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Varieties of Strategies: Societal Influences on British and German Responses to the Global Economic Crisis

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ABSTRACT *The current global financial and economic crisis has led to widespread calls for multilateral policy co-ordination. However, national strategies towards financial market regulation and domestic stimulus programmes considerably diverge in cross-country comparison. Why do policy reactions to the crisis differ? Following a societal approach to preference formation, I argue that national strategies are strongly shaped by value-based ideas and by sectoral interests. While ideas on the role of politics in governing the economy can, for example, lean more towards trust in market forces or instead favour governmental regulation, interests may influence governmental positions according to the economic relevance of the respective sector. An analysis of the discourse and the measures regarding stimulus packages and financial market regulation in Britain and Germany supports this argument and shows that ideas as expectations, institutionalised ideas and material interests reinforced one another in influencing governmental strategies.*

KEY WORDS: economic policy, financial market regulation, societal approach, Germany, United Kingdom

The global financial crisis, which dramatically escalated in autumn 2008 and since 2009 is severely affecting the real economy in industrialised and emerging economies, is considered to have reached a magnitude only comparable to the world economic crisis of the post-1929 years. After the demise of Lehman Brothers in September 2008, financial markets collapsed and stock markets crashed. As a result of the huge and only partially transparent holdings of ‘toxic assets’ by banks, which would have to be written off, especially those containing subprime mortgage loans, banks did not trust each other any more. Consequently, inter-bank lending and borrowing dried up. This in turn has had dramatic implications for the real economy as loans for trade, manufacturing and service production have been strongly reduced because of higher risks and a widespread loss of trust. Many banks as well as non-banks have been approaching bankruptcy conditions and in 2009 many industrialised countries were suffering shrinking economic activity, that is, a severe recession (Helleiner, 2009; Hodson & Quaglia, 2009; Pauly, 2009; Rodrik, 2009; Wade, 2008).

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Governments have responded to this crisis of financial markets and the real economy with rescue and stimulus programmes and propositions for new regulations nationally and globally.

First, troubled financial institutions such as Northern Rock in the UK, American International Group in the USA and Hypo Real Estate in Germany were rescued with huge injections of money by governments. For the banking community in general, a safety net was established in the form of guarantees covering hundreds of billions of Euros, dollars and pounds in order to provide liquidity and strengthen trust in the static credit market.

Second, governments have been smoothing the downturn of the real economy with large stimulus programmes in a Keynesian attempt to increase domestic demand through deficit spending. Planned stimulus packages included some automatic stabilisers and by early 2009 already totalled 4.8 per cent of GDP in the USA, 1.5 per cent in the UK and 3.4 per cent in Germany in 2008–2010 (The G20. Talking-shop-on-Thames, *The Economist*, 14 March 2009, p. 67).

Third, governments have become engaged in new regulation for financial markets nationally and multilaterally that would help prevent a similar crisis in the future. At the global level, these attempts have been conducted within the G20, a group which includes the G8 states as well as emerging powers such as China, Brazil and India. At the regional level, the member states of the European Union (EU) have also striven to develop improved modes of governance. The propositions range from strengthening the International Monetary Fund (IMF) to new regulations for banks and other financial actors such as hedge funds and rating agencies.

While the crisis affected industrialised countries severely, national positions and policy responses have shown considerable differences. Divergences on both regulatory reform and economic stimulus packages can be detected even among member states of the European Single Market such as Germany and the UK. The goal of this paper is to trace and explain national policy responses to the crisis. What happens when an external shock, such as the global crisis, meets path-dependent national ideas and institutions? Did countries react differently from one another, as would be expected given ideational differences among societies and varieties of capitalism? Or did the crisis also trigger a new convergence?

Societal Approach to Preference Formation: Ideas and Interests in Economic Policy

In order to analyse the questions raised above, this paper will use a societal approach to comparative political economy, stressing the influence of value-based ideas and material interests on governmental positions and policy making (Schirm, 2009, pp. 503–507). This approach seems promising for the comparative explanation of differing governmental positions vis-à-vis the global economic crisis because the crisis directly affects the societal level, that is, voters and economic sectors, which both can be presumed to influence the government. In following a societal approach, I will recur to the liberal theory of preference formation (Moravcsik, 1997) and focus on the influence of domestic politics on governmental preferences as well as on the interaction between globalisation and domestic politics (Busch, 2004; Hay & Rosamond, 2002; Katzenstein, 1978; Milner & Keohane, 1996; Schirm, 2002a, pp. 33–56).

