

## THEME 01

# The next Great German Surge

GERMANY

NATIONAL  
CHAMPIONS

DIGITAL ECONOMY

In just two decades, Germany has transformed itself from the sick man of the Eurozone into its economic powerhouse. However, the German economic powerhouse is showing signs of decay, and action is needed to boost Germany's economy. Given the country's cultural-historical context and its current position, we can expect a new surge of German innovation.

## Our observations

- OECD data on digital infrastructure shows that Germany's adoption rate of [fiberglass](#) is one of the lowest of all OECD countries (2.3%, compared to the 23.3% OECD average). Likewise, Germany has one of the lowest levels of point-of-sale (POS) transactions conducted with [cash](#) in Europe. Both can be considered proxies of Germany's weak digital infrastructure, and indeed, German business leaders claim that Germany's outdated [digital infrastructure](#) is hurting its competitiveness.
- Germany is the fourth largest economy in the world, and very reliant on [exports](#), which account for 47.2% of its GDP (compared to 11.9%, 19.8% and 16.1% for the U.S., China and Japan respectively, the world's largest economies). Furthermore, five of its six [largest export markets](#) are in trouble: the U.S. and China are embroiled in their trade war, Italy is in a technical recession, the U.K. is coping with Brexit, and France is under heavy pressure at home (only the Netherlands, its fifth largest export market, is relatively stable).
- Germany ran the world's largest [current account surplus](#) in 2017 (the latest year for which data is available). Furthermore, Germany has one of the highest [gross savings rates](#) as well as the highest [government budget surplus](#) of large economies (only resource-dependent Norway and the small Cayman Islands have a higher budget surplus). As such, Germany is a major contributor to "global imbalances" between savers and investors, net importers and exporters as well as on fiscal policy, thereby increasing [financial instability](#) as well as hindering the [post-crisis recovery](#) of the Eurozone.
- Germany has one of the highest [GDP per capita](#) in the world, with currently record-low [unemployment](#). However, [inequality](#) is on the rise in the country, especially since the [2004 Hartz reforms](#) that arguably eased some of the labor market rigidities that hurt Germany's economy in the past decades. Furthermore, it has made Germany's divisions change: instead of the East-West, the [North-South divide](#) is becoming more prominent on a whole range of socio-economic indicators. Furthermore, [migration](#) issues and a changing demographic make-up are hotly debated topics in Germany.
- Germany, in contrast to other European and Anglophone countries, has taken a pragmatic stance in the global backlash against Huawei, and China's [Made in China 2025](#) plan in general. Indeed, this week, Merkel [voiced](#) willingness to work with Huawei and Chinese companies, as long as privacy is safeguarded and German regulation is respected. In the same line of thought, Germany has been critical of European sanctions on Russia, and Germany will continue to support a highly contested natural gas pipeline (Nord Stream 2) from Russia to Germany, despite the [Ukraine tensions](#) and [U.S. sanctions](#).
- There is strong affection between the Chinese and Germany: a 2016 extensive [survey](#) found that 89% of the Chinese say that German companies are excellent high-tech industrial producers, 85% have a very positive image of products "made in Germany" and 65% say that they like German culture, emphasizing German tolerance, flexibility, working ethos and pragmatism. Data from the World Value Survey and Geert Hofstede's cultural dimensions also show that Chinese and Germans are similar on cultural themes such as "long-term perspective" or the importance of work in life (as exemplified in the German word "Arbeitsfreude").



## Connecting the dots

Just in 1999, *The Economist* called Germany the “[sick man of the Euro](#)”. Fast-forward two decades, and Germany has become the undisputed economic power of the Eurozone. Germany is a typical export economy, with weak domestic consumption and its economic power founded upon its industrial base, such as robotics, electronic equipment and products as well as chemicals. Such high-end manufacturing and engineering is rooted in a strong tradition of craftsmanship in Germany: already in the Middle Ages, Germany’s economy was organized around guilds (which were destroyed in England and never existed in the U.S.), in which apprentices could learn and work in the shops of their masters to “master” their skills. Still, “master craftsman” is an honored title in Germany (“[Werkmeister](#)”). This was amplified by a cultural background that places high value on work as well as a focus on orderliness and discipline. In his study on the relationship between capitalism and religion, sociologist [Max Weber](#) indeed claimed that German Protestantism was related to the hard-working and thrifty German labor ethos. As a result, German business had a strong local responsibility, as the German state had a decentral and accommodating role as the individual *Länder* of Germany and specific cities always had a large degree of autonomy to formulate their own economic policy. Combined with strong labor unions that protected German laborers, the German industry and state made long-term economic plans, a process called “[Konzertierte Aktion](#)”, to boost Germany’s competitiveness. An example of this is the 2011 “[Industrie 4.0](#)” plan, a strategic initiative to boost Germany’s engineering and manufacturing capabilities, and an explicit [source of inspiration](#) for China’s Made in China 2025. This results in a long-term alignment between German state and industry on the one hand and societal parties (including universities) on the other. As such, Germany is the prime example of what [Michel Albert](#) has called the Rhinelandic model of capitalism, with a focus on stakeholder instead of shareholder value, long-term wealth instead of short-term profits and cooperation instead of competition. This is exemplified by Germany’s *Energiewende*, a concerted action to reduce Germany’s carbon footprint, which was also largely driven by the German state in collaboration with German [energy cooperatives](#) (*Genossenschaft*).

