

Realizing a New Social Market Economy in Europe in the Coming Years



Otto Hieronymi

*The Union shall work for the sustainable development of Europe based on balanced economic growth, a **social market economy**, highly competitive and aiming at full employment and social progress, and with a high level of protection and improvement of the quality of the environment. . . It shall combat social exclusion and discrimination and shall promote social justice and protection. . . It shall promote economic, social and territorial cohesion, and solidarity among Member States. . .*

(“Article 3: The Union’s Objectives”, Draft Constitutional Treaty, in Norman, Peter (2003): *The Accidental Constitution. The Story of the European Convention*, EuroComment, Brussels, pp. 352–353, emphasis added)

Abstract Powerful centrifugal forces of nationalism and protectionism are currently threatening the economic, social, and political achievements of Europe and the Western community, undermining the prospects for sustained growth, employment, productivity and social progress. They could reinforce rather than reverse the fateful trend of growing inequality of income and wealth within and among nations. The shortcomings of globalisation, such as the excessive role of volatile short-term finance, make it difficult to benefit from its advantages. Among the large spectrum of different models of market economy implemented in Europe since the 1940s, the “social market economy” has been by far the most successful in both economic and societal terms. Today many elements of the social market economy are incorporated in the tradition and policy “rulebooks” not only in Germany, its country of origin, but also in numerous other European countries, and the European Union itself. There have been two major distinct trends with respect to the model of the social market economy: (1) the original version developed and implemented by Ludwig Erhard that put the emphasis on growth and social progress, and (2) the one promoted by the “Ordo-liberals” with their emphasis on austerity and market fundamentalism. The

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conclusion of this chapter is that the European Union and its member countries should work together to develop a new social market economy for the years to come inspired by the original first version of the social market economy with emphasis on growth and social progress.

1 Introduction

The renewing of the economic and societal models at the national, European Western, and universal levels represents the most important challenge for theory and political practice in the years ahead. The subject of the 30th Mondragone International Seminar was highly topical because of the continued crisis and uncertainty in the world economy, the current confusion in economic and social theory and policy, the political tensions in Europe and in the United States and last but not least because of the unprecedented centrifugal forces in the Western Community. Thus, the present author argues that the time is ripe for creating a new economic and societal model that will be based on the original principles of the social market economy.

This chapter is divided into four main sections: (1) success and failure of economic and societal models and theories and the search for a new consensus in economic theories and policies; (2) the main features of the original model of the “social market economy”; (3) two trends and the main aspects of the “social market economy” currently relevant for Europe, the Western Community and the world economy; (4) the conditions for building a social market economy for the twenty first century.

2 The Success and Failure of Economic and Social Theories and Policies and the Search for a New Consensus

The achievements of Europe, the United States and Japan—the Western Community as a whole—have proven to be much more solid and far reaching than it was expected or hoped for at the start in the second half of the 1940s. These achievements were spectacular in each of the three principal convergent areas: politics and political order, the economy, and the domestic and collective security of each of the member countries.¹

The transformation and changes have been probably the most profound and most visible in Europe. A decisive break with some of the most pernicious traditions of the

¹See Hieronymi, Otto, Bensky, Daniela and Stoyanova, Teofana (2008): “Quale Ordine Politico Interno e Internazionale Futuro per l’Europe et per il Mondo?” in: *La Politica, Festival della Modernità, Spirali*, Milano, pp. 101–147.

European nations, which had brought decades and centuries of war and suffering to themselves and to the rest of the world, was and remains the single most important feature of this new reality.

2.1 *The Competing Models and Schools of Economic and Social Order*

The following were the main competing schools and models actually implemented at various times in Western European countries since the late 1940s: (1) the welfare state; (2) Keynesianism; (3) indicative planning; (4) monetarism; (5) post 1970s neo-liberalism (to be distinguished from the original concept of neo-liberalism that had been part of the theory of the social market economy) and (6) the social market economy.²

All six models were essentially variations of the market economy, with different degrees and types of government controls and responsibilities. Under all six systems governments play an active role—this was also true for monetarism, neo-liberalism and the social market economy and not only for the first three approaches listed above.

