-political-economic integration of Europe has been one of continuous struggle against the neo-liberal concepts of market freedom.

6.6.4 Reactions to the Financial Crisis

The Financial Crisis came to the full attention of the Sarkozy Presidency towards the end of 2008. Right after the crisis hit, the government took a distinctly Keynesian approach to the economic downturn. In 2008, the President decided to use Keynesian solutions by promoting investment instead of austerity, pledging 26 billion Euros over two years to fight the negative effects of the crisis (Scigacz 2008). A third report was created by Alain Juppé and Michel Rocard entitled “Investir pour l’Avenir” (invest in the future, own translation) (Juppé, Rocard 2009, 1) which spelled out the best way to spend that money so as to make sure that the French economy can be grown over the medium and long term in a sustainable way. This report will be analysed more closely in the following chapter.

Additionally the government also put into place measures to support consumption, such as credits for people buying a new car to replace their old one. It also embarked on a number of construction and renovation projects mostly for social housing (Scigacz 2008). These actions fall squarely within the

French dirigiste tradition, as well as within the state's traditional definition of the responsibility for care, which is still very much alive even with the recommendations of the Commission Report. Although it should be noted that the Commission Report did not set out to destroy the old French concepts of the state's rights and responsibilities, the report was designed to adapt this setup as far as possible to the new global and European landscape. In addition to the stimulus plans, the Sarkozy government also commissioned another report by the Commission for Growth to develop a long-term plan for France to deal with this crisis.

6.6.5 A proposal for reform (part 2)

The financial crisis did not impact France as heavily as it did Portugal, Greece, Spain, Ireland and Italy. France was also able to weather the 2007/2008 crisis better due to its high levels of internal consumption as well as a more diversified economy than other countries in the EU (Attali 2010, 40). Right after the crisis hit, the Sarkozy government commissioned a second report, regardless of how much the French economy was affected by the crisis, in order to formulate a plan of action for once the crisis was over.

"Une ambition pour dix ans" (a strategy for the coming decade, own translation) was the second plan to be developed by the Commission for Growth. The report does show the experiences gained from the first report written by the commission. This second report acknowledges the progress made in France due to their initial report, of which the majority of their proposals have been instituted in some form or another into French law (Attali 2010)

However, the new report has lost nothing of the urgency of the first report and goes further in its neo-liberal recommendations for reform than the first report did. The principles upon which this report is based are the same as those of the first report. It aims at being non-partisan in its recommendations. However, in this report the Commission acknowledges that differing political majorities may give different priorities to their recommendations (Attali 2010). This could be seen as a distancing on the part of the commission from the Sarkozy Presidency, which the previous report seemed to approve of, at least implicitly.

This second report is in essence a reiteration of the first report with updated recommendations to take account of the reforms already instituted and with adapted recommendations to the context of a financial crisis. This adaptation, however, means that austerity principles are also being introduced to some extent within this report. The report itself acknowledges this (Attali 2010, 8). This report therefore focuses on reforms it considers "urgent" in the short- and long run.

> We propose a ten-year strategy based on:
> 1 Two immediate imperatives: debt reduction, to prevent the tragedy of a loss of sovereignty, and jobs, to end the scandal of mass unemployment, notably among the young;
> 2 Two long-term priorities: education and the management of the major growth sectors, including the environment, natural resources and major infrastructure. (Attali 2010, 242)

The two immediate imperatives, particularly debt reduction, are designed, if phrased indirectly, to avoid France falling under the EFSF or ESM protective umbrella and thereby forfeiting of its budgetary sovereignty. The second imperative is a reaction to the increased unemployment rates (see Chapter 8 for details) created by the recession. Furthermore, it is yet another acknowledgement of the power of the neo-liberal concept, and of the changed relationship between the state, industry and the market. The market is now seen even by the report to set the terms, which the state needs to engage, if it wishes to entertain a successful economy.

The two long-term priorities focus on larger issues such as education, environment, natural resources and major infrastructure. This again sounds like and indirect hint towards a Keynesian state-managed growth push once the crisis has been weathered.

The report points again to the significant economic, social and political deficits with which France has to deal. Irrespective of the reforms already undertaken, the French economy continues to be unable to compete with other major economies on the European (i.e. Germany) and global level (i.e. USA) with high unemployment as a result of this low competitiveness. The Commission identifies as a major reason for this lack of competitiveness, a *lack of effective governance* leaving much of the potential of the French nation and its people untapped (Attali 2010, 240).

> Our Commission seeks to speak in the name of future generations and defend their interests (Attali 2010, 241)

In order for the French economy to recover its competitiveness, it needs to start embracing risk once again. The high risk-aversion of the French is at the core of the stagnant economy and the difficulties resulting from it (Attali 2010, 34). This high risk-aversion is also, according to the report, caused by the high labour costs in France. Those high costs stem from the high costs of insurance that the employers must pay on behalf of their employees, which are disproportionately higher than those, which are paid by the employee. This discrepancy is especially striking in the lower income segment (Attali 2010, 39). Due to these high costs for the employers, taking on a new hire would mean high costs if that new hire did not meet the needs of the company, this is a risk that many companies want to avoid.

This problem of risk and high labour costs is a neo-liberal reform point. Considering how the issue is framed, i.e. as problem of cost and risk aversion, the solution to that would lower costs and lower risk aversion, which can both be achieved through a liberalisation of the employment market and a liberalisation of hiring and firing practices. This could be considered as the second report advocating German Hartz-style reforms.

The social dialogue (among state, unions and employers), which negotiates the level and distribution of these payments, has also suffered as a consequence of this risk aversion. With the continuous erosion of union power, the unions want to maintain what power remains to them. The resulting almost obstinate and unchanging negotiating position that has set in between the unions, the state and the employers, has remained unchanged for over 30 years (Mouriaux 2013). It is one of the greatest obstacles on the path to reanimate the French economy (Attali 2010, Jeanneau 2013).

This argument is an expansion of the argument before about the high labour costs. The report argues that all sides, especially the unions need to be willing to compromise on their demands for the good of the French economy.

This report requires the state to make considerable cutbacks but always with an eye towards limiting the harm done to the weaker parts of society (Attali 2010). This reduction in spending is achieved through efficiency gains and a reduction of administration instead of reductions of services as well as giving a greater role to private insurance providers (Attali 2010, 245). These spending cuts include a number of extraordinary measures over a three year period, which includes a pay freeze for state employees, natural redundancy measures, as well as a freeze on an increase in state social contributions (Attali 2010, 79-80).

This again is a neo-liberal point put forward by the Commission, trying to decrease expenditure through pay freezes and efficiency gains. This point shows the limits of what reforms in France can achieve without a constitutional amendment, since the report once makes a point about deficit reduction and pay freezes goes straight into saying that that needs to be measured so as to disadvantage the poor as little as possible.

The report requires the government to increase its tax revenues especially through the closure of tax loopholes and tax exemptions (Attali 2010, 82-83), which includes the abolition of tax shields and increases in the inheritance tax (Attali 2010, 244), parallel with the cutbacks of the state budget, in order to bring the budget deficit back under control.

The most controversial of the proposals in the report was the *social protection reform* (Attali 2010, 89-91). This proposal is the closest this report gets to emulate the spirit of the German Hartz reforms. This statement comes very close, though cannot be equated, to the notion of “Fördern und Fordern” (Deutscher Bundestag, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt, 2003, Article 1, Kapitel 1) to the German conception of social provisions.

> it responds to a logic of rights to provisions rather than to a logic of rights to be accompanied and duties of insertion into society (own translation) (Attali 2010, 90)

In the short-run, the government should also consider a push for increased possibilities for job creation. It further argues for continued training between employments as well as during employment (Attali 2010, 246-247).

In the long-term, the report looks at improving the education system to reduce the number of school dropouts as well as increase the skills taught at school. It is supposed to become a fully integrated system where children and young adults are accompanied all along their educational journey. The long-term view of the report also looks at environmental preservation, specifically through the investment in ecological innovation and competitiveness (Attali 2010, 249).

Aside from these necessary reforms this report also wants to give back to the French a taste for risk and innovation (Attali 2010, 250), which the “overbearing” and generous social security, work and economic protection have substantially atrophied. The report as the title suggests, takes an overall long-term stance on these reforms while addressing the most pressing problems at the time as well.

This is a reiteration of the original short-term goals at the beginning of the second report. This part fleshes out further the problems with the current state of affairs and continues to argue for a more neo-liberal approach to things by reducing the “overbearing” and generous social security so as to be willing to take on more risk.

This report again had a great impact on the actions of the Sarkozy government as it closely follows its prescriptions. By 2011, VAT is increased and tax loopholes are closed, and the fiscal shield is abandoned. Even an extraordinary tax on high incomes is proposed, but the taxes on savings are reduced (Scigacz 2008). Furthermore, the Report suggested a greater integration within Europe to tackle the crisis on a European level, which would in turn help France as well as the other EU members (Attali 2010).

The report contained a specific proposal to seek among all the European countries a close alignment with Germany and its attempts at dealing with the crisis. This suggestion is unsurprising since the second report took a more neo-liberal direction than the first report, a direction, which seemed to be inspired to some degree by the German Hartz reforms.

As a result of these suggestions, there was a marked *rapprochement* of the French President and German Chancellor on matters of austerity throughout 2011 and 2012 until Nicolas Sarkozy lost the Presidential election to François Hollande (Reland 2011).

6.7 Hollande

While the argument that Sarkozy lost the election to Hollande because of Sarkozy’s reform course towards austerity and Hollande’s strong opposition to austerity would be an overstatement as there were many other contributing factors. This is not to understate that Hollande’s election promise to renegotiate the ESM treaty and the austerity prescriptions (Fouquet and Deen 2012) in particular didn’t have an impact upon that election.

Had Sarkozy been re-elected for a second term, a continued common front might have been established between Germany and France in their advocacy of austerity. This would also have continued the French government's move to implement further austerity measures and engaged in further efforts at market liberalisation.

Hollande was elected on a social democratic message, more in tune with the French state traditions. This message was in opposition to the neo-liberal concepts espoused by his opponent and which have been implemented within France as pointed out above. However, Hollande's economic campaign promises were left in large part unfulfilled, as he was confronted with a stagnating economy and a continued loss of competitiveness and increasing unemployment especially among the young (see Chapter 7). This and party internal as well as personal problems have made him a rather weak French President, although he still aims at defining France as the alternative to Germany in terms of dealing with the crisis and the economic recession in Europe.

The distinguishing feature of French politics is that, even if there is appetite for reform, and the political will exists to follow through on those reforms, the reform effort is not brought to conclusion due to popular or parliamentary opposition. As was the case during the Sarkozy Presidency these efforts were always tempered either by the French constitutional provisions or by the French population. However, all parties are to blame for the stalled "social dialogue" throughout the time period here analysed. This "ossification" of positions among the social partners was one of the central problems that were being addressed in both Commission reports commissioned by the Sarkozy government. Finding the right balance between the rights of employers and the rights of employees and between state action and market forces has not been easy, though the Commission for Growth has made the most wide-ranging and concerted effort to do so. The financial crisis has only deepened the resolve of the Commission for reform.

6.8 Conclusion

France has a tradition of strong state presence and leadership and a catholic sense of care for others. It was especially since its third Republic that France been a very caring and worker friendly state, mostly due to the continued influence the French Communist Party exercised in the third and particularly in he fourth Republic. The influence of the PCF only started to wither in the late 50s. The reforms of the Mitterrand regime that were supposed to further empower unions in the 1980s have only hastened their decline, leaving a weakened left in its wake. However, their principles have lived on in the French constitution and its amending parts as well as within French law and French social conscience.

French politics and French policy has long followed a quite dogmatic route. Different governments have instituted some policies and repealed others because of party political dogma. However, all governments have adhered to a dirigiste tradition of political-economic action regarding external and internal political economic influences. These policy institutions had different effects on different parts of the system, though usually they favoured workers' rights over employers' rights.

The French dirigiste tradition has been continuously challenged by the neo-liberal economic concept, considering that it is opposed to the free market concept, which is at the centre of its economic concept. Since the 1970s neo-liberalism has continuingly gathered in strength. The French dirigiste concept has over time changed its modus operandi, from indiscriminately propping up French industry in the beginning to more selectively directing economic forces within France and protecting only important French industries. This evolution has come about as a reaction to the increasing power of neo-liberalism and its influence upon the policy making within the EU, which established the EMU and the Maastricht treaty. However, over time, the social dialogue, which has made the dirigiste model an effective tool for the French government, has stalled between social partners and continues to be a chronic problem within France.

On the one hand it was able to slow the increasing pressures of neo-liberalism for reform but on the other hand, it also suspended to some extent the active engagement of the dirigiste concept with the changing realities of the international political economy.

Therefore, it has been one of the aims of the Commission for Growth to reduce this ossification not only in the short but also in the long term. The report proposes to achieve this using a variety of liberal as well as Keynesian methods as well as proposing reforms to the social dialogue between unions, the state and the employers. While the more conservative governments have tried to liberalise the French economy, an attempt, which, during the 1990s, has largely only succeeded in privatising former government owned industries such as energy, and finance as any attempt at changing social provisions has met with strong popular and union opposition. In the later part of the 2000s these industry liberalisations have taken on more steam, as have some social reforms.

The election of Nicolas Sarkozy brought with it the biggest change to social security, employment and unemployment legislation since the election of François Mitterrand in 1981. Sarkozy created the Commission for Reform whose initial report consisted of 316 recommendations for reforms designed to make the French economy more competitive in the long run. These reform proposals acknowledge the power of the neo-liberal concept and try to adapt to the dirigiste economy further towards neo-liberal logics, without changing significantly the state's understanding of care for its citizens but allowing it to continue to adapt to the pressures of the neo-liberal system.

Once the 2007/2008 financial crisis also started to impact the French economy, President Sarkozy tasked the Commission to work out a second report designed to deal with the fallout of the crisis and chart a way back to sustainable economic growth. This second report once more embraced neo-liberal concepts by proposing on the one hand further cuts to state expenditures and a balance to the French budget, which was one of its central aims. The points enumerated within the report once again influenced the economic politics of Sarkozy and explains his repeal of his tax reforms. However, Sarkozy initially followed an expenditure-led strategy to resolve the crisis based on the report by former Prime Ministers Juppé and Rocard (2008) whose report will be analysed more closely in the following chapter. With the benefits of this strategy slow to materialize, and the economic situation deteriorating, the President decided to follow the advice of the Commission report and began working towards a European response to the crisis.

This led to close alignment with Germany. This had, as a consequence, the reversal of the President's original spending policy with regards to the crisis and a turn towards a more austerity led way also undertaken by Germany. As will be demonstrated in the following chapter, France remains an example of a different solution to the austerity and liberal reforms of Germany. Particularly since the election of François Hollande as President of France the French government support for austerity has all but evaporated. One reason is the continued inability of the French government to conform to the EMU rules of GDP to debt ratio or the level of new debts a country can contract per year (LeMaître, Ducourtieux 2014). For this and other reasons, the French government is intensively lobbying the German government to relax its austerity stance and consider embarking upon an investment approach in response to the crisis in concert with a more relaxed approach to austerity (see Chapter 8)

Chapter 7 The socio-economic development of France: a quantitative analysis

7.1 Introduction

France is Europe's second largest economy and no natural advocate of austerity. France's view of the austerity conditions is commensurate to France's own understanding of the role of the state within the economy as well as the French dirigiste concept. This concept has evolved with the changed and changing nature of the international political economy, however, with the ossified dialogue between the social partners, the evolution of the concept is becoming less certain.

Considering that the French government has decided to support the European political and economic integration project with the signing of the Maastricht treaty and the implementation of the EMU it has accepted that some of its practices (particularly its dirigiste and social welfare traditions) must evolve to be able to respond to the pressures of neo-liberalism. As will be demonstrated using French economic and social data, the French economy has been unable to cope with the new economic realities of the European neo-liberal agenda and its budgetary policies.

Although France continues to play a central role within the European project, its importance in terms of the Euro Zone management and rule setting is now being overshadowed by Germany. In order to understand the circumstances, which caused this French decline, this chapter evaluates the French economic performance beginning with the Presidency of François Mitterrand and concludes with the Presidency of Nicolas Sarkozy as well as casting a general look at the French economic performance after the first two years of the Hollande presidency. This chapter considers the economic developments including unemployment, economic performance and income performance, as well as social indicators and poverty levels and income differences as well as benefit recipients.

It was during Nicolas Sarkozy's Presidency that the financial crisis hit France, which required further action by the French government. Therefore, the French government initially decided to shore up the economy through targeted spending and a revitalised form of French *dirigisme* and by maintaining a high level of domestic demand through continued high levels of social spending, thereby providing an opposite and alternate solution to the German austerity method to solve the troubles of the EZ crisis. The penultimate section will consider the merits of the spending approach, which the French government under Sarkozy initially embarked on. However, these actions were followed the following year, by the reversal of many of those policies after the French government decided to align itself with the German crisis response policy to shore up the stability of the Euro Zone.

An embrace of German style austerity politics also followed this alignment. For the last legislative period, the Sarkozy government embarked on a deficit reduction project presented by the then French Prime Minister François Fillon. This project was designed to get the French deficit under control and comply with the EU deficit regulations established under the Maastricht treaty and defined within EMU rules. The first years of the Hollande presidency heralded an attempt to return the social democratic principles by reducing the deficit through tax increases. However, as this chapter will show, economic growth remained stubbornly low and unemployment and budget deficits kept on rising.

This chapter first provides an overview of the economic development of France. This chapter uses economic data from 1950-2011 and from 2001-2014, to determine trends within employment, social security, as well as French economic performance. *This data will allow this thesis to consider, if the trends in France were helped or hindered by the slow pace of reforms.*

This thesis understands that reforms require time to translate fully into the economy as well as into datasets, which makes current economic data speculative as well as the results drawn there from. Situating this evolution in a historical context, this first section of this chapter, deals in very general terms with France's economic development after WW2 until the 1980s, a period called the "Glorious Thirty", which ended at the beginning of Mitterrand's presidency.

Understanding the period of the "Glorious 30" is important, as it confirmed the state as an agent of care and economic governance in the minds of the French for generations to come and made the French case for their use of *dirigisme*. The next section of this chapter then analyses how the French economy was impacted by the global economic downturn of the 1980s and 1990s, and the actions by the various Mitterrand-led governments during that time, which further reinforced the public understanding of the state as an institution of care but also demonstrated its limitations, especially in the face of the establishment of the EMU and the Maastricht Treaty. This is also an important time to investigate, as it set the tone for decades of economic management. French policy-makers, after realising their inability to affect global economic forces, developed the idea of “traitement social du chômage” (social treatment of unemployment) (Teyssier 2012, 513). This analysis will also include an investigation of the French economy during the Presidency of Jacques Chirac, which also included an economic downturn.

The final section of this chapter investigates the reforms of President Sarkozy, whose Presidency coincided with the start of the 2007/2008 financial crisis as well as briefly considering the first years of the Presidency of François Hollande. The Sarkozy Presidency contained a number of reforms and policy reversals. It tried to actively engage with the crisis through investment by following the plan Juppé-Rocard (2009), however, in the end bowed to the German principle of austerity, whereas President Hollande has campaigned on a promise to renegotiate the austerity prescriptions. The French government is still trying to reform its economy and make it more competitive as well as in agreement with the stability criteria and at the same time tries to get more time to achieve these reforms as well as get the reforms more relaxed in general.

This section considers these points in turn. Because of this crisis, Europe and France are now faced with a stagnant, recessionary economy (INSEE 15.05.2013), as well as an increasing sovereign debt level and low (or lower) projected growth figures for the EU as a whole (Heitmeyer 2012). Therefore, the final section looks at the effects the financial crisis had on the French budget as well as the effects on France’s ability provide a counter concept to that of German austerity.

As this analysis will use datasets to evaluate the performance of the French economy throughout a period of time that has seen a number of social reforms as well as economic boom and bust cycles, data for this period of time is still relatively recent and subject to change as this analysis progresses.

Due to the complexity of the question set in this thesis, a large number of factors need to be considered in the analysis. Therefore, this thesis has decided to use a number of different data sets provided by different international institutions. These institutions include the World Bank, the IMF, the WHO, EROSTAT and the OECD. It also includes the French national statistics office

INSEE. Using this many different data sources may lead to some of the data not being 100% verifiable with other data sources used. However, these are all well regarded international institutions, which use these same statistics in their own models, and therefore this thesis is confident that the data provided by them is accurate.

7.2 France during the "Glorious 30"

After the end of WW2, Europe entered a period of rapid growth aided by the Marshall Plan and the reconstruction efforts required in Europe. This period of growth also included increased public consumption, which evolved during the 1950s, 1960s and 1970s to a level rivalling the American consumption.

Table 7.1 GDP growth and work Productivity
En % par an

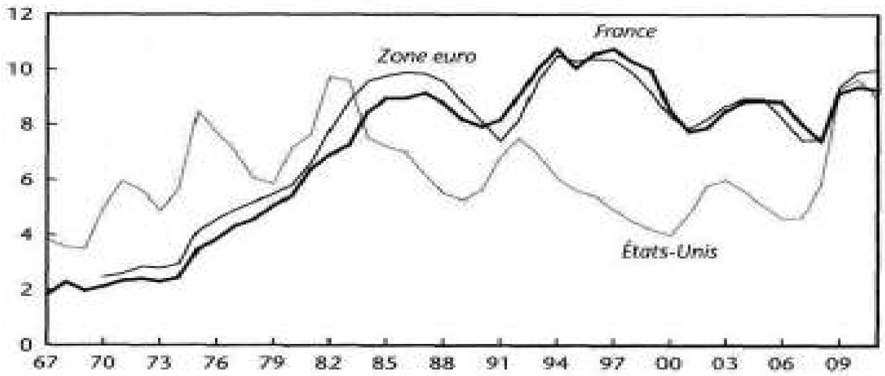
	1950-1973	1973-1979	1979-1990	1990-1997	1997-2000
PIB					
France	5,0	2,8	2,5	1,3	3,6
EU 15	4,8	2,4	2,3	1,7	3,1
United States	3,6	2,6	3,0	2,9	3,1
Productivity per capita					
France	5,0	2,6	2,1	1,3	1,4
EU 15	4,5	2,7	1,9	0,9	1,1
United States	2,5	0,7	1,1	1,4	2,9

Sources: OCDE MEI, Maddison (1994)
(OFCE 2012, 20)

Table 7.1 shows that these large levels of growth, are on average 1.4% higher in France than in the US between 1950 and 1973. This high level of growth was due to industrial production techniques seeping into every economic sector, which also shows at what speed the French and the other European economies evolved during that 30-year period (OFCE 2012). Looking at these numbers it is not hard to imagine how people would come to expect a continuation of comfort and aid from a government.

After the first oil shock and the end of the Bretton Woods monetary system, the speed of economic growth with which France and the EU developed was halved (Table 7.1). The levels of growth and the economic progress, which had started after WW2, had ended by 1975 and a countermove of high unemployment and low growth had set in. This countermove was a large contributing factor in the increase of the power of the neo-liberal economic concept.

Table 7.2 Unemployment in France, the USA and the Euro Zone



Note: unemployment level according to the International labour office (ILO)
Source : OCDE MEI
(OFCE 2012, 22) (copy of table chômage en france aux Etats-Unies et ans la zone euro

As Table 7.2 shows, the end of the period of high growth in Europe during the 1970s also affected the unemployment levels in the EU, the US and France. Table 7.2 shows, a marked rise in the unemployment rate in 1974 for the US the EZ and France (the EZ and France had a steady increase while the US line continuously fluctuated), which is consistent with the reduced economic activity for the US, the EZ and France highlighted in Table 7.1.

De Boisdeffre and Joly (1991) argue that the reasons for the higher rate of unemployment were caused by higher labour costs and lower qualified labour after the end of the 30 Glorious Ones. This argument can be substantiated by the fact that since the Accords Mattignon (1936) the French labour unions have gained significant powers of negotiation and protection for their workforces. The Accords Mattignon (1936) allowed workers to unionise and not be discriminated against during the hiring process or during work distribution because they were already part of a union. The Accords Mattignon (1936) also included a pay increase of 7%-15% of the worker's salary. Every firm even SME's gained worker representation and employees were no longer allowed to be sanctioned by the firm if they went on strike (Accords Matignon 1936). The Accords Mattignon provided unions with a lot of power and workers with a lot of protection, which were a contributing factor to the higher labour costs in the 1980s.

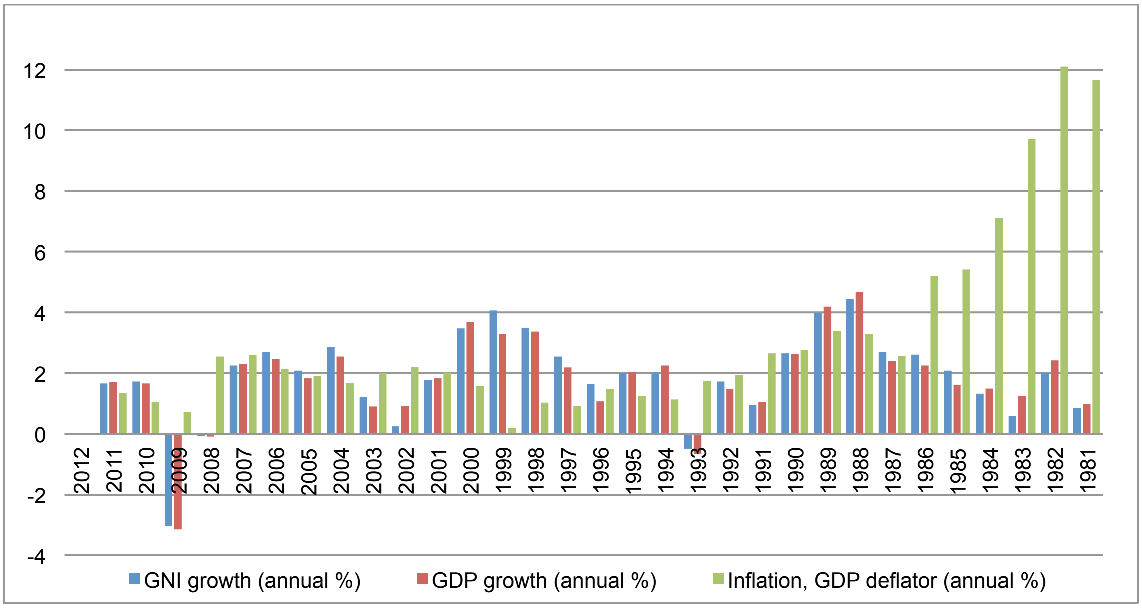
7.3 After 30 years of Economic Growth, 30 years of French political stasis

As the previous chapter argued, during the Mitterrand Presidency, a pattern of political stasis became set in French politics. This led to an ossification of negotiating positions among the social partners, which in turn prevented any substantive labour market or social reforms to be passed, which may have helped to deal with the economic fluctuations during the 1980s, 1990s and 2000s.