Interests are defined here as material economic considerations of domestic actors which are shaped through the costs and benefits induced by market conditions and expected from

policy initiatives. Ideas are defined as path-dependent and value-based collective expectations on how politics should govern the market. While interests can be traced by showing the relevance of the respective sector and its economic circumstances, ideas can express themselves in societal attitudes and, in an institutionalised form, in the political culture and system of a country. By considering institutions as a codified form of path-dependent ideas, the societal approach of this paper also relates to the ‘Varieties of Capitalism’ literature (Fioretos, 2001; Hall & Soskice, 2001; Scharpf & Schmidt, 2000), but treats institutions as subject to interpretation in discourses (Schmidt, 2009). Like interests, ideas can change, but changes take longer than changes in interests because of the path-dependent character of ideas. Thus, by investigating (1) the interpretation of institutions and policies in the light of ideas and interests, and (2) the governments’ receptivity to ideas and interests, the societal approach complements the stability-focused and the firm-centred view of institutions suggested by the ‘Varieties of Capitalism’ approach.

The societal approach employed here also attempts to complement rational and reflective institutionalism (Hall & Taylor, 1996; Keohane, 1988; Schmidt, 2009). Compared to rational institutionalism, which suggests an objective nature of institutions and focuses on transaction costs, the approach of this paper seems more promising, because it analyses the interpretation of the market and its regulative institutions by investigating ideas as an independent variable and policy-discourse as a method. Compared to reflective institutionalism, which argues that the meaning of institutions is shaped by intersubjective communication, this paper’s approach seems more promising because in addition to including the reflective dimension by analysing the role of ideas, it also analyses the role of material economic interests in political discourse. The relevance of considering both societal ideas and interests in the analysis is underlined by Hall and Thelen (2009, pp. 27–28) who state that, ‘although the interests of firms and workers are crucial to particular modes of coordination, capacities for coordination also depend on ... a set of shared understandings about how other actors will behave’. Further, Blyth (2002, p. 251) stresses that ‘structurally given interests’ need to be instructed by ‘ideas that inform agents’ responses to moments of uncertainty and crisis’.

Summing up, the societal approach proposed here is related to institutionalism but also distinct from it in that it focuses on actors and not on institutions, specifically on actors’ ideas and interests as driving forces for governmental preference formation. Thus, institutions do figure prominently in this paper, but are subject to interpretation by societal actors in light of their ideas and interests.

By using the variables ‘interests’ and ‘ideas’, this paper addresses both the more recent changes brought about by global markets as well as the longer term values and institutions of the societies affected by globalisation. In pluralistic societies, ideas and interests can compete in influencing preferences. Also, different interests and different ideas can compete amongst themselves. In addition, both can interact with each other in a non-competitive way. For example, dominant ideas can reinforce or weaken specific interests, and changing interests can trigger a socialisation process which alters societal ideas (Schirm, 2009, p. 504). Furthermore, the intensity with which interests influence governmental positions may depend on the set of ideas on the related issue, such as the ideas of ‘individual responsibility’ and ‘trust in market forces’ supporting the interest in ‘liberalisation’ and ‘light touch regulation’. But when do ideas prevail over interests or vice versa? In this regard, I argue that ideas prevail in discourse and policy positions when

interest groups either support the dominant ideas and possess political (articulation) and economic (jobs, revenue) strength or oppose the dominant ideas but do not possess political and economic strength.

In sum, the purpose of this paper is to give a theoretically informed explanation of the empirical puzzle about the reasons for the variation in strategies used to respond to the crisis. The core argument is that the positions of governments towards the financial crisis, specifically towards new regulation and economic stimulus programmes are strongly influenced by domestic ideas and/or interests. This argument is based on the assumption that governments in democratic political systems seek re-election and are therefore responsive to dominant societal influences ranging from specific lobby groups to the attitudes of voters in general. Thus, governmental positions express preferences originating from societal influences prior to international strategies and interstate negotiations.