²From the literature on the social market economy see the following examples: Hieronymi, Otto (2002): “Wilhelm Röpke, the Social Market Economy and Today’s Domestic and International Order”, in Otto Hieronymi, Chiara Jasson and Alexandra Roversi, Editors: *Colloque Wilhelm Röpke (1899–1966), The Relevance of His Teaching Today: Globalization and the Social Market Economy*, HEI-Webster University, Cahiers HEL, Geneva; Hieronymi, Otto (2005): “The “Social Market Economy” and Globalisation: The Lessons from the European Model for Latin America”, in Emilio Fontela Montes and Joaquín Guzmán Cueva (Eds): *Brasil y la Economía Social de Mercado*, Cuadernos del Grupo de Alcantara, pp. 247–300; Hieronymi, Otto and Lo Cascio, Martino, Editors (2016): *A New Social Market Economy for the 21st Century* Emilio Fontela: Economist and Global Researcher, ARACNE Editrice, Roma; Lenel, Hans Otto and Others, (Editors) (1997): *Soziale Marktwirtschaft, Anspruch und Wirklichkeit Seit Fünfzig Jahren*, ORDO, Jahrbuch für die Ordnung von Wirtschaft und Gesellschaft, Band 48, Lucius and Lucius, Stuttgart; Müller-Armack, Alfred (1946, 1990): *Wirtschaftslenkung und Marktwirtschaft*, Kastell Verlag, München; Müller-Armack, Alfred (1949): *Diagnose unserer Gegenwart*, C. Bertelsmann Verlag, Gütersloh; Müller-Armack, Alfred (1971): *Auf dem Weg nach Europa, Erinnerungen und Ausblicke*, Gemeinschaftsverlag Rainer Wunderlich, Tübingen und C.E. Poeschel, Stuttgart; Müller-Armack, Alfred (1974): *Genealogie der Sozialen Marktwirtschaft, Frühschriften und weiterführende Konzepte*, Verlag Paul Haupt, Bern; Posluschny, Myra (2006): *Walter Eucken und Alfred Müller-Armack: Ein Vergleich ihrer Konzeptionen des Ordoliberalismus und der Sozialen Marktwirtschaft*, GRIN Verlag GmbH, Norderstedt; Röpke, Wilhelm (1950): *Mass and Mitte*, Eugen Rentsch Verlag, Erlenbach-Zürich; Röpke, Wilhelm (1951): “Austerity”, reprinted in Röpke Wilhelm (1962): *Wirrnis und Wahrheit*, Eugen Rentsch, Erlenbach-Zürich; Röpke, Wilhelm (1958): *Ein Jahrzehnt Sozialer Marktwirtschaft in Deutschland und Seine Lehre*, Verlag für Politik und Wirtschaft, Köln-Marienburg; Schlecht, Otto (1990): *Grundlagen und Perspektiven der Sozialen Marktwirtschaft*, J.C.B. Mohr (Paul Siebeck), Tübingen; Wünsche, Horst Friedrich (2015): *Ludwig Erhards Soziale Marktwirtschaft—Wissenschaftliche Grundlagen und politische Fehldeutungen*, Lau Verlag, Reineck, München.

An important objective of the “common policies” at the European and the universal levels has been to influence or even shape the national models and policies. There is no doubt, however, that the “national models” have played an important role, and continue to play also today in shaping rules and policies at the European and global levels.

2.2 The Three Levels of Economic and Societal Order and Policies: National, European and Global

Since the second half of the 1940s three levels of rules and policy-making structures and models have been shaping the economic and monetary development of the European countries: (1) their own national “economic and societal” models; (2) the rules and structures developed in the process of European integration and the European Union in particular; (3) the “global economy” and the universal rules and institutions of “globalization”.

The various aspects of these three levels have been at times conflicting and at times converging. Much of the academic and policy debate turns around the relative importance of each of these levels (and their respective hierarchy) and how the three levels can and should be adapted in order to better achieve national and global objectives.

The principal objective of the international economic and monetary organizations and of their rules and decisions was to create a favourable *international* economic order that would serve the interests of all member countries. The broad features as well as some of the specific details of this new international economic and monetary order had been defined in a complex dual process: political negotiations and inspiration from economic theory, new and classical.

In recent years level 2 (European Union) and level 3 (globalization) have received a growing emphasis, increasingly at the expense of level 1 (national model and policy-making). Although the autonomy of national economic and monetary policy making has been systematically diminishing ever since the end of World War II in all market economies—and not only in small countries but also in the large leading ones like the United States, Japan or Germany—the national models and the quality of national policies remain crucial in the positive or negative results at the national and global levels.

2.3 Internalization and Integration

The adoption of detailed, binding international rules on economic and monetary policy was one of the main innovations of the post-1945 international order. This trend, which started with the League of Nations, gained momentum with the

planning and the implementation of the so-called Bretton Woods institutions. Its scope and importance greatly increased with the Marshall Plan institutions (OEEC and EPU) and subsequently with the start and progress of European integration.³

The emphasis on rules related to international economic relations—trade and currencies—was based on the collapse of the international economic and monetary order in the 1930s and its disastrous economic and political consequences. Also, theories, concepts and policies related to international economics played a central role in designing the international economic and monetary organizations and their rules.

At the same time it was also evident that the state of the international economy was closely related to the conditions of the national economies, the national policies and the basic economic models adopted by the various countries. The fact that there is a close link between international economic and monetary policies and national economic “models” was one an assumption shared at by the architects of virtually all of the major international economic organizations. By and large this assumption has been proven correct over many years of practice.

The objectives, scopes and rules and functioning of the international economic organizations have evolved over time partly because of changing conditions in the national and world economy, and partly because of changing theories and policy objectives.

In this process international economic and monetary organizations have tried time and again, with greater or lesser success to influence and even bring about major changes in the “economic model” of their member countries.

2.4 The Main Features and the Crisis of Globalization

Globalization represents the broadening, deepening and widening of trends that had started in the post-war period. It is the continuation of a trend towards a gradual opening of national economies to competition from abroad. Thus, international economic relations and competition in general are the primary elements of the concept. Globalization, however, also has an important domestic dimension both in terms of the role of states and the functioning of markets.

³The thinkers who were responsible for the concept of the social market economy also played an important role in the development of the post-war liberal international economic order. This was especially true for Wilhelm Röpke and the other members of the so-called “Geneva school”. See: Hieronymi, O. (Ed.). (1982). *International order – A view from Geneva.*, Geneva: IUHEL. Graduate Institute of International Relations; Hieronymi, O. (Ed.). (1987). *Technology and international relations.* London: Macmillan; Hieronymi, O., Bensky, D., & Stoyanova, T. (2008). *Quale Ordine Politico Interno e Internazionale Futuro per l’Europe et per il Mondo?* In *La Politica, Festival della Modernità* (pp. 101–147). Milano: Spirali; Slobodian, Q. (2018): *The Globalists, the End of Empire and the Birth of Neoliberalism*, Harvard University Press, Cambridge, Mass.

