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We'd rather pay than change the politics of German non-adjustment in the Eurozone crisis

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Abstract

Germany's large current account surplus has been widely criticized, especially against the backdrop of the role of macroeconomic imbalances in the Eurozone crisis. We argue that Germany's resistance to reduce its massive current account surplus through an expansionary policy at home is rooted in distributive struggles about the design of possible adjustment policies. To explore this argument, we leverage original survey data from 135 German economic interest groups, qualitative interviews with interest group representatives and policymakers, and data from public opinion surveys. We show that while there is general support for internal adjustment among German interest groups, they disagree heavily about which specific policies should be implemented to achieve this goal. Together with a broad public and elite-based consensus to avoid a break-up of the Eurozone, this polarization turns financing into a politically attractive strategy. Rather than being rooted only in German ordoliberal ideas or Germany's export-oriented structure, distributive conflicts contribute significantly to Germany's resistance to reduce its large current-account surplus. Because similar dynamics can be observed in other surplus countries, we argue that distributive struggles within surplus countries played an important role in interstate conflicts about the management of the crisis.

Keywords International political economy · Comparative political economy · Eurozone crisis · Global imbalances · Distributional conflicts · Interest groups · Germany

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1 Introduction

In recent years, Germany has accumulated a massive and growing current-account surplus. By exporting more than it imports and saving more than it consumes and invests at home, the country has accumulated the world's largest current-account surplus, reaching almost 8% of its GDP in 2017 (IMF 2018). This is widely viewed as a source of concern, as global or regional imbalances and the credit booms they fuel have often been a key driver of balance-of-payments crises (Schularick and Taylor 2012). Not surprisingly, Germany has been widely criticized for this development and faces considerable political pressure to rebalance its current-account. International policymakers such as the French president, the director of the International Monetary Fund, the head of the European Central Bank (ECB), and the US president have decried the German current-account surplus as “unbearable”,¹ a “serious threat”,² an “unresolved issue”³ and quite simply “very bad.”⁴ Germany's surplus has fueled political resentment and, perhaps most threatening to Germany, protectionist impulses among major trading partners such as the United States. This has created incentives to reduce the current-account surplus that go beyond a purely economic rationale. Nonetheless, Germany has been reluctant to implement policies that would induce the large-scale domestic macroeconomic adjustment needed to reduce the surplus.

Beyond this political pressure, Germany's reluctance to rebalance is also puzzling for domestic reasons. Although the effects of internal adjustment in Germany are debated (Kollman et al. 2015; Felbermayr, Fuest, and Wollmerhäuser 2017), there are a number of arguments in favor of such measures. First, the current-account surplus is associated with low levels of public and private investment that have fueled heated debates over the country's ability to sustain future growth (Bach et al. 2013; Südekum and Felbermayr 2017). Second, a rebalancing designed to lower Germany's trade surplus could result in improved infrastructure, higher domestic wages, higher rates of inflation, and more domestic consumption. While some of these developments would be at odds with the interest of some societal groups, not everyone would be hurt. To the contrary: groups as diverse as workers in the nontradables sector, whose wages are likely to rise, homeowners repaying mortgages, who would face a declining debt burden as inflation rises, or those relying on public investment can benefit from rebalancing (Frieden and Walter 2017). Moreover, Germany's high export-dependence, which is reflected by the surplus, leaves the country exposed to negative economic and political developments abroad. Despite making economic growth dependent on foreign demand, current-account surpluses also are always associated with net capital outflows. Especially, in the German case, these investments abroad have often generated only small or even negative returns (Baldi and Bremer 2015; Hünnekes, Schularick, and Trebesch 2019). In the Eurozone crisis, for example, German banks were heavily exposed to the risk of a default in deficit states (Bibow 2013; Steinberg and Vermeiren 2015). All of this is not to say that internal adjustment would only have positive consequences. After all, the current-account surplus is associated with new jobs in the export sector, low

¹ Bloomberg (2017), “France's Macron Says German Trade Surplus Harmful to EU Economy”, 17.04.17.

² IMF (2017): “Transcript of an Interview with IMF Managing Director Christine Lagarde with the Leading European Newspapers Association”, 20.04.17

³ ECB (2017): “Press Conference with Mario Draghi, President of the ECB, 9 March 2017.”

⁴ 4CNBC(2017): “Trump reportedly calls Germans ‘very bad’”, 26.05.17.

inflation, and high savings, which is important for an ageing society such as Germany. What the discussion shows, however, is that the economic case against internal adjustment is far from clear.

In sum, the reluctance of Germany (and other surplus countries) is both puzzling and has far-reaching consequences. Nonetheless, research on the sources of this reluctance is scarce, just like research on surplus country politics more generally. Existing work has predominantly focused on two explanations: the importance of ideas and the role of growth models. Ideas-based explanations emphasize that strongly-held beliefs about the merits of prudent economic policies (Brunnermeier, James, and Landau 2016; Bulmer 2014; Dullien and Guérot 2012; Matthijs 2016; Young 2014) or the causes of past crises provide coherent justifications for non-adjustment (Howarth and Rommerskirchen 2013). During the Eurozone crisis, for example, the ordoliberal reading that deficit states needed to reform their economies to regain competitiveness, whereas stimulating growth in surplus countries would only risk surplus countries' hard-earned standing on international markets and endanger price-stability has been shown to have driven policymaking in Germany, but also other EMU surplus countries such as Austria or the Netherlands (Matthijs and McNamara 2015; Schäfer 2016; Young 2014). In contrast, the growth-model explanation emphasizes the structural importance of the export sector for surplus-country economies (Baccaro and Pontusson 2016; Hall and Soskice 2001; Klein and Cukier 2009). It argues that the need to preserve export competitiveness in surplus countries creates a large coalition of policymakers, employers and workers, all of whom are opposed to internal adjustment measures that would expand domestic demand, lead to higher inflation, and a rise of the domestic wage level (Hall 2012; Höpner and Lutter 2014; Iversen and Soskice 2018).

Both of these approaches provide valuable insights into surplus country resistance to adjustment. However, they also leave open some questions. For one, existing explanations paint a picture of surplus countries that are domestically united in their resistance towards macroeconomic adjustment, either because of the dominance of economic ideas or because safeguarding the export-led growth model constitutes the national interest. Yet, analogous to the distributive struggles in deficit countries (Eichengreen 1992; Simmons 1997; Walter 2013), adjustment politics in surplus countries generate diverging interests (Frieden and Walter 2017; Walter et al. 2020). It is not obvious, for example, why workers in the non-tradables sector should support wage restraint against the backdrop of a widely criticized trade surplus. By assuming a homogenous national interest or national economic ideology, existing approaches cannot account for divergent societal preferences and their influence on policymaking. Second, existing approaches concentrate on fiscal and monetary policy as well as wage-setting issues. Macroeconomic adjustment decisions are, however, multidimensional. Resistance to internal adjustment has significant consequences abroad. It risks global and regional financial stability and increases the financing needs of deficit states, especially when private capital inflows into these countries dry up. Understanding why surplus countries opt against internal rebalancing, thus also requires understanding how surplus country decision-makers evaluate these alternatives relative to the option of adjusting domestic policies in a way that reduces the current-account surplus.

Our paper seeks to answer these questions and hence to complement existing research on the lack of rebalancing in surplus countries. It does so by studying the

drivers of Germany's policy responses to the Eurozone crisis, during which Germany's (and other EMU surplus countries') unwillingness to rebalance has been criticized particularly heavily (Blyth 2013; Eichengreen 2017; Frieden and Walter 2017; Matthijs and Blyth 2015). Although the size of possible spill-overs remains contested (Blanchard, Erceg, and Lindé 2017; Caporale and Girardi 2013), many researchers have argued that an expansion of German domestic demand could have helped crisis countries creating additional export opportunities and countering the deflationary pressures within the union as a whole (Baldwin et al. 2015; Lane 2013; Wihlborg, Willett, and Zhang 2010). Political pressure to undertake domestic rebalancing was large. Nevertheless, despite some limited steps such as the introduction of a minimum wage in 2015 and agreeing to the introduction of a surveillance mechanism at the European level which monitors both unsustainable current-account deficits as well surpluses,⁵ consecutive German governments have done much less to spur domestic demand and investment than international organizations and other member countries did call for (IMF 2014, 2017a). This lack expansion during the crisis is especially surprising since Germany in many ways is a most-likely case for internal adjustment. Not only were severe balance-of-payments imbalances a key driver of the Eurozone crisis (Baldwin and Giavazzi 2015; Jones 2015; Lane 2013; Obstfeld 2012), the crisis also occurred in a highly institutionalized context which should have facilitated cooperation. Finally, the fact that the crisis took place in a monetary union made major exchange rates realignments between Germany and the crisis countries prohibitively expensive. Given this set-up, Germany provides a particularly insightful context for exploring surplus countries' reluctance to adjust.

