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## The postwar West German economic transition: From ordoliberalism to Keynesianism

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**INSTITUT FÜR WIRTSCHAFTSPOLITIK  
AN DER UNIVERSITÄT ZU KÖLN**

The Postwar West German Economic Transition:  
From Ordoliberalism to Keynesianism

by

*Johannes R. B. Rittershausen*

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## *Abstract\**

The Federal Republic of Germany has experienced a fundamental shift in economic philosophy from Ordoliberalism to Keynesianism. This paper elucidates the main tenets of both schools of thought and their eventual influences on economic policy from 1945 through the late 1960s. West Germany's transition to Keynesianism follows a relatively cohesive narrative, as the complexities of event history resonate to similar effect in academic and political spheres. By the end of this investigation, intellectual quagmires surrounding economic successes of the postwar period appear as the logical consequences of an academic community that underestimates the importance of normative economic philosophy for policy implementation and society writ large. Reconnecting historical narrative with economic philosophy thus serves in a dual capacity, clarifying a particularly controversial period in economic historiography while also illuminating the underlying problems of our present circumstance.

*A year after I started this project under the auspices of the Flynn Grant from Georgetown University's Center for German and European Studies it is finally finished, and only then because of the invaluable assistance of numerous kind individuals. In Cologne, Germany, the Institut für Wirtschaftspolitik facilitated my summer research agenda, with special gratitude extended to Benedikt Langner, Philipp Paulus, Vera Streibel, Steffen Roth and a cadre of harried yet ever so patient librarians. Holger Wolf and Marcelo Resico motivated my original ideas and have repeatedly proved to be founts of boundless advice and knowledge. Jost Dülffer, Roger Chickering and Richard Kuisel also contributed many helpful comments on the final drafts. Gisela and Mattias Driesch deserve more than a byline of thanks for their endless hospitality and support. Views expressed by this paper reflect those of the author alone.*

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# *Table of Contents*

	<i>Page Number</i>
<b>1. Introduction</b>	<b>4</b>
<b>2. Intellectual Quagmires</b>	<b>4</b>
<b>3. Philosophical Underpinnings</b>	<b>9</b>
3.1. Ordoliberalism	9
3.1.1. Competitive Markets and Monopoly Power	9
3.1.2. Stable, Functioning Prices	11
3.1.3. Social Policy and Government Intervention	12
3.1.4. Conclusions	15
3.2. Keynesianism	15
3.2.1. Employment Theory and Business Cycles	16
3.2.2. Fiscal Demand Management	17
3.2.3. Prices, Wages and Money	18
3.2.4. Conclusions	19
3.3. Ordoliberalism and Keynesianism	19
<b>4. The Economic Historical Record</b>	<b>20</b>
4.1. Time Period 1: (1945-1948) “Original Debate”	20
4.1.1. Historical Situation	20
4.1.2. Academia	20
4.1.3. Politics	22
4.2. Time Period 2: (1948-52) “Social Market Economy”	25
4.2.1. Historical Situation	25
4.2.2. Academia	26
4.2.3. Politics	28
4.3. Time Period 3: (1952-1960) “Wirtschaftswunder”	29
4.3.1. Historical Situation	29
4.3.2. Academia	31
4.3.3. Politics	35
4.4. Time Period 4: (1960-1970) “Keynesianism”	38
4.4.1. Historical Situation	38
4.4.2. Academia	40
4.4.3. Politics	41
4.5. Summary	44
<b>5. Conclusions</b>	<b>45</b>
5.1. How should one account for West Germany’s postwar economic success and its subsequent decline to a “Welfare State”?	45
5.2. The transition from Ordoliberalism to Keynesianism	46
5.3. What lessons are there for today?	47
<b>6. Translation Endnotes</b>	<b>49</b>
<b>7. Bibliography</b>	<b>52</b>

## 1. Introduction

Few periods in history are as intellectually challenging as mid-twentieth century Germany. Powerful associations of world war, totalitarian regime and atrocity resonate beyond their immediate temporal circumstance, informing scholarship across the disciplines. For German economists, 1945 initially presented a destroyed nation, territorially divided, razed of infrastructure, and condemned for heinous crimes. Consequently, founders of the new West German state shared a historical imperative, each cherishing the opportunity to re-form a stable and just society.

Shared goals, however, did not translate into an operational consensus. Instead, two broad academic conceptions formed, which promoted divergent visions of the optimal economic order. In previous decades this argument often evolved from the ends of the philosophic spectrum, manifested as bitter spats among *laissez faire* liberals, communist-leaning socialists and their various partisan offshoots. Post-Hitler, the radical economic doctrines of extreme free-marketers or collectivists held little appeal. As the scholar Walter Eucken wrote:

The argument today is not at all that between laissez-faire and economic planning. It is not a matter of conflict about whether the state should interfere only a little or somewhat more. Actually the defenders of laissez-faire have completely disappeared. The conflict is a different one. One side, to which I belong, is of the opinion that the state must influence, or even directly establish, the forms and institutional framework within which the economy must work. It should, however, avoid the attempt to steer directly the everyday business of the economy. Others believe that the state must not just establish the framework, but must influence the day-to-day working of the economy on the basis of central planning.<sup>1</sup>

The two “moderate” philosophic approaches, known loosely as Ordoliberalism and Keynesianism, were distinguished by the extent and manner of government involvement in daily economic life. This paper examines these two schools of thought and their influences in the first two decades of the Federal Republic of Germany (FRG). By elucidating the philosophic transition of economic policymaking from Ordoliberalism to Keynesianism in both academic and policy realms, interested observers are afforded a clearer lens through which to interpret postwar German economic history and its numerous intellectual quagmires.

## 2. Intellectual Quagmires

Despite an unenviable starting situation, West Germany’s reconstruction efforts rapidly proved to be an unequivocal triumph. As early as the mid 1950s, the German economy was a phoenix resurrected.<sup>2</sup> Postwar economic successes, however, remain academically problematic. How should one account for West Germany’s swift economic renaissance? Are there lessons from that time period for today? Scholars responded to such questions with a surfeit of diverse literature. Text, for example, often focused on the influential

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<sup>1</sup> Eucken, 1950; in Nicholls (1994, pp. 185)

<sup>2</sup> Ludwig Erhard (1958: 232) wrote of the German economy: “The phoenix arises from its ashes.”

roles of outsiders (viz. the Americans) in the Federal Republic's economic gestation<sup>3</sup> and, similarly, to West German development within the European project.<sup>4</sup> Without discounting the importance of exogenous variables during the reconstruction period and after, West Germany's internal economic development occupies perhaps the most contentious intellectual battleground.

A primary departure point in postwar German economic historiography concerns authors' treatment of the National Socialist period. Initially, economic rationale followed the broader *zeitgeist* of 1950s and 60s West Germany.<sup>5</sup> For many, the catastrophe of WWII and the Nazi period erased previous ideology, government and infrastructure, providing a *Stunde Null* or "Zero Hour" situation in which to completely refashion economic society. Ludwig Erhard, the putative "father" of the *Soziale Marktwirtschaft* (Social Market Economy), frequently contrasted the "old hierarchy" and its material and moral deficiencies with his new brand of "prosperity through competition." (Erhard, 1958: 1) The stunning success Erhard attributed to the liberalized market economy presupposed a new beginning, overcoming repression with an order that was wholly distinct. As long as the economic "Wirtschaftswunder"<sup>6</sup> flourished, so did the *Stunde Null* historiography.<sup>7</sup>

In 1955, Henry Wallich published the *Mainsprings of the German Revival*. Wallich attributed the still nascent economic recovery to a mix of international movements (viz. East-West geopolitical tensions), remaining postwar factor endowments (such as high human capital), and finally, the auspicious economic policies of Allied and German authorities. He stressed a fundamentally new order of competition or "free market policy" including its positive influences on growth, price stability, employment, and trade surpluses. Linkages between periods, whether during Weimar or National Socialist regimes, were not significant variables, except as pedagogical reminders of what deliberative policy and fortuitous occurrence could overcome.

In the late 1960s and early 70s, "continuity" emerged as a hotly debated theme. In 1967, the esteemed volume *The German Economy, 1888 to the Present* by Gustav Stolper was posthumously republished with addendum contributions by Knut Borchardt and Karl Häuser. It was an attempt to link, at least chronologically, events on both sides of Hitler's

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<sup>3</sup> Prominent examples include Volker Berghahn's (1986) *Americanization of West German Industry*, Milward's (1984) investigation of British participation in reconstruction, a superb collection of essays edited by Junker (2004) on the United States and Germany from 1945-1990, and extensive clashes over the Marshall Plan, perhaps best summarized in a volume edited by Maier and Bischof (1991). For a comprehensive investigation of the Western Allied powers' economic relations with their zones and West Germany's eventual reintegration into the world economy see Buchheim (1990).

<sup>4</sup> See Postan's (1967) *An Economic History of Western Europe*; Laqueur's (1992) *Europe in Our Time*; and the investigation of *Coal, Steel and the Rebirth of Europe* by Gillingham (1991).

<sup>5</sup> The overall gestalt was to downplay the Nazi period in society and politics. See Frei (2002) for a thorough account of the FRG's attempt to "overcome the past" through a concerted *Vergangenheitspolitik*.

<sup>6</sup> It should be noted that Erhard did not favor the "miracle economy" interpretation. "What has taken place in Germany during the past nine years is anything but a miracle. It is the result of honest efforts of a whole people who, in keeping with the principles of liberty, were given the opportunity of using personal initiative and human energy." (1958: 116)

<sup>7</sup> See Arndt (1966) for another "*Stunde Null*" history written in this period.

rule. In and of itself, this presented a challenge to the *Stunde Null*, especially as Borchardt in particular was a long-time political opponent and intellectual critic of Erhard's liberal economic philosophy.<sup>8</sup> The Stolper tome set a precedent for future continuity narratives, foremost of which are Karl Hardach's (1980) *The Political Economy of Germany in the 20<sup>th</sup> Century* and Hans-Joachim Braun's (1990) *The German Economy in the Twentieth Century*.

The *Stunde Null* came under direct assault in 1975 from Werner Abelshauser's book *Wirtschaft in Westdeutschland, 1945-1949*. Where previous conceptions discussed a unique Wirtschaftswunder, he identified similar economic performance in other European nations of the time. He also attributed West Germany's fantastic growth to pre-1945 trends. The "economic miracle" was consequently less than miraculous, just a series of medium-term business cycles within a *longue durée* upward trend.<sup>9</sup> Abelshauser also argued that National Socialist industrial prowess set the stage for postwar achievements. He pointed to figures such as the net industrial production of goods, which at the end of 1946 was almost twice the value of a decade earlier. (1975: 52)

Substantive questioning of the zero hour thesis and its ensuing economic successes followed. If Erhard's *Soziale Marktwirtschaft* lacked explanatory creditability given long term internal and international trends, then his philosophical policymaking was for relative naught. "Continuity" threatened both the economic identity of West Germany and the psychological comfort of being wholly different from National Socialist times. How was one to account for alleged accomplishments of the Social Market Economy?

The 1970s were a decade of economic stagnation in Germany. As the downturn ended, previous standards of growth and employment remained elusive. Scholars wondered why. In the absence of definitive evidence that Erhard's liberalism was directly responsible for the *Wirtschaftswunder*, Abelshauser's critics attempted to refocus the debate surrounding *Stunde Null* towards a more normative position. Simply stated, when Erhard's philosophy governed, indisputable success followed, whereas post-Erhard events presented a decidedly mixed, and from the '70s on, stagnant track record. How, such supporters asked, did the Social Market Economy transition from market-based success in the 1950s and 60s to negative connotations of a bloated "welfare state" in later decades? Continuity theory lacked rhetorical persuasiveness when framed by economic performance.

In the 1990s, scholars attempted to resurrect the liberal-defined Social Market Economy. While interest in Ordoliberalism and other neoliberal philosophy never completely

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<sup>8</sup> More polemic histories appeared later, such as Heinz-Dietrich Ortlieb's (1974) opus which condemned "Playboy-Democracy" and liberal "dogma", asserting instead Free Socialism and a classless society.

<sup>9</sup> Abelshauser recently (2004) affirmed his analysis. Knut Borchardt (1991) also adopted similar reasoning by proffering a "secular trend" growth argument in the stead of *Wirtschaftswunder*. Dietmar Petzina is associated with the Abelshauser movement as well, including one co-written (with Abelshauser) volume *Deutsche Wirtschaftsgeschichte im Industriezeitalter. Konjunktur, Krise, Wachstum* (Düsseldorf: Droste, 1990). Other relevant Petzina works include *Wirtschaftspolitik im britischen Besatzungsgebiet 1945 – 1949* (Duesseldorf: Patmos, 1988) and (with R. Ruprecht) *Wendepunkt 1945? Kontinuität und Neubeginn in Deutschland und Japan nach dem 2. Weltkrieg* (Bochum: Universitätsverlag Brockmeyer, 1991). In the Anglophone world, Alan Kramer (1991) wrote from the perspective of a "fundamentally healthy" German economy at war's end.

waned,<sup>10</sup> circumstances relating to the post-communist transition,<sup>11</sup> German Reunification,<sup>12</sup> and unrelenting “Eurosclerosis”<sup>13</sup> spurred renewed curiosity. Two transformative works were published during this period. The first was (1992) *The Fading Miracle*, by Giersch, Paqué and Schmieding, whose introductory remarks announced their philosophical inclinations: “In our view, the main lesson comes down to one fundamental proposition: miracles emerge when spontaneity prevails over regulation, and they fade when corporatist rigidities impair the flexibility for smooth adjustment.” (pp. xi) Supporting text, however, was less advocacy and more chronological blow-by-blow, with a stress on impartiality and neutral, often quantitatively-rendered interpretations. In stark contrast to the vigorously partisan literature of previous decades, the *Fading Miracle* conveyed the tone and semblance of encyclopedic organization and knowledge.

Anthony J. Nicholls (1994) followed with an unabashed defense of “German neoliberalism.” He explored its early philosophical influences and provided biographical sketches of various Ordoliberal personalities, constructing a narrative that stressed ideologically-motivated policy implementation. Accordingly, Ordoliberalism and its associated scholars assumed a central role in postwar economic debates, eventually leading to Ludwig Erhard and the *Soziale Marktwirtschaft*. While Nicholls’ analysis derived significant inspiration from its normative focus, it nevertheless established a precedent based on extensive archival research and clear, well-reasoned argumentation.<sup>14</sup>

Prevailing research allowed neoliberal academics to argue for a variation on the *Stunde Null*, at least insofar as founding philosophy was concerned. Post Abelshausen, the focus turned to individual academic contributions – Erhard, Müller-Armack, Eucken etc. – emphasizing their determination to achieve an *Ordnungspolitik* redefinition of German economic society. It was relatively persuasive to insinuate a link between the writings of particular liberal scholars (which tended to focus on price stability, anti-cartel legislation, and limited government intervention) and early institutional developments of the FRG.<sup>15</sup>

Most recently, Nützenadel (2005) addressed intellectual elites, as he argued in favor of an “expert culture” that framed much of Germany’s postwar history. The leading economic personalities of the Federal Republic indeed afforded researchers a luxury often absent in other polities: many influential policymakers were in previous incarnation academics and thus they left numerous sources articulating their philosophies and viewpoints. Nützenadel elucidated the decision-making processes of economic policy by referencing

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<sup>10</sup> Varying accounts were provided by Blum (1969) *Soziale Marktwirtschaft, Wirtschaftspolitik zwischen Neoliberalismus und Ordoliberalismus* and in articles by Siegfried Karsten (1985) and Konrad Zwieg (1980).

<sup>11</sup> Wolf (1993), for example, used a Wallichian evaluation of the “Lucky Miracle” to rebut the attentions of those looking for a ready-made post-communist transition model.

<sup>12</sup> See Smyser (1992) for a traditional *Stunde Null* history, yet motivated by the “new *Stunde Null*” in 1989.

<sup>13</sup> A term originally coined by Herbert Giersch in “Eurosclerosis”, Kiel Discussion Paper No. 112, (*Institute for World Economics*, 1985).

<sup>14</sup> Van Hook (2004) also deserves particular mention. His book revisits ground covered by Abelshausen (1975), Buchheim (1990), and Kramer (1991), yet manages to contribute fresh material on most fronts (see, for example, a superb discussion on the balance of payments and Korean crises in 1952; p. 204-232).

<sup>15</sup> See Riha (1985), Grosskettler (1989) & (1994), Karsten (1992), Reiter & Schmolz (1993), Broyer (1996), Witt (2002), Oswald-Eucken (1994), Vanberg (2004), and Goldschmidt (2004).



the character and ideology of relevant participants, resurrecting a dialogue between the policy and academic worlds. This approach provided a remarkably effective analytical tool in contrast to the literature’s previous advocacy of broad “secular trends” and paradigmatically-rigid reasoning.<sup>16</sup>

In sum, academic dissonance over the “facts” created discursive spaces that were claimed by ideologically motivated narratives. The literature thus evidences a tendency to elucidate its author’s philosophical inclinations rather than what, afforded “original position” insight, actually transpired. Postwar German economic history must therefore endure twice the scrutiny, from both epistemologically-motivated historians and more normative actors seeking justification for current political agenda.

How, then, to answer the fundamental questions surrounding economic historiography of the 1950s and 60s?<sup>17</sup> This paper approaches such debates from two positions. First, academic movements translated by-and-large into economic policy in the Federal Republic. Second, insofar as intellectuals conceived of policy from a historically informed position, strict *Stunde Null* dichotomies cease as relevant descriptive variables. In creating a new state, policymakers corrected for historical phenomena through their philosophical stances, instilling simultaneously “continuous” and new institutions/policies. The methodological premise follows as such:



A rigorous history that tracks this process avoids epistemological paralysis, providing an operable economic historiography which also informs current circumstance.

This paper asserts that a relatively misunderstood dialogue between academic and political spheres underpins German economic history following the Second World War. Addressing these historiographical problems first requires a working familiarity with the two intellectual movements concerned, Ordoliberalism and Keynesianism. A reader is then optimally positioned to re-examine Germany’s economic event history. Having traced the origins and development of current trends, underlying difficulties of and suggestions for our current circumstance emerge.

<sup>16</sup> Continuity theory did not disappear. Götz Aly (2005), for instance, recently published a controversial book which asserted that the “soziale” policies of the SME relied heavily on Nazi innovations.

<sup>17</sup> 1) How to account for West Germany’s rapid economic renaissance? 2) Are there lessons for today?

