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## The Economic Order of Post-Brexit Europe and the Role of Germany: An Ordoliberal Perspective

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### 4.1 Introduction

The completely unexpected decision by the British public to vote for Brexit in the 23 June 2016 referendum raised the question of the future shape of the European Union. After an initial shock, the European Commission in March 2017 reacted and issued a White Paper on the future of Europe in which it presented five scenarios for discussion on how Europe could evolve by 2025. Implicitly, the White Paper revealed a preference for a great leap forward towards a political union (Berthold 2017; Eder et al. 2017), which was subsequently underlined by European Commission President Jean-Claude Juncker in his State of the Union Address on 13 September 2017.<sup>1</sup> The ideas of a separate

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<sup>1</sup>Accessible at [http://europa.eu/rapid/press-release\\_SPEECH-17-3165\\_en.htm](http://europa.eu/rapid/press-release_SPEECH-17-3165_en.htm).

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budget for the eurozone, a common finance minister and a joint parliament, put forward by French President Emmanuel Macron, also point towards a “more Europe” trajectory.

The aim of this chapter is to analyse these options of the White Paper process for the future character of the EU’s economic order and the role of Germany in it. An ordoliberal perspective is applied for this purpose. This is interesting for two reasons. First, already in the 1950s ordoliberal economists and politicians in Germany, in particular Wilhelm Röpke and Ludwig Erhard, debated about the economic and political constitution of Europe. Many of their arguments are still strikingly topical today in times of Brexit. Second, Germany is the biggest and economically most powerful EU member country. It was a key player in the eurozone crisis, and its weight will increase in an EU without the UK. Thus, Germany is expected to play a leading role in shaping post-Brexit Europe (see, e.g., *New York Times*, July 4 2016). This raises the question of whether Germany itself favours a distinct model of European integration after Brexit. Some scholars contend that Germany might advocate a governance structure with a strong ordoliberal flavour (Blyth 2013, p. 142; Biebricher 2014; Cardwell and Snaith 2018). Ordoliberalism provided the theoretical foundation of Germany’s post-World War II economic system, known as a social market economy.

In order to assess the European Commission’s post-Brexit EU scenarios as well as Germany’s real-world economic policy preferences at the national and supranational levels, this chapter develops an ordoliberal reference model of European integration as an analytical framework. It will be argued that the ordoliberal reference model is largely supportive of the British vision of a free market-oriented and decentralised economic order of the EU rather than of an ever closer union as advocated by France and the European Commission. Nevertheless, Germany is unlikely to promote an inherent ordoliberal economic order in the EU for two reasons: first, Germany’s own economic policy has increasingly departed from the ordoliberal ideal. Second, the “sacralisation” of the European project in German politics and public opinion makes it almost taboo to question the trajectory of European integration towards a federation, even if criticism was due from an ordoliberal point of view.

The remainder of this chapter is organised as follows. After an outline of the underlying understanding of ordoliberalism (Sect. 4.2), Sect. 4.3 develops the ordoliberal reference model. Through this lens, Sect. 4.4 analyses four post-Brexit EU scenarios, and Sect. 4.5 explores the likelihood that Germany might advocate reshaping the EU post-Brexit using the ordoliberal reference model. The chapter ends with concluding remarks (Sect. 4.6).

## 4.2 Definition of Ordoliberalism

Ordoliberalism is a branch of classical liberalism that evolved during the Nazi period in the 1930s around economist Walter Eucken (1891–1950) and two jurists, Franz Böhm (1895–1977) and Hans Großmann-Doerth (1894–1944), at the University of Freiburg in Germany. It is therefore also known as the Freiburg School, although other prominent ordoliberal thinkers worked at other universities, such as Wilhelm Röpke in Marburg and Geneva and Alexander Rüstow in Heidelberg.

The ultimate aim of their research programme was to seek an economic system that would provide for a high degree of human dignity and prosperity given the negative experiences with the planned economies of Nazi Germany and the Soviet Union, interventionism during the Weimar Germany period and in the period before World War I, which they labelled *laissez-faire*, when the formation of cartels to restrict competition received support from policy-makers and the courts. The research concept of ordoliberalism rests on the premise that the institutional framework—or “the order” (*ordo* in Latin)—is crucial for the nature of the economic and societal system as it determines the range of individual freedom of action and structures incentives underlying individual action. According to ordoliberals, individual freedom and prosperity can best be ensured in what is called a competitive order (*Wettbewerbsordnung*). The task to set up and ensure an appropriate institutional framework for it is attributed to a strong but limited government.

This focus on the institutional framework of economic life as well as the importance of competition is a point of interest that ordoliberalism has in common with classical liberalism,<sup>2</sup> the Austrian School as well as New Institutional Economics and Public Choice Theory. A growing body of empirical literature on why some societies are rich and others poor underscores the ordoliberal insight into the central importance of the right institutional set-up for prosperity (e.g. North 1990; Olson 2000; Acemoglu and Robinson 2012). Hence, it is difficult to clearly delineate ordoliberalism from these related research programmes and denounce it as a thing of the past, an ideology or a German *Sonderweg* (special path). Rather, much of the early Freiburg School can be regarded as preceding today's New Institutional Economics and Public Choice Theory (Streit and Wohlgemuth 1997; Goldschmidt et al. 2009; Wohlgemuth 2013a, b). Meanwhile, a younger generation of German economists (e.g. Manfred Streit, Viktor Vanberg, Michael Wohlgemuth, Lars Feld, Nils Goldschmidt, Gerhard Wegner and Joachim Zweynert) advances the ordoliberal approach through the incorporation of Hayekian Austrian economics,<sup>3</sup> the New Institutional Economics of Douglass C. North and Elinor C. Oström, and the Public Choice Theory of James M. Buchanan. This modernised, broader understanding of ordoliberalism underlies the ordoliberal reference model for European integration and the subsequent discussion of the positions of the European Commission and Germany on the EU's post-Brexit economic order.