We argue that this reluctance is rooted in distributional conflicts about the specific design of internal adjustment policies and the attractiveness of the alternatives: external adjustment and financing. Internal adjustment is contentious, because it can be implemented in very different ways, many of which benefit some groups, but also hurt others. As a result, even in situations in which there is general support for strengthening domestic demand, important economic interest groups disagree about how to achieve this goal. The resulting polarization in positions about how to adjust internally can lead to a stalemate between major economic interest groups and prevents them from jointly pushing for domestic expansion. This makes internal rebalancing unlikely especially in contexts in which good economic fundamentals decrease the political priority of domestic reforms. If, at the same time, broad elite and popular consensus exists that external adjustment is to be avoided, this leaves financing as the last option on the table, an option that becomes particularly attractive when it can be designed in ways that push the burden of adjustment onto deficit countries.

We examine this argument using original survey data from 135 German economic interest groups, qualitative interviews with German policy-makers and interest-group representatives, as well as public opinion data. Our results show that in the context of the Eurozone crisis, different types of interest groups, such as employer associations, trade unions, or social policy groups varied significantly

⁵ This mechanism is part of the newly established Macroeconomic Imbalance Procedure. Importantly, surplus countries insisted on an asymmetric treatment of the different current-account positions, in which deficits of more than 3% of GDP are characterized as unsustainable, whereas surpluses only get monitored if they are 6% of GDP or larger (Moschella 2014).

in their support for and opposition to specific possible internal adjustment policies and that these differences are largely in line with their material interest. When confronted with internal adjustment policies to which interest groups were opposed, their support for financing increased. Because financing was also a less salient issue for most interest groups and because there was widespread determination to avoid a break-up of the Eurozone, conditionality-based financing in the form of bailout packages became the politically expedient alternative. In a final step of the analysis, we explore to what extent these findings travel beyond Germany. For this purpose, we present a brief analogous analysis of interest-group preferences in the two other main surplus countries in Eurozone: the Netherlands and Austria. We show that interest-group preferences in these two countries exhibit a remarkably similar pattern to those in Germany. These findings underscore that distributive struggles among interest groups are an important factor underlying surplus countries' reluctance to rebalance.

2 The argument: Distributive struggles and the politics of (non-)adjustment

Why has Germany been reluctant to adjust its large current-account surplus? We argue that non-adjustment in the face of a large current-account surplus is rooted in distributional conflicts about the specific design of internal adjustment and the attractiveness of the alternatives, external adjustment and financing. Although most economic actors could benefit from some internal adjustment measures to expand the economy, most of these measures also inflict substantial costs on others. The resulting polarization in opinions about how internal adjustment should be achieved makes internal adjustment politically costly. Building on existing research on the political economy of balance-of-payment crises, the following section develops this argument in more detail.

2.1 Adjustment strategies in surplus countries

When balance-of-payments crises erupt, surplus countries have three options to contribute to solving the immediate crisis and addressing the underlying economic problem (Frieden 2014; Frieden and Walter 2017; Pepinsky 2014): First, they can try to avoid any adjustment on their part and simply provide crisis-ridden deficit countries with funds to cover the financing needs that private markets are no longer willing to provide.⁶ Second, they can allow their own economies to adjust externally through the exchange rate. Third, especially in the long run, surplus countries can contribute to reducing the economic imbalances underlying the crisis by adjusting internally and changing their own domestic economic policies.

The first option, financing, means that surplus-country governments provide deficit countries with the means to sustain their deficits. Such financing can take multiple forms. One possibility is to directly transfer resources to deficit countries, for example in the form of bailouts or through more institutionalized transfers, such as common

⁶ Current account deficits are usually funded by private capital inflows. Balance-of-payments crises emerge when these inflows dry up.

financing instruments (e.g., Eurobonds) or the introduction of joint automatic stabilizers (e.g., a pan-European unemployment scheme).⁷ Moreover, deficit countries usually have accumulated large amounts of debts. Here, surplus states, which tend to be among the main creditors, can contribute to burden sharing by agreeing to debt relief and debt restructuring. Importantly, financing by surplus states can be made conditional on the implementation of adjustment measures in crisis countries. In that case, financing may also help shifting the long-term burden of adjustment on to deficit states. Nonetheless, all financing measures are costly. Bailouts and transfers use surplus countries' tax payers' money, whereas debt relief imposes losses on surplus countries' banks and financial institutions. How societal groups evaluate the costs and benefits of financing may, therefore, not only depend on the specific form of the transfer but also on the amount of money that is spent on bailouts, debt reliefs, common stabilizers etc. (Bechtel et al. 2017).

The alternative option is to rebalance, that is to allow surplus country economies to adjust. This can occur via the exchange rate (so-called *external adjustment*), or through changes in the domestic economy (so-called *internal adjustment*). Through an exchange-rate appreciation, external adjustment makes exports more expensive, stimulates imports, and, reduces the trade surplus. As in deficit countries, the costs of external adjustment increase with the rigidity of the exchange-rate regime. Accordingly, external adjustment is costlier in countries with pegged rather than flexible exchange rate regimes and in a monetary union, external adjustment implies a (at least a partial) break-up of the union, which is likely to create a host of uncertainty and financial turmoil.

However, surplus countries can also adjust their economic policies internally by providing incentives for market actors to save less and invest more. Here the goal is to boost domestic demand and imports, and to reduce capital outflows. In contrast to external adjustment, internal adjustment can be achieved through various policies, ranging from more public investment in infrastructure and schools and lower corporate taxes, to an increase in wage or pensions. Rebalancing generally implies higher domestic wages, higher rates of inflation, more domestic consumption, and less savings and investment abroad. This is good for some groups (e.g. domestically oriented workers), but bad for others (e.g., the export sector). It is important to point out that the choices between the three adjustment strategies only arise in the longer run. In the early crisis period debates may focus on policies with immediate effects such as financing and external adjustment. However, the longer the crisis lingers, the more the long-run reduction of imbalances through internal adjustment becomes an option.

2.2 Adjustment trade-offs for economic interest groups

What determines surplus countries long-term response to balance-of-payment crises? We argue that situations where “doing nothing” is not an option – for example because a devaluation or default of a major deficit state in crisis also reverberates among surplus countries as it was the case in the Eurozone crisis – surplus countries' approach to crisis management will be influenced by the

⁷ The latter option, however, is only available for countries in strong cooperative settings, such as the European Union.

preferences of important economic interest groups (Broz and Frieden 2001; Grossman and Helpman 2001; Malang and Holzinger 2020). During the Eurozone crisis, such economic groups were crucial for a number of reasons, especially when it came to internal adjustment. First, most countries with large current-account surpluses in the Eurozone are coordinated market economies (Iversen and Soskice 2018). In these systems economic interest groups are traditionally deeply involved in economic policy decisions (Hall 2012; Schmitter and Streeck 1991). This is especially the case for issues pertaining to questions about internal adjustment: in coordinated market economies policies such as domestic investment policies, measures to stimulate wage growth or tax reforms often are directly negotiated between the government and organized interest groups. They are also issues that are squarely in the competence of national policymakers, so that the influence of European-level decisions is limited. Although existing research reaches conflicting conclusions about the role of interest-group preferences on bailout and institutional reform decisions taken at the European level (Kudrna et al. 2018; Tarlea et al. 2019), this suggests that internal adjustment policies at the domestic level have been subject to intense interest group pressure. Second, a large body of literature has shown that the influence of interest groups is inversely related to the salience voters attach to a policy issue (Culpepper 2011). Here it is important to differentiate the salience of the different crisis strategies (external adjustment, internal adjustment, and financing). During the Eurozone crisis, questions about financing or a potential break-up of the monetary union were highly salient questions for the mass public (e.g., Bechtel et al. 2014; Schneider and Slantchev 2017). The high salience of questions concerning external adjustment and financing limited the role of economic interest groups in these policy areas (Kudrna et al. 2018). However low unemployment and stable growth in Germany substantially decreased the salience of domestic economic reforms in the eyes of the German electorate (Steinbrecher 2014; Walter et al. 2020). In such a setting organized interests tend have much more influence. In sum, both the motivation and the ability of interest groups to influence policymaking was much higher with regard to internal adjustment than with regard to external adjustment or financing.