## 3. *Philosophic Underpinnings*

### 3.1. Ordoliberalism

The word “liberalism” evokes a long lineage of distinguished economic scholars. Adam Smith originally revolted against mercantilist conceptions, envisioning in his seminal book *Wealth of Nations* a marketplace where the unfettered efforts of individual actors achieved the most efficient and equitable distribution of scarce resources. (Viksnins, 1997: 30) Smith is regarded as the original apologist for non-interventionist competitive society, and even after centuries of modification and redefinition, liberalism continues to be envisaged on the basis of individual freedom, market-based competition and the absence of government intrusion.

Ordoliberals<sup>18</sup>, however, were defined less by their liberal pedigree and more for their critique of pure *laissez faire* persuasions. While Ordoliberalism<sup>19</sup> passionately affirmed competitive free markets, it was motivated from the historical observation that concentrations of power in both public and private spheres distorted functioning exchange economies. Thus, the long-term viability of free markets required a rule-bound and limited yet powerful form of government intervention. To quote the prominent liberal academic Wilhelm Röpke:

A market economy and our economic program presuppose the following type of state: a state which knows exactly where to draw the line between what does and what does not concern it, which prevails in the sphere assigned to it with the whole force of its authority, but refrains from all interference outside its sphere – an energetic umpire whose task it is neither to take part in the game nor to prescribe their movements to players, who is rather, completely impartial and incorruptible and sees to it that the rules of the game and of sportsmanship are strictly enforced. That is the state without which a genuine and real market economy cannot exist. (Röpke, 1950: 192)

Defining the “rules of the game” of a competitive market society was an Ordoliberal scholar’s underlying mission. The following section will outline the basic tenets of Ordoliberalism as they relate to German economic policy in the postwar era.

**3.1.1 Competitive Markets and Monopoly Power** – The temporal location of 1930s Freiburg im Breisgau, a university city in provincial Baden under an increasingly despotic Nazi regime, provided the setting for much of the intellectual activity now associated with Ordoliberalism. By chance, economist Walter Eucken (1891-1950), jurists Franz Böhm (1895-1977) and Hans Grossmann-Doerth, (1894-1944) and others found themselves independently researching from various standpoints the same issue:

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<sup>18</sup> Scholars Walter Eucken, Hans Grossmann-Doerth and Franz Böhm are thought of as the core Ordoliberal establishment. However, the German neo-liberal tradition encompasses a much larger informal membership, many of whom espoused similar ideals. Sympathetic academicians prominently included Wilhelm Röpke, Alexander Rüstow, Constantine von Dietze and Leonhard Miksch, notwithstanding more politically notable personalities such as Alfred Müller-Armack and Ludwig Erhard.

<sup>19</sup> “Ordoliberalism” stems from the Latin *ordo*, which means inner order, in contrast to *ordinato*, or one externally imposed. (Grosskettler, 1989: 43)

private power in a free society.<sup>20</sup> (Rieter & Schmolz, 1993: 96) The result of these investigations was a blending of the fields of law and political economy.<sup>21</sup>

Freiburg academics believed that combating harmful concentrations of power necessitated both disciplines. An otherwise competitive marketplace often failed from lax legal structures. Examples included: a) the sub-optimal allocation of resources based on monopoly-skewed pricing, b) the *de facto* closing of previously accessible markets to other producers, c) overly-generous patent protections, d) limited liability law, and e) the arbitrary application of liability law. (Eucken, 1952: 178) These creeping restrictions threatened the efficiency and equity of unencumbered market distribution. Thus, anti-monopoly policy in particular was to be embedded into a state's legal system, along with safeguards against labor monopsony, such that discretionary imperatives of policymakers were limited to the maintenance of competitive markets. (Möschel, 1989: 142) Eucken suggested that the aim of anti-cartel legislation was to induce the bearers of economic power to behave as if they operated in a regime of perfect competition. (Zweig, 1980: 25)

Perfect competition remained more of an ideal than a pragmatic model. Franz Böhm admitted: "Practical policies to establish competition and to check anti-market power...[cannot] mold reality into the image of the theoretical model of perfect competition. Suffice it to create as much competition or rivalry as is practical under given circumstances." (in Zweig, 1980: 26) Anti-cartel legislation, however, provoked sanguine suggestions. Eucken recommended that a politically neutral *Monopolamt* (Cartel Office) be responsible for regulating issues relating to market power. (Eucken, 1952: 294) As Friedrich A. Lutz, one of Eucken's first students aptly summarized: "It seems to me that no situation is less desirable than one in which determination of the share of the national product is left to economic and political power struggles." (Lutz, 1956: 152)

The more politically involved Ordoliberal cadre, particularly Alfred Müller-Armack and Ludwig Erhard, were similarly opposed to monopoly power. They considered the protection of free competition to be the most important "social" principle of their Social Market Economy. (Müller-Armack, 1956: 84) Erhard betrayed the extent of his monopoly power worries in a letter to Chancellor Konrad Adenauer in 1949: "Such important problems as decartelization and liberalization...[are] problems which must be properly solved if our social market economy is not to become a farce." (in Nicholls, 1994: 271)

Erhard anticipated attempts to limit competition, as well as the reflexive policy influences of strong concentrations of private power in the public sphere. Special interests, while inevitable in the context of a free society, were to be de-fanged within the state's bounded regulation of the economic process. "Government also is constantly faced with a considerable temptation to meet the contradictory demands of many pressure groups... Thus it is not only the pressure groups that scratch each other's backs but also the pressure groups in association with the government. It is certainly no exaggeration to describe these directly opposite events...as a danger to the social system." (Böhm, 1996:

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<sup>20</sup> For more on the history of the Freiburg School, its membership and resistance to Nazism see Grosskettler (1989), Rieter and Schmolz (1993), Goldschmidt (1997) and Vanberg (2004).

<sup>21</sup> Böhm, Eucken & Grossman-Doerth's "The Ordo Manifesto of 1936" explains the law/economics dynamic.

66) Hence, Eucken and other Freiburg Ordoliberals conceived of a *Wirtschaftsverfassung* (economic constitution) to exactly define the role of government in the economy, such that the crucial underpinnings of economic policy remained absent from the realm of discretionary politicking or the sway of possible anti-competitive interests. (Vanberg, 2004: 10-11) Improper lobbying in the public sphere and monopolistic arrangements of private power were seen as one in the same, both attempts to suspend competition and the numerous societal welfare benefits therein entailed.

**3.1.2. Stable, Functioning Prices** – For Ordoliberals, free and open markets were inextricably intertwined with a stable, functioning system of reflective prices. Twentieth Century German history provided considerable evidence for the destabilization of society due to catastrophic price volatility. During the post World War I hyperinflation – where in 1919 one U.S. dollar was worth 8.4 Reichmarks and by late 1923 that same dollar bought 4.2 trillion RM – economic and civil society all but collapsed. (Campbell, Holt, Walker 1996, pp. 163) Rampant inflation, however, was not the only monetary difficulty. Government intervention either in fixing or artificially valuing prices also carried ill effects. With a corrupted price mechanism, it was impossible to value and thus maintain efficient, competitive economic activity. As Eucken pointed out, when the Nazi regime froze prices and wages in 1936, they “no longer expressed the relationship between needs and supplies...calculations based on these prices for products and for the means of production could not command the factors of production to meet the needs of the plan; profit and loss calculations and budgets gave no information as to whether the factors of production were being combined optimally for the production of goods as planned by the central authorities.” (Eucken, 1948a: 91) Without an accurate gauge of costs and benefits, production and consumption became arbitrary, at least from the standpoint of markets, while every ‘uninformed’ decision by households and firms multiplied the capricious distribution of scarce resources. (Eucken, 1948: 28) Eucken concluded that Hitler’s regime extended control over the exchange economy simply by freezing prices, which made the entire market edifice dependent on governmental allocation and direction.

Wilhelm Röpke coined the term “repressed inflation” to describe a situation in which prices should rise, but the state prevents monetary devaluation. “Open inflation is bad enough because it is the cause of crying injustices and because it leads to unbalanced production. Repressed inflation is, if anything, somewhat worse because it adds stagnation to unbalanced production and unjust distribution.”<sup>22</sup> (Röpke, 1947: 247) He was referring in particular to the postwar monetary reality of occupied Germany. Heinrich Rittershausen, a specialist in monetary theory, described the situation in early 1948: “The pricing system we have has come down to us from 1936. Until 1945 it was adjusted [upwards] by about 40 or 50 per cent. Since 1945 it has been further adjusted by an amount which on average has been 20 per cent of the original price level.” (in Nicholls, 1994: 188) This arbitrary system of valuation bore little relation to scarcity conditions. A vicious cycle was established as compulsory valuations became ever more fictitious, forcing the government to redouble controls in order to maintain its policy, and so on. (Röpke, 1947: 247) The result for the everyday worker was a return to primitive

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<sup>22</sup> See *Against the Tide* (Röpke, 1969) chapter 6 for further clarification of ‘Repressed Inflation.’

barter exchange, or the use of “cigarette currency”<sup>23</sup>, complemented by subsistence farming and production, all under the auspices of an authoritarian government. Eucken colorfully borrowed Lenin’s expertise: “To destroy civil society, one must debauch its monetary system.”<sup>24</sup> (Eucken, 1952: 255) For Ordoliberal, flawed pricing directly caused economic disaster and political totalitarianism.

**3.1.3. Social Policy and Government Intervention** – The divergence of Ordoliberal thought from traditional neo-liberal musings, as espoused by “hands-off” Manchester School or Austrian thinkers, came in its assertion of obligations beyond bounded protections of competitive markets. Traditional neo-liberals, like Friedrich von Hayek, distrusted Ordoliberalism’s interest in social justice and equitable distributions of wealth.<sup>25</sup> Hayek was not fond of the so-called “social intervention.” He found in the word ‘social’ itself an excuse to disguise a collectivist, and hence anti-social, agenda.<sup>i</sup> Yet Ordoliberal conceptions of market intervention derived from witnessing the numerous horrific turns of 20<sup>th</sup> Century German history. Scholars viscerally understood that a large majority of citizens must share in the prosperity of the free market system for it to enjoy long-term stability. However, Ordoliberal conceptions varied widely as to what a proper social intervention entailed. Seen in retrospect, this academic dissonance became vital to the economic policy implementation process of the FRG.

Ordoliberals believed that the true social benefits of their system derived inherently from the long-term stability of competitive markets. The social dogma of Ludwig Erhard can be summarized in three basic tenets: a) the suppression of arbitrary and disorderly political and economic power, b) the elimination of monopolistic structures and c) the ceaseless functioning of individual freedom and competition. (Goldschmidt, 2004: 12) Little else was required to ensure the enduring welfare of most citizens.

Eucken, however, presented a more complex theoretical picture. The “constituting” fundamentals of his competitive order were complemented by “regulating” principles. Other than the strict control of monopoly power, these included the public regulation of severe supply side anomalies such as drastic unemployment, the redistribution of income through progressive taxes, and the correction of societal externalities due to large discrepancies between short-term profits and the long-term collective interest. (Eucken, 1952: Ch. XVI) This vague language sanctioned a broad swath of possible policies. Eucken distinguished, in particular, public health initiatives (Grosskettler, 1989: 50) and the need for environmental regulation.<sup>ii</sup> Presumably, basic unemployment insurance, disability coverage and state-funded education also met the re-distributive mandate. Unfortunately, particulars of Eucken’s regulating principles were not as well defined as

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<sup>23</sup> Werner Plumpe (2004: 295) reported that in 1946, “one cigarette could fetch more than could be earned by a full day’s work.”

<sup>24</sup> “*Um die bürgerliche Gesellschaft zu zerstören, muss man ihr Geldwesen verwüsten.*” As an interesting aside, Lenin’s famous quote actually emanated from the pen of John Maynard Keynes, and despite many attempts to authenticate his sourcing, Keynes’ *Economic Consequences of the Peace* (1920: 235) remains its first accredited reference.

<sup>25</sup> For various writings on the relationship between Hayek, Austrian thought and Ordoliberalism see Oswald-Eucken (1994: 7), Streit & Wohlgenuth (1997) and Vanberg (2002).

they might have been, owing to his early death in 1950. It is, however, safe to assume that for Eucken, social policies were only acceptable insofar as they did not infringe upon the primacy of stable, reflective prices in a fully competitive marketplace.

Müller-Armack more aggressively asserted a social function for the state. Motivated in part by a strong Catholic faith<sup>26</sup>, he wrote extensively on social mandates, especially concerning income equality. “Income redistribution is brought about through welfare benefits, equalization of pensions and compensation payments, housing grants, subsidies *et cetera*.” (Müller-Armack, 1956: 84) Fundamental differences with other Ordoliberals arose from such opinions, which encouraged government subsidization of housing, food and so on. More rigorous Freiburg types worried that such steps constituted an unacceptable tampering with prices.

Alexander Rüstow also advanced a bold imperative for government intervention:

If we were agreed that every new condition of equilibrium which arose in the normal way was the most appropriate solution even though many frictional losses and disagreeable phases had to be overcome en route, it would seem highly advisable to try to achieve this condition without (sic) delay... That would be interference in precisely the opposite direction to that in which we have hitherto proceeded, i.e. not contrary to the laws of the market but in conformity with them: not to maintain the old situation but to bring about a new one, not to delay the natural course of events but to accelerate it. (Rüstow, 1932: 184-85)

He offered the example of an agricultural sector threatened by structural change resulting in a lack of competitiveness. In this instance, the role of the government would not be to protect the failing sector, but rather to encourage a rapid transition to a new equilibrium.

If we then decided to emulate the Manchester school and simply let things take their course, the following condition would supervene only after decades of distress... Those capable of adjustments would have carried them out accordingly: those not in a position to do so would have been forced to quit their plot of land and try elsewhere to find somewhere of permanence. My proposal is that this final situation should be immediately established by accelerating and facilitating the potential adjustments by educational and financial aid. (Rüstow, 1932: 185)

Rüstow thus presented a new social logic for structural unemployment insurance and educational assistance: government interference to hasten a ‘new equilibrium’ by helping the transitionally displaced.

While examples of governmental interaction with economic society often displayed a marked social mentality, Ordoliberals insisted that such measures 1) were limited in scope to the truly social-fabric-ripping vagaries, 2) would not disrupt the primacy of prices and anti-monopoly controls and 3) were not influenced by biased interest groups.

There was, however, a second type of state intervention, which dealt primarily with business cycles, or the fluctuations of employment, investment, consumption and income growth through periods of boom and bust. Most Ordoliberals declared active attempts to ‘smooth’ or manage such cycles as dangerously close to centralized planning, which they dreaded. Hans Willgerodt summarized the liberal critique of anti-cyclical policy: “A continuous series of counter-measures by the Government to reverse economic trends

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<sup>26</sup> See Müller-Armack (1955) “Wirtschaftspolitik in der sozialen Marktwirtschaft” for more on his Catholic sway.

puts the public...in a mood of continuous expectation of change. As a result, the range of complementary governmental services begins to fluctuate – particularly in respect of state investment. In conjunction with an official policy of structural distortion, this state action...tends to exercise a destabilizing impact on the economy and on [individual] planning.” (Willgerodt, 1979: 164) In the end, measures meant to manage business cycles actually exacerbated investor uncertainty, causing the very swings in growth and unemployment they were meant to solve.

Other Ordoliberals, such as Müller-Armack, Eucken and Röpke, entertained more nuanced opinions on business cycle management. Müller-Armack thought the state should engage in limited (and vaguely defined) business cycle management: “Within the framework of budget stability and a sound monetary constitution, however, politico-economic dynamism can certainly be maintained and, if necessary, fortified by contra-cyclical measures.” (Müller-Armack, 1956: 85) In fact, early writings of Müller-Armack displayed enthusiastic support for active monetary business cycle policy, especially to cool off a credit boom. (Müller-Armack, 1929: 665)

Eucken also endorsed “supply anomaly” intervention. He believed a government must actively engage in labor markets during situations of drastic structural unemployment, for example by subsidizing minimum wages, such that lower labor costs encouraged additional hiring (Eucken, 1952: 304). Röpke told a more monetary story, suggesting that depressions stemmed in the first instance from dire capital market conditions:

If in such a situation the elasticity of demand for credit becomes almost absolutely rigid, attempts at credit expansion will not lead to the desired expansion of total demand for commodities, but merely to an increase of general liquidity. Now the reluctance of entrepreneurs to enter upon new investment is due not only to the confidence crisis, to the recession of prices, and to the over-investment of the previous boom, but also to the fact that entrepreneurs will not dare, for the purpose of long-term investment, to have recourse to short-term credits...unless a marked recovery of the stock exchange points to the possibility of an early consolidation...The same line of reason suggests that it is well-conceived policy...for central banks or similar authorities to take the initiative by means of heavy buying, in preventing a total collapse of security markets. (Röpke, 1933: 436-37)

Röpke believed that normalcy in labor markets would be restored by extending long-term credit at reasonable rates, a task only a government body could reasonably undertake.<sup>27</sup>

While various authors endorsed wide-ranging intervention methods, sparse application was the unifying aspect of all Ordoliberal “counter-cyclical” measures. Such policies were intellectually derived from the experience of the Great Depression – during which anywhere from 28-32 percent of German workers applied for unemployment insurance – and it was to a similarly disastrous situation that Ordoliberals addressed their interventionist oeuvre. (Voth, 1995: 802-3)<sup>28</sup> As Röpke wrote, “We have to distinguish

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<sup>27</sup> While business cycle theory is now mostly associated with Keynes, a simultaneous (and autonomously anticipatory) movement also occurred in Germany involving such academics as N. Neisser, W. Lautenbach, G. Haberler and of course Röpke. For a closer look at such “proto-Keynesian” ideas see Klausinger (1999).

<sup>28</sup> Interestingly enough, Voth (1995) argues that even the Great Depression in Germany cannot be considered a literal failure of strict classical principles (downward pressure on wages until the labor market clears.) In fact, real wages remained relatively high – an indexed 118 in 1929 vs. 100 in 1913 – as lowering them was not a politically

between a primary and a secondary phase of the crisis. The latter is characterized by a *circulus vitiosus* which constantly interferes with the attainment of a new equilibrium.” (Röpke, 1933: 434) Only in the instance of a “vicious cycle” morass was public intervention sanctioned. If the choice was to err on the side of too little or too much government involvement, Ordoliberalism favored the former.

**3.1.4. Conclusions** - In Ordoliberalism one finds both idealistic and pragmatic visions of the optimal economic order. While often profoundly utopian in their thinking – viz. the functioning of democratic government without special interest involvement – scholars like Eucken, Böhm, Röpke, Erhard and Müller-Armack were ultimately concerned that their ideas be implemented in reality. For that generation of Germans, drawing a sharp distinction between the academic and real worlds seemed naïve and foolish given two World Wars and Weimar’s numerous economic catastrophes.

