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Book Review — Digitized Version

[Book Review of] Lange, Thomas ... The economics of German unification: an introduction Cheltenham, Elgar, 1998

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nounced heterogeneity of the countries concerned. *Anja Hochberg* comes in principle to similar conclusions by applying the theory of optimum currency area to the two Germanies and to the EMU member countries, respectively. According to her, only a few of these countries fulfil the necessary criteria for a monetary union and a lot of institutional restructuring, e.g. on the labour markets, still has to be done in order to overcome heterogeneity and inflexibility. However, she sees integration not only as a shock, but also as a chance to revise old institutional and economic structures. Whereas this chance went by in Germany without bringing urgent reforms on the way, it is not yet too late for EMU.

Taking a general look at the book, it can be considered a useful reminder of crucial policy questions in the east German transition process. It hits many sore points, especially concerning the challenge of the German economic model in the aftermath of unification, which seemed to be very successful in past decades, but which failed to acknowledge that reforms were overdue. The extremely broad perspective, however, often causes a loss of structure and blurs the actual target of the book: Is it meant to give a general ideological controversy or rather concrete policy recommendations for a viable adjustment process in east Germany? Because it mixes both, it remains vague in its message. Considering this, it can be recommended to readers who intend to pick certain aspects of unification and get induced to critically reflect them. But those who expect that the pieces of the puzzle called "east German transition", which are presented in the book, would in the end come together to form a picture might find themselves disappointed.

Katja Gerling

Lange, Thomas, and Geoffrey Pugh, *The Economics of German Unification: An Introduction*. Cheltenham 1998. Edward Elgar. XXIII, 209 pp.

Thomas Lange and Geoffrey Pugh discuss German unification, dealing with problems of economic development in the first five years as well as investigating its wider repercussions and medium- to long-term perspectives. They should be well qualified for this undertaking, as both are teaching economics not only in the UK, but are also holding appointments in transition countries, Thomas Lange in Romania and Geoffrey Pugh in both Poland and Albania. The book intends to serve a variety of different interests and readers: those who may be looking for business opportunities created by unification, those who are studying other countries in transition, those who are designing economic policy or are in the business of consulting on it, those who may be interested in the fiscal consequences of economic and monetary integration, those who may be interested in the implications for trade and finance in the European Union and those who may be interested in the feedback effects of unification on western Germany.

Chapters 1 to 8 cover all major macroeconomic, microeconomic and institutional, historical and international issues related to unification and transition. Though the introduction is lengthy – devoting between half a page or even two pages to each of the following chapters – the reader may be appeased when figuring out that the introduction mainly collects the introductory paragraphs of each chapter.

Chapter 1 discusses unification as a major macroeconomic shock for the east German economy, the J-curve of economic reform, the fiscal consequences and the similarities as well as the differences to other countries in transition. Chapter 2 and 3 are retrospective. Chapter 2 sets out to explain east Germany's economic backwardness and its difficulties to overcome it by the inability of the socialist system in dealing with product and market complexities. However, the extensive theoretical treatment for making this largely uncontroversial point seems to be somewhat out of proportion, especially

as it is not specific to unification. Chapter 3 compares the currency union of 1948 with that of 1990. The case of 1948 is dealt with very extensively, probably more than it would have been necessary to make the point, namely that measures taken in 1948 and 1990 were very similar in spite of economic conditions which were starkly different.

Chapter 4 on restructuring and privatization discusses the role of the Treuhandanstalt as the most important single instrument for transition. It suggests that more rigorous employment and investment guarantees and more active restructuring might have improved the employment and investment outcome of privatization, yet it does not recognize that this strategy may have backfired, deterring investors rather than attracting them.

Chapter 5, mostly descriptive, discusses labour market consequences of unification and identifies productivity, namely labour productivity, as the key parameter to solve employment problems. Chapter 6 is probably the most interesting one, elaborating on the role of factor prices for the process of adjustment and catching-up. Specifically, it discusses a two-phase, high-wage, high-tech strategy to preclude a low-wage, low-tech path of development for east Germany and to promote convergence with west Germany on a high level of income. However, it clearly points out that this strategy may be risky as it crucially hinges on wage moderation in the second phase – which may not be brought about at the appropriate point in time or in the appropriate size.

Chapter 7 compares initial forecasts on catching-up from various sources with empirical evidence and discusses the prospective course of development. Chapter 8 discusses the impact of currency overvaluation resulting from a tight monetary policy in order to offset the effect of fiscal expansion on international competitiveness and the impact of unification on monetary cooperation within the European Union. Reading through the eight chapters, one recognizes that the interests best served are those in economic policy design, especially those in labour market policy.

Chapter 9 reviews lessons and presents conclusions. The authors emphasize political failures – early denying the necessity to make sacrifices on part of political actors in order to finance unification and making a misleading historical comparison between 1948 and 1990 – as reasons for an increased long-term cost of re-establishing national unity. They point to the importance of guaranteeing the stability of property rights as the key institutional precondition for a high level of investment which has been severely impeded by the principle of restitution. With respect to labour market adjustment, they conclude that active labour market policies have proved costly and insufficient. Rather, wage moderation is necessary now in order to boost profitability and investment so as to establish more (high-tech) equipment needed to employ the workforce at the prevailing wage level. A high-wage, high-tech strategy of adjustment is also seen as a superior instrument for upgrading workforce qualification via learning-by-doing rather than via conventional training schemes in the framework of active labour market policy.

With respect to integration on the European scale, the authors point out that any unexpected event as for instance German unification could result in a major asymmetric shock which may be difficult to absorb when exchange rates are fixed. Therefore, monetary union should not be driven by a political agenda. Finally, they discuss unification as a trigger for wide-spread institutional changes boosting all-German competitiveness. This scenario, however, which is presented as a long-term perspective on the effects of unification, seems to be too optimistic, at least from the point of view of 1998.

In all, this monograph is a valuable addition to the so far only modest niche of English literature on German unification. It gives a comprehensive account of unification: it gathers empirical findings, offers theoretical treatments – originating both from the already existing literature and from the authors' own research – and presents discussion-provoking hypotheses on economic policy design.

Birgit Sander