What shapes the preferences of economic interest groups with regard to the management of balance-of-payment crises? We build on work that has analyzed the politics of adjustment in deficit countries (Walter 2008, 2013, 2016) and conceptualize preferences based on the trade-offs interest groups make between the net costs of external, internal adjustment, and financing. They will prefer the option from which they benefit the most or, if all options are costly, the option which is least costly for them.⁸ In general, we can distinguish three types of interest groups: A first type is vulnerable to internal adjustment (for example because it represents a highly inflation averse group), but not to a revaluation of the exchange rate. Because financing is costly as well, this first type is likely to prefer external adjustment to any other form of crisis management. A second type would gain from a boom in domestic demand but would lose from an

⁸ We use a stylized example where governments must choose between the three types of strategies. Of course, combinations of these options are also possible (e.g. some policies that increase domestic demand, some exchange rate appreciation, and some financing). The underlying distributional considerations are likely to be the same in these situations, however.

exchange-rate appreciation. Because internal adjustment creates net benefits for this group while financing is costly, interest groups of this type will favor internal adjustment over external adjustment or financing. Finally, a third type is vulnerable to internal as well as external adjustment. This type of actors should be most willing to provide deficit countries with some form of financing.

This prediction is complicated, however, by the fact that internal adjustment, financing, and to a lesser extent external adjustment can be implemented in different ways. When it comes to internal adjustment, for example, policymakers intent on boosting domestic demand can increase public investment in infrastructure and schools, but they can also reduce corporate taxes or cut red tape for businesses to incentivize private investment. Moreover, they may raise the minimum wage, increase pensions, or expand unemployment benefits. Whereas all these measures help to rebalance the economy, their distributional implications differ widely. As a result, interest-group vulnerabilities to internal adjustment are likely to be policy-specific. While one group may benefit from one type of internal adjustment policy, the same group could, at the same time, be hurt by another policy aimed at boosting domestic demand.

In the same vein, interest group vulnerabilities towards financing, and to a lesser extent external adjustment, are also policy-specific. The costs that financing puts on different societal groups in surplus countries depend on how exactly funds are provided to deficit states. Bailout packages, for example, are largely borne by the taxpayer, whereas debt relief and haircuts on private loans to deficit countries impose costs on surplus-country investors (Copelovitch and Enderlein 2016). However, for many forms of financing, it is much more difficult to predict who exactly is going to have to pay the costs of these policies and how high these costs will actually be. For example, the distributive consequences of the provision of emergency liquidity assistance or public debt cuts are often opaque and it is unclear which societal group and at what point in time will have to pick up the bill. While generally unpopular, financing measures (with the exception of debt relief) are thus unlikely to produce well-organized and vocal opposition from specific interest groups. Politically, this means that many financing policies are likely to be less contested amongst economic interest groups than adjustment policies with clearer distributive consequences. Finally, policy options are much more limited with regard to external adjustment, where the options revolve only about the level of revaluation and exchange rate regime choice.

Overall, this discussion suggests that we should expect variation in how interest groups evaluate different policy options for internal adjustment and financing, and less variation regarding to external adjustment. Especially concerning internal adjustment – the adjustment strategy for which we expect the position of interest groups to matter most – most policy proposals will garner support from some groups but will also provoke fierce opposition from others. This not only makes internal adjustment a politically difficult strategy to pursue. Stalemates amongst interest groups also mean that policymakers will often feel little pressure to implement policies for internal rebalancing.⁹ Moreover, we expect internal and external adjustment strategies with clear distributive implications to be much more salient for interest groups than

⁹ This is especially the case when domestic economic conditions are good and boosting domestic demand is not a salient issue for voters (Walter et al. 2020).

financing. Taken together, the political difficulties of finding broad consensus on how to adjust internally coupled with large influence of interest groups in this issue area and the possibility of designing financing forms that are acceptable to different domestic stakeholders result in a generally low propensity of surplus countries to adjust internally, even in contexts where opposition to external adjustment is high.

3 Research design

To examine how distributive struggles among different societal interests shaped Germany's policy approach in the Eurozone crisis, we pursue a mixed-methods approach that includes an analysis of original survey data from German interest groups, in-depths qualitative interviews with German interest-group representatives and policymakers, and the analysis of public opinion data.

Much research on the role of societal interests in economic policymaking makes strong assumptions about the preferences of different interest groups, but often uses only broad proxies to operationalize these preferences. We follow a different approach. Rather than inferring policy preferences on theoretical grounds, we conducted an online survey of German interest groups and asked them about their specific policy preferences and reactions to the trade-offs inherent in crisis management. Our population of interest, identified using the German Bundestag register, is 488 interest groups with a minimum of 500 members that represent the interest of a relatively well-defined subset of societal interests that engage in economic or social policy-issues. We contacted heads of specialized divisions such as economics or international affairs, chief executives, or board members via two waves of emails and subsequent reminder phone calls between September and December 2016.¹⁰ 136 interest groups completed our survey, resulting in response rates of 28% which corresponds to typical response rates in interest group survey research (Marchetti 2015). Among the respondents, 56% are employer associations, 32% are professional associations, 7% are trade unions, and 5% are social policy groups. This distribution reflects the overall distribution of economic interest groups in Germany (Dür and Mateo 2013).

We complement this survey data with information from 13 qualitative interviews with interest-group representatives and policymakers. Interest groups were selected based on their size and relevance for the overall economy and represented a wide range of sectors including manufacturing, finance and services, domestic- and export-oriented associations and trade unions including members with different levels of income. The interviewed policymakers were directly involved in economic policy making during the crisis, such as officials in the finance ministry and the ministry for economic affairs and members of parliament in the relevant commissions. Interviews were conducted

¹⁰ We thus conducted the survey after the crisis had calmed down but at a time when discussions over different financing approaches, Eurozone reforms, and macroeconomic imbalances were still ongoing. Nonetheless, several of our questions asked respondents to answer retrospectively about their policy preferences at the peak of the crisis. To ensure that this did not systematically skew the responses, we validated survey answers with press releases, reports, and other interest group publications on similar topics between 2010 and 2015 whenever possible. We did not find any evidence that interest group responses differed due to the timing of our survey. An overview of the documents we used for this purpose can be found in the online appendix (p. 5).

between November 27 and December 8, 2017 in Berlin. A complete list can be found in the appendix (p.6).

4 Analysis

In our empirical analysis, we explore three related questions: a) how German interest groups evaluated different policy options available to achieve external adjustment, internal adjustment, and financing, b) how they chose between different crisis resolution strategies and the inherent trade-offs they pose, and c) how these distributional concerns interacted with ideas and the wider German structural setting to influence German policy choices during the crisis.