When Ordoliberalism did influence policy in the new FRG, its strengths and weaknesses shined through. On the basic principles and structure of society – or the free market allocation of scarce resources, uninhibited competition and stable reflective prices – there was little disagreement or hesitation. However, when deliberating on government intervention for social purposes, Ordoliberals were conflicted about necessary or tolerable policy. It was obvious from ever-present problems of collective action and the global Great Depression crisis that some sort of society-level externality and business cycle management was required, but to allow for a discretionary mandate in those areas also opened the Pandora’s Box of centralized planning. The closest Freiburg thinkers came to a “practicable” implementation strategy was the *Wirtschaftsverfassung*, or a definition of fiscal and monetary parameters which “caged the beast” of government intervention. Such genres of constitutional thought spawned quite a bit of fervor across the Atlantic in later decades;<sup>29</sup> however, in the German postwar institutional context the concept received scant attention at best. In as much, accounting for the “social” motivations of the *Soziale Marktwirtschaft* requires additional investigations. Ordoliberalism was not the only philosophic foil for West Germany’s economic policy.

## 3.2. Keynesianism

Returning to hardships in the Great Depression and the various nefarious experiences of the interwar period, it is hardly surprising that a new brand of economic theory would emerge to challenge the obviously lacking status quo. While neoliberalism proper trumpeted a return to free markets, John Maynard Keynes saw events in a different light. For him, ultimate failings were intrinsic to the basic assumptions of classical economic theory, which supported liberal ideals on free market allocation. Recourse for these errors was found in active and informed governmental management of macroeconomic trends.

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feasible solution given the threat of social instability. (Voth, 1995: 803) Amid this wage-inflexibility morass, classical economic convention even suggested raising wages to spur a “substitution effect”, encouraging labor-replacing capital formation despite 30% unemployment. (ibid: 817-818) It was exactly this classical explanation of “wage stickiness” that Keynes addressed.

<sup>29</sup> For more on the linkages between the Constitutional Economics qua James Buchanan and Freiburg Ordoliberalism, see Liepold (1990) and Vanberg (1998)



**3.2.1. Employment Theory and Business Cycles** – Classical interpretations of employment rely on the unfettered equilibrium of supply and demand in labor markets. In a situation of ‘disequilibrium,’<sup>30</sup> for example an influx of new labor into the workforce or an exogenous change in the demand for labor, – caused by new technology, a decrease in the demand for products, etc. – wages adjust accordingly and markets clear. Employment is thus a neutral factor, as equilibrium maintains itself through the fluctuation of wages. ‘Involuntary’ structural employment should not exist in a hypothetical world.

During the economic crises of the interwar period, classical theory suggested that wages should decrease until all jobless-but-willing workers were accommodated. The massive involuntary unemployment of the 1930s represented in graphic detail, however, the drastic flaws with such suppositions. Keynes<sup>31</sup> wrote:

The classical theorists resemble Euclidean geometers in a non-Euclidian world who, discovering that in experience straight lines apparently parallel often meet, rebuke the lines for not keeping straight – as the only remedy for the unfortunate collisions which are occurring. Yet, in truth, there is no remedy except to throw over the axiom of parallels and to work out a non-Euclidean geometry. Something similar is required today in economics. We need to throw over the second postulate of the classical doctrine and to work out the behavior of a system in which involuntary unemployment in the strict sense is possible. (Keynes, 1936; 1949: 16-7)

The error resulted from classical theory’s failure to account for the “stickiness” of wage adjustments. (Gottschalk, 2002: 7) For Keynes, the relationship between wages and employment also reflected a given public’s propensity to consume, the marginal efficiency of the capital schedule, and the real interest rate. He asserted “if, without any change in these factors, entrepreneurs were to increase employment as a whole, their proceeds will necessarily fall short of their supply-price.” (Keynes, 1936; 1949: 261) Thus, increasing employment by lowering wages required the redefinition (in terms of a firm’s marginal cost and revenue calculations) of other variables, including consumption patterns, the efficiency of capital (given more labor inputs) and interest rates. Labor markets simply did not clear to equilibrium in a short period of time, if at all.

Keynes also focused his critique on the problem of ‘aggregate demand,’ especially during downswings in the business cycle. (Keynes, 1936; 1949: 258) He attempted to show that a drop in aggregate demand necessarily followed from declines in employment, as opposed to the classical assumption that firm investment increased as consumption declined, balancing total demand. For Keynes, prices fell with wages, but because wages were “sticky,” there was a *real* income distribution away from capital owners. Thus, savings were not converted into investment as firms had a disincentive to invest based on their relatively high real costs of labor, not to mention the original fall in consumption. Falling wages and prices at home also eroded trade balance purchasing power, further reducing real incomes and decreasing the marginal propensity to consume. (ibid: 263) Finally, expectations often manifested in reality, so “a vicious cycle of unduly pessimistic estimates” weighs upon perceptions; investment and consumption fall as a consequence. (ibid; 1949: 264)

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<sup>30</sup> This is a tricky term, because theoretically-speaking, disequilibria of this sort should not exist.

<sup>31</sup> Among other famous (and frequently misquoted as he was referring specifically to monetary crises and not employment or business cycle policy per se) Keynes-isms was the observation that, “in the long run, we are all dead.” (Keynes, 1923: Vol. 4, Chp. 3, pp. 65)

Economic recession is therefore caused by deficient demand for both labor and goods, which continue to reinforce one another. Unemployed workers result from firms not selling enough goods and services, while firms resist increasing production because of insufficient aggregate demand, which remains deficient because people are unemployed! (Gottschalk, 2002: 8) In sum, the negative effects of relatively minor and routine business cycle fluctuations can snowball into larger economic problems because of self-perpetuating aggregate demand losses.

Keynes' *General Theory* redefined the dependent variables of economics, focusing attention on levels of employment and per capita calculations of national income vis-à-vis wages. (Keynes, 1936; 1949: 254) Vicious cycles of aggregate demand loss and sticky wage adjustment led to a logical normative position concerning the role of government in economic society. Keynesianism unequivocally called for the maximization of employment through the macro-level demand management of business cycles.

### **3.2.2. Fiscal Demand Management** – Keynes concluded that the state must guide fluctuations of aggregate demand, if possible without centralizing economic life:

I conceive, therefore, that a somewhat comprehensive socialization of investment will prove the only means of securing an approximation to full employment; though this need not exclude all manner of compromises and of devices by which public authority will co-operate with private initiative. But beyond this no obvious case is made out for a system of State Socialism which would embrace most of the economic life of the community. It is not the ownership of the instruments of production which it is important for the State to assume. If the State is able to determine the aggregate amount of resources devoted to augmenting the instruments and basic rate of reward to those who own them, it will have accomplished all that is necessary. (Keynes, 1936; 1949: 378)

Keynesian demand management differed from other forms of statism in the ownership of the means of production. Keynes affirmed the market allocation principles celebrated by classical economists in spheres of micro activity, amending only their macro economic aggregates. He wrote, “apart from the necessity of central controls to bring about an adjustment between the propensity to consume and the inducement to invest, there is no more reason to socialize economic life than there was before.” (Keynes, 1936; 1949: 379) The state therefore requires only the tools necessary to achieve full employment over both the short and long term. This position, however, does not preclude state ownership should it be deemed necessary.

Keynes was less precise on the actual functioning of the fiscal prerogative. “All sorts of policies for increasing the propensity to consume” complemented a “socially controlled rate of investment” through business cycles. (Keynes, 1936; 1949: 325) Further scholarship articulated such policies in more detail.<sup>32</sup> Indeed, modern fiscal macroeconomics emerged from the intellectual tradition established by Keynes' demand management. The idea that one can mimic reality with a model, not just as an illuminating epistemological endeavor, but to pinpoint suboptimal economic behavior and craft targeted macro-level interventions, is, philosophically-speaking, Keynesian.

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<sup>32</sup> See Gordon (1990), Mankiw (1990) and Samuelson (1939).

**3.2.3. Prices, Wages and Money** – Traditional understandings of unemployment were not the only casualties of Keynes’ probing mind. He also targeted the underlying assumptions of classical monetary theory:

In equilibrium – i.e. when the factors of production are fully employed, when the public is neither bullish of securities...and when the volume of saving is equal both to cost and to the value of new investments – there is a unique relationship between the quantity of money and the price level of consumption-goods and of output as a whole, of such a character that if the quantity of money were double the price-levels would be double also. Such an exact balance is, of course, only a theoretical possibility. In the actual world a change in anything is likely to be accompanied by some change in everything else. (Keynes, 1930; 1958: 146-7)

The implications of this “sticky” real price adjustment de-linked the exact relationship of money supply and inflation. Ergo, nominal fluctuations in money supply partly transferred to other “real” variables, such as output, consumption and employment.<sup>33</sup> As to the policy implications of this monetary dynamic, Keynes was less explicit, focusing more of his attention on investment and consumption facets of demand management.<sup>34</sup>

Some decades later, in 1958, A.W. Phillips articulated the relationship between nominal changes in wages (and consequently overall nominal prices) and unemployment figures. Drawing on historical data in Britain from 1861-1957, Phillips found that unemployment and nominal wage growth rates were negatively correlated and, importantly, non-linear. (Phillips, 1958: 285) The logarithmic shape of Phillips’ curve seemed to confirm his hypothesis that tight labor markets during business cycle booms caused employers to bid wages rapidly up, whereas loose labor markets with high rates of unemployment witnessed a relatively slow downward wage revision. (ibid: 283) Statistical evidence supported the conclusion that both marginal and absolute rates of unemployment were correlated with nominal wage levels:

It seems from the relation fitted to the data that if aggregate demand were kept at a value which would maintain a stable level of product prices the associated level of unemployment would be a little under 2.5 percent. If, as is sometimes recommended, demand were kept at a value that would maintain stable wage rates the associated level of unemployment would be about 5.5 percent. (Phillips, 1958: 299)

Thus, increasing nominal wages inversely affected unemployment, advancing the hypothesis that price changes could be used to manage overall macro employment levels and thus national and per capita income. The Phillips Curve’s non-linear shape indicated that nominal changes were most potent during the peaks and troughs of the business cycle, firmly placing monetary policy in the pantheon of powerful demand management tools. Plus, exact targeting of the substitution quotient between inflation and employment was not technically necessarily, as planners were assured that increasing nominal prices would decrease unemployment in any case.<sup>35</sup>

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<sup>33</sup> For example, increasing money supplies spurs a change in the velocity of money, as the general populace is less likely to hold on to an inflating currency. Thus, the marginal propensity to consume rises. People buy more stuff. Businesses produce more. Output rises. Businesses hire.

<sup>34</sup> Keynes, however, endorsed discretionary monetary policy to influence output and steady investment through business cycle fluctuation. See Book VII, *A Treatise of Money* (1930a; 1958a) for more in this vein.

<sup>35</sup> Incidentally, such trust proved premature, as was viscerally demonstrated during the 1970’s “Stagflation.”

**3.2.4. Conclusions** - Keynesian policymakers are aided by two major policy instruments in their mandate to combat unemployment and stabilize the inevitable business cycle booms and busts: fiscal demand management (of both consumption and investment) through taxation and government spending, and the targeting of nominal wage rates using the overall money supply and, accordingly, price changes. Keynesians continue to define the interaction of the two policy strategies to this day. (Vines and others, 1983: 13)

Normative Keynesian literature envisions state intervention as the primary fix for aggregate demand problems. The academic and practical debate therefore revolves around the most appropriate means to measure and redress market deficiencies. Keynesianism posited proactive and pragmatic economic science, seeking, as Joseph Schumpeter aptly wrote: “to make that vision of our age analytically operative.” (Schumpeter, 1949: 80) Once fully articulated, it was indeed a vision that would motivate policymakers all over the world, including those in Germany.

### **3.3. Ordoliberalism and Keynesianism**

Before advancing to the historical analysis, it is informative to first reflect on the two major philosophical underpinnings of German economic policy. In many senses, Ordoliberals and Keynesians shared the same basic principles: a belief in the underlying efficiency and equity of free market allocation and the necessity of state intervention to protect economic society from phenomena outside the agency of individual actors. They also agreed as to the power of nominal price changes, except Ordoliberals feared possible inflationary and deflationary consequences while Keynesians embraced the discretionary monetary imperative as a valuable tool.

Reasons for and methods of government involvement in economic life differed completely. Private power concentration was a non-issue for Keynes, presumably because adverse effects on employment or overall output would be set straight by the state. In fact, having fewer but larger enterprises made macro stewardship of the economy easier. On the other hand, Ordoliberals were appalled at the type of state *dirigisme* Keynes supported,<sup>36</sup> seeing it as an unacceptable subordination of freedom in micro affairs to the macro prerogatives of central planners. Here, indeed, was a major distinguishing theme: Ordoliberals by-and-large thought in terms of micro behavior – shaping the parameters and rules of individual initiative – whereas Keynesians embraced macro management – dictating the ebb and flow of aggregate demand. In addition, “fixed” versus “discretionary” government prerogatives effectively summarized the interventionist methodology of Ordoliberalism and Keynesianism, respectively.

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<sup>36</sup> Röpke wrote: “After the world has for many years – and indeed far too inactively – put up with a devastating depression, people will only be too eager to make every and any sacrifice in order to forestall the repetition of such a tragedy even on a small scale... To make matters worse, even leading economists (particularly the late J.M. Keynes) come and tell us in rather incomprehensible books that what we have to sacrifice for the sake of economic stabilization is... a mere problem of continuously prolonging the boom by means of the business cycle mechanism and thus, in an exceedingly dangerous manner, attention is diverted from the deeper causes upsetting the equilibrium.” (Röpke, 1950: 171-2)

The ontological difficulties of comparing Ordoliberalism and Keynesianism also merit a brief disclaimer. Ordoliberalism is a historical understanding,<sup>37</sup> a philosophical assessment of the optimal economic and legal order. Keynesianism, on the other hand, is a model in the most rigorous way, with assumptions, formulae, quantitative methodology, and an internally coherent mathematics. Any attempt at a comparative analysis, therefore, runs the risk of relating “apples to oranges,” philosophy to econometrics.<sup>38</sup>

In the subsequent historical analysis, it is imperative to keep the two genres of economic thought in mind. A narrative unfolds around the gradual shift, in both academia and policy, from an Ordoliberal consensus in the late 1940s and early 50s to an eventual Keynesian coup. By the end of the 1960s, Keynesianism was the operative blueprint for the economic dealings of the FRG. This dynamic, in turn, provides an instructive framework for approaching broader questions of policy and theory.

## ***4. The Economic Historical Record***

### **4.1. Time Period 1: (1945-1948) “Original Debate”**

**4.1.1. Historical Situation:** Post World War II German policymakers faced an unenviable economic situation: ten million people dead, 81 percent of urban housing destroyed, 740 of 958 important bridges bombed and industry all but halted. (Laqueur, 1993: 6-7) In 1945, industrial production achieved only 10 to 15 percent of pre-war capacity.<sup>39</sup> Agricultural yields fell, such that the average daily caloric consumption per person decreased from the rationed 2000 in 1943 to virtual starvation levels of 700-800 in 1947. (Tuchtfeldt, 1955: 60) Feeding the populace was complicated by a massive immigration of German minorities from Soviet controlled regions, about 10 million by 1950.<sup>40</sup> The Nazi *Zwangswirtschaft* (coercion economy) also remained mostly in place, which continued centralized decision-making over prices, production prerogatives and infrastructure (re)construction. Given a collapse of the monetary system, hoarding was common, as was a proliferation of black market activities. Finally, the former Reich depended on the charity of its victors, who separated it into four administrative zones and imposed often divergent policy agendas.<sup>41</sup>

**4.1.2. Academia:** With this bleak economic picture as a backdrop, German academics in the British and American Zones began to discuss reform. It was obvious to all involved

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<sup>37</sup> This should not be methodologically confused with Historicism (a la Gustav von Schmoller), to which Eucken especially was vehemently opposed.

<sup>38</sup> Nevertheless, Ordoliberalism and Keynesianism remain economic “fruit.”

<sup>39</sup> The severity of the situation has, however, been questioned, notably by Werner Abelshäuser (1975). He pointed to figures such as the productive potential (stock of capital and labor), which at the end of the war remained eleven percent higher than in 1936. I find this argument somewhat analogous to telling a man who has lost both arms and legs “At least you still have your health.”

<sup>40</sup> The population density of West Germany in 1950 was 502 per square mile, compared to 380.5 in the old 1937 Reich boundaries and just 51 per square mile in the US. (Tuchtfeldt, 1955: 61)

<sup>41</sup> For a more immaculate historical rendering of this time period see Nicholls (1994) chp. 5, Laqueur, (1992) Parts 1 & 2, Abelshäuser (2004) Teil II, and Bark & Gress (1989) p. 5-74 among others.

that the Nazi *Zwangswirtschaft* edifice had to be replaced. The question remained, however, with what? Ordoliberal already agreed on basic principles, and went about assertively advancing a free market system based on immediate monetary reform and the cessation of quotas, price fixing, rationing and centralized controls, all the while remaining vigilant about harmful power concentrations at both private and public levels.

Ordoliberal academics pushed their agenda in both the scholarly and popular press. Röpke wrote a vicious polemic, “Die deutsche Frage”<sup>42</sup> in 1945, in which he slammed Germany’s recent totalitarian history and examined the “deeper causes of the German disaster.” He wrote, “National Socialism was not a Dragon lurking in the primeval forests of Germany, but a national variety of a larger zoological species called Totalitarianism, which, for the first time in our modern age, had been bred in Russia in 1917.” (Röpke, 1946: 513) He thus identified economic collectivism as the root evil, condemning the “weak, dishonest or stupid” in the academic profession who had tamely acquiesced to the 1933 collectivization. Röpke’s full wrath fell on those (especially “Prussian” bureaucrats) who continued to assert centralized economic planning after the War. His withering and often vitriolic attacks were echoed, albeit more gently, by Eucken, who wrote several levelheaded critiques of central controls.<sup>43</sup> One of Eucken’s students, Leonhard Miksch, was well placed at the British central economics administration in Minden, which he used as a platform to emphasize the disasters of planning and the promise of free market alternatives. (Nicholls, 1994: 171-72) In 1947, he published a book entitled *Wettbewerb als Aufgabe*<sup>44</sup> which reiterated Ordoliberal principles while focusing in more detail on the exact threats to “full competition”. Such efforts exemplified an Ordoliberal intellectual movement that promoted a common agenda and offered proposals to counter problems of the day.