Two major factors gave a strong boost to this phenomenon: (1) the changes that led to the renewed emphasis on markets, private initiative and limiting the economic role of the state in the 1970s and 1980s, first in the United Kingdom and then in the United States, followed by the large majority of the OECD countries and parts of the developing world and (2) the collapse of the system of planned economy in the Soviet Union and its European satellites.

The principal aspects of globalization include the following:

1. Liberalization of markets (including labour markets) and in particular of international trade, as well as of payments and services (the liberalization of the movement of people—migration—across borders receives less emphasis).
2. Deregulation, i.e. the reduction or elimination of government regulations for individual sectors, products, etc. For many it also means reducing or even eliminating legislation to enforce competition.
3. Privatization and the withdrawal of government from all “economic activities”. This also means the replacement of traditional “public services” by profit-motivated private companies.
4. The prohibition of all forms of government subsidies and “industrial policies”.
5. Prohibition of government intervention in foreign exchange or financial markets.
6. A systematic effort to reduce “social expenses” and the rights of organized labour.

The greatest challenge for economists and even more for policy makers is: how to deal with the current important shortcomings of globalization⁴ without destroying its undeniable positive features and the lasting stimulus for economic growth and well-being that result from international economic integration.⁵

Among the main concerns about globalization one can mention there is a need for correcting and rebalancing the various features and objectives of globalization (de-emphasizing the primacy of global finance,⁶ correcting the prevailing “short-

⁴See Chapter 1 on “From ‘Global Finance’ to the Crisis of Globalization” in Hieronymi, Otto, Editor (2009b): *Globalization and the Reform of the International Banking and Monetary System*, Palgrave, Basingstoke, pp. 1–69 and Hieronymi, Otto (1998): “Agenda for a New Monetary Reform”, in *Futures*, Vol. 30, No.8, pp. 769–781, Pergamon, Elsevier Science Ltd.

⁵“The first decades after World War II were marked by an expansion of free trade. This process was until the break in 1973/74, especially in Europe through in Europe associated with a massive expansion of the welfare state. The stabilization of incomes by social benefits facilitated the descent from economic protectionism and, combined with the general increase in wealth, reduced the resistance against the change of economic and social structures. Against these tendencies to civilize capitalism towards a decidedly social market economy, there have been strong counter-movements since the 1980s, especially in the United States . . . and in the United Kingdom. Ritter, Gerhard A. (2010), *Der Sozialstaat. Entstehung und Entwicklung im internationalen Vergleich*, Dritte, erweiterte Auflage, R. Oldenbourg Verlag, München p. 255.

⁶“The growing recognition in recent years of the shortcomings of the orthodoxy prevailing until 2008 by some their most vocal exponents and practitioners especially in central banks has been a major positive development. This radical shift of perception can be illustrated by the case of Martin Wolf, Chief Economics Commentator of the Financial Times.” in Hieronymi, Otto (2016): “The

termism” and bringing back a more balanced approach to solidarity and competition), and the need to redefine the scope of government responsibilities vs. the market. Under globalization the scope of national government economic policies has become more and more restrained by explicit international agreements and by the interpretation of what is and what is not compatible with a properly functioning market economy. This rule and its implementation are at the heart of the perception of how “globalization” functions or ought to function. It is, of course, one of the principal sources of criticism of globalization: both from the side of “market fundamentalists” and from the enemies of the market economy.⁷

3 The Main Features of the Original Model of the Social Market Economy

The social market economy is a “rule-based” system, where the quality of both the laws and official decisions and of the institutions plays an important role for the economy as well as for the society as a whole. It has been widely recognized that “the European model of a Social Market Economy has been able to deliver high levels of prosperity, growth and social cohesion for the past 60 years in Western Europe and in many other countries in the world. For a long time, the Western world, and particularly the European Union, has been seen as a success story.”⁸

The concept of the social market economy originated in Germany and played an essential role in the success of the post-war reconstruction of the German economy and society based on the principles of freedom and solidarity, democracy and respect for human rights. At the start the concept was far from uncontested. In the long run the social market economy also played an important role in the orientation of European integration. Ludwig Erhard was not only the “father of the social market economy (and of the Germany economic miracle) but also had a major role in the orientation of the efforts towards of European integration along liberal lines towards

Crisis of International Finance, the Eurozone and Economic Growth”, in Rossi, Stefania A. and Malavasi, Roberto, Editors (2016): *Financial Crisis, Bank Behaviour and Credit Crunch*, Springer, New York, pp. 14–15.

⁷George Soros, one of the most famous and successful financial speculators of our time showed considerable contrition in the light of the near-meltdown of the world economy as a result of the 2008 crisis: “The prevailing paradigm cannot explain what is happening. The case for abandoning the prevailing paradigm is even stronger: The belief that markets tend towards equilibrium is directly responsible for the current turmoil; it encourages the regulators to abandon their responsibility and to rely on the market mechanism to correct its own excesses.” Soros, George (2008): *The New Paradigm for Financial Markets. The Credit Crisis of 2008 and What it Means*, Public Affairs, New York, p. 102.