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<sup>2</sup>Classical liberalism, also known as 'old liberalism' or 'liberalism in the European sense', is not the same as North American liberalism ('new liberalism' or 'modern liberalism'). Although both share a strong belief in personal freedom, American liberalism gives much paternalist and interventionist power to the state similar to the European Social Democrats (Butler 2015).

<sup>3</sup>In 1962, this most prominent representative of the Austrian School took the chair for economic policy at Freiburg University and his insights are also sometimes referred to as the *Hayekian Ordnungstheorie* (Wohlgemuth 2001, p. 214; Goldschmidt 2006, p. 17). In particular, his view of competition as a discovery procedure has become widely accepted by younger economists in the Freiburg tradition (see, e.g., Streit 1995). For more details on common grounds and differences between Hayek and the early ordoliberals, see Streit and Wohlgemuth (1997), while Wohlgemuth (2013b) has more information on the overlapping between Austrian economics in general and ordoliberalism.

## 4.3 Ordoliberal Reference Model for European Integration

### 4.3.1 Importance of Individual Freedom

Like classical liberals and Austrian scholars, ordoliberals give priority to individual freedom in social, political and economic life (Streit 1995; Horn 2010; Butler 2015). For the early ordoliberals, this presumption was mainly derived from a Christian perspective as many of them (e.g. Eucken, Röpke and Müller-Armack) were practising Christians.<sup>4</sup> In this view, freedom is something given to every single person by God that constitutes his dignity. This means personal responsibility before God, respect for his fellow men as well as neighbourly love as the central driving force for voluntary solidarity (Schüller 2001). In addition, individual freedom is valued in a utilitarian sense following Jeremy Bentham (1746–1832), Adam Smith (1723–1790) and David Hume (1711–1776) as the best way to maximise the welfare of society as a whole, because it allows people to display their creativity and engage voluntarily in the mutually beneficial exchange of goods and services (Eucken 1952/1990, pp. 155ff.; Butler 2015).

Yet, all liberals agree that this individual freedom can never be absolute since different people's freedoms may conflict. So there has to be a minimum necessary restraint to protect the freedom of other individuals. For ordoliberals, competition is the most effective tool to constrain the misuse of individual freedom to the detriment of others, while at the same time preserving his personal dignity and unfolding people's productive power to the fullest extent possible.

### 4.3.2 Central Role of Competition

Competition is central in the ordoliberal approach as an instrument of constraining power, but also as a discovery procedure. It should therefore

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<sup>4</sup>For more detail, see Goldschmidt (1998), Lorch (2013), Plickert (2016), and Hien (2017).

be at the core of European integration. The concern to establish a mechanism that would effectively constrain power was central to early ordoliberal thinkers (see Böhm 1957/1960) and motivated by German economic and legal history where private attempts to close markets, e.g. by forming cartels, were considered legitimate uses of the freedom of contract. If economic power becomes vested in the formation of private law, it impairs the political system and allows for infringements on the liberty of others (Streit and Wohlgemuth 1997). At the same time, it cripples the price mechanism and its allocative potential. Competition curtails economic as well as political power and so safeguards individual freedom by giving the opportunity to choose and run away from bad to better transaction partners. That is why Böhm (1961, p. 22) called competition “the most genial disempowering instrument”.

Hayek (1978) highlighted competition’s function as a discovery procedure to overcome the problem of knowledge. As he (1945) explains, the knowledge of what is needed, who needs it, and who has the means to meet these needs is dispersed and fragmented among the millions of individuals who compose society and is often held in inarticulate forms. Moreover, the cognitive abilities of every human being to capture and process all of this scattered information are limited. This makes it impossible for a centralised body of experts and politicians to gather in its totality the knowledge required to steer an economy into a certain direction. Instead, market competition through profit-and-loss feedbacks and changes in relative prices is best suited to mobilise the available bits of scattered knowledge to ensure a high level of prosperity. Profit-and-loss feedbacks provide the necessary incentive for individuals to acquire constantly new knowledge about consumer needs and how these should be met. If they do it successfully, they are rewarded by profits; otherwise, they suffer losses which urge them to correct their errors. Meanwhile, Kirzner (1973, 1997) emphasised that the main driving force in this discovery procedure is not governments but alert private entrepreneurs. Because entrepreneurs invest their own resources, they must be careful and astute when making investment decisions, while government bodies are generally institutionally precluded from capturing pecuniary profits in the course of their activities (Kirzner 1978).

### 4.3.3 Institutional Requirements

To unleash and maintain competition in both its disempowering and discovering functions, certain institutional requirements must be met. They are most prominently described by the famous “principles” laid down by Eucken (1952/1990, pp. 254ff.). Although they have been developed for a national economy, they can also be applied to supra-national entities (Bökenkamp and Hesse 2016). At the core of the so-called constituent principles, conducive to the emergence and maintenance of the competitive order, is a workable price system that in the Hayekian interpretation transmits information in a codified manner about what should be produced and supplied and how this should be done and when. Further necessary principles are sound money, open markets, freedom to contract, private property, the enforcement of accountability (*Haftung*) for one’s actions and predictability of economic policy. If competition remains hampered despite the implementation of these principles, Eucken (1952a, p. 292ff.) proposes further political interventions which he laid down in the so-called regulating principles. These comprise antitrust laws, income redistributing tax laws and laws to curb or avoid external effects.

While most Austrian economists question the need for these regulating interventions, they as well as classical liberals and institutional economists widely accept the importance of the constituent principles (Butler 2010, 2015). Hayek (1973, 1960) argued that a predictable, non-violent and self-regulating competitive and social order arose only when these principles were general (without exceptions), universal (applying to everyone) and stable (not changing very often). Such an order then tackles economic challenges with greater creativity and effectiveness than any centrally planned order.