7.3.1 The decline of the 1980s

During the 1970s and 1980s two oil shocks reverberated through the world and the French economy. As Table 7.1 showed, *GDP* growth rates had halved to about 2.5% in the late 70s. Table 7.3 shows the low levels of *GDP* growth throughout the first half of the 1980s which were also shown in Table 7.1 but more importantly, Table 7.3 shows the *high levels of inflation* that developed in France *after the second oil shock*.

Table 7.3 Economic Growth Indicators 2

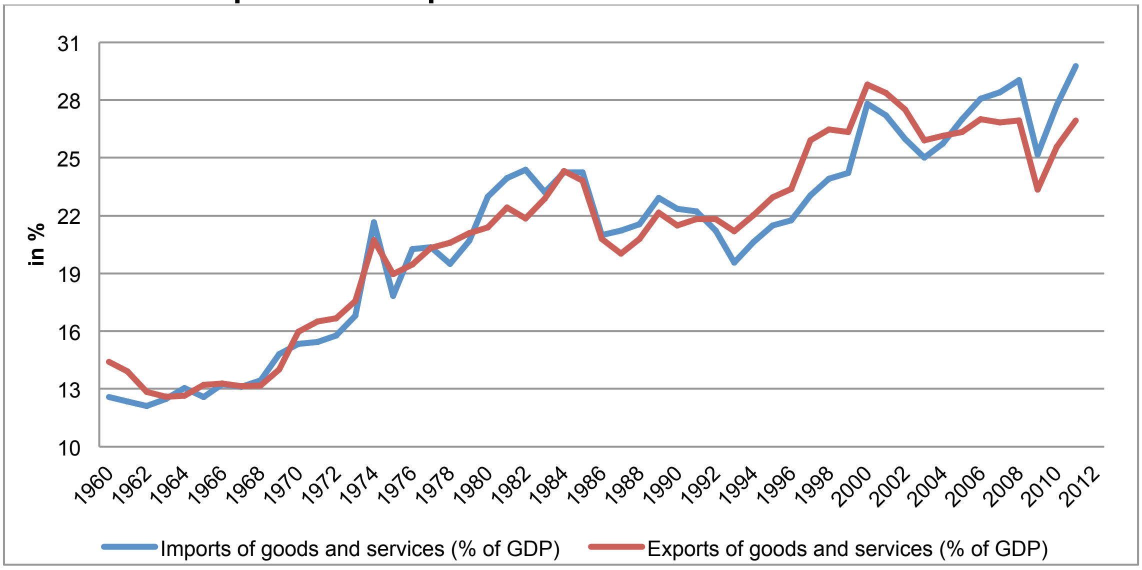


WB Data (accessed 2012, own presentation)

These high inflation levels were exacerbated by the government's support and encouragement of domestic consumption. Since there was a global economic downturn, the French strategy involved stimulating internal competition in order to stimulate internal production, which fits with Keynesian economic theory. This effort was designed to spur consumption of internal products but, as Table 7.4 shows, all throughout the 80s but especially in the early 80s imports largely exceeded exports. As a result, the level of inflation in

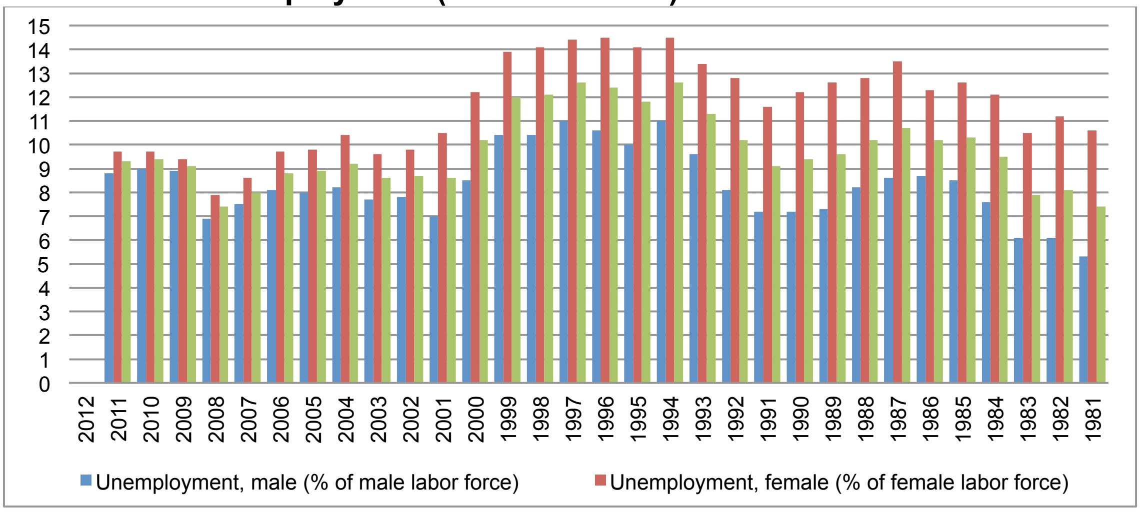
France was almost eleven times higher than GDP growth. The inflation increased because domestic spending was artificially increased to bolster domestic production. However, domestic consumption did not only consume local products but had to be compensated with imported goods, causing inflationary pressures.

Table 7.4 Imports and Exports of Goods and Services



WB Data (accessed 2012, own presentation)

Table 7.5 Unemployment (Male & Female)



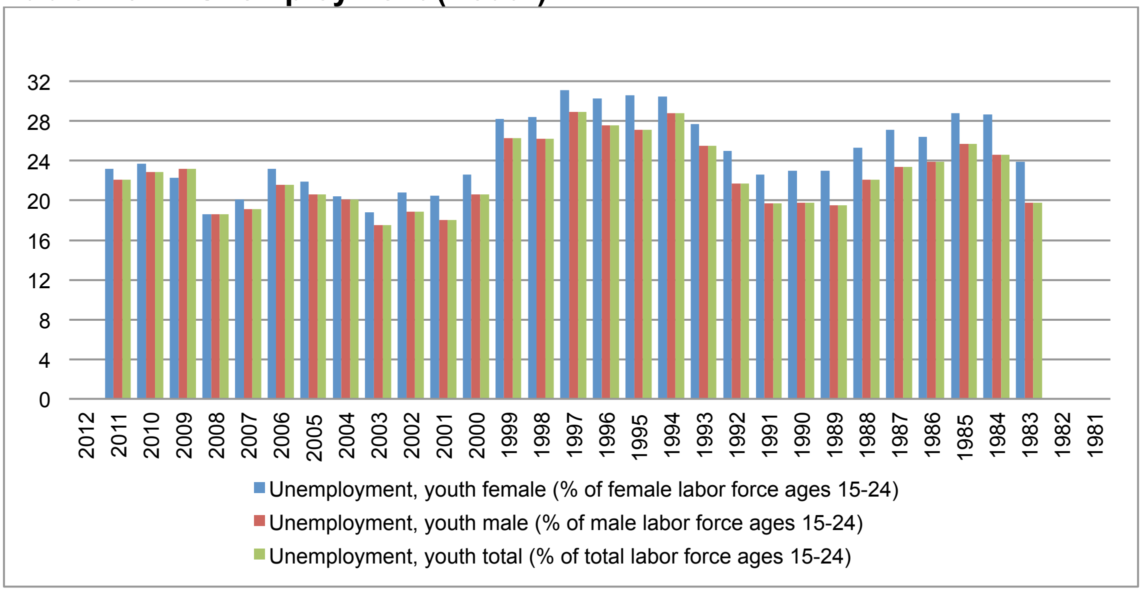
WB Data (accessed 2012, own presentation)

The rise in unemployment depicted in Table 7.2 and Table 7.5 was not halted by the efforts of the Mitterrand government. Even though the Mitterrand government had instituted programmes and reforms designed to increase employment such as public works projects and reforms to the working times (39-hour week in 1982, see Chapter 6) and the retirement age (reduced to 60 from 63 in 1981, see Chapter 6), the unemployment rates continued to climb (see Table 7.5). It was only after 1982 once the Mitterrand government decided to maintain French support for the European project and the common currency that the government focussed on implementing some neo-liberal prescriptions to reduce inflation, so that domestic consumption could begin again. This decision helped unemployment to start going down and levels of GDP started to grow (see Table 7.3). It should also be noted that differences in unemployment between Men and Women remained high throughout that time, and it was only with the economic upturn of the early 2000s that the unemployment figures between men and women started to equalize (see Table 7.5), however, women continue to be the most vulnerable to unemployment.

7.3.2 The declines of the 1990s and 2000s

After a brief economic recovery from 1984 to1988 (Table 7.3) and a rise in GDP to an above four percent annual growth in 1988 (see Table 7.3), 1991 marks the beginning of yet another period of reduced or negative growth in France. With this period of slow growth came also a period of increased unemployment (Table 7.5) with women again being the worst affected. The difference of this economic contraction, as compared to the one of the 1980s, was that this period was particularly hard on the French youth (Table 7.6).

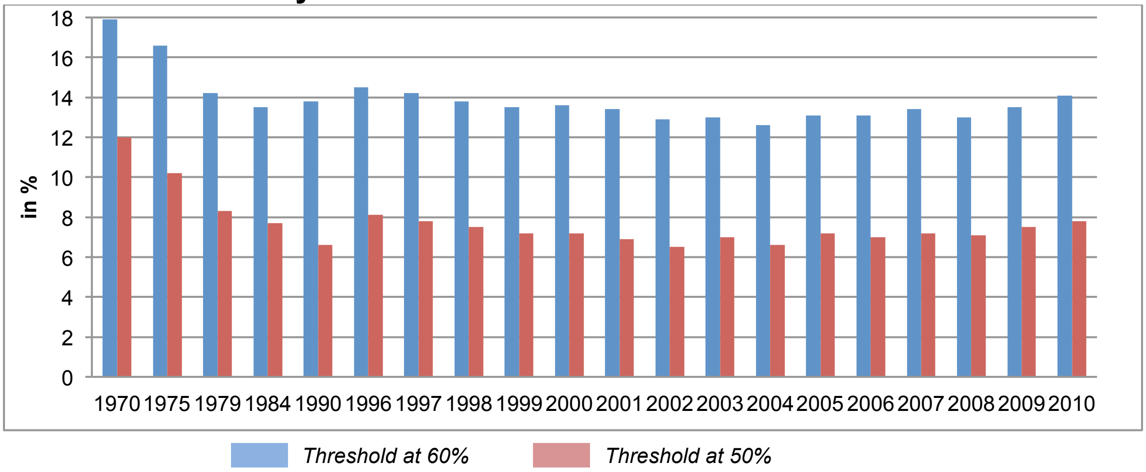
Table 7.6 Unemployment (Youth)



WB Data (accessed 2012, own presentation)

As Table 7.6 shows, youth unemployment between 1994 and 1997 reached its highest level to date with almost a third of all young people between 15 and 24 years without employment. Worst off were young women, whose unemployment rate was constantly higher than the employment rate of the male youth. Although these numbers do not show a healthy economy, the negative impacts on society have not been as severe as one would expect from those numbers. As Table 7.7 shows below, the slow economic performance of France did not have equally negative effects on poverty rates.

Table 7.7 Poverty Levels

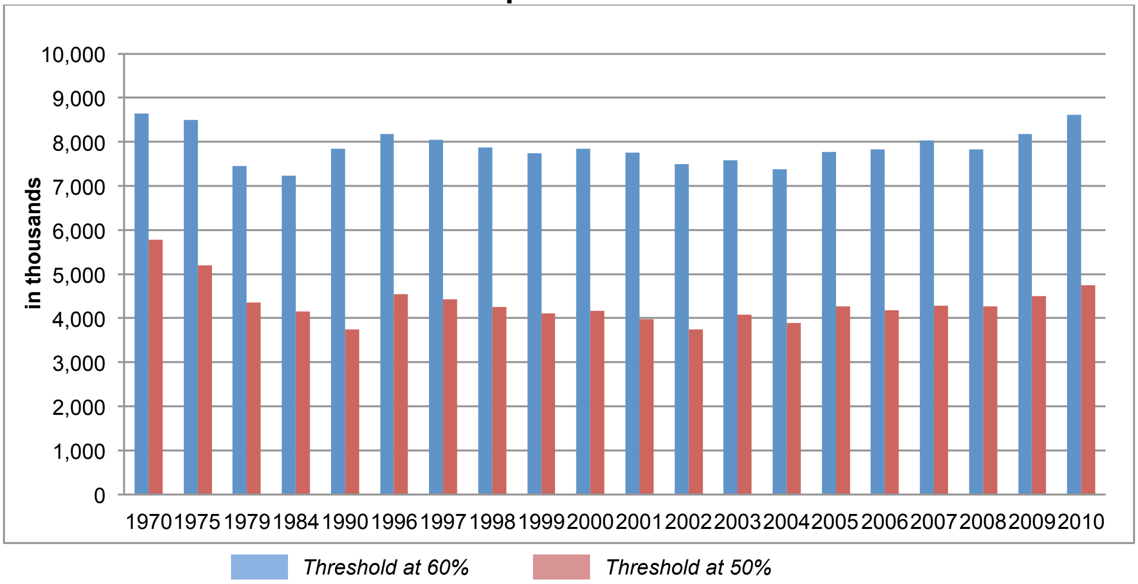


INSEE 2011, Sources : Insee-DGI, enquêtes Revenus fiscaux 1970 à 1990, Insee-DGI, enquêtes Revenus fiscaux et sociaux rétropolées 1996 à 2004, Insee-DGFiP-Cnaf-Cnav-CCMSA, enquêtes Revenus fiscaux et sociaux 2005 à 2010.

Table 7.7 shows that, after a period of poverty reduction all throughout the 1970s which was a result of the strong growth of the French economy at the time, there was an increase in poverty throughout the 80s and mid-90s. The increase in poverty came about during the second economic downturn in the 80s. Considering the generally depressed state of the economy from 1990-1996 (Table 7.3), the impacts on poverty were not as severe as one might expect. The impact was also partial: the section of people who earned 60% of median income were less affected than the section earning 50% of median income whose poverty levels rose to their highest point since 1979.

After 1996, the increase in poverty was once again reduced as the French economy recovered from its slowdown. The decreasing trend continued throughout the rest of the 1990s and into the 2000s, albeit at a far less rapid pace than throughout the period of the 1970s. Starting in 2004, one can once again distinguish a trend of increasing poverty. This increase becomes apparent when one considers the absolute poverty numbers in Table 7.8, where an increase in the number of people in poverty from 2004 onwards can be seen.

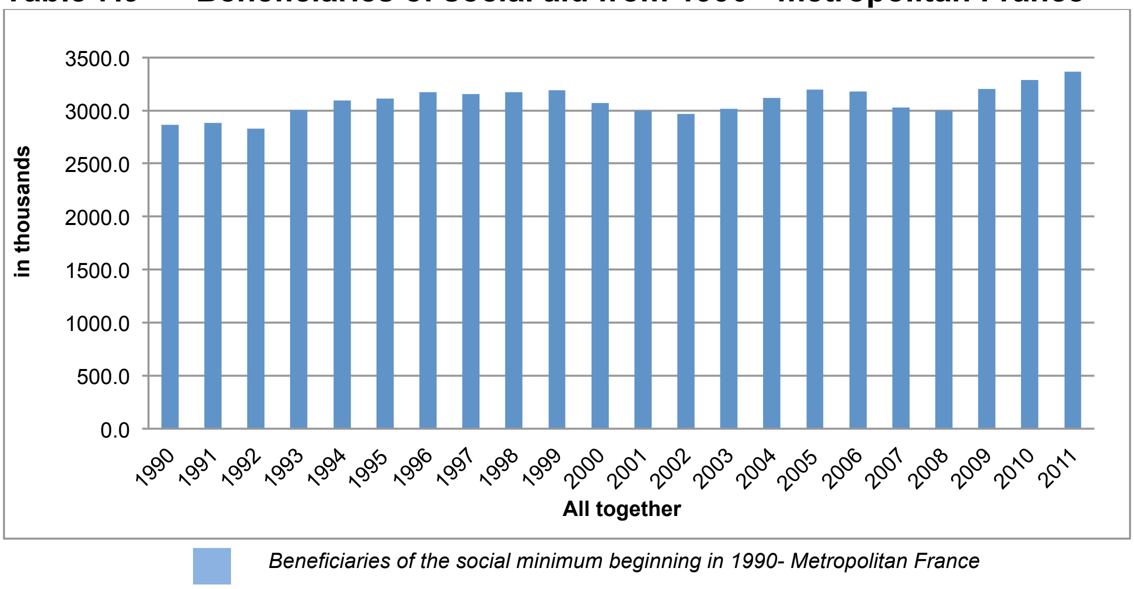
Table 7.8 Number of Poor People



INSEE 2011, sources: Insee-DGI, enquêtes Revenus fiscaux 1970 à 1990, Insee-DGI, enquêtes Revenus fiscaux et sociaux rétropolées 1996 à 2004, Insee-DGFiP-Cnaf-Cnav-CCMSA, enquêtes Revenus fiscaux et sociaux 2005 à 2010.

The benefits received by the French population to be able to maintain their living standards go some way to explain the low fluctuations in the poverty numbers. The state had taken on a greater responsibility for providing for people if they are unable to do it for themselves when Mitterrand implemented the RMI in 1988. Table 7.9 demonstrates the evolution of the RMI payment since 1990. If one compares the trends from Table 7.3 on GDP growth with the amounts of RMI beneficiaries one can see a similarity in the trends i.e. RMI goes up when GDP growth goes down. This suggests a correlation between economic performance and people in need of aid as well as the presence of state intervention in society.

Table 7.9 Beneficiaries of social aid from 1990 - metropolitan France



INSEE 2011a, Source: Cnamts, Cnaf, MSA, Drees, Pôle Emploi, FSV, Cnav, CDC.

Table 7.10 shows the different benefits available to the French population. This table includes all benefits available (including the ones that have ceased) to demonstrate the variety of benefits available to people who are not as well off as others. The RSA and the RMI beforehand comprise the largest part of the benefit amount available to people in need and are the ones most widely available to people (see Table 7.19). The other benefits are additional amounts designed to alleviate a specific condition of inequality, the size of which the government decides is the greatest cause of inequality.

Table 7.10 French forms of social spending

Income of active solidarity (Revenu de solidarité active) (RSA) socle (1)
Jobseekers Allowance (Revenu minimum d'insertion) (RMI)
Allocation for an Isolated Parent (Allocation de parent isolé) (API)
Allocation for adults with disabilities (Allocation aux adultes handicapés) (AAH)
Additional allocation for disabilities (Allocation supplémentaire d'invalidité) (ASI)
Allocation for specific solidarity (Allocation de solidarité spécifique) (ASS)
Insertion allocation or Temporary waiting allowance (Allocation d'insertion) (AI) ou (Allocation temporaire d'attente) (ATA) (2)
Additional old age allowance and solidarity allocation for older people (Allocation supplémentaire vieillesse) (ASV) et (allocation de solidarité aux personnes âgées) (ASPA) (3)
Allocation for widows (Allocation veuvage) (AV)
Allocation for retirement (Allocation équivalent retraite – remplacement) (AER)

(1) The RSA replaces the RMI and the API in metropolitan France beginning on the 1st June 2009, and in the overseas territories from the 1st January 2011. Only part of the RSA (the RSA socle) is considered a social minimum.

(2) The ATA replaces the AI for the entries beginning on the 16th November 2006.

(3) The ASPA entered into force on the 13th January 2007. It substitutes for the new beneficiaries the old allocations ASV.

INSEE 2011a Source: Cnamts, Cnaf, MSA, Drees, Pôle Emploi, FSV, Cnav, CDC.

This variety of benefits shows how important state involvement is in France. Although the different allocations vary in monetary amount that is available for each individual, they are cumulative, thus (in theory) providing every aid seeker with enough money to allow him to participate as fully as possible within society.

> These social minima are designed to ensure a minimal income to a person (or his family) without employment and precarious prospects of reemployment. These are non-contributory social payments, meaning that they are paid out without having to have contributed to the fund. (Insee 2014, définitions minima sociaux)
> This type of benefit is paid with regards to the resources available thus allowing the beneficiaries to reach a certain level of comfort (Insee 2014, définitions minima sociaux)

Considering the increasing amount of unemployed people in France at the time, this generous provision of state aid was a substantial drain on the financial resources of the French government. So much so that the French state has breached the stability and growth pact limiting the national debt to 60% of GDP and to a 3% of GDP increase per annum (Feldman 2003).

This financial commitment remains important in France to this day and continues to be a major staple of French government expenditure and remains a major area of refrom.

7.4 The French conundrum two decades into the new millennium

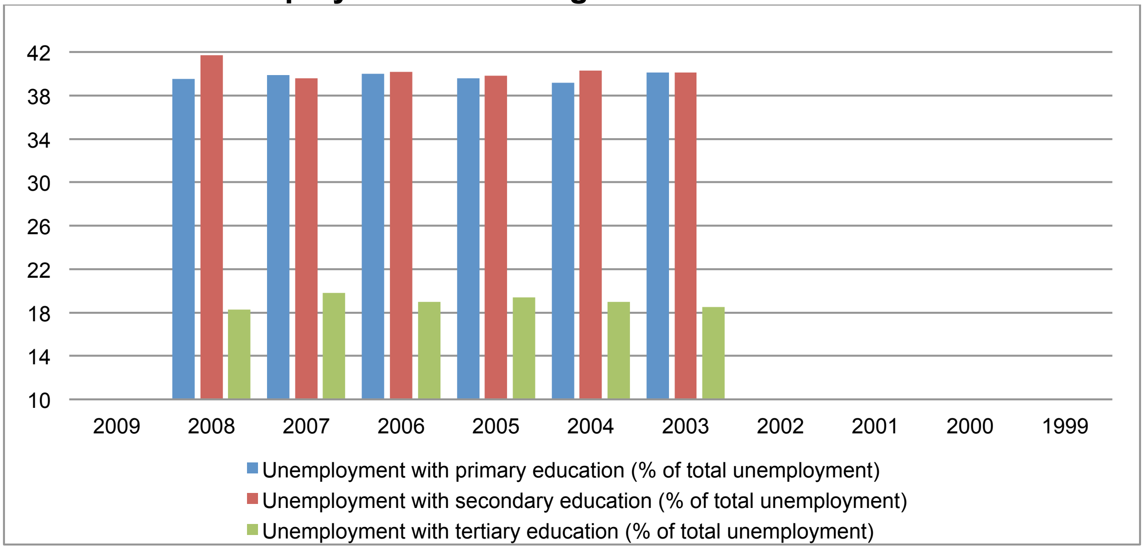
After a long period of low economic growth and a brief period of recovery in 2002, the second term of Jacques Chirac began with the lowest level of economic growth in 9 years, a stagnating poverty rate and stagnating unemployment levels.

7.4.1 2002-2008

France went through a period of low unemployment (see Table 7.5 & 7.6) at the beginning of Chirac's second term (2002-2007) compared to only two years before in 2000 when unemployment was much higher. The introduction of the 35-hour week in 2001 likely played a role in that change. The introduction of the 35-hour week meant that people worked fewer hours during the week, which in principle would mean that companies had to increase their staff in order to get through the work that needed to be done.

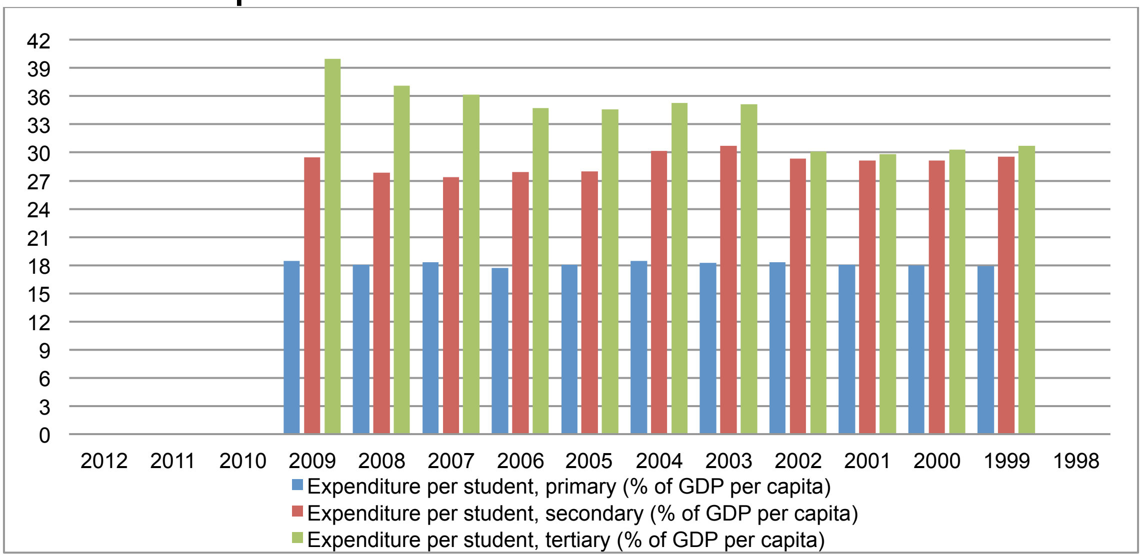
Table 7.11 shows that people who were out of work during 2003-2008 were largely people who only had primary or secondary education. Thus people with lower qualifications were about twice as likely to be unemployed as people with higher qualifications. This trend is comparable to the trend in Germany (see Chapter 6). It shows that education, irrespective of country or social standing, is important and that any amount of national social spending should include significant educational funding to enable people to get better qualifications and increase their chances of employment.