⁸In European People’s Party (2009): *The Social Market Economy in a globalised World*, Congress Document adopted by the EPP Statutory Congress Bonn, 9–10 December 2009.

a common market, rather than on the model of government control and cartel agreements that was the blueprint of the European Coal and Steel Community.⁹

The main features of the original model of the Social market economy can be summed up in the following ten points:

1. The social market economy is a liberal economic and societal model—it is superior to the state-controlled models (socialism) both in terms of economic efficiency and political freedom.
2. However, the social market economy also requires appropriate government policies and in particular effective social policies.¹⁰
3. Thus, the 19th (Manchester) model as well as the ultraliberal (“libertarian”) approach advocated in the latter part of the 20th century was rejected by both the original authors and practitioners of the social market economy.
4. Competition is an important dimension of the market economy. However, “social Darwinism” is rejected in the original model of the social market economy. Social policies have multiple objectives: to support the losers in the competitive process, encourage political acceptance of the market mechanism and fulfil common tasks that cannot be dealt with through private initiative (“public service”).
5. The price mechanism is an essential part of the market economy. One of the tasks of government policies is to assure the appropriate working of the price system and to handle necessary price controls and price interventions in the least intrusive way.
6. The social market economy is not only an economic but also a political and societal model. One of its most important features is the recognition that there has to be an informed and open debate about the division of tasks between governments and markets and the private economy. The encouragement of small and medium-sized enterprises is necessary for political and economic reasons.
7. Monetary stability is a key condition for the success of the social market economy. Inflation is perceived as a threat to both economic efficiency and social stability. Also, sound fiscal policies are important both for political and economic reasons. Systematic “austerity policies” are however the sign of a failure of government policies and lead to a dangerous “vicious circle” of stagnating or falling living standards and pressures on output and productivity.
8. The overall objectives of the social market economy are sustained growth and social and economic progress for all. All should benefit from expanding output:

⁹See Müller-Armack, Alfred (1971): *Auf dem Weg nach Europa, Erinnerungen und Ausblicke*, Gemeinschaftsverlag Rainer Wunderlich, Tübingen und C.E. Poeschel, Stuttgart.

¹⁰By the beginning of the twenty first century, when the liberal market economy had triumphed beyond all previous hopes, points (1) and (2) were among the key elements of the social market economy that came to be most systematically forgotten and denied in our globalized world and world economy. Hieronymi, Otto (2002): “Wilhelm Röpke, the Social Market Economy and Today’s Domestic and International order” in Otto Hieronymi, Chiara Jasson, Alexandra Roversi (editors): *Colloque Wilhelm Röpke: The Relevance of His Teaching Today*. HEI-Webster University, Geneva, p. 11.

a constant widening in income and wealth among the few and the lower classes is fundamentally wrong and is a sign of the malfunctioning of the market economy. The “proletarianization” of large portions of the population (today’s “marginalization”) contributed to the rise of communism and national-socialism. The social market economy was designed to avoid repetition of similar developments.

9. The social market economy is open to the world and exports and imports increase both the welfare of the community and the efficiency of the national economy. However, cut-throat competition is not any more acceptable in foreign trade than it is among domestic companies.
10. European and global economic integration are welcome but there is a danger in excessive bureaucratization of international organizations. National policy-makers need sufficient room for responsible policies that take into account the specific conditions they have to deal with. The importance of local conditions and of autonomy has to be recognized within a federalist framework.

The validity of the basic concept of the social market economy is not limited to Europe and even less to the German speaking countries on the Continent. The international recognition of the theory and practice of the social market economy compared with Keynesianism can be illustrated with a quote from the famous British economist and biographer of Keynes Lord Skidelsky: “Those who value the market as an institution must be concerned to keep its support system in good repair. The state’s role is essentially threefold: (a) to create and maintain an appropriate legal framework for market exchange; (b) to limit and supplement the market where necessary; and (c) to ensure that the market is politically acceptable. A social market economy is, above all, one which is embedded in social arrangements regarded as “fair”. . . The German model had the great advantage of concentrating attention on the legal, social, and technical conditions required to make a market economy work well. Such clarity was never achieved in Britain, where old-fashioned capitalism, socialism, the Welfare State, and Keynesian macroeconomics were wrapped in an ill-assorted package labelled the ‘mixed economy’. The consensus which sustained this mixture proved to be highly vulnerable, because it concealed a basic ambivalence about the justification of markets, and indeed about the private enterprise system itself.”¹¹

¹¹Skidelsky, Robert (1989): *The Social Market Economy*, Social Market Foundation Ltd., Paper no. 1, London, pp. 3 and 6.

4 Two Trends and the Main Currently Relevant Aspects of the Social Market Economy

The overall conclusion of the present chapter is that the experience of the post-war model of the social market economy provides the best starting point in the search for a new common economic and societal model for the European and Western countries as a whole. However, over the years one could observe a growing rigidity in the academic interpretation of the theory and practice of the social market economy. Both the critics and the defenders of the social market economy have tended to reduce the concept to the so-called “ORDO liberalism” and the “Freiburg school”.

The issues on which this narrowing of the focus of the social market economy has been particularly evident included the “social dimension”, the role of the State and the international dimension. Another issue was the issue of “bigness” and the concentration of private economic power, this time not through cartels, but through mergers and acquisitions (buying out the competition in the name of “greater efficiency”).”