### 4.3.4 Restraining Political Power

Conferring upon the state, the task of creating and ensuring a functioning institutional framework for the competitive order poses the problem of the abuse of political power. Eucken (1932) and Böhm (1933)

saw politicians in much the same way they viewed economic agents: as self-interested actors rather than benevolent social wealth maximisers exclusively committed to the public interest. Policy-makers are not only exposed to the pressure of interest groups seeking selective benefits that provide them advantages over rival firms (e.g. subsidies and protection against competitors). They have an incentive to supply rent to secure re-election and retain power (Buchanan 1987). This is why the Freiburg ordoliberals called for a strong but limited state. It should be strong enough to resist the pressure of interest groups, but at the same time limited to pursue only the genuine task of protecting competition using market-compatible instruments (*Ordnungspolitik*).

However, the early ordoliberals grouped around Eucken did not elaborate on how a political constitution could look like to prevent and limit the arbitrary use of political power.<sup>5</sup> Later, Hayek (1979, ch. 17) did develop such a constitutional proposal. He argued that the legislative institutions of the time were preoccupied with awarding privileges to interest groups to acquire political support to the detriment of the general rule. Hayek therefore proposed a bicameral legislature: an upper chamber (the legislative assembly, pp. 112ff.) limited to enacting abstract rules needed to preserve the competitive order, and a lower chamber (the governmental assembly; pp. 119ff.) controlling the government and deciding on the provision of public services.

At least formally, the EU has a bicameral legislature, with the Council of Ministers as a sort of upper chamber and the European Parliament as the lower chamber. However, although its powers have continuously increased, the European Parliament neither has the power nor the will to repeal acts of the Commission. As *The Economist* (2017) has reported, rather than controlling spending and curbing the executive, the European Parliament often behaves more as a lobby group “whose main aim seems to be to spend more and to augment its own powers”. As a result, the national heads of government, who make important decisions

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<sup>5</sup>As Vanberg (1988, p. 24) put it, ordoliberals have “devoted astoundingly little explicit argument to the issue of what constitutional provisions might be required to make the ‘strong government’ perform to its proper task and not use its power in an undesired way”.



in the European Council in a bargaining process, can effectively ignore their parliaments and bypass national voters (see also Streit 2011).

Given the peculiarities of the democratic process, attempts to profoundly change the existing rules of the game face insurmountable difficulties. This would require a binding decision of self-restraint by those who neither have a vested interest nor are likely to face massive pressure from the voters to do so (Streit 2000). In this situation, the only effective way to curb political power is competition between different jurisdictions. This allows people to choose not only through voting but also through exiting. At the same time, competition between legal entities acts as a discovery procedure to find out the appropriate institutional framework for a market order. The exit of mobile resources (capital and labour) allows citizens to test the expediency of available institutional arrangements and induces political actors to adapt to the preferences of the population and to develop innovative institutional solutions to the existing problems (see also Streit and Wohlgemuth 1997). Therefore, interjurisdictional competition must be an essential element of the ordoliberal concept of the EU.

### 4.3.5 Decentralisation

This insight into the disempowering and discovery properties of competition prompts a further normative conclusion for European integration: that political decision-making should be decentralised as much as possible to the national or even regional and local levels following the principle of subsidiarity (e.g. Hayek 1944/2006, 1979; Röpke 1951/2009, 1959, 1961/1964). This not only alleviates the power and knowledge problem, as political decision-makers at lower levels have a better understanding of local conditions, but also better ensures respect for national peculiarities and preferences.

Ordoliberal scholars fear that a powerful supranational authority in Europe might misuse its power to impose interventionist and redistributive policies between regions and so limit economic freedom. In this context, they stress the advantage of small political entities. This is in contrast to the view popular among proponents of an ever closer union that single

European countries are too small and weak to compete effectively with big global players such as the USA, Russia or China. However, Röpke (1959, p. 170f.) pointed out that such big entities are more tempted to harmonise and protect their economies and so limit freedom, whereas for small states closing the economy is not an option. Therefore, small states are “islands of economic reason” (Röpke 1959, p. 170; Mises 1927/2002; Marquardt and Bagus 2017; Vaubel 2017). Raico (2013) underscores in his analysis of the origins of the “European miracle” that Europe’s economic success in the past few centuries has essentially been rooted in its diversity and the coexistence of and competition between small states, which creates the ability for its people to easily emigrate from one political jurisdiction to another and learn from each other.<sup>6</sup>

#### 4.3.6 The Right to Exit

The disempowering and discovery functions of competition can further be enhanced in a supranational association if not only the individual citizens have the right to exit but also its subunits. This implies as an additional normative conclusion their right to secession. As a number of studies show,<sup>7</sup> federal states tend to centralise, mainly for two reasons. First, politicians and bureaucrats aim to increase their power by establishing tax and regulatory cartels, and second, bureaucrats and organised interest groups try to escape the attention of voters by shifting

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<sup>6</sup>British philosopher and political economist John Stuart Mill (1806–1873) and Germany’s greatest poet Johann Wolfgang von Goethe (1749–1832) argued in much the same vein. Mill (1869/1999, Ch. 3) concluded: “What has made the European family of nations an improving, instead of a stationary portion of mankind? Not any superior excellence in them, which when it exists, exists as the effect, not as the cause; but their remarkable diversity of character and culture. Individuals, classes, nations, have been extremely unlike one another...Europe is, in my judgment, wholly indebted to this plurality of paths for its progressive and many-sided development”. Goethe, meanwhile, wrote in 1828: “*Frankfurt, Bremen, Hamburg, Lübeck sind groß und glänzend, ihre Wirkungen auf den Wohlstand von Deutschland gar nicht zu berechnen. Würden sie aber wohl bleiben, was sie sind, wenn sie ihre eigene Souveränität verlieren und irgendeinem großen deutschen Reich als Provinzialstädte einverleibt werden sollten? – Ich habe Ursache, daran zu zweifeln*” (in: Johann Peter Eckerman: *Gespräche mit Goethe in den letzten Jahren seines Lebens* - Kapitel 287, <http://gutenberg.spiegel.de/buch/-1912/287>).

