

# The Magic of Economic and Social Development

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Decent Work and Economic Growth remain crucial factors for the future of mankind. In the recent catalogue of the UN Sustainable Development Goals (SDGs), they rank 8th; however, they also represent crucial prerequisites for the first four SDGs which are:

- (1) No Poverty,
- (2) Zero Hunger,
- (3) Good Health and
- (4) Well-Being and Quality Education.

Therefore, sustainable economic development is highly appreciated not only among entrepreneurs and citizens but also among electorates and governments all

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over the world. It makes voters happy thereby increasing their approval of politicians.

Unfortunately, however, sustainable economic development is difficult to attain—especially if the country starts from a position of poverty, illiteracy, violent conflict or destruction. Few countries have made it successfully through these changes (most prominently Asian economies like Singapore, South Korea, China being among them)—while many others sooner or later fail or progress very slowly. For example, countries such as Argentina and parts of Brazil could not convert temporary prosperity—resulting from the export of natural resources—into permanent wealth and flourishing. Instead, they lost their global income position if their main markets dried up or the products lost their position in an international value chain.

Before that background, the history of the Federal Republic of Germany after 1950 is even more remarkable. Today, the country regularly ranks amongst the most respected, politically stable, economically consolidated. For seven decades now, West Germany (after 1990: united Germany) has benefited from a well-organised socio-economic system. Gross domestic product (GDP)—although it is certainly not a perfect indicator of the quality of life in a country—nevertheless represents an important indicator of long-term socio-economic performance. After the founding of the West German state in 1949, the national product rose continuously. Starting from around 50 billion € in 1950, 526 billion € were reached in 1974 and 3043 billion € in 2015. Since 1950, there have only been two exceptions in this uninterrupted history of growth: the financial crisis in 2009 and the Covid-19-year 2020. In 2019 Germany, with a population of 82 million people, produced the fifth-largest GDP in the world—behind much larger countries such as the USA (more than four times the German population), China (about 15 times) and Japan (about 1.5 times the German population).

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## **Germany Around 1950: An Unlikely Candidate for Economic Growth and Development**

But what many people are no longer aware of today is that predicting this development 70 years ago would have been a risky bet. To understand this better, let us take a moment to look back at the country's situation in 1949. After 12 years (1933–1945) of the totalitarian, criminal and aggressive Nazi dictatorship, Germany was literally in ruins at the end of the Second World War. Not only had 80% of German cities been destroyed including most of the transportation infrastructure and some industrial sites. Moreover, also the social and cultural life had been devastated, which was probably even more disastrous. The country had waged an aggressive war against most of its European neighbours. It had deprived them of their sovereignty, occupied and maltreated them, bringing a tremendous amount of death and destruction also to thousands of innocent civilians. Enormous war crimes were committed especially in Poland and Russia, where millions of captured

soldiers and civilians were killed. Most seriously, however, was the systematic and continuous factory-style killing of more than 6 million Jewish people (and other minorities like Sinti and Roma) in the gas-chambers of annihilation camps like Auschwitz-Birkenau, Treblinka, Sobibor, etc. People of all ages from the old to the baby were killed systematically and without mercy: The so-called ‘Holocaust’ represents one of the most infamous and unbelievable crimes against humanity in history. It was committed by the German people and in the name of Germany; it will be forever connected to the history of the country.

As a consequence of these most infamous and disastrous misdeeds, the country of the perpetrators remained an outcast on the European continent for years. Moreover, aggression and brutality had also turned against German people themselves: Over 8 million citizens had lost their lives as soldiers—but also as civilians, when British and American bombers turned German cities into a blazing sea of flames. Subsequently, when the Eastern parts of the country were incorporated into the Polish territory, more than 3 million German refugees had to flee their homes. Those who survived the hardships flooded into mostly destroyed German cities or overcrowded rural areas—with little more than what they wore on their bodies. After 1945, the remaining German territory was divided into four occupation zones—with the three Western ones (administered by the US, English and French army) later becoming the ‘Federal Republic of Germany’ while the Eastern one (occupied by the Russian army) came under communist rule and later turned into the ‘German Democratic Republic’.

From an economic point of view, these developments strangled the free flow of goods among the different parts cutting deeply into the traditional trade structure of the county. Moreover, during the disastrous winter of hunger in 1946/47 alone more than 400 000 Germans starved to death, died of frost, hunger-related diseases or took their lives out of sheer despair. Now, what would an unbiased observer expect for the economic future of such a country? Not very much, I suppose.

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## **Explanation of the Economic Miracle: The Role of Institutions**

Given the manifest contradiction between the negative point of departure and the most stable further development during recent decades: What may have been the reasons for this amazing development?

- Much is attributed to the fact that after the series of existential crises from 1914 to 1949 the German people were desperately longing for improvement of their material situation. After the ‘zero hour’ of the late 1940s—it is said—things could only get better. As seen above, however, many people around the world are desperately longing for such an improvement of their living conditions; but only very few of them are ultimately successful in attaining it. Wishful thinking

alone does not create reality. Many countries get stuck in dilemmas and crises—sometimes for decades, generations or even centuries.

- Another popular argument focuses on the ‘nature’ of German people, who are assumed to be disciplined, hard-working, and well-coordinated: Character traits that supposedly qualify them to build up a successful economy. From a more comprehensive analysis of the country’s history, however, we do not find a lot of success stories that would qualify for proofing this ‘German nature’. Since the start of modern times, the semi-independent German states were rather beaten with economic and political backwardness—constantly lacking behind their European neighbours in the West. Moreover, even during the 20th century, the period of the so-called ‘Weimar Republic’ (1919–1933) was characterized by extreme political and economic instability. Dominated by industry cartels and omnipresent economic power structures, few entrepreneurial activities could actually blossom during that time. Rather, unemployment rates were constantly high—and soared after the financial crisis of 1929.

Moreover, even contrary to the stunning success of Western Germany, painful stagnation of living conditions prevailed in the neighbouring Socialist ‘German Democratic Republic’. In order to prevent their own population from fleeing the country in large numbers to the Federal Republic, Eastern German authorities built the Berlin wall and fortified the inner-German border. Finally, the GDR collapsed in 1989/1990 also because East Germans were desperately longing to leave the self-proclaimed ‘workers’ and farmers’ paradise’ in order to settle down in the West. Thus, as history proves, ‘German nature’ (whatever that fuzzy concept actually means) is not a probable candidate for explaining the country’s sustainable economic growth.

- Finally, there are voices stressing the importance of economic aid from the American allies. In order to strengthen ‘their’ administrative zones in the competition against the communist East, the US pumped millions of dollars into the embryonal business structure of Western Germany. Moreover, the US Government convinced France and Britain to limit German reparation payments and industrial dismantling until 1951 and favoured the foundation of a common European market. Of course, US investment certainly supported German development; for example, loans for start-up companies were granted on good terms from these funds on an ongoing basis. However, comparable positive conditions were granted to other European countries as well—with much less favourable consequences.

No doubt, several factors contributed to the economic success Western Germany experienced after the total disaster of the first half of the 20th century. However, those factors are far from even partially explaining it. Rather, during the 1950s economic and social institutions emerged (the so-called ‘Social Market Economy’) which organized the economy in line with the dominant value traditions of the country. In other words, during these years, Germany embarked on a path of socio-economic development, which reflected some deep-rooted social capital neglected in earlier periods.

## **Social Market Economy: Realizing the Potential of Private Entrepreneurship**

Much has already been written about the (West-) German social and economic system of the Social Market Economy since its emergence after WW II.<sup>1</sup> The model ultimately dates back to the concepts of economists and social scientist from the so-called Ordoliberal Freiburg school—including scientists like Walter Eucken, Franz Böhm, Wilhelm Röpke and others. Already during the Weimar Republic, they had fought against the overwhelming concentration of private power and the omnipresent cartels in the German economy. These included for example the famous ‘Rhine barons’ of the steel and coal industry, the ‘IG Farben’ consortium—representing the highly cartelized chemical industry—as well as the media mogul Alfred Hugenberg, whose ultraconservative party ended up supporting the disastrous National Socialist party. During the infamous racist and totalitarian Nazi dictatorship (1933–1945), economists like Röpke had to flee Germany while others like Eucken and Böhm nurtured an opposition spirit at the University of Freiburg and—in the middle of terror, genocide, massive destruction and notorious war crimes—worked on developing plans for an alternative post-WW II German Economy.