The three names most closely associated with the theory and implementation of the social market economy were Ludwig Erhard, for many years the Minister of Economy in the cabinet of Chancellor Konrad Adenauer, and subsequently the second chancellor of the Federal Republic, Professor Wilhelm Röpke an economist and philosopher who had escaped from Hitler’s Germany and lived in exile in Geneva, and Alfred Müller-Armack, for many years the closest collaborator of Erhard in the Ministry of Economy. Incidentally, Müller-Armack is generally credited with having coined the term “social market economy”.

4.1 *A Flexible, Rule-Based Order*

The social market economy is a rule-based system. Yet, in many respects it has proven to be more flexible and adaptable than some of the competing models.

The principal areas where the lessons of the social market economy may prove to be particularly helpful today and in the future include the following: (1) finding the balance in the division of tasks between private initiative and markets and government responsibilities; (2) balance between competition and social justice and support; (3) dealing with monopolies and the abuse of economic power; (4) balance between diversity and convergence; (5) stimulating sustained growth and social progress¹²; and (6) balance between national models and rules and European and global institutions and structures.

¹²“The democratic welfare state is not the finished product of history in the last 150 years. Much more, like the parallel phenomena of the nation state, the constitutional state and the constitutional state, it is necessarily unfinished. Its survival will depend on its ability to adapt to the changing economy, society and politics and to withstand the tension between freedom and social security.

The theory of the social market economy does not lend itself to the kind of definitions and presentations that gave such a powerful boost to the word-wide triumph of Keynesianism in academic and policy circles after the death of the master.

One of the major strengths of the social market economy is the linking of different levels of economic and social policy and the “macro” and the “micro” levels of the economy. For a didactic approach this is a handicap as is the lack of the analytical tools developed in the form of the aggregates of the national accounts based on Keynesian theory. (Richard Stone, an eminent disciple of Keynes, played an important role in this crucial development).

4.2 The Original and the ORDO Version of the Social Market Economy

One can distinguish two main currents at the level of both theory and practical implementation:

1. The first and original and most important version is the one associated with the names of Erhard, Röpke¹³ and Müller-Armack. It was also the one that corresponded to the actual policies implemented by Erhard. This version puts a greater emphasis on economic growth combined with social progress and helping the “losers” in the competitive market process. Röpke and Erhard both insisted that the social market economy represented a clear break with 19th century liberalism and laissez-faire. Also, it is important to mention that under this heading economic growth and social progress were more important than “austerity”: “Erhard did not seek to implement a theoretical ideal of a market economy, but pursued a successful policy that upheld the values of human dignity and personal autonomy. He carried out this mission and declared that the freedom of modern economic activity and social security require a material well-being in which all can share. He stated time and again that the basic objectives and foundations of a liberal policy are: prosperity for all (Wohlstand für Alle), full employment, performance-based pay, price stability and stable and sustained economic development.”¹⁴
2. The second current is linked to the so-called “ORDO-Liberalism”. The principal names to remember here are Friedrich Hayek (who rejected the very word

Ritter, Gerhard A. (2010), *Der Sozialstaat. Entstehung und Entwicklung im internationalen Vergleich*, Dritte, erweiterte Auflage, R. Oldenbourg Verlag, München p. 220” (1989 edition).

¹³In many respects the earliest and most influential book for the subsequent development of the model of the social market economy was the first volume of his famous trilogy written by Wilhelm Röpke (1942) under the title *Die Gesellschaftskrisis der Gegenwart. Der Dritte Weg* (The Societal Crisis of Our Time. The Third Way) Eugen Rentsch Verlag, Erlenbach-Zürich.

¹⁴Wünsche, Horst Friedrich (2015): *Ludwig Erhards Soziale Marktwirtschaft – Wissenschaftlich Grundlagen und politische Fehldeutungen*, Lau Verlag, Reineck, München p. 338.

“social”), Ludwig von Mises, Walther Eucken and their disciples. The ultra-liberals who gained ground since the governments of Mrs. Thatcher in Britain and of Ronald Reagan in the United States, and who basically reject the concept of the social market economy belong to the followers of Hayek and von Mises.

One can find many aspects of this concept in the rules incorporated into the framework and functioning not only of the German or Swiss Governments, but most importantly also of the European Union. There are elements in the EU “rule-book” and practice that reflect the first version, others are more directly inspired by the second ones. These aspects include the belief in the virtue of “austerity” and rigid respect of “rules” versus policies. It should be emphasized at this point that the version of the social market economy that most people outside Germany have come to experience is this second version.

When referring to the “original concept of the social market economy” in the framework of the present article, it is the concepts respectively the policies developed by Röpke, Erhard and Müller-Armack that we have in mind.

While there have been important common features in the thinking of Walter Eucken on the one hand and Röpke, Erhard, and Müller-Armack, on the other hand, the latter three did not belong to the Freiburg School or the *Ordo* tradition.¹⁵ They were all “economic liberals” in the sense that they recognized the necessity of building and maintaining market economy with a properly working price system and private property and economic freedom. At the same time, one of the common traits of their thinking was the rejection of the ultra-liberal 19th century version of capitalism.

5 Conditions for Building A New Social Market Economy

Europe and the Western Community as a whole face the most severe crisis since the 1950s. The tsunami-like centrifugal forces are threatening to tear apart the European and Western Communities and are undermining the very foundations of the highly successful post-war liberal and democratic international economic and political order.