<sup>7</sup>See e.g. Krane (1988), Vaubel (1994, 1996, 2009).

political decision-making away from the local to the central or supra-national level (Vaubel 2013). In this situation, “secession, or the threat thereof, represents the only means through which the ultimate powers of the central government might be held in check. Absent the secession prospect, the federal government may, by overstepping its constitutionally assigned limits, extract surplus value from the citizenry almost at will, because there would exist no effective means of escape” (Buchanan 1995/2001, p. 71). Thus, secession is seen as a defence right against centralistic and discriminatory legislation that, if formally enshrined in the constitution or treaties, puts politicians and bureaucrats of different countries under competitive pressure to provide less centralisation, redistribution and other discriminatory legislation (Doering 2002; Vaubel 2013). The right to secession has in fact been incorporated in the Lisbon Treaty where Article 50 gives member states the right to leave the EU. Yet, hardly anyone in the EU institutions expected that a member country might really choose this option as they do everything they can to discourage secession (Vaubel 2013).

### 4.3.7 A Flexible EU of Different Clubs

Table 4.1 summarises the cornerstones of the ordoliberal reference model for European integration. Setting them implies a rather loose and flexible cooperation of states as the desirable form of European integration that respects national preferences with a high degree of decentralisation based on free economic and institutional competition including the right to exit the association as a whole, as well as certain fields in which member states want to do less together. The result would thus be a community of different clubs based on the common market as its core. The former liberal European Commissioner with dual German-British citizenship, Ralf Dahrendorf (1929–2009), called this in 1979 a “Europe à la carte”. Solidarity in this model of Europe is not equal to large transfer payments among member countries, because they eliminate the incentives for market reforms and in the long run create a situation where some countries live at the expense of others, which, in turn, raises resentment among the member countries. On the

**Table 4.1** Cornerstones of an ordoliberal reference model for European integration

Building blocks	Purpose
Individual freedom	Value in its own based on Christianity Driving force of economic progress
Competition	Dismantle economic and political power
<ul style="list-style-type: none"> <li>• Within the national economies</li> <li>• Among member states</li> <li>• Between member and non-member states</li> </ul>	Discovery procedure <ul style="list-style-type: none"> <li>• In the economic sphere</li> <li>• In the political sphere (institutional competition)</li> </ul>
Institutional requirements	Keeping markets open
<ul style="list-style-type: none"> <li>• Constituent principles</li> <li>• Regulating principles</li> <li>• Universalisability</li> </ul>	
Restrained political power	Prevent rent seeking and provision
Decentralisation and right to exit	Restrain economic and political power Reducing epistemological problems

Source Own depiction

contrary, European solidarity in this sense is playing according to the rules of market competition, which includes the application of the principle of accountability for one's decisions (Erhard 1957/1964; Röpke 1961/1964).

This ordoliberal reference model of Europe has the advantage of withstanding the strains wrought by human imperfections which arise from the lack of omniscience (limited knowledge) and benevolence (self-interested behaviour) of both economic and political decision-makers. The competitive order can correct for these imperfections by allowing a competitive trial and error learning process, allowing freedom of entry and exit, and by channelling selfish motives of individuals into what is beneficial to the society. The central problem of the eurozone and the migration crises stems exactly from the self-interested behaviour of its member countries that violate (d) agreed-upon rules (of the Stability and Growth Pact and the Dublin Accord). This, in turn, is related to the missing credibility to impose sanctions on those who break rules. Hence, the fewer areas are regulated by integration from above the fewer opportunities to violate rules. In addition, the social interdependence costs understood as the sum of decision-making costs

and external costs will be much lower than in a one-size-fits-all ever closer union. In a Union of 27 diverse member states, decision-making costs are high because it is more difficult to agree in a heterogeneous than a homogeneous group. Equally, the external cost resulting from the choices made by the relevant body contrary to the individual country's own interest rises with the fear of being overruled in majority voting (Buchanan and Tullock 1962).

## 4.4 Scenarios for EU's Post-Brexit Economic Order

Documents as part of the White Paper process provide indications about the possible shape of the EU's economic order post-Brexit. The White Paper process was initiated by the European Commission led by Jean-Claude Juncker in response to the Brexit vote, and it sketches five scenarios of what the EU27 could look like by 2025.<sup>8</sup> The documents address the order among the remaining member states as well as the relations to the UK and other countries outside the EU.

### 4.4.1 The Internal Order of the EU

The five scenarios of how the EU's internal economic governance could develop in the next decade range from business as usual to a "multi-speed" Europe to "doing less more efficiently" and "doing much more together".

From the ordoliberal perspective, the preferable option would be scenario 2 (nothing but the single market), complemented with elements of scenario 3 (those who want more do more) and scenario 4 (doing less more efficiently), as this comes nearest to the reference model of a loose, decentralised and flexible association based on economic and

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<sup>8</sup>All the documents of the White Paper process are accessible at [https://ec.europa.eu/commission/white-paper-future-europe-reflections-and-scenarios-eu27\\_en](https://ec.europa.eu/commission/white-paper-future-europe-reflections-and-scenarios-eu27_en).

institutional competition. However, in the last two scenarios, some problems are caused by areas that the Commission suggests should be assigned to the supranational level. These include the harmonisation of taxes, social, environmental and consumer protection standards, and innovation policy. This would be detrimental to ordoliberal principles, because it further reduces and, in the extreme case, eliminates economic and institutional competition as a discovery and disempowering procedure.

A further problem with option 3 is that it does not specify what “those who want more do more” exactly means. In today’s EU, there are already coalitions of those wanting to do more together in the Schengen and euro areas. Widening this option to cover other areas, such as defence and social issues, would be in line with the ordoliberal concept of flexibility. However, this would not be the case if this suggestion were to be understood as an intermediate stage on a predefined trajectory towards an ever closer union where some member states move ahead faster than others. Such an “ever-closer-one-size-fits-all-sooner-or-later” option is not really compatible with genuine flexibility, where different countries engage in mutual integration in different policy areas (Wohlgemuth 2017c).