Operationalisation

In the following, the argument that policy positions towards the financial crisis are shaped by domestic interests and/or ideas will be examined through an analysis of the discourse and of the measures taken in the UK and in Germany covering the period between the aggravation of the crisis in September 2008 to the third G20 summit in Pittsburgh in September 2009. The two countries were chosen in order to compare two different sets of ideas and interests: a liberal market economy heavily shaped by financial services and a co-ordinated market economy strongly shaped by manufacturing. Two policy-cases will be considered: the positions and measures towards new regulation of financial markets and towards economic stimulus programmes. In examining the public discourse, this paper will use speeches by the responsible politicians (finance ministers, heads of government), official documents and articles from established serious newspapers. These statements will be examined with regard to whether the positions represent the material interests of domestic groups or whether they refer to path-dependent ideas dominant in the two countries. In empirically tracing the variable 'ideas' in the UK and Germany, the paper refers to research on differing ideas in the two societies (such as in Fioretos, 2001, pp. 220–221; Hodson & Mabbett, 2009; Schirm, 2002b, pp. 223–234, 2009, pp. 508–509), and to public opinion polls. The latter show that, while both countries share core ideas on the role of the government in governing the market, they also clearly differ. For example, while the ideas of 'individual responsibility' and 'trust in market forces' receive stronger support in the UK than in Germany, those of 'collective solidarity through the state' and 'trust in governmental regulation' garner more support in Germany than in the UK.

These societal ideas can be made empirically plausible with data from the World Values Survey (WVS). As an exemplary indicator of the different relevance of the ideas 'trust in governmental regulation' versus 'trust in market forces', WVS data show that 66.7 per cent of Germans but only 42.5 per cent of British respondents tend to support the statement that 'the government should take more responsibility', while only 33 per cent of Germans but 49.9 per cent of British respondents tend to agree to the statement that 'we need larger income differences as incentives' (WVS, 2006). As an indicator for the ideas 'individual responsibility' versus 'collective solidarity', WVS data show that 67 per cent of Germans but only 50.1 per cent of British respondents are supportive of the statement 'incomes

should be made more equal', while 33.3 per cent of Germans and 57.5 per cent of British respondents agree to the statement that 'people should take more responsibility' (WVS, 2006). In light of these differences with regard to the independent variable 'ideas', the general hypothesis—that societal ideas and/or interests shape governmental strategies—can be specified for the two policy fields under scrutiny.

Concerning new rules for financial markets, the hypothesis is that pro-market ideas and the large financial sector in the UK will reinforce each other in opposing stricter regulation of financial markets, while the more regulation-friendly attitudes of Germans will prevail over the material interests of the banking sector. This divergence can be explained in that the banking sector is much less economically relevant for the German economy and also comprises fewer regulation-averse actors, such as hedge funds and investment banks dominant in the British financial sector.

With regard to the responses to the economic crisis by stimulus measures, the hypothesis is that, because stimulus packages mostly do not affect specific interest groups but, rather, the electorate in general, their form will reflect dominant ideas vis-à-vis the role of politics in governing the market (ideas comprising voters' attitudes and ideas codified into institutions). Therefore, Germany's stimulus package will reflect the existence of huge automatic stabilisers shaped by the idea of 'collective solidarity' and the consensus concerning price stability, while UK stimulus programmes will reflect the limited automatic stabilisers as well as the greater acceptance of rapid policy changes in the liberal market economy.

Regarding discourse analysis, it is important to bear in mind that a public statement referring to interests or ideas does not necessarily provide the real reasoning behind the government's position. When governments underline preferences with ideas, they can, for example, also draw a rhetorical picture to promote hidden material agendas, such as protectionism or liberalisation. However, public statements provide evidence for what the government considers to be acceptable to the voters and, therefore, legitimate. Thus, I assume that governmental positions will in principle reflect attitudes grounded in real, endogenous patterns of legitimate ideas and interests. In order to secure this link between governmental preferences and societal ideas and interests, the evidence on governmental positions focuses on quotes from finance ministers and heads of government who (based on the assumption of self-interest to remain in office) will ground their positions in patterns acceptable to and thus legitimate in the eye of voters. Positions of expert bureaucrats are not considered because the paper aims to explain the positions as stated by the responsible politicians, who are accountable to voters and therefore presumably receptive to societal influence.

Thus, the analysis in this paper only attempts to shed light on the preference formation of politicians responsible for the management of the economic crisis and not to investigate the positions of other relevant actors such as central bankers. The quotes in the case studies serve as examples of a broader discourse, and were selected in a representative way to show the core arguments of the above-mentioned political decision-makers.