Table 7.11 Unemployment according to education



WB Data (accessed 2012, own presentation)

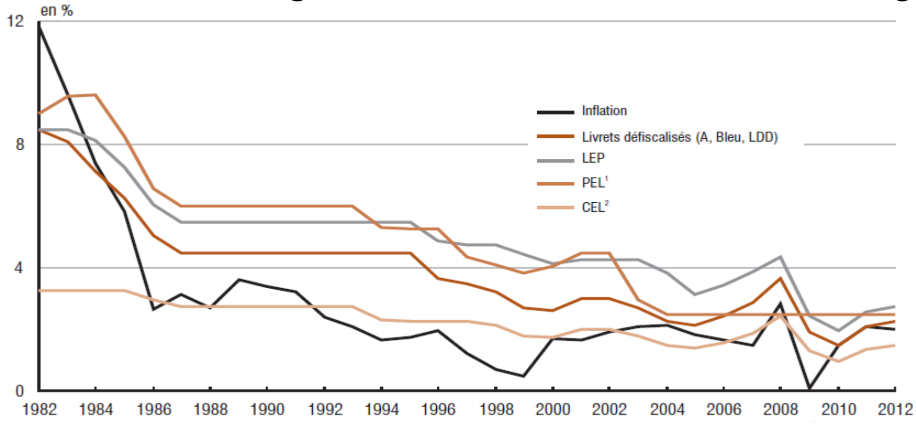
Table 7.12 Expenditure Per student



WB Data (accessed 2012, own presentation)

In that respect, Table 7.12 shows that funding for tertiary education has increased as of 2003 by approx. 5% per student. This can also be considered as a move by the French government to improve the level of education of its youth to increase its possibilities for employment. Irrespective of that increase, the unemployment numbers of people with tertiary education have continued to increase if only slowly (see Table 7.11). Overall though, the GDP data in Table 7.3 suggests that the years of the second Chirac Presidency were years of plenty comparatively for France and for French society.

Table 7.13 Average nominal returns on investment savings



Livrets défiscalisés (A, Bleu, LDD): Tax-free Savings Accounts (A, Blue, LDD)
1. PEL opened that year. The interest rates of the PEL are presented with bonuses included until 2002 and excluded from 2003. Before 2003, the bonus form the state was included in the interest rate of the PELs. Since 2003 the bonus of the state is conditioned on being awarded a house savings loan (PEL) and the interest rates are given without state bonuses. For the PEL opened since 1st august 2003, the bonus reaches 2/5 of the earned interest rate up to the limit of 1525 euros (or 2/5 of the interest rate corresponding to a monthly transfer of 237 euros during 10 years with an initial transfer of 225 euros).
2. The interest rates of the CEL are presented without state bonuses. The awarding of the state bonus is conditioned by being awarded a PEL. Since the 16 of June 1998, the bonus is equal to half of the interest acquired up to 1144 euros.
Area: Metropolitan France until 1989, France since 1990
Source: Insee, Legifrance
INSEE 2012 (1. Taux de rendement nominal moyen des différents livrets) Fiche thema (patrimoine) p. 125.

Table 7.13 confirms this trend. Economic monetary theory argues that, through a reduction of the interest rates, consumption can be incentivised by making spending money more attractive than saving money (Carlin & Soskice 2006). The decrease in the return on the different savings accounts (Livrets défiscalisés, LEP, CEL) and the return on loans (EPL) especially after 1996 and continuing throughout the 00s shows how consumption was encouraged throughout that time. Consumption was further encouraged since the inflation and savings rates came closer and closer together over that same time period making it ever less profitable to save.

Table 7.14 shows that the differences in inequality between 2002 and 2008 did not change all that much. Although there has been a slight increase in differences between the rich and the poor, in favour of the rich, this was a negligible increase. Table 7.14 shows in the second to last line in that table, the calculation establishing the income differences between the wealthiest 20% and the poorest 20% (see also note in the appendix to the statistic below). The wealthiest 20% only went from being 4.1 times better off than what the poorest 20% in 1996 to being 4.3 times better off than the poorest people in France in 2007 and 4.5 times better off than the poorer people in France in 2010. This is further evidence that the endeavours of the French state to establish and manage a redistributive society were being quite effective. However, this came at the cost of reduced competitiveness.

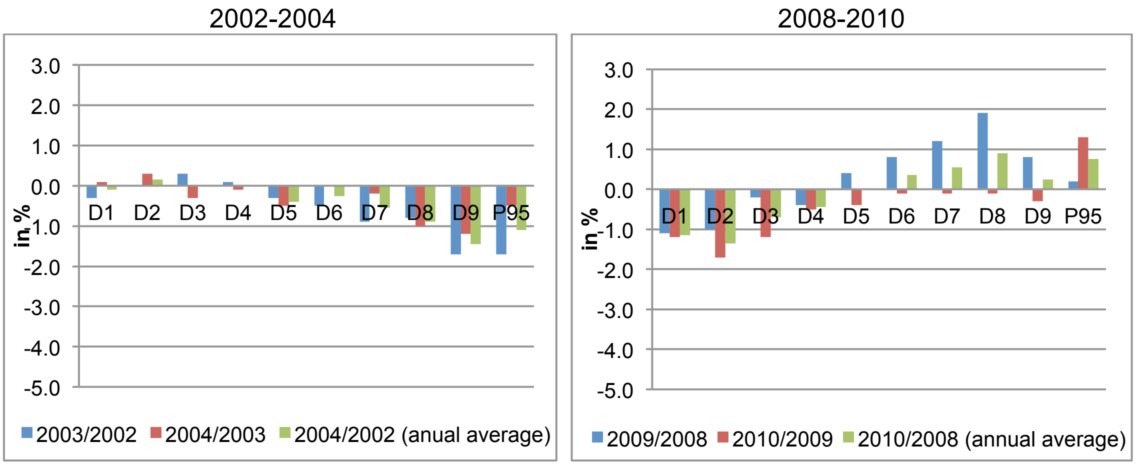
Table 7.14 Standard of living levels and inequality indicators

	1996	2002	2003	2004	2005	2006	2007	2008	2009	2010
Standard of living (in € 2010)										
Median (D5)	16350	18150	18100	18010	18320	18580	18980	19290	19360	19270
First decile (D1)	8690	10120	10080	10100	10120	10250	10460	10690	10570	10430
Ninth decile (D9)	30530	34340	33780	33350	33920	34950	35420	36120	36380	36270
Final twentieth (P95)	37230	42900	42210	41990	43180	44120	44800	45430	45530	46140
Interdecile relations										
D9/D1	3,5	3,4	3,4	3,3	3,4	3,4	3,4	3,4	3,4	3,5
D9/D5	1,9	1,9	1,9	1,9	1,9	1,9	1,9	1,9	1,9	1,9
D5/D1	1,9	1,8	1,8	1,8	1,8	1,8	1,8	1,8	1,8	1,8
(in %)										
S20	9,0	9,3	9,3	9,3	9,0	9,0	9,0	9,0	8,9	8,7
S50	31,0	31,1	31,2	31,2	31,0	30,7	30,7	30,9	30,7	30,2
S80	63,0	62,3	62,4	62,4	62,0	61,6	61,8	61,6	61,8	61,0
(100-S80)/S20	4,1	4,1	4,1	4,0	4,2	4,3	4,3	4,3	4,3	4,5
Gini index	0,279	0,281	0,280	0,281	0,286	0,291	0,289	0,289	0,290	0,299

Explanation: Metropolitan France, people living in a household where the income is taxed is positive or zero and where the person of reference is not a student
Reading of the statistic: in 2010 the 20% poorest owned 8.7% of the level of the standard of living, the 20% richest owned 39% of the standard of living (relation between the bottom and the top 20%) or the richest owned 4.5 times more than the poor.
Source: Insee-DGI, enquêtes Revenus fiscaux et sociaux rétropolées de 1996 à 2004. Insee-DGFiP-Cnaf-Cnav-CCMSA, enquêtes Revenus fiscaux et sociaux 2005
Houdré, Missègue, Ponceau 2013 Vue d'ensemble – inégalités de niveau de vie et pauvreté p.10.

Table 7.15 shows a different aspect to this analysis. The left hand side graph shows how the living standards of the different income groups have changed over the years. The left side table shows at the bottom the standard of living deciles from D1 (bottom 10%) to P95 (top 5%). Between 2002-2004, the green bar in the table, representing the average decrease in the standard of living, shows that the lowest incomes have maintained their quality of living. However, the upper incomes beginning with the top 60% (D6) have suffered increasing losses in their living standard. The greatest losses to their quality of life have been suffered by the top 10% (D9) followed by the top 5% (P95). As the right table shows, between 2008 and 2010 when the 2007/2008 crisis hit France, the picture was reversed. The green bar indicating the average change in standard of living shows that the bottom 50% (D1-D5) have lost standard of living with the biggest losers being the bottom 30% (D1-D3). It should also be noted that during the crisis (2008-2010) the top 40% (D6-P95) have managed to increase their standard of living, in particular the top 20% (D80) and the top 5% (P95) which would suggest a transfer of wealth from the bottom to the top. Table 7.16 will investigate this point further.

Table 7.15 Evolution of some deciles in standards of living



Field: Metropolitan France, where the person living in an ordinary household isn't a student.
Reading: In 2003, the first décile of the standard of living has fallen by 0.4% compared to 2002. Between 2002 and 2004 it has fallen by 0.1% on average
Sources: Insee-DGI, enquêtes Revenus fiscaux et sociaux rétropolées 1996 à 2004: Insee DGFiP-Cnaf-Cnav-CCMSA, enquêtes Revenus fiscaux et sociaux 2005 à 2010
Houdré, Missègue, Ponceau 2013 ,Vue d'ensemble – inégalités de niveau de vie et pauvreté p.11.

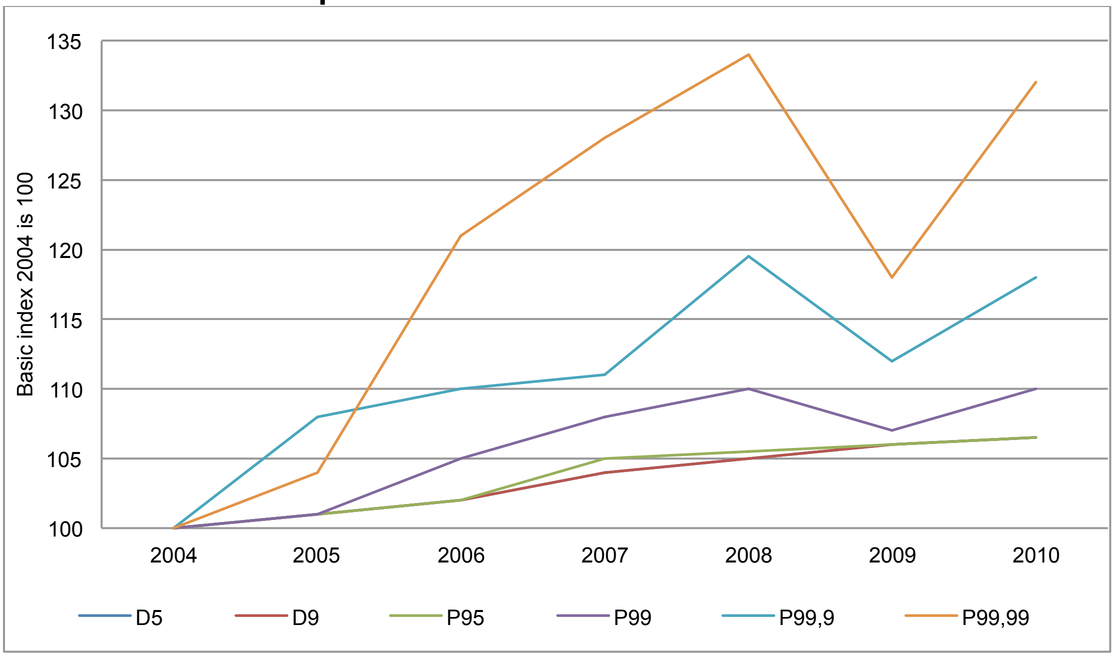
Table 7.15 shows the evolution of the standard of living from 2002-2004 and Table 7.16 shows the evolution of income from 2004. Table 7.16 allows the bridging of the years between 2004 and 2008 that were not investigated in Table 7.15. Table 7.16 shows a concentration of wealth in the high-income segment beginning in 2005. The incomes between the middle earners (D5, dark grey line on the table) and the top 10% (D9, dark brown line on the table) and top 5% (P95 dotted line on the table) of earners have remained virtually on par throughout the last decade.

However, the earnings of the top 1% (P99, light grey line) have started to grow at a bigger rate from 2005 onwards. It is however the earnings of the top 0.1% (P99.9, black line) and 0.01% (P99.99, light brown line) which have increased at a near exponential rate from 2005 onwards. Considering the reduction in the standard of living between 2002 and 2004 that was demonstrated in Table 7.15, it could reasonably be argued that the negative impact on the standard of living was mitigated after 2005. This interpretation finds support in the second statistic of Table 7.15.

Considering the income evolution on Table 7.16 which shows the income evolution of the top 50% of earners, it shows that the income increases between the 5th declie and the 99th percentile (D5, D9, P99) have grown at the same pace. However, from 2005 to 2008 and once again after 2009 the top 1% of the French population have seen their incomes increase as opposed to the remaining 99% of the French population. The top 0.1% and the top 0.01% in particular have, with the exception of 2008, managed to increase their wealth continuously in comparison to the remainder of the French population. It can be concluded that at least the top 50% to the top 99% of the French population have remained within range of one another. Table 7.15 (on the right from 2008-2010) suggests that the bottom 50% of the French population have been left behind to a certain extent. This conclusion is commensurate with the conclusion reached by Crouch (2011), who argued that the success of the current neo-liberal economic system is predicated on a concentration of wealth among the few and increase of debt of the larger mass of people with which the few can trade and increase their profits.

This is a poignant example of how much the French economy is enmeshed within the global neo-liberal economic structure and how dependent even France is upon its continued functioning. It further shows that France is also required to conform to the rules, which the economic structure sets, for France to be able to thrive politically and economically.

Table 7.16 Evolution of some deciles in terms of declared income by consumption unit between 2004 and 2010



Champ: France métropolitaine, personnes appartenant à des ménages fiscaux dont le revenu déclaré par unité de consommation est strictement positif.: Feild: Metropolitan France, people belonging to a fiscal household where the declared income by consumed unit is strictly positif

Lecture: en 2010, le seuil plancher du dernier dix millième de la population (P99,99) est supérieur de 32% à celui de 2004 en euros constants.: in 2010 the highest level of income of the last thousandth of the population (P99,99) is 32% greater than the one in 2004 in constant euros.

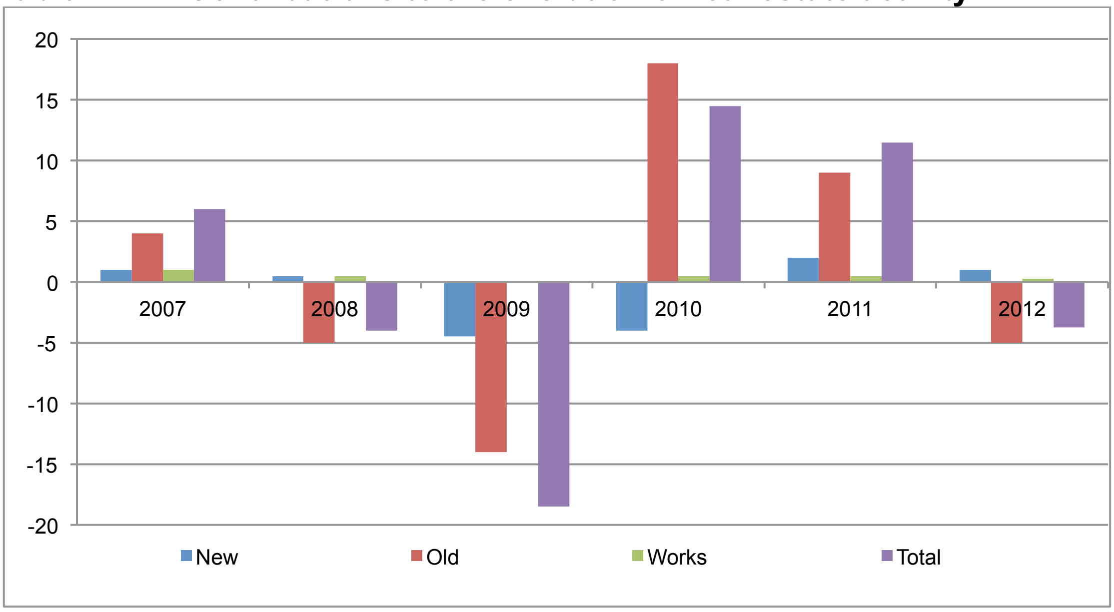
Sources: Insee-DGFiP, Revenus fiscaux localisés (RFL) 2010, calculus Insee

Houdré, Missègue, Ponceau 2013, Vue d'ensemble – inégalités de niveau de vie et pauvreté p.15

7.4.2 2008-2012 and 2012-2014

Considering the fact that in 2007 the financial crisis hit the US and then in short order hit Europe, France experienced the effects of the crisis by 2008. Table 7.3, 7.4 and 7.5 demonstrate well the initial change in the levels of equality, which have held steady over at least the last decade. Table 7.15 shows that between 2008 and 2010 the people in the lowest income deciles have experienced the same reduction in their living standards as the highest income deciles had in the space of 2002-2004. However, the incomes of the 5th to the 9th deciles over that same period (see Table 7.16) have seen no particular variation to their past progression. It is only in the 1%, 0.1% and 0.01% income ranges that the biggest changes have occurred. They have suffered a cumulative loss of income of approximately 25% between 2008 and 2009. However, those losses have virtually all been recovered in the period of 2009-2010 (Table 7.16).

Table 7.17 Contributions to the evolution of real-estate activity



New	Contribution in points
Old	
Works	
Total	Evolution of the total acquisitions and work done in value (in %)

Source: Compte du lodgement 2011

Caicedo 2012, Observations et statistiques (n 150 decembre 2012) Page 2.

The period of 2008-2012 is a period of strong variations as Table 7.17 demonstrates. Here it can be seen that the recession of 2008 and 2009 had a significant impact on construction. It was only after 2009 that construction picked up again. Table 7.17 shows that in 2010, purchases of houses have picked up again (purple columns) after an equal reduction the previous two years. The building of new houses (blue columns) on the other hand only picked up again in 2011, however, at a lower rate. Table 7.17 further shows that the whole construction sector (green column) began to decline again in 2011 and going into recession again in 2012.

This is due to the depressed economic and business climate in France (see Table 7.18). Table 7.18 shows the business climate in France over time. The figure 100 in the table represents the baseline. If the indicator goes above 100 the business climate is positive, if the indicator goes below 100 the business climate is negative. A negative business climate represents a negative outlook by the French business community, which translates into reduced economic activity. Table 7.18 shows that, after a brief period of recovery from 2009 to 2011, the business climate in France has once again started to deteriorate and is continuing to do so. In 2013 the indicator has fallen to its lowest level since 1993 the 2008-9 period not withstanding since that was when the crisis hit France. This deterioration is also reflected in the decreasing trend of GDP growth in France (see Table 7.3).

Table 7.18 Business climate indicator for France

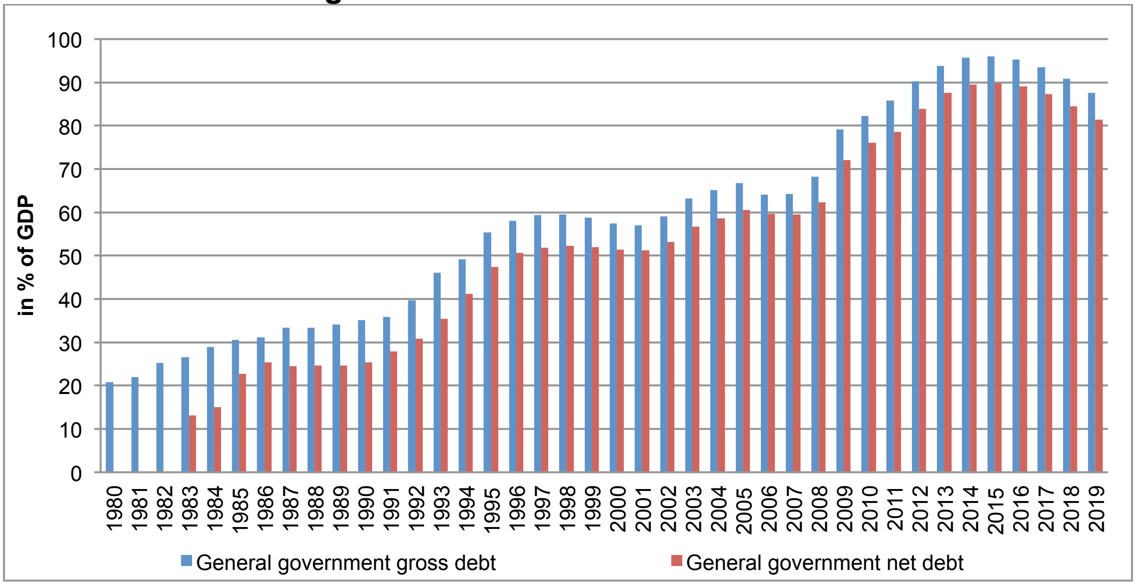
Baseline at 100 with a standard deviation of 10

Sources: Insee, enquêtes de conjoncture
Tavernier 2013, Informations Rapides (24 avril 2013 n.93)

The business climate (Table 7.18) and economic data demonstrate that the post 2008 effects continue to impact the French business climate. Table 7.18 shows a “double dip” recession in terms of business outlook between 2008 and 2012. A negative business climate does not preclude a continued good economic growth but it is a strong argument against it (in the short to medium term). Neither does a negative business climate preclude high social payments largely created by payments by the government to maintain a certain standard of living. These payments coupled with the depressed business climate, however, suggest that French deficits will rise substantially over the period from

2009 to 2013. This is substantiated by the IMF world economic outlook figures (see Table 7.19).

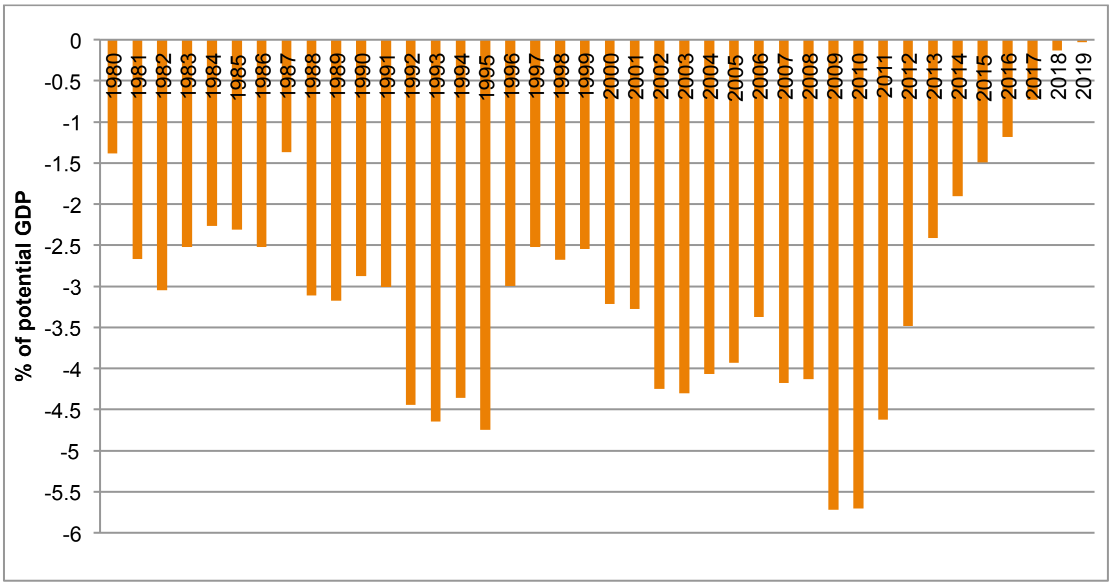
Table 7.19 General government debt



IMF world economic outlook (2014) (own representation)

General government gross debt includes all debt of the French government, and general government net debt is all the French debt that is not held by French institutions. This distinction is useful to see exactly how much of the French deficit is held by third parties and by how much the French debt exposure to third parties is, since those parties are most likely to demand higher interest rates during an eventual debt refinancing. This table shows that France has been in breach of the Maastricht criteria since 2003. Table 7.18 also shows that the level of debt is looking to be reduced as of 2015. The reason for this are the stringent measures implemented with the six-pack and two-pack rules (see Chapter 3) which require countries to submit their budgets to the Commission for approval. This however does not mean that the savings that the French state will undertake will be akin to the reforms that Germany has undertaken in the late 1990s and early 2000s.

Table 7.20 General Government Structural Balance



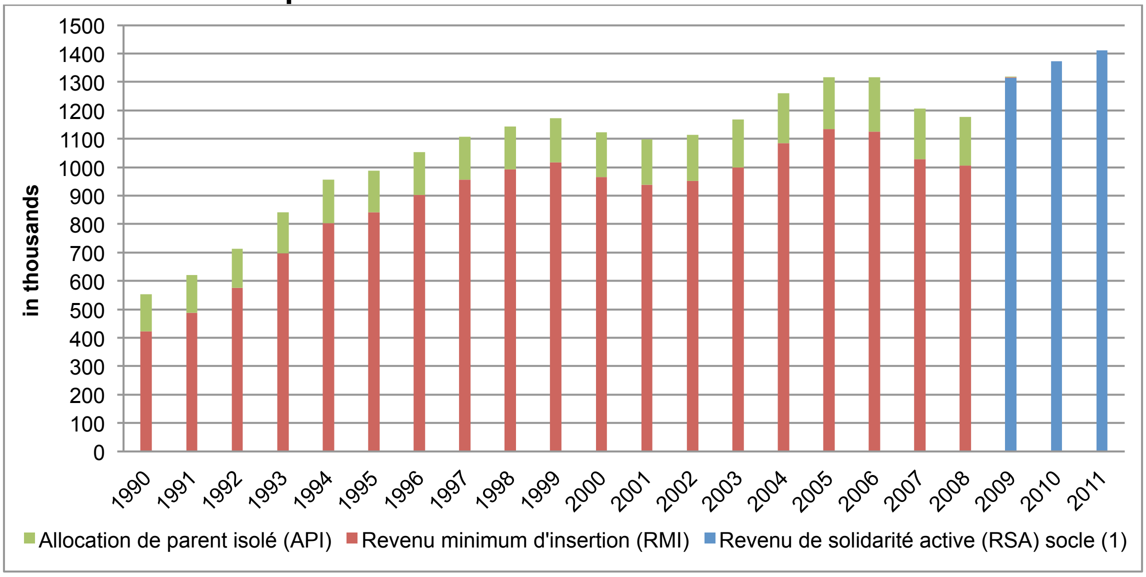
IMF world economic outlook (2014) (own representation)

The French government structural balance further underlines the trend that was discernible in Table 7.20 as well as in Table 7.3. The structural balance describes the total balance of payments income of a nation. Which for France shows that the French state has had greater expenditures than incomes, those deficits are predicted to be reduced significantly only after 2012.