4.1 How do interest groups evaluate different policy options?

Our argument suggests that interest groups diverge in how they evaluate these strategies because they represent different societal groups with diverging material interests. To test this hypothesis, we presented interest groups in our survey with a set of possible policies that were discussed in policy circles during the Eurozone crisis as options to achieve a rebalancing or to finance deficit states. Because the policy options for internal rebalancing and financing¹¹ ranged significantly more widely than the policy options for external adjustment, we presented interest groups with five different options for the former and three options of a Eurozone break-up. Table 1 presents the different options interest groups were asked to evaluate on a scale from 1 (strongly oppose) to 5 (strongly welcome).¹²

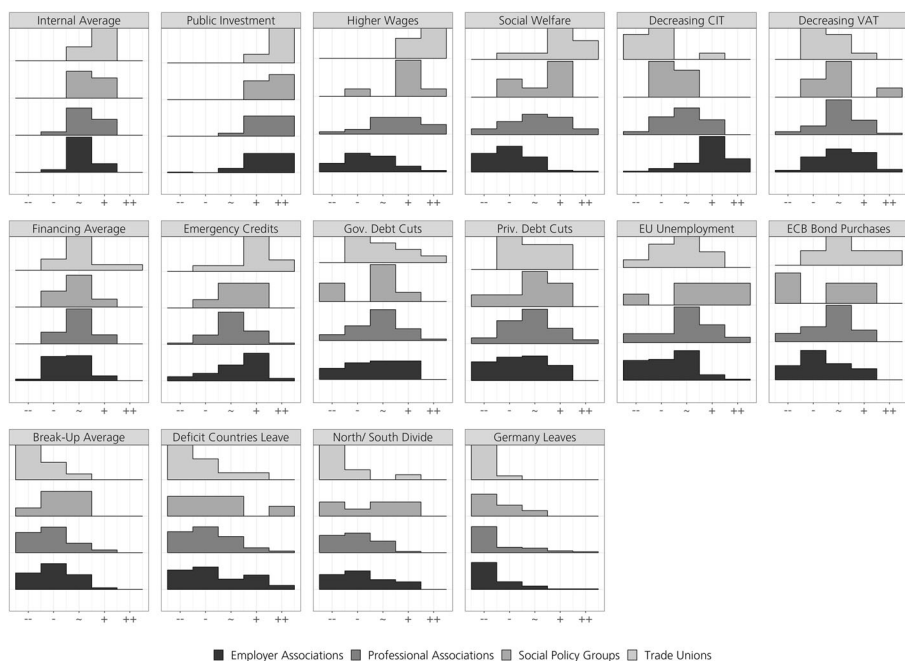
Starting with internal adjustment, Fig. 1 shows an overall support for domestic expansion. When we take the average across all policy options (first row), most interest groups generally evaluate internal adjustment positively. Our interviews with major economic interest-groups reinforce this finding. Interest-group representatives from the two major trade unions DGB and Verdi, but also two employer associations, including the highly export-oriented association of the metal industry voiced concerns about Germany's large current-account surplus (Interviews DE1, DE2, DE7, DE8). Several groups worried about the international implications of the large surplus, including exposure to shocks on foreign markets but also possible political repercussions if Germany failed to reduce the surplus (Interviews DE1, DE2, DE6). Even representatives who rejected the notion that Germany's large current-account surplus contributed to the Eurozone crisis stated that the German economy had underperformed in terms of private and public investment in recent years and voiced support for specific policies that would serve to counter this trend (Interview DE3). Rather than presenting a unified front in favor of continued trade surpluses, most of the actors we interviewed thus

¹¹ Note that we did not quantify and vary the size of domestic expansion policies (e.g. *how* much more public spending) and financing measures (*how* much money is spend on different transfer measures) in order to keep the survey at a manageable length. Previous research has shown that, especially, in the case of financing, the size of bailouts influences support for them amongst voters (Bechtel et al. 2017). While our design does not allow for testing this for interest groups, our interviews did not indicate that the size of the bailouts, debt cuts etc. was a salient issue for organized interests (see below).

¹² Summary statistics for all policy evaluations can be found in the appendix (p.1).

Table 1 Policy options in the survey by crisis strategy

Internal Adjustment Policies	Financing Policies	External Adjustment Policies
Public infrastructure spending ("Expand public investment, for example in education or infrastructure.")	Provision of bailouts ("Provide financial assistance and loans through the European rescue funds.")	Deficit countries leave the EMU ("Deficit countries like Spain or Greece leave the Eurozone")
Higher minimum wage ("Increase low wages, for example by raising the minimum wage")	European unemployment insurance ("Introduce European unemployment insurance.")	Divide into North/South Eurozones ("The EMU divides into a North and a South block with different currencies.")
Public spending on welfare ("Expand public spending on social welfare programs.")	ECB bond purchases ("The European Central Bank purchases government bonds and other assets.")	Germany leaves the EMU ("Germany leaves the Eurozone")
Decreasing VAT ("Reduce the rate of the value added tax")	Haircuts on public sector debts ("Reduce the debt that crisis countries owe the German state as a result of the European bailout packages.")	
Decreasing corporate taxes ("Reduce taxes for companies")	Haircuts on private sector debts ("Reduce the debt that crisis countries owed German private banks at the beginning of the crisis.")	

**Fig. 1** Density plots of policy-specific evaluations of different crisis management strategies

favorable policy adjustment that would increase domestic demand and reduce the surplus.

In line with our expectation that interest groups are likely to evaluate different policy options within the same adjustment strategy differently, however, this general support masks considerable divergence in policy evaluations, especially with regard to internal adjustment and financing. With the exception of more public investment, there are clear differences in interest groups' evaluations of different internal adjustment policies. Whereas, for example, a large majority of trade unions, social policy groups and professional associations viewed a higher minimum wage or more spending on social welfare positively, most employer associations felt that this would be harmful. When it comes to lower taxes for businesses, this picture is reversed. This is also in line with qualitative evidence from our interviews. Both major trade unions we talked to stressed the need to increase minimum wages, to expand the coverage and bindingness of collective bargaining and to re-regulate opt-out clauses and temporary employment contracts (Interviews DE7, DE8). At the same time, they rejected tax breaks for companies or efforts to deregulate the service sector in order to stimulate private investments - the last one being a concern that they shared with representatives of the craft association. Many employer associations, on the other hand, emphasized the expansive effects of corporate tax cuts (Interview DE2), the reduction of red tape in service industries (Interview DE3) or the deregulation of credit provision (Interview DE6). At the same time, most industry groups had fought against the introduction of the minimum wage in 2013 and stated that they would lobby against further attempts to re-regulate labor contracts.

There is one issue that all groups agreed on: the need for more public investment, especially for road and digital infrastructure. However, opinions again diverged on the question how to finance these investments. While trade unions and craft associations demanded financing through public money and possibly new public debts, many employer associations insisted on the introduction of more private-public partnerships, which would also provide new investment opportunities to large institutional investors (Interview DE5, DE8).¹³

We see a similar, though much less pronounced pattern of variation for different financing policies, where the mode is indifference for all financing policies except bailouts, which are evaluated slightly positively. As we will describe in more detail below, our qualitative evidence also supports the finding that most economic interest groups were quite supportive of international transfers.

Finally, variation among interest groups was much more limited with regard to external adjustment: Virtually all interest groups opposed a German exit from the Eurozone, and while there was more variation about the question of whether a deficit country in crisis should leave, all interest groups exhibited a strong preference for avoiding a break-up of the Eurozone. In our interviews, major employer associations and trade unions univocally stated that their members depended crucially on the stability of the monetary union in its current form. Groups in tradable sectors mainly feared that a breakup would lead to unforeseeable exchange rate and market volatilities, disruptions on financial markets, as well as threats to European economic integration

¹³ See also <https://www.wallstreet-online.de/nachricht/9013536-bericht-einigung-fratzscher-kommission-investitions-masterplan>

more generally. They also mentioned the return of trade barriers as a possible long-term consequence of a Eurozone breakup (Interviews DE1; DE2; DE3). However, even non-tradable sector interest groups, such as those focused on retail or construction, emphasized that a breakup would have extensive negative effects on their members. Main concerns were a general depression of the economic climate as well as higher credit and refinancing costs for their members due to insecurity and friction in the financial markets (Interviews DE5).

4.2 What drives differences in policy evaluations?

To what extent do interest groups' material interests explain this variation in policy preferences? To examine how groups' exposure to different strategies explain their preferences, we classify groups according to their main sector of economic activity and use this classification to collect data on two measures of exposure: interest groups' trade dependence and their demand elasticity.¹⁴ A group's trade dependence is measured as the share of the output that it exports to other countries in the Eurozone and proxies the degree to which a group would be hurt by a breakup of the monetary union.¹⁵ For demand elasticity, we assess how much a group would benefit from a general, internal adjustment-related expansion of domestic demand. We focus on the income elasticity of demand for the goods the members of an interest group produce, because it reflects how much increases in aggregate income will affect the demand for a specific good or service. We construct an ordinal variable that ranges from 1 for very inelastic goods (e.g., food and tobacco) to 6 for very elastic goods (e.g., financial services and personal care activities). The higher the income elasticity of demand for the main good an economic group provides, the more it should benefit from internal adjustment.¹⁶ Finally, because different types of interest groups represent groups with different material interests, we additionally include dummy variables that capture if a group is an employer association, a professional association, or a trade-union (the baseline are employer associations). Summary statistics for all variables are shown in the appendix.