The ideas of these thinkers substantially circled around the challenge of how to prevent the return of economic power structures, branch cartels, etc., which would (again) oppress private competition, dictate prices and prevent progress. As reflective economic policy masterminds, the architects of the social market economy naturally also differed from one another. One important common denominator of their thought, however, was putting the private, personally liable entrepreneur at the centre of economic and policy concepts. The first conservative-liberal West-German Government under Chancellor Konrad Adenauer and his minister of economics Ludwig Erhard (1949–1963) especially focused on the ‘Mittelstand’ (small and medium-sized enterprises, SMEs), which became a cornerstone of their economic and social policies. In sharp contrast to the German Democratic Republic (1949–1990), where private ownership of production was subsequently abolished and economic processes became part of a socialist political agenda, West German economic policies concentrated on creating an adequate socio-economic environment for the private founder-entrepreneur. In particular, it is these founders, who drive economic and social development, create economic value in a region and ultimately promote technical and organizational progress. More precisely, they hire employees, build up

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<sup>1</sup>Compare, for example the following publications: Muresan, S. S. (2014): *Social Market Economy. The Case of Germany*. Heidelberg-New York Springer. Hasse, R. H., Schneider, H., Weigelt, K. (Ed.). (2008): *Social Market Economy. History, Principles and Implementation – from A to Z*. Konrad Adenauer Foundation: Johannesburg (ZA). Koslowski, P. (Ed.) (1998): *The Social Market Economy. Theory and Ethics of the Economic order*. Heidelberg-Berlin: Springer. Nicholls, A. J. (1994): *Freedom with Responsibility. The Social Market Economy in Germany 1918–1963*. Oxford: Clarence House. Hartrich, E. (1980): *The Fourth and Richest Reich. How the Germans conquered the Postwar World*. New York: Macmillan Publishing.

production processes and offer their products and services on competitive markets—thereby always shouldering the economic liability for a potential failure.

Consequently, if the social market economy is first and foremost about private entrepreneurs and entrepreneurial activity, the Government—but also business associations and unions, chambers, the educational sector, communal and regional administrations—should support and nurture them. Consequently, economic policy in the context of the social market economy is supposed to become SME policy (*‘Mittelstandspolitik’*) in the sense of supporting the foundation and growth of small and medium-sized (*‘Mittelstand’*) companies. Moreover, according to the concept of *‘subsidiarity’* derived from Christian social ethics, this was executed respecting the autonomy and co-responsibility of local and regional administrations. Consequently, SME policies were executed

- (a) on the national level: secure property rights, stable currency, efficient infrastructure, transparent and moderate taxation, appropriate social and health policies, labour law;
- (b) on the federal state (*‘Bundesländer’*) level: educational system, traffic and housing infrastructure, cultural policies;
- (c) on the regional governmental level: factory inspection, trade supervision, regional planning, etc.

The spirit of the Social Market Economy ultimately aimed at improving the financial, infrastructural, organizational, educational, social and cultural conditions for the emergence of entrepreneurial activities. Hence, private entrepreneurs and public policies should not fight against but mutually support each other—both playing their own genuine role for a prosperous community. One counterargument to that approach may pop up immediately in many readers. Why should public policy, why should social organizations support a process which ultimately results in the accumulation of wealth for some private entrepreneurs and their families? Should the national and regional government not rather focus primarily on the poor and disadvantaged individuals and improve *their* lot—for example by directly providing decent housing, food, clothes, health care, basic schooling etc. to them? In post WW II Germany, the poverty and abject misery of millions of needy, impoverished and disparately poor persons was as obvious as it is in many poor countries today. From a social market economy perspective, however, the government can never permanently guarantee the financial support and social integration of millions of poor people in a sustainable way. Rather, from a systematic point of view, the poor can ultimately only make a living themselves: above all by offering work—at least as long as social and economic conditions allow that to happen. Consequently, it is primarily the role of the private entrepreneur to organize and offer that work: by providing goods and services to clients and hire workers for that purpose. Neither government nor other public institutions should prevent (or try to substitute!) private Entrepreneurs from playing that essential role. Rather, the public should concentrate on empowering, supporting and controlling the social and economic activities of competing entrepreneurs—thereby making sure that their

companies comply with the common rules of the market competition. In particular, employers must honour the human rights and personal freedom of their workers, pay their salaries in due time, guarantee healthy working conditions, assist them in increasing their professional proficiency and career etc. They must uphold employees' freedom of organisation, as expressed, for example, in the formation of trade unions (workplace co-determination plays an important role in the German economy, dating back to the early 1920s; freedom of association is enshrined in the constitution). The public duty to create an adequate framework ('Ordnungsrahmen'), which supports but also controls private companies, determines the genuine role of political actors in the Social Market Economy—on the different levels of local, federal state and national Government.

Now, if the Social Market Economy is indeed preliminary about setting the stage for independent founder entrepreneurs: What exactly are the most important policy instruments for that purpose? Traditionally, economists focus on macroeconomic conditions, for example legal guarantees of property rights, decent tax and social security requirements, lower barriers to entry and the prevention of currency friction improving trust. These are indeed crucial institutional factors. However, if we focus more precisely on the necessities of founder-entrepreneurs, we perceive that the factors mentioned above are necessary but not sufficient. Rather beyond a reasonable stable macroeconomic environment, founder-entrepreneurs are primarily in need of two factors:

- (a) easy access to local capital as well as
- (b) regional professional education.

Correspondingly, in the context of the Social Market Economy, specific regional institutions have evolved for both aspects, which particularly promoted the generation and growth of small and medium-sized institutions: regional savings and cooperative banks as well as chambers of commerce based professional education. From a systemic point of view, both represent important intermediary elements, which—each in its own way—correspond with the 'public good' character of service provision for SMEs.

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## **The Role of Intermediary Regional Institutions for Development**

Start-up capital is generally provided by private investors. Hence, from an economic point of view, it clearly represents a private and not a public good. However, banks generally tend to avoid risks and therefore primarily lend money to clients, who are already wealthy and can provide back-up securities in exchange. Consequently, bankers are often reluctant to finance start-up entrepreneurs, which would require a relatively high risk of losing investment capital. Therefore, in the context

of the Social Market Economy, politicians favoured the emergence of regional capital markets in the form of savings or cooperative banks.

Savings banks (“Sparkassen”) developed in Germany at the beginning of the 19th century—mostly in cities or even rural areas as district saving banks.<sup>2</sup> Most of them were developed as communal sponsorship; moreover, during the 1930s, regional building societies (‘Landesbausparkassen’) emerged for the financing of local construction activities. Only after WW II, however, were savings banks able to assume their main economic role as investors into regional SMEs. Primarily, they were required to finance large parts of the necessary (re-) construction activities in German cities during the 1950s and 1960s. Beyond the positive economic development, however, technical change of payment transactions became crucial. More precisely, after 1957 cashless payment of wages and salaries was gradually introduced—promoting the integration of German employee households into the banking sector. Consequently, with the institution of the ‘current account’ at the savings bank (Sparkasse), large sections of the German population became “bankable” for the first time—thereby boosting the capabilities of saving banks to grant loans. Moreover, during the 1960s, the West German savings banks fostered the blossoming saving culture—by introducing many new products and services. Examples include the acquisition loan (1960), the cheque card and the savings bank letter (1967), the overdraft facility (1968) and the savings bank obligation (1970). In 1967, the liberalization of the banking industry even fostered competition among local banks: during the 1970s, they started to install ATMs and account statement printers, which can be used supra-regionally since 1996. In contemporary Germany, the savings banks are still market leaders in small and medium-sized corporate customer business, 63% of the SMEs do business with these public-sector banks.<sup>3</sup>

But then, where is the public good element? Saving banks emerged on a regional basis: thus, they are generally owned by the municipality or local government. Therefore, their main purpose is not to maximize profits for their owners but to sustainably support the economic development of the region. Similarly, cooperative banks basically represent local (mutual) credit associations, which are also eager to support promising local business activities. Still today, if you ask a German founder-entrepreneur for an important moment in the history of his or her venture, many of them tell you with lucid eyes, how the CEO of the local savings or cooperative bank became the first person to share the dream and invest into their—at that stage still rather modest—economic endeavour. Therefore, even if it is not emphasized in economics textbooks, Germany’s widespread system of local and regional banks represented a crucial success factor for the economic development of post-WW II Germany. Most of the founder-entrepreneurs would have never been successful, if it had meant queuing up in private banks in economic centres like Duesseldorf, Stuttgart, Frankfurt or Munich; rather a self-reliant local banking

<sup>2</sup>I owe this historical information to the DGSV website: <https://www.dsgv.de/content/dam/dsgv-de/der-verband/downloads/Geschichte-SFG-DSGV.pdf> (7.1.2021).