Another disclaimer applies to the question of how ideas and interests make their way into policy measures. In this regard, the paper only attempts to show whether the presumed correlation between ideas and/or interests on the one hand, and positions and measures of the governments on the other hand can be empirically demonstrated. Finally, differences between political parties as an explanatory variable for cross-national divergences in economic policy making (Westrup, 2007; Zohlnhöfer, 2007) will not be considered,

because there were not relevant in the years under scrutiny here. While Germany was ruled by a ‘Grand Coalition’, in the UK, the ideas underpinning economic policy have not changed, and, in addition, the government and the conservative opposition agreed that financial sector reform must not jeopardise the interests of ‘the City’ (Hodson & Mabbett, 2009, pp. 1041, 1055).

Case I: Financial Market Regulation

Despite common intentions on financial market regulation, clear differences in the interpretation of the crisis and of the precise form of regulations become visible when analysing speeches and interviews of heads of government, that is, Gordon Brown and Angela Merkel, and finance ministers, Alistair Darling and Peer Steinbrück.

Germany: Measures and Discourse

The German government strongly advocated stricter regulation of financial markets. Both Merkel and Steinbrück frequently stressed the necessity to control all financial market actors, all financial products and all financial marketplaces. This has been the German position since the G20 meeting in Washington, DC in November 2008 (Merkel, 2008a).

With regard to the interpretation of the crisis situation, Steinbrück and Merkel criticised the ‘Anglo-American’ economic model as being responsible for the financial crisis and praised the advantages of the German Social Market Economy. Steinbrück complained that the Anglo-American model has been promoted by its supporters as superior to the continental European economic models (Steinbrück, 2008). The German government considered the financial crisis to constitute an ‘Epochenwende’ (epochal turning point), which demands fundamental changes in economic governance in the form of better regulation and less trust in market forces (Steinbrück, 2009a). Unlike the UK government, the German government emphasised international institution-building. Chancellor Angela Merkel (2008b) stressed the necessity to create European regulators and a ‘World Economic Council’ along the model of the UN Security Council with similar powers but composed of industrialised as well as emerging markets and developing countries. Merkel (2008a) also proposed strengthening the IMF by giving it the power ‘of punishing member countries who do not abide by the common rules similar to the powers of the World Trade Organization (WTO)’.

On specific regulatory measures, Germany favoured stricter control of tax havens and hedge funds, higher capital requirements for banks, as well as a stronger IMF with regard to its resources as well as its power over member states. The German government wanted ‘international standards on transparency and regulation to be applied completely also in “non-cooperative” countries’, such as tax havens (Steinbrück, 2009b). Together with France, the German government promoted the creation of new European financial market agencies with the power of forcing national agencies to take action vis-à-vis national financial market actors. A European Systemic Risk Board and three new European agencies (for stock markets, banks and insurance companies) were created in June 2009, but none of them obtained the power to force national authorities to undertake measures which would have budgetary implications. *The Economist* (4 July 2009a, p. 69) comments: ‘The new structures may not live up to . . . expectations. The risk board . . . has only the power of its voice.’ Thus, the new agencies will remain rather powerless vis-à-vis their

national counterparts. Finance Minister Peer Steinbrück criticised that, because of British resistance, the EU Summit in Brussels in June 2009 did not give the new European surveillance agencies the preventive powers to force national regulators to act, which were desired by France and Germany. In addition, Steinbrück articulated his general frustration about the British reluctance to introduce new rules by arguing that, contrary to the G20 agreement at the London Summit in April 2009, Britain would now pursue a ‘restoration of old circumstances’ (Steinbrück, 2009c).

With regard to the payment system for managers, the German government issued a new code which is supposed to reduce bonuses, and the German Financial Supervision Authority (BaFin) provided a new regulatory framework, which restricts bonus payments in general and especially for short-term and risky management. In March 2009 the government issued a draft bill (which passed the Bundestag in July) on tighter regulation and higher capital requirements for banks, lifting capital and liquidity reserves above the Basel II level.

Summing up, the German government attributed the crisis to flaws in the liberal ‘Anglo-American’ model and emphasised the need for stricter regulation of financial markets as well as improved and new international institution building. This interpretation of the crisis and of the responses it requires clearly shows a lack of trust in the self-regulating forces of the market, sees mere surveillance of the market as insufficient and underlines a willingness by the German government to transfer national sovereignty in order to strengthen binding global and regional rules and their enforcement by international organisations. In Steinbrück’s (2008) view, the global crisis proved the weakness of the Anglo-American model and would therefore lead to a ‘multipolar’ world financial system in which the Anglo-American model would no longer dominate to the degree it did before the crisis. While ideas such as ‘trust in governmental regulation’ can be identified as core influences on the discourse and measures in the German case, specific interests could not be detected. This can be attributed to the relatively small size of the German financial industry compared to the British financial sector and to the near absence of hedge funds in Germany (see evidence in UK case).