Although officially neutral, the European Commission made it clear that it was least enthusiastic about option 2 (Spiegel-Online 2017), while favouring the most federal option of “doing much more together” (Wohlgemuth 2017b; Berthold 2017). As expressed in the White Paper, the Commission believes that a big disadvantage of the second scenario is the persistence of different tax policies as well as product, social and environmental standards, because it fears a “race to the bottom”. Furthermore, the Commission worries about the resurgence of bilateralisms that might prevent the EU from speaking with one voice in a number of international fora on global issues such as “climate change, fighting tax evasion, harnessing globalisation and promoting international trade”. This belief is in stark contrast to the ordoliberal insights as it fails to understand the productivity and freedom-enhancing powers of institutional competition. As Kirzner (1973, 1997) pointed out, what is crucial (“necessary and sufficient”) to induce and maintain competition is that markets are kept open. But this does

not require harmonisation of all national rules but their mutual recognition following the *Cassis de Dijon* decision of 1979. This implies that products and services lawfully produced in one member state must be freely marketable in all other member countries. Hence, based on these institutional prerequisites, ordoliberals unequivocally support the free flow of products, services and capital. With regard to the free movement of labour, Röpke (1959) would have shared the Brexiteers' demand for an encompassing right of the national states to steer external and internal EU immigration to protect national identity and not to overburden the accommodation capacities of a country to integrate migrants.

European Commission President Jean-Claude Juncker reaffirmed his preference for the great leap forward towards an ever closer federal state in his State of the Union Address on 13 September 2017 when he proposed an expansion of the Schengen area, the eurozone and the banking union to the whole of the European Union as well as the establishment of a European Social Standards Union. This would amount to pressing ahead with a one-size-fits-all policy that furthers economic and institutional competition as a discovery and disempowering procedure. In doing so, the EU would undermine the foundation for liberty and prosperity. According to Hayek (1958), a free common market is a sufficient basis for a working interstate federation as it prevents government meddling with the economy and preserves peace by keeping social interdependency costs low.

#### 4.4.2 Relations with Non-EU Members

Equally problematic from an ordoliberal perspective are suggestions outlined in the new reflection paper on globalisation as well as in Juncker's State of the Union address on external relations with non-EU countries. Both documents underline the EU's reluctance to make unilateral concessions and grant free trade with non-EU members at any price. The EU wants to defend its "strategic interest" and "legitimate public policy objectives" and "fight for a fairer global order". In this context, "fair" means provision of "a level playing field" by preventing or eliminating tax evasion, government subsidies and "social dumping"

through “harmful and unfair” lower social, health and environmental standards” (p. 13). Instead, the EU wants to promote a “race-to-the top’ approach” (p. 13). Rather than fostering economic and institutional competition to curb excessive taxation and to find appropriate standards as well as other institutional settings and innovations that meet consumers’ preferences, this policy is protectionist in nature as it aims at raising the rivals’ cost and making all countries equally sclerotic and uncompetitive. Hence, the policy conflicts with the crucial ordoliberal constituent principle of open markets.

Keeping markets open through eliminating entry barriers is essential for enhancing the disempowering and discovery properties of competition. Therefore, ordoliberals would suggest upholding and deepening the common market with the UK after Brexit and even recommending unilateral trade liberalisation. However, for political reasons, this seems a quite unlikely option for the EU27. Not only would this conflict with the EU’s foreign trade policy stance, which is predicated on the reciprocity of intergovernmental bargains. In the EU institutions, there are also strong forces that want to deter other EU countries with large Euro-sceptic movements from choosing the same path as the UK.<sup>9</sup> Therefore, a new institutional arrangement for the EU27-UK relations will have to be negotiated.

## 4.5 What Drives Germany’s Post-Brexit EU Policy?

Regardless of whether Germany favours a certain scenario or even a distinct direction for EU policy post-Brexit, the EU economic order presupposes that German policy-makers are guided by a specific economic philosophy and that there is a realistic chance to implement it.

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<sup>9</sup>See, e.g., a BBC report (<http://www.bbc.com/news/uk-politics-41140564>) citing the EU’s chief Brexit negotiator Michel Barnier as saying: “We intend to teach people... what leaving the single market means”.



### 4.5.1 Economic Philosophy

In the ongoing public debate on Germany's role in the EU, scholars and media have focused on the German government's appeal to obey rules and undertake austerity measures in the management of the eurozone crisis—amid calls by other member countries for transfers and Keynesian policies—in a clear reference to the legacy of ordoliberalism, the economic philosophy underlying Germany's social market economy concept (see, e.g., Bonefeld 2012; Dullien and Guerot 2012; Blyth 2013; Biebricher 2014; Van Esch 2014; Young 2014; *Economist* 2015; Nedergaard and Snaith 2015; Stelzenmüller 2015; Feld et al. 2015; Brunnermeier et al. 2016; Cardwell and Snaith 2018). Therefore, one might expect that the potential ordoliberal governance of the EU's economic system will be strengthened after Brexit. However, this presupposes that the German policy-makers' mindset is really shaped by that economic strain of thinking.

To what extent, if at all, ordoliberalism drives German policy-makers is a complex question that faces insurmountable difficulties in disentangling various influences (see also Biebricher 2014). A content analysis of speeches by selected political figures in terms of how often they refer to ordoliberal terms and thinkers, as conducted by Hien (2017), is at best a first hint. Even if politicians publicly referred to ordoliberal principles, actual economic policy might point to the opposite.

Even though the rules of the game are central to ordoliberal thinking, and the insistence on accountability for one's debts and on low inflation reflects two of Eucken's constituent principles, accountability and good money, they alone do not make German economic policy ordoliberal. Meanwhile, Germany's inclination to rules may also reflect a historical experience that can be traced back to the Holy Roman Empire of the German Nation. Like today's EU, it was a multi-ethnic complex composed of hundreds of quasi-independent subunits (principalities and duchies). Power was highly decentralised and vested in these entities. Yet, what bound them loosely together under a relatively powerless emperor was rules that sanctioned these rights and regulated the relation to the emperor. The same holds for the constituent states of the German Empire after 1871. As Leipold (2006) explains, these legal bonds and

regulations were crucial in shaping Germany's informal institutional setting in the century-long absence of common ideological and religious ties and a common national identity (see also Habermann 2013).