A wide variety of personalities opposed the liberal position. Each endorsed some form of planned economics. Perhaps the most militant socialist was the union leader Viktor Agartz, who would accept little less than complete state economic consolidation and political centralization. Although in a position of power as head of the Bizonal Economic Administration in 1947, he survived only six months because of quarrel with Allied authorities over his proposed nationalization of coal. (Giersch et.al, 1994: 33) Opposing Agartz’s Marxist approach, the prominent economist Gerhard Weisser published *Form und Wesen der Einzelwirtschaften*<sup>45</sup> in 1947, which asserted the need for both devolved markets and centralized direction. He distinguished between levels of economic activity – the individual, the group, and the total aggregate – each of which required market initiative in some cases and government direction in others. (Weisser, 1947: 27) Overall, the approach was Keynesian in substance, positing a mix of planning and the market, tailored to the particular political situation of postwar Germany. Perhaps the most notable feature of an otherwise rather nebulous analysis, however, was Weisser’s sympathy for certain types of monopoly power. He distinguished in particular “free cartels” and

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<sup>42</sup> Translated (1946) as “The German Dust Bowl.” “The German Question” was too provocative apparently.

<sup>43</sup> See Eucken (1948) “What Kind of Economic and Social System?” & (1948a) “On the Theory of the Centrally Administered Economy: An Analysis of the German Experiment.”

<sup>44</sup> “Competition as the Task”

<sup>45</sup> “Form and Character of the Individual Economy”

harmful “coercive cartels.” (ibid: 75) Taken in total, Weisser simply asserted that good and bad forms existed in every economic phenomenon, and an optimal society maximized the positive, rather than the negative.

The most cohesive set of planning recommendations were to be found in Wilhelm Kromphardt’s 1947 publication *Marktsplaltung und Kernplanung in der Volkswirtschaft*.<sup>46</sup> He proposed inserting market incentives into a planning framework, whereby ration cards issued to each person under government production prerogatives were passed directly to retailers and manufacturers, who would use them to purchase raw materials. (Kromphardt, 1947: 8-9) Thus, ration cards became a de facto currency based on a vaguely price-based system, although one tightly controlled by the government’s *Produktionplan*. (ibid: 10) This method, he theorized, would stop the massive misallocation and psychologically demoralizing nature of centrally controlled systems, while accommodating individual preferences. In addition, implementation was relatively straightforward within existing political and economic frameworks. This idea of *Marktsplaltung*, or “final consumer allocation” within a planned system, proved a popular alternative to Ordoliberalism.

The recurrent problem with all of these planning schemes, whether methodologically Marxist, Keynesian or “pragmatic”, was that they required targeted plans! Yet the optimal goals, say, for coal or pantyhose production (let alone distribution of inputs between the two), remained elusive. In the end, socialist-leaning academics were disunited over both means and ends, positing various mixtures of planning and market economics with diverse and often dubious objectives. While Ordoliberals marched in lock step (ironically perhaps), planners argued with one another. The organizational differences within the academic world were reenacted in political reality.

**4.1.3. Politics:** As economic problems continued to mount, politicians were afforded the unique *Stunde Null* or “Zero Hour” opportunity to start anew.<sup>47</sup> By the time of Viktor Agartz’s acrimonious exit in the summer of 1947, the Bizone Economic Administrative Authority of the combined American and British areas was well established as the economic decision-making body. (Nicholls, 1994: 178) At its head was a Bavarian Christian Social (CSU) politician, Johannes Semler, who proved to be a wishy-washy supporter of both liberal reforms and the entrenched *dirigisme* culture, depending, it seemed, on the audience. Under his auspices, however, a new council of economists from various backgrounds was proposed, such that a balanced ‘objective’ body of internationally respected experts could provide legitimacy for Semler’s politicking amidst Allied indifference and frequent hostility.<sup>48</sup> (ibid: 185) The administrative task of choosing participants and organizing meetings fell to a liberal-leaning economist and Bizone authority, Dr. Hans Möller. Semler’s objectives for the *Beirat* were to remain secret, however, as he was cashiered over an amusing, at least in retrospect,

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<sup>46</sup> “Market-Splitting and Core Planning in the Economy”

<sup>47</sup> Academic conscience again compels mention of Abelshausen, who continued his assault on the popular Zero Hour understanding, most recently in a chapter entitled “Keine Stunde Null” (2004: 22-28).

<sup>48</sup> This council was technically named the *Wissenschaftlicher Beirats bei der Verwaltung für Wirtschaft des Vereinigten Wirtschaftsgebietes*. Henceforth, *Beirat* will suffice.

misunderstanding with American authorities in late January 1948.<sup>49</sup> (Giersch et. al, 1994: 34) Consequently, the “*Beirat*” experts met to discuss Germany’s economic future at the same time a new economic leader was to be chosen.

Möller and his remaining staff brought together a veritable “Who’s Who” of economists, both from within and outside the then governing administrative authority. Inaugural meetings were held in Königstein on January 23<sup>rd</sup> and 24<sup>th</sup>, 1948. Ordoliberalism was represented by a contingent of “Freiburgers”: Eucken, Böhm, Adolf Lampe, Erwin von Beckerath and Miksch, as well as other liberal sympathizers: Rittershausen, Möller, Theodor Wessels and Müller-Armack. The most famous “planners” were also in attendance: including Weisser, Kromphardt, Erich Preiser, a young professor from Hamburg named Karl Schiller, the strong SPD unionist leader Otto Veit, in addition to a cadre of Minden planners such as Günther Keiser and Helmut Meinhold. Occupying the middle “swing position,” were Walter Strauß, Hans Peter, Oswald von Nell-Breuning and Otto Hoffmann. (Möller Archive, *Band 31*)

Semler opened the proceedings with what proved to be his farewell address:

We are all devoting ourselves to questions such as “Where is our economy going?” To what extent can it work by itself and to what extent must it be provided for by state economic administration?...Can the economy operate alone in the interests of the population at large and to what extent is the state and administration forced, for its part, to undertake direction of the economy? To what extent...will it be necessary...to reform the relationship of the state to the individual? (in Nicholls, 1994; 186-87)

Ordoliberals’ emphatic position was aptly summarized as a “*Sprung ins kalte Wasser*.”<sup>50</sup> It entailed a familiar three-pronged plan: a) currency reform, b) the cessation of all price/production controls and c) the control of monopoly power. Rittershausen, Eucken, Miksch and Lampe made the case for immediate monetary reform, citing the dismal conditions of barter exchange and repressed inflation, both consequences of a malfunctioning price system. Any attempt to continue arrangements of fixed prices, Rittershausen said, was “a nearly unrealizable work of art.”<sup>51</sup> (Nicholls, 1994: 188) Keiser and Weisser countered, however, that to let prices loose would simply exacerbate bottlenecks. To this Miksch responded that bottlenecks stemmed from the controls in the first place. He further declared, “The currency reform will already be a total failure if the controlled economy has to be kept going after the reform has taken place.” (ibid: 191) Limiting concentrations of power also sparked debate. Böhm offered forceful voice on the subject, and Rittershausen stated somewhat hyperbolically: “Only if it is possible in the future to be confident that there can in all circumstances be a method of controlling monopolies and positions of market dominance (*wirtschaftliche Vormachtstellungen*), will we be able to find a basis on which to unite all parties in Germany.” (ibid: 188)

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<sup>49</sup> Semler made an unfortunate word choice with “Hühnerfutter” in criticizing US food aid. He was alluding to unnecessary shipments of corn and other such foodstuffs that Germans could (or would) not eat directly. It was translated, however, as “chicken feed,” which offended the magnanimous Allied victors.

<sup>50</sup> “Leap into cold water” or the immediate, no-holds-barred transition to a free market economy.

<sup>51</sup> *ein kaum zu leistendes Kunststück*



Socialists proposed counter-plans, many based on Kromphardt's 'final consumer allocation' ideas. Karl Schiller offered a notable variant. He envisioned the state as a monopolistic power devoted to optimal allocations by rewarding resources to firms with the lowest costs. Thus, a mixed system of competitive cost schedules would determine the distribution of resources, while the state reserved the final word in setting national output and employment goals.<sup>52</sup> (ibid: 194) Socialists also pointed out that impending Marshall Plan aid presumed a centrally administered approach, as the U.S. required concrete economic plans and European-wide coordination before disbursing funds. (Giersch et. al; 1994: 96-97)

Although not recognized at the time, many of the socialist's plans reflected Keynes' ideals, with market forces combined with frequent government intervention to preserve full employment, affordable pricing schemes, and growth targets. The inherent problem, however, was that no matter how well reasoned such ideas were, they posited at least the partial perpetuation of defunct war controls still in place. It was much less persuasive to argue that the current planning and price fixing were a disaster, but this other (similar) type of planning and price fixing would work. Those who advocated a total overhaul, the 'leap into cold water,' held a rhetorical advantage. By the end of the first day, Franz Böhm was elected chairman of the *Beirat* and Ordoliberal opinions represented the majority. (Nicholls, 1994: 191)

Simultaneous with the ascension of Ordoliberalism as the guiding doctrine for reform in the *Beirat*, Ludwig Erhard was chosen as Semler's replacement in the Bizone. He brought distinct liberal credentials and a dogged persistence to the post. His unabashedly liberal ideas, however, inspired much incredulity, especially among the entrenched Minden authorities. Twelve days into Erhard's term on April 18, 1948, the *Beirat* issued its final memorandum. Ending the 1936 price freezes and introducing immediate monetary reform were the main proposals, followed by an abolition of all controls on industrial production save those on import licenses. Just as important, however, was the content of recommendation 12: "To prevent the abuse of economic power the *Beirat* believes the immediate and effective control of monopolies and their pricing policy to be indispensable." (Nicholls, 1994: 204-5) These admonishments echoed Erhard's views (Goldschmidt, 2004: 12) and provided the domestic intellectual legitimacy he required to implement his policies without delay.

In retrospect, the *Beirat's* debate was a microcosm of the political and intellectual climate in 1948 West Germany. Opinion was firmly divided between Ordoliberals and various planners, yet those supporting free markets benefited from an academic consensus and their unambiguous opposition to existing planning schemes. In the battle of ideas, postwar Germany proved the ideal political and economic environment in which to assert the Ordoliberal agenda.

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<sup>52</sup> Twenty years later, as we shall see, a variant of this same "*Globalsteuerung*" approach would again resurface in German economic policy.

## 4.2. Time Period 2 (1948-1952) “Social Market Economy”

**4.2.1. Historical Situation** – On June 20, 1948 the Bizone implemented a radical monetary reform. The Deutsche Mark (DM) replaced the Reichsmark with a conversion ratio that was drastically scaled according to the character of the debts, from zero (public debts), 6.5 percent (bank deposits and reserves), 10 percent (mortgages and private debt) all the way to a 1:1 per capita exchange rate for the first 40 DM. (Hardach, 1980: 107) Therefore, every individual was extended 40 DM (with 20 more two months later) and firms were granted 60 DM per employee. Public authorities collected the equivalent of one month’s revenue. (Giersch et. al, 1994: 36) In total, 93.5 percent of the former monetary stock was withdrawn from circulation, with more than 400 billion in RM claims and liabilities nullified. (Braun, 1990: 155) Along with the actual currency reform, Erhard’s liberalizations took effect. On the twentieth, 400 items were immediately removed from the list of controlled commodities. By July 1948, ninety percent of the previously existing price controls were abolished, formally ending the 1936 price freeze. (Stolper et. al, 1967: 228)

The immediate results of the reform remain a thing of lore. “Almost overnight, shops were again full of goods that had not been seen for years; production rose by 50 percent within six months, and in the following year it increased by an additional 25 percent.” (Laqueur, 1992: 82) The mere hint of a stable money provided the impetus necessary for long-repressed consumer tendencies to manifest in force. It also brought the rampant black market above board, such that huge stocks of hoarded goods were instantaneously transferred into the legitimate economy. (Braun, 1990: 155) This eruption of consumer demand led to massive increases in production and jobs creation in a short period of time.

Not all the consequences were favorable. Despite a huge monetary contraction, the massive unleashing of consumer demand was immediately reflected in prices. Four months after the reform, consumer prices rose at an annualized rate of 33.1 percent, while producer prices skyrocketed 45 percent. (Giersch et. al, 1994: 42) Labor unions declared a general strike on November 12, 1948, agitating for the resumption of price controls. (Hardach, 1980: 108) Economic authorities did not flinch, however, realizing that short-term inflation was inevitable in an economy where prices had been frozen at unnaturally low levels for twelve years. In addition, the growth of consumer demand (which caused prices to rise in the first place) meant handsome profits for industry, which began investing and expanding production. By 1949, the first threat to the market economy, inflation, was over. (Stolper, 1967: 230)

A second major challenge emerged with unemployment. Employment seemed to increase steadily – from June to December 1948, by 230,000 new jobs alone – yet the net statistics, given the colossal influx of refugees, remained dismal. Despite annual growth rates of over 25%, the West German economy could not produce jobs quickly enough. At its peak, the unemployment rate was 12.2 percent in March 1950. (Giersch et. al, 1994: 46) Once again, Erhard and the other Ordoliberal policymakers did not blink from the barrage of Keynesian criticism and dire predictions of impending economic and social

implosion.<sup>53</sup> They stood behind the maintenance of price stability and economic non-intervention, rejecting short-term fiscal employment stimulus.

By 1950, the crisis of the pre-Reform German economy was mostly resolved. However, one major sector remained rigidly controlled: the current account (imports/exports and the balance of payments.) The Joint Export-Import Agency (JEIA) was the Bizone's foreign trade authority from 1947 onward. It organized its negotiations in two categories. The first concerned goods that satisfied the basic needs of the West German populace, such as food, energy, pharmaceuticals, and agricultural supplies. This was financed at first by the Allied authority and later by Marshall Plan funds. "Category B," or the raw materials for industrial production, had to be paid for in dollars earned from export earnings or trade within the European economic area. (Braun, 1990: 156) War-torn Europe had a hard time coming up with exportable goods, and there was a chronic dollar shortage. This disequilibrium was acute in West Germany, where the current account deficit totaled 158 million dollars in 1949 and 243 million in 1950. (ibid: 157) This deterioration led to the European Payment Union (EPU), which together with the Marshall Plan sought to liberalize trade relations among European countries. In essence, an aggregation of Europe's current account balance verses the United States occurred. Each country was granted a certain amount of multilateral credits, which diminished European reliance on physical dollars to conduct trade with one another. In retrospect, the very concept of a rigid quota-based current account system to encourage free trade produced a paradox. Indeed, Erhard was a vociferous opponent of the scheme, and the JEIA was one of his favorite targets. (Nicholls, 1994: 211)

Simultaneous with the founding of the EPU in June 1950, war broke out on the Korean Peninsula. A resurgence of war demand in the USA created a drastic balance of payments crisis in Germany. After only two months, Germany had exhausted 60 percent of its annual EPU quota, as a rapidly expanding economy demanded larger amounts of imported resources in an increasingly competitive international marketplace. In June of 1950 Germany's deficit in the EPU area was 7 million dollars, but by early October the debt rose to 71 million. (Giersch, et. al, 1994: 102) Erhard did not waiver from his liberalizing agenda, optimistically predicting the crisis would soon pass.<sup>54</sup> Indeed, the Korean War and its ensuing boom stimulated global demand, placing Germany's increasingly reconstructed industry in the perfect position to export to the rest of the world. (Stolper, 1967: 233) By the end of 1951, the current account rose to a 392 million dollar surplus, a remarkable swing of 635 million dollars in one year. (Braun, 1990: 157) The Ordo-liberal inspired Social Market Economy weathered yet another storm.

By 1952, the *Soziale Marktwirtschaft* was firmly entrenched. It had transformed the economy overnight and bested initial inflation, unemployment, and a balance of payments crisis. The stage was set for "*Wirtschaftswunder*."

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<sup>53</sup> The academic substance of these critiques will be thoroughly discussed in the next section.

<sup>54</sup> After an internal spat of some ferociousness, an investment plan was enacted in January 1952 (by which time the crisis was over). It allowed for government investment of DM 1 billion in large concerns such as coal, steel, and electricity. (Van Hook, 2004: 228) Abelshauser (2004: 166) characterized the event as a "retreat to the Corporate Social Market Economy" and the functional end of liberal policy in the FRG.

**4.2.2. Academia** – “*Währungsreform*” (monetary reform) was a much-debated topic in post war Germany. A surfeit of proposals surfaced on the issue: from the watershed Colm-Dodge-Goldsmith act, to the numerous separate “plans;” including the Warenmark, Lampe, Hoffmann, Pfeleiderer, Ilau, Dalberg and Keiser designs. Advisory opinions (*Gutachten*) were issued by Eucken and Miksch on one side of the ideological spectrum and Veit and Schumacher on the other. (Möller, 1961) When Erhard pushed through the reform on June 20, 1948, it was crafted and implemented mostly by the Western Allied authorities. (Giersch et. al, 1994: 36) However, Americans and the British did not control the intellectual agenda. Erhard embodied the Ordoliberal vanguard, forcefully asserting an end of controls to coincide with the increasingly successful currency reform. On June 22 he declared, “The entire body of economic legislation which has hitherto governed trade and industry in the combined American and British Zones of Occupation is to be completely terminated – at least in regard to controls and prices...A wide measure of agreement has been obtained on the need to annul the bulk of the current legal provisions to coincide with the Currency Reform.” (Erhard, 1948: 31)

Perhaps Erhard’s “wide measure of agreement” referred to the academic *Beirat* recommendations, but it was clear that significant resistance remained to his liberal machinations. The famously eccentric<sup>55</sup> *Die Zeit* journalist Countess Dönhoff wrote in 1948 “If Germany were not already ruined, this man, with his absurd plan to abolish all controls, would certainly bring that ruin about. God protect us from him ever becoming Economics Minister. That would be the third catastrophe after Hitler and the dismemberment of Germany.” (in Nicholls, 1994: 212) More concrete criticism emanated from prominent socialists like Eduard Heimann, who lamented the transitional costs of Erhard’s “leap into cold water,” which included unpleasantly high unemployment:

Professor Erhard, Economics Minister of the Federal Republic of Germany...has proceeded to demolish economic controls in that impoverished country in the frankly expressed belief that some unemployment is a good thing for the economic system. The Marxist theory of the industrial reserve army as indispensable for capitalism and profit is thus accepted by the modern liberals, and they choose capitalism rather than full employment. (Heimann, 1950: 273)

Heimann was indicative of a “class warfare” critic, many of whom labeled Erhard’s liberalizing as an inevitable return to *Laissez faire* robber-baron capitalism. On the academic side, a kindred socialist spirit, Erich Preiser, wrote critiques in a more Keynesian vein. His article “The Social Problems of the Market Economy”<sup>56</sup> favored government interventions, such as directed infrastructure and capital investment to resolve “real structural and systematically chronic unemployment.”<sup>57</sup> (Preiser, 1951: 17) He proposed a Keynesian scheme of pre-financing investment through money creation. (Giersch et. al, 1994: 56) Only after full-employment policies were implemented, was one “allowed” to speak of a socialistic Market Economy.<sup>58</sup> (ibid: 25)

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<sup>55</sup> See her famous autobiography (1988) *Kindheit in Ostpreussen*, (Berlin: Siedler Verlag)

<sup>56</sup> “Die soziale Problematik der Marktwirtschaft” Incidentally, it was written as a response to Franz Böhm’s influential article “Die Aufgaben der freien Marktwirtschaft.”