United Kingdom: Measures and Discourse

The British government rhetorically agreed with the German government on the necessity of new rules for financial markets in order to prevent future financial market and real economy crises. It differs, however, from German positions on the interpretation of the crisis and the new regulations as well as on the substance of measures to be taken.

With regard to the interpretation of the crisis situation, the British government essentially argued that the financial crisis was caused by the failure of individual actors (managers, banks), but not by the system (Darling, 2009c). Thus, while the German government advocated new rules to control the market, the UK government favoured more surveillance over individual action and frequently warned against protectionism and over-regulation, often framing new rules and international co-ordination as measures to limit protectionism and means to enhance market efficiency. The need for open markets was underlined in public declarations, as was the self-responsibility of markets and the benefits of open financial markets. Regulation was not stressed to the extent that it was by the German government. The chancellor of the exchequer, Alistair Darling (2009b), stated that international co-ordination is necessary ‘in order to prevent protectionism’ (and not to

improve regulation) and sees ‘more important problems than a pan-European financial surveillance, because Asia and the US are also important for London as a global financial marketplace’.

In an official document listing the ‘UK objectives for the G20 in 2009’, Darling (2009a) made clear that after the first objective—the ‘return of trust and confidence to financial markets’—the second objective must be to ‘retain and build on the benefits that open financial markets bring to the world economy’. Improved regulation did not figure among the official UK objectives. Instead, better governance was demanded in a voluntaristic manner from banks: ‘We need improved governance of financial institutions. We should press for more active, informed and capable boards. We must demand better due diligence and care of clients’ interests. And we must expect improved ethics.’ With this statement Darling emphasised the government’s argument that the crisis was caused by individual (boardroom) mistakes, not by systemic failure.

With regard to specific regulatory measures, the UK followed the above-mentioned argument and advocated foremost a reform of the payment system for bankers. In addition, the government agreed with other EU governments on the need to supervise tax havens, but was criticised for not really pursuing the goal put forward rhetorically. In accordance with this observation, the Chief Inspector for tax havens, Michael Foot, has stated he does not see any necessity that these tax havens be more regulated (Volkery, 2009). The Treasury published a new voluntary code of conduct for banks, to dissuade them from constructing intricate tax-avoidance schemes. With regard to new European regulatory bodies and as mentioned in the previous section on Germany, the British government was successful in preventing the European Systemic Risk Board and the new EU agencies from being given the power to intervene in national financial market regulations (Traynor, 2009).

In July 2009, the Treasury presented a 176-page paper on reforming financial markets which reflected the government’s argument that boardroom failure, not the system, was responsible for the crisis. Consequently, the paper did not demand substantial reforms in the form of new, binding rules. The paper was welcomed by the British Bankers’ Association but criticised by the Liberal Democrats as a ‘return to business as usual’ (Treanor, 2009a). Alistair Darling defended the current financial market regulation system by pointing to the importance of preserving the competitiveness of the City and its one million jobs in financial services, to the £250 billion of tax generated by the sector in the past nine years, and to the individual but not systemic failures as the cause of the crisis (Treanor, 2009a). The British financial industry’s share in total value added was roughly double that of the German financial industry’s share in its country’s total value added in the mid-2000s (Bickenbach *et al.*, 2009). *The Economist* (9 July 2009b) comments on the relevance of the City:

The earnings from financial services in a good year add over £25 billion to government revenues, and the financial sector employs over 1m people across the country. Against that is the loss in economic output from a full-scale crisis, which averages around 20% of GDP, according to an IMF working paper.

Thus, sectoral interests dominated general economic interests in influencing the UK government.

With regard to the stricter regulation of hedge funds desired by Germany and France, the British government actively opposed the proposals of its fellow EU members

(Zimmermann, 2009). The government lobbied against new rules vis-à-vis other EU member countries to convince them not to regulate hedge funds at the European level (Reuters, 2009). Financial services based in London account for 80 per cent of all hedge-fund assets managed in Europe (*The Economist*, 25 July 2009c, p. 28). In sum, the British strategies towards regulating financial markets demonstrated trust in market forces, distrust in regulation and the prevalence of the financial services interests over general economic concerns (see Darling 2009a).

