

# Analysis of the economic problems after the unification of Germany

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**Abstract.** The fall of the Berlin Wall, one of the eight major political upheavals in Eastern Europe in 1989, fueled popular enthusiasm for reunification, directly undermined the East German government's plans for control and reform, and put the German question back on the international political agenda. The different economic paths and outcomes between the GDR and the Federal Republic of Germany led to different social outcomes, resulting in different social structures and social problems. In the end, the economic and social model of federal Germany came to the fore, but the after-effects of reunification and the new national environment forced Germany to embark on a different economic path after reunification. Such new changes in the economic sphere constantly triggered corresponding changes in the structure of German society. How to view these changes is a new problem facing contemporary German studies.

**Keywords:** GDR, FRG, Germany, Economy, Reunification.

## 1. Introduction

The German question has always been one of the most important issues in the all-directional game between east and West camps during the Cold War. After The Second World War, GDR and FRG each walked out of two completely different economic development paths, until 1989, the occurrence of the Eastern European upheaval put an abrupt end to all these. While many scholars have expressed surprise at this sudden turn of events, McAdams says, "I was as surprised by these developments as any observer, and could not have foreseen the twists and turns of the heady weeks of November and December 1989." [1] In fact, the outbreak of the GDR crisis, the collapse of the Berlin Wall and the subsequent reunification of Germany are largely related to the temptation of external factors or external environment. Under the interaction of social contradictions within GDR gradually deepened due to the stagnation of economic development and west Germany's efforts for national unification, the crisis finally broke out comprehensively and became an opportunity for German unification. After the reunification of Germany, the economic development of Germany is also worth paying attention to. How the Federal Government of Germany overcame the practical difficulties after the reunification of Germany and transformed the new federal states from the backward areas receiving large-scale transfer payments into the help of economic development is a hot topic. This paper intends to interpret the economic development before and after the unification of Germany and Germany from the perspective of economics and look for policies worth reference.

## 2. The economic situation of east and West Germany before unification

### 2.1 The state of the economy in the GDR

The economic development of East Germany is obviously characterized by the political need leading the economic development, that is to say, the economic goal is set in advance from the political standpoint and all political and administrative means are used to make all economic activities revolve around this goal. This unnatural artificial synchronization of politics and economy means that both the formulation and implementation of five-year economic plans and the establishment of industrial structures are based on this goal. Influenced by the technology transfer of the Soviet Union after the war, the industry in the Soviet occupied area developed rapidly. East Germany's growth was also reflected in the Labour market, with employment in the east already above pre-war levels by

1947 and firms hoarding workers. Unemployment fell from over 9 percent at the end of 1945 to just over 1% in mid-1948. East Germany did not make significant adjustments to its economic goals when the 1950s showed them to be flawed. Ritschl found that problems had already appeared in 1950, when the economy of East Germany, whose economic foundation was no worse than that of West Germany, was immediately overtaken by West Germany. [2] Although the East German government in the 1960s carried out a series of economic management system reforms due to economic factors, they still served the constant national political goals. In 1964 the East German government proposed to "replace planning management and central command leadership with a combination of central planning and economic leverage". [3] Sodaro and Michael J suggested that they appear to have been launched for reasons other than those of pure economic rationality.[4] In the mid-1970s, the reforms were halted for purely political reasons: GDR and Soviet leaders feared that going too far would change the country's political color. The synchronization of politics and economy is not based on economic facts, but on artificial goals, and the result is bound to depart from the law of economic development, and then cause unbearable costs. According to the data of the East German State Statistics Office, since the 1970s, the actual economic level of East Germany began to fail to reach the target set in the economic plan, during which the average gap between economic sectors was about 2.94%. One of the root causes of the final failure of East Germany's economy lies in the failure of the relationship between politics and economy in this artificial binding model.

Second, the Soviet economy was characterized by low production capacity for civilian goods but high demand, which meant that the Soviet Union had to extract corresponding goods from other Soviet bloc satellites to meet its internal needs. Within CMEA, the GDR was primarily an exporter, but at prices determined by the Soviet Union. This makes the foreign trade prices to meet the requirements of the Soviet Union often at the expense of national economic interests. As a result, East Germany could not obtain enough civilian goods to meet its domestic demand, which led to east Germany's economic dependence on the West. This economic fact was one of the main reasons for the high debt of the GDR at the end of its existence. At the end of east Germany's economic production was affected by the disruption of its production plan, and its production capacity declined. As a result, its export to western countries significantly decreased, which severely weakened the solvency of East Germany, which further deepened the economic crisis of East Germany. Data from the Berlin Institute for Economic Research weekly show that east Germany's exports and imports fell sharply in 1990 compared with 1989.

In a word, from the perspective of economics, the final failure of East Germany's economy not only lies in the planned economy system itself, but also lies in its adherence to ideology and some principles of planned economy. As a result, the decision makers failed to make timely adjustments according to the specific situation, thus continuing to violate economic laws. From a social point of view, planned economy should have advantages in favor of macro-control, but the plan divorced from reality and economic laws has turned such advantages into disadvantages. The reason for east Germany's economic failure should be that it ignored economic facts, violated economic laws, failed to adjust the system in time, and finally lost the opportunity to implement effective reform. What needs to be explained here is that economic restructuring does not mean abandoning the planned economy completely and finally stepping on the road of comprehensive market economy. There is also a middle way combining the two.

## 2.2 The state of the economy in the FRG

FRG's economy recovered after being badly damaged by the war. In the early postwar period, much of the original production capacity was lost due to the destruction of the war and the dismantling of some of the factory machinery and equipment after the war. In addition, Fascist Germany was defeated, Germany was divided into two, occupied and controlled by the Soviet Union, the United States, Britain and France respectively. West Germany was in a predicament of insufficient raw materials and extreme food shortage. The proportion of various industrial sectors was seriously out of balance, and the national economy was in chaos. West Germany's industrial production in 1946

was only 22.9% of that in 1938, and its employment was only 76% of that before the war. West Germany produced only 106 million tons of coal that year, 27.8 % of what it produced in 1938. Generating capacity was 22 billion KWH, 39.80% of that of 1938. It produced 2.56 million tons of steel, 11.3 % of that in 1938. In 1948, West Germany's industrial output was only 4.3 % of that of western countries, compared with 10.4 % in 1937-38 before the war. All foreign markets and overseas investments of the Third Reich were lost, accounting for only 0.5% of western foreign trade in 1947, compared with 10.3% in 1938 before the war, and the economy fell into a severe recession. Before the war, Germany was in a leading position in industrial production and science and technology among European countries. During World War II