Figure 2 summarizes the main findings from OLS regression analyses of the correlates of support for each policy option listed in Table 1.¹⁷ Taken together, our findings suggest that the interest groups' evaluations of crisis policies reflect real material considerations. For internal adjustment, the analyses show that groups which produce goods and services with higher levels of demand elasticity evaluated internal adjustment policies more positively. Hence, the more groups were likely to benefit from an increase

¹⁴ Using the statistical classification of economic activities in the European community (NACE) at the two-digit level, we can differentiate between 99 distinct fields of economic activity. For groups that represent actors from more than one sector, we take the unweighted averages of all the sectors present among their members. Categorizing groups into areas of economic activities is more challenging for social policy groups such as Caritas than it is for sectoral employer associations or professional associations that represent professions in certain sectors such as the German Medical Association. To check for robustness, we therefore rerun the analysis without social policy groups. Table A2.6–A2.8 in the appendix shows that this does not change the results.

¹⁵ Data from the input-output tables provided by the German National Statistical office (Destatis, 2011).

¹⁶ Our categorization is based on several empirical studies (European Commission 2007) and the COICOP categorization of the UN Statistics Division. For details, see Table A2.1 in the online appendix.

¹⁷ Table A2.3 – A2.5 in the online appendix presents full regression results.

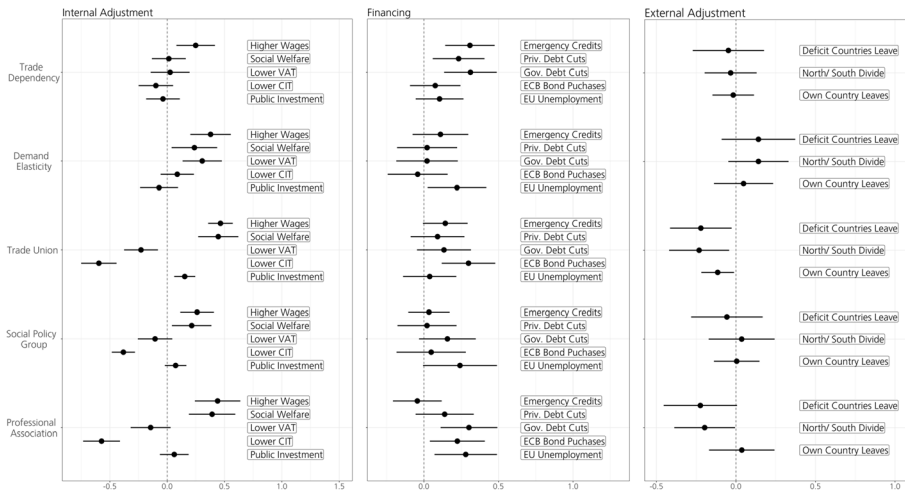


Fig. 2 Effect of interest groups' material exposure on their policy evaluations. OLS Regression coefficients. All variables are standardized; all models include robust standard errors. The baseline category for interest group dummies is employer associations

in domestic incomes, the more they supported internal rebalancing. Moreover, groups' evaluation of different forms of internal adjustment also reflected the material interests of their members. Compared to employer associations, trade unions and social policy groups were more supportive of measures to increase lower wages and social spending, whereas they opposed tax cuts, especially for private companies. Support for such tax cuts was significantly higher among employer associations.

Material interests also underpin support for financing policies. The more groups relied on exports to other members of the Eurozone, the more positively they evaluated various options for providing deficit countries with financial resources. Trade-reliant interest groups were particularly supportive of relief for debt owed to the German state. Trade unions, social policy groups, and professional associations tended to evaluate some forms of financing more positively than industry groups. While some of this could reflect material considerations—for example, trade unions' support for the monetary expansion of the ECB could be interpreted as prioritizing employment over price stability—norms of international solidarity were also likely to play a role, underscoring arguments that both material interests and ideas played a role in the Eurozone crisis.

Finally, counter to our intuition, we do not find that trade-reliant groups are more opposed to Eurozone-breakup scenarios than groups that focus mostly on the domestic economy. As we have seen above, this is likely to stem from the fact that all groups, independent of their market orientation, were deeply concerned about the material repercussions of external adjustment.

4.3 Policy salience

Our argument also suggests that policies that lead to rebalancing through internal or external macroeconomic adjustment are likely to be more salient than financing policies, because the distributional effects of most forms of financing are more opaque and too long-term for interest groups to strongly care about them.

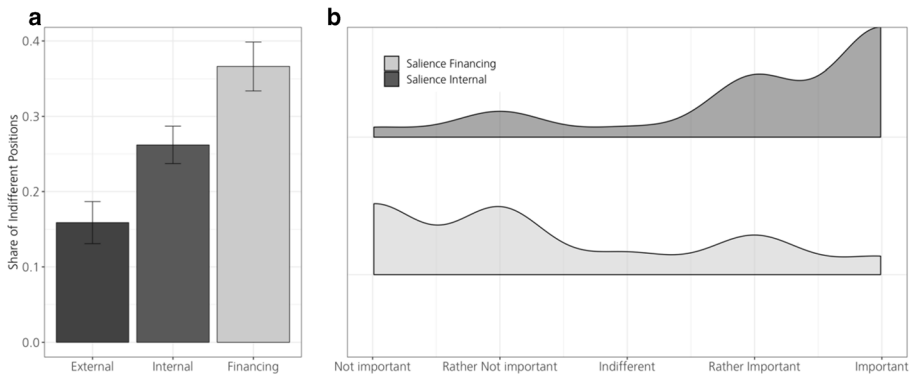


Fig. 3 a Average Share of Policies Groups are Indifferent about, b Salience of Internal and Financing Policies

Fig. 3a confirms this argument. It shows the average share of policies that interest groups were indifferent about for each crisis strategy. Whereas only 16% of interest groups were indifferent about the external adjustment and 26% about the internal adjustment policies included in the survey, over a third (36%) showed themselves as indifferent towards financing measures. To assess policy salience more directly, we also asked respondents how important each policy was for their organization's political work. Fig. 3b shows a stark contrast in salience between internal adjustment and financing.¹⁸ Almost 80% of the groups stated that policies related to internal adjustment were important or rather important for their political work. In contrast, only 19% said the same for financing policies.

Qualitative evidence confirms this picture. While most interviewees supported financial rescue measures, the specificities of the bailout regime or the further steps to institutionalize transfers ranked very low on their political agenda (Interviews DE1; DE2). Even within large and encompassing employer associations—such as the Federation of German Industries (BDI) - there was no formal consultation about the specificities of financing policies. As a representative of a large umbrella association for business groups put it: “The potential costs of these measures were never really thought of or discussed. [...] There are simply 50 other topics that are of much greater importance to our members (Interview DE1).” Similarly, none of the policymakers we talked to could remember major consultations with interest groups about financing measures (Interviews DE9; DE10; DE11; DE12). Finally, this finding is also in line with the results from Kudrna et al. (2018), who show that economic-interest groups had little influence on Germany's positions in European negotiations over bailouts and other financing measures.

4.4 Trade-offs and difficult choices between external adjustment, internal adjustment, and financing

Until now, we have studied interest groups' evaluations and the salience of different forms of internal adjustment, external adjustment, and financing separately. However, crisis politics needs to be understood as choices among trade-offs. As we have argued

¹⁸ Because of space constraints, we only asked these questions about internal adjustment and financing.

above, the preferences and political strategies of different economic groups in the crisis are likely to be driven by how they weigh the costs and benefits different strategies against each other. This is especially important in a setting in which groups strongly disagree about the desirability of different policy options within each strategy. As this makes it difficult to implement forms of domestic expansion or financing suiting everybody's interests, understanding what drives decisions between costly alternatives is crucial.