This cultural-historical background explains why Germany’s industrial infrastructure is unique, and arguably the best of the world. However, this doesn’t hold for its digital infrastructure. With the upcoming battle for digital hegemony, Germany fears being left behind by American and Chinese big tech. Within the information economy, the only large German company is SAP (which is nonetheless largely U.S.-owned). However, there is ample room to improve Germany’s digital power. This week, Germany launched a new industrial policy, called the “[Nationale Industriestrategie 2030](#)”. In line with the German tradition, the plan articulates

a long-term strategy to form German and European champions with state and societal support for 10 strategic sectors, as well as a state investments fund that would be used to pre-empt foreign takeovers of big German companies. We have written before that [creating these champions](#) will become an ever-important quest for European economies. And Germany has the potential to reap this strategic opportunity, as it has the financial means, originating from its current and budget surpluses, to make large investments in its digital infrastructure. And recently, Germany created significant state funds to boost domestic innovation in [senior-based economies](#), such as [AI](#), [electric](#) and [autonomous mobility](#), [quantum computing](#), and [nanotechnology](#). This comes at a delicate time: Germany presented its new industrial policy a day before the European Commission blocked the Franco-German [merger](#) between Siemens and Alstom and the German [acquisition](#) of Aurubis by Wieland. In the past years, EU regulators have blocked large German takeovers and consolidation efforts, putting Germany in a bind: the country is, given its history and geography, bound by Europe (Germany’s constitution even explicitly connects its fate to Europe’s). But as Germany emerged as the European geo-economic power from the European debt crisis between 2010 and 2015, we can expect that it will translate its economic clout into more political power and bend European regulation to its will. This year is already a crucial year for that, as Germany is [likely](#) to deliver the next president of the European Commission or president of the European Central Bank, leading to looser regulation on pan-European mergers or tighter monetary policy.

Furthermore, Germany is also increasingly looking eastwards. In part, it is because it is forced to do so as its current export markets are in trouble. But Germany is also the only Western European country with a long border with Central and Eastern Europe (e.g. Poland, Czech Republic, Austria), and has high hopes to serve its fast-growing consumer markets. But even further east, Germany is looking to gain strategic complementarities with China, as Germany’s geo-economic strategy puts it in line with China as both countries prefer a multilateral, rule-based world order, putting them together at odds with Trump’s America First agenda. And as German and Chinese innovation and business practices have cultural similarities, innovation and exchange between both countries might flourish as well along the Eurasian trade routes. Whereas other European companies remain wary, German companies are already investing heavily in China’s Belt and Road Initiative, such as [Siemens](#), [Daimler](#), [BASF](#), and Germany’s government remains willing to work with Chinese counterparts. Indeed, more integration between China and Germany, coupled with a boost of its digital innovativeness, might even create a second German “*Wirtschaftswunder*”.

## Implications

- The above developments might be accelerated by Angela Merkel’s [decision](#) to leave German politics by 2021. After 16 years of serving as Chancellor, and as Europe’s strongest leader since the Eurozone crisis, Merkel might use Germany’s huge fiscal and savings funds to make boosting Germany’s digital competitiveness her legacy project.
- From a cultural perspective, a German digital economy might also undermine its social contract. For example, big tech companies provide less [employment](#) than traditional, “old economy” companies do, which might face resistance from Germany’s labor unions and the German social contract. Furthermore, Germany’s war history has made it wary of privacy issues (e.g. [Google Maps’ street view](#) option is hardly available in Germany), further undermining the adoption of digital consumer practices such as fintech. However, there is also a chance to create a German or Rhinelandic version of the digital ecosystem, with an explicit focus on embedding digital technologies in society and a strong focus to collectively develop new technologies. We already see this in the industrial ecosystem of [Bavaria](#), differing from Silicon Valley with its focus on cooperation instead of pure competition.