<sup>3</sup>Data from finance magazine 09/16 citing a study of Greenwich Associates <https://www.finance-magazin.de/banking-berater/banking/firmenkundengeschaeft-deutsche-bank-verliert-im-mittelstand-1385331/> (7.1.2021).



organization existed for them, which was not only open for their projects but rather welcomed them as (potential) promoters of regional economic development. Complementarily, successful founder-entrepreneurs often serve as members on the Supervisory Board of their local bank later on, thereby continuously infusing their SME spirit in its organizational and service behaviour. Moreover, this system brought forward a generation of local bank directors and financial decision makers, who perceive themselves not primarily as anonymous capital market investors; rather they serve ‘their’ start-ups as benevolent and ‘practically wise’ consultants: to promote their business success—and of course to also secure the repayment of their loans.

In this context, the traditional federal structure of the German countries also plays an important role. During the feudal period of the ‘Holy Roman Empire of German Nation’ a ‘patchwork carpet’ of very heterogenous kingdoms, chiefdoms, church-ruled principalities, free cities etc. had emerged. After the Reformation, confessional conflicts between Catholic and Protestant territories opposed the process of national unification in Western European neighbour countries, where powerful national centres emerged much earlier. When the medieval Empire finally dissolved, some regional authorities even became independent heads of states: they found themselves a unified German National Territory only as late as 1871.

Until today, a practical consequence of Germany’s ‘delayed statehood’ (H. Plessner) is the polymorphous structure of the country. In sharp contrast to dominating political and economic centres like Paris or London, Berlin—originally the capital of Prussia—could never play a comparative integrative role. The violent oppression of federal structures during the centrist and totalitarian Hitler dictatorship (1933–1945) fortunately remained a short episode. With the founding of the Federal Republic of Germany in 1949, the country consciously returned to the traditional pluri-centricity of political and economic structures—expressed also in the name of the young state. Subsequently, it was precisely this federal structure that effectively favoured the emergence of local financial markets and independent savings banks/cooperative banks in each region.

### **... and professional training**

A second essential for the emergence of small and medium-sized Enterprises is a qualified work force, which requires sound professional education of workers at low cost. Consequently, professional education infrastructure plays a comparably important role for economic growth and social development of the German ‘Social Market Economy’:

- First and foremost, education creates a future generation of competent founder-entrepreneurs, who can challenge incumbent firms and existing technology with new products, business models and value chains;
- Moreover, education brings about and constantly regenerates the production skills of qualified workers.

In a nutshell, professional education—unfortunately often ignored in economic analysis—represents a crucial ingredient of sustainable socio-economic development. Modern differentiated education systems with comprehensive compulsory education, elementary schools as well as flexible forms of secondary education—did not emerge until the 19th century. This also applies to the German vocational school system, which began at the end of the 19th century but only underwent important reforms and modifications in the second half of the 20th century. However, strong traditions of vocational training, including its formative and character-building elements, are rooted much deeper in German history. Already in the medieval cities, guilds played an important role as public associations of craftsmen, merchants and other professional groups vis-à-vis the nobility, the clergy and the rest of the people. The guilds, which came into being as early as the 13th century, were structured according to specific professions (bakers, butchers, butchers, etc.) and organised themselves hierarchically, with the guild master being elected by the free craftsmen-entrepreneurs in their assembly. The guild was not an open association, but membership was compulsory for all craftsmen of a particular guild in the city. The city guilds in particular determined the number of free craftsmen's organisations admitted there. In addition, they supervised the process of succession and drew up regulations in this regard. They also set prices as well as quality standards for their goods—and served as a contact point for customers who felt cheated by a guild member. Finally, it was the guild that established and enforced basic rules for the in-service training of young people—whereby apprentices were taken in and successively integrated into the highly organised social life of the guild. After a few years of service, apprentices then received the journeyman's certificate, which was officially issued by the political authorities. In addition, they could continue to obtain the master craftsman's certificate and eventually found their own craft organisation—if they could raise the financial means or married the widowed wife of a deceased owner.

Involvement in the guilds played a decisive role in the entire lifestyle and private networks of the craftsmen and their families—from birth to the grave. Only in the early modern period did the medieval guilds gradually lose their integrative role. Finally, in the course of the liberal reforms of the early 19th century, they were completely eliminated as intermediary organisations. More precisely, the compulsory membership of a craftsman or merchant in a guild was finally abolished when freedom of occupation was proclaimed as a result of the French Revolution. Now every free citizen was considered to be endowed with the right to be self-employed—regardless of the need to join a particular professional group or to abide by its rules. Even though the guilds lost their public character during this period, the social and cultural capital they had accumulated over centuries remained influential. This was especially true for the need to determine the standards of and to set a guideline for vocational training.

In this tradition, chambers of commerce were founded in Germany in the 18th and 19th centuries, inspired by French precursors—in the sense of a self-governing body representing and organising the interests of business. More precisely, the first German chamber emerged in the western city of Elberfeld and Barmen, the centre

of (textile) industrialisation in 1830. Precursors such as the medieval guilds or the “Assembly of Respectable Merchants in Hamburg” (1519) are vaguely reminiscent of this organisation. On closer inspection, however, they show few similarities with the social functions and basic rules of a modern chamber. In particular, voluntary membership in the chamber initially prevailed for business people—according to the liberal mainstream of the early age of industrialisation. For example, when the Prussian government decided to regulate the Elberfeld Chamber barely 20 years after its foundation, membership still remained voluntary.

This only changed after the Second World War—and even then rather surprisingly. During the centralistic Nazi dictatorship, the chambers had been misused for totalitarian infiltration and increasing government control of the economy. Consequently, American and British occupation authorities rejected professional associations and even vetoed plans to introduce compulsory membership in chambers directly after the war. After 1949, important political leaders of the young Federal Republic remained undecided (K. Adenauer) or even voted against compulsory membership (L. Ehrhard). Nevertheless, it was introduced in 1956 by the federal government—formed exclusively by the Christian Democratic Union during this legislative period. As a result, the chambers became “professional corporations under public law”. In this intermediary role as “public representation of the interests of industry”, they indeed played a decisive role in the continuous growth of the German industry described above—including its overwhelming success in international markets during the following decades. The main reason lies in their crucial importance for the German system of vocational training, the so-called dual system.

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## The Dilemma of Professional Education

Professional education is generally organized either in public or private responsibility. In the context of exclusively public professional school systems, government agencies organize courses and hire their own teaching staff for that purpose. Consequently, educational plans and course descriptions are developed *detached* from ongoing professional practice in companies. As a result, public professional education loses touch with the changing necessities of day-to-day operational procedures in the corporate sector. Vocational profiles in purely state schools quickly become outdated. Furthermore, public teachers usually rely on methods, subjects, tools, etc., that they have learned during their own training. This results in a lack of knowledge about technological progress or changing business models. It follows that training courses delivered only by public sector teachers often lack practical relevance and are of limited value to the rapidly evolving business environment. Therefore, young people graduating from such a public school system may not be the most attractive candidates for private companies as long as they lack relevant operational experience. However, their contact with the labour market, in terms of concrete contacts with potential employers, is limited. As a result, the transition from the education sector to the labour market can be rather difficult for

young people. Moreover, candidates who eventually find employment may find that their experience in the ‘sheltered sector’ of public schools has not adequately prepared them for the difficult day-to-day challenges of corporate reality.

On the other hand, elements of general knowledge (e.g. in mathematics, physics, languages, basic technical knowledge, etc.) are rarely taught in exclusively private sector (company-based) training systems. Furthermore, in-company training programmes often lack a comprehensive list of competencies that a trainee is supposed to acquire or of subject areas that he/she is supposed to pass through. Since there is usually only limited supervision of the programme, students run the risk that the quality of the training will fall victim to the demands of day-to-day business.

Moreover, the company as a (potential) trainer faces a difficult dilemma. If it invests a lot of time and money in training some people, it runs the risk that they will later leave to work for a competitor. Other companies may decide to avoid the expense of vocational training and instead poach trained employees from their competitors. As a result, we often find situations of the “prisoner’s dilemma” type of game theory in private vocational training. In a given region the business sector as a whole may clearly benefit from well-developed vocational training structures. The individual company, however, will not invest in them unless it is guaranteed that relevant competitors will contribute to the costs of the training programmes. Since every company ultimately follows the same strategy of “making the others pay”, in the end there are collectively few resources available for educational training: This is exactly what describes the current situation in many countries around the world.