Comparison

In contrast to Germany, the UK government interpreted the crisis not as a systemic crisis of open markets, but instead as a failure of individual boardrooms and, therefore, showed little enthusiasm for the strengthening of binding, international rules and multilateral organisations. The societal idea of ‘trust in market forces’ as well as the strong material interest of the financial sector can be detected as dominant characteristics of the British discourse and government positions. In contrast, the positions of the German government were shaped by the interpretation of the crisis as a failure of the international market system, by the dominant societal idea of ‘trust in governmental regulation’. Both countries’ positions diverged in relation to ideas about the role of the state and the market in governing the economy. In the UK, societal ideas and the interests of the strongly affected and economically very relevant financial sector reinforced each other. In Germany, the lower societal ‘trust in market forces’ and higher ‘trust in governmental regulation’ prevailed and the interests of the smaller financial sector did not appear in government positions. In addition, Germany’s traditionally more favourable attitude towards supranational European policies presumably contributed to demands for powerful EU financial agencies, while the British reluctance to cede sovereignty was plausibly reflected in its resistance to the transfer of power onto the European level.

Case II: Bank Rescue and Domestic Stimulus Packages

The UK and Germany initiated large-scale programmes to rescue national banks and to stimulate their national economies in face of the rapidly approaching economic downturn after the outbreak of the crisis.

Germany: Measures and Discourse

With regard to the rescue and bailout of banks after the aggravation of the crisis with the demise of Lehman Brothers in September 2008, the German government showed a more moderate pace than did the UK. Only after two months had passed were German financial institutions given a large safety net in the form of guarantees (up to 400 billion Euro) in order to boost trust and overcome the blockade of inter-bank credit. In addition, an 80 billion Euro programme was created through which banks could borrow money from the state to increase their equity. A new agency was founded, the *Sonderfonds Finanzmarktstabilisierung* (SoFFin), to supervise the safety and rescue programme.

Unlike the UK, the German government did not force needy banks to use the resources and guarantees of the safety programme: ‘The preference for a hands-off and voluntary approach is very much in line with the industry-led response to crisis in Germany

highlighted in the varieties of financial capitalism literature' (Hardie & Howarth, 2009, p. 1031). Due to this policy, the goal of normalising lending was not achieved to the degree hoped for, since banks were hesitant to use government aid for fear of acquiring the image of being vulnerable. In reaction to the credit squeeze for many companies, the Federal Government and the Länder set up special programmes in 2009 to secure credit and guarantees for small and medium-sized firms which could not get money from private banks (Bartsch *et al.*, 2009). The bank most severely affected by the crisis, the Hypo Real Estate, was nationalised in summer 2009 after receiving over 90 billion Euro in guarantees and equity. The debate about rescuing banks with public money and guarantees evolved around the need to save systemically relevant banks ('too big to fail') in order to prevent a complete breakdown of financial markets.

With regard to its economic stimulus programme, Germany was heavily criticised by its European neighbours and the US for not spending more to increase domestic demand through deficit spending and lowering taxes. Indeed, the initial German stimulus package was quite small, but the criticism apparently neglected the huge automatic stabilisers of the German welfare state. Because unemployment money and other social security transfers are much higher in Germany than in the UK, public expenditure and demand stimuli automatically increase substantially during an economic downturn. Especially expensive for the government, but also powerful in preventing unemployment, was the transfer of workers to the Kurzarbeit-scheme under which employees work fewer hours per week and the government subsidises part of their salary. This scheme reduced the financial burden for the employer and workers were prevented from being sacked because of the crisis-induced temporary reduction in business for their companies. The second stimulus package, decided on at the beginning of 2009, involved new explicit transfers. In addition, the government stimulated the demand for cars with 5 billion Euro for the Abwrackprämie ('cash for clunkers'). It involved a 2,500 Euro bonus to each buyer of a new, environmentally sound car who simultaneously agreed to the destruction of an old car. Germany rejected lowering taxes in response to the crisis and its finance minister portrayed the reduction of VAT in the UK as 'crass Keynesianism' that would lead to a huge deficit which would take a generation to pay down:

The same people who would never touch deficit spending are now tossing around billions. The switch from decades of supply-side politics all the way to a crass Keynesianism is breathtaking. When I ask about the origins of the crisis, economists I respect tell me it is the credit-financed growth of recent years and decades. Isn't this the same mistake everyone is suddenly making again, under all the public pressure? (Steinbrück quoted in Watt *et al.*, 2008)