Expenses in benefit payments (see Table 7.21) have continued to rise all throughout 2008 to 2012 as though there was no crisis. Considering the reduced income of the state due to the depressed economic situation (Table 7.18) and the lacklustre recovery of the economy once the crisis had passed, the national deficits have continued to climb, increasing the pressures on the economy. It also increased pressures by the EU institutions for France to bring its deficit under control as well as reduce the deficit to the 60% of GDP threshold outlined in the SGP, further lowering the French standing and French power within EU institutions charged with focussing on these issues.

The continued benefit payments did, however, help maintain levels of poverty as well as maintain consumption levels within France; this did prevent an even bigger economic contraction than the one that occurred as people were able to maintain their purchasing power (see Tables 7.6) thereby continuing to provide productive outlets for industries. Additionally, considering that the French state had not yet significantly reduced its spending, it too was and continues to be a major client to French industry.

Table 7.21 Beneficiaries of social payments from 1990 - France métropolitaine



(1)The RSA replaces the RMI and the API in Metropolitan France beginning on the 1st June 2009, and on the 1st of January in the overseas territories. Only a part of the RSA (the RSA socle) is considered as a social minimum.
Champ: France métropolitaine
INSEE 2011a Source: Cnamts, Cnaf, MSA, Drees, Pôle Emploi, FSV, Cnav, CDC (own calculations)

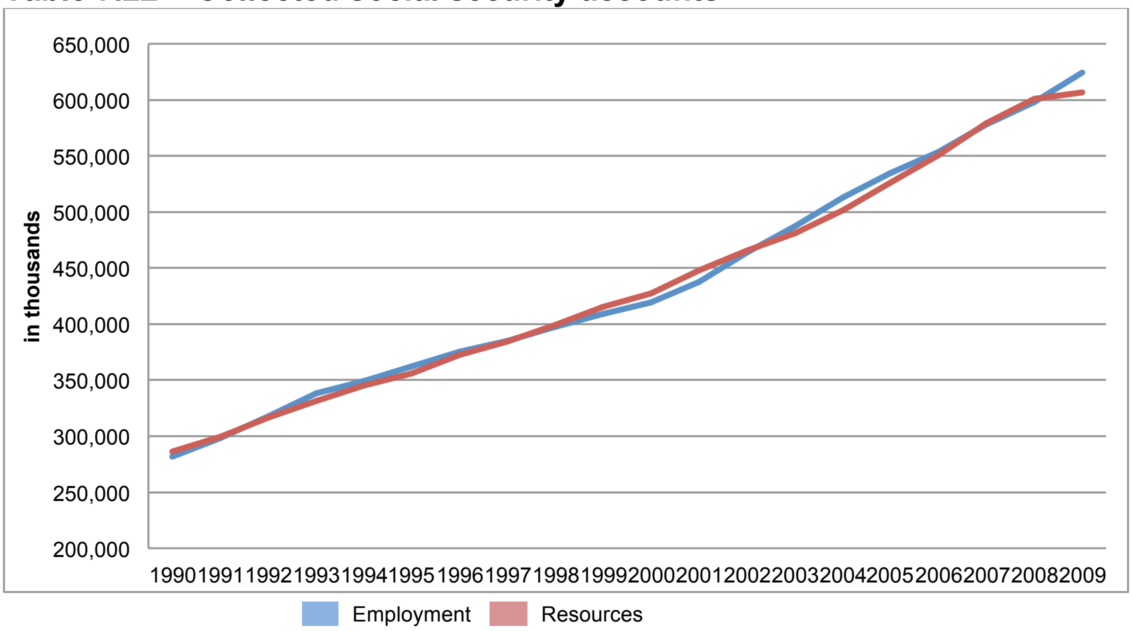
Table 7.21 shows the general trend that the benefits paid to the French population have increased from 1990 to 2006. Because in 2009 the API and RMI payments are combined in the single RSA payment this table includes both API and RMI payments in one column so as to show more clearly and more consistently how the benefit trend has evolved. Only from 1999 to 2004 was there a reduction in the benefits. This reduction is likely the result of the economic growth that picked up again during those years, creating more jobs and thus requiring fewer welfare payments to be made.

2007 and 2008 saw reductions in the RMI benefit payments for the first time in 7 years. This reduction was offset, however, by another increase in payments in 2009. In 2009, the RMI was also transformed into the RAS, which combined the RMI and the API payments into one single payment (hence the blue colour for that bit of the figure). Table 7.21 also shows that the 2008 to 2009 increase was the most significant 1-year increase in the benefit since 1990. The increases can be partly ascribed to the increased necessity for people to maintain their standards of living during times of economic contraction, thereby maintaining their levels of consumption. The increase may also have been influenced by the argument made in the “Report for French Growth” (Attali 2008) the unemployed who are looking for jobs should also be paid for these efforts, arguing that the search for a job is a job in its own right.

These RMI and RSA payments are quite effective as they reduce inequalities among high and low earners. The RMI and RSA have reduced by half the inequalities between the highest 20% and the lowest 20% of earners in France in 2010 (Direction de la diffusion et de l'action Régionale 2011, p5). Two thirds of this reduction is due to benefit payments, and the last third, is due to taxes (Direction de la diffusion et de l'action Régionale 2011, p5). This also points to the fact that these redistributions have changed in the mechanisms they use to decrease these inequalities. As the "Portrait Social 2011" argues, the social contributions have become the main method of inequality reduction instead of taxation (Direction de la diffusion et de l'action Régionale 2011, p.6).

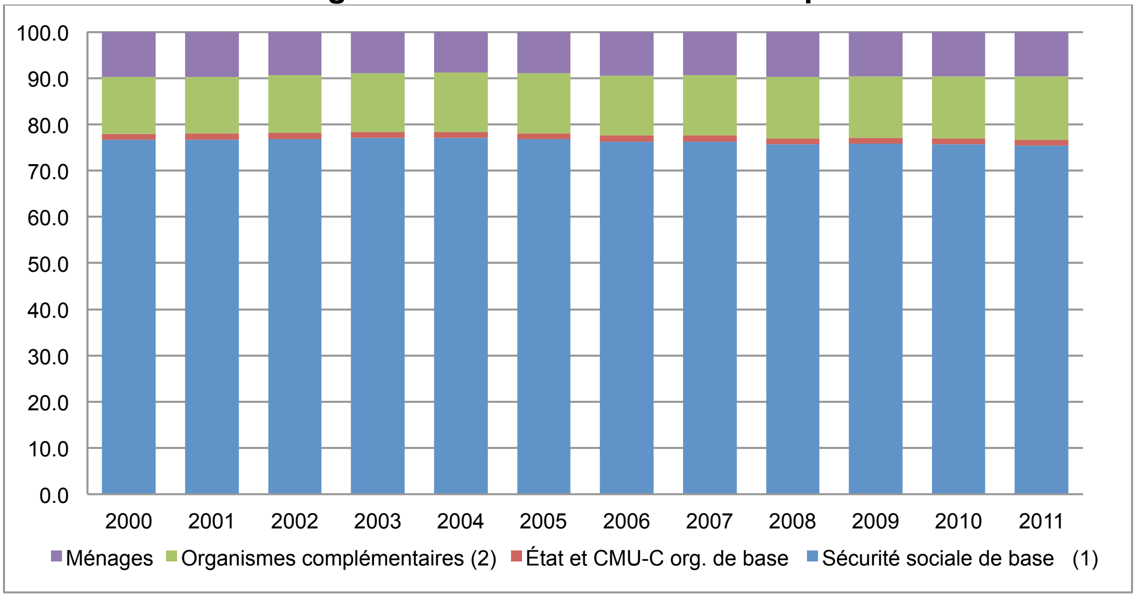
Table 7.22, shows that social security contributions (Resources, Red line) and the use (Employment, blue line) of that funding have been continuously increased since at least the 1990s. It is worthy to note that every time the blue line reaches above the red line, the Social Security accounts were in deficit and required aid from the state to balance the books. In 2008 the social security income has flattened, however, the use of social security has continued to rise, adding further pressure to the French deficit since the deficit is funded by the state (Table 7.22). While this in itself is nothing new as there were other years when this was the case, this gap is bigger than any gap since 1990. If it continues, the social security deficit will start to weigh in on the French budget deficit.

Table 7.22 Collected social security accounts



INSEE 2009 Source: Drees. (own calculation) access 06-09-May-2013 for all non WB IMF statistics

Table 7.23 Financing structure of the healthcare expenses



Zaidman, Garrec, Bouvet, Koubi 2012, Sources: DREES, Comptes de la santé.
Ménages: households, Organismes complémentaires (2): complementary organisations (2),
État et CMU-C org. De base: state and basic universal healthcare coverage, Sécurité sociale de base: basic social security
(1) including the public hospital deficit
(2) including CMU-C payments transferred by these organisations (own calculation)

Table 7.24 Financing structure of the healthcare expenses in %

	State	Social Security	Private Insurance	Households	Others
NED	8.5	77.2	5.2	5.5	3.6
NOR	73.3	12.2	..	14.2	0.2
DAN	84.6	0.0	1.7	13.7	0.1
LUX*	16.0	68.0	3.1	11.6	0.0
CZE	5.4	77.9	0.2	15.3	1.3
SUE	81.1	..	0.3	17.8	0.9
JAP*	8.6	71.6	2.5	16.3	1.1
FRA	**3.9**	**73.7**	**14.2**	**7.6**	**0.7**
GER	**6.7**	**70.5**	**9.6**	**12.4**	**0.8**
AUT*	32.3	44.8	4.7	16.8	1.3
BEL	10.9	64.7	4.8	19.4	0.2
FIN	58.9	15.2	2.2	20.2	3.4
ESP*	68.6	4.6	5.5	20.7	0.6
POL	5.9	66.3	0.7	23.7	3.4
CAN	**68.8**	**1.4**	**13.2**	**15.0**	**1.6**
AUS*	69.0	0.0	8.2	19.4	3.4
SLK	6.4	61.4	0.0	27.2	5.0
POR	66.0	1.3	4.6	27.5	0.6
SUI	18.9	46.3	8.6	25.1	1.0
HON	8.6	55.7	2.5	26.9	6.3
KOR	12.0	47.5	5.9	33.8	0.7
USA	**5.8**	**43.3**	**34.7**	**12.3**	**3.8**

* data 2009 (or last year known)
Zaidman, Garrec, Bouvet, Koubi 2012 Sources: Eco-Santé OCDE 2012. *(own highlighting)*

Table 7.23 and Table 7.24 break down the payments of French social security. Table 7.24 shows the way in which social security payments are spread compared to different countries around the world. Table 7.24 shows that three quarters of the French funding for social security stem from contributions (worker and employer), whereas in Germany those contributions are more spread out over the different pillars of contributions. The amount that should be noted is the amount of private social security and state contributions. The state contributions to social security only constitute 3.9% of the overall expenditure on social security. They are the lowest state funded contributions to social security in Europe, even lower than those for the US who are at 5.8% and lower than Germany's at 6.7%. Another important number to note is the one denoting the private contributions. French Private Contributions to social security are the highest in Europe with 14.2% more than 30% higher (own calculation) than in Germany even though the German Hartz reforms set Germany on a path to greater private health insurance, and second only to the US with 34.7% of total contributions.

The number that is also important to consider, is the social security amount set at 73.4%. This amount represents the amount paid by employer and employee towards social security. This number is by far the highest number of them all, and one of the highest rates on the list. It explains the number of people unemployed in France to some extent, as such a high level of social security contributions also increases the payroll costs of firms.

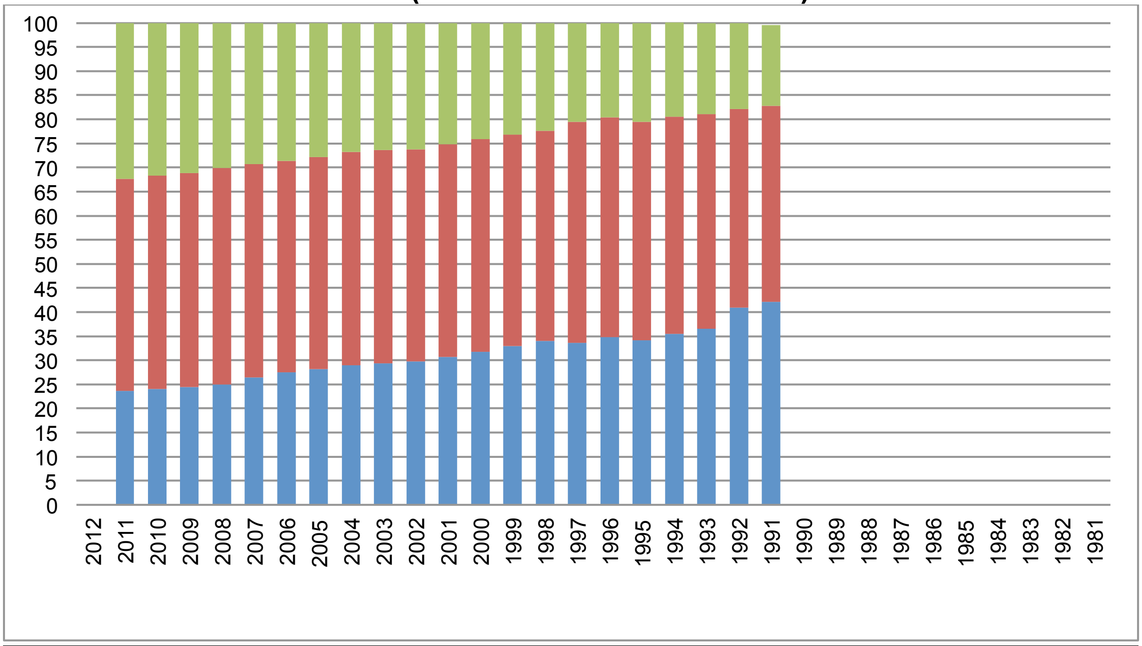
The reason why the French private contributions are so high, is because private insurances were introduced as a consequence of the French participation within the EMU and the Maastricht Treaty, requiring the government to make efforts at greater liberalisation of the economy. In this sense, private insurance was the French answer to the neo-liberal and industry requirement of greater liberalisation of the labour market and the French constitutional requirement of not making people worse off by reducing social protections (Howarth 2002, Green 1983).

Comparing the German and French numbers, one can see a greater balance in the funding for German social security than in France's social security whose focus is on standard employer and employee paid social security and payments for private social security. This would suggest a greater vulnerability of the French social security system to payment shortfalls than the German system has. This was pointed out in the Table 7.22.

Although differently balanced than other social security systems, the balance of social security, which the French system strikes, favours employer and private contributions instead of a greater burden sharing among all the social security payments. If the French government would diversify its income sources for social security, by increasing other sources of funding such as household- or state contributions, the French government could revitalise its economy. Doing so would allow the French state to reduce the employer and employee contributions, which would reduce the labour costs making labour in France cheaper and more attractive for foreign and domestic firms. The very high private insurance figure does suggest that the neo-liberal narrative of better performing private enterprises instead of state enterprises in the provision of services is taking hold in French national consiousness.

Educational funding has followed a similar path to that of social security funding especially in the case of tertiary education. As Table 7.9 above demonstrates, levels of funding for primary and secondary education have remained approximately the same. The sums on tertiary education however have, after 2002, continuously increased. This was also the case for 2008 and 2009 when the worst effects of the crisis were being felt in France. How much of a positive effect this spending may have had on education is unclear, as over the past 20 years there has been an upward trend for people in work with a level of higher education (Table 7.25). This is a strong indication that over the medium and long term, unemployment in France can be reduced through continued investment in education and further training. It should also be noted that this statistic does not break these numbers down into the educational levels of the parents or their current level of employment, which would give an insight into how these distributions are affected by the students' environment. This leads to the conclusion that the unemployment market in France is becoming ever more polarized. Considering Table 7.11 and 7.15 in turn shows that unemployment is more likely among people with secondary but especially primary education as their terminal degree. The people most likely to gain employment have earned a university degree.

Table 7.25 Labour Force (educational achievement)



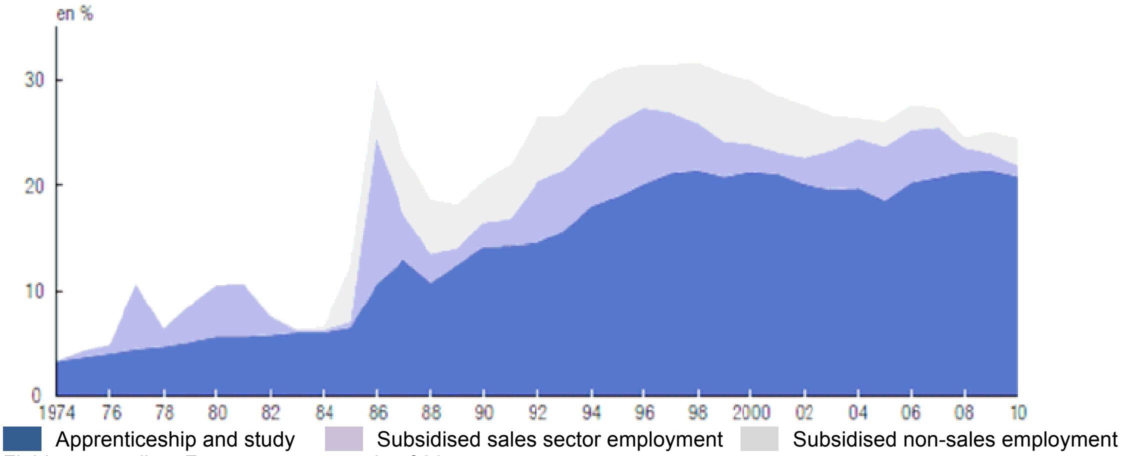
	Labour force with primary education (% of total)
	Labour force with secondary education (% of total)
	Labour force with tertiary education (% of total)

WB stat. Access 07-05-2013 (own representation)

Consequently, the French government has taken corrective measures to redress this problem in the labour market. This was done through the establishment of a number of different programmes, which used as their guiding principle “qualifier et accompagner” (Qualify and accompany, own translation) (Aeberhardt, Crusson, Pommier 2011, 153). These actions have formed part of the French government’s efforts since these trends were first discovered.

The idea of the French government was based on two principles. One solution was to increase the level of qualifications of the unemployed youth to make it easier for them to find a job. Another solution was to reduce the cost of employment of young people, increasing the incentives of firms to hire young people (see Table 7.26). It is argued that increased hiring of young people even in time limited positions would help them gain experience as well as increase their qualification, making it easier for them to find permanent employment later (Aeberhardt, Crusson, Pommier 2011). Table 7.26 shows the evolution of three different projects the government launched to get young people successfully into employment. Table 7.26 shows that there has been a marked increase in the amount of people who gained employment out of these programmes from 1985 onwards. The study and work programme (Apprentissage et Alternance) was the least successful of those programmes, however, it still managed to account for approx. 20% of young people gaining employment. The most successful programmes were the subsidised work programmes particularly in the non-sales sector, which accounted for approx. 30% of all youth employment between 1996 and 1998. Since the early 2000s the subsidised employments have lost some of their success and have gone down almost to the level of work while study programmes (with an approximate success rate of 20-25%). All three programmes can still be called a success in 2010.

Table 7.26 Percentage of places receiving funding for young people according to the category measured



Field: metropolitan France, young people of 26 years
Aeberhardt, Crusson, Pommier 2011, 154

Although unemployment remains high, all of the efforts by the French government did have a number of positive impacts on French society. As the "Portrait social 2011" confirms, in general inequalities between the different classes within France have remained largely the same between 1996 and 2009 (Direction de la Diffusion de l'Action Régionale 2011, 5).

Another positive effect of the state intervention is the high level of satisfaction that people have in life. A satisfaction survey in 2010 showed a 7 of 10, which after a deep recession in 2008 and 2009 is a number not to be ignored. Although the people out of work only show a level of satisfaction, which is at 6.1 of 10 (Direction de la Diffusion de l'Action Régionale 2011, 9), this is still a comparatively high level of satisfaction while it does demonstrate the depressing effects unemployment can have on people. Considering the persistently high levels of unemployment, this should be an important concern for the government.

The financial crisis once more underscored the importance of reducing unemployment and addressing further structural issues pointed out in this analysis as the analysis of the previous chapter, in order to bring back growth to the French economy and financial stability to the French state. Table 7.26 is an example of the French state trying to adapt to the neo-liberal environment and to the pressures exerted on it by the markets and industries. The following section analyses two ways in which the government resolved to tackle the problem.

7.4.3 Investir pour l'avenir

Once the crisis unfolded in Europe and it started to impact the French economy, the French government initially reacted in a traditional Keynesian way and in opposition to the neo-liberal concept as well as the pro-austerity argument of the German government. Nicolas Sarkozy commissioned a report by the two former prime ministers, Alain Juppé and Michel Rocard. The report, which they published was in keeping with French state tradtions, and provided a clear dirigiste argument promoting targeted medium to long-term spending by the French government in order to return to a path of sustainable economic future growth. It is the same argument that the French government has used on the European level by François Hollande since his election by pleading for more investment within Europe to foster economic growth (EurActiv.com, Reuters 2012).

The report by Juppé and Rocard (2009) was mindful of the fact that a significant increase in the general government debt could lead to higher interest rate demands by international lenders as happened with the refinancing attempts of the PIIGS (see Chapter 2). The Juppé/Rocard report understood that it needed to address this issue. Nevertheless, they argued in favour of increasing French debt in order to invest it in the French economy to help transform it into an economy for the future, capable of dealing with such crises as well as in the long run reduce the French debt. This investment in the French economy, according to Juppé and Rocard (2009), would not only bring economic benefits in the medium to long run in the form of tax income and lower government debt, but also bring social benefits to the population in the form of better healthcare making it also cheaper. Sustainable energy and sustainable transport and new industries would create most importantly more employment, as well as provide widespread benefits to the whole society. Although their plan would increase investment, these investments would have to be made under rigorous scrutiny in order to make sure none of those funds were wasted, since budgetary constraints would still have to be kept in mind.

This proposal runs directly counter to the neo-liberal economic concept and to the German argument of austerity measures by cutting down on government spending and government involvement within the economy to allow the market room to create economic growth. The Juppé/Rocard report was also a model of French dirigiste principles since it called for the state to fund industries and find ways to monitor their investment. Another dirigiste characteristic of the report was the belief that the state would be capable of "creating" growth (Juppé, Rocard 2009) which runs counter to the economic argument that neo-liberalism and industry makes (Crouch 2011).

The size of the investment (and the debt raised to finance it), which the report wanted to raise to reanimate the economy, amounted to 35 billion Euros, spread over seven axes of investment (see Table 7.27). 16 billion Euros, almost half of the available budget, was earmarked by this report to be used as funding for universities and research. The remaining 19 billion were earmarked for projects designed to stimulate the economy and create jobs by direct and indirect means. These investments also carried with them projected returns on investment through scientific breakthroughs, interest payments, or royalties (Juppé, Rocard 2009, 15). The commission led by former Prime Ministers Alain Juppé and Michel Rocard was of the opinion that strong government intervention was necessary to identify and help implement the investments effectively and to administer the returns in a way that is of the greatest benefit to all people.

> The current changes are deep and the challenges are immense. They will not be able to be faced in time without a resolute and reasoned intervention by the state (Juppé, Rocard 2009, 20) (own translation)

> These investments carry within them benefits for the rest of society. However, these "positive externalities" are not taken into account in the calculations of private investors. The state must therefore reinforce the incentives to realise these investments (Juppé, Rocard 2009, 20-21) (own translation)

Table 7.27 Juppé/Rocard Investment Plan

Action	Objective	Amount
1st axis: support university education, research and innovation		16,0 Billion Euro
1	Privilege the emergence of research excellence university campuses	10,0 Billion Euro
2	Invest in research equipment, support educational innovation and reinforce the appeal for research in France	2,0 Billion Euro
3	Create some campuses for innovation of world standing, give more value to the results from public research and support collaborative research	3,5Billion Euro
4	Support equal access to higher education and foster interest in the sciences at a young age	0,5 Billion Euro
2nd axis: support the development of innovative SME's		2,0 Billion Euro
5	Encourage the creation of innovative firms and social innovation	0,5 Billion Euro
6	Improve access to financing for innovative SME's	1,5 Billion Euro
3rd axis: accelerate the development of the living sciences		2,0 Billion Euro
7	Support innovation in the agro-biotechnologies	1,0 Billion Euro
8	Make cooperative research more dynamic in the health care sector and the life sciences	1,0 Billion Euro
4th axis: develop clean energies and efficient resource management		3,5 Billion Euro
9	Develop clean energies and the market for recycling services	1,5 Billion Euro
10	Create technological research institutes in the clean energy sector	1,0 Billion Euro
11	Prepare the nuclear technologies for tomorrow	1,0 Billion Euro
5th axis: create the city of tomorrow		4,5 Billion Euro
12	Support the development of sustainable cities	2,5 Billion Euro
13	Accelerate the thermal renovation of social housing	2,0 Billion Euro
6th axis: invent the mobility of the future		3,0 Billion Euro
14	Prepare the vehicles of the future	1,0 Billion Euro
15	Develop tomorrow's aeronautical and space industry	2,0 Billion Euro
7th axis: invest in the digital society		4,0 Billion Euro
16	Accelerate the installation of high-speed internet in France	2,0 Billion Euro
17	Develop the use and innovative digital contents	2,0 Billion Euro
Total		35,0 Billion Euro

(Rapport Juppé, Rocard 2009, 16)

The first axis of this report is dedicated to the support of higher education. A vibrant, well-funded higher education system and research environment is essential to attract businesses to France (Juppé, Rocard 2009). High valued research and education provides a ready pool of knowledge and innovative thinking to firms without having to import it from somewhere else. A high number of research institutes and higher education facilities with high reputations thus have a positive effect on the business climate in a country.

