

The Challenges of the German Reconstruction with Two different Economic Systems



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Economic Aspects of the German Reunification

TASK 2

Describe the economic challenges of the German reunification with two different economic systems (market economy versus centralized planned economy) and discuss alternative solutions.



Content

- ❑ Economic situation of East Germany (Centralized planned economy)
 1. Advantages
 2. Challenges
- ❑ Economic situation of West Germany (Market economy)
 1. Advantages
 2. Challenges
- ❑ Alternative solutions
- ❑ Implementation of the recommended solution



Introduction

- ❑ Review of Planned Socialism
- ❑ Review of Market Capitalism
- ❑ Rise of Cold War animosities
- ❑ Reconstruction of the two Germany economies



Economic situation of East Germany

A **centrally planned economy**, also known as a command economy, is an economic system in which a **central authority**, such as a government, makes **economic decisions** regarding the manufacturing and the distribution of products.

Five Characteristics of a Command Economy

01

The government creates a central economic plan.

02

The government allocates all resources according to the central plan.

03

The central plan sets the priorities for the production of all goods and services.

04

The government owns monopoly businesses.

05

The government creates laws, regulations, and directives to enforce the central plan.

Command economy advantages

- low levels of inequality and unemployment,
- the common good replacing profit as the primary incentive of production,
- large amounts of resources for large projects can be manipulated without lawsuits or environmental regulatory issues.

Command economy challenges

- lack of competition,
- lack of efficiency,
- the development of a black market and other coping strategies,
- goods production is not always matched to demand,
- innovation is discouraged and leaders are rewarded for following orders rather than taking risks.

Trabant (so-called “Trabi”, 1959~1991)

A symbol of the inefficiency of the GDR’s planned economy



Economic situation of West Germany

Social Market Economy (SOME)

- Coined by Alfred Müller-Armack
- Implemented in West Germany by Ludwig Erhard under Konrad Adenauer
- Def. A socioeconomic model combining free market capitalist economic system alongside social policies that establish both fair competition within the market and a welfare state
 - Buyers and sellers negotiate and regulate prices and production
 - Free from the government's intervention

Economic situation of West Germany

Advantages of SOME

- Promote and protect economic freedom
 - Pricing freedom
 - Free choice of workplace
 - Private property protection
 - Investment
 - Competition
 - Innovation
 - Diversified market and products
 - High efficiency→ economy growth
- Balance between work and capital in enabling competition
- Provide social security to who cannot participate in the economy

Economic situation of West Germany

Challenges of SOME (or free market)

- Monopolization
- Price fixing
- Existence-threatening unemployment
- Poor working conditions
- Ethical issues
- Existing social and economic gap
- Lack of optimization resulted from market competition

Solutions

Existing Solutions

German Unity Fund (Fonds Deutsche Einheit) (1991-1994)

Bond Issue / federal budget support

Solidarity surcharge (Solidaritätszuschlag, so-called “Soli”)

5.5% additional tax rate for income tax / corporation tax (abolished from 2021)

Solidarity Pact I / II (Solidarpakt I / II)

Solidarpakt I (1995-2004) / Solidarpakt II (2005-2019)

Above all, to modernize the infrastructures in the new federal states

Solutions

Other possible Solution

Attracting investment from foreign / domestic conglomerates

Creating new economic environments / R&D

Supporting the scale-up of native companies

Recommended Solution

Building large business clusters in the new federal states

Connecting native firms to new economic environments created by conglomerates

- (Re-)Inflow of population
- Enabling the sustainable growth of the eastern economy
- Reducing the economic gap between the old and new federal states.

Implementation

Bremen



Rhein-Ruhrgebiet (NRW)



Köln-Bonn (NRW)



Hamburg



Berlin



Implementation

TESLA GIGAFACTORY 4 BERLIN JUNE 20, 2021

An aerial photograph of the Tesla Gigafactory 4 construction site in Berlin. The image shows a large, rectangular building under construction with a grey roof. The surrounding area is a mix of dirt, sand, and construction materials. In the foreground, there are stacks of tires and other materials. A large yellow crane is visible on the right side of the site. The background shows a line of trees under a clear sky.

**One of the most transitional policies in this
period:
The Treunhandstalt:
“Trust Agency”**

What was this Agency?

- It was an agency established by the GDR, in order to re-privatize and privatize East German enterprises, prior to German Reunification
- It was responsible for 8,500 state-owned enterprises.

- It also took over around 2.4 million hectares of agricultural land and forests, the property of the former Stasi, large parts of the property of the former National People's Army, large-scale public housing property, and the property of the state pharmacy network.

In a nutshell:

The THA had transformed East Germany from a state-owned to a predominantly privately owned economy in a very short time.

Differences with other transitional economies process:

- Social and political stability and peace. There are few signs of the government and the THA having facilitated a second 'economic miracle' in East Germany.
- The 'dramatic' deindustrialization and the explosive increase of unemployment, there has been no wide-scale social unrest or political violence.

(Financial Times 1993; Der Spiegel 1993: 95)

Thus, this characteristic of the 'German model' appears also to have survived unification.

Conclusion

- ❑ **Centralized planned economy vs. Market economy**
 1. Advantages
 2. Challenges
- ❑ **Alternative solutions**
- ❑ **Potential future alternatives to diminish the geographic German gap**



THANK YOU
FOR YOUR ATTENTION

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