¹⁵According to a recent comparison of Müller-Armack’s and Eucken’s theories: “Eucken’s *ordoliberalism* and the social market economy of Müller-Armack are by no means the same two interchangeable concepts for one and the same theory. Rather, it is about two separate models. . . Müller-Armack argues that Eucken does not sufficiently consider social and sociological problems . . . According to Müller-Armack, the market economy requires additions in two directions. On the one hand through social policy, which brings the ethical values of social justice and social security. . . , and on the other by a societal policy that integrates fundamental common values (including individual freedom) that make competition and the market economy politically acceptable.” Posluschny, Myra (2006): *Walter Eucken und Alfred Müller-Armack: Ein Vergleich ihrer Konzeptionen des Ordoliberalismus und der Sozialen Marktwirtschaft*, GRIN Verlag GmbH, Norderstedt.

A common feature of these problems and the solutions being sought is that they all have to do one way or another with the responsibilities (and power) and policies of governments (and of their international tools, i.e. international organizations and international law) and with human freedom, security and prosperity (and with the threats to economic prosperity and to social justice and progress).

The “solution” or rather the “solutions” at most levels require a combination of innovation and reparation and confirmation of what is working and the replacement of what is not working (or is outright harmful), rather than a sweeping series of revolutions. What we need is a firm but balanced approach that may have to include the necessary dose of trial and error: one may call it “radical centrism”.

This requires reducing the relative weight of short-term financial decisions in the economy; correcting the “austerity-inspired” approach to fiscal balance and the debt problem; bolstering and reforming the international monetary system of which the euro and the dollar will remain the main pillars; improving the respect of social standards in the so-called developing world; combating the rise of nationalism and political extremism; strengthening solidarity between and within national economies.¹⁶

5.1 *Austerity Is Not the Solution*

The principal conditions for the building a new social market economy in Europe and in the Western Community include economic, political and ethical issues at the micro, macro and global levels.

As stated previously it is in the original concept of the social market economy that emphasized “prosperity for all” rather than “austerity” (without trying make a carbon copy that would be contrary to its very spirit and would ignore the changed circumstances) that we can find inspiration in the search for a new balanced economic and societal order. Part of the conclusions of the author is that many of

¹⁶Following the collapse of the communist regimes in 1989–1990 in Eastern Europe, the logical choice for the model for reconstruction and regime change would have been the social market economy. Yet, the only leader to have chosen this path was Prime Minister Jozsef Antall of Hungary. His government received no encouragement whatsoever from their foreign partners (including the Federal Republic of Germany) the major international organizations. See: Hieronymi, O. (1990). A ‘Grand Design’ for Balanced Growth, *International Economic Integration and the Development of a Modern Social Market Economy in Hungary*. In O. Hieronymi (Ed.), *Economic policies for the new Hungary* (pp. 10–18). Columbus, OH: Battelle Press ; Hieronymi, O. (2001). *Du Communisme à l’Economie du Marché Sociale. Du Socialisme à l’Economie de Marché*, sous la direction d’Andras November, *Nouveaux Cahiers de l’IUUD*, No. 12, Genève; Hieronymi, O. (July 2013). *Regime Change in Hungary, 1990–1994, the Economic Policies of the Antall Government*, *Hungarian Review*, Budapest, pp. 36–47; Hieronymi, O. (1996). *International capital markets and the financial integration of the transition countries*. Unpublished Manuscript; Hieronymi, O. (2000). *The main features and the current relevance of the European Model of the Social Market Economy*. Unpublished manuscript.

the current interpretations of the concept and the tradition of the social market economy are more harmful than useful in pursuing this objective.¹⁷

The first condition is to redefine the fundamental principles and goals of the future economic and societal model: sustained economic growth together with social progress and the protection of the environment; the full use of current and future human resources; free and liberal economy without the recent excesses of ultraliberal ideology; reversing the growing inequality within and between the national economies; a new concept of competition at the national and internal levels; balance between the responsibilities of government and the private sector; a new federalism that will allow an efficient interaction between the national, the European and the global levels.

It is important to recognize and redefine the link between market efficiency and equity and social justice. Under this heading the single most important task is to reverse the pernicious trend of income and wealth concentration in fewer and fewer hands. This is certainly not a call for replacing the market economy with socialism which not only failed everywhere in terms of economic efficiency and wealth creation: it was also a failure in terms of creating sound social policies.

There is a need both to strengthen and to modernize social policies.¹⁸ Well-designed and well-implemented social policies are among the principal sources of an efficient and dynamic economy. They contribute to the development of a healthy, well-trained work force and stimulate entrepreneurship across all social groups and classes. Importantly, they are also an essential condition for people to accept and adjust to change and not see them as an existential threats for themselves and for their children.

The philosophy and practice of the social market economy were among the factors that made competition and the risks of being on the loser side (at least temporarily) politically acceptable to the so-called working classes. The concept and practice of “labour peace” (*Arbeitsfrieden*, *la paix du travail*) did not mean the absence of potential tensions and disagreements between employers and unions. It provided them, however, with a shared view that employers and owners, on the one hand, and wage earners, on the other hand, had a common interest in efficiency and growth. Thus, it was also an important factor in raising productivity and in job creation.