To explore policy choices constrained by the trade-offs inherent in crisis management, we therefore asked interest groups in a second step to choose between different crisis response packages that embodied these trade-offs. For this purpose, we constructed two different choice sets in which respondents had to choose between three policy packages that correspond to internal adjustment (internal adjustment policies, limited financing, and no external adjustment), external adjustment (no internal adjustment, no financing, and external adjustment, i.e., a breakup of the Eurozone), and financing (no internal adjustment, extensive financing, and no external adjustment). The packages were customized for each interest group individually. For this purpose, we asked respondents in the first part of the survey to not only rate but also rank the different policies within each crisis strategy from their most to their least-preferred option. We then used these rankings to build customized policy packages. A first choice-set included only those policies in the respective strategy that each interest group had evaluated most favorably. The scenario thus illustrates the kind of strategies groups prefer when the adjustment trade-offs are relatively mild. The second set, however, confronted respondents with a much more difficult choice; it included only bad options—that is those policies that interest groups opposed most strongly. Figure 4 shows how the different packages were presented to respondents. Respondents' choices of their preferred package in each of the two scenarios are used to generate two categorical variables: one that records interest groups' preferred crisis strategy in a less constrained and one that records their choice in a highly constrained context.

Fig. 5a shows the distribution of choices in each of the two scenarios. On the left-hand side we see interest groups' preferred crisis strategies when the policy packages include those policies they prefer most. Under these circumstances, we find that an overwhelming majority of groups would favor internal adjustment. 67% of interest groups in our sample support internal adjustment tailored towards their preferences, whereas less than 20% chose financing and less than 10% a breakup of the monetary

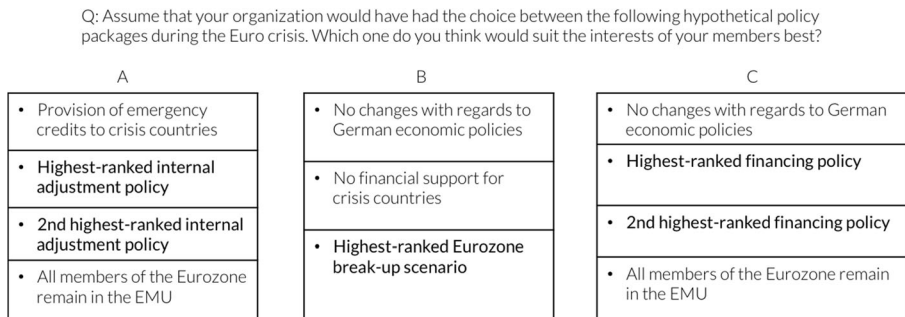


Fig. 4 Customized construction of choice set for the three different crisis strategies

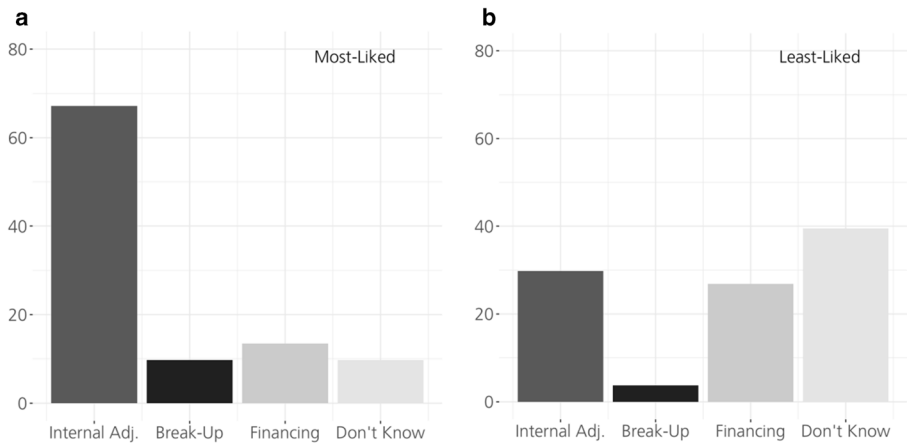


Fig. 5 a: Choices between most-liked Adjustment Packages, b: Choices between least-liked Adjustment Packages

union, even if these strategies equally contain their most preferred financing and external adjustment policies.

This picture changes dramatically in the highly constrained scenario, where interest groups are confronted with difficult trade-offs (Fig. 5b). When interest groups have to choose between crisis strategies that contain their least-preferred policies, only 30% of respondents remain supportive of internal adjustment. At the same time, even fewer groups select a breakup of the Eurozone (typically a German exit from EMU), and financing becomes significantly more attractive. When the trade-offs are difficult, interest groups also find it much harder to voice clear preferences, as the high number of “Don’t know” shows. Taken together, these changing patterns of support suggest that interest groups are finely attuned to the distributive consequences of different possible crisis policies. They are not fundamentally opposed to internal rebalancing of the economy, but show little enthusiasm for it if internal adjustment contains policies that they oppose.

We next explore how interest groups’ policy-specific preferences shape their crisis strategy choices in difficult trade-off situations. Interest groups are likely to form their crisis preferences based on the relative net costs or benefits of internal and external adjustment and financing, respectively. As long as groups benefit from the specific internal adjustment policy under consideration, we expect them to support domestic rebalancing. Financing, on the other hand, should become attractive when interest groups are confronted with trade-offs between forms of internal and external adjustment to which they are particularly opposed.

To examine this argument, we focus on choices between internal adjustment, financing and don’t know in the constrained trade-offs scenario, in which groups have to choose between crisis strategies that contain their least-preferred policies. As not even 4% of our respondents chose a Eurozone breakup in the least-preferred scenario, we do not model choices for external adjustment. We recode our dependent variables into dummy variables that take the value of one if a group chose an option and zero if it did not. As our analysis has shown that interest groups’ policy evaluations are related to their material interests, we assume that groups would benefit from policies they support and are vulnerable to policies they oppose. This allows us to proxy interest groups’ policy-specific vulnerabilities with their ratings of their least-preferred policies. To

Table 2 Probit Regression: Likelihood of choosing adjustment strategies with least-liked policies.

	Adjustment Choice - Least-Liked Packages		
	Internal (1)	Financing (2)	Don't Know (3)
Average Rating lowest ranked internal adjustment policies	0.919*** (0.216)	-0.602*** (0.214)	-0.056 (0.188)
Rating of all other internal adjustment policies	-0.385 (0.286)	0.301 (0.315)	0.070 (0.261)
Average Rating lowest ranked external adjustment option	-0.343 (0.312)	0.307 (0.250)	0.046 (0.236)
Rating of all other external adjustment options	-0.357** (0.168)	0.035 (0.154)	0.041 (0.153)
Market Liberalism	-0.181 (0.155)	0.064 (0.178)	-0.024 (0.151)
European Integration	-0.091 (0.172)	0.422** (0.185)	-0.181 (0.136)
Professional Association	-0.669 (0.417)	0.308 (0.376)	0.156 (0.309)
Trade Union	-0.245 (0.577)	0.203 (0.606)	-0.115 (0.625)
Social Policy Group	-0.247 (0.477)	-0.524 (0.621)	0.483 (0.573)
McFadden R-Square	0.22	0.13	0.027
Observations	103	103	103

* $p < 0.1$; ** $p < 0.05$; *** $p < 0.01$

all models include robust standard errors.

make sure that our findings are not driven by a group's general position towards internal and external adjustment, we control for their average evaluations of all remaining policy options within each crisis strategy (i.e., all policies except the most disliked one(s)). We additionally control for the type of interest group as well as the organization's general opinion about European integration¹⁹ and their overall attitude towards the role of the state in the economy.²⁰

Table 2 presents the results of probit regression analyses of the choice of internal adjustment (models 1), financing (models 2) and don't know (model 3) when faced with difficult trade-offs. The results show that interest groups' support or opposition to specific policies are, indeed, related to their choice of crisis strategies. The more opposed

¹⁹ "Now thinking about the European Union, some say European integration should go further. Others say it has already gone too far. Where does your organization stand on this question?" (1 "Has gone too far"; 5 "Should go further").