How can this ‘Professional Education Dilemma’ be overcome? As known from game theory literature, this is far from easy. Even if the call for more professional training is widespread and its necessity is generally acknowledged, little is going to be achieved in that respect. In the absence of adequate corporate engagement, however, candidates find themselves either clamped as cheap auxiliary labour without much formative relevance; or their training follows very closely the respective systems, production technologies and cultural standards of their training company—thereby preventing them from easily switching to a competitor. Young people who have been poorly trained during their apprenticeship, however, end up facing a high unemployment risk in their future professional life.

As seen above, the regulations for vocational training move between the “Scylla” of an exclusively public system and the “Charybdis” of an exclusively private system. The latter lacks an ongoing motivation and stream of resources while the former remains void of the up-to-date knowledge and competence to continuously adapt professional training schemes. Thus, from a game theory perspective, competing companies clearly find themselves in a prisoner’s dilemma, which prevents market solutions to emerge. Complementarily, professional training as part of the public education system lacks relevant market information to perform.

## The Dual VET System in Germany

Against this background, the ‘dual system’ of vocational education and training (VET)—as it gradually emerged in Germany—represents an institutionalized cooperation between public and private actors: it may be called a particular type of public-private partnership. In its current form, its mostly tri-annual educational programs combine periods of practical training (executed in the training company) with elements of ongoing schooling (executed in the public professional schools). The two elements are traditionally combined on a weekly basis (with 3 days a week working in the training company and 2 days a week in the professional school). Alternatively, they can also be combined on a monthly or yearly basis according to the necessities of the production or learning process. Most importantly, the structure and contents of both elements—public school education on the one hand and company practical training on the other—are specified in fixed educational schemes, which are known upfront. This specific educational cooperation also forms the basis of the final examination—which in turn is divided into a practical and a theoretical part.

Within the dual VET system, however, private companies do not only serve as places for vocational training; rather, representatives of the business sector are also in the driver’s seat through the chamber system and contribute to the emergence of new professions. So while some training courses still follow more traditional lines (for craftsmen such as bakers, cooks, carpenters, etc.), others have emerged only recently—following proposals from companies and discussions with public sector representatives within the dual system. Thus, vocational training is regularly adapted to changing technological and organisational requirements. In cooperation with the chambers of commerce and the ministries of education (which in Germany are organised at the Länder level), the “Federal Institute for Vocational Education and Training” regularly plays an important role. For example, the Institute also monitors the numbers of trainees in a training occupation; those with less attractive offers are either modernised or closed. Furthermore, in the course of technical innovations and/or changing business models and value chains, completely new “occupations” are being added, resulting from innovative forms of company practice. For example, a new scheme for training “mechatronics engineers” was developed in the automotive industry. More recently, the training profile of an “IT salesperson” or a “social media communicator” emerged.

In this way, the dual VET system combines important aspects of practical orientation/added value for companies with a complementary element of external public supervision (see Fig. 1.1 Different VET systems). Within the dual system, the chambers serve as service providers for the companies—but not only; they are also advocates for the trainees and their training needs. As a result, it is much easier to find a job after a chamber examination than after visiting a public vocational school or even many types of university education. This is due to the fact that in-company vocational education and training already has essential characteristics of a professional job due to its dual structure (i.e. the combination of school-based and in-company training). Further advantages are the contractual and organisational

	PUBLIC SYSTEM	DUAL SYSTEM	PRIVATE SYSTEM
EDUCATION IN	STATE SCHOOL ONLY	BOTH PLACES	PRIVATE COMPANY ONLY
Practical orientation	--	++	++
Adaptive to technical change	--	++	++
Labour market attractiveness	--	++	++
Business experience	--	++	++
Labor market exposure	--	++	--
Induces professional ethos	+	++	--
Includes general knowledge	++	++	--
Program supervision	++	++	--
Comprehensive schemes	++	++	--
Industry-wide acceptance	++	++	--

Source: Prof. Dr. Andre Habisch Catholic University Eichstaett-Ingolstadt

**Fig. 1.1** Different VET systems in comparison

integration into the company as well as the protection under labour law or company contracts.

The system also offers many advantages for apprenticeship candidates. They can choose in advance from the more than 300 apprenticeship occupations currently available. To do so, they inform themselves about the occupations that interest them in the materials provided by employers and chambers. The occupations should really appeal to them and correspond to their personal preferences. However, they also learn that some apprenticeships are much more popular than others—such as car mechanic, office clerk or policeman (more popular with boys), doctor’s assistant, governess and retail saleswoman (more popular with girls). These are therefore more difficult to achieve and more competitive, while professions such as concrete builder, insurance agent or IT specialist are in high demand among employers and graduates usually earn better.

In addition, companies also differ greatly from one another. They advertise training places, so potential trainees inform themselves and choose the offers they consider most attractive. As a result, an apprenticeship at an attractive brand such as SAP or BMW may be more highly rated in the peer group than attending a secondary school or even university. Young people apply to the company they find most attractive and—if successful—sign a training contract. The duration of the training, the curriculum, the training allowance/trainee wage and holiday entitlement are usually regulated by law.

Moreover, trainees in such a system earn their own money from day one. Salaries vary from several hundred to more than a thousand euros, depending on the job description and the year of training. Earning their own money at a young age thus strengthens young people’s motivation and self-esteem. The trainees attend the vocational school to acquire general basic knowledge; the remaining time they

spend in the companies to gain insights into concrete work steps under real working conditions. Here, they are usually integrated into real professional processes. Finally, the trainees have to prove their acquired skills in an examination. At the invitation of the chamber, both entrepreneurs and teachers sit on the examination boards. After passing the examination, a generally recognised training certificate is awarded. This official document can be used for further applications, but also represents a step towards higher education studies, for example at a university of applied sciences. As a rule, however, 2/3 of apprenticeship graduates remain in their training company. Some supplement their skills with further training, others change to a different profession.

In 2020 around 500 000 young people—about half of all adolescents of school-leaving-age—will be trained in the dual VET system. More than 400 000 German companies actively offer training as an important instrument to reinforce their workforce; and more than 2/3 of them keep their trainees. As professional training is such an important investment into the future and it is more and more difficult to attract capable young people in an ageing society, training conditions are subject to continuous improvement. Many family entrepreneurs are personally active in educating and retaining apprentices. Moreover, educational profiles are continuously adapted to meet societal and professional demands.

In addition, another important feature of the dual system compared to a purely market-driven approach to VET should be mentioned. Typically, trainees in company-based programmes take learning modules that are arbitrarily selected and prescribed by the training company. Consequently, learning outcomes are not certified; graduates, therefore, find rather limited appreciation in the general labour market. In such a context, young people are merely “trained”. So-called “blue collar” jobs, therefore, suffer from a bad reputation and are often perceived as catch basins for school dropouts or poor performers. Other course graduates hop from job to job—mostly in low-paid service occupations—or they even combine 3 or 4 of them to make a living. Consequently, they never really develop a professional identity or ethos. In contrast, in the chamber-supported dual VET system, it is said that apprentices “learn a profession”. This also involves aspects of personality development, the formation of a professional identity and a corresponding ethos. Consequently, the completion of training represents a fixed component of professional identity that can serve as a formal step in the life course.

Finally, in the dual system, it is also possible to continue training for a further 2–5 years in order to obtain the master craftsman’s diploma. After passing the final examination, the dual VET systems’ formal requirements for setting up one’s own business and training apprentices are fulfilled. In the business premises of a Central European hairdresser, car repair shop, plumber, carpenter, butcher, baker, etc., the outstanding role of professional qualifications is made visible by the fact that the master craftsman’s certificate hangs on the wall. Showing it openly to every customer is a clear indication of the owner-entrepreneur’s professional identity—including a corresponding promise of good quality.