The key developments that have marked the evolution of the national economies and of the European and world economies in recent decades, and are likely to have a

¹⁷The mistaking of austerity for stability can be the principal obstacle to economic growth, the solution of the debt problem and the realization of a successful social market economy, See: Hieronymi, O., & Stephanou (Eds.). (2013). *International debt – Economic, financial, monetary, political and regulatory aspects*. Basingstoke: Palgrave; Blyth, M. (2013). *Austerity. The history of a dangerous idea*. Oxford: Oxford University Press.

¹⁸In the strategy for growth adopted by the European Union the social dimension plays an important role. The Pillar of Social Rights is about delivering new and more effective rights for citizens. It builds upon 20 key principles, structured around three categories: (1) Equal opportunities and access to the labour market (2) Fair working conditions and (3) Social protection and inclusion.

continued role in the policy debate and practice, include globalization, information-related technological change, the relentless widening of the gap between the “successful” and the “less successful or outright losers” and the excessive weight of short-term finance on the real economy. These developments, directly or indirectly, have contributed to the ideology that “social policies” that aim to ease the burden of the consequences of these trends should not be considered as “anti-market”, “unnecessary costs”, but rather, if well designed and implemented as “necessary costs”, cost that are indispensable for sustained growth and for the proper functioning of a liberal (social) market economy.

5.2 The European Union, Subsidiarity and Solidarity

Today there is a tendency to visualize the economic and social policy debate and conflicts within the European Union as the result of unbridgeable differences between the traditions of the “South” and the “North” as if economic policies were the results of geographic and ethnic factors. This approach is confusing and misleading in many respects. Its adoption and spreading to the highest levels of decision-makers (not to mention real or pseudo scholars) can have severe consequences. Although many German politicians and economists believe that the “social market economy” is not an “export product”, this is an expression of intellectual nationalism. Helping to build a successful “social market economy” across Europe—with the emphasis on growth and social progress, rather than on just “discipline” and austerity—is also the interest of Germany.

One of the challenges of our time is to find a balanced approach between (1) common policies, at the European and global levels and (2) policies that take into account local and national policies. This is a requirement not only in Italy but also in Germany or France: “subsidiarity” is a central feature of this model which does or should allow keeping important policy functions and responsibilities at the national and provincial levels, including the fiscal domain. This is well illustrated by importance of the German “Länder” and of the Swiss “Cantons” in shaping in particular a local competitive business friendly environment (the famous “Rahmenbedingungen”)

5.3 GDP Is Not Enough: The Importance of Qualitative Growth

The quality of life and the need to respect the humane dimension of technology, industrial production, and economic activity in general, have been among the important aspects of the concept of the social market economy developed by Wilhelm Röpke as early as the 1940s and 1950s. At the time—just as today—this

was considered to be non-conventional economics that could be ignored by policy makers according to both Keynesians in the 1950s and 1960s and ardent monetarists and market fundamentalists in later years. However, Röpke's ideas remain highly relevant also for the new version of the social market economy to be implemented in the twenty-first century. (See Hieronymi 1987; Röpke 1942, 1950.)

In the 1980s the Swiss government created a working group on “qualitative growth” in order to give more substance to the issue of managing the environment in its legislative program. One of the problems raised in the working group was the difficulty to compare the by then traditional measures of GDP and its components with the natural-science based indicators used in the discussions on the protection of the environment. The group recognized the problem lack of an effective cost-benefit approach to deal with environmental quality and the benefits of environmental protection that would be as transparent and easy to deal with as the Keynes-Stone national account system. Today this is still a major problem both for analysis and policy alternatives and for public debate in general. Yet, mainstream economists and environmentalists have been slow to recognize the need to find a solution for this problem.

The truth of the statement “GDP is not enough” has been only gradually accepted. The current search for finding an adequate solution can be illustrated by the work carried out in the framework of the OECD under the awkward-sounding title “advancing research on well-being metrics beyond GDP”. (The three most famous names associated with this on-going work are Joseph E. Stiglitz, Amartya Sen and Jean-Paul Fitoussi). The latest report (November 2018) recognizes the importance of the search for new “quantitative-qualitative” tools that are robust and user-friendly: “There is no simple way of representing every aspect of well-being in a single number in the way GDP describes market economic output. . . We need to move beyond ‘GDP’. . . Different metrics. . . could have shown that the consequences of the recession (2008–2010) were much deeper than GDP statistics indicated, and governments might have responded more strongly to mitigate the negative impacts of the crisis.”¹⁹

5.4 The Euro and International Monetary Order

For many years important elements of the social market economy have been present in European economic and social policy making. They have thus contributed to the unprecedented achievements of the European countries in terms of living standards and social standards. The importance of the framework and tradition of the social market economy has been more systematically recognized by political leaders than

¹⁹OECD (2018), *Beyond GDP: Measuring what counts for economic and social performance*, OECD Publishing, Paris—<https://doi.org/10.1787/9789264307292-en>

by the economics profession. This was true both at the national level and the level of the European Union.

Upholding the euro is an essential condition for the successful implementation of the social market economy at the European level. This was demonstrated by the European Central Bank and its President Draghi who had the courage to go beyond the narrowly defined initial (Bundesbank-inspired) mandate of the ECB. Chancellor Helmut Kohl was probably the most important advocate and architect of the European Monetary Union (EMU). He also belonged to those who implicitly or explicitly followed the Erhard, Müller-Armack, Röpke tradition of a social market economy open towards the world.