This axis aims to invest in research campuses and equipment on the one hand by creating high-class research institutes in France but also by attracting high-class researchers to France. It also attempts to motivate the younger generation of Frenchmen (and especially women) to get into the hard sciences (Rapport Juppé, Rocard 2009, 30). The benefits of these investments would be long term and socio-economic. They would provide a more widely educated workforce and help make France more attractive for companies; by improving the French business climate through their ready access to knowledge and innovative research.

The second axis is dedicated to the support of SME's. The second axis aims at helping people to start up their own small businesses. The report wants to help fund those businesses because traditionally SME's have a high failure rate. Due to the financial crisis, the banks no longer want to shoulder the risk of financing a potentially losing business; thus the government needs to step in to take over that role (Juppé, Rocard 2009).

The returns on such investments are not limited to socio-economic benefits, such as reduced unemployment and increased economic growth. Such investments would also include financial benefits, such as dividends and increased tax incomes in their various forms. These returns would help reduce the financial burden on the state since the investment in small businesses would create employment and stimulate consumption. All of these things provide positive effects on government finances, allowing the state to pay down its debt and finance social security and other national and international commitments more quickly.

The third axis aims at supporting research into biotechnologies. The report sees advances in biotechnologies as well as advances in healthcare as crucial in the development of sustainable economies. The benefits this funding would provide to France and French society are financial, economic and social. Just as for the SME funding, the revenues from the credit provided and from the licences that that research generates as well as the return of the money borrowed would create increased revenue for the state (Juppé, Rocard 2009). Advances in biotechnologies may also create health care benefits, making healthcare cheaper by improving preventative care or potentially developing cures for chronic or wasting diseases, which would help reduce the current healthcare spending.

The fourth axis is aimed at funding sustainable energies (Juppé, Rocard 2009, 35). The report argues that significant investments in this growth market would be a good investment for France. It would allow France to move itself into a global leadership position in the sustainable development market. It would additionally create new industries, thus contribute to the French GDP, and help reduce unemployment. It would also create further revenues for the state through profit participation and interest payments as in the previous funding proposals (Juppé, Rocard 2009, 98). It would also reduce carbon emissions and the negative effects they produce (Juppé, Rocard 2009, 101).

The fifth axis follows the same ecological line of thinking as the axes 3 and 4. However, it focuses on the city. The development of more ecological cities would increase the health of its inhabitants as well as create energy and other resource savings making France more energy independent. This investment would also create jobs and stimulate growth (Juppé, Rocard 2009).

The sixth axis focuses on the automotive industry. This report argues the state should invest with a particular focus on the development of newer engines and eco-friendly transport mechanisms (Juppé, Rocard 2009, 39). This investment would have many economic benefits over and above the initial investment; it would help establish new industries within which French industries would have competitive advantages that would create new jobs in the long-run (Juppé, Rocard 2009).

The seventh and final axis of the report focuses on investments in information technology especially on high-speed Internet, which were made a priority in previous reports by the Commission for Growth. Coverage of the entire country with high-speed Internet is an essential part of a well-functioning modern economy. This is more emphatically the case as there are many avenues of growth for firms with access to high speed connections including the development for services especially designed for the internet, which have tremendous growth potential (Juppé, Rocard 2009, 128).

The way this report suggests to achieve these investments, without overly increasing the borrowing or the public deficit, is through a redressing of the public finances in the long run and a shift of the financing methods away from borrowing to a different allocation of state funds, which would not increase the deficit (Juppé, Rocard 2009 22).

Juppé and Rocard argue that if correctly applied, all of these axes of growth provide a sensible and logical long-term investment and growth strategy. The development of this investment strategy demands a significant and close involvement of the state within the economy and the sectors within which it invests in, in particular.

The Juppé/Rocard report goes directly against the neo-liberal economic concept. By reinforcing instead of reducing the duties of the state, by accepting shorterm increases in debt for in many cases potential returns and in dealing with the “necessity” for rebalancing the budget in a longer timeframe than the Attali Report and a much longer timeframe than the German state would. It also deals in a longer timeframe than neo-liberal economics whose aim is to reduce time between results as much as possible. The Juppé/Rocard report provided an alternative to the German austerity concept. The report not only argued for targeted spending in a dirigiste fashion, but it also argued that the focus of any reductions in state expenses, should only fall on spending which *does not impact on the future ability of the French state to develop its industry* and a sustainable method of economic development (Juppé, Rocard 2009, 23). This report was an attempt at reversing the neo-liberal momentum and an attempt at returning to a state-led management of the economy. However, considering the institutionalised power of neo-liberalism in Europe and the global reach of the concepts as well as the industry's promotion of those neo-liberal concepts, the Juppé Rocard (2009) report was doomed to failure. Not because it was a bad report with bad ideas, but because of the overwhelming power of the neo-liberal concept and its widespread embrace.

7.4.4 The Plan to Balance the French Public Finances

After the initial spending push undertaken after the beginning of the crisis in 2008 the French government reversed its spending policy by 2011 (AFP 2011a) since the French economic growth remained slow and its debts kept rising (see Table 7.19). Once the PIIGS countries began to have trouble refinancing their debts on the international financial markets and currency speculations about the end of the Euro became more widespread, the French government began aligning itself with the German position of austerity to avoid any such problems of debt refinancing. The EFSF and the ESM were established to ward off any such attacks in the future and was provided with enough capital to do so. Since the German economy was the strongest in Europe and the biggest contributor to the EFSF and the ESM the German government was able to influence its setup in pushing for austerity conditions to be inserted in a rescue scenario for a country. The financing of the EFSF and the ESM and the prevailing German narrative about the necessity for austerity, made it necessary for France to introduce actual cuts in spending. In 2011, the French Prime Minister François Fillon published plans to bring the deficit back under control and reduce the French public debt (AFP 2011a) thereby embarking France on the road to austerity.

Table 7.28 Comparison of the 24th August and 7th November plans

Effort in billions of Euros	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**Saved debt**	**% of expenses 2016**
Announcement of the 24th of august	**1,2**	**10,4**	**9,9**	**9,4**	**8,7**	**8,7**	**48,4**	**11%**
Announcement of the 7th November	**0,0**	**7,0**	**11.6**	**13,3**	**15,3**	**17,4**	**64,7**	**52%**

(Copy of table Comparison des plans du 24 août et du 7 novembre)
Rapport Fillon in AFP 2011, source government, published in: La Liberation.

Table 7.28 shows two different plans of attack to reduce the French deficit. The August plans had more immediate effects but spread the spending cuts more or less equally over five years. The November plans delayed the bulk of the spending cuts until 2013, but the cuts would be deeper and the savings greater.

First, the government gave priority to its efforts of deficit reduction and built on those efforts that it had already taken. Second, it would expand these measures of debt reduction by increasing savings and by spreading those savings as equally as possible over five years, from 2011-2016. The Rapport Fillon (AFP 2011a) spread the government's saving's efforts among eight areas of government spending. The first area where spending would be cut was government expenditure. The savings achieved here aimed to bring the annual public deficit back to 0 by 2016. These savings would be achieved through a freeze in public spending except pensions and public debt as well as a reduction of tax exemptions and loopholes (AFP 2011a).

Table 7.29 Projected savings over time period 2011-2016

Measures in billion euro	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**	**Avoided debt in 2016**
Effort in expenditures tied to planned reforms	10,6	21,9	31,4	40,4	50,8	64,5	219,7
Measures announced the 7th November to curb spending	0,0	1,8	3,7	6,0	7,4	9,0	28,0
Total spending	**10,6**	**23,7**	**35,2**	**46,5**	**58,2**	**73,6**	**247,7**
Efforts in income tied to planned reforms	11,4	22,4	21,9	21,4	20,7	20,7	118,6
Programmed closure of loopholes	0,0	0,0	3,0	6,0	9,0	12,0	30,0
Measures announced the 7th November to increase income	0,0	5,2	7,9	7,3	7,9	8,4	36,7
Total income	**11,4**	**27,6**	**32,8**	**34,7**	**37,6**	**41,2**	**185,3**
Total of savings through measures proposed on the 7th November	**0,0**	**7,0**	**11,6**	**13,3**	**15,3**	**17,4**	**64,7**
Overall total	**22,0**	**51,3**	**68,0**	**81,2**	**95,8**	**112,7**	**433,1**

Rapport Fillon in AFP 2011 source government published in: La Liberation.

The second area of focus concentrated on further efforts by the state to accelerate the reforms of the pension system, which was introduced by the Sarkozy government in 2010. This report wanted to bring forward the implementation of the reform by one year, which would help the government reduce its expenditures since these reforms would (among other things) extend the year of the retirement age from 60-62 years and the extension of the time people have to pay contributions into the system before they can receive their full pension benefits (AFP 2011a).

The third effort was a freeze of the salaries of the members of the Government and the President (AFP 2011a), in addition to the planned salary freeze of the remaining French public employees. This top-level pay freeze was coupled with a call to the managers at top firms in France to follow that example. This effort at deficit reduction would not bring many savings by itself, but it did provide an opportunity to the French cabinet members to lead by example. It should also have made potential future measures more palatable to the population since this move demonstrated to the population that this belt tightening would not be a one-sided affair. This saving's focus would also reduce the funding for political campaigns the state provides to political parties by 5% (AFP 2011a).

The fourth effort was a delay and a reduction of the revaluation of social payments the French state makes to people. This delay and reduction of social payments would create long-term savings of approx. 0.9 billion Euros between 2012 and 2013. However, the revaluations would not impact programs such as retirement payments RSA payments or other exceptional payments, which the government has committed itself to (AFP 2011a).

The fifth effort was a tax increase on the profits of big enterprises. This tax increase would see the enterprise tax rate rise from 33.33% to 38.33% for the near future. This action was expected to earn the government 1.1 billion Euros between 2012-2013. The taxes for SME's would remain the same (AFP 2011a). The sixth effort was a VAT increase to the lowest VAT bracket and will increase that level from 5.5% to 7%. This VAT bracket applies to goods such as books and restaurant-prepared food. This move should have netted the state a further 1.8 billion Euros in increased revenue per year (AFP 2011a).

The sixth effort at debt reduction was another tax increase. This tax increase would be achieved by stopping the indexation of the salary that corresponds to a certain tax bracket (AFP 2011a). The indexation of the salary is done to keep account of inflation. Freezing it to the level of the previous year means that people will have to pay more in taxes since the change in inflation for the New Year is not taken into account (LeParticulier 2013). This is an indirect way of raising taxes, which will raise 1.7 billion Euros in 2012. The final effort of deficit reduction, which the Prime Minister's proposal outlined, consisted of another tax increase. This increase would focus on taxes, which are levied on interest and dividends. The Report wanted to increase that tax level from 19% to 24%. This tax increase should have netted the government another 0.6 billion Euros a year.

The plans proposed by the Commission for Growth and the Juppé-Rocard Commission tackle the structural problems of the French economy and did so in a balanced way by finding inefficiencies in the budget and reducing them but at the same time also using spending to support economic growth which would provide increased income to the state in the medium to long run instead of just proposing tax increases and cost-cutting measures without any real plan for economic development. The debt reduction plan put forward by François Fillon is in my view a one-sided, short to medium term solution to reduce the levels of French debt. The measures proposed in this plan are easy and quick solutions to a larger structural issue, which this report does not address.

The Fillon plan (AFP 2011a) is a clear indication that the Sarkozy government was ready to implement austerity measures. As the Fillon plan also showed, the French government was not going to go down the same road of structural reforms than Germany did in 1998 since it did not change anything in its social payment procedures. The Fillon plan suggests to me that the French government is unable to move past its own state traditions and conceive of the French state as anything other than the central governing nexus of the French political economy. Any move of the French state towards neo-liberal economics will likely always be tempered by *dirigisme*.

The Fillon plan attempted to balance the budget through increased taxes and reduced spending. The increase of the various tax rates, particularly the income tax rates for businesses, would have more than likely stifled growth and economic balance instead of fostering it. This plan, to function correctly would also require a robust level of growth. As Chapter 8 will demonstrate, the projected economic growth in France is very low; in addition, France will not meet its deadline to bring its budget in line with SSM rules for the second time after it was extended from 2013 to 2015 (dpa, AFP, sdo 2014, LeMaître 2011).

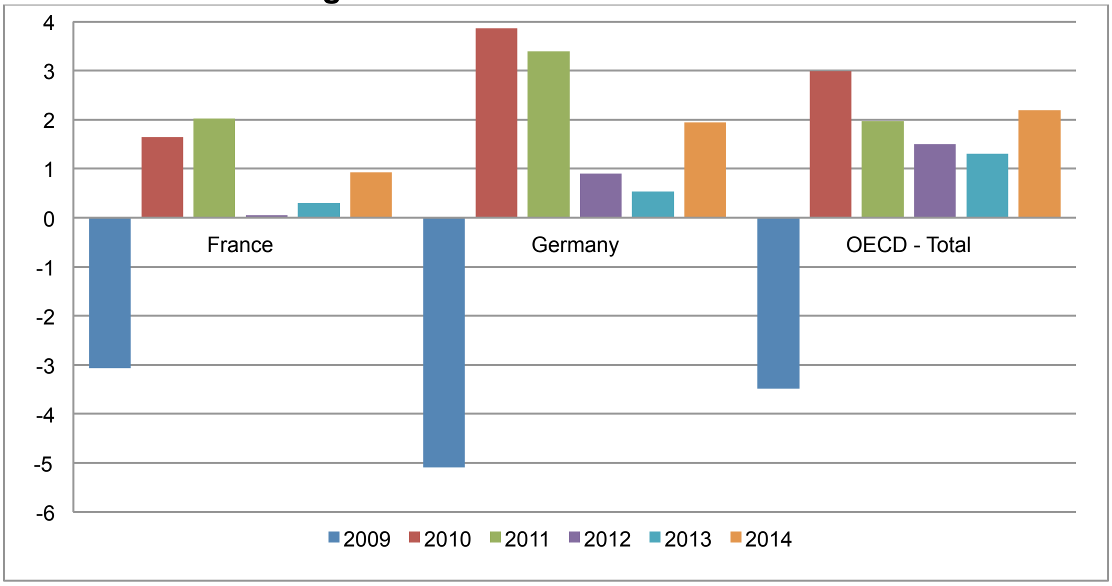
7.4.5 The first reforms of Hollande

François Hollande has attempted to position himself as the standard bearer for the anti-austerity faction within the EU. However, his political and personal failures more than his economic ones have contributed to his failure in that respect. This thesis will focus on the reforms proposed by the Hollande administration related to the political-economic development of the French economy (Thillaye 2013).

The reforms introduced by the Hollande government were socialist in nature, beginning with once again reducing the retirement age from 62 to 60 years. The French government also increased income tax particularly on the rich and raised the minimum wage (Thillaye 2013).

Whereas for Germany the way led through an austerity restructuring of the workforce, empowering its industry, the French government decided once more to take the route of investment in industry to spur on reindustrialization and production, an attempt, which is similar to the points raised by the Juppé-Rocard report previously analysed. The differences, however, are that the French government also included to a number of labour market reforms. The government established a 20 billion Euro fund to reduce employer contributions to make hiring more attractive in France. The government also simplified hiring and firing procedures including making working contracts more flexible to allow companies to adapt to changes within the economy (Thillaye 2013). All of these reforms, however, did not have the desired effect on the French economy, which has continued to decline in the international arena. Table 7.30 shows significantly lower levels of growth that France has to contend with as compared to other countries like Germany. This slow growth requires decisive action, which so far has been lacking from the French government.

Table 7.30 Real GDP growth



OECD (2014c) (own representation)

7.5 Conclusion

This chapter has attempted to provide an overview of the economic performance and the social evolutions, which affected the economy since the end of WW2. It looked at indices of healthcare, unemployment, education and industrial performance (in the form of GDP evolution).

The chapter demonstrated that disparities in wealth between rich and poor have remained steady for much of the last two decades. Even in the aftermath of the 2007/2008 financial crisis, differences in wealth have remained steady at their historical disparity levels, except for the top 1%, most especially for the top 0.1% and 0.01%. Those incomes have seen a significant increase over the last four years.

The French economy has many strengths; France has a diversified economy and many production sectors, it has a growing and well-educated labour force and strong internal consumption. The Commission for French growth in its report also points out that France still has a positive demography, providing it with a generational stability leaving it with a “less“ burdened pension system than Germany for example. It was these benefits that allowed it to maintain relative independence and allowed it to weather the crisis relatively unscathed.

However, France also faces major challenges, which it needs to address urgently. As was demonstrated in this chapter, the French attempt at spending its way out of recession did not produce results quickly enough for the global neo-liberal economic concept and caused increased stresses on the national budget at a time when the debt refinancing had become ever more expensive and difficult for countries with large deficits. The low economic growth and high unemployment figures investigated in this chapter do show a struggling French economy. As will be analysed in Chapter 8, French economic power has declined compared to Germany which despite 2010-2012 being a time of crisis has managed to deliver a comparatively strong showing compared to France. This was one of the contributing factors of the greater influence Germany was able to wield in the ESM and EFSF and Euro rescue deals. The single biggest problem France faces is its continuously decreasing competitiveness on the global markets. This decrease is due, among other points, to its high labour costs (see Table 7.23) and high levels of taxation on businesses and an inflexible economy. High levels of unemployment, especially for young professionals and resulting from a depressed economic outlook, is a situation the French state and the French economy have to currently contend with.

Other reforms proposed by the Commission for French Growth included efforts at further liberalisation of the economy and gains in efficiency within public as well as private institutions. These reforms were an attempt not necessarily to end the dirigiste method of state intervention within the political economy of France but to adapt that style of political economic governance to modern circumstances of global trade and European integration.

The Report published by the Juppé/Rocard Commission provided a good example of a plan for a modern dirigiste state. The plan tried to deal with the long-term challenges for the economy by providing a line of economic growth and potential economic outlays for the short and medium term issues to free market forces. Allowing the directions to develop and evolve freely and only intervene in a longer term, very much like the principle of Adam Smith's "invisible hand". Had the French government followed this report more closely, France might have adapted to the crisis on its own terms as well as take a leading role in shaping them in Europe in the medium term.

The strategy of government spending, which the government had started in 2009, to stimulate the economy was a successful way to shore up domestic spending. However, the investments that the government provided were stopped after 2011, leaving consumption free to decrease again. The labour costs and labour regulations were left unchanged, meaning that French industries could not fully capitalise on the investments that were provided for them. In 2011, France joined the course of Germany's crisis management strategy, which focussed particularly on austerity. The problem of the increasing French deficit was taken much more seriously, especially in terms of its abilities to continue to finance its social programs at the level it has done up to now.

In 2011, in accordance with the French government's new policy priorities, the French Prime minister François Fillon presented his plan to implement the austerity measures France would undertake to reduce its deficit. These plans involved few austerity measures in the way they were undertaken in Germany or in the way it is proposed for Euro Zone countries in financial difficulties. The plans in part even moved against the Report by Juppé and Rocard, by increasing taxes on corporations, as well as closing down tax rebates and loopholes. The increase in the lower rate of VAT was also a blow to the French economy as it increased the prices in the service and tourism industry including restaurants, which is a large sector of the economy in France. The plan by Fillon (2011) also included spending cuts on social programmes and a freeze of government member pay as well as an increase in the speed of the retirement reforms. The spending reductions outlined in this plan assuming at the time that the economy would develop in the way the French government expected it to, were designed to increase year on year to have eliminated annual budget deficits by 2016 and set France on a path to pay off its deficit over the long term.

The election of François Hollande changed the French government's policy priorities once again away from austerity towards a balanced approach to deficit reductions. While the Hollande government attempted to introduce a number of reforms which where in accordance with the liberal principles, it also pandered to its left flank spending large sums of money. These expenditures increasing the French deficit without similar response by the French economy.

While the result of the spending policy of the Hollande government did not yield the results that were expected, the principle with which they were implemented is sound. The answer to France's debt problem is to take the long-term view. Using the logic of the Report by Juppé and Rocard, one solution would be to increase spending in a targeted way and ensure that there is as little waste as possible. At the same time, the effectiveness of other government expenditures should be determined and that spending cut which does not help the people or the government. The investments were designed to revitalise the economy and create jobs if not in the short run, at least in the medium and long run. Once unemployment goes down, social programmes to help those that are unemployed will automatically require fewer funds thus increasing the savings of the state. The additional taxes paid by the people returning to work will also help reduce the deficit. As this is a long-term project, the government in these reforms requires patience and steadfastness.

The proposals that were put forward by French governments over time all have in my view solid concepts to reform part or all of the French socio-political system according to a dirigiste view of economic management. However, considering that these efforts for reform are being implemented within a global neo-liberal economic environment, their implementation will not have the time necessary to develop its positions and actions quickly enough to achieve results which an austerity focussed reform package could and which a neo-liberal economic framework expects. This is one explanation why the French government, after attempting a dirigiste solution to quickly follow up with another neo-liberal solution, and why now, the Hollande government is attempting to implement another combined dirigiste method with more neo-liberal concepts integrated.

Having now considered the German and French economic standing the next chapter will assess the economic performance of Germany and France together. This is done to make a more precise determination of the divergent economic growth patterns as well as to investigate how both countries can find a way to work together. As this chapter will show, their economic development is not as far apart as one might think, and Germany’s power is not yet as great as to wholly disregard the misgivings of France when it comes to austerity policies.

Chapter 8 Austerity and Spending: combined approaches towards a new European Future

8.1 Introduction

The socio-political-economic analysis of France and Germany, completed in Chapters 4-7 of this thesis, revealed many differences and similarities between the two countries. It is the objective of this final substantive chapter to investigate if there remains any ideological or economic overlap between those two countries and determine if a common position can be synthesised. To this end, this chapter draws upon the research conducted throughout this thesis in order to determine if the distinct national state traditions and economic concepts, upon which the French and German economies are based, still allow for a common understanding and common solutions to the problems created by the 2007/2008 financial crisis.

This chapter also assesses comparatively, if the liberalisation of industries and labour markets undertaken by the German and French governments had positive or negative political economic impacts, before considering if these reforms have changed the welfare position as this thesis argued in Chapter 2.

In order to determine the relative political-economic standing of Germany and France in relation to each other and in relation to the Euro Zone, a comparison of the economic performance of both economies will be undertaken. This is done to view how the political-economic balance between both countries has changed and analyse what kind of common policies can be distilled from their actions that could be used to tackle the fallout of the crisis in both countries and beyond.

The structure of the chapter is as follows. First, this chapter compares the social and economic differences of the German and French governments focussing on German and French state traditions as well as the constitutional framework of both countries. This thesis in its analysis investigated the last three decades to determine if there have been any kinds of similarities within the approaches or conceptions of both governments regarding social welfare. This analysis has taken into account different time periods in its analysis of the French and the German cases. The different time frames were used to demonstrate the evolution of the thought of social welfare. In Germany, the evolution of a different conception of social welfare started in 1998 with the arrival of the SPD. In France, it started in 1981 with the arrival of François Mitterrand and his social and labour reforms, which reinforced the previously existing conceptions of social care. Mitterrand's Presidency reinforced them to such an extent that they were kept in place all throughout the 1990s and 2000s. This section shows that, although the parties and their actions are separated by space and time, their actions have resulted in a convergence of incomes and inequalities to similar levels. This section also shows that the German and French actions over those thrity years have come to a tipping point for different reasons. As will be demonstrated, the French system has reached its limit in providing equality and is actually now worsening the level of inequality in some areas. The German level of inequality, while having improved over the years has now levelled off. Considering the economic situation Europe finds itself in, the reduction of inequality does not look to be improved further.

The second part of this chapter looks at how these conclusions have impacted the economic performance of both countries. It examines how these countries have fared in terms of their economic performance and the evolution of welfare requirements within the country; this is done using international unemployment and economic performance statistics. This shows, on a general scale, as opposed to the more detailed analysis in Chapters 5 and 7, the economic evolution of both countries and its social repercussions.

The third part of this chapter investigates the recent efforts and actions undertaken by France and Germany in their fight against the economic crisis in Europe. This section gives a particular focus to the events happening throughout 2013 and 2014, which are the most recent and most telling actions by both governments in their fight against the crisis and have not been analysed by this thesis so far. It is during that time that major changes in the economies as well as the relationship between Germany and France have occurred, which has significant bearing on the analysis that has been conducted in this thesis. Finally, this chapter will consider a possible synthesis of the German and French spending and austerity positions. This synthesis will base itself on the common arguments that were used throughout 2014 in favour of more investment and less austerity to establish future policies and actions within the Euro Zone to deal with a stagnant economy due to the 2007/2008 economic crisis.

8.2 Consequences of German and French political economic concepts

The economic concepts, which the German and French governments used, differed ideologically from each other. Those differences stem from a number of state traditions, some being more modern than others. The effects they had on the political economy of France and Germany were also different for either country. This section investigates the political economic consequences of the ideological decisions taken by the German and French governments to either intervene or not intervene in the market and social affairs of their countries.

8.2.1 State traditions and their historical differences

Germany and France have had different state traditions for many generations. While they once shared concepts of the state, the German and French concepts have since diverged. However, that divergence was not that great as to prevent them from cooperating with one another on a variety of issues.

The French concepts of the state were inspired by Latin specifically Roman concepts of the state as a tool for the submission of society. This was combined with other theories of the state as a social entity, creating the state as a part of society. The French concept also included Catholic concepts of submission onto a higher authority and generosity towards others. This was a particular attraction to communists, which were a very strong force within France throughout its modern history. Their power extended so far in France that they even had a significant hand in helping craft social security and welfare legislation (Dyson 2009).

The German concepts of the state were inspired by Greek concepts of individualism and knowledge collection. This was combined with other theories of state to create a self-limiting state, which allowed individuals to find their own path to self-fulfilment. One way the state did that was by allowing people to try new concepts and to learn from them. The German state traditions are also very much influenced by Protestantism which further reinforces the individualistic nature of people as well as reinforcing a notion of respect for the law above all else (Dyson 2009).

8.2.2 German action and French inaction: the constitutional reason

The ability of a government to reform the state or to redefine the rights and duties of the state always begins with the constitutional provisions, which define the Government's scope of action. Chapter 4 and Chapter 6 investigated the constitutional definitions of the French and German states and the flexibility that the national constitutions provide both countries to re-interpret their duties as a state. The investigation of the constitutional provisions demonstrated that Germany's constitution explicitly allowed for a redefinition of welfare provisions, and a redefinition of the state's responsibility to provide them, according to the economic situation in Germany. The German constitutional provisions do not specifically require there to be any social security, rather the provisions allow for the implementation of social security laws. Therefore, the definition of what constitutes the provision of care is defined by the SGB, which contains twelve parts regulating in detail each aspect of social welfare (Bundesministerium der Justiz und für Verbraucherschutz1949, Lampert 1992).