Likewise, the preference for low inflation could just as well be explained by Germany's bad historic experience with the hyperinflation of 1923 and 1945 (Bökenkamp 2016). And Germany's call to curb budget deficits could merely be an expression of its national self-interest for the simple politico-economic reason of limiting Germany's liability for other countries' wrong policies and of avoiding the moral hazard arising from easy access to someone else's money. Although a large section of the German public is pro-European, it might be difficult to explain to domestic voters the need for constant financial transfers to countries that are reluctant to correct flawed policies.

Moreover, an ordoliberal economic policy agenda would require that not just two, but *all* constituent principles are fulfilled. So insisting on low inflation and debts while fixing prices in certain markets would be inconsistent and not compatible with ordoliberalism. Furthermore, ordoliberalism is not about setting and enforcing rules per se. It is about setting and enforcing *rules that are conducive to competition* as a discovering and disempowering procedure. This is an essential difference as rules or laws can also be set and enforced to restrict or even oust competition. In this respect, too, Germany has a long tradition that goes back to eighteenth-century Prussia and the concept of the police and welfare state. Characteristic for its style was a strong omnipresent government that was not only responsible for the enforcement of law and order, but also for the social well-being of its citizens and therefore regulated through "enlightened" bureaucrats and kings (for more detail, see Habermann 2013; Leibold 2006). As a result, until the post-World War II period, Germany actually had a statist tradition (Habermann 2013; Wehler 2014; Bökenkamp 2016; Brunnermeier et al. 2016). By contrast, France until World War II advocated *laissez-faire* and a rule-based economic policy referring to classical liberal economists Jean-Baptiste Say and Frédéric Bastiat (Bökenkamp 2016; Brunnermeier et al. 2016).

But German economic policy after the end of World War II, specifically the country's social market economy system, was also full of examples of rules that hampered competition and favoured particular vested

interests. One of the latest examples is a renewable energy policy measure—instituted by the new federal government of Chancellor Angela Merkel—that completely banned market forces. A similar policy scheme was being discussed with regard to the automotive industry under the motto *Verkehrswende* to promote e-cars (see, e.g., Gastel 2017). The level of subsidies to the selected sectors such as coal, steel, shipbuilding, energy and transport rose almost uninterruptedly beginning in 1970, even after Chancellor Kohl assumed office and his conservative-liberal coalition government committed itself to reducing such subsidies and strengthening market forces. According to Laaser and Rosenschon (2016), in 2015, the total volume of subsidies reached its highest level ever, at EUR 168 billion. Other more recent violations of ordoliberal principles are the minimum wages and maximum prices in the rental market—because they are government interventions into the market process in pursuit of specific market outcomes (see also Erlei 2014).

Ordoliberalism is considered to have been most influential only in the first phase of the social market economy from 1948 to 1966 under Ludwig Erhard, Germany's first post-war economics minister until 1963 and later chancellor until 1966 (Habermann 2013; Sally 2016). Although he made the notion of the social market economy popular, Erhard clearly stood for a free market economic policy on both the national and European levels. For Erhard, the social market economy was not understood as a “third way” between extreme socialism and extreme capitalism, but a market economy (Goldschmidt 2004). He (1966, p. 320) was convinced that “the freer an economy is, the more social it is”. Ludwig Erhard's free market policy worked and transformed West Germany into Europe's economic powerhouse. However, Erhard and his ordoliberal advisors did not succeed in making the reforms long-lasting (see Rüstow 1961; Röpke 1966; Habermann 2013). Many far-reaching regulations of markets and industries prevailed (e.g. in agriculture, housing, transportation, energy, services and crafts), and antitrust legislation was filled with many exemption clauses that allowed for the restriction of competition.

In the 1960s, the ordoliberal component of economic policy progressively diminished with the rise of Keynesianism and the persistence of egalitarian ideas (Feld et al. 2015). As a result, socially and, in recent

times, ecologically motivated interventions increased and gradually displaced the market (for more detail, see Schüller 2002; Bökenkamp 2010). Like in Prussia's police and welfare state, the view came to prevail that enlightened benevolent policy-makers must and can engineer the free market to produce desirable results in the name of social justice and ecology (Habermann 2013). This resulted in a regulated economy that is ranked 26th worldwide (down from 17th) in the latest 2017 Index of Economic Freedom compiled by the Heritage Foundation (2017), far behind Switzerland (No. 4), Estonia (No. 6) and the UK (No. 12), and in a vast welfare state that is increasingly ill-equipped to tackle demographic challenge. On the European level, since the Maastricht Treaty of 1992 Germany increasingly adopted the French approach to economic policy, with an emphasis on the "primacy of politics" and a preference for supranational collective actions (Schüller 2011). Chancellor Angela Merkel has continued this course. Her government has advocated an energy transition and tax harmonisation and for the most part supported France's push for a European economic government.

Ordoliberal principles seem to prevail at the Bundesbank and in the German Council of Economic Experts (GCEE), which advises the government and the country's central bank (Feld et al. 2015). In a lecture given in 2008, the former chief economist of the European Central Bank (ECB), Jürgen Stark (2008), said that the work of the ordoliberal Walter Eucken was "a constant source of inspiration" for him. In an annual Walter Eucken lecture in Freiburg in 2013, Jens Weidmann (2013) underscored the importance of ordoliberal insights in successfully managing the EU's manifold crises. Meanwhile, former GCEE Chairman Olaf Sievert (2003) said that the Council always focused on ordoliberal rather than interventionist policies. In the current line-up of the Council, one of its members, Lars Feld, concurrently works as the head of the Freiburg-based Walter Eucken Institute. Together with three of the four other members (except pro-unionist Keynesian economist Peter Bofinger), Feld is usually critical of the government for its interventionism.<sup>10</sup> However, their influence on politicians should not

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<sup>10</sup>See, e.g., Jahresgutachten 2014/2015: "Mehr Vertrauen in Marktprozesse", or Jahresgutachten 2013/2014: "Gegen eine rückwärtsgewandte Wirtschaftspolitik".

be overestimated; decision-makers often take such advice with reservation or ignore it altogether (see Straubhaar 2014; *FAZ* 2009). So ordoliberal principles at best play only a minor role for Germany's government in economic policy-making. Therefore, for the time being, it is unlikely that Germany will be promoting a distinct ordoliberal alternative option for the EU's economic order after Brexit.