²⁰ "Whether the government should actively intervene in the economy and regulate the economy or whether economic processes should be left to the market only is a fundamental economic policy question. Where does your organization stand on this question?" (1 "Comprehensive interventions"; 5 "No interventions at all")

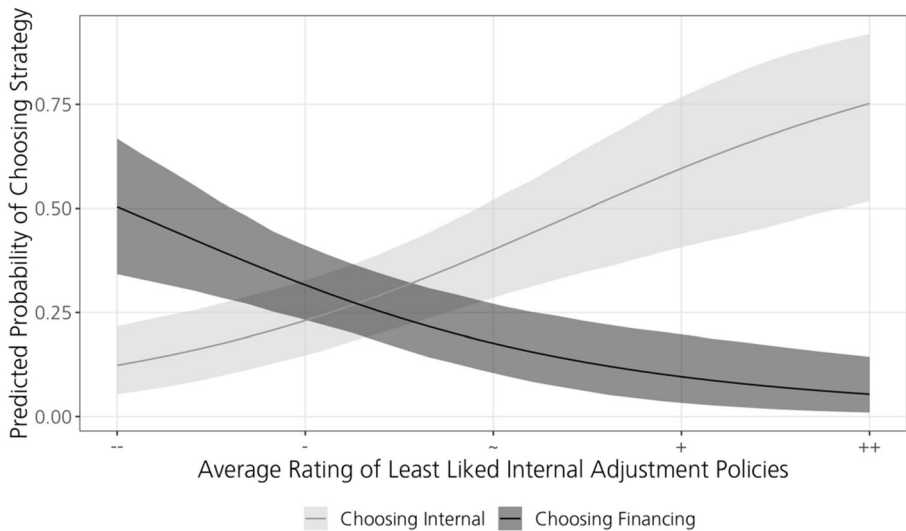


Fig. 6 Predicted probability of choosing internal adjustment and financing at average ratings of least-liked internal adjustment policies. Based on Model 3 in Table 2

groups are towards the specific internal adjustment policies in question, the less likely they are to support domestic expansion. In contrast, the rating of the least-liked external adjustment strategy (usually German exit from the Eurozone), offered as an alternative, does not have any effect on this choice. This is likely related to the fact that an overwhelming majority of interest groups oppose such a policy. Finally, interest groups' evaluations of the other internal adjustment policies do not have an effect. While this is perhaps not surprising given that these policies are not on offer, it suggests that the choice of internal adjustment is not driven by a general support for internal rebalancing. Interestingly, neither interest groups' evaluation of European integration nor of state interventions make interest groups more likely to support internal adjustment.

Turning to financing (model 2), we expect that this should be an attractive alternative for groups who are opposed to both external and internal adjustment. Indeed, we find that the more opposed an interest group is to the specific internal adjustment policies at offer, the more likely it is to choose financing as its preferred crisis strategy, but the rating of the least-liked external adjustment policy once more has no effect. We also do not find a significant effect of interest groups' rating of those internal and external adjustment policies not included in the policy packages. However, a general support for European integration is positively correlated with the likelihood of choosing financing. All findings remain unchanged when running multinomial logistic instead of probit regressions (see Table A3.1 on p.5 in the appendix).

To facilitate the interpretation of these results, Fig. 6 plots the predicted probabilities of choosing internal adjustment and financing across different levels of opposition towards interest groups' respective least liked internal adjustment policies.²¹ Groups that are generally supportive even of their least-liked internal adjustment policies have a predicted probability of about 75% of selecting internal adjustment but only of 7% for

²¹ To avoid fixing the organization type to an arbitrary category, the model for the predictions does not include organization type fixed effects. However, including such effects leaves the results substantially unchanged.

choosing financing as preferred crisis strategy. Results are turned upside down for groups who strongly oppose the internal adjustment policies under consideration. For these groups, the predicted probability of selecting internal adjustment lies only at about 10% whereas the likelihood of supporting financing rises to more than 45%. The probability for a group to prefer financing over other crisis responses is thus larger the more opposed it is to the specific form of internal adjustment under consideration.

In sum, our analysis of the interest-group data shows that a majority of groups prefers internal adjustment over other possible crisis responses, but only as long as this domestic expansion is achieved through policies that serve their interests. The costs and benefits – and hence the evaluations – of different internal adjustment policies, however, differ across groups. When trade-offs become difficult, the picture is far less clear and opposition to specific internal adjustment policies is then also associated with more support for financing, even in its unpopular variants. Moreover, a large majority of groups is strongly opposed to external adjustment.

5 Political implications of the interest-group findings

What does this imply for the politics of non-adjustment, to what extent are our findings generalizable, and how do our findings tie in with existing research on surplus countries in the Eurocrisis? In this last section, we discuss these questions for both domestic and European-level politics.

5.1 Implications for the domestic politics of German (non-)adjustment

The interest group analysis provides two important insights for domestic politics: First, distributional conflicts about how to rebalance the economy foreclosed concerted efforts amongst interest groups to push towards an encompassing program of internal adjustment.²² Whereas during the crisis years, Germany, did implement some limited forms of domestic expansion – above all the introduction of a general minimum wage (Mabbett 2016; Marx and Starke 2017) – several interview partners mentioned that a stalemate among interest groups about how to boost domestic demand prevented organized interest from pushing for more encompassing measures (DE1; DE7; DE13). This was especially relevant as the benign economic climate in Germany resulted in low salience of economic issues for German voters (Steinbrecher 2014; Walter et al. 2020). Debates about the current-account surplus and possible adjustment policies, thus, took place mainly among a small circle of political experts and organized interests, in which distributional conflicts about the microeconomic effects of various adjustment measures often inhibited meaningful reforms (DE1). In the end, the two coalition governments during the crisis, for example, fewer tax reforms than had any other German government (Rixen, 2019) and many proposals on public spending, expansionary labor-market as well as service sector reforms were swiftly scooped off the political agenda (DE13; Bandau and Düming, 2015).

²² For more details on how distributional conflicts about specific policies blocked economic reforms that could have contributed to internal rebalancing see Walter et al. 2020.

Second, the clear opposition towards external adjustment coupled with the low salience of financing policies among interest groups, made international transfers politically attractive. In fact, we find that economic groups were quite open even to disliked options of interstate transfers. So why was the German government's approach to financing rather restrictive and tied to strong conditionality (Schneider 2018; Schneider and Slantchev 2017)? One explanation is that the German political elite was influenced by ordoliberal ideas, which made them very reluctant to engage in more generous financing schemes (Brunnermeier, James, and Landau 2016; Bulmer 2014; Matthijs 2016). Another, complementary, explanation is the reluctance of voters to support such a strategy (Bechtel et al. 2014; Schneider and Slantchev 2018). Using representative public opinion data from 2010 to 13, Fig. 7 shows that more than 70% of Germans were generally against financial support for highly indebted countries. Opposition was even stronger when asked about concrete measures such as the expansion of the European rescue funds and the introduction of Eurobonds and, importantly, this rejection was universal across party lines. Moreover, while financing was of little importance for interest groups, they did matter a great deal to voters. When asked in 2013, more than 85% noted that the management of the Eurocrisis would matter or even matter a lot for their electoral decisions. The issue was thus more important than some domestic issues such as for example tax policies (Jung et al. 2015). Importantly, our interviews also showed that policymakers were acutely aware of this popular opposition and described it as one of the main reasons against more encompassing approaches to financing (DE9; DE10; DE11; DE12).

At the same time, however, the German public shared interest groups' desire to keep the Eurozone together (see Fig. 8). With the exception of Greece, a large majority of voters was against any deficit country leaving the common currency. Similarly, almost three quarters thought that returning to a national currency would be bad for Germany. While German voters were deeply skeptical about interstate financing, they showed little appetite for external adjustment either (Jung et al. 2013, 2014).

Taken together this suggests that German crisis politics were caught in a difficult spot. External adjustment was off the menu, internal adjustment was hampered by distributional conflicts amongst interest groups and financing was extremely unpopular amongst German voters. To a certain extent, our finding thus help to understand not only Germany's reluctance to adjust its own economy but also its hesitant, biding and piecemeal approach to the management of the European financing and bailout regime crisis more generally.

