

The German Moment in a Fragile World

“Germany is *Weltmeister*,” or world champion, wrote Roger Cohen in his July 2014 *New York Times* column¹—and he meant much more than just the immediate euphoria following Germany’s first soccer world championship since the summer of unification in 1990. Fifteen years earlier, in the summer of 1999, the *Economist* magazine’s title story depicted Germany as the “Sick Man of the Euro.”² Analysis after analysis piled onto the pessimism: supposedly sclerotic, its machines were of high quality but too expensive to sell in a world of multiplying competitors and low-wage manufacturing. Germany seemed a hopeless case, a country stuck in the 20th century with a blocked society that had not adapted to the new world of the 21st century, or worse, a society that was not even adaptable.

Things since then have changed significantly. In the summer of 2013, more than a year before the triumph in Rio de Janeiro, the *Economist* reversed its own verdict—Germany now appeared on the front page as “Europe’s Reluctant Hegemon.”³ In 2014, Germany came out on top for the second year in a row in the BBC’s annual country rating poll as the country with “the most positive influence on the world.”⁴ Simon Anholt’s annual “Nation Brand Index” also put Germany in the top spot in 2014.⁵

Foreigners are not the only ones to note this remarkable transformation. Twenty-five years after unification, the gap between former West and East Germany in both income and productivity has not quite disappeared but shrunk very significantly. Both have reached approximately 80 percent of those in the West.⁶ And if we can believe the regular polling of Germany’s so-called socioeconomic panel, those living in East Germany have never been as content and satisfied with life as they are today.⁷ Somewhat surprisingly, the same is true

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of the grand coalition governing Germany since late 2013: in stark contrast not only to most of Germany's neighbors in Europe but also to the United States, satisfaction with how the country is being run is at an all-time high. Fully 59 percent are "satisfied" or "very satisfied" with their government—more than at any moment since unification.⁹

It is against the backdrop of this remarkable appreciation that the thesis of a "German moment" deserves a more thorough examination. How did we get to this moment? Four elements of success stand out. But because we Germans never fully trust our good luck—except in soccer—four fundamental challenges are also worth exploring. Only if Germany addresses them successfully will this "German moment" last for more than a happy but fleeting chapter of our history.

Strength from Weakness

In order to appreciate the nature and evolution of the rise from "sick man of the Euro" to "reluctant hegemon of Europe," it is important to understand that Germany managed to turn many of its perceived weaknesses into at least four strengths. First on the list is what has become known as "Agenda 2010," a reform package introduced in 2003 that revamped an expensive social welfare system, addressed the growing challenge of demographic decline, and introduced new flexibility into the labor market. Resistance was strong. Eventually Chancellor Gerhard Schröder and his Social Democrats lost power in the 2005 elections

because of widespread opposition to the "Agenda 2010" reforms. But the effects were lasting and far more consequential than many expected. They helped Germany profit enormously from the following decade of globalization. In more than one way, Germany successfully adapted its "*contrat social*," its "social contract"—the Agenda reforms were far more than an economic package designed to reduce labor unit costs and to make Germany competitive again. They embodied the

acknowledgement that Germany must adapt to the pressures of globalization, and that it could do just that while still preserving the essence of its close state-business-labor relations and the strong tradition of social cohesion. This has paid off: unemployment today, at less than 6 percent, is barely half of what it was in 2005.

The second important strength is Germany's strong manufacturing base. Remember that this was considered a strategic weakness not too long ago. The future, we were told at the turn of the millennium, lay in the service industry,

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most of all in financial services. To be fair, German banks and managers must take their share of the blame for quite a few stupidities during the build-up of the financial bubble in 2008. German Savings&Loans thought they could play in the big league, buying so-called “structured investment vehicles” that ruined their balance sheets after 2008 and required massive bail-outs. Local communities and city treasurers thought they could free up much-needed liquidity by leveraging city assets from energy providers to public transport companies. For instance, the London High Court just recently let the City of Leipzig off the hook, holding the investment bank UBS responsible for a dubious cross-border-leasing contract concluded in 2003 that would have brought Leipzig to the brink of bankruptcy in 2014.¹⁰ In many other cases it will take a long time to pay off the debt incurred through those massively misguided transactions. But overall the backbone of German industry stayed intact. This is not necessarily because of a clever strategy, but rather because of a combination of traditional German skepticism toward the short-term business perspective (dominant in other countries) and because of the structure of industry.