### 4.5.2 The Primacy of European Unity and Stability

European integration takes high priority in German politics. In view of the country's history, there is a deep-seated belief in Germany in the European project. Even in the preamble to its constitution, Germany committed itself to serve for peace as an equal partner in a united Europe. It is therefore almost taboo to question European integration (Wohlgemuth 2017a) and an imperative of Germany's foreign and European policies irrespective of party lines to keep the EU united and stable and continue integration. However, this always requires compromises to bridge differences between different members and strains of thinking (Steinmeier 2016; Besch and Odendahl 2017; Helwig 2017). Traditionally, in these efforts, Germany has always sought close coordination with France. Regardless of different policy preferences, these two countries usually succeeded in reaching compromises, making both countries major drivers of European integration. The introduction of the euro under Chancellor Helmut Kohl, despite warnings from many economists, was the most prominent example of the priority Germany gives to upholding European unity over economic principles.<sup>11</sup> This Franco-German axis, as "the saviour of the European project", has gained even more importance after the Brexit vote and the erosion of the hitherto strong German–Polish relationship since the Law and Justice party came to power in Poland in 2015. The Franco-German team-up gained new momentum after the election of Emmanuel Macron as France's new president on 14 May 2017.

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<sup>11</sup>For more detail, see Bagus (2010), Starbatty (2013).

Macron won the election with a clear pro-EU agenda and concrete proposals, such as an economic government with a eurozone budget for joint investments and an EU finance minister. Although Germany is in general supportive of an economic government for the eurozone (see, e.g., *Welt* 2017), it is not clear to what extent both countries share the same understanding. Mussler (2011) and Wohlgemuth (2017a) argue that the current German government with Finance Minister Wolfgang Schäuble wants an economic government primarily to restore the rule-based economic coordination and surveillance of competitiveness in the eurozone, including the impartial automatic enforcement of the stability pact following strict criteria. But raising and spending European taxpayers' money or issuing joint eurobonds would not fall within the minister's remit (Wohlgemuth 2017c). Yet, this is only the position of the CDU and the liberal FDP. Ahead of the 24 September 2017 federal elections, the German liberals campaigned on a market-oriented message and called for phasing out bailout funds, an orderly state bankruptcy, a streamlined exit process in the eurozone (Helwig 2017) and an amicable Brexit (Wohlgemuth 2017d).

Instead of binding legal commitments, France favours political discretion and intergovernmental decisions on how to spend the money raised from common taxes or mutualised debt instruments. Yet, given the German government's interventionist economic policy record at home, it is likely that the visions of both the French and German governments for a reform of the eurozone might not differ that much (Berthold 2017). German ordoliberal economists often describe Angela Merkel as a chancellor with no principles, except for staying in power (Berthold 2017), and "changing her mind according to public opinion and political opportunity with disarming nonchalance" (Wohlgemuth 2017d). France's Macron, in his September 2017 "Initiative for Europe", and the European Commission, in its 6 December 2017 roadmap for deepening the eurozone, both called for a separate eurozone budget, a common EU finance minister, common deposit protection and the establishment of a European Monetary Fund. These proposals were in general welcomed by the new German federal government in its coalition treaty in March 2018 (Bundesregierung 2018). Meanwhile, in May 2018, a group of

154 economists, most of them anchored in the Freiburg and Austrian Schools as well as in Institutional Economics and Public Choice Theory, issued a public appeal to the new federal government in which they dismissed calls for deeper eurozone integration (*FAZ* 2018).

### 4.5.3 Germany's Position in EU Institutions

A further factor making it unlikely for Germany to push for a comprehensively distinct model for the EU's post-Brexit economic order is its position in key EU institutions where major decisions are made. This, in turn, depends on the voting rules.

Germany on its own can only block decisions in the permanent rescue-funding programme of the European Stability Mechanism (ESM) where decisions are made about austerity measures in exchange for loans. There, the voting rights of each ESM member are equal to the number of shares allocated to it in the authorised capital stock of the ESM as set out in a February 2012 annex to the treaty establishing the ESM. Germany's share in the paid-up capital is the largest, at almost 27%. It therefore has in principle a blocking minority. However, the most important decisions<sup>12</sup> taken by the EMS Board of Governors require mutual consent. Only in the ESM emergency voting procedure, which decides on financial assistance, and in areas of minor importance to the current anti-crisis policy,<sup>13</sup> can Germany use its blocking minority (European Stability Mechanism 2012).

In the European Central Bank, which was originally modelled after the German Bundesbank, Germany has even less power to influence monetary policy. Under the one-member-one-vote rule, Germany has regularly been outvoted in the ECB Governing Council by countries with a different view on macroeconomic stability (Italy, Portugal,

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<sup>12</sup>These include decisions to provide stability support to an ESM member, the choice of instruments, conditions and terms of such support, calling in authorised unpaid capital, changing the authorised capital stock and adapting the maximum lending volume.

<sup>13</sup>They include setting out the detailed terms of accession of a new member to the ESM, appointing the managing director and approving the annual accounts of the ESM.

Greece, Spain and France). The same may happen with the proposed economic government for the eurozone. Even if it were to be modelled after fiscally responsible Germany, it is likely that Germany and its smaller allies, such as Austria, the Netherlands, Luxemburg, Finland, Ireland, the Baltic states and Slovakia, would find themselves in the minority amid efforts to push through the proposal (Trebesius 2017). Similarly, Germany has a minority position in the Supervisory Board and the Single Resolution Board of the banking union, because both these organisations follow the one-member-one-vote principle. However, the Council of the EU can reject decisions made by the Single Resolution Board on the liquidation of banks within 24 hours if it finds that the bankruptcy is against the public interest.