<sup>57</sup> “Die echte strukturelle Arbeitslosigkeit und eine systembedingte chronische Arbeitslosigkeit”

<sup>58</sup> “Nur wer sich dieser Gesamtaufgabe bewusst ist, darf von sozialer Marktwirtschaft sprechen.” Notice the subtle response to Böhm’s title by using the term “Gesamtaufgabe.” (or *Total* challenges)

Karl Schiller also published profusely, focusing his critiques on governmental non-intervention and the lack of macro controls. In a 1951 lecture, Schiller highlighted the four largest problems existing in the economy: 1) the unacceptable span separating production indices and synchronized investment 2) the pervasive investment difficulties of the “*ordnungspolitische Wirtschaftsverfassung*” in optimally apportioning raw materials 3) the disproportionate income distribution between the different Länder which was also a problem of effective investment and 4) the worsening of Germany’s “terms of trade” relative to other European countries (stemming from the Korean Boom’s price-relations), damaging external trade balances, which Schiller labeled as Germany’s greatest threat. (Schiller, 1951: 7)<sup>59</sup> He thus proclaimed the debate over government direction “in the blink of an eye” became obsolete.<sup>60</sup> It was obvious to him that the market alone could not solve these problems; government involvement was required to guide investment, income distribution and the external trade balance.

Despite these protests to Erhard’s deregulation and non-intervention, Ordoliberalism held the trump card and that was success. Their ideas had been implemented and flourished. As Erhard stated triumphantly ten weeks after the Reform:

Prior to the Currency Reform, the economy could no longer be described as functioning properly. A highly developed and sophisticated market had relapsed into the methods of a primitive barter economy as a result of the monetary chaos and the megalomaniacal (sic) insolence of the bureaucrats in our centrally controlled economy. All orderly forms of production had ceased. What remained was a soulless jumble of frightened individuals, devoid of any sense of responsibility, with everyone solely concerned to cling to his or her individual existence. In the meantime, we have overcome this situation. It seems like a miracle – although it was just judicious planning in the best sense of the term – that we managed to master this social chaos within a matter of days thanks to a new currency and a resolute shift in economic policy. (Erhard, 1948a: 36)

The critics of Ordoliberalism simply could not compete with the basic tenets of market allocation, which had indeed proved to be the antidote to the hated *Zwangswirtschaft*. Planners were thus thrust into intellectual disarray. Some continued to fulminate the hackneyed Marxist collectivization doctrine while others, such as Preiser and Schiller, adopted overt Keynesian motifs. This internal division of the left transferred into the political realm, ensuring the Ordoliberal grip on politics for years to come.

The period of 1948-1952 proved to be the Ordoliberal heyday. Their ideas garnered practical legitimacy, outpacing other schools of thought. Liberal ebullience would be cut short, however, by the early deaths of the “father” of Ordoliberalism, Walter Eucken, and his well-connected student, Leonhard Miksch, in 1950. These two staunch “defenders of the faith” would be missed.

**4.2.3. Politics** – The first democratic elections for West Germany’s future government were held on August 14, 1949. They featured a pitched battle between a pre-war party, the Social Democratic Party (SPD) and the newly formed Christian Democratic Union

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<sup>59</sup> Interesting here is the overt challenge to Ordoliberalism, as Schiller posits only the state is able to optimally determine overall investment. He cites the British Socialist T. Balogh’s *Germany: An Experiment in “Planning” by the “Free” Price Mechanism* (Blackwell, Oxford) as evidence that even after 18 months “new bottlenecks” continued to appear in the economy. (Schiller, 1951: 11)

<sup>60</sup> “Ein Problem ‘Lenkung, ja oder nein’ existiert also im Augenblick nicht mehr.”

(CDU).<sup>61</sup> Unsurprisingly, the major debate hinged on economic policy. Erhard's success was already well advertised in the voting populace, but the SPD continued to assail his "social market economy" as a disgrace to *their* word, the appropriation of which masked a process whereby discredited capitalist forces and old Nazi industrialists were returning to power. (Nicholls, 1997: 68) The SPD and its fiercely dynamic leader, Kurt Schumacher, utilized the tried and true capitalism vs. socialism campaign rhetoric. By 1949, however, Erhard's program was already an unequivocal success, and in his statements he espoused a vernacular that eschewed Marxist jargon. He spoke endlessly of markets, competition and freedom. The SPD alienated many voters who felt genuinely liberated and more prosperous.

Konrad Adenauer, the former Lord Mayor of Cologne and head of the CDU, noticed Erhard's popularity and invited him to join the CDU, proposing that the Social Market Economy become the permanent economic platform of the party. The "Düsseldorf Principles" of July 1949 enshrined Erhard's policies as the official party program. In August, German voters cast ballots for their first parliament. Of 31.2 million eligible voters, 24.5 participated (78.5 percent) with the results as follows: CDU/CSU 31%, SPD 29.2 %, the Free Democrats (FDP) 11.9% and the twelve other parties and independents 27.9 percent.<sup>62</sup> (Bark & Gress, 1989: 243) The political legitimization of Erhard's program passed by less than two percent, although a later coalition of the CDU with the FDP (among others) expedited governmental workings.

Many in the SPD, especially Schumacher, were enraged by the results of the election. It was an affront to their dignity, to have suffered so much during the Nazi time only to be removed from economic decision-making. During Schumacher's post-election rants, however, he confirmed the SPD's socialist leanings, sticking to the complete socialization of natural resources and heavy industry. (Bark & Gress, 1989: 244) His opposition to Adenauer was impassioned; there was even an incident in late 1949 when he was banned from Bundestag debate for several days after violating parliamentary procedure. (Nicholls, 1997: 90) Shut out of government and increasingly rebuffed by German voters and the Allied authorities, the SPD struggled to compete with the Adenauer government. In 1953's election, the CDU/CSU/FDP received 56.7% of the vote, increasing their majority in the Bundestag by exactly 100 seats.

### **4.3. Time Period 3: (1952-1960) "Wirtschaftswunder"**

**4.3.1. Historical Situation** – A sense of fond nostalgia for the 1950's remains engraved in the collective German memory. The numbers were truly astounding, worthy of the

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<sup>61</sup> Along with their allied Bavarian wing, the CSU.

<sup>62</sup> By zones, the CDU gained 67, 45 and 27 seats in the British, U.S. and French zones, respectively, while the SPD won a corresponding 78, 41 and 12 respectively. (Heidenheimer: 177) This is interesting, as essentially, it was the French zone (the area not immediately in the Bizonia authority) that won the election for the CDU.

label “economic miracle.”<sup>63</sup> (See Figure 1) For the decade, annual GDP growth averaged 8.3 percent, with unemployment falling from 11 percent in 1950 to 1.3% in 1960 despite a population increase of 5 million people. Real wages also increased at a healthy average rate of 6.8 percent. Most unusual for a period of explosive growth, decreasing unemployment and strong wage growth, prices did not rapidly increase. Inflation averaged 1.36% over the decade. Wage gains were therefore transferred almost intact to consumers. High GDP and population growth, low unemployment, wage increases, and low inflation were indeed recipe for *Wirtschaftswunder*.<sup>64</sup>

**Figure 1: Macro Economic Data in Germany from 1950 – 1960**

	<b>GDP Growth (%)*</b>	<b>Un-employment Rate (%)</b>	<b>Population (in 1,000)</b>	<b>Wages **</b>	<b>Prices †</b>	<b>Real Wage Change (%)</b>
<b>1950</b>	-	11	50,958	136	26.4	-
<b>1951</b>	9.7	10.4	51,435	153	28.4	12.24
<b>1952</b>	9.3	9.5	51,864	167	29	9.36
<b>1953</b>	8.9	8.4	52,454	176	28.5	5.38
<b>1954</b>	7.8	7.6	52,943	180	28.6	2.27
<b>1955</b>	12.1	5.6	53,518	193	29	7.01
<b>1956</b>	7.7	4.4	53,340	209	29.8	8.14
<b>1957</b>	6.1	3.7	54,064	220	30.4	5.18
<b>1958</b>	4.5	3.7	54,719	231	31.1	4.97
<b>1959</b>	7.9	2.6	55,257	244	31.3	5.51
<b>1960</b>	8.6	1.3	55,958	264	31.8	8.00

\* GDP price adjusted: chain-linked index (year 2000 = 100)

\*\* Average gross monthly earnings (in present euro)

† Consumer price index for 4-person-households with medium income wage earners (1995 = 100)

Source: *Statistisches Bundesamt*, <http://www.destatis.de/>

<sup>63</sup> The 1950s economic boom was not, however, a unique German phenomenon. The decade witnessed healthy, but not “miracle” growth in most Western countries:

<b>Country</b>	<b>Ave. GNP Growth 1949-54</b>	<b>Ave. GNP Growth 1954-59</b>
<i>West Germany</i>	8.4	6.6
<i>Austria</i>	5.7	5.7
<i>Italy</i>	6.4	5.7
<i>France</i>	4.8	4.1
<i>Belgium</i>	3.7	2.5
<i>Great Britain</i>	2.7	2.3
<i>Denmark</i>	3.7	3.4
<i>Switzerland</i>	5.7	4.6
<i>Finland</i>	5.3	3.5
<i>The Netherlands</i>	4.9	4.1
<i>USA</i>	3.6	3.3

Source: Abelshauser (1975) pp. 12

<sup>64</sup> All figures from *Statistisches Bundesamt*, <http://www.destatis.de/>; author’s calculations

While we recognize in retrospect the 1950's economic performance as an extraordinary circumstance,<sup>65</sup> continuing prosperity infused ordinary Germans with an infectious optimism.<sup>66</sup> Although only a decade removed from postwar economic disaster, the Ordoliberal lessons were rapidly being pushed to the back burner. There was a tendency to forget the original importance of limited government intervention.

The drastic turn around of Germany's economy also affected the fiscal picture. By 1952, a country with long institutionalized memory of massive deficits had balanced its national accounts. In 1955, Bonn was running a 1.3% surplus, the accumulation of which was invested by Finance Minister Fritz Schäffer at the central bank with an eye towards reconstituting Germany's military. Excess revenues became known as the *Juliusturm* (Julius Tower), a reference to the fortress where Prussian kings had stored their war booty. (Braun, 1990; 179) The figurative "piles of cash" further eroded the sacrificing *Sprung ins kalte Wasser* mentality of politicians and citizens. Ordoliberal successes bred complacency and apathy; economic triumph paradoxically signaled doctrinal irrelevance. In the eyes of many, and certainly an increasingly reformed SPD, the time had come to apportion the spoils of *Wirtschaftswunder*. Newfound thriving circumstances seemed to demand, illogically, a reappraisal of the hitherto Ordoliberal policy.

**4.3.2. Academia** – Socialist thinkers and politicians were forced to swallow their previous theorizing and politicking during the implementation of Erhard's Social Market Economy. Not only were Ordoliberal ideas proving economically successful, but electorally-speaking, the old collectivist ideals were being trounced at the polls. Wilhelm Röpke summarized the socialist's dilemma: "Ludwig Erhard and his group stepped into a situation of so-called repressed inflation which was really nothing less than the stark and complete bankruptcy of inflationary collectivism, countered with a resolute return to the market economy and monetary discipline. What is more, Erhard was unsporting enough to succeed beyond all expectations." (Röpke, 1960: 23) Gisbert Rittig termed it the "Crisis of Socialism." (Rittig, 1955: 5) Socialists required fresh ideas that could unite, reinvigorate, and inspire people in both intellectual and political circles.

At the forefront of this redefinition was the now famous professor from Hamburg, Karl Schiller. As early as the *Beirat* debates he had become an advocate of the Keynesian "mixed" economy, with macro planning added to individual initiative. During the 1950's, his ideas solidified. In 1953, he published *Challenges and Trials: to a New Order for Society and Economics*,<sup>67</sup> a compilation of his lectures. In it, he laid the groundwork for the "practical character of our economic policy from a socialist standpoint." (Schiller, 1953: 139)<sup>68</sup> It eschewed what Schiller vividly called the "sinister and ghastly experiment

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<sup>65</sup> Relating, as Abelshauser wrote, to the reconstruction of a destroyed Germany (2004: 281).

<sup>66</sup> See Haselbach (1998). He asserted that in a post-Nazi society stripped of nationalism and an acceptable unifying culture, economic success attained symbolic significance in the recreated "German identity." When a downturn did eventually occur, however, it was therefore not just economic in nature, but a direct attack on the new German identity, making policy responses emotionally charged and often irrational.

<sup>67</sup> *Aufgabe und Versuche: Zur Neuen Ordnung von Gesellschaft und Wirtschaft*

<sup>68</sup> "Thesen zur praktischen Gestaltung unserer Wirtschaftspolitik aus sozialistischer Sicht"



with totalitarian socialist systems”<sup>69</sup> in favor of a free market with full competition. (ibid: 140) The complete implementation of Ordoliberal ideas, however, was not desirable. In the end, the state remained responsible for “coordinating” the total economy. (ibid: 144)

Protecting the democratic process, Schiller claimed, could not be left to impersonal market forces, and all possible tools necessary to achieve a better social coordination should be at the macro planner’s disposal. (Schiller, 1953: 166-7) One source of abuse was the over-concentration of market power. Like the Ordoliberals, Schiller continually returned to this point, except that he wanted the government to assert a more proactive (instead of just a regulatory) role. With a centralized investment plan and an “expansionary stability mechanism,” the government could approach full competition policy with unbounded capabilities. (Schiller, 1968: 58) Ordoliberal approaches, on the other hand, treated competition policy like a “muted trumpet,” they lacked macro stability and direction tools necessary to complete the job.<sup>iii</sup> This proved to be a shrewd political argument, as it coincided intellectually (albeit not in the policy realm) with the views of Erhard, thus blurring the line between Ordoliberal and Keynesian philosophy.

Schiller was less receptive to Ordoliberal worries concerning inflation. Their logic, he noted, was premised on a mistaken historical anxiety; contrary to the situation after the First World War in which massive reparations were paid by the printing press, in 1945 all war debts were nullified. Thus, he concluded that democracy was secure.<sup>iv</sup> Policy makers could use expansionary monetary and fiscal tools to guide the new, financially stable democracy, options which were absent in the interwar period. Why then deny the nascent West Germany potentially useful Keynesian policies? Optimally, there would be a *staatliche Preispolitik* that emphasized a systematic *Wirtschaftsplanung* input-output analysis.<sup>70</sup> (ibid: 146-7) He concluded in language that could be mistaken for the ecumenically-inclined Eucken or Müller-Armack; market freedom and government-directed ordering were intertwined in a “Higher Bond” that Christian values and social brotherhood endorsed. They could not be separated.<sup>v</sup>

Schiller’s colleagues remained unclear about the basic premises of his ‘new socialism,’ which he characterized as “market forces where possible; planning where necessary,”<sup>71</sup> so he published another pamphlet entitled *Socialism and Competition*.<sup>72</sup> In it, Schiller tackled the persistent question “what is socialism?” By way of an answer, he conceived of merging free markets and social prerogatives through comprehensive income, price, tax, and full employment policy. (Schiller, 1955: 32-33) In the new socialism, the *leitmotif* was providing equal opportunity for all to participate in the market economy and reap its benefits. Government ownership with its authoritarian dictation of micro

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<sup>69</sup> “unheimlichen und grausamen Experimente totalitär-sozialistischer System”

<sup>70</sup> Schiller’s italicized German is especially emphatic here, stressing the need for State price policy and central economic planning.

<sup>71</sup> “Wettbewerb soviel wie möglich, Planung soviel wie nötig” (Schiller, 1955: 29) Technically, the translation is “Competition as far as possible, planning as far as necessary” but variations on the theme occur with regularity. The statement is often cited (inaccurately perhaps) as the “summing-it-all-up” philosophic phrase behind the Social Market Economy. (see Laqueur: 206)

<sup>72</sup> *Sozialismus und Wettbewerb*, (1955)

incentives and production quotas were passé; socialism was defined as pursuing socially-oriented macro goals by means of market allocation.

Schiller was not the only prominent academic to advance a mix of government planning and free markets as the new social alternative. Astonishingly, given the author's previous devotion to total state control and planning, Gerhard Weisser wrote an article in 1956 entitled "The Multifarious Ways of Social Life."<sup>73</sup> He wrote, "Democracy is an indispensable postulate from the standpoint of every free political movement; but it alone is not enough to vouchsafe the freedom of social existence."<sup>vi</sup> (Weisser, 1956: 168) Government intervention was needed to complement the basic democratic and individualistic market economy, until the social character of life was guaranteed, thereby truly ensuring universal freedom.

Erich Preiser was also a Keynesian convert. In a volume of essays on business cycles in the postwar world, Preiser and his assistant Wilhelm Krelle attempted to refute the traditional analysis of the German miracle "that *all* investment in Germany so far has been autonomous;" i.e., Germany's sudden recovery was achieved without centralized demand management. (Preiser & Krelle, 1955: 123) In their argument, the authors reinterpreted Erhard's Ordoliberal miracle as the sum product of various Keynesian stimuli, both fiscal and monetary. Traditional socialists began to rationalize Ordoliberal successes in terms of Keynesian logic.

To begin with, they reevaluated June 20, 1948: "the creation of money connected with the currency reform led to a significant expansion of consumer demand, to increases in prices and production, and to high profits." (ibid: 147) This observation was right out of a Keynesian textbook; inflate the money supply and consumer demand increases.<sup>74</sup> The next year witnessed, however, only modest intervention, and thus little progress:

The period between the spring of 1949 and the spring of 1950 may briefly be characterized as a period of general return to normal economic conditions. It was marked by rising output, falling prices, slightly falling profits and unchanged investment; while employment did not continue to rise, it did not fall either, yet unemployment increased. (Preiser & Krelle, 1955: 149)

In other words, the Ordoliberal's focus on prices and reducing government controls led to a stagnating labor market. The following year they returned to macro fiscal management, including public works projects and "refinancing aid" plans.<sup>75</sup> (ibid: 150) "Summing up, it can be said that between the spring of 1950 and the summer of 1951 the upswing in the economy, which had been slowly induced by expansionary policies, was propelled into a boom by the outbreak of the conflict in Korea. The government's program, political expectations, and the rise in world market prices were the essential determining factors of this development." (ibid: 152) Once again, price inflation and government intervention were painted as the major determinants of success. Finally, a "settling down economy" after the summer of 1951 could be traced to government handling:

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<sup>73</sup> A better translation of *Vielgestaltiges soziales Leben* than "Polymorphic social life"

<sup>74</sup> Never mind that the stated methodology of the Reform drastically *decreased* the supply of money.