Much of Germany’s engineering and manufacturing strength has its base in mid-sized, family-owned companies that have not followed the gospel of shareholder value. Many of them are still not listed at the stock market, but rather inherited from generation to generation. And many of them are world market leaders in their own field. Thus, it is not only Siemens or the big car makers but the many, many companies—for example in the machine-tool sector—that have reaped the profits of globalization. They took advantage of European enlargement in 2004, producing and selling in Central and Eastern Europe, but they were also quick to adapt to the rise of Asia and particularly to the Chinese manufacturing boom, which to a significant degree has been driven by German machine-tools. This summer, Germany’s total exports for the first time surpassed 100 billion Euros in a single month.¹¹ Taken together, these two factors—the Agenda 2010 and a strong manufacturing sector—combine to form a competitive economy with a strong sense of inner cohesion, based on a solid social security system and comparatively limited income inequality.

The third strength—and I deliberately list it among the strengths here, although it is hotly debated and certainly not without risk—is Germany’s strong push for a transition toward renewable energy and a greener economy. Hastened by the March 2011 Fukushima reactor meltdown, the German government decided to speed up phasing out 22 still operating nuclear reactors and replacing them with renewables. There are many issues yet to solve, like mobilizing the necessary investment, building the smart-grid that can bring wind energy from the North Sea to the factories of the South, making the “*Energiewende*” compatible with a more unified European energy policy, and dealing with the

rise of energy prices for both consumers and industry which threatens to become a major disadvantage in global competition. (This latter development is partly due to the shale boom driven by advances in fracking technology in the United States. One of the certainly unintended consequences of this is the import of emission-heavy coal from West Virginia and other U.S. states to Germany while some of our modern gas-fired plants sit idle—with Germany’s overall emissions rising.) But, while finding the proper mix of bridging energy and getting the regulatory framework right remains a huge challenge for the German government, the country is tackling a crucial issue now for the world of tomorrow.

Today, only about 20 percent of worldwide middle-class consumption comes from the rising societies in Asia. By 2030, their share is projected to rise to more than 50 percent.¹² Decoupling economic growth and consumption from the depletion of natural resources is the only viable strategy if we want to keep the world an inhabitable place in an age of the rapidly growing global middle class. Reducing Germany’s or even Europe’s own emissions is only a minor element of this. It will be of far greater importance and

Sustainability will become an ever more important element of Germany’s global brand.

consequence to develop the technology and concepts that are transferrable and affordable, making a difference where it really matters for the global climate and environment such as in China, India, and the many other emerging societies. Sustainability—both in the sense of technological breakthroughs and conceptual advances—will become an ever more important element of Germany’s global brand and, as a potential provider of a viable model for all three dimensions of

sustainability—economic, ecologic, and social—of its contribution to a future international order.

The fourth pillar of success is that Germany has managed to become a much more open society than it used to be. Little-noticed, Germany became the number two country on the OECD’s 2014 immigration list, second only to the United States and ahead of classic immigration states like Canada or Australia. In 2013, net immigration to Germany reached about 437,000 persons, and today more than 16 million people living in Germany have a migration background (either first-, second-, or third-generation), almost 20 percent of the population;¹³ most of them have become German citizens. This has made Germany a far more diverse and dynamic, open and creative society.