Thus, it is plausible to argue that the combination of two factors shaped Germany's specific policy vis-à-vis the crisis, that is, the decision for relatively low new stimulus packages. The first is Germany's broadly shared ideational consensus on fiscal discipline, the '*Inflationstrauma*' (Hartwich, 1998, p. 67), evident since the hyperinflation in the Weimar Republic and enshrined in Ludwig Erhard's post-war recipe of the Soziale Marktwirtschaft (Schmidt, 2001, pp. 1–2). The second are the relatively high automatic stabilisers of the institutionalised idea of 'collective solidarity through the state', which lead to an automatic increase in governmental spending in times of economic crisis. In line with their plea for fiscal discipline at the creation of stimulus programmes, both Merkel

and Steinbrück started in June 2009 to argue for a rapid reduction in governmental aid and stimuli. Nationally, at the EU level, and at the G8 Summit in Italy, the German government demanded an ‘exit-strategy’ (Steinbrück 2009d) from big spending in order to ‘secure states’ future financial ability to act’ (Merkel quoted in Spiegel Online, 2009).

United Kingdom: Measures and Discourse

Regarding the rescue and bailout of banks, the British government reacted quickly to the problems of its national financial institutions. The Northern Rock bank was already nationalised at the beginning of 2008 and other banks, such as the Royal Bank of Scotland (RBS) and Lloyds Banking Group, were saved by large injections of public money. The huge October 2008 rescue package for banks, amounting to a total of £300 billion in guarantees and equity, was constructed in an obligatory way which forced needy banks to use it, thus differing starkly from the German government’s voluntaristic approach to banks in its respective package. Throughout 2009 RBS remained the biggest problem for the British government, which had raised its guarantees for troublesome RBS loans to £280 billion and its stake in RBS to 84 per cent by November 2009 (Treanor, 2009b). Compared to the measures in Germany, the British government acted quicker, more decisively in securing banking activities, and with larger sums in order to secure the health and competitiveness of its financial sector. This can plausibly be attributed to the more important role of financial services for the UK than for the German economy (see above).

As for the economic stimulus programme, the British government entered into high levels of deficit spending by increasing expenditure (e.g. for infrastructure, training) and especially by lowering VAT. As early as November 2008, the British government set up its first £billion stimulus package and lowered VAT from 17.5 per cent to 15 per cent in order to boost demand and cushion the approaching recession. With these steps, the UK’s new measures were quicker to come and larger in volume than Germany’s response, but it ultimately did not reach the same percentage of GDP. According to *The Economist* (14 March 2009, p. 67), Germany’s stimulus measures including some automatic stabilisers reached a total of 3.4 per cent of GDP in 2008–2010 compared to Britain’s 1.5 per cent (with the USA at 4.8 per cent). To a large extent, this can be attributed to the lower automatic stabilisers in the UK. Also, the British prime minister apparently was quicker to abandon long-standing convictions such as the—at least rhetorically praised—principle of fiscal prudence, arguing that ‘extraordinary times require extraordinary action’ and that policy-makers all over the world were ‘leaving behind the orthodoxies of yesterday’ (Brown quoted in Sparrow, 2008). Brown also justified the large budgetary deficits due to a decrease in revenue and an increase in spending with low automatic stabilisers: ‘We decided that a normal injection of resources into the economy, letting automatic stabilisers work, would be quite insufficient to deal with the scale of loss of output’ (Brown, 2009).

In 2009, the British stimulus package was enlarged as specific, non-banks could now also benefit from rescue measures, since the government acknowledged its intention to borrow more money to help strategically important industries. In spring 2009, a £22 billion programme was initiated to help small and medium-sized firms with guarantees and, in April, the UK followed Germany with a cash-for-clunkers programme with a bonus of £2,000 available to all car-buyers who agreed to the destruction of their (at least) 10-year-old cars. The British government declared in the summer of 2009 that it would raise taxes for all incomes above £150,000 yearly to 50 per cent in reaction to the rapid growth of public

debt due to the measures taken in response to the crisis (Elliott *et al.*, 2009). Contrary to the German government's international initiative for an 'exit strategy' to the mounting public debt induced by the stimulus packages, the British chancellor warned against such an endeavour: 'I am confident global recovery will come. But we are not there yet. . . . As we draw up our plans we must accept that the biggest risk would be to exit before the recovery is real' (Darling quoted in Hopkins, 2009). This greater willingness of the British government to increase public debt and to run inflationary risks corresponded to the greater readiness of the population to take on personal debt, evidenced by Britain having half of the total of European credit card debt and by the British "'borrowing against the house price" culture' (Keegan, 2009). Thus, both countries' strategies towards new public debt induced by stimulus programmes seem to be in line with path-dependent societal ideas.