The French constitution contained a number of provisions, creating a legal framework that would not allow such latitude of movement. The French constitution contains two sections within the constitution as well as different sections within the preamble (which has constitutional validity), which frame social security entitlements. In addition to that, the Preamble also includes five points framing the rights of the workers within French society (Carcassonne 2011).

The differences between the constitutional frameworks of France and Germany explain how France has reached a level of political stasis, which has made it very difficult for its government to enact any kind of social reform. While the French stasis among the different social partners has prevailed for the last 30 years, this stasis is now considered to be (and has started to become) a significant burden for the French economy and by now its society as well. Germany on the other hand was able (albeit with a certain amount of luck and cunning) to implement wide-ranging reforms of its economy and its labour market. The results the German actions achieved, in terms both of the economic push it has given Germany as well as the ability to weather the global economic storm, cannot be denied.

8.2.3 The consequences of "Fördern und Fordern" and "Traitement Social du chômage"

Out of the state traditions and the frameworks of the German and French constitutions, different social concepts would develop and be developed and framed in accordance with the party in power within the respective country. The timeframe analysed in this thesis considers the concepts developed by the German and French socialists respectively, consisting of the German concept of "Fördern und Fordern" and the French concept of "Traitement Social du chômage". Both these concepts yielded different political-economic results, as the tables of this section will show.

Table 8.1 is the first indicator, which demonstrated increased income inequality in France compared to Germany. Table 8.1 shows three things. In the first column one can distinguish that income has increased more on average in France and in Germany than within the other OECD member countries. The second and third columns show upon which section of the population i.e. the bottom 10% or the top 10% this increase has had the greatest impact. Table 8.1 shows that the income discrepancy over the years from 2007 and 2011 the income discrepancies have increased significantly within France as compared to Germany where the differences have remained steady. This shows a rapid increase of the level of inequality within France while the inequality in Germany has remained steady over the same period if one considers the data in Table 8.2.

Table 8.2 show that throughout the 1980s and the late 2000s, inequality in France has remained virtually unchanged though favouring the bottom decile whose income increase was 0.3% higher (own calculation) than the top decile. In Germany, these discrepancies have increased by a much higher factor. This is a first example of the decreasing power of the French state in its ability to maintain its economy and its social equality in balance. This is a point, which shall be revisited in short order.

Table 8.1 Poorer households tended to lose more or gain less

Annual percentage changes in household disposable income between 2007 and 2011, by income group

	Total population	Bottom decile	Top decile
France	0,3%	-1,3%	1,7%
Germany	0,4%	0,8%	0,8%
OECD 33	**-0,53%**	**-1,67%**	**-0,78%**

Notes: Data for 2008 refer to France, Germany, There is a break in the series in 2011 for the United Kingdom, and results are not strictly comparable. 2011 data for Ireland and the United Kingdom are provisional. OECD-30 average excludes Hungary, Mexico, Switzerland and Turkey.
Extract from Figure 3. Poorer households tended to lose more or gain less
Source: OECD 2014 a

Table 8.2 Household income increased faster at the top

Trends in real household income-by-income group, mid-1980s to late 2000s
Average annual change, in percentages

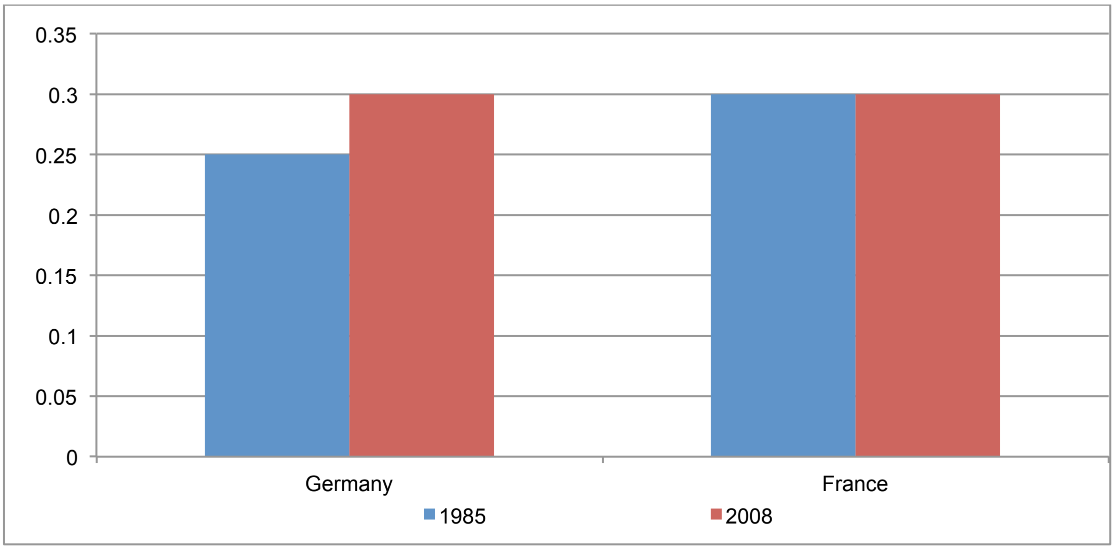
	Total population	Bottom decile	Top decile
France	1,2	1,6	1,3
Germany	0,9	0,1	1,6
OECD 27	**1,7**	**1,3**	**1,9**

Note: Income refers to disposable household income, corrected for household size and deflated by the consumer price index (CPI). Average annual charges are calculated over the period from 1985 to 2008, with a number of exceptions: 1983 was the earliest year for Austria, Belgium, and Sweden; 1984 for France, Italy, Mexico, Turkey; 1986 for Finland, Luxembourg, and Norway; 1987 for Ireland; 1988 for Greece; 1991 for Hungary; 1992 for the Czech Republic; 1995 for Australia and Portugal; and 1996 for Chile. The latest year for Chile was 2009; for Denmark, Hungary and Turkey it was 2007; and for Japan 2006. Changes exclude the 2000 to 2004 for Austria, Belgium, Ireland, Portugal and Spain for which surveys were not comparable
Source: OECD Database on Household Income Distribution and Poverty.
StatLink http://dx.doi.org/10.1787/888932537370
OECD 2011 Extract from table 1 Household increased faster at the top from Divided we stand: Why Equality Keeps on Rising p. 23.

Table 8.4 further underscores the changing pace of the differences between France and Germany. As Table 8.3 has shown, while the levels of income inequality in France have remained largely the same, they have significantly increased in Germany. Both countries in 2008 had approximately the same level of income inequality within their countries. The increase in German income inequality of approximately 5% could be considered another example of the countries polarisation of the workforce due to the Hartz laws expansion of the low-income segment during the years of 1995-2008, the Hartz laws only being in effect since the early 2000s.

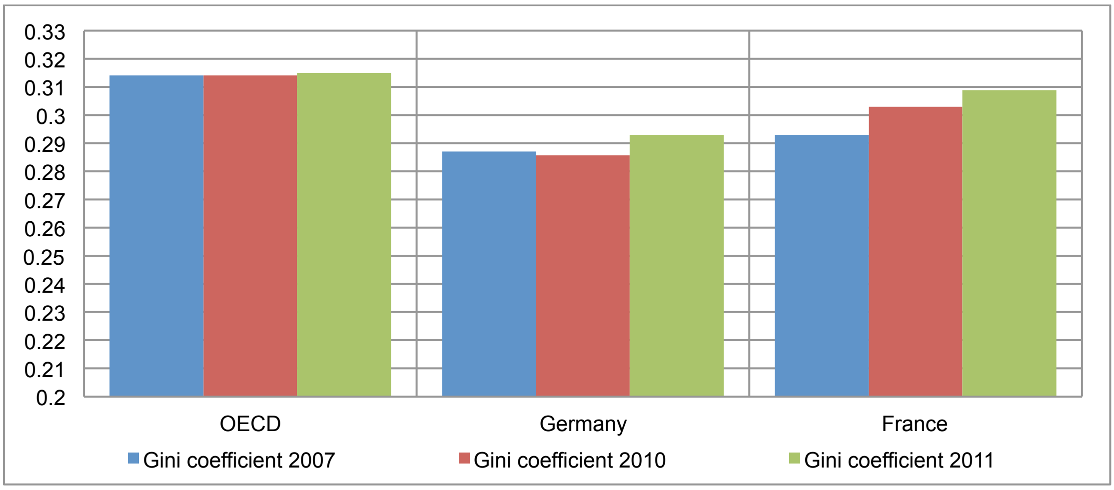
However, after 2007-2008 and the financial crisis had become an acute problem in Germany and in France, as would its aftermath, the ability of either country to redistribute its income inequality has shifted. There was a marked slowdown within the increase in income inequality in Germany (as already evidenced within Table 8.1) and a slight increase in income inequality in France (whose reason could stem from the increased levels of unemployment analysed within the previous chapter), making them approximately equal within their level of income inequality. This is also further evidence of the strain both these systems are under due to the economic crisis caused by the 2007/2008 financial crisis, as neither country is making much progress in reducing income inequalities. Evidenced for this is indicated by the by the steady level of income inequality within the OECD member countries (Table 8.4).

Table 8.3 GINI Coefficient evolution 1



Soucre: OECD Database on Household Income Distribution and Poverty.
Statlink http://dx.doi.org/10.1787/888932535185
OECD 2011, Copy of Figure 1: Income inequality increased in most, but not all OECD countries (Gini coefficients of income inequality, mid-1980s and late 2000s) in Divided we stand: Why Inequality Keeps on Rising, p 24

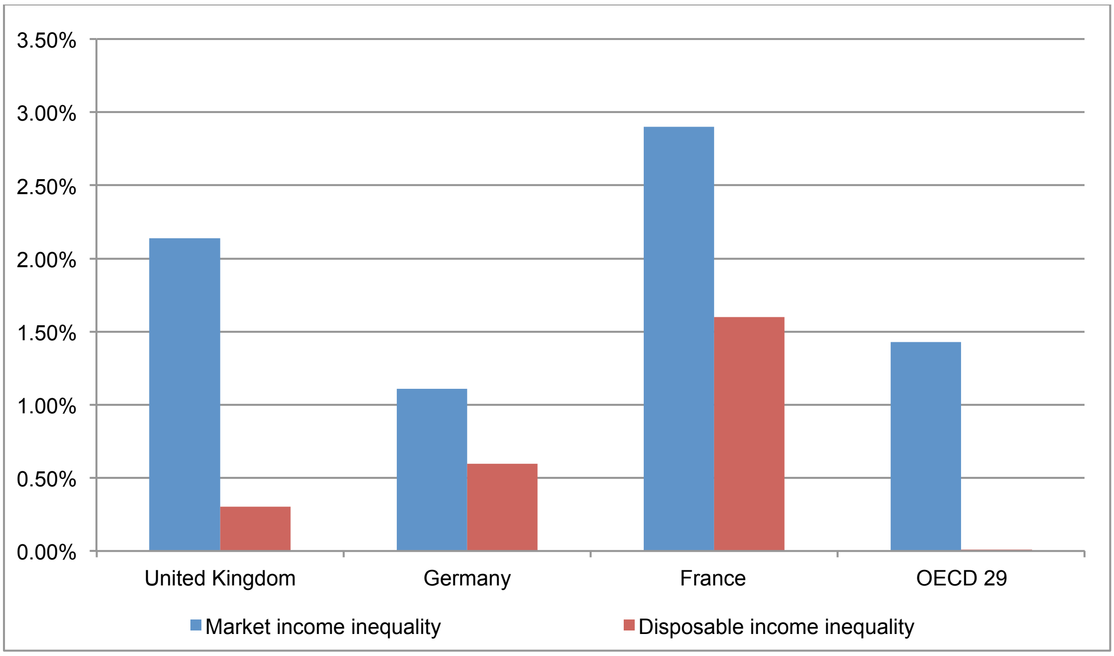
Table 8.4 GINI Coefficient evolution 2



Notes: Data shown for; 2008 for France, Germany,. The OECD average for 2007 includes 2009 data for Switzerland. The OECD average for 2011 includes 2009 data for Japan and 2010 data for Belgium.
Income distribution data refers to the total population and are based on equalised household disposable income, i.e. disposable income adjusted for household size. The Gini coefficient takes values between 0 for a perfectly equal income distribution where every person has the same income, and 1, which refers to a situation of maximum inequality where all income goes to one person. TheS90/S10 income share ratio refers to the ratio of average income of the top 10% to the average income of the bottom 10% of the income distribution. Working poor are those living in households with a working age head and at least one worker with income below the poverty line.
Source: Source: OECD 2014a

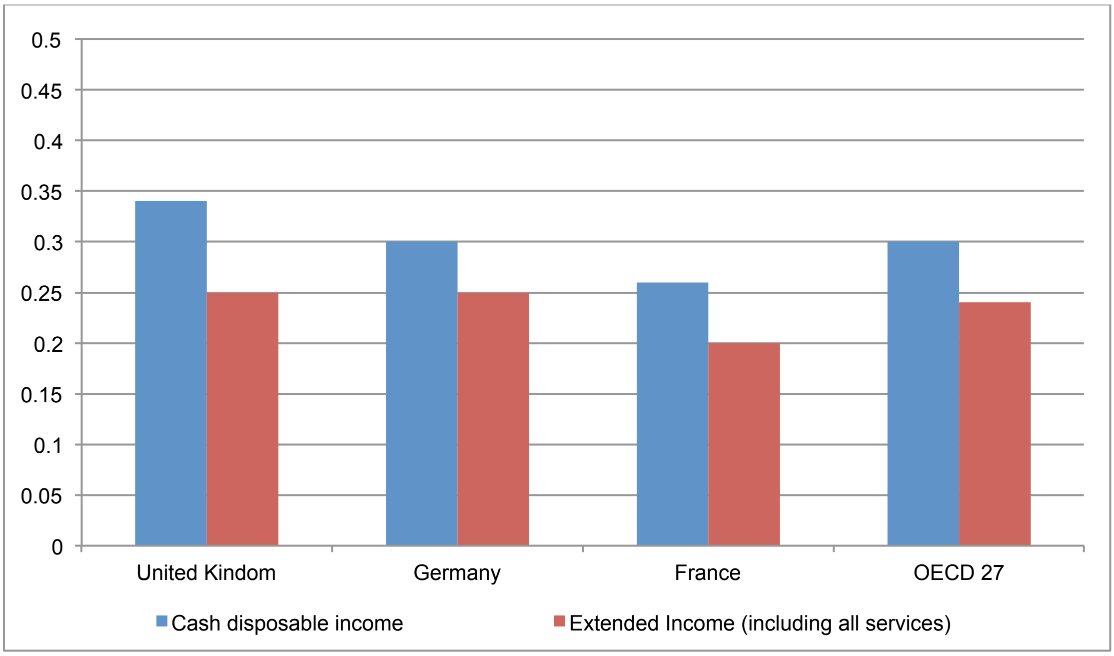
Table 8.5 Market income inequality

Percentage point changes in the Gini coefficient of household market and disposable incomes between 2007 and 2011



Notes: Data for 2008 refer to France, Germany, There is a break in the series in 2011 for the United Kingdom, and results are not strictly comparable. 2011 data for Ireland and the United Kingdom are provisional. OECD-30 average excludes Hungary, Mexico, Switzerland and Turkey.
Extract from Figure 1. Market income inequality rose considerably
Source: OECD 2014a

Table 8.6 Benefit Redistribution

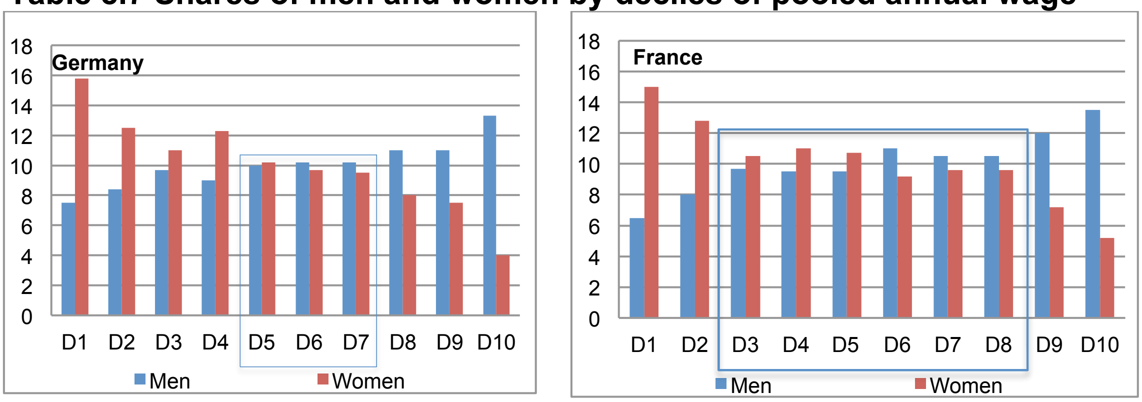


OECD 2011, 39 Copy of Figure 11. In-kind benefits from public services are redistributive in all OECD countries (Household income inequality Gini coefficients before and after accounting for services from education, health, social housing and care services, 2007) Divided we stand: Why Equality Keeps on Rising, 39

The manner in which incomes are redistributed is shown in Tables 8.5 and 8.6. These tables show the ability of the state to equalise incomes. Table 8.5 shows the differences in gross income (market income) within countries in red and the disposable income (net income) in blue. Table 8.5 how taxation (social payments included) manages to reduce the income inequalities within (for our example) Germany and France. Table 8.6 shows the same with the gross income in blue and the disposable income level in the red bar, however, focussed on the redistributive effects of social services only. The total income redistribution and the welfare redistribution show that the German government and the French government are able to reduce income inequality through taxation and social provisions. However, previous tables (8.1-8.4) demonstrate that France's ability to reduce inequality, and redistribute wealth, although greater than Germany's, are being severely tested.

This is especially true considering the lacklustre economic growth in France as well as in Germany (although less so), which is shown in Table 8.9. Looking further at Table 8.8 one can see that from the end of 2012 until the beginning of 2014 economic confidence returned to the EZ as well as the EU: however, that returned confidence did not translate into higher growth within either the German or the French economy. Considering that Table 8.9 shows another spell of reduced confidence for the remainder of 2014, a robust recovery does not seem to be a possibility currently. Therefore there is a strong possibility that if the economic situation does not improve, income inequality will increase.

Table 8.7 Shares of men and women by deciles of pooled annual wage



Source: EU-Silc 2009 Population: full-year full-time employees of the population of reference (individuals aged 20-59, students and pensioners excluded); Ponthieux 2013, 13.

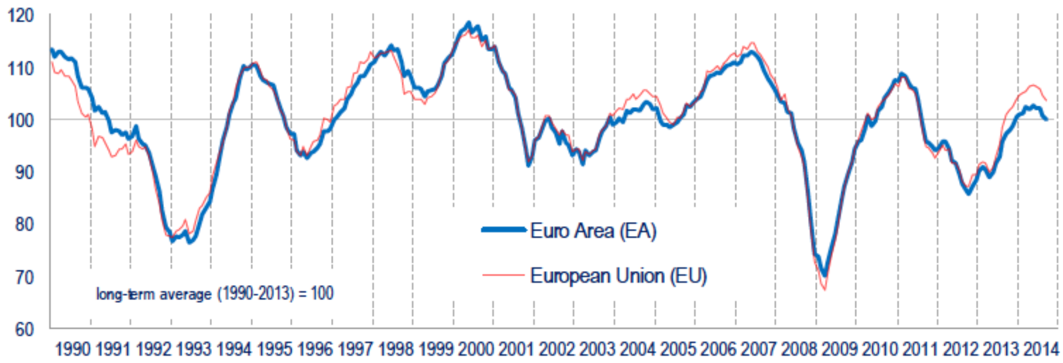
Another impact of the political economic decisions made in France and Germany are on gender differences in terms of income. These differences are larger in Germany than they are in France. Table 8.7 shows that incomes of men and women in France are much closer together starting from the bottom 30% to the top 80% of earners (framed columns). This suggests equal access to jobs as well as a high level of equality (women getting the same salary as men). Considering both these graphs a second trend also becomes apparent. Even though the French have a larger section of the working population whose wages are at close to equal levels, both Germany and France show a trend where, considering the red columns of female wages, women are earning less than men the higher we go in the income deciles. And the reverse is true for men. Considering the blue columns, the income of men increases with every decile.

Although a larger share of women has an income equal to that of the men in France, both France and Germany still have a way to go in terms of making pay between men and women equal. The trends show clearly that there is still some way to go until pay is equalised among the sexes in either country.

8.2.4 Economic results of the French and German approaches

The economic impacts of the French and German economic methods differed from country to country in the same way that the political efforts did. The results of these different methods also affected the standing of France and Germany in Europe and affected their relevance in the European post-crisis environment. This section not only considers the impacts the different economic ideologies had on the German and French economies, but also what influence these differing ideologies provided to France and Germany in the Euro Zone response to the aftermath of the 2007/2008 financial crisis.

Table 8.8 Economic sentiment indicators

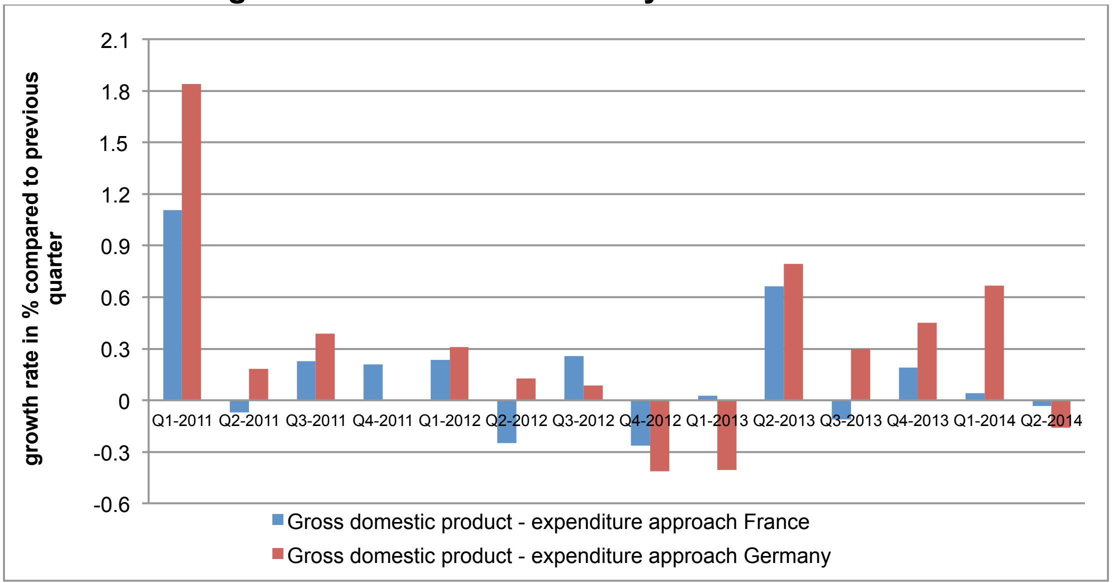


source: European Commission (2014c)
Copy of Graph 1 Economic sentiment indicator (s.a.) in European Commission 2014, 1. Accessed on 25.10.2014

Table 8.8 the Economic sentiment indicator is similar to the Business Climate indicator analysed in Chapter 7. The economic sentiment indicator combines the confidence indicators of different industries to develop a confidence indicator for the whole economy. As with the business climate indicator analysed in Chapter 6, 100 forms the baseline of economic sentiment. An economic sentiment indicator which is lower than 100 is indicative of low economic confidence and an economic sentiment indicator which higher than 100 is indicative high economic confidence. The most recent economic confidence data shows a European picture of once again decreasing economic sentiment moving further away from the boom years of 2005-2007 and the immediate post crisis era of 2010, and the fluctuations over the past two years do not inspire confidence that this pattern of increasing confidence will continue. This picture is particularly troubling for Germany as its export economy relies on a strong EU market.

In terms of German and French growth, the picture remains bleak. Table 8.9 shows quarterly GDP growth figures for France (blue) and Germany (red). The table shows that the OECD *projections* as used in the individual chapters were more positive than the actual growth numbers shown in Table 8.9. The current GDP numbers show no real stability, but rather wide variations within the respective economic performance of France and Germany, with France's economic performance being almost continuously lower than Germany's. In fact, the average rate of growth for France over the period here analysed is of 0,874% (own calculation) as opposed to the German growth, which lies at about 1,528 % (own calculations). These numbers show healthier levels of growth in Germany than in France. Despite the higher levels of growth of the German economy, which in a European context is quite good, the differences in the French and German growth are, in terms what is usually considered as good economic growth, of about 2% annually, negligible. The differences are, however, indicative of a greater economic distancing between the two countries.

Table 8.9 GDP growth France and Germany



OECD 2014 (own representation)

It should be noted that Germany at the beginning of 2013 officially entered into recession with two successive quarters (Q4 2012 and Q1 2013) of negative growth (Carlin, Soskice 2006). Thereafter the business climate has improved again, as Table 8.8 shows. Table 8.9, further shows that the German economy managed to quickly recover from the 6 months of recession with continued growth for the following quarters.

To complete the picture of the economic state of Germany and France, one should also take a look at the level of indebtedness of the countries and their abilities to service that debt. As Table 8.10 shows, public debt rising for both Germany and France. After 2011 these debts would begin decreasing for Germany, however, they would continue to rise continuously for France. As of 2011 the French state would see its level of debt increase breach the EMU guidelines of maintaining a nation’s level of debt at 60% of annual GDP. Those debt levels have continued to rise unbroken and are set to continue to do so until at least 2015 according to the OECD; however, after 2014 they are set to rise more slowly.

Germany thus is more self-sufficient in terms of its requirements than France; this effect can be explained by the different policies both countries engage in. A further explanation is the different state traditions of Germany and France. In terms of social welfare provision, the German approach requires lower levels of expense than the French system. This is because the German state tradition has many points of overlap with the neo-liberal economic concepts as was discussed in Chapters 4 and 5 whereas French state theory opposes many of the principles of neo-liberal economic concepts, particularly the notion that the market could do the work of the state. This difference only further underscores the difference in conception of their respective economies within their constitutional frameworks as well as, to a certain extent, within the fabric of the global economy.