## The Dual VET System: Advantages for Sustainable Socio-Economic Development

The dual VET system thus represents an important success factor of the social market economy in Germany. In particular, the technical and professional competence of graduates of the dual system supports the high-quality standards of production processes in the German economy—and thus also success in international markets. The constant change in production technologies, in particular, requires not only innovative engineers but also well-trained, motivated and qualified skilled workers. The continuous adaptation of industrial production to changing technologies is therefore crucial for international competitiveness. Just like the electrification of cars in the past, today the digitalisation of production processes, for example, poses a major challenge. To meet this challenge, not only new machines and technical equipment must be introduced, but a different corporate culture is also required. This includes more co-responsible employees who have a high level of technical understanding as well as the ability to operate complex machines, analyse and solve difficult problems, anticipate bottlenecks, etc. The dual VET system represents a complex cooperative mechanism capable of training these types of highly skilled specialists. It is important to understand that chambers indeed play an indispensable role in this respect. Even more: without their specific structure as an organisation under public law, the dual VET system would not have been able to develop.

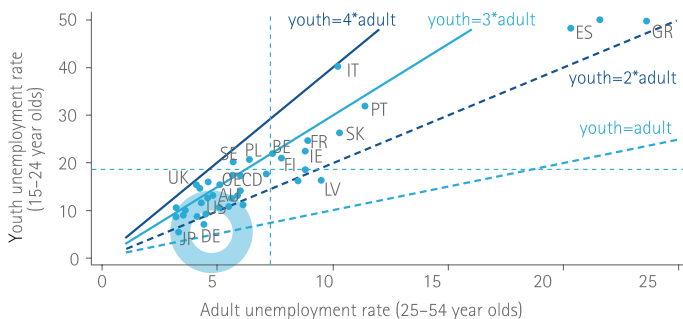
The prominent role of the dual VET system becomes particularly clear when comparing the youth unemployment rates of different countries worldwide (see Chart 1, which compares countries in this respect<sup>4</sup>). Youth unemployment is one of the most vexing obstacles to economic development, as it entails notorious skill shortages, delayed (economic and product) innovation and ultimately limited growth. At the personal level, youth unemployment is the cause of many young people's personal problems (micro-level), such as unfulfilled dreams and aspirations, the feeling of being superfluous and rejected, the loss of self-esteem and the inability to provide financially for themselves and their family. As a result, these personal problems of young people contribute significantly to social and political problems such as increased youth crime unrest and political instability, exploitation of (cheap) labour and a waste of human resources<sup>5</sup>.

Different empirical indicators prove that Germany enjoys a very advantageous position in the international ranking of youth unemployment—in the European as well as international context (see Fig. 1.2: Pastore, F. (2018)). The relative disadvantage (RD) of young people in the labour market is measuring the youth unemployment rate in relation to the general unemployment rate. Only in Germany and Japan do young people have *the same* chances of finding a job compared with adult and more experienced job seekers. On the contrary, young people's chances

<sup>4</sup>Data from OECD <https://data.oecd.org/unemp/youth-unemployment-rate.htm> (07.01.2021).

<sup>5</sup>See Aaltonen, M.; Macdonald, J.M.; Martikainen, P.; Kivijuori, J. (2013): Examining the Generality of the Unemployment-Crime Association, in: *Criminology* (51) 3, pp. 561–594.





Source: Author's own compilation based on OECD data. IZA World labor  
 Online at: <http://stats.oecd.org/>

**Fig. 1.2** Pastore, F. (2018): World-wide comparison of youth unemployment. Youth unemployment in Germany is low mainly due to dual vocational education and training

are less than half as large compared to adults in Greece and the US, approx. only a third as large in France, Belgium and the OECD mean and only about a fourth as large in the UK, Sweden and Italy<sup>6</sup> (see Pastore 2018, data for 2015).

Even more impressive is the difference, when we compare the absolute disadvantage (AD) of young people. The NEET rate measures the number of young people Not in Education, Employment or Training in relationship to the educated, employed or trained young people (according to the national education system in the age bracket of under 29-year olds). According to the EU statistical office, the total unemployment rate of young people (data from 2018 or latest available) is 6,8% in Germany, but 8,6% in the US, 11,9% in the OECD total, 12,1% in the UK, 22,3% in France, 24,8% in Italy, 38% in Spain and more than 40% in Greece. Of course, there may be multiple reasons for the relatively low youth German unemployment rates. However, it seems very plausible that the dual VET system (including the critical role of business involvement in that respect) plays an important role in that achievement.

Beyond its beneficial influence on youth unemployment, another consequence of this type of educational system is, that it substantially contributes to the success of German industrial products on international markets. If we follow the economic theory of comparative advantage in international trade relations (D. Ricardo), we would expect that countries specialize in production processes with comparative cost advantages. For example, we would expect industrial production to be moved

<sup>6</sup>Pastore, F. (2018): Why is youth unemployment so high and different across countries? IZA World of Labor 2018: 420 (doi: 10.15185/izawol.420), Data for 2015; orig. article: Pastore, F. (2015): The European Youth Guarantee: labor market context, conditions and opportunities in Italy. IZA Journal of European Labor Studies, 4 (1).

to host countries outside Europe, where salaries are much lower and production processes may be organized substantially cheaper. A shift of production processes to low-salary countries is indeed precisely what we observe for low-quality production, for example in the textile or outdoor clothing industry. Quite surprisingly, however, we do *not* perceive this trend for sophisticated technical product processes in the automotive industry, in mechanical and electrical engineering, in chemistry etc. Here, industrial companies in Germany paid an average of 34.10 euros per hour in 2017, compared with only 11.30 euros in the Czech Republic, 9.10 euros in Hungary and as little as 4.90 euros in Bulgaria. Nevertheless, 21.6% of the German automotive products, 16% of the mechanical engineering and chemistry and 15.9% of electrical engineering are exported to international markets. Overall, the German industry contributed 23.1% to the total value creation in Germany—compared to only 10% in France and 9% in the United Kingdom.<sup>7</sup>

Summing-up, even with very high labour costs in Germany, many cars, machines, chemical substances and electrical devices are still produced nationally, although companies could save substantially by shifting production to already existing factories in Eastern Europe. Here, the availability of professionally trained workers represents the crucial competitive advantage for the production of high-quality sophisticated goods. The dual VET system keeps jobs in the country even in the context of a high division of labour and strong international competition of production sites.

Another positive aspect is more culture related. The dual VET system, which is generally accepted and well established in Central Europe, opens a door for many young people to alternative career biographies beyond the general educational hierarchy of primary school—secondary school—grammar school—college—university. In many countries of the world, this prevailing educational hierarchy indeed produces a social class system, in which financial success and prestige directly depend on one's level of formal education. However, many young people cannot develop their strengths in such a system: for example, those who only develop a clear perspective for themselves later in life or those who are more practically oriented. In contrast, the dual VET system also enables skilled workers, craftsmen, medical assistants and other apprenticeships to have a better sense of self-worth, prestige and earning potential.

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## The Dual VET System—A Team Product

The institutional architecture of the dual VET system is laid down in the federal law on vocational education ('Berufsbildungsgesetz'). In general, § 76 stipulates that the so-called competent body controls the implementation of practical

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<sup>7</sup>Data from Frankfurter Allgemeine Zeitung FAZ 30.4.19, p. 17.

vocational training in the company.<sup>8</sup> The relevant chambers have been designated as the competent bodies. These include the Chambers of Industry and Commerce (IHK), the Chambers of Trades and Crafts, the Chambers of Agriculture and the Chambers of Liberal Professions such as the Medical Association. More specifically, the Chambers of Industry and Commerce (IHK), the Chambers of Trades and Crafts, the Chambers of Agriculture and the Chambers of Liberal Professions, such as the Medical Association,

- monitor vocational training (Section 76 § 1 No. BBiG),
- keep a register of training relationships into which the essential contents of each vocational training contract are to be entered (§ 34 BBiG),
- advise the persons involved in vocational training on all training issues (§ 76 BBiG),
- monitor the suitability of the training staff and the training centre (§ 32 BBiG),
- form the examination committees for the acceptance of the nationwide uniform interim and financial statement audit (§§ 48(1), 39(1) BBiG),
- issue certificates valid throughout Germany, that is skilled worker and apprenticeship certificates (§37(2) BBiG),
- accompany and support the implementation of stays abroad (§ 76).

For that purpose, chambers are obliged to set up a *vocational training committee* (Sec. 77 § 1 BBiG). It consists of six honorary representatives of the employer's organizations and six representatives of the employees (trade unions). In addition, six teachers from vocational schools participate in an advisory capacity. As a joint body, the vocational training committee must be informed and consulted on all important matters of vocational education and training (Sec. 79 § 1 BBiG).