<sup>75</sup> In rebuttal, it might also be said that keeping a constant percentage rate of employment was actually a remarkable feat given a migration of 10-12 Million refugees in the decade following 1945.

It became more and more apparent that a further increase in the social product had become dependent upon the elimination of bottle-necks...A number of proposals and plans to this effect were put forward; the one finally chosen was the so-called Investment Aid to industry. Under this plan it was proposed to raise 1 billion DM through contributions by firms, for the purpose of investment in bottle-neck sectors. (ibid: 153)

It was thus necessary for government to step in and mitigate bottlenecked sectors. For Preiser, fluctuations in investment, prices, output and employment were glibly explained using Keynesian lingo.<sup>76</sup>

Given the rapid transition of many socialist thinkers from Marxist concepts to Keynesianism – and their appropriation of previously scorned ideas such as competitive markets in the process – one might expect a strong response from the Ordoliberal establishment. This did not occur. Eucken and Miksch were dead. Böhm was fully involved trying to see his monopoly and market power concerns through the Bundestag, Rüstow was ensconced writing his three-volume epic<sup>77</sup> and Erhard and Müller-Armack were too busy with quotidian matters at the Ministry of Economics to engage in academic debate. The only figure who picked up on the socialists' shift (and had the time to sufficiently address it) was Röpke. He published a short article, "Front Lines Old and New in Economy Policy" in 1958:

A few days ago, I received a newspaper article from Germany in which my friendly opponent of 1947 had written warm words of approval for the market economy, a competitive price-system and private ownership; and he clearly found nothing in this view that was irreconcilable with the apparently unchanged opinions and attitudes of a convinced Socialist. Now a change like this, made within the space of a mere ten years, is quite astonishing, and I am inclined to regard it as all the more significant because it is typical of the situation, in theory and in practice, in which the Socialist movements of the free world find themselves today. (Röpke, 1958: 94-5)

Socialism, Röpke explained, had "shifted attack," and now stood for the "Welfare State," based on fiscal policy, full employment, and continuous wage increases. (ibid: 98) These interventions Röpke wrote – in direct response to the 'bottleneck' assertions of Preiser and Krelle – would prove harmful in the long run:

Any increase in State interference which could deflect the market economy from the course set by competition and price adjustment, any excess of arbitrary rules and regulations, any curtailing of incentives, any official price-fixing or limitations set to the fundamental economic freedoms will lead to failures, bottlenecks, diminished achievement and destruction of the market equilibrium. It is true, these will be dealt with fairly smoothly at first. But as interference increases, so will they grow until they finally become

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<sup>76</sup> Preiser was not the only prominent socialist economist to rationalize economic conditions in terms of business cycle policy. Fritz Baade of Kiel University wrote a pamphlet in 1955, "Einige Grundsätzliche Gedanken zur Konjunkturdebatte" (Several Theoretical Foundations for Business Cycle Debate) in which he distinguished between "Orthodox" non-interventionism and "Reformer" Keynesian active policy, siding with the latter in terms of "mobilizing the working reserve and directing investment" (Baade, 1955: 156)

<sup>77</sup> Rüstow, A; (1950, 1952, 1957) *Ortsbestimmung der Gegenwart: Eine universalgeschichtliche Kulturkritik*, v. 1, 2, 3. Rüstow did, however, publish an article called "Wirtschaftsethische Probleme der sozialen Marktwirtschaft" (Ethical Economic Problems of the Social Market Economy in Boarman, 1955) which included the relatively famous phrase: "Konkurrenz ist nun einmal keine Solidarität." (Competition is now not social solidarity) (ibid: 54) Hardly what one would call a ringing rebuke of the socialist's interventionist leanings, although Rüstow did go on to say religion and other non-economic phenomena should provide the necessary social glue.

a public catastrophe. And the worst of it is that these disturbances caused by State interference are put forward as proof of the inadequacies of the free economy itself, and taken as an excuse for still greater degrees of interference, while it is not everyone who can see that the fault should be laid at the door of interference in the first place. (Röpke, 1958: 100)

In a single statement, Röpke criticized the premises of both Schiller (mix market and planning) and Weisser (real ‘freedom’ requires planning):

True, it is certainly a step forward that the Socialists who have been converted to the idea of a free economy should have put forward the slogan, “market economy where possible; planning where necessary,” for this shifts the burden of proof onto the planner. But in applying this maxim, what becomes important is how much proof is required; and unfortunately the Socialist is still the sort of man whose spiritual constitution allows him to take the increase of constraints on society far more lightly than others – and this is not in the least affected by his contention that it is often in the name of freedom that he accepts them. (Röpke, 1958: 102)

Röpke made it clear that the new socialism was just as bad as the old, perhaps even worse because it shrouded itself in the misleading vernacular often associated with Ordoliberal successes. Indeed Röpke’s assertion, essentially, that “a wolf in sheep’s clothing is still a wolf” was to prove prescient.

The turbulent academic debate of the 1950’s was of decisive importance to the German political and economic situation. Recognizing a bankrupt theoretical body, Karl Schiller almost single-handedly transformed Marxist socialist tendencies to Keynesianism. As earlier noted, even when Ordoliberalism was ascendant, there was scant agreement on the “social” facet of the *Soziale Marktwirtschaft*. Suddenly, socialist thinkers had the answer, and it was Keynesianism. What better describes the mandate of a “social market economy” than the undeniably pragmatic statement “market whenever possible, planning where necessary?”

**4.3.3. Politics** – It would be a mistake to ignore the political contributions of the SPD in the aftermath of their 1949 electoral loss. Despite formal exclusion from the ruling coalition and consistent internal wrangling over party doctrine, the SPD remained a forceful voice for large segments of the population, especially workers’ interests and unions. Nor were the Social Democrats impotent in influencing the policy-making process. The largest SPD victory in the early fifties was actually conceived and passed by CDU forces: the “Betriebsverfassungsgesetz,” or a constitutional protection of worker’s rights. On July 19, 1952, the Bundestag passed a law that mandated labor be represented (with voting rights) in any enterprise with more than five employees. The law also provided guarantees on liability compensation, cooperative associations (like unions), health insurance, and the equivalent of third representation at the corporate board (*Aufsichtsrat*) level. (Heilemann et. al; 2003: 36) This law enshrined in German industrial relations the principle of *Mitbestimmung* or “Codetermination.”

The Ordoliberals were not as enthusiastic about *Mitbestimmung*. The faint distinctions, in practice, between “co-ownership” and “co-determination” raised eyebrows. More troubling, the new arrangement legislated an incestuous sort of bargaining process, a

circumventing of competitive wage setting (and therefore real prices).<sup>78</sup> The concentration of economic power in this manner was anathema. Yet, the idea was well-liked among the electorate and Adenauer, whose adherence to Ordoliberalism lasted only insofar as they remained politically popular, seized the opportunity to make CDU inroads in the SPD “proletarian” constituency.<sup>79</sup> (Nicholls, 1994: 309-10) For the SPD, codetermination was an ideological coup against liberal economic policy. However, Adenauer’s shrewd political support for *Mitbestimmung* blurred the political lines for traditionally SPD blue-collar voters, and thus it most likely contributed to the CDU’s landslide victory in 1953.<sup>80</sup>

In the meantime, Schiller was working to move his party towards a Keynesian economic platform. In the wake of their 1953 electoral collapse, the SPD met in Berlin in July of 1954. Schiller asserted his intellectual ideas. The resulting “Berliner Aktionsprogramm”, however, did not officially replace SPD protocols, which continued the mostly Marxist party doctrine with a vaguely Keynesian bent, what Otto Veit summarized as the “Magna Carta of liberating the worker.”<sup>vii</sup> (Held, 1982: 254) Doctrinal tension within the SPD did not abate in Berlin.

The issue of monopoly power also loomed large in the minds of Ordoliberal policy-makers. Adenauer was in principle a firm supporter of anti-cartel legislation. He had previously made the break-up of companies with monopolistic characteristics – where economies of scale were not necessary for technical, social or economic reasons – a central plank of his political platform. (Schwarz, 1986; 1995: 374) It seemed that the CDU, which held a majority in the Bundestag and was theoretically united behind anti-cartel legislation, would easily pass laws in this area. However, Erhard and Franz Böhm, who spearheaded many of the efforts, faced an uphill battle.<sup>81</sup> While resolutions were floated continuously throughout the early 1950s, not until July 1957 was a law passed. For one, CDU-supporting industrialists and their *Verbände* were opposed to such legislation, forcing Adenauer and Erhard to tread carefully. (Nicholls, 1994: 334) The question was whether the doctrinal insistence on anti-monopoly legislation would trump political considerations.

The SPD, for its part, relished the opportunity to be a spoiler. With economic crisis firmly in the past, Erhard and his allies, whom the SPD derisively called the “Erhard Brigade,”<sup>82</sup> could not appeal to a 1948 sense of urgency. They were reduced to rather lame warnings of cartel power as a potential saboteur of the Social Market Economy and Adenauer’s

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<sup>78</sup> This “wage inflexibility” and the codetermination bargaining process are often cited today as a major factor in Germany’s current labor market problems. (Siebert, 2005: 95)

<sup>79</sup> The CDU’s affinity for *Mitbestimmungsrecht* can actually be traced to its pre-Erhard, 1947 “Adenauer Programm.” This asserted the principle of distributive power (*machtverteilendes Prinzip*) and the right for codetermination on fundamental issues of “planning and social structure.” (Schwarz, 1986; 1995: 374) Incidentally, this platform also asserted public ownership for mines and heavy industry. (ibid)

<sup>80</sup> The CDU also had a strong labor wing, and this was solidified by the *Betriebsverfassungsgesetz*.

<sup>81</sup> Ordoliberal efforts were not aided by recent public remembrances of de-cartelization, a very unpopular American policy related, philosophically-speaking, to the infamous Morgenthau Plan.

<sup>82</sup> A backhanded reference to the reactionary *Brigade Ehrhardt*, which attempted a Putsch in March 1920.

plan to economically integrate the FRG with Western Europe. (Nicholls, 1994: 353-4) In a show of precisely the sort of behavior Ordoliberalists wanted to prevent, powerful business interests, such as the *Bundesverband der Deutschen Industrie* (BDI), continued to thwart meaningful legislation. While many in the SPD also wanted to see some sort of anti-cartel policy – especially framed around the putative need for macro-level planning – and Karl Schiller, for one, had long articulated his concerns about concentrated market power and “pressure groups” in an unregulated market economy, (Schiller, 1951: 14-5) the opposition party was content to encourage internal CDU strife, favoring whichever position caused the most confusion.

As a result of these maneuvers, the final “Gesetz gegen Wettbewerbsbeschränkungen” as implemented on the January 1, 1958, was a relatively weak document. It established an anti-cartel office and forbade price fixing and monopoly market power. (Heilemann, 2003: 67) However, many loopholes also found their way into the final draft, including provisions that allowed small businesses to opt out of “price competition” and tolerated cartel arrangements where it made “economic sense.” (Nicholls, 1994: 336) Together with the *Mitbestimmungsgesetz*, the 1950’s solidified a corps of law that mostly contradicted Ordoliberal intentions concerning private concentrations of power.

It would be remiss, however, to assume that the Ordoliberal program completely ran out of momentum. A law consolidating the Bank deutscher Länder into a strengthened central bank entered into effect on August 1, 1957. (Heilemann, 2003: 65) For those concerned with the primacy of a stable, non-inflationary currency, the new Deutsche Bundesbank was a major victory. “Buba” authorities enjoyed a high degree of independence. While members on its Board of Managers were nominated by the Federal government to fixed 8-year terms, the more influential Central Bank Council was chosen by Bundesbank representatives. Government officials were allowed to attend meetings, but only as non-participants. Additionally, the central bank advised the Government on monetary matters, albeit without extending a return prerogative to Bonn. The primary task of the Bundesbank was, above all else, to safeguard the Deutsche Mark. (MacLennan et al, 1968: 169) Over the next decades, the Bundesbank’s reputation would become synonymous with monetary stability.

Throughout the 1950s Schiller and his ideological allies in the SPD attempted to move their party’s economic platform to Keynesianism. Success came in 1959. From November 13 to 15, the SPD held a congress at Bad Godesberg in order to redraft the German Social Democrat program for the first time since the Heidelberg meetings of 1925, when the party had adopted the vastly outdated and vaguely embarrassing motto *Demokratie ist nicht viel – Sozialismus ist das Ziel*. (Democracy is nothing much – Socialism is the goal). (Bark & Gress, 1989: 445) The “Godesberger Programm” marked a fundamental shift in the politics of the SPD. It brought a complete overhaul, addressing everything from atomic bombs to physical education. The statements on economic policy, however, deserve more than a passing glance:

## Figure 2: The Godesberger Programm – Basic Policy Statement of the SPD

- The goal of social democratic economic policy is to ensure, for all, growing prosperity, fair participation in the national economy and a life of liberty without degrading dependence or exploitation.
- Economic Policy must secure full employment, which together with a stable currency increases productivity and general prosperity.
- In order that everyone shares in the prosperity, the economy must adapt to constant structural changes according to a plan, so that balanced economic development is reached.
- The modern State constantly influences the entire economy through its tax and finance decisions, over the money and credit systems, its tariff-, trade-, social and price strategy, its public orders as well as in agriculture and housing policy. More than one third of the national product is administered with a public hand. It is thus not a question whether [central] arrangement and planning of the economy is appropriate, rather in whose favor these decisions are made. The State cannot extract itself from this responsibility. It is responsible for a farsighted economic policy that should be limited to an indirect influence of the economy.
- Free consumer and job choice are crucial foundations in the social democratic economic policy, as are free competition and entrepreneurial initiative. Autonomy for employees and employers' associations through collective bargaining is also a substantial component of the liberal order. Totalitarian State-control destroys liberty. Therefore, the SPD affirms the free market where competition prevails. However, where markets are distorted by the supremacy of particular interests or groups, they require various interventions to uphold economic freedom. Competition as far as possible, planning as far as necessary!

*Source: Deutsches Historisches Museum, author's translation* <sup>viii</sup>

This platform could have been excerpted from Schiller's writings over the previous decade. From the emphasis on complementary free market forces and Keynesian interventions – targeting full employment and coordinating “balanced” economic development – to the regulatory responsibilities of the state, the program shifted the underlying economic philosophy of the SPD from Marxism to Keynesianism. Schiller's catch line was also unmistakable: “competition as far as possible, planning as far as necessary!”

### 4.4. Time Period 4: (1960-1970) “Keynesianism”

**4.4.1. Historical Situation** – The 1960s began as the 1950s had ended, with healthy (although not torrid) growth, minimal inflation, epically low unemployment, and ‘brand name’ recognition for the Social Market Economy all over the world. Numbers again help elucidate the overall picture:

**Figure 3: Macro Economic Data in Germany from 1960 – 1970**

	<b>GDP Growth (%)*</b>	<b>Un-employment Rate (%)</b>	<b>Population (in 1,000)<sup>83</sup></b>	<b>Wages **</b>	<b>Prices †</b>	<b>Real Wage Change (%)</b>
<b>1960</b>	8.6	1.3	55,958	264	31.8	8.00
<b>1961</b>	4.6	0.8	56,589	293	32.6	10.7
<b>1962</b>	4.7	0.7	57,247	322	33.5	9.6
<b>1963</b>	2.8	0.8	57,865	347	34.5	7.6
<b>1964</b>	6.7	0.8	58,587	380	35.3	9.2
<b>1965</b>	5.4	0.7	59,297	418	36.5	9.7
<b>1966</b>	2.8	0.7	59,793	442	37.8	5.6
<b>1967</b>	-0.3	2.1	59,948	440	38.4	-0.5
<b>1968</b>	5.5	1.5	60,463	467	38.8	6.0
<b>1969</b>	7.5	0.9	61,195	525	39.6	12.0
<b>1970</b>	3.0	0.7	61,001	591	40.9	12.0

\* GDP price adjusted: chain-linked index (year 2000 = 100)

\*\* Average gross monthly earnings (in present euro)

† Consumer price index for 4-person-households with medium income wage earners (1995 = 100)

Source: *Statistisches Bundesamt*, <http://www.destatis.de/>

On the face of things, the economic performance in the 60s continued 1950s trends (see Figure 3). Save for the numerically anomalous year of 1967, GDP growth averaged 5.2% and unemployment hovered around 0.8% with the overall population rising by 5 million. Real wages increased at a meaningful clip (9%). Upon closer inspection, however, the sixties proved more of a transition period from the “miracle” to the mediocre, rather than a strict extension of *Wirtschaftswunder* success. (Giersch et. al, 1994: 125)

During the 1960s the economic situation shifted in its underlying philosophy, which affected policy decision-making. One indication of the Keynesian move towards “managed growth” was the establishment of the *Sachverständigenrat* (Council of Economic Advisors or SVR) in June 1963. (Heilemann, 2003: 90) This body, which comprised five experts, was to advise the German government on economic trends and appropriate responses. Its mandate encompassed four areas: price stability, employment, external balances (in both trade and financing) and a “constant and appropriate” rate of growth.<sup>ix</sup> While the SVR retained little power to draft specific policy, it was entrusted with identifying harmful trends and crafting ways to avoid or mitigate them. Operational Keynesianism relied on the technocrat, an apolitical economic entity possessing the requisite knowledge and modeling methods to accurately target demand and employment deficiencies while implementing interventions. The SVR served this function.

<sup>83</sup> It is worth noting that statistics measuring the active working population and/or persons engaged in economic activity actually *fell* over the decade. In 1960, 26.3 million participated in the labor force, whereas in 1970, only 26.1 million did. Unfortunately data does not exist for the early 1950s, but from 1957 to 1960, labor force participation increased by ca. 500,000 persons. (*Statistisches Bundesamt*, <http://www.destatis.de/>)



Attempting to put the *Sachverständigenrat*'s recommendations into practice revealed a large functional gap between the experts and the policymakers. This chasm was rectified in May 1967 with the passage of the Law for the Promotion of Economic Stability and Growth.<sup>84</sup> This provided the necessary legal framework for Karl Schiller's demand management (*Globalsteuerung*). (Giersch et. al, 1994: 147) Article 109, Sections 3 and 4 of the Basic Law were amended, endowing federal policymakers a wide discretionary anti-cyclical mandate.<sup>x</sup> (Zuck, 1975: 63-5) From that point on, Keynesian policy in the Federal Republic of Germany became a question of "when" and "how" rather than "if."