There are, of course, myriad other reasons that have contributed to Germany’s remarkable “turn-around” over the past fifteen years. Taken all

together, they have transformed the country into a winner of globalization and formed a society that is much less afraid than most of its peers of the pressures produced by the process of constant “creative destruction.”

Future Challenges

Can this German moment last? Is this success sustainable? In order to answer such questions, we must now examine several of the challenges that might come. Four in particular stand out for Germany. To start again with the economy, the first challenge is the potential effect of major technology leaps for Germany’s economic model. For instance, in the auto sector, a big question is whether the car of the future will represent another platform for information and knowledge, with the engineering side a mere accessory. Most of the digital innovation comes from Silicon Valley companies—can German manufacturers keep their edge in integrating IT components into their superior engineering products? Who will dominate what the experts call “industry 4.0,” or “the internet of things”? Will German companies be quick and agile enough to strengthen their IT expertise—or will they lose out to big technology companies that will penetrate and dominate one industrial sector after another? Here is a particular German strength that could possibly become a weakness in the future. Strengthening education and research and investing in high-technology development—both public and private—has therefore been a major priority of this, as well as the last, German government.

The second long-term challenge involves demographic trends. Even with the major immigration of the past years and the greatly expanded efforts at integration, the overall demographic trend points toward a shrinking German population. Shortage of qualified labor will be as much of an issue as the long-term sustainability of health care, pensions, and social welfare. The ratio of those financing the “generational contract” and those whom it supports is constantly worsening now that the baby-boomers are about to retire in Germany. This is, by the way, also an interesting factor in the debate about the national debt. A growing society like the United States can more credibly claim to outgrow its debt-to-GDP ratio. For a demographically declining country like Germany (and with it much of the European continent), this is quite a different proposition. Organizing a reasonable and balanced immigration system that addresses both our humanitarian responsibility in the face of ever-increasing migration pressure from Northern Africa, the Sahel, and other crisis-stricken areas and the needs of Germany’s economy and society, while recognizing the limits of our capacity to absorb and fully integrate people from diverse ethnic and religious backgrounds, will be one of the most important tasks of Germany in the decade ahead. Here, Germany still has an open window

of opportunity, while in many of its European partner countries the rise of nationalist and populist sentiment has already closed this window.

The third major challenge is Europe and the future of the European Union. What was intended to be a quantum leap in the integration process of Europe—the creation of a single European currency, the Euro, in 2002—has turned into the most serious challenge to this integration project since its inception more than half a century ago. The creation of a monetary union without the full integration of economic and fiscal policies has not led to the intended gradual convergence of the Eurozone’s economies, but rather to a widening split and a continuing divergence that threatens the cohesion of the overall integration project. Starting in early 2010, financial markets demanded growing interest rate differentials on sovereign European debt, varying from member state to member state. Much has been said and written over the four-and-a-half years of the Euro crisis on the origins and possible solutions to this crisis. For the most part, U.S. and German approaches to managing this crisis have differed pretty sharply: while Washington pushed for massive stimulus spending and quantitative easing of monetary policy, Germany instead advocated tough structural reforms in order to limit moral hazard and to foster a sustainable long-term convergence of the Eurozone economies. Suffice it to say that while there has been a major effort at Eurozone solidarity, with stabilizing guarantees and funds provided by Germany in the area of 300 billion dollars—for an economy not a quarter the size of the U.S. economy—the crisis is not over yet.

It is a crisis of excessive sovereign debt in some member states or of excessive bubbles in others (such as the real estate and banking sector), but generally it has morphed into a crisis of confidence in the European project and a crisis of governance in many member states. The challenge of rewriting the “social contract,” of balancing anew the contributions of all parties and groups to the overall interest of society in a very different international competitive environment, is a difficult and painful process. Some societies have made major progress along this path—certainly Ireland, Portugal, and Spain. In others, there is a widespread defensive, if not an outright gloomy, perspective on globalization and an overall negative assessment of the balance of opportunities and risks that come with it. The loss of certainty, the loss of security, the speed of change—many feel that they have lost the ability to act as masters of their own fate, and they suspect their governments have lost it as well.