In addition, a federal state (Bundesland) *Committee for Vocational Education and Training* is also set up by the state government (Landesregierung). This committee, too, is composed equally of representatives of the employer's organizations, the trade unions and the state authorities; half of the latter representatives have to be experts in matters relating to the school system (Sec. 82 § 1 BBiG). The State Committee has the tasks of

- advising the state government on vocational education and training issues,
- contributing to the continuous development of the quality of vocational education and training,
- guaranteeing—in the interest of a coherent VET structure—the cooperation between its company-based and school-based elements. Moreover, the committee has to ensure that vocational education and training is taken into account in the reorganisation and further development of the school system (§ 83 BBiG).

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<sup>8</sup>The information in this paragraph is taken from the comprehensive PhD thesis of Sonja Baron, *Das Duale Ausbildungssystem unter dem Einfluß der EU-Bildungspolitik. Entwicklungsprozesse und Herausforderungen*, VdM Verlag Dr. Müller, 2013.

In other words, the State Committee represents a regional joint platform for the VET players and their stakeholders at state level. In addition to their participation in the Vocational Training Committee and the Regional Committee, the social partners (trade unions and employer organizations) take on other tasks on the company level. For example, the Works Constitution Act ('Betriebsverfassungsgesetz') and the Personnel Representation Act ('Personalvertretungsgesetz') confer social partners with extensive rights of co-determination in the implementation of vocational training. For that purpose, the 'Youth and Trainee Representative Body' was set up to represent the interests of trainees under certain conditions: f.e. to monitor compliance with the applicable laws, ordinances, accident prevention regulations, collective agreements and works agreements (Sect. 60 § 1 No. 2 BetrVG). Summing up, the social partners—trade unions as well as employer associations—are also involved in curriculum development and coordination.

School-based dual VET elements are the responsibility of the respective federal states (Bundesländer). Within the framework of the Standing Conference of the Ministers of Education and Cultural Affairs of the States (KMK), the Ministers of Education and Cultural Affairs of the individual states exchange views on the organisation of vocational education and training and, if necessary, coordinate their activities. The KMK thus represents a coordinating body of the federal states. Its permanent secretariat assumes further tasks in vocational education and training. According to the information on the KMK website, these include, for example

- information on developments in the field of vocational education and training;
- development of framework curricula and coordination with training regulations;
- development of complementary offers for initial vocational training at vocational schools, coordination of offers and identification of needs;
- development of agreements on mutual recognition of diplomas and entitlements to access higher education through vocational training;
- development of additional labour market offers for higher performers, for European qualifications and for foreign languages.

Moreover, in the concert of different obligations and responsibilities for the dual VET system, the federal Institute for VET (BIBB) has to be mentioned as an important player. This is a federal institution under public law that has legal capacity and is based in Bonn (Sec. 89 BBiG). In principle, it carries out its tasks within the framework of the Federal Government's education policy. The tasks assigned to it in § 90 (2) and (3) of the BBiG include

- scientific research on vocational education and training research;
- preparation of training regulations;
- writing the annual report of the Federal Ministry of Education and Research (BMBF) and the implementation of vocational education and training statistics;
- participating in international cooperation in vocational education and training.

The President and the Board form BIBB's executive bodies. The Board is made up of equal numbers of representatives from employers, employees (trade unions), the federal states and the federal government.

Through their involvement in BIBB, *the associations and trade unions are provided with regulatory tasks that otherwise can only be performed by state institutions*. However, the overall involvement of interest organisations described above has several advantages:

- the active involvement of the social partners is intended to achieve self-commitment to the objectives or agreements;
- their expertise is used, and the state is relieved of the difficult tasks of finding compromises and building consensus;
- for that purpose, however, the government must hand over political powers to the associations and offer them incentives for cooperation.

Moreover, the broad involvement of partners in the design of the dual VET system contributes to the improvement of the quality of training. The complex system of representation in the dual VET system also guarantees nationwide uniform standards and ensures quality. Due to the distribution of responsibilities and the established control and safety systems, dual vocational training is also of high quality by European and international standards.

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## The Dual VET System: The Role of the Chambers

Summing-up, what is the Chamber's role in the dual system of vocational education and training?

- (1) As seen above, together with the Committee for Vocational Education and Training on the State level, the Chamber's Vocational Training Committees play a crucial role in the complex process of defining the dual system's educational schemes. Currently, more than 330 schemes are taught in the German VET system. In the complex process of maintaining and adapting existing programs, the chambers abolish outdated and shrinking ones and form or substantially redefine new ones—according to changing technologies or processes in the companies. Moreover, chambers play an important coordinative role; as they cooperate with business associations, unions, governmental organizations etc. in a complex network.
- (2) In this context, chambers represent and organise the multifaceted interests of the business sector. That is why their role as a public organization is so crucial. A private club or NGO could not qualify for partnering with a state government on equal footing in sovereign tasks as important as defining vocational educational schemes. Likewise, as a mere lobby group of their member firms,

chambers could not maintain the right to full representation of the business sector in that process. Rather, defining educational schemes in the public-school system represents an important function, which regularly triggers important political conflicts. Hence, the status of the chamber of commerce as a public law organization is essential for its legitimation in order to officially take part in that process.

- (3) The regional chambers cooperate with the VET Committees, the Federal Institute for Vocational Education and Training (BIBB) in order to coordinate the process of defining and adapting the dual system's educational schemes. This important maintenance and innovation process requires access to internal company information from different sectors. The chamber can legitimately execute that information transfer because it represents an elected self-administrative instrument of its member companies.
- (4) Moreover, together with the ministry of education the chambers also have to guarantee the quality of educational processes in the training companies. Chambers organize the registration of the educational contracts between companies and the apprentice's plan, organize and execute intermediate and final examinations—mostly in their own chamber buildings—, guarantee the certification of the apprenticeship diplomas, coordinate and mediate the cooperation of company members with the vocational school etc. Moreover, regular controls of apprenticeship practice take place. If gross violations are found, the chambers can even revoke the training permit.
- (5) Last but not least, the chambers also recruit the staff for the final examinations. For that purpose, entrepreneurs, managers but also employee representatives volunteer in chamber-of-commerce examination committees; in Germany, regularly several 100 000 hours of voluntary work are done here every year.

The last point especially exemplifies the mediating role of the chambers in the Social Market Economy. Obligatory membership in a chamber reminds the manager/entrepreneur to go beyond their legitimate commercial interests. In the context of the Social Market Economy, they are also supposed to keep an eye on the common good of her/his social environment. Subsequently, chambers also help to trigger, support and channel corresponding citizenship engagement of businesses. Therefore, *obligatory membership very tangibly represents entrepreneurial co-responsibility*—as an expression of 'business sustainability'. This already finds a clear expression in the governance structure of the chambers themselves—as an entrepreneur serves as the Chamber President on a voluntary basis and members volunteer their time on many time-consuming committees. Moreover, the constant engagement of chamber volunteers on the dual VET system's examination committees represents another strong expression of the underlying entrepreneurial ethos—strongly differentiating the German 'coordinated capitalism' from the British or American 'liberal capitalism'.

## **Self-administration and ‘Indirect Public Administration’: Core Elements of Social Market Economy**

### **Chambers as Instruments of Indirect Public Administration**

The Central European chamber system—similar institutions that exist in other countries such as Austria, Switzerland, parts of northern Italy and parts of France—can be seen as a prominent example of subsidiary, self-governing structures. In addition to chambers of commerce and industry, there are also other professional institutions such as chambers of crafts, chambers of doctors, dentists, pharmacists, bar associations, chambers of agriculture, etc. They all represent self-governing structures called *indirect state administration* (“mittelbare Staatsverwaltung”). This principle implies that governments—both national and state—do not always exercise their administrative function directly; rather, they control and govern indirectly through subordinate self-governing bodies, often constituted as public law corporations.

In the context of the German system of ‘Social Market Economy’ self-administrative bodies and indirect state administration play an important role. Both limits government officials to a purely supervisory and regulatory function, which is a reaction to the lessons of 20th century German history. More specifically, party-dominated and ideology-driven governments prevailed in both communist East Germany (1949–1990) and Nazi Germany (1933–1945). They systematically dictated their will and overruled “practically wise” decision-making. In the context of the social market economy, on the other hand, it is no longer up to politicians or ministerial officials to decide about many aspects of business-related, academic, medical, legal, regional or cultural issues of society. Rather, it is delegated to the organized self-administration of professionals from their respective areas. They have to decide autonomously and according to the standards, they have developed themselves. Hence, the Social Market System empowers independent and fact-/problem-based decision-making beyond mere ‘political correctness’. Thereby, also organisational and administrative continuity across changing governments is guaranteed and the scope for decision-making and participation of professional experts is opened up.