**4.4.2. Academia** – By the end of the fifties, Schiller had distinguished two types of socialism – one based on the collectivization of the means of production, the other based on a central direction of the economic process. He steered his party, the SPD, in the direction of the latter. (Schiller, 1955: 14) The "free socialist way as mixing competition and planning" favored by Keynesians was certainly the prominent economic feature of the Godesberger Programm,<sup>85</sup> and Schiller twisted Eucken's original argument for a "centralized directing mechanism" (i.e. stable, reflective prices) into justification for Keynesian planning. (ibid: 16-7) In academic terms, an ingenious 'coup' had thus been orchestrated, such that Socialism subsumed the successes of Ordoliberalism, claiming to add only Keynesian finishing touches.<sup>86</sup>

A book by Erich Preiser, published in 1967, provided evidence of the subtle intellectual transition – the passing of the baton – from Ordoliberalism to Keynesianism. Preiser was an avowed Keynesian, a strong voice against the totalitarian excesses of Nazism, but a supporter of planning after the war. The book, *Political Economy Today: Foundational Problems of the Market Economy*,<sup>87</sup> left little doubt that his academic orientation remained consistent. It opened with chapters on social problems of the free market and the perils of business cycles.<sup>88</sup> However, from the introduction, casual readers could be deceived into thinking that Preiser's personal brand of economic philosophy had been instrumental in founding the Social Market Economy, that he was a founding muse in the *Beirat*, the logical successor of Eucken.<sup>xi</sup> Preiser and Eucken were genial colleagues, united in loathing Nazism, but there was little link between their economic agendas. In fact, Preiser and other prominent planners had authored a minority report *against* the recommendations (to liberalize regulations and institute a currency reform) of the 1948 *Beirat Gutachtung*. (Nicholls, 1994: 205) Yet by 1967, the Keynesian revolution in academia was so complete that distinguishing Preiser's viewpoints from the founding Ordoliberal economic policies was no longer relevant.<sup>89</sup> Preiser was simply labeled a prominent voice (and expert) from the *Soziale Marktwirtschaft* time.

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<sup>84</sup> Gesetz zur Foerderung der Stabilitaet und des Wachstums der Wirtschaft (Heilemann, 2003: 111)

<sup>85</sup> Der freiheitlich-sozialistische Weg einer Verbindung von Wettbewerb und Planung. (Schiller, 1955a: 245)

<sup>86</sup> One doubts if Eucken would have been pleased at the expropriation of his logic to justify, for instance, production methods involving workers' control councils (Schiller, 1955: 20-21), which were very similar to contemporaneous developments in Yugoslavia. (Nicholls, 1994: 368)

<sup>87</sup> *Wirtschaftspolitik Heute: Grundprobleme der Marktwirtschaft* (1967)

<sup>88</sup> Der soziale Problematik der Marktwirtschaft (p. 11) & Gefahrenpunkte der deutschen Wirtschaftskojunktur (p. 38)

<sup>89</sup> Hagemann (2004) wrote of an "Americanization of Economics" which replaced German Ordoliberalism with on one end of the philosophical spectrum Chicago-style neoliberalism and on the other, Keynesianism.

The creation of the *Sachverständigenrat* in 1963 signaled the government's intent to involve itself in the macro policy process. As the SVR's advisory mandate suggested, federal control was to include active participation in employment and labor markets as well as the optimal setting of growth targets. However, the legitimacy of the new Keynesian institution rested on the appearance of objectivity; technical, apolitical economic operations realized by experts. Former *Beirat* members and academics published articles in this vein. The "Freiburg Krise" founder Erwin von Beckerath together with Herbert Giersch authored an edition confronting "The Problem of Normative Economics in Political Economic Consultation."<sup>90</sup> (Rieter & Schmolz, 1993: 97) Another member of the ecumenical Nazi resistance movement, Oswald von Nell-Breuning, wrote an article entitled "Objectivism and the Sachverständigenrat."<sup>91</sup> For these "normative giants" – both of whom previously championed morally guided, anti-Nazi social science – the sudden endorsement of objective methodology was an about-face. It was, however, indicative of the 1960's academic environment, as personalities associated with Ordoliberalism and the original Social Market Economy began to endorse Keynesian policy.

Ordoliberalism receded from the academic scene, and by the mid-1960s it was at best an afterthought, a circumscribed historical aside in the primarily Keynesian agendas of policy-makers.<sup>92</sup> In fact, the "normative" economics of the 1940's and 50's had been for all intensive purposes replaced by quantitatively "objective" Keynesianism.

**4.4.3. Politics** – In 1961, "Der Alte" Konrad Adenauer was pushing 85 years, the same age, his opponents muttered, of President Hindenburg in 1933.<sup>93</sup> Yet, the octogenarian forged onward into a fourth term. The CDU's grip on power lessened noticeably, however, losing five percent to the Social Democrats along with its absolute majority in the 1961 election. (Nicholls, 1997: 164-5) In order to secure a coalition with the FDP, Adenauer promised to resign the chancellorship to Ludwig Erhard after a two-year period. (Bark & Gress, 1989: 472) The days of CDU invincibility seemed at an end.

Karl Schiller again proved to be the most eloquent and persuasive SPD voice on economic matters, and he continued to press the Keynesian message. In a compilation of essays on economics and society published in 1964, he repeated his two-decade-long argument for enhanced macro coordination of the economy. (Schiller, 1964) With the SPD finally united behind his economic vision and the academic flank secured, Schiller was poised to make his *Globalsteuerung* program a reality.

Ludwig Erhard, both as Minister of Economics and after 1963 as Chancellor, resisted enhanced fiscal discretionary mandates. However, Keynesian pressure mounted from all

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<sup>90</sup> Beckerath v. E. et al. (1963) "Probleme der normativen Ökonomik und der wirtschaftspolitischen Beratung"

<sup>91</sup> Nell-Breuning, v. O (1963) "Versachlichung und Sachverständigenrat"

<sup>92</sup> Ordoliberalism's 'decline' was also hastened by the deaths of two of its original and most forceful advocates: Rüstow in 1963 and Röpke in 1966.

<sup>93</sup> In March 1960, President Eisenhower commented that "there are clear signs of growing senility particularly in Adenauer's tendency to focus on a single point, with loss of perspective on the whole range of considerations." (FRUS, 1993: 240)

sides. Schiller's prognostications on the latent *Wachstumsproblem* (growth problem) have already been noted as have his numerous warnings on the state's lack of preparation for managing business cycles. In November 1965, the Sachverständigenrat's second annual report pointed with concern at unregulated tension between rising inflationary pressure and economic expansion. It recommended a new strategy to combat such problems (viz. the tradeoff between expansive growth and price stability), known as Concerted Action. (Giersch et. al, 1994: 143) This strategy amounted to a social compact between the major agents of Germany's economy: fiscal and monetary authorities, the unions, and employer associations. These players were to meet periodically to coordinate wages and target growth goals. As a former State Secretary in the Ministry of Economics, Otto Schlecht, explained in 1969:

Concerted Action is a short cut between the principal institutions of the economy in their autonomous wage and price decisions and the government, which must coordinate the aggregate economic elements. In the present situation economic goals in our free, non-authoritarian society can be preserved only if the economic power groups have more understanding for the economic interdependencies. These voluntary co-ordination efforts will not work against the market; rather they are most likely to strengthen the market....In relation to wage policies, the strategy does not simply imply general appeals (moral suasion) or meaningless coffee parties, but neither does it restrict wage autonomy nor directly command social partners. Specific branch decisions on investment, prices, profits, wages etc., have to be left to steering by the market...The aim of Concerted Action is restricted to enlightening the partaking groups about the economic inter-relationships and to obtain understanding for the necessary decisions of the state – after mutual consultations – for its global steering, order and structural policies. (in Zweig, 1980: 41)

Erhard's government expressed distaste for Concerted Action measures. The differences between "coordination" and subversion of competitive market wage-bargaining seemed ill-defined. Erhard also had a sanguine history of weathering Keynesian protest, sticking successfully to Ordoliberal models. Recommendations and recriminations from personalities like Schiller often fell on deaf ears; until the first German economic downturn since the immediate postwar era occurred in 1966/67.

The causes of the slight recession – negative 0.3% growth in 1967 – are less than clear. The Bundesbank tightened monetary policy severely in May 1966, in what was seen as a public demonstration that inflation (which averaged 3.44% in 1965)<sup>94</sup> would not be tolerated. Yet exports, West Germany's particular strength, continued to rise throughout the recession. The sharp cyclic downturn of 1966/67 reflected a sharp drop in domestic demand. (Giersch et al, 1994: 145) Unemployment climbed to 2.1% (!) and nominal wages decreased for the first time in recent memory. More than anything, the 66/67 recessionary blip resembled a classic 'crisis of confidence' or a 'wanted recession' rather than reflecting an endemic problem with the economic order.<sup>95</sup> (ibid)

For Germans of the time, however, the recession was profoundly unsettling. To quote Dieter Haselbach:

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<sup>94</sup> *Statistisches Bundesamt*, <http://www.destatis.de/>, author's calculation. Measures a consumer price index for 4-person-households with medium income wage earners.

<sup>95</sup> See Fels (1988) for a more complete discussion of the 1966/67 recession.

The [West German] founding myth was that of a people that had mastered its deepest crisis by mastering the economy, a people with a right to eternal economic success...The myth of economic success included a promise. Any darkening of the economic horizon in Germany...was immediately perceived as a crisis of identity. The first to experience this was the father of the economic miracle, Ludwig Erhard,...who was swept away by a temporary economic downturn. (Haselbach, 1998: 121)

The downturn was indeed a fortuitous political event for the SPD. Schiller's precautionary academic oeuvre and economic politicking were finally corroborated by real circumstances, and a jittery German public rewarded his soothsaying with their electoral attention. Popular support for Keynesian policy and institutions was such that in 1966, Chancellor Erhard was forced to consider some sort of *Konjunkturpolitik* and the general coordination of economic policy. Even after his Social Market Economy aura was irreparably breached by recession, Erhard's proposals remained half-hearted attempts to stave off an increasingly Keynesian-leaning electorate.

For the first time, Erhard's lack of enthusiasm for "economic coordination" – as well as his inability to enforce internal CDU party discipline – proved politically disastrous. (Nicholls, 1997: 187-8) As he sought to raise taxes to balance the fiscal shortfall caused by recession, the CDU's coalition crumbled. In October 1966, ministers belonging to coalition partner FDP revolted against the hike, spurring the CDU's Georg Kiesinger to negotiate a "Grand Coalition" with the SPD. Erhard resigned on the 29 of November. Karl Schiller was appointed Minister of Economics.

"Concerted Action" was officially adopted on February 14, 1967. (Heilemann, 2003: 108) In conjunction with a steady lowering of key interest rates by the Bundesbank, the Grand Coalition implemented an augmented version of Erhard's original *Konjunkturpolitik*; the *Gesetz zur Förderung der Stabilität und des Wachstums der Wirtschaft* (StWG), which passed in May of 1967. The mandate focused on four familiar areas in an effort to direct business cycles: price stability, full employment, favorable current account balances and targeted growth rates. Together, these became known as the *Magisches Viereck* (Magic Quadrilateral).<sup>xiii</sup> All fell under the broad rubric of Schiller's demand management (*Globalsteuerung*). Within a couple of months of Erhard's removal, implementation of the Keynesian revolution was in full swing.

Concerted Action and *Globalsteuerung* represented the death knell for Ordoliberalism in political life (despite assertions that the new policy simply complemented earlier conceptions of the Social Market Economy). Christian Watrin summarized the transition as "a break away from the market economy as an order based not on collective aims but on common spontaneous rules, and its substitution by the idea that some pre-set objectives ought to be pursued by all groups, totally in conflict with liberalism and the steering of the economy by anonymous price and market forces. The 'enlightened market economy' of Schiller in its program thus becomes socialistic." (in Zweig, 1980: 41) The relatively quick official changeover of economic policy seems baffling in retrospect. Many in the CDU were still committed to Ordoliberal principles, as were the minority FDP, which held around 10% of the seats in the Bundestag. Yet the Grand Coalition provided a forum for a 'meeting of minds' between the governing parties. Had the SPD been governing alone or with a left of center partner, such a rapid transformation to

Keynesian policies would not have occurred without significant opposition. (Nicholls, 1997: 198) As it happened, the CDU was the partner party and could hardly oppose them. No doubt many policymakers also did not recognize, at the time, the historical significance of Schiller's appointment or the StWG legislation. Whatever the case, the Grand Coalition was politically essential for the transition to Keynesianism.

The 1967 economic downturn recovered after about a year. GDP growth averaged 5.5% in 1968 and the economy regained its previous strength. Real wages soared in the last years of the decade, transferring double digit percentage increases to workers. Government spending also increased handily, from an adjusted gross expenditure (in present Euros) of 75 billion in 1966 to 121 billion in 1972. To put these numbers in perspective, in the period from 1951 to 1965, government spending rose by 46.4 billion.<sup>96</sup> In his tenure as Economics Minister, Schiller presided over the same amount of government spending in six years as Erhard had in fourteen.<sup>97</sup>

By means of wage increases (vis-à-vis Concerted Action compromises) and invigorated fiscal spending, Keynesian stimuli functioned as promised and restored the economy to high growth rates. Schiller and the SPD were rewarded in the next round of elections (1969), gaining three percentage points and convincing the FDP to switch sides and support their coalition. The CDU/CSU, despite holding the largest bloc of Bundestag seats, was the minority under the SPD/FDP government of Willy Brandt. Schiller headed a new "Super Ministry," a merger of the finance and economics portfolios. (Bark & Gress, 1989a: 154) The Keynesian era, as conceived by Schiller and others in the early years of the Republic carried the day. The policy-influencing tenets of Ordoliberalism, with the exception of price stability, were rendered moot by 1967.<sup>98</sup>

## 4.5. Summary

The previous periodization of economic events, academic trends and political happenings portrays the underlying shift of West Germany's economic society from Ordoliberal to Keynesian philosophy.<sup>99</sup>

As we have seen, Ordoliberalism and Keynesianism maintained different conceptions of the optimal economic order and were often incompatible. The greatest divergence manifested in the realm of government intervention, where original Ordoliberal mandates limited the interference of centralized authorities. However, even in the heyday of Ordoliberal-influenced policymaking, theory was often compromised, for example with

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<sup>96</sup> All figures from *Statistisches Bundesamt*, <http://www.destatis.de>; author's calculations

<sup>97</sup> Real inflation from 1966-1972 averaged 2.96% compared with a 2.14% average from 1951-1966.

<sup>98</sup> Incidentally, by 1981, formal budgetary expenditures by the central state apparatus (as a % of GDP) were higher in West Germany than in the Soviet Union, at 49.8 and 47.1 percent, respectively. (Kornai, 1992: 135)

<sup>99</sup> Precedent for this argument exists: see, Hagemann's (1984) *From Ordnungs to Konjunkturpolitik: the Functional Development of State Economic Policy in West Germany from 1948-1967*, (title translated from German). This book, however, chronicles the "rise and fall" of the Social Market Economy and the policy transition, without delving into philosophic motivators. There is relatively little mention of Ordoliberalism and Keynesianism or their intellectual advocates.

monopoly power issues. In other cases the ideals endured, such as with an independent monetary policy focused on stable prices. Keynesianism, on the other hand, built momentum as time progressed. By 1967, remaining questions concerning business cycles, social programs and centralized economic guidance were no longer methodologically normative – viz. ought the state to intervene – but rather technical in nature, focusing instead on questions with a marked “where, when and how” character.

Can an argument that relies on an intellectual understanding of reality prove persuasive? Ordoliberalism was forged as a scholarly reaction to Hitler’s regime and Weimar failures. It evinced a strong normative component, but an incomplete synthesis of detailed recommendations. Therefore, actual FRG developments of “Ordoliberal” economic policy perhaps owed as much to the political exigencies of continual crisis management as to the ruminations of Eucken and Röpke. In fact, it is inchoate to argue that Ordoliberal musings received a cohesive implementation, or even a privileged position within the political processes of Adenauer’s government. It is also something of a misnomer to equate intellectual endeavors with reality, the ontological Ordoliberal and Keynesian structures with political “sausage making.”

Despite such imperfections and endless caveats, there exists a trend, intellectual perhaps, but descriptive of postwar German economic history nevertheless. After National Socialism, Ordoliberalism proved to be a powerful narrative, a motivating philosophy in early economic decision-making. In time, however, successes and changing circumstances dictated a process whereby the economic atmosphere, the philosophic aura surrounding the policy process, shifted focus, assuming a Keynesian worldview and its accompanying baggage.

Thus, a subtle but dramatic change in economic philosophy occurred in the Federal Republic, one that informs a myriad of issues in both policy and theoretical realms.

## ***5. Conclusions***

### **5.1. How should one account for West Germany’s postwar economic success and its subsequent decline to a “Welfare State”?**

Accepting the historical argumentation of this paper assumes the *prima facie* understanding that economic success has been related to the postulates of Ordoliberalism.<sup>100</sup> A striking correlation exists between the philosophical bent of policy

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<sup>100</sup> Abelshauser’s (1975) arguments challenge the endogenous “Social Market Economy” policy explanation of postwar economic success. Even though they are of tangential importance to the Ordoliberal-Keynesian narrative, his assertions deserve some attention here. First, secular trend constructions, which argue growth rebounded to long-term trend after the war’s interruption, over-aggregate and thus distort economic phenomena. While a popular methodology to contextualize history – see, for instance, Giovanni Arrighi’s *The Long Twentieth Century*, (London: Verso, 1994) – it does a poor job of explaining individual economic behaviors. Second, Abelshauser states that foundations from the Nazi period (in terms of industrial capacity, human capital and infrastructure) underpinned growth in the postwar era. While partly justified, this argument ignores the composition of the factors of production,

and the overall performance, in terms of high GDP growth and low unemployment figures, of West Germany's economy. As long as Ordoliberal-inspired policy remained the ultimate arbiter of economic activity, success followed. After Keynesianism and the centralized dictation of business cycle policy took over in the latter 1960s, middling growth figures, consistently higher unemployment figures and general economic sclerosis began to dog German society.

Definitively linking Ordoliberalism to *Wirtschaftswunder* or Keynesianism to subsequent stagnation, however, would require a still more protracted treatise, and even the most convincing analysis would be unlikely to convince those predisposed towards other economic beliefs. In as much, inspiring minds will undoubtedly find faults plaguing the use of this analysis – both in terms of internal argumentation and numerous exogenous factors left unconsidered<sup>101</sup> – as a basis for cogent commentary. That said, the Ordoliberal-Keynesian investigation still challenges the Federal Republic's economic record to useful effect.