Comparison

The comparison of the policies and the discourses in Germany and the UK with regard to the rescue of banks and the economic stimulus packages shows that the measures reflected the different path-dependent ideas and their codified institutional form. The German side did not have to invest so much in new stimulus packages because of the huge automatic stabilisers such as the relatively large unemployment benefits and the Kurzarbeit scheme. These automatic stabilisers reflected the widely shared ideas of 'incomes should be made more equal' as well as 'collective economic solidarity' and confirm the expectation that the state should provide a shelter against the grievances of the market. At the same time, the German reluctance to lower taxes (such as the UK with VAT) reflected the longstanding idea of price stability and the resulting expectation of fiscal prudence, popular in Germany since the inflationary experiences in the Weimar Republic and codified in the Bundesbank laws.

In Britain, the rapid reaction to the crisis also followed predominant ideas and their institutionalised forms as well as the 'Varieties of Capitalism' model in its pace (rapid instead of incremental change) and in its size (VAT), due to the very limited automatic stabilisers. The relatively small size of the latter can be considered a codified form of the societal ideas of 'individual responsibility' and 'trust in market forces'. However, both countries' measures were similar in their goals of rescuing the banking system and increasing demand to cushion the economic downturn. Britain was quicker to adjust to new circumstances than Germany, possibly because of its more flexible conception of economic policy making (compared to Germany's co-ordinated market) and because of the greater need to create programmes due to the smaller automatic stabilisers. In sum, the need to respond to the interests of specific groups (the crisis-ridden banks and companies) and to the general interest in cushioning the economic crisis led to similarities. On the other hand, the specific characteristics of the stimulus programmes showed persistent differences reflecting societal ideas and their codified, institutionalised form, such as the welfare system and the flexibility/inflexibility in changing economic policy.

Conclusion

German and British strategies towards the global financial crisis and the economic downturn were strongly shaped by domestic ideas and interests. This finding corresponds to the societal approach to International Political Economy (IPE) used in this paper to trace and explain convergence and divergence of policy answers towards the crisis. Variation could be detected

between the two countries and with regard to the two policy fields analysed. In the case study on financial market regulation, the British government followed the dominant societal ideas of ‘trust in market forces’ as well as the interests of the economically significant financial sector. In the UK, dominant societal ideas and interests reinforced each other resulting in the government’s resistance to new, binding, national and international rules for financial markets. In Germany, the dominant societal ideas of ‘trust in governmental regulation’ prevailed, and the German financial sector was not as economically relevant as the City of London and also did not completely share their British counterparts’ material interests (such as the protection of hedge funds and investment banking crucial for the UK). Of course, both countries share an appreciation of governmental rules as well as of market forces. The difference is one of emphasis.

With regard to the economic stimulus programmes, both governmental discourses as well as measures clearly reflected the dominant societal ideas. While the ideas of ‘collective solidarity through the state’ and ‘trust in governmental regulation’ as well as their codified, institutionalised form of large automatic stabilisers shaped German policy, the ideas of ‘individual responsibility’ and ‘trust in market forces’ as well as limited automatic stabilisers shaped the British stimulus measures. Consequently, the German package was smaller than its British counterpart because of the pre-existing, large automatic stabilisers in the welfare institutions (such as short-time working and higher unemployment transfers). In addition, German reactions to the economic downturn reflected the traditional ideas of fiscal prudence and of incremental change, while the British reaction was quicker and more ready to embrace large budget deficits.

Thus, the analysis shows that the dramatic external shock of the worst economic crisis since 1929 did not lead to a convergence of economic policies. Instead, responses to the crisis largely followed ideas as expectations, institutionalised ideas and material interests. The latter did not contradict the former, but both rather reinforced each other. The implications of this finding for the two countries does not bode well for new global economic governance. Divergences of path-dependent ideas will not be overcome easily at the international level because they can only be settled by building a new consensus, while differences in interests can in principle be bridged more easily through compromise. Certainly, the new EU agencies and the G20 seem to represent a good start for achieving multilateral consensus, but the successful creation of new rules for global markets will likely require persistent dialogue over a long period of time. However, if consensus is the long-term ideal, then respecting and coordinating diverging ideational convictions and competitive interests through common rules of conduct might be a useful first contribution to better management of the world economy.

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