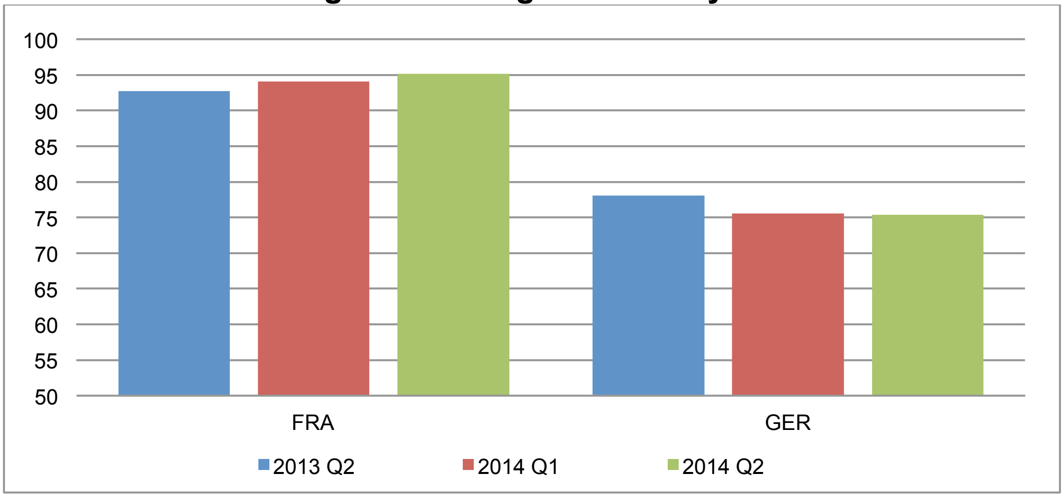
Table 8.10 General government net financial liabilities, as a percentage of GDP

	2007	2008	2009	2010	2011	2012	2013	2014	2015
France	35,697	45,863	52,22	57,527	62,326	70,308	73,591	76,038	77,066
Germany	42,573	44,562	49,033	49,47	50,484	50,463	49,09	47,793	45,845

OECD 2014b

The growth in sovereign debt is generally speaking no cause for concern as long as the country is able to service that debt. Therefore, a look at the amount of real government debt for Germany and France becomes necessary. Here the picture continues to favour Germany. As Table 8.11 shows, the French level of debt has increased to 95% of GDP in the second quarter of 2014. Germany, on the other hand, has managed to reduce its level of debt but it continues to remain above the Maastricht and ERM criteria. However, considering the trend of German debt, and good economic performance (within the circumstances), German debt is much more sustainable.

Table 8.11 General government gross debt by Member State



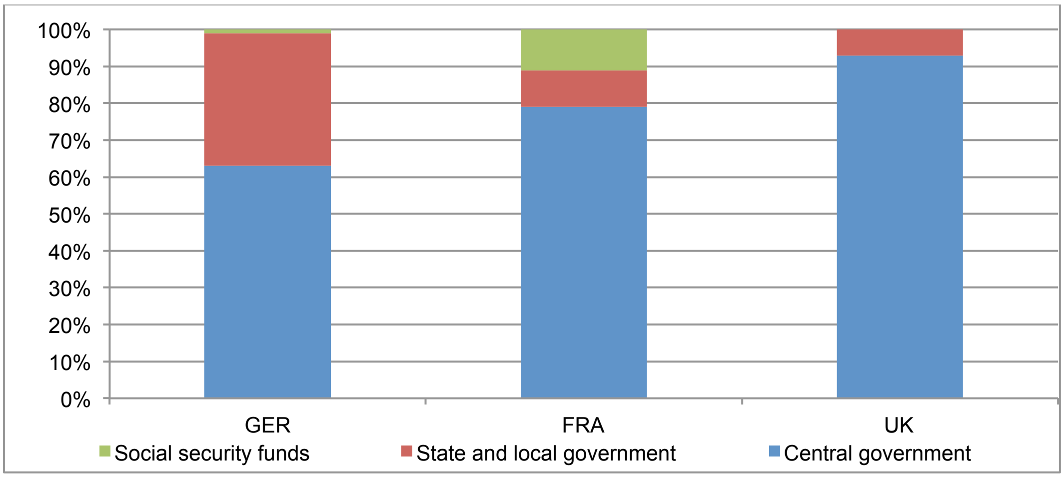
Extract of table: General government gross debt by Member State in percentage , in Allen 2014, 2

However, this should be nuanced by the numbers in Table 8.12, which show the national distribution of these debts. It should also be mentioned that, even though both countries' debt levels lie above what the EZ considers to be acceptable levels, the level in itself is not as important as the ability of the nation to service that debt. It was shown in Table 8.9 that economic growth in Germany and France is lacklustre at best and their ability to service that debt is also decreasing. However, as was shown throughout the tables so far, Germany continues to remain in a better position than France in this area.

Table 8.12 shows that, in Germany, over a third of the sovereign debt lies with the state and local government. However, the size of that debt does raise some questions about how far the German government can limit that debt increase since the *Länder* within Germany have budgetary authority within their own territory. If the states keep on making debts, government savings may not matter. In France, the more worrying number stems from the social security funds, which take up a comparatively significant amount of the national budget. Considering that France has a very diversified social insurance market with a large private sector (see Chapter 7), this number should be much lower. The fact that it is so high means that the social security system is running a deficit. This could be due to a reduction of the number of contributions due to the high unemployment in France coupled with a continued high demand of social security provisions.

Irrespective of these levels, the size of the new debt acquired by France is a matter of concern in Germany and the EU, which continues to insist on a reduction of the French debt (Artus 2013). This is another example of the increased influence of Germany in European politics.

Table 8.12 Government Debt 3



Eminescu 2012, 2 *Source:* Eurostat (online data code: gov_dd_ggd).

Germany has a more flexible labour market, and a more liberal -i.e. deregulated- market place and a high degree of qualified labour, so businesses are more attracted to Germany since investments and continued high levels of production continue to enable Germany to service its increasing debts and to be seen to do so. France, with its high labour costs and less flexible labour market and higher regulations and state interventions in the market are seen as a less attractive place to do business by industries.

8.3 Welfare within a Neo-Liberal framework: Common Concepts different applications

France and Germany have both faced the oil crisis of the 1970s and the collapse of the Bretton Woods system as well as the second oil crisis in the late 1970s. Although there are many differences between the German and French concept of social welfare and the state's duty to provide employment to its people, many of those differences stem from the same basic ideas, which are applied in a different way. As was pointed out in the previous section, the differing legal and governmental frameworks provide different room for manoeuvre to the French and German governments in terms of reform proposals and applications of those reforms. These were especially narrow for French governments and more lax for the German government when comparing both to each other within the context of the global neo-liberal economy.

Different legal and governmental frameworks are, however, only part of the story in this respect. The economic framework and the economic priorities of the countries are also important. France has, since the de Gaulle era, favoured a type of “autarkic” (Bradford 1990, 33) economic position. Mitterrand went through an “import substitution” (Bradford 1990, 33) phase to create an inward looking economy, which was still very much in the spirit of de Gaulle, even though it was adapted to the political and economic realities of the time, which could also be qualified as “export push” (Bradford 1990, 33). A similar evolution applies to Germany, which was always a country with an “export oriented” (Bradford 1990, 33) economy. Having slowly over the last 20 years developed the strongest productive capacity in Europe, Germany slowly turned into an open economy (Bradford 1990, 33) in order to further promote its exports. These different economic conceptions cause different solutions to be considered in order to resolve the (common) issues that both countries faced.

The different legal and governmental frameworks were to some extent integrated on the supra national scale of the EU with the establishment of the European Exchange Rate Mechanism, and the signing of the Maastricht Treaty. The signing of these treaties created a common market and common rules for the member countries to abide by, which required countries and governments to adapt their economies. The results of those adaptations were analysed in Chapters 4 – 7.

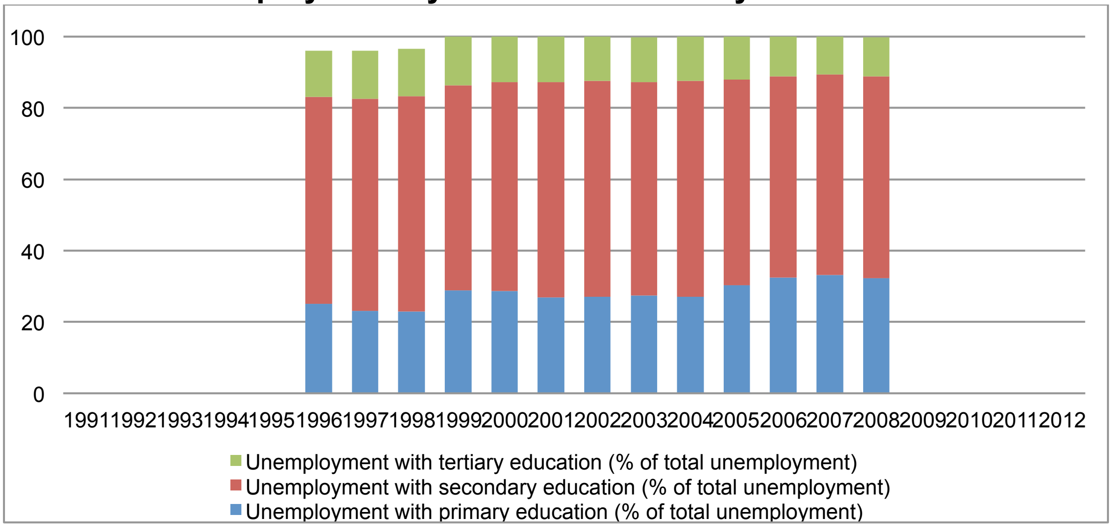
Due to their differing economic principles, Germany and France used and continue to use different macro- and microeconomic tools to achieve their aims, within the limits of a common currency and common market rules. The Germans opted for reforms on the supply side (labour reforms and liberalisation of the economy - i.e. less state intervention) and the French opted for reforms of the demand side (i.e. redistributive measures and government intervention to bolster demand and create jobs or incentivise hiring). These differences are politically apparent in the reports and other writings published by the respective French and German governments (SPD 1998 manifesto, The Third Way, the Hartz Report, French Commission for Growth Reports, Juppé/Rocard Report, Fillon Plan), and economically apparent with the different economic performances of Germany and France.

A good example of the practical consequences of these different philosophies is youth unemployment. The French have found that youth unemployment was becoming an increasing problem; this is a problem the Germans also faced. The reactions to it in both countries were very different, but, in keeping with the rest of their respective philosophies i.e. “French dirigisme” and “German Fördern und Fordern”, which they have used to deal with the neo-liberal framework which the Maastricht Treaty established. The French government supported the youth by providing “contracts for the future” (Aeberhardt, Crusson, Pommier, 2011). They either paid part of the social security costs of the young employees to make them more attractive to employers or gave subsidies to employers in other ways to encourage them to employ people preferably hard to place people like the young and the old. They also provided young people with training opportunities and other aid packages such as work placements to enable them to gather experience and go on to another job with greater ease (Aeberhardt, Crusson, Pommier, 2011).

The German government with their Hartz reforms have gone in a different direction. They have chosen to emphasise the personal responsibility of the individuals in finding work. Personal responsibility was emphasised through the cutting and conditioning of benefit payments including those tied into education. The conditions for receiving benefits are not as harsh as are those for finding work. To receive benefits from the state, proof of progress and regular attendance have to be demonstrated to the Employment Agency. Unemployed people also have a choice to try to look for work or to get further education (Erstes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, Zweites Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2002, Drittes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003, Viertes Gesetz für moderne Dienstleistungen am Arbeitsmarkt 2003).

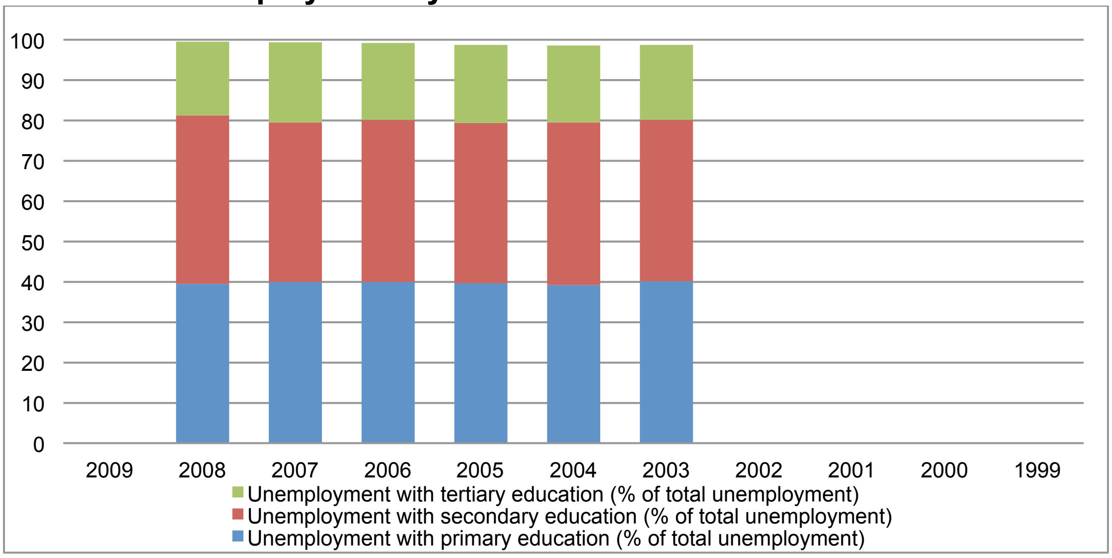
Both paragraphs above show that Germany and France see education and further training as effective methods for helping reduce unemployment and gain competitive advantage. Both paragraphs also demonstrate that the educational setup in both countries use different methods to achieve this aim. Both methods are in keeping with their own national philosophies of *state dirigisme* and *encouragement of personal responsibility,* while at the same time trying to navigate the constrictions of the neo-liberal agenda.

Table 8.13 Unemployment by education Germany



WB economic data 2012 (own representation)

Table 8.14 Unemployment by education France



WB economic data 2013 (own representation)

As shown in Tables 8.13 and 8.14 the French tactic had a greater equalising effect on unemployment as opposed to the German approach, which shows an unemployment rate for secondary education that is twice as high as for primary education. This means that the German approach to education and training is more polarising than the French approach. Low wage jobs may be another reason for that polarisation. A consequence of that might be Germany's workfare programme, which makes unqualified labour more easily replaceable by making it less expensive (although at the expense of the worker).

The French model by contrast tries to provide as much experience to any level of education, to provide citizens with the greatest possible chances at getting a job as well as providing subsidies to the firms to make the cost of labour cheaper. Table 8.14 shows that there is greater equality in the percentage of the people out of work with primary or secondary education, and a likely cause of that is that France does not have a low-income sector of the same size than Germany or have its *workfare* requirements. Both those tables, however, show that completing a higher education degree is the best solution to combat unemployment.

General unemployment was another problem common to Germany and France and provides a further example. The French and German answers to tackle that problem were again different. Whereas the French continue to use a *dirigiste* method of reducing working hours and retirement age. This *dirigiste method* has also involved public works projects, research projects and efficiency gains in industry and the public sector by investing in computers and the Internet as well as long term investments in higher education. These methods address the problem of the comparative advantage of the French workforce. The latest reforms have also addressed the issues of flexibility of the labour market with the introduction of new ways of laying people off (Jeanneau 2013), if this becomes necessary, as well as reducing the procedures required in the redundancy process. However, France continues to ignore the aspect of the higher cost of labour (see Table 8.15).

Table 8.15 Labour Costs per hour in EUR 2008-2013 whole economy excluding agriculture and public administration

	2008	2010	2011	2012	2013	2013 Non-wage costs (% of total)	Change 2013/2008, %
EA-17	25,7	26,9	27,5	28,0	28,4	25,9	10,4
EA-18	25,5	26,7	27,3	27,8	28,2	25,9	10,4
EU-28	21,5	22,4	22,9	23,4	23,7	23,7	10,2
GER	27,9	28,8	29,6	30,5	31,3	21,8	12,2
FR**	31,2	32,6	33,6	34,3	34,3	32,4	9,9
UK	20,9	20,0	20,1	21,6	20,9	15,3	-0,3

**For France, the aggregate shown for the whole economy also excludes NACE Rev. 2 section P (Education).
Eurostat 2013, Eurostat 2014

The column for the year 2012 represents the hourly wage that person earns in that country. The column marked “Non-wage costs” shows how much that wage is composed of social security contributions, taxes and any other legally required payments. As this table shows, the labour costs in Germany and France are very different. The costs are higher in France than they are in Germany with people working in France gaining on average 3 Euros more an hour than in Germany; however, wages in Germany have grown at a slightly higher rate over the period of 2008-2013. Non-wage costs in France are 10,6% (Table 8.3 own calculation) higher than in Germany, which shows why cheap labour is drawn to Germany rather than to France and why the German unemployment rate has decreased so significantly since the Hartz reforms were introduced. This picture is, however, set to change since in 2015 Germany will introduce a minimum wage designed to boost internal consumption (euractive.de, Reuters 2014).

8.4 The future of the European social state

As was investigated in Chapters 4-7 the Maastricht Treaty and the European Exchange Rate Mechanism institutionalized on a European scale the neo-liberal concepts of market economics. While countries were more or less quick to come around to implementing neo-liberal policies within their national economies they eventually did and the sectors that were liberalized often included the financial sector, as was the case for Germany and France.

In Europe, the blame for the financial crisis falls to some extent upon the liberalized financial sector. An analysis of the complete development of the crisis and the exact interplay between the applications of neo-liberal concepts towards the liberalisation of industries (particularly the finance industry) falls outside of the parameters of the analysis conducted here. However, the analysis conducted here supports the argument made by Crouch (2011). Crouch (2011) argues that the state had a significant involvement within the liberalisation of the financial sector by allowing the neo-liberal concepts to shape the process of liberalisation.

The German state instituted its reforms ahead of the financial crisis, providing the German economy with the ability to react rapidly to the crisis environment. This gave the German economy the chance to adapt a different post-crisis position to other EU or EZ countries that did not implement such reforms. This was the case for France. The French economy managed to weather the immediate crisis because of its redesigned dirigiste economic framework and because it applied some of the neo-liberal economic pressures while at the same time maintaining strong internal consumption. However, in the long term, internal consumption was not enough to pull the French economy out of a stagnant economic situation. Since this internal consumption relied to some extent upon the financial and economic support of the French state, this support fuelled an increase in the French debt. Within the context of the French recovery an austerity, fuelled economic recovery would be disastrous since the

French economy does not contain enough solid free market foundations whereupon the French state could build a vibrant economy on. Another problem with French austerity would be its impact on French internal consumption. Austerity would undermine the main pillar of French economic power.

These differences in economic power caused significant stresses to the Euro Zone fabric after the 2007/2008 financial crisis, as some of its member countries came to the brink of collapse, which could have led to a breakdown of the currency union and an end of the Euro and possibly another, deeper recession. To prevent this collapse, rescue measures were implemented, which were designed to avoid the default of national economies and allow them to reform their economies (using austerity) and start growing them once more. The ESM regulations were designed so that countries could prevent their own default in the future. In order to be able to do that, funds need to be available and they need to be backed by countries that do not have possible default issues. The other member countries whose public finances were still considered in good enough health fulfilled this role. Chief among those countries was Germany as Europe’s biggest economy and after that France, as Europe’s second biggest economy (ESM 2013). The measures instituted to prevent the default of the Euro Zone economies were introduced in Chapter 3 of this thesis. What will follow here is an analysis of the projected consequences of the application of German style austerity in Europe as opposed to a more balanced approach including some French style targeted expenses.

As the comparative analysis has so far demonstrated, the German and the French economies show some differences in income disparities and quality of life (though the evolutionary trends are starting to coalesce). The French and German levels of income disparity are coalescing. The German economy, however, is more robust than the French one. The German economy has stronger GDP growth, lower unemployment and has a positive balance of payment account. Because of these factors, the German economy is able to service effectively its current level of debt. There are many similarities between them, especially debt increases, and slow economic performance inside and out, which is a particular problem for Germany with its export-centred economy. On the whole, both countries economically do not demonstrate as wide differences as their social and political discourse and actions would suggest.

The differences that are there do show advantage for Germany especially in the long term, if the economic course is held.

Germany has therefore taken the front seat in terms of economic policy setting on the European scale. Since the Greek debt crisis, Germany has been thrust into a leadership role as the continent's strongest, largest and most powerful economy (despite a lacklustre performance over the last two years). This explains to a point the reputation of a stern parent Germany has received in Europe. Because the German government has implemented austerity politics in Germany since 2003 and they have had success with those policies, they believe they are using rational arguments (Calla 2013, 9) when recommending austerity policies to the other Euro Zone countries. Their own success with austerity has left them with a distinct lack of flair when it comes to explaining their reason for their continued and unbending insistence on doing it their way (Calla 2013, 10).

The German line tended to focus exclusively on austerity. This was more due to their internalised insistence on following the rules and on a self-limiting, non-interventionist state (Dyson 2009) and European budgetary rules (which Germany strongly influenced) only allowed for a 3.5% increase in the public debt per year. It also meant that the countries that got into that situation of near default had to get out of it themselves and do so according to the rules.

Austerity was recommended to re-establish confidence in the market. Austerity would reduce the size of government to allow the private sector to find new avenues of growth (Timbeau 2013, 11) and lead the EZ out of the recession. Austerity therefore has, in a sense, become synonymous with neo-liberalism (Crouch 2011). However, this did not happen; in fact, austerity worsened the crisis (Timbeau 2013, 13) in the EZ. Austerity had further negative effects other than delaying economic recovery. These deep cut measures have had the worst effect on healthcare, as well as human health in general as Stuckler and Basu (2013) effectively demonstrate.

8.4.1 The beginning of a new deal: negotiating a balance between austerity and spending

While the establishment and signing of the Maastricht treaty was a reaction to the power of neo-liberalism within the global economy, its establishment was pursued with a certain willingness due to the projected benefits of being able to regain influence within the global market economy, the establishment of the EFSF and the enforcement of its rules was met with much more reticence by the respective national governments. In fact, the implementation of austerity measures and the enforcement of the six-pack, the two pack and the ERM rules have only been tepidly embraced by the European nations.

The election of the socialists and François Hollande in France and the appointment of Matteo Renzi in Italy as President and Prime Minister respectively has further cooled any support by the second and third largest Eurozone economies towards the German backed austerity argument and have caused the German chancellor to appear increasingly isolated on that issue. This is especially so since the German socialist party, which is the current coalition partner of Chancellor Merkel's Christian Democratic Union, has voiced its support for a more spending oriented approach (dpa, AFP, sdo 2014, LeMaître and Ducourtieux 2014).

A rapprochement between the positions of austerity and spending must therefore be a possibility. This possibility was given form during the 50-year celebration of the Elysée Treaty and Franco-German Friendship. Both countries also used this opportunity to agree on a common set of propositions to deepen the European Monetary Union (Bundesregierung 2013, 1). In a Press statement of May 2013, the German and the French governments respectively, put forward their common plan to rekindle growth and employment for all in Europe. The statement and the points it raises offer effective synthesis of the positions held by Germany and France. The positions announced in May form a promising starting position for a more sustainable growth agenda, which is not limited to austerity.

> The efforts undertaken by Member States to continue growth friendly fiscal consolidation stabilize the euro zone, preserve its integrity and thus restore confidence in the future of EMU. They are conducted in full respect of the existing rules of the Stability and Growth Pact and the Treaty on Stability, Cooperation and Governance in the Economic and Monetary Union which offer the necessary flexibilities" (Bundesregierung 2013, 1).

The essential point is, and this is a significant change in direction from traditional German orthodoxy, that austerity is important for credibility, but it should not come at the expense of growth. Particular attention in this is given to youth unemployment, which this proposal aims to tackle with an investment of 6 billion Euros in the short-term to quickly and effectively tackle this problem (Bundesregierung 2013). This investment will be used to implement the “Youth Guarantee” to ensure places of education, apprenticeship, traineeship or employment are offered to all unemployed youth under the age of 25. This also includes incentives and aides for SME’s.

Further efforts to reduce general unemployment are also planned under the “Compact for growth and jobs”. These include improvements (i.e. further liberalisations and enforcement of necessary regulation) of the European Internal Market, reindustrialisation efforts of Europe, and improvements in international Trade through negotiations of bilateral agreements (e.g. the USA-EU open trade agreement) (Bundesregierung 2013).

These catchphrases used in this statement are reminiscent of phrases used in French reports analysed in Chapter 6, demonstrating significant input from France. The particular policy foci are influenced by Germany as they focus on German priorities such as trade, markets and exports.

The 3rd July of 2013 saw the German government host a European youth jobs summit with members of all 28-member states attending. It was a summit officially designed to develop strategies to spend the 6 billion Euros earmarked to tackle youth unemployment. However, irrespective of the Press statement, the German Chancellor continues to insist that further spending cuts and labour liberalisation are a necessary requirement for job growth and economic growth (Moulson 2013).

This position has not changed since then. However, the calls for more investment have grown louder. This is especially so since the German Finance Minister has presented the German state budget for 2015, which no longer includes any new debts to be contracted, and as detailed in Chapter 5, a steep reduction in investments is planned instead. This does show the same inability in Germany as has been previously demonstrated in France (see Chapter 6 and Chapter 7) to move beyond the German state traditions.

The economic data analysed in this thesis shows that even within countries like Germany that have successfully applied austerity within their economies, their economic performance is not at a level comparable to strong growth, but rather at a level of economic stagnation. Data (see Tables 8.9, 8.10, 8.11) further suggest that continued application of austerity would actually cause more damage than harm to the European as well as the global economy. Therefore, while the French government must address the French deficit increase, and the social security framework within France must be rethought as is demanded by Germany, the French should be given more time to achieve this particularly since their efforts to bring their deficit in line with EU rules would fall short for 2015 which was the year it was supposed to be resolved. Germany on the other hand should not cling to a budget that holds no new debt if this goes to the detriment of new investments. The German government should consider Keynesian principles of government investments more closely. Government investments are necessary to prop up industrial confidence considering its current low level and thereby entice industry to produce again and eventually create jobs.

The new European Commission under the presidency of Jean-Claude Junker is leading by example in that field, having promised to commit 300 billion Euros to fight unemployment and bolster growth throughout Europe (Reilhac 2014) while at the same time insisting that budgets needed to be realised within the limits set forward within the treaties.