On both accounts he differed significantly from the negative Bundesbank-ORDO view of European integration and the common currency: “Within the framework of consensus and co-operation Kohl found himself operating with two loose but discernible coalitions of actors in constructing a negotiating strategy for EMU (European Monetary Union)—which can be characterized as the ‘security’ coalition and the ordo-liberal coalition. . . What united the security coalition was the belief that EMU was centrally about binding Germany into Europe. EMU was perceived as at the heart an historic and political issue of making European unification irreversible. . . The Bundesbank’s. . . officials harboured a deep-seated caution about entering and discharging external commitments like the EMU.”²⁰ Today the importance of the euro for the success (and even survival) of the European project, and hence of the social market economy, is recognized by some American economists who in the past tended to belong in the camp of the euro-sceptics.²¹

For many years the present writer has argued that the “euro is not enough” and that one of its greatest shortcomings was that it by-passed the issue of the absence of a stable rule-based Western or global international monetary system: “One of the principal conditions to assure the long-term development and success of the liberal international economic and political order is the return to a stable, equitable and rule-based international monetary order.”²²

In an earlier article (the first version of which had been published in Japanese) I argued in favour of an “expanded EMS: “The goal is not that the United States and Japan should ‘join’ the EMS or the European Monetary Union as such, but that they should negotiate with the European Union a monetary system that will have similar objectives and similar rules to those of the original EMS.”²³

²⁰Dyson, Kenneth and Featherstone, Kevin (1999): *The Road to Maastricht, Negotiating Economic and Monetary Union*, Oxford University Press, Oxford, pp. 261–262.

²¹“This book has shown that the euro can be saved, should be saved in a way that creates the shared prosperity and solidarity that was part of the promise of the euro.” Stiglitz, Joseph E. (2018): *The Euro. How a Common Currency Threatens the Future of Europe. With a New Section on Brexit*, W.W. Norton & Co., New York, p. 325.

²²Hieronymi, Otto (October 2009a): “Rebuilding the International Monetary Order: the Responsibility of Europe, Japan and the United States”, *Revista de Economia Mundial*, Madrid, No. 29, pp. 197–226, p. 197.

²³Hieronymi, Otto (1995) “The Case for an ‘Extended EMS’: A New International Monetary Order to be Built by Europe, Japan and the United States”, in SZABO-PELSOECZY, Miklos (Editor):

A similar preoccupation with international monetary instability was expressed by the Japanese central banker Toyoo Gyothen, although, in good Japanese fashion he stopped short of suggesting that Japan should take the initiative towards a new system: “. . . Japan, even more than the United States, needs a system of multilateral rules rather than ad hoc, bilateral negotiations under mutual threats and accusations.”²⁴ It is paradoxical that several decades later it is an economist associated with the ultra-libertarian Cato Institute who comes to suggest that President Trump, the proven enemy of all forms of multilateral cooperation should take the initiative to create a new rule-based international monetary system.²⁵

6 Conclusion

This chapter on a new social market economy for the twenty first century, may be concluded with a reference to an article written in 1978 ago on the occasion of the 50th anniversary of the Marshall Plan and of the start of European integration. The article called for a new approach to domestic and international monetary reform for the following main reasons: (1) the increasingly dogmatic character of dominant monetary and financial theories and policies; (2) we are in uncharted waters: the world has changed profoundly since the 1970s (3) the deflationary bias of the dominant doctrine and the danger of a protectionist-interventionist backlash. (See Hieronymi 1998)

The article did not offer set solutions for all these issues. Its conclusion was, however, that without such a debate and a consensus on a balanced new approach, there was a real threat of a backlash, the threat of losing the advantages of liberalization and globalization, and of a return to increased monetary and economic nationalism²⁶ and excessive government intervention and control. Unfortunately some of this analysis has proven to be correct.

Since then we have seen the 2008 world financial and monetary crisis, BREXIT, Boris Johnson and President Trump and their attempts to destroy the post-war international order through protectionism, xenophobia and nationalism, Viktor Orban whose illiberal democracy aims at undermining the values and traditions of the free world. All this, however, should not serve as an excuse for pessimism and

The Global Monetary System After the Fall of the Soviet Empire, (In Memoriam Robert Triffin—1911–1993, Sixth Conference of the Robert Triffin-Szirák Foundation, Szirák, 1993), Averbury, Aldershot, 1995, p. 63.

²⁴Toyoo Gyothen in Volcker, Paul and Gyothen, Toyoo (1992) *Changing Fortunes: The World's Money and the Threat to American Leadership*, Times Books, New York, 1992, p. 66.

²⁵“We have not had a rule-based international monetary system since President Nixon ended the Bretton Woods Agreement in August 1991. Today there are compelling reasons—political, economic and strategic—for President Trump to initiate a new international monetary system.” Shelton, Judy (2018): “The Case for a New International Monetary System”, in Dorn, James A., Editor (2018): *Monetary Policy in an Uncertain World. Ten Years After the Crisis*. Cato Institute, Washington, DC, p. 291.

²⁶On the nature and risks of economic and monetary nationalism see Hieronymi (1980).

inaction about building a new social market economy in the years ahead in Europe and across the Western Community. The enemies of the liberal domestic and international order are far from having earned a final victory. We should rather remember and seek inspiration in the lessons of how the world had been saved by democracy, the courage and hard work of previous generations and how the corrupt and authoritarian regimes built by earlier strong men have disintegrated under their own injustice and intolerance. (On democracy and peace see Huntley 1980, 2001, 2006.)

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