Subsidiary self-administration represents a crucial, but nevertheless hidden and even forgotten aspect of the enduring economic and cultural success of the German socio-economic system. It relies on the trustworthiness of local knowledge, cultural autonomy and sound judgement in the context of regional or professional institutions. It thereby empowers

- Problem-orientated debates searching for pragmatic solutions;
- Adaptive learning, which generates new solutions in a critical trial-and-error-process;
- Incremental innovations, which are embedded in local cultures and practices;

- ‘Practical Wisdom’ of local decision making, which is aware of its responsibility towards the common good.

On the contrary, however, there are of course also challenges connected with such an approach:

- Structural conservatism may hinder innovation, especially if it threatens the socio-economic position of local powerholders;
- Self-administration may avoid effective supervision of agreed-upon rules, especially if the latter collides with the interests of powerful groups or individuals;
- More generally, powerful families or groups may abuse self-administrative freedom for their own particular interests;
- Necessary changes may overstretch the power of self-administrative bodies.

Therefore, subsidiarity should be executed in the spirit of regulatory goals such as solidarity aid for weaker groups and individuals, respect of personal dignity and the orientation towards the common good of the region or nation. Obligatory membership of entrepreneurs in the (public) chambers—in contrast to the club model of private Chambers—clearly sets the scene for an orientation towards public goals.

In this respect, the subsidiary structures of “organised self-government” differ substantially from market exchange relationships. Chambers should certainly strive to create value for their member companies; however, they must never be perceived exclusively as pure service providers for them. Rather, as organs of self-government, they also have to *critically control* the behaviour of their member companies and check whether they actually comply with the basic professional rules. Specifically, in the area of dual VET, the chamber representatives must make sure that the factual content of company-based training actually corresponds to the defined framework given to the trainees. Furthermore, they should regularly check that the personal rights of the trainees are respected—thereby also safeguarding the reputation of the dual VET system as a whole. Preventing a member from neglecting its training mandate thus protects the long-term interests of the member company from its short-term failures. With the strong emphasis on the service function of chambers for their members in the liberal 1990s, however, this genuine compliance function of self-governing bodies was neglected—and their social role both internally and externally blurred. Thus, if self-governing bodies such as chambers are only perceived as mere lobby organisations for their members (from the outside) or as mere service providers (from the inside), central aspects of their public role are lost. Properly understood, chambers go substantially beyond the scope of their members’ short-term interests.



## Self-administration in the Labour Market, Health Care and Social Sector

An important field of application is the institutional organisation of labour relations and labour law. Here, self-government and the neutrality of the state guarantee peaceful industrial relations and an innovative dynamic of product and service development. Self-governance in industrial relations looks back on a long tradition in German history: As early as November 1918—at the end of the First World War—the Stinnes-Legien Treaty was signed, which was the first document of mutual recognition of trade unions and employers' associations and the initial document of a tradition of social partnership. Stinnes-Legien and beyond created tripartite institutions between representatives of workers/trade unions, employers' associations and the government. They subsequently played an important role in the German labour market system. For example, the Federal Employment Agency maintains a nationwide network of local employment offices. It is responsible for the payment of unemployment benefits, active labour promotion benefits, promotion of vocational training, certain types of social benefits, etc., with around 100,000 employees (2018). The Agency's Administrative Board is the central governing body of the Agency: it consists of seven volunteers representing employees/trade unions, employers and public bodies. The Governing Board supervises and advises the Executive Board, takes note of the Agency's budget and approves the annual report. In its tripartite composition, it represents the character of the Federal Agency as a self-governing body.

Subsidiarity also plays an important role in the wage-setting process in the German economy. The so-called autonomy of collective bargaining, i.e. the free negotiation of salaries of public and private sector workers employed according to statutory pay scales, is even enshrined in Article 9 of the German Basic Law. Its most important consequence is that politics should not interfere in the highly regulated process of free wage setting—for example by preventing strikes and lockouts. Rather, this process is organised and carried out autonomously by trade unions and workers' associations at the regional level—according to the legal requirements of collective bargaining law.

Moreover, on a corporate level, self-administrative elements found their way into labour relations' governance structures. Co-determination rights of the worker's council were also drafted as early as 1920—but found themselves reorganized only during the 1950s.<sup>9</sup> Subsequently, works councils could be established in every

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<sup>9</sup>The works council law was drafted as early as 1920 with active participation of Catholic social scientists like Prof. Goetz Briefs but was abolished by the Nazi Government in 1934. In 1952, the Works Council Constitution Act came into force, which, in the tradition of the Weimar Works Council Act, regulates extensive information, consultation and co-determination rights of the works council. It prescribes "trusting cooperation" between management and the works council. In addition, it also contained provisions on corporate co-determination in the supervisory board of corporations; see Teuteberg, H. J. (1961): *Geschichte der Industriellen Mitbestimmung in Deutschland. Ursprung und Entwicklung ihrer Vorläufer im Denken und in der Wirklichkeit des 19. Jahrhunderts*, Tübingen, Mohr, 1961.

company larger than five permanent employees entitled to vote. The costs of the works council's activities must be borne by the employer—including training and work leave (in companies with more than 200 employees, the shop chairmen have to be completely exempted from work). Moreover, works councils possess important co-determination rights for enforcing labour regulations or during the recruitment process. Correspondingly, if those rights are violated, the shop chairman/woman can sue the management in public labour courts: the tri-partite structure of the German labour governance institutions becomes manifest, here. Even if only about one-third of companies are effectively endowed with a works council, the mere existence of those participatory institutions plays an important role in relatively peaceful and constructive labour relations. Moreover, the institutional empowerment of workers via works councils and other institutions corresponds with the existence of strong and professional unions, which cooperate under the roof of the German Federation of Trade Unions (DGB). Consequently, professional and self-reliant union representatives in a tripartite governance structure cooperate with employer's representatives also in corporate governance committees (*Aufsichtsrat*) of the large stock listed companies.

Summing-up, German labour law does not primarily rely on detailed legal rules and regulations only; rather subsidiary structures of self-administration and autonomous conflict regulation—empowered by a system of public labour courts—play an important role. One important implication of such a subsidiary framework is that company representatives and HR departments have to develop a *cooperative leadership style*—namely in their own interest. Subsidiary social institutions subsequently trigger the emergence of a respectful corporate culture and support the consolidation of a corresponding professional ethos of leaders. For example, an HR manager who wants to climb-up the career ladder in a co-determination company will have to successfully interact with labour representatives in the works council. This of course also includes an awareness for regional consequences of corporate decisions—for example on workers and their families. Practical wisdom often prevails within committees of self-administration, because social partners—more than politicians in federal ministries—are interested in pragmatic and problem-oriented decision-making.

#### **Practical Wisdom—Innovations and Solidarity**

Practical wisdom embodied in self-administrative governance structures may also bring about important innovations. For example, during the early 2000s social partners in wage-negotiating-committees crafted a system of 'working hours accounts'. They enabled workers to 'save' overtime work hours in boom times and 'un-save' them later on or in times of economic crisis. Subsequently, the tri-partite labour governance structure mentioned above triggered a political process, in which the result of the locally developed model developed into a standard element of the German labour law system. Some years later, when the global financial crisis hit in 2008, this flexible organizational element decisively increased employer's room for manoeuvre.

For example, many SMEs kept their staff in employment even in situations, in which they had lost up to 50% of their turnover on global markets! On the empty German labour market, they knew that—once their workers had been laid-off—they would never find so experienced and dedicated specialists again. The ‘work hour accounts’ enabled them to bridge a few months paying the salaries without having any returns from international sales. Of course, when the crisis persisted during late 2008 and 2009, they also had to put their private money to work. When the crisis was finally over in 2010, however, those companies were the first to satisfy the quickly rising global demand, because they still had their staff on board. Thus, an ethos of pragmatism and solidarity (*Practical Wisdom*) nurtured in the context of self-administrative institutions had fostered the emergence of labour market structures, which helped many companies to successfully manoeuvre through the crisis. Moreover, the experience of having mastered the crisis together strongly reinforced the spirit of solidarity among entrepreneurs and employees in the German ‘Mittelstand’ for the upcoming years.