For Germany, this poses a particular challenge: it owes much of its recent success to its ability to adapt to the challenges of a competitive global environment—politically, economically, socially, and culturally. But at the same time, the overriding lesson of German history is that the “German question” is only put to rest within the solid framework of an integrated Europe.

Germany is a country too large to be just one among many and too small to dominate the continent.

What if Germany's partners are no longer able or willing to submit themselves to the competitive pressures of a globalizing economy? What if current reform efforts across the Eurozone fail to produce the economic convergence that is ultimately at the core of internal cohesion? What if Germany would at some point find itself in a situation where integration and solidarity with its European partners and its prosperity in a globalized economy seem to become mutually exclusive? It would be a fundamental strategic dilemma between the two imperatives of competitiveness and integration—a choice to be absolutely avoided. Therefore, it is imperative that Germany charts a path forward for the Eurozone and the entire European Union that revitalizes the entire European economy—not only the German one. The most important weakness and limitation of the “German Moment” therefore lies in being just that: a German and not a European moment.

What if European integration and prosperity in a globalized economy become mutually exclusive?

The fourth and final major challenge is one that we share across the Atlantic. It is the threat of globalization “under siege.” A recent McKinsey study found that Germany is possibly the “most connected” of all major economies if you take together the flows of goods, money, people, and information.¹⁴ Germany therefore has much to lose from a crumbling liberal international order. Unfortunately, this order faces threats on a number of fronts. One of them is a Russia that defines its own future less in cooperation with the West and more in opposition to us, if not in limited conflict. It is a Russia that increasingly isolates itself from outside influences, that reduces interdependence rather than builds on it. Much of the current confrontation seems to be driven by domestic political considerations, which also means that even a settlement in Ukraine will not allow us to go back to “business as usual” with Russia. We are facing the unpleasant prospect of dealing with a Russia that has made unpredictability a signature element of its strategy.

Another threat is the rise and unspeakable brutality of the group that calls itself “Islamic State” in Iraq and Syria (ISIS), or of their fellow spirits of Boko Haram in Nigeria. Ever more frequently we are confronted by countries with weak institutions that can crumble under the pressures of globalization: high population growth, high and mostly disappointed expectations, few economic perspectives, no political empowerment, pervasive corruption—all these are ingredients for the emergence of fragile states. The more complex the world

becomes, the greater the human desire for simple, clean, and pure frameworks and identities. They can be ethnic, they can be religious, they tend to be exclusive rather than inclusive, and more often than not they tend toward violence. This threat will hardly go away. To the contrary, we will increasingly have to cope with it in our own societies. One of the most worrying developments around ISIS has been the growing number of young people who grew up in Germany and who have gone to Syria to fight in the ranks of ISIS. Estimates today are above 550, more than ten times the number of those who made their way to fight for the Taliban in Afghanistan.¹⁵ We also face global pandemics—like Ebola—that threaten to spread via the transmission mechanisms of an interconnected world and that completely overwhelm the fragile countries where they originate.

Finally, and perhaps most importantly, we face the rise of China and with it of an authoritarian version of capitalism that is not as easily convergent with our ideals as we might have thought or hoped. This rise has repercussions far beyond Asia that will change the way we produce, the way we consume, and will change the environment in which we live. We have every interest in China's peaceful, non-violent rise, and eventual transformation. But what are the instruments to bring this about?¹⁶

Can Germany Help (Re)build Global Order?