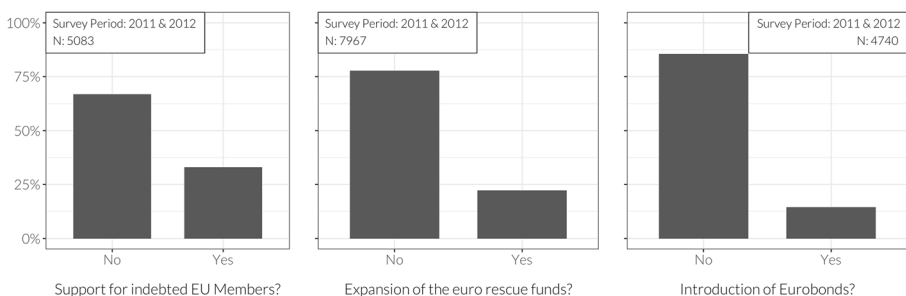


Fig. 7 German public opinion about financing. Data from Jung et al. (2013, 2014)

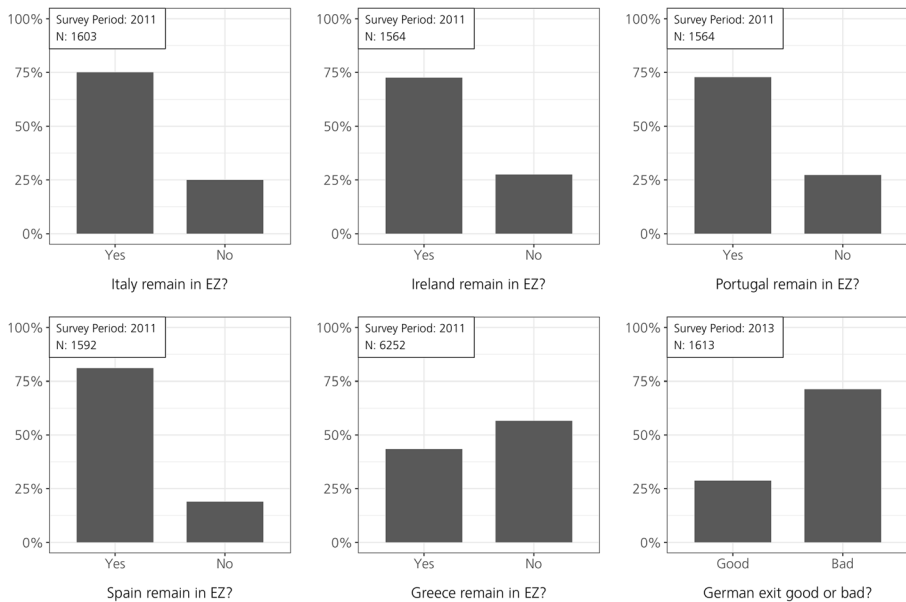


Fig. 8 German public opinion on external adjustment. Data from Jung, Schroth, and Wolf (2013, 2014)

5.2 Implications for European crisis management

An obvious question is whether our analysis highlights Germany-specific dynamics or whether it generalizes to other surplus countries. To explore this question, this last section presents a brief analysis of interest group preferences in the two other main surplus countries in Eurozone: the Netherlands and Austria. Figure 9 presents similar analyses of strategy choices of 105 interest groups in Austria and 116 in the Netherlands (for more details, see Walter et al. 2020). The patterns are strikingly similar to the ones observed in Germany. A large majority of Austrian and Dutch interest groups prefers their most-liked form of internal adjustment over any other crisis response. However, this support collapses as soon as internal adjustment contained groups' least-liked policies. In the difficult trade-off scenario between unpopular options, financing once more becomes more popular, and many groups like in Germany switch into the “don't know” category. This suggests that distributional issues are likely to make internal adjustment politically difficult to achieve in surplus states more generally.

What do these findings imply for Eurozone crisis management at the European level? Existing work has highlighted that surplus countries held very similar positions during the crisis (Walter et al. 2020; Wasserfallen and Lehner 2018). While Germany was a key actor, countries like Finland, Austria or the Netherlands shared its rejection of internal adjustment and harsh stance on financing (Armingeon and Cranmer 2017). This homogeneity of positions facilitated coalitions building amongst creditor states and added to their political leverage in European bargaining about crisis resolution strategies (Schimmelfennig 2015). In line with our analysis, surplus countries were particularly successful in securing

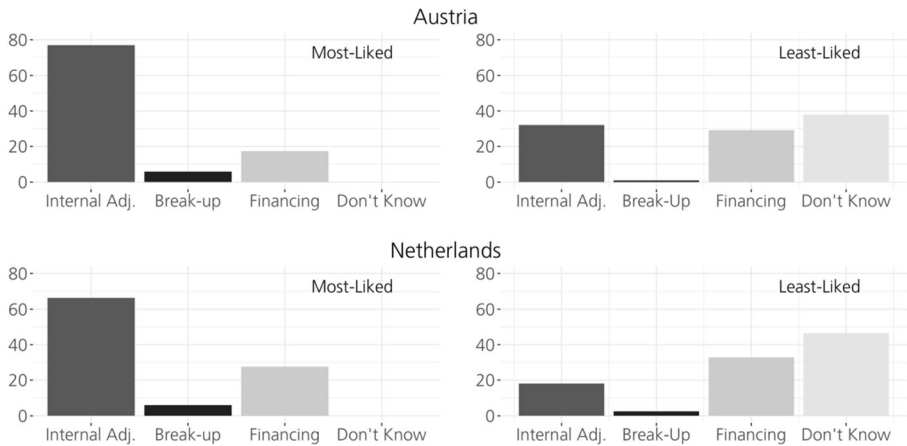


Fig. 9 Choice between most-preferred (left) and least-preferred (right) crisis strategies in Austria ($n = 105$) and the Netherlands ($n = 116$)

European-level decisions that limited the amount of internal adjustment expected of surplus countries and pushed the internal adjustment burden more squarely on the shoulders of deficit countries, but were more willing to compromise on issues related to financing (Walter et al. 2020). Our argument suggests one source of surplus country homogeneity and ultimately negotiation success: If distributional conflicts around the specificities of internal adjustment were similar in other surplus states, this – together with similar ordoliberal ideas and export-oriented economic models – explains why none of these countries broke rank and called for a more balanced approach to adjustment.

6 Conclusion

Germany's and other surplus countries' reluctance to rebalance their current-account and to contribute to international burden-sharing in times of debt and current-account crises remain a key challenge to the political and macroeconomic stability of the Eurozone and the global economy more generally. In this paper, we highlight a new and important aspect underlying the politics of non-adjustment surplus countries. Leveraging the case of Germany in the Eurocrisis, we use original survey data and in-depths interviews, to show that, although there was strong general support for strengthening domestic demand, different groups disagreed heavily about how to achieve this goal. Distributional conflicts about the specificities of internal adjustment, therefore, have made internal adjustment politically difficult to achieve, even in a context where the potential costs of external adjustment have effectively ruled out any other solution but financial transfers from surplus countries to deficit states.

These findings have a number of political and theoretical implications. First, they add to our understanding of the political factors that hampered a more balanced and effective management of the Eurozone crisis. Given that the one-sided approach to the

balance-of-payments problems in the Eurozone have remained a political bone of contestation until today, understanding the political conflicts that have shaped the positions of surplus countries on these issues is crucial for both academics and policymakers. Second, our evidence suggests that the German current-account surplus is less structural than it is often assumed. The findings presented in the paper show that it would be possible for countries like Germany arrive at a more balanced current-account by designing packages of internal adjustment that garner broad-based political support. As we emphasize above, this is by no means an easy task and will require difficult compromises. But our evidence points to the fact there is nothing that dictates countries like Germany to run surpluses at the current magnitude. For the Eurozone, this is good news.

Finally, our findings also have important implications for studying the political economy of balance-of-payment crises and global imbalances more generally (Broz et al. 2016; Frieden and Eichengreen 2001; Kinderman 2008; Eichengreen 1992a; Simmons 1997; Walter 2013).²³ So far, research on these issues has been characterized by a one-sided focus on the role of deficit states. However, our evidence from Germany, Austria and the Netherlands suggest that distributional conflicts within surplus countries play a similarly crucial role in the build-up and maintenance of financial imbalances. Given that these conflicts made it difficult for surplus countries to rebalance even in a highly institutionalized setting such as the Eurozone crisis, in which both political and economic pressures were high, suggests that rebalancing in “normal times” is not an easily achievable policy goal. Understanding these conflicts and how they play into the stickiness of large current-account surpluses in more detail will thus be crucial for arriving at a better understanding of the drivers of global financial imbalances.

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