Other areas for the application of subsidiary self-administrative structures within the German society are welfare and social policy. More concretely, the majority of German citizens are subject to statutory insurance obligations—ranging from health care, old-age, long-term care insurance to car, fire insurance, professional and private liability insurance etc. Self-administrative elements guarantee a balance of interest of insured people, their employers and the government. A tangible consequence of this kind of self-administration is social elections, in which the representatives of the different groups are appointed. Elected people volunteer in influencing the direction and policies of the insurance organizations. Even in the organization of hospitals, day-care-centres, retirement homes etc., the government does not take over directly rather it defines rules and delegates the operational responsibility to independent welfare associations with ideological roots (Caritas of Catholic Church, Diakonia of Protestant Churches, Worker’s Welfare of the Labour Movement, German Red Cross etc.) which build up and maintain organizational structures in their own responsibility and according to their own rules.

Furthermore, similar structures exist in the health care system. Here, representatives of health insurance, hospitals and general practitioners negotiate with each other regarding the framework conditions of the healthcare system and regularly adapt them to new circumstances. For example, an important institution in that respect is the ‘Joint Federal Committee’ (‘Gemeinsamer Bundesausschuss, GBA’): the supreme decision-making body of the self-administration of doctors, dentists, psychotherapists, hospitals and health insurance funds. The GBA determines the benefits catalogue of the statutory health insurance (Gesetzliche Krankenversicherung, GKV) for more than 70 million compulsorily insured persons in the form of guidelines. *It therefore determines which medical care services are reimbursed by the statutory health insurances and which are not.* This

extremely important decision with enormous financial consequences is made by the 13 members of the commission, of which 5 represent the service providers (German Hospital Society, DKG, as well as the National Association of Statutory Health Insurance Physicians, KBV) and one represents the National Association of Statutory Health Insurance Dentists (KZBV)). The other 5 representatives are nominated from the service demand side, represented by the umbrella organization of statutory health insurers. Moreover, three impartial members are jointly nominated: they must not have been employed in organizations of service providers nor in organizations of service users during the last year preceding their appointment. Subsequently once the GBA is constituted, federal state ministries and the national ministry for health limit themselves to setting the scene and controlling the proper execution of the legal obligations of subsidiary self-governing organizations.

### **Regional Self-administration in Autonomous Municipalities, Cultural and Academic Sector**

Self-administration rights of local, regional and state-level bodies are laid down in Art. 28 of the German Constitution and in many Federal State Constitutions. The financial and administrative autonomy of municipalities and municipal associations guaranteed by constitutional law cover the right to fix their own communal fees, autonomous planning and hiring as well as fixing their own statutory law. If these rights are violated, representatives can sue upper-level representatives in the Federal Constitutional Court. Communal bodies organize their own democratic elections in Germany. Elected majors are independent heads of their local administration and are not subject to the authority of the Prime Minister of their federal state (Bundesland) or even of the Chancellor of the Federal Republic. Rather they decide independently in their realm—as long as no higher-level issues are concerned.

In a similar way, academic research and public education are also structured in autonomous self-administrative decision processes. For example, important decisions are made in self-administrative research organizations like the German Research Foundation (DFG), the Leibniz-, Fraunhofer- and Max-Planck-Society, in self-administrative peer review and evaluation procedures, etc. Political funders from ministries or administrations may determine the overall topics of certain research projects; however, they are not supposed to intervene concretely in the selection process of certain projects, make executive research decisions or manipulate the results. Universities administer themselves via elections for the academic senate, the faculty councils, the university council as well as different commissions. Professors are endowed with freedom of research and education—implying that they can follow their own research agenda and are not subject to any external demands. Education policy is a matter of the federal states in which the central government is not supposed to intervene directly.

Even public broadcasting organizations possess a constitutionally guaranteed freedom, which grants them independence from political parties and government

authorities with regards to their reports and editorial contributions. A Broadcasting Board monitors compliance with the statutory broadcasting mandate. In addition, the Broadcasting Board guarantees the openness of access to the program of the public broadcasters for various socially relevant groups in accordance with the diversity assurance concept devised by the legislator. Indeed, the Broadcasting Board does not determine the program planning directly, which is the responsibility of the Director-General. However, the Broadcasting Board advises the director with regard to program planning. It is composed of members of various associations listed in the respective Interstate Broadcasting Treaty. These include, for example, trade unions, women's associations, churches, journalists, independent charities, the German Association of Cities and Municipalities, the German Sports Federation, environmental organisations, cultural organisations, parliamentary groups etc. Moreover, delegates from different public bodies—from the Federal Government, the Federal States to local administrations, are members but should not form the majority. Represented groups and organizations choose their representatives independently and according to their own statutory rules so that the Broadcasting Council represents a cross-section of the population.

Finally, churches and religious communities possess a right to self-determination in Germany—as they are not as such part of the self-administration of the state. In order to protect their autonomy, however, even churches are in many cases constituted as public-law organizations. Their autonomy includes the right to autonomous hiring as well as the right to establish their own statutes—as long as they are in accordance with general principles of law, such as human rights or non-discrimination. Similar subsidiary self-administrative structures exist in the jurisdiction but also in unusual areas such as hunting associations, fire brigade associations etc.

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## **Conclusion: What Could Be Learned from the German Experience?**

This article started with the—initially rather improbable—economic success of (West) Germany after the Second World War. More specifically, neither an ominous 'German nature' nor external support sufficiently explains this sustainable growth over decades. Rather, more important was the institutional framework of the Social Market Economy, which gradually emerged from the 1950s onwards. Economic policies of Social Market Economy systematically focussed on small and medium-sized family enterprises—endowing them *inter alia* with sources of local finance as well as excellent structures of dual VET. In particular, Public-law chambers with obligatory membership enabled German (and Central European) companies to overcome a cooperation dilemma and establish a sophisticated structure of cooperation in professional education.

Beyond Central Europe, however, many entrepreneurs around the globe still find it impossible to organize comparable structures of a comprehensive professional education system. What could they learn from the German case study in a more general perspective?

## **Valuing the Wisdom of Practical Elites**

In a decades-long process, a public chamber and self-government system has emerged: Here, the spirit of civic engagement and professional identity is continuously brought forth and nurtured. This organisational structure—and especially the independent consultation and “practical wisdom” embedded in it—can tame regulatory frenzy and ideological zeal. It should enable independent and informed decision-making: The “wisdom of practitioners”. Even though this goal is a generally accepted principle among the German public, it is also repeatedly challenged by political actors when it prevents them from achieving their political goals. Admittedly, the decision-making processes of self-governance are cumbersome and prevent quick and personalised initiatives and actions; they are based on regular and “wise” decisions by professional practitioners rather than on spectacular political interventions with high visibility. On the other hand, they usually follow participatory rules and are therefore regularly at odds with the interests of powerful elites. By setting and continuously improving certain institutional standards, they enable collective learning and a gradual professionalisation of processes.

## **Building on Existing Networks of ‘Social Capital’**

As seen above, the special circumstances of German history led to a public chamber system after 1949 with compulsory memberships and contributions for every German entrepreneur. As a result, the chambers emerged as strong self-governing public institutions. The existence of these structures subsequently enabled further reforms, which step by step gave rise to the dual VET system that exists today. Economists speak of “path dependency” in this context. The German VET system cannot therefore be understood without the institutional framework that supports it: chambers, but also employers’ associations and trade unions, research institutions etc. are the most important elements here. As seen above, without these structures a “prisoner’s dilemma” situation can easily arise between the various companies involved. They might fear that investing in the further training of their employees will lead to the well-trained employee being poached by a competitor who has saved corresponding costs and can therefore now entice them with a higher salary. Moreover, if all potential partners fear such exploitation, a cooperation will never come about, even if it would have been beneficial for the entire region.

In summary, this means that the dual VET system is difficult to reproduce in a context without corresponding structures. But what could be done? Implementation would be most promising where traditions of successful cooperation between

different companies ('social capital') exist. Existing networks can then serve as a 'functional equivalent' for the structures we try to illustrate in this book. An exclusive partnership network that successfully trains and develops 'its' apprentices and embraces the positive outcomes of the training investment should be built. Then, in a second step, also bystanders can be convinced of the meaningfulness of the project as a whole. A culture of cooperation and identity building, as is strongly developed in many regional chambers in Germany, can then gradually emerge and spread to the entire region. In any case, corresponding bottom-up processes seem much more promising than a top-down political implementation that neglects the nuts and bolts of creating a lively culture: Wisdom can be destroyed quickly but is difficult to develop!

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