## 5.2. The transition from Ordoliberalism to Keynesianism

Although specific arguments concerning the relative merits of Ordoliberalism and Keynesianism are sufficiently left to the forensic eloquence of numerous aforementioned academics, the path of transition from one philosophic paradigm to the next deserves mention. As the nineteenth century poet Charles Baudelaire wrote: “My dear brothers, never forget, when you hear the progress of enlightenment vaunted, that the devil's best trick is to persuade you that he doesn't exist!”<sup>xiii</sup> Karl Schiller and other likeminded Keynesians framed their policy as a logical continuation of the Ordoliberal-inspired Social Market Economy. Their language was couched in the lingua franca of Ordoliberalism; it was often anti-monopoly, pro-market allocation and virulently anti-communist. In Germany, however, Keynesianism was falsely conceived of as a non-change, a technical fine-tuning of otherwise healthy economic processes, an infusion of a previously ill-defined social facet into the *Soziale Marktwirtschaft*.

By hiding the normative implications of Keynesianism (centralized management of investment flows and employment prerogatives) and retreating behind a fortress of quantifiable and supposedly objective methodology, – viz. growth targets, natural rates of unemployment, etc. – policymakers afforded their efforts a degree of neutrality.

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erroneously equating an autarkic, centrally-dictated Nazi war industry with the FRG's export oriented, *Mittelstand*-driven capacity. Finally, he asserted that the 1950s and 60s were “boom” years internationally, and Germany did not stray too far from global trends. In fact, West German growth was an order of magnitude larger than even the most prosperous countries (see footnote 60). Using Abelshauser's own statistics from the decade 1949-1959, Germany averaged 7.5% annual GNP growth versus 2.5% in Great Britain, 3.1% in Belgium and 4.5% in France, all of which also sustained heavy losses in the war and practiced instead more *dirigiste* reconstruction schemes. The FRG's growth was twice that of the United States over the same period of time. In sum, it is difficult to deny deliberative Ordoliberal policy at least a marginal role in the economic successes.

<sup>101</sup> Prominent examples include: a) the 1970's Oil/Stagflation Crises, b) the heavy burdens, for all involved, of Reunification c) rapidly globalizing economic trends, which are making high cost countries uncompetitive, and d) demographic aging and the possible negative consequences thereof.

Economists consequently became problem solvers in a technical, bureaucratic sort of sense, as they attempted to model reality with ever-improving quantitative methodology, working towards a vision of the omnipotent Keynesian technocrat, who, armed with optimal diagnostic and implementation tools, successfully prognosticated and preemptively managed all manner of economic evils.

In as much, the theoretical and political workings of Keynesianism resemble a treasure hunt, as scholars excavate through layers of data in search of enhanced predictive capacities, more responsive models and the perfect intervention. Yet, for all of the burrowing and the fantastic trove of new knowledge thereby gained, economic trends remain fickle, with even the most sophisticated short and long-term forecasts rarely borne out in reality. Lost in the digging, policymakers have misread the economic “treasure map”. Even the soundest body of “objective” theory does not modify original Keynesian prescriptions, and those oft-ignored normative ramifications have transformed the German economic sphere to today’s suboptimal condition.

### **5.3. What lessons are there for today?**

It would be much too simple to advocate for a return to the policies of Erhard’s era. Times have changed and current economic conditions both within and outside the Federal Republic are drastically different than they were in the 1950s and 60s. Yet, one can still learn from the Ordoliberal prescriptions behind *Wirtschaftswunder* success.

German pundits (knowledgeable and otherwise), policymakers, scholars, and interested observers have in recent times often approached their numerous domestic economic woes as particular problems requiring rectification in a vernacular of individually customized solutions. Frequently referenced quagmires include convoluted and overly ‘rigid’ labor markets (including permanent unemployment), continually moribund conditions in the Eastern Länder, fiscal deficits, increasingly under-funded social programs, middling educational fortitude, consumer trepidation, fertility decline, decreasing global competitiveness, immigrant-focused xenophobia, and so on. However, perhaps partial responsibility for these myriad and ostensibly unconnected problems resides with the underpinning rationale for state interaction with society. Centralized apparatuses are currently charged with regulating economic and social prerogatives, manipulating aggregate demand and intervening with market forces using discretionary legislative imperatives and corporatist wage bargaining. In as much, markedly Keynesian incentive frameworks have been institutionalized in such a way that the present situation resulted.

Current norms of structural unemployment and stagnant growth are symptomatic of a larger infirmity that has remained largely undiagnosed or overlooked.<sup>102</sup> Policymakers are

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<sup>102</sup> It is interesting to note that a nascent Neo-liberal movement does currently exist in Germany. Horst Seibert (2005), Herbert Giersch (amusingly, given his formative role in the SVR), and Hans Werner-Sinn (2005) are notable proponents of supply-side solutions. Werner-Sinn, for example, recently wrote: “The excessive Keynesianism, which only a fringe group of economic professors (*Volkswirtschaftslehre*) clings to, is in international practice dead.” (2005: 21, *author’s translation*) The proof, however, is in the pudding, and as of yet, economic policy lacks a cohesive response to the welfare state apparatus. Also, one is hard pressed to



therefore unable to simply isolate one problem, say labor market rigidity, and deal with it separately from the entire philosophic bent of economic society. Revisions that do not take into account faulty Keynesian assumptions are doomed to fail. For example, as previously discussed, Keynes based his theory on the “stickiness” of the wage-price adjustment process, which eventually mandated centralized macro demand management to mitigate unemployment and business cycle oscillations. Under this rubric, government authorities have been primarily concerned with ameliorating and anticipating the fallout of economic fluctuations. The most basic of fallacies, *post hoc, ergo propter hoc*, affirming the consequent, is thus reinforced; to base policy on the “stickiness” of prices and wages is necessarily to accept this state of affairs, codifying the underlying problems. Instead, as Röpke so convincingly wrote in 1950, policymakers should concentrate on shaping underlying incentives to minimize the root causes of stickiness, or as Ordoliberalists clarified, non-competitive processes.

Ensuing implications address the necessity of reevaluating the entire German economic sphere as a failed Keynesian experiment. While much more research and policy definition needs to be done in the vein, the political conditions for a nascent resurgence of Ordoliberal policy may currently exist.<sup>103</sup> Recent developments, namely the formation of Germany’s second “Grand Coalition” between the SPD and CDU/CSU in 2005, broker intriguing possibilities. Recalling the first Grand Coalition’s decisive role in implementing Karl Schiller’s Keynesian economic ideas, it is conceivable that given effective leadership and a well-articulated vision (both of which are conspicuously lacking) the current party formation might marshal the political legitimacy necessary for a sweeping overhaul of the defunct Keynesian state. Wishful thinking or historical conceit, perhaps, but a provocative hypothetical nevertheless. Policymakers should think big, a new “*Sprung ins kalte Wasser*,” and redefine an economic and social platform that is motivated by market competitiveness, price stability and limited, non-discretionary government intervention. Recent history confirms this program not as an “Anglo-Saxon invasion,” but the fruition of a previously successful German academic movement.

Current efforts at economic reform in Germany require a reconnection with Ordoliberal philosophy. For the last several decades, economists have focused on specific problems, attempting to fix them using the latest Keynesian-inspired modeling and policy tools. However, as Germany’s recent woes partly depict, the consequences of misjudging the normative character of economic society are indeed dismal. Economics is at its disciplinary roots the study of scarcity, and conclusions as to optimal resource distribution eventually require subjective, philosophically-motivated judgments. Keynesian prescriptions have failed in this capacity. Ordoliberal ideals are worth revisiting within Germany’s inevitable process of economic reform.

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find a credible, mainstream voice in Germany that categorically rejects Keynesian demand management as the original Ordoliberalists did. Competitive order solutions, as such, have not been seriously entertained.

<sup>103</sup> This is helped by a resurgence of interest in the *Wirtschaftswunder* time from the popular press. In 2005, for instance, *Der Spiegel* ran a series detailing the 1950s, which included a relatively thorough inspection of the economic debate between Abelshauser and Erhardian/Ordoliberal ideas. See Alexander Jung, “Plotzlich waren die Regale voll” (*Der Spiegel*: n. 52, 2005) p. 48-53.

## 6. Translation Endnotes: Original German Text as Cited

<sup>i</sup> In diesem Sinn scheint mir viel von dem, was sich heute als sozial gibt, in dem tiefern und echtern Sinne des Wortes ausgesprochen antisozial zu sein. (Hayek, 1957: 84)

<sup>ii</sup> Das System arbeitet sehr genau, aber es berücksichtigt nicht die Rückwirkungen, welche die einzelwirtschaftlichen Pläne und ihre Durchführung auf die gesamtwirtschaftlichen Daten ausüben – falls diese Rückwirkungen nicht im eigenen Planungsbereich der einzelnen Betriebsleitung spürbar werden. Man denke an die Zerstörung von Wäldern in Amerika, die den Boden und das Klima weiter Gebiete verschlechterte und zu einer Versteppung führte. Es geschah, weil in der Wirtschaftsrechnung des Waldbesitzers diese Wirkungen auf die Gesamtwirtschaft nicht oder kaum zum Ausdruck kamen. Oder man vergegenwärtige sich die gesundheitlichen Schäden, die durch chemische Fabriken und deren Abwässer in vielen Fällen hervorgerufen wurden. (Eucken, 1952: 302)

<sup>iii</sup> Eine „Wettbewerbspolitik mit gestopfer Trompete“ ist kein Element einer auf Stabilität und Wachstum gerichteten Politik. Beide zu erreichen, das hängt entscheidend auch von der Intensität der Funktionsfähigkeit der wirtschaftlichen Konkurrenz ab. (Schiller, 1968: 58)

<sup>iv</sup> Aber, was wichtiger ist, in *positiver Hinsicht* hat die zweite deutsche Demokratie sich in vielem besser gewappnet und – soweit sie bisher konnte – geschlagen. Der Exzess einer *offenen Inflation* als Folge der Kriegsfinanzierung wurde *dismal vermieden*. (Schiller, 1953: 10)

<sup>v</sup> Freiheit und Ordnung sind beide *für* sich nicht absolut zu nehmen, nicht rein *für* sich in Totalität existenzfähig. *Sie müssen gegeneinander und miteinander aufgehoben werden*. Die höhig Verbindung zwische beiden kann man sehen in der christlichen Gerechtigkeit und Nächstenliebe. Man kann sie auch in der sozialistischen Brüderlichkeit erblicken. Das scheint uns so furchtbar verschieden zu sein. (ibid: 160)

<sup>vi</sup> Demokratie ist eine unerlässliche Forderung vom Standpunkt jeder freiheitlichen politischen Bewegung aus; aber sie allein *genügt* nicht, um die Freiheit des sozialen Lebens zu verbürgen.

<sup>vii</sup> „Die ‘industrielle Reservearmee’ muß endlich durch Maßnahmen der Vollbeschäftigungspolitik *für* immer demobilisiert werden. Dies ist die Magna Carta der Befreiung der Arbeitenden.“ (Held: 254)

<sup>viii</sup> Figure 3 Text:

- Ziel sozialdemokratischer Wirtschaftspolitik ist stetig wachsender Wohlstand und eine gerechte Beteiligung aller am Ertrag der Volkswirtschaft, ein Leben in Freiheit ohne unwürdige Abhängigkeit und ohne Ausbeutung.
- Die Wirtschaftspolitik muß auf der Grundlage einer stabilen Währung die Vollbeschäftigung sichern, die volkswirtschaftliche Produktivität steigern und den allgemeinen Wohlstand erhöhen.
- Um alle Menschen am steigenden Wohlstand zu beteiligen, muß die Wirtschaft den ständigen Strukturveränderungen planmäßig angepaßt werden, damit eine ausgeglichene Wirtschaftsentwicklung erreicht wird.
- Eine solche Politik bedarf der volkswirtschaftlichen Gesamtrechnung und des Nationalbudgets. Das Nationalbudget wird vom Parlament beschlossen. Es ist verpflichtend für die Regierungspolitik, eine wichtige Grundlage für die autonome Notenbankpolitik und gibt Richtpunkte für die Wirtschaft, die das Recht zur freien Entscheidung behält.
- Der moderne Staat beeinflußt die Wirtschaft stetig durch seine Entscheidungen über Steuern und Finanzen, über das Geld- und Kreditwesen, seine Zoll-, Handels-, Sozial- und Preispolitik, seine öffentlichen Aufträge sowie die Landwirtschafts- und Wohnbaupolitik. Mehr als ein Drittel des Sozialprodukts geht auf diese Weise durch die öffentliche Hand. Es ist also nicht die Frage, ob in der Wirtschaft Disposition und Planung zweckmäßig sind, sondern wer diese Disposition trifft und zu wessen Gunsten sie wirkt. Dieser Verantwortung für den Wirtschaftsablauf kann sich der Staat nicht entziehen. Er ist verantwortlich für eine vorausschauende Konjunkturpolitik und soll sich im wesentlichen auf Methoden der mittelbaren Beeinflussung der Wirtschaft beschränken.

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- Freie Konsumwahl und freie Arbeitsplatzwahl sind entscheidende Grundlagen, freier Wettbewerb und freie Unternehmerinitiative sind wichtige Elemente sozialdemokratischer Wirtschaftspolitik. Die Autonomie der Arbeitnehmer- und Arbeitgeberverbände beim Abschluß von Tarifverträgen ist ein wesentlicher Bestandteil freiheitlicher Ordnung. Totalitäre Zwangswirtschaft zerstört die Freiheit. Deshalb bejaht die Sozialdemokratische Partei den freien Markt, wo immer wirklich Wettbewerb herrscht. Wo aber Märkte unter die Vorherrschaft von einzelnen oder von Gruppen geraten, bedarf es vielfältiger Maßnahmen, um die Freiheit in der Wirtschaft zu erhalten. Wettbewerb soweit wie möglich Planung soweit wie nötig!

<sup>ix</sup> **SVR Artikel 2:** Der Sachverständigenrat soll in seinen Gutachten die jeweilige gesamtwirtschaftliche Lage und deren absehbare Entwicklung darstellen. Dabei soll er untersuchen, wie im Rahmen der marktwirtschaftlichen Ordnung gleichzeitig Stabilität des Preisniveaus, hoher Beschäftigungsstand und außenwirtschaftliches Gleichgewicht bei stetigem und angemessenem Wachstum gewährleistet werden können. In die Untersuchung sollen auch die Bildung und die Verteilung von Einkommen und Vermögen einbezogen werden. Insbesondere soll der Sachverständigenrat die Ursachen von aktuellen und möglichen Spannungen zwischen der gesamtwirtschaftlichen Nachfrage und dem gesamtwirtschaftlichen Angebot aufzeigen, welche die in Satz 2 genannten Ziele gefährden. Bei der Untersuchung sollen jeweils verschiedene Annahmen zugrunde gelegt und deren unterschiedliche Wirkungen dargestellt und beurteilt werden. Der Sachverständigenrat soll Fehlentwicklungen und Möglichkeiten zu deren Vermeidung oder deren Beseitigung aufzeigen, jedoch keine Empfehlungen für bestimmte wirtschafts- und sozialpolitische Maßnahmen aussprechen. *Source: <http://www.sachverstaendigenrat-wirtschaft.de/orga/gesetz.php>*

<sup>x</sup> **Pre-1967 text of G.G. Article 109:**

- (1) Bund und Länder sind in ihrer Haushaltswirtschaft selbständig und voneinander unabhängig.
- (2) Bund und Länder haben bei ihrer Haushaltswirtschaft den Erfordernissen des gesamtwirtschaftlichen Gleichgewichts Rechnung zu tragen.
- (3) Zur Abwehr von Gefahren für das gesamtwirtschaftliche Gleichgewicht können durch Rechtsverordnung der Bundesregierung Vorschriften über Ausmass und Art der öffentlichen Verschuldung erlassen werden
- (4) Das Nähere zur Durchführung der Absätze 2 und 3 regelt ein Bundesgesetz mit Zustimmung der Bundesrates.

**Post-1969 version of G.G. Article 109:**

- (1) Bund und Länder sind in ihrer Haushaltswirtschaft selbständig und voneinander unabhängig.
- (2) Bund und Länder haben bei ihrer Haushaltswirtschaft den Erfordernissen des gesamtwirtschaftlichen Gleichgewichts Rechnung zu tragen.
- (3) Durch Bundesgesetz, das der Zustimmung des Bundesrates bedarf, können für Bund und Länder gemeinsam geltende Grundsätze für das Haushaltsrecht, für eine konjunkturgerechte Haushaltswirtschaft und für eine mehrjährige Finanzplanung aufgestellt werden.
- (4) Zur Abwehr einer Störung des gesamtwirtschaftlichen Gleichgewichts können durch Bundesgesetz, das der Zustimmung des Bundesrates bedarf, Vorschriften über
  1. Höchstbeträge, Bedingungen und Zeitfolge der Aufnahme von Krediten durch Gebietskörperschaften und Zweckverbände und
  2. eine Verpflichtung von Bund und Ländern, unverzinsliche Guthaben bei der Deutschen Bundesbank zu unterhalten (Konjunkturausgleichsrücklagen),

erlassen werden. Ermächtigungen zum Erlaß von Rechtsverordnungen können nur der Bundesregierung erteilt werden. Die Rechtsverordnungen bedürfen der Zustimmung des Bundesrates. Sie sind aufzuheben, soweit der Bundestag es verlangt; das Nähere bestimmt das Bundesgesetz.

<sup>xi</sup> Die Aufgaben, die der Wirtschaftspolitik in den Jahrzehnten nach dem zweiten Weltkrieg gestellt sein würden, haben Erich Preiser schon im Kriege beschäftigt; davon zeugen einige Aufsätze aus dieser Zeit, die

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später unverändert nachgedruckt werden konnten. Mit Erwin v. Beckerath, Walter Eucken, Adolf Lampe und andere Kollegen hat er die Probleme der Nachkriegswirtschaft bis 1944 im Freiburger Kreis, seit 1948 im „Wissenschaftlichen Beirat bei der Verwaltung für Wirtschaft des Vereinigten Wirtschaftsgebietes“ diskutiert und in Gutachten behandelt. Der Mitarbeit in diesem Gremium, das seit 1950 als „Wissenschaftlicher Beirat beim Bundeswirtschaftsministerium“ tätig ist, hat er einen guten Teil seiner Arbeitskraft geopfert. (Preiser, 1967: 7)

<sup>xii</sup> Preisniveaustabilität, Vollbeschäftigung, außenwirtschaftliches Gleichgewicht, stetiges und angemessenes Wirtschaftswachstum.

<sup>xiii</sup> See Baudelaire's poem "Le Joueur généreux": "Mes chers frères, n'oubliez jamais, quand vous entendrez vanter le progrès des lumières, que la plus belle des ruses du diable est de vous persuader qu'il n'existe pas!"

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