Given its considerable strengths and the formidable challenges ahead, what is Germany to make of its “German moment”? Germany is currently undergoing

If this is a “German moment,” to what purpose are we going to use it?

an intense process of reflection about its own role in the world. A process that asks critical questions about the scope of our international responsibility and interests, about the instruments at our disposal, and about the limits of our capabilities.¹⁷ If there is indeed something like a “German moment,” the crucial question becomes, “to what purpose are we going to use it?”¹⁸

Foreign policy begins at home, the old adage says. A strong foundation in economic strength and social cohesion is necessary to project influence abroad and shape outcomes. Germany clearly has a strong foundation here, but this strength is not yet a strategy. The major focus for Germany's future foreign policy¹⁹ could be two-fold: contributing more to the pressing crises of our days, but also spending more energy and creativity on exploring and building new elements of order wherever possible. All the while, the European Union will remain the major reference frame for all German foreign policy.

It is highly likely that permanent and parallel crises will no longer be the exception but rather the rule of foreign policy in an increasingly fragile globalized world. Crisis is the “new normal.” We have to adapt to this permanent challenge by strengthening our instruments and our crisis response, something the German government has tried and demonstrated in its response to the crisis in Ukraine, in relations with Russia, in the mobilization against ISIS (including weapons deliveries to the Kurdish peshmerga in Northern Iraq), and in scrambling to contain the Ebola virus in West Africa.

On the broader issue of “order,” we are faced with a situation where the old order is contested in some parts, fraying in others, substituted by parallel structures, or even disintegrating in parts of Africa and the Middle East. At the same time, it is easy to define why we would need more global governance, not less, given the challenges of climate change or the cyber and internet domain. Where can we, as Europeans and Americans, contribute to the defense and stabilization of an international order that serves our common interests? And even further: where and how can we contribute to establishing new elements of order—maybe on a regional level, or maybe for functional challenges like the proper balance of security and privacy in the digital age?

The new order will be less coherent and less consistent than the “Pax Americana” that emerged after World War II. It will resemble more of a patchwork. But that alone is no reason not to pursue order wherever it is sorely needed to make the world a more just, more peaceful, more prosperous place. This is best done together with strong partners and allies. It concerns me greatly that mutual trust across the Atlantic has suffered over the last year, according to most opinion polls.²⁰ We must not let our relationship be defined by what divides us, but instead realize how much we have in common compared to all other major players around the globe.

One important element of an emerging order would be the conclusion of a Transatlantic Trade and Investment Partnership (TTIP) that is currently under negotiation between Washington and Brussels. Its importance would extend far beyond the economic realm. It would send a strong signal that the transatlantic community asserts itself in shaping the future of globalization, in setting standards that we would like to see emulated and adopted in other parts of the world.

A final point: in the world of tomorrow, our ability to shape desired policy outcomes in third places will shrink due to the multiplication of actors and the increasing complexity of the problems we face. Foreign policy will require humility and the ability to accept contradictions and differences. Whenever we are confronted with a crisis, we are all too quick to point out a failure of Western policies. This attitude (widespread also in the world of Western policy analysts) is in more than one way self-defeating. The past decade taught us some

lessons in the limits of our capabilities to shape the world. Sober analysis suggests that these limits will be even more pronounced in the future. We should not succumb to the temptation of moral relativism as a consequence, but simply apply a more realistic assessment of the size of the challenge and of our limitations in shaping desired outcomes in the short term.

I firmly believe that the power of the West's own example—of a life with opportunities, liberties, physical and social safety, and an ability to learn from our own mistakes—remains our most potent instrument of “soft power” in the longer term. It is exactly in these categories of competitiveness and cohesion, of openness and integration, of a viable model of sustainability, that Germany has much to contribute to the future of international order.

Notes

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8. The title owes its inspiration to Kofi Annan’s contribution to the “Review2014” project, a broad review of Germany’s foreign policy initiated by Foreign minister Frank-Walter Steinmeier in February 2014. Results are to be announced in early 2015. See www.review2014.de. This essay is a revised version of a lecture delivered to Eric M. Warburg chapters of the American Council on Germany in Denver, Dallas, Minneapolis, Philadelphia, Alexandria and Boston as part of the Henry Kissinger Speaker Program in October 2014, supported by the Bosch Foundation.
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