8.5 Conclusion

As it currently stands, austerity is here to stay, as the German government is not retreating from its insistence on national budget discipline and adherence to treaty rules. The necessity of reversing national habits of chronic overspending cannot be denied, and neither can the economic success of austerity measures before the 2007/2008 crisis in the German case. However, the German case for austerity is not without its flaws. Chapter 6 and this chapter have shown that neither the European economy nor the German economy have seen signs of a significant and continuing trend of recovery after the initial shock of the crisis had passed and the French economic performance also leaves a lot to be desired.

However, as this lacklustre economic performance shows, the case made by the French Prime Ministers Juppé and Rocard in favour of targeted spending needs to be reconsidered. This type of government intervention should be done in a more effective way, especially since the research conducted in this chapter and the previous chapter showed that the French social spending policy is reaching the limits of its effectiveness. Medium-and long-term investments in France need to be considered only with a look at increasing output or reducing debt in the short run.

The individual approaches Germany and France have proposed to deal with the crisis have yielded only mixed results. Neither approach's advantages entirely outweigh their disadvantages. The austerity method on the other hand increases the polarization of society into rich and poor and makes society less fair. The *dirigisme* method increased debt, and, with a stalled discourse among the social partners, competitiveness is reduced over time, also causing social polarization.

I argue that a balanced approach of targeted spending especially on healthcare, education and employment measures should take precedence over long term spending cuts. The maintenance of national and intra-European access to healthcare, education and employment should be guaranteed by the state(s). For that to happen, money needs to be spent. In the short term, programs and expenditures, which do not show any positive effects should be reduced or cut. The tax code should be revisited to optimise state funding and tax rules should be enforced. Both austerity and *dirigisme* have their merits but they are only effective if applied together. Showing that state spending can be made more cost effective, without reneging on the social contract, is important. Providing the economy with medium- and long-term outlays for goods is also an important part of a European wide recovery.

The final chapter of this thesis will now consider the implications of austerity and spending which have been considered here more closely as well as review the arguments made in this thesis. It will finally consider what avenues for further research this thesis has opened up and where that further research may lead.

Chapter 9 Conclusion

9.1 Introduction

This thesis set out to evaluate, from a political economy perspective, the neo-liberal and classical liberal concepts of state action and welfare within the context of the post 2007/2008 financial crisis environment in Europe. Using Germany and France as similar case studies that act as core drivers of the EU integration project, this thesis wanted to evaluate the historical evolution of the German and French concept of political economic liberalism with respect to welfare and of state action within both the individual national contexts and the European context of the Euro Zone crisis. This thesis has also enquired about the influence these changes in conception (in Germany and France) had on the European Union and the Euro Zone response to the post 2007/2008 crisis, given that Germany and France are the largest countries in the EU and the Euro Zone.

Research in the area of the 2007/2008 financial crisis and the changes in conception of welfare and state intervention on a national and international level bases itself largely on case by case analyses of specific tangible events - i.e. asset bubbles bursting, faltering economies, and episodes of over regulation (Johnson 2010; Smith, Suchanek, Williams 1998; Erkens, Hung, Matos 2012; Stiglitz 2009; Kindelberger 1986, Crouch 2011). Research in IR however does not focus much on the power of the concepts of capitalist ideology and the evolution of welfare as part of the state, which are underlying these events (Strange 1987, 2002). Therefore, this thesis asked the question:

> What are the implications of global change for European welfare states in the context of global and Euro Zone crisis?

This chapter provides a synthesis of the theoretical implications made in this thesis. It will support the analysis of John Maynard Keynes (1936) and Adam Smith (1904, 2009) on the necessity for state intervention, Susan Strange's (1998) arguments about financial power structures, Colin Crouch's (2011) analysis about the power of financial institutions and industries and the neo-liberal economic concept which allows for their accumulation of wealth, Kenneth Dyson's (2002, Dyson and Wilks 1983) concepts of state traditions and Gøsta Esping-Andersen (1990, 1999) and Christopher Pierson's (1991) theories of welfare evolution. All of these perspectives add to the argument that welfare was a continuous integration process of the state *within* society, as a carer for the population; this culminated in the creation of the welfare state which was undermined by the neo-liberal expansion and perfection of financial markets and the increased power those markets could draw upon. This evaluation forms the basic argument of this thesis.

This conclusion highlights the arguments made in the theoretical chapters to compare the differing concepts applied in France and Germany. It first considers the results of the analyses of the political economic consequences of the changed conceptions of welfare and state intervention in Germany and France and those repercussions on the Euro Zone rescue. This evaluation answers the question posed in this thesis by extrapolating the events within Germany and France and applying these actions upon the Euro Zone.

The third section of this chapter investigated specific descriptions of policy solutions considered by Germany and France to solve the aftermath of the 2007/2008 crisis on the European level and supported or opposed by France and Germany. The repercussions of these individual concepts of crisis evolution have already been investigated in the previous section. This section (a) summarises the combined suggestions of both countries and compares them with the principles of the theory developed here and (b) makes suggestions about further action.

The fourth section of this chapter acknowledges the limitations of this analysis. The data focussed on a small number of crucial factors within two countries as most similar case analysis prescribes. Due to the nature of the most similar case study focus and the particular positions and characteristics of Germany and France, a number of the findings of this thesis are not directly applicable to the full range of EU countries (i.e. Greece, Malta *etc).* More importantly, however, the wider theoretical arguments about the neo-liberal approaches and consequences to welfare, and the problems of austerity measures are not only applicable to all of the Eurozone but to the wider global arena.

The penultimate section of this thesis considers the potential avenues of future research that the analysis has indicated. This section argues for a more inclusive and comprehensive study of the austerity enactments and their specific political economic repercussions upon the enacting nations; this would provide a much more insightful view of the short to medium term societal impacts.

The final section provides some final, core reflections on the concept of liberalism and how it has been driving the European political economy particularly before and after the Euro crisis. It also provides an overview on how that concept has changed the way in which nations choose to exercise their power and spend their resources. The thesis will conclude that the best way to ensure employment, education and social security is through the correct application of austerity and spending.

9.2 Substantive study

This section situates the substantive findings within the larger framework of the research conducted within this thesis by drawing together the points from all the substantive chapters and relate them to the points made in the theoretical section of this thesis.

The setup of the EU as it stands today still favours national interests and national influences. The German and French influences are the most significant. For any country seeking to achieve the implementation of most types of EU policy across all of the EU institutions they will require the support of Germany and France. The German political economic reforms implemented 15 years ago, redefined state involvement and state provision of welfare and have provided Germany with steady economic growth and higher national income. This was done at the price of reductions in the standard of living, job security and middle class wealth.

This economic success has empowered Germany on the European level; it allowed Germany to push for similar reforms within European institutions, quoting the success of the reforms within their own country. Germany was able to put EU member states on this course of austerity using a number of factors that played in its favour. As Crouch (2011) argues, neo-liberal economic concepts were used successfully by industry and finance to redefine market operations as the most efficient and effective methods of providing any kind of goods to people including welfare and other traditionally state provided resources. Susan Strange’s (1988) concept of structural power allowed this thesis to follow the unfolding and expansion of the neo-liberal economic concept, which was nowhere more successful on the global scale than in finance. Germany was able to successfully use this structural power because of its own state traditions, which found a lot of overlap with the neo-liberal economic concepts that the German government uses to govern its economy. Its state traditions also made sure that it actively engaged with the concept. The neo-liberal economic theory, as was argued in Strange (1986, 1998; see also Chapter 3), has become the economic theory used in the global economy. The EU was also modelled along such neo-liberal lines, which is why Germany was able to reach the position that it did: as the structures by which the EU is set up share to some extent the characteristics by which the German state was modelled. By contrast, France continued to have a more closed concept of neo-liberal economics due to its state centric conceptions that see the state as a principal guiding force for society as well as the economy. Therefore French governments espouse more classical-liberal ideologies, contributing to its loss of power within the EU, which works on neo-liberal principles. Germany used its structural power to insert austerity conditions within the rules guiding the EFSF, the ESM and the stability pact; these are two new EU institutional actors through which Germany is able to exercise its structural power.

Since the economic depression is set to continue (see Chapter 8), and austerity seems to have worked within Germany while it was in economic difficulties, Germany's influence has grown even stronger within the EU institutions. So much so that one could consider Germany's economic agenda-setting ability in Europe to be hegemonic. If Europe follows the German *diktat*, debt would have to be tangibly reduced in the short term in every EU member country and particularly within the Euro Zone. This would include budget cuts, which would be focussed on welfare as one of the biggest segments of national budgets and as a favoured reduction by neo-liberals. Such a reduction would lead to a nullification of the authority of rule of the state as was argued in Chapter 2. The reduction of the state could lead to a codification of welfare provision rules by the European Council and Council of Ministers. This would align the states across the EU under a Germanstyle framework but also under EU authority, rather than separate national authorities.

The welfare implications of France are in opposition to the German profile and approach. The stagnation of the French political economic reform has done little for the French unemployment rate and French economic competitiveness except harden negotiation lines among social partners. The political traditions enshrined in France's constitution and political history prevent the French state from any significant reduction of the welfare provisions, leaving the French government with fewer options to revitalise its economy. Over the last 15 years, France's manipulation of demand and state *dirigiste* strategies has managed France's unemployment rate and has maintained the French population's power of consumption at high enough levels to maintain domestic consumption levels. It has done so, among others, through welfare contributions to its citizens. These actions were undertaken by increasing the French deficit, and not by addressing the French economy's structural problems. The continuingly increasing deficit and the remaining structural problems in France allowed for little growth after the 2007/2008 financial crisis. Although some reforms were started under the Sarkozy Presidency, they were not enough to resolve all of France's structural problems. The following reforms by President Hollande have had similarly no significant impact on the global performance of the French economy.

The French solution of the Euro Zone debt crisis goes, as was pointed out in the previous chapter, down the road of continued spending, particularly investment spending. This solution would not use austerity to such a large extent to address the European structural problems and the issues of competitiveness of the different countries. This effort would once again strengthen the states' role but it would require more cooperation between states, which, given the current EU setup, I would consider to be difficult. The increase in the deficit on a European level would, without positive outlays in the medium term, put a burden on the economic performance of the Euro Zone. This would demand more government aid, causing a spiral of increasing debt and slow to negative growth.

This thesis therefore proposed, in Chapter 8, for Germany and France to go down the road of a common approach. This approach would combine austerity and spending into one political economic strategy, which would help reform the EU economies and put the EZ back on a track for growth by making its national economies more competitive. This economic growth realised by this common approach, coupled with the establishment of the EFSF and the ESM, can safeguard the EZ from further currency attacks and put it on a track for sustainable growth.

9.3 Theoretical implications

The neo-liberal concept has adverse effects on the social sphere as it attacks social relations among and between the people and the state by individualising people and increasing their own responsibilities as well as the competition among them (see Chapters 4, 5). The analysis of the German economy and society has shown that the neo-liberal reforms of the German state changed the state's interpretation of its role in society and within the economy; those changes in interpretation in turn caused a change in the actions of the state towards its population. This changed interpretation aided the economic growth of Germany. The neo-liberal reforms helped contribute to a substantial reduction of unemployment within Germany both in the west and in the east. The neo-liberal reforms also helped in increasing the low-income sector and contributed to the increase in income differences between rich and poor. It also contributed towards the increase in in-work poverty and general poverty as well as the increased risks of children to fall into poverty.

The classical liberal concept lacks a drive for reform or radical adaptation to changing economic situations due to its focus on the bonds and responsibilities of the state towards its citizens (see Chapters 6, 7). The French state and the French economy have shown that the classical liberal concept reinforced the traditional role of the state within society and within the French economy. The classical liberal concept is focussed on supporting internal demand through provision of financial aid to people with low or no income. This in turn helps reduce inequalities among the population of the country. The classical liberal concept in France operationalised as *dirigisme* consists of an active state presence within the political economy. This consists in large part of economic agenda setting and in providing funding for industries and research. The economic impact of these measures is not as strong as the impact of the German reforms since the evolution of the French economy did not present any additional signs of economic growth. This thesis did present indications that the support of internal consumption did have a positive influence on the economic evolution of the French economy. The unemployment levels also showed no indication of having improved with state measures such as funded employments for young people, which as a program in itself was very successful especially in the 1990s, or a reduction in the number of working hours within a working week or with the reduction of the retirement age.

The research conducted in this thesis leads me to conclude that neo-liberal and classical liberal theories can provide solutions to the internal inconsistencies of capitalism. Those solutions are, however, also imperfect as they are both based on the capitalist system and therefore are themselves flawed as the financial crisis and attempts at its resolution have indicated. The substantive chapters demonstrated that an over reliance on either (classical or neo-liberal) liberal economic theory would have adverse effects on either part of the political economy. For classical economics these adverse effects included a steep increase in inflation and the loss of consumption power, which could turn into a vicious circle. For neo-liberal economics it was the transformation of markets into perfect economies rapidly reacting to changes within their environment, resulting in volatilities, which would destroy the economic system.

This thesis has concluded that Susan Strange's theory of state market interaction through structures of power (Strange 2002, 1986, 1995, 1998,1996), Crouch's (2011) research on the relationship between industry and the state, and Dyson's work (2002, Dyson and Wilks 1983) provide the best approach for illuminating the inconsistencies that plague the capitalist system. Although it still relies on the economic principles of either classical liberalism or neo-liberalism, structures of power consider both the state and the market as recipient and instigator of actions. While Susan Strange (1997, 1995, 1970) freely admitted that state regulation or state action in general was always going to lag behind market actions, the implementation of the new Euro Zone financial supervision rules should reinstate a more sober business culture within the financial institutions. This could, if not eliminate the kind of financial dealing that created the 2007/2008 financial crisis, at least make such speculations become the exception instead of the norm. This conclusion, however, needs to be qualified with the use of the research of Crouch (2011) since he argues that the neo-liberal relationship, within which the state and industry find themselves in, will always be epitomized by the pressures of the industry on the state to reduce regulation and make the economic system more habitable for industry operations.

This thesis also agrees with Esping-Andersen's (1990, 1995) definition of the different welfare frameworks in operation in Europe and with Christopher Pierson's (1991) analysis of the recent evolution of European welfare states. The concepts of Esping-Andersen's framework categorising welfare states have not been updated to reflect the current political economic situation within France, Germany and the rest of Europe. This would force us to re-think Esping-Andersen's categories and what they mean for the welfare state. A new analysis of the German and French welfare state configuration would shift both countries into different categories, which would allow better comparisons to be made among the different welfare systems in a wider study of the implications of a change in the European welfare conception.

Esping-Andersen's (1990) theory on the social redistribution efforts before the welfare state was created is correct but incomplete: since he fails to account for the fact that they have evolved over time. The same can also be said for Christopher Pierson's (1991) analysis, which focuses on the monetary aspect of the implementation of the welfare state. This thesis argues that social redistribution in medieval times through to the Renaissance and into Modernity was a process of continuous evolution and adaptation of the concept of redistribution towards a duty of care of the state. It was only with the implementation of the Bismarck reforms that this concept became fully integrated within the framework of the state, creating the first welfare state. The implication of this argument is that the state, if it were to destroy the welfare state as neo-liberal theory urges it to, would not only destroy welfare but itself as well in the process, leaving a completely unshackled market in its wake. The consequences of such an event would have serious impacts on the EU as an institution and should be the subject of further study.

9.4 Limitations of the study

This thesis investigated the variations in unemployment and unemployment pay, income and income differences as well as levels of education and social welfare contributions in Germany before and after the Hartz reforms. This thesis also investigated the variations in unemployment and unemployment pay, income and income differences as well as levels of education and social welfare contributions in France over the space of three Presidencies. This is a limited sample of issue areas because it is a focused comparison of most similar case studies. It necessarily only provides a limited overview of the overall performance of the German and French economies. The limited size of the sample does provide the essential data to answer the question posed in this thesis. The evaluation of the data was done using a most similar comparison method without the use of specific data analysis. The lack of an in-depth data analysis has drastically reduced the number of links that can be drawn between the different data sets.

The best data available should always be emphasised, but it limits the kind of statistical analysis that was possible, because the data was not primary but secondary data from a variety of different sources. The reputation of the sources from where the data was taken (such as; the OECD, the World Bank, the IMF, German and the French national statistical offices), and their overlapping and concurrent trends within the same data sets, enables a general analysis of the trends caused by the German and French governments over the last half-century. This confidence in the data and its analysis lets the thesis stand behind its answer to the research question posed in this thesis.

9.5 Policy implication

The policy implications of this thesis relate to each of the points made in the substantive and theoretical implications. Situating itself within the structuralist argument of Susan Strange (2002, 1986, 1995, 1998, 1996 and Crouch 2011) and within the political-economic arguments of Adam Smith (1904) and John Maynard Keynes (1936), this thesis developed its own understanding of the role of welfare within the makeup of the state because of those theories. The state cannot completely withdraw itself from the economic sphere without also withdrawing itself from the social sphere, since doing so would cause it to cease to exist. A major policy implication of this analysis is that the state involvement within the political economy of a country needs to be reasserted and not diminished. This thesis has demonstrated that a re-evaluation of the state's policy priorities along either of the ideological lines of capitalist doctrine here analysed may expand or contract the state's political-economic powers.

The substantive implications analysed in this thesis demonstrate that either choice has consequences within the political-economic setup of the country in question. The policy implications of the neo-liberal route provide more power to the markets and industries while weakening the power of the state and of the workers within that economy. The policy implications of the classical liberal route provide more power to the state and the workers and weaken the economic power of the markets and the industries, with long-term consequences for the competitive capacities of the nation in question.

Both these policy implications have been changed by the use of the concept of structural power. The EU as an institution backed and influenced by its member countries can wield such power as well as be a conduit of that power to and from different nations. The 2007/2008 financial crisis impact on the Euro Zone has changed the existing policies during its immediate aftermath (2009-2012). German power within the EU institutions has grown which enabled it to persuade the EU Commission to implement austerity prescriptions for aid received under the EFSF or ESM umbrella.

It is the argument of this thesis that Franco-German cooperation, instead of German leadership and French agreement, provides an entirely new set of policy implications. A combined Franco-German front with a combined set of solutions to combat the aftermath of the 2007/2008 crisis, which includes austerity measures as well as economic guidance and financing, could allow the European economies to find room to grow without being overburdened by austerity prescriptions. These policy implications will still have a strong focus upon austerity. Investment spending designed to create demand and jobs will complement austerity prescriptions in this scenario. The austerity prescriptions in this scenario are also softened by longer time frames within which issues identified by the Troika of International agencies need to be addressed and in which way they need to be addressed.

Overall, this thesis considered a wide variety of policy implications largely because this thesis considered it important to demonstrate the complexity of the issue of the 2007/2008 financial crisis within the political economy of the Euro Zone, without using too many different angles of analysis. Other possible avenues of research are considered in the following section.

9.6 Recommendations for future research

This thesis attempted to shine a light upon a very complex issue of international political economy - i.e. national welfare provision within the EZ after the 2007/2008 financial crisis. This issue was intermeshed with many different economic, political and social aspects, nationally and internationally- only some of which were investigated in this research. This research has subsequently left a number of research areas unexplored for the sake of focus.

This research also did not pursue certain avenues of inquiry, which would deserve further investigation and analysis in the context of the post 2007/2008-crisis world because those avenues were not relevant to the core research question. Areas of inquiry, which need to be further explored, are as follows.

Considering that the evolution of welfare has led to its integration within the political economic actions of the state, research should be conducted upon the size, shape and the continued necessity of the state. This research would follow on and expand upon the theories investigated in Chapters 2 and 3 of this thesis. This avenue of research should also include an analysis of the bio-politics of Michel Foucault (2004, 2008), whose research focuses precisely on the changed nature of the state and its relation to its population though the institution of welfare as a responsibility and duty of the state. The works of Foucault which speak directly to that issue are "society must be defended" (2004) and "the birth of bio-politics" (2008). An analysis of his work would open up a discussion about the power of control states have over their population by providing social services like healthcare, and education and how those powers are impacted and shaped within a market environment.

Further analytical study could also be undertaken, using the research done in Chapters 2-3, by focussing on the discussion of the merits of neo-liberalism and classical liberalism within political economy and the Euro Zone using the works of Karl Polanyi, especially his book *The Great Transformation* (2001). His work is on point with this analysis in the sense that it also critiques the failures and inconsistencies as well as the negative impacts of capitalist societies (Polanyi 2001). However, the focus of Polanyi's (2001) analysis remains on the notion that, for capitalism to create a perfectly free market, capitalism would need to create a permanent split between politics and economics i.e. between the state and the market (Polanyi 2001). This thesis only considers the notion that the neo-liberal forces of capitalism forced a reconceptualization of the duties of the state. Therefore Polanyi's work and analysis would be better served if it was used as the central line of argument within a new research project.

Avenues for further research can also be pointed out within the substantive part of this chapter. For one, an individual national analysis could be undertaken of any Euro Zone or European country using the theoretical principles developed in this thesis and by conducting an in-depth statistical analysis of the political economic repercussions of the ideological move of the state in question. Interesting candidates to conduct such an analysis would be Italy, Spain or Portugal. Their economies were under the EFSF and ESM umbrella and had to implement the austerity guidelines that came with that protection. Using this analysis we could investigate how far removed the current state provisions are from the ones before austerity and if those austerity impositions have changed the state's own conception of its role in society or if the Italian, Spanish and Portuguese governments have found other ways to achieve their austerity targets without having to change their state concepts. Another interesting study could focus on those European states that are not part of the EZ such as the UK and Denmark. Since they have other tools of economic management at their disposal, did they need to implement austerity or were they able to maintain their traditional state concepts?

Additionally, it could be measured what kind of impact this ideological change has on the state's international standing. Secondly, a larger study could be undertaken which would analyse the behaviour of all the countries within the Euro Zone. This analysis could consider the increase or the loss of influence among the other members of the Euro Zone, according to what extent and with what measure of success they implemented austerity.

Continuing on the thought of analysing the behaviour of states, using the work of Crouch on industry state relations and Dyson's work on state traditions, an analysis should be conducted on the political impacts of economic pressures upon nations. This analysis should consider if there is a causal relationship between nationalism and national economic performance and if any potential relationship evolves differently within different economic systems.

One particular relationship, which this thesis did not analyse for the sake of space and focus, was the relationship in France between the ossification of state, industry and labour relations with the increasing power of neo-liberal economic concepts and their pressures upon the French economy. Considering how the state, industry and labour relationship was created within a global Keynesian economic system, its transposition within a neo-liberal economic system with different values and priorities would have changed the relationship between the contracting parties and could have an influence on the willingness of either or all parties to negotiate. A closer analysis of this relationship would complement very well the analysis of the general political impact of changing economic circumstances.

A final avenue of research relates to future actions of the EU regarding the economic crisis, which continues to rage on within Europe. This thesis only introduced the concept of international political economic co-operation to tackle the Euro crisis by proposing a general plan of action based on the continuing struggle of the French and other European governments to loosen the austerity restrictions and at the same time increase the investment on a national and European level to stimulate growth and reduce unemployment. The final section of Chapter 8 argued for its merits as opposed to the singular German-led austerity plan. Considering that the new Commission President has vowed to invest heavily in such measures, further research should be conducted on the evolution of any co-operative effort that may be established between nations at a European level and on the international political economic consequences of that evolution.

9.7 Conclusion

This thesis set out to investigate two different capitalist political-economic principles and the political-economic influence those two capitalist ideologies have had on the countries of Germany and France. This thesis analysed how a change in their political-economic ideology changed their standing within Europe and the Euro Zone. The way this research did this was by focussing first on the state and its role within society and then on its role within the economy, which was a necessary step to be able to link it to the theory of structural power. The analysis of structural power, focussed on the interplay of the state and the markets. The use of this theory has been neglected over the years, in favour of purely economic analyses. The reason this thesis used the theories of Colin Crouch, Kenneth Dyson and Susan Strange's structural approach is precisely because its use of political economy which allowed for a two way connection to be established between the state and the market, and to do so on an international scale which is moderated by other power structures as well.

The evaluation of the development of welfare was a further necessary point to be considered since it linked into the political economic actions of those states within the Western European democratic traditions: these actions were central to the states' reason for being. The investigation of the change in conception of the role of the state and its provision of welfare in Germany and France was a good way to demonstrate the practical impact of the theory thus developed. For the analysis to be completely compatible with the international aspect of Strange's theory and to observe the reach of these effects, their impact needed to be mediated through the actions of Germany and France on the Euro Zone rescue efforts, which were also analysed.

The questions that this thesis addressed fit squarely within the field of international political economy. The question addresses a field of study which has not received much attention so far by international political economists who favour economic and monetary analyses. It addresses the issue of a too narrow focus of the analysis of crises on economic and normative aspects foregoing an analysis of the changes in discourse on the level of concepts, which are at the basis of economic changes.

The conclusion this chapter reaches therefore is that the use of complex answers to a question is the necessary and correct approach and the insistence on a single point of view to solve a problem is rarely the right course of action. In the case of the thesis, relying solely on the German or the French answer to the 2007/2008 financial crisis repercussions on the Euro Zone is not a good way to deal with this economic crisis because both approaches have detrimental effects to the economy and most importantly to society.

The German approach contributed to an increased polarisation of the economy, which helped to increase significantly the income differences between the rich and the poor; it also contributed to the increase of the low-income sector. The French approach tried to reduce the already existing polarisation of society. This approach succeeded avoiding a deterioration of the income differences in the short term but increased public deficits and made no visible contribution to economic growth. Both approaches therefore demonstrate why the individual application of these concepts is not a workable solution since state traditions may not be compatible with these concepts as was seen in this analysis with France. Furthermore, the continued application of the austerity prescriptions and enforcement of the new and extended budget controls and deficit brakes have a number of negative side effects. Among others, the reforms countries need to implement in order to fulfil those prescriptions are in some instances very painful and provoke public opposition. This opposition has found an outlet in the recent European elections, which saw a great number of nationalist parties (left and right) as well as other types of protest parties get elected to the European Parliament. While the opposition to austerity might not be the entire reason for this increase in nationalist voting as well as nationalist power, within the nations themselves, the imposition of austerity is a major component of the popular frustration.

None of the approaches considered here are perfect. However, recent events like the latest European election results and the recent economic growth projections predict a future fraught with challenges and obstacles that need to be addressed nationally as well as on the European level. An effective and compelling case in defence of a pure austerity approach needs to be made if it is to continue to be implemented. At the same time, other options need to be explored that move beyond crisis management and into growth creation. A clear vision for Europe and its nations needs to be articulated and implemented, to take back momentum form nationalist parties and provide momentum for a European recovery.

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