Nor in the EU Council can Germany alone impose its preferences in the qualified majority voting procedure despite its biggest share of votes by population (16.06%). It needs allies. Under Article 16 of the Treaty on the European Union, as of 1 November 2014 the qualified majority is reached when 55% of the member states (16 of 28, or 15 of 27 after Brexit) representing at least 65% of the EU's population approve an act. In the case of a proposal from neither the Commission nor the High Representative, the qualified majority is 72%. In addition, there is the possibility to stop proposals through a blocking minority. This must include at least four Council members representing at least 35% of the EU's population (European Council 2017).<sup>14</sup> Without the UK, voting power in the Council will shift towards statist-oriented rather than stability-minded countries. Germany will find it harder to build up blocking minorities.

Table 4.2 classifies EU member countries into liberal and statist economies, using the Heritage Foundation's 2017 Index of Economic Freedom, and assigns to them their votes by population according to an EU vote calculator. Although the more liberal-oriented countries will retain their blocking minority after Brexit, their share will decrease from almost 50% to 42%. The blocking minority might be lost, in particular

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<sup>14</sup>In cases where not all member states participate in voting (e.g. acts adopted only by euro-area or Schengen member states, or within enhanced cooperation), the qualified majority is calculated only on the basis of the participating member states.



**Table 4.2** Council voting weights in the EU before and after Brexit (% of total EU population)

Liberal economies			Statist economies		
Member state	Before Brexit	After Brexit	Member state	Before Brexit	After Brexit
EE	0.26	0.30	RO	3.87	4.44
IE	0.91	1.05	BG	1.40	1.61
UK	12.79	–	CY	0.17	0.19
LU	0.11	0.13	BE	2.21	2.53
NL	3.37	3.87	MT	0.09	0.10
LT	0.57	0.65	HU	1.92	2.21
DK	1.12	1.28	SK	1.06	1.21
SE	1.96	2.24	ES	9.09	10.42
LV	0.39	0.44	FR	13.05	14.96
FI	1.07	1.23	PT	2.02	2.32
DE	16.06	18.42	IT	12.00	13.76
CZ	2.04	2.34	HR	0.82	0.94
AT	1.71	1.96	SI	0.40	0.46
PL	7.43	8.52	EL	2.11	2.42
<i>Total</i>	<i>49.79</i>	<i>42.43</i>	<i>Total</i>	<i>50.21</i>	<i>57.57</i>

Source EU's vote calculator <http://www.consilium.europa.eu/en/council-eu/voting-system/voting-calculator/>; Heritage Foundation (2017)

if Poland, with its share of 8.52% of the population, moved from the liberal to the statist group. Such a move cannot be excluded given the Polish ruling Law and Justice party's interventionist and nationalist economic policies as well as its increasingly anti-German rhetoric. So this underscores the importance of the UK as an ally for promoting a distinct economic policy agenda.

In fact, the ordoliberal reference model of European integration described in Sect. 4.2 is largely congruent with the British vision of Europe and many Brexit arguments. While migration did play a role, some deeper causes are anchored in the British classical liberal tradition, which, despite periods of socialist experiments, was always present in Britain.<sup>15</sup> It has engrained the following principles of the British

<sup>15</sup>For a profound and detailed presentation of the Brexit arguments, see the film "Brexit: The Movie" (<https://mises.org/blog/brexit-movie-makes-economic-case-against-eu>) and Smith (2016).

mindset, which drove support for Brexit (Bökenkamp and Hesse 2016; Wirtz 2017): (1) free markets, (2) localism (i.e. policy-makers should be as close to citizens as possible) and (3) small government. In fact, according to one pollster, the second principle was the chief motive for “Leave” voters, both Tory and Labour (Ashcroft 2016).

As Bökenkamp and Hesse (2016) showed, all British prime ministers since the UK’s accession to the European Economic Community (EEC) in 1973, irrespective of party affiliation, have viewed the EEC or EU not as an end in itself but as a means to enhance prosperity, freedom and democracy. Accordingly, free trade among member states *and* with the rest of the world is viewed as the heart of European integration, and the national states as its main actors. This implies subsidiarity, decentralisation and flexibility to accommodate the diversity of EU members. In contrast, for politicians in continental Europe, including former European Commission President Jacques Delors, the common market is a means to create a European federal state, and therefore, they advocate centralisation, harmonisation and regulation of the common market (Geddes 2013). Ludwig Erhard (e.g. 1957/1964) and Wilhelm Röpke (1959) were sympathetic to the British vision of Europe, while they heavily criticised the French view. So Britain would actually be Germany’s most natural partner if it wanted to promote a profound ordoliberal reform path for the EU.

## 4.6 Conclusions

In the 1950s, Wilhelm Röpke anxiously argued against integration trajectories towards centralisation and harmonisation in Europe. He warned that such processes, instead of boosting economic growth and bringing people together, would prove to be an “explosive and an instrument of disintegration” (Röpke 1955, p. 96; similarly in Röpke [1959, §88]). Roughly 60 years later, the exit of the UK, the rise of Euro-sceptic movements and parties in many member countries and the infringement procedures against Poland are alarming indications in support of Röpke’s warnings. So Europe is at a crossroads.

From the ordoliberal perspective, the way out of the current crises is not more unification, centralisation and harmonisation, but a flexible Europe of different clubs based on a free and open single market following the motto “those who will and can”. This would best ensure competition as a disempowering and discovery procedure and at the same time account for Europe’s heterogeneity. There are two rather spontaneous forces that might set the course in this direction contrary to the intentions of the European Commission and pro-ever-closer-union political elites. First, insurmountable collective action problems in an entity with 27 heterogeneous member states make it impossible to agree on further steps towards an ever closer union. Second, persistently slow growth resulting from the EU’s institutional sclerosis exhausts its resources and leaves no other option than to “do less but more efficiently” and so to reinforce subsidiarity and rely on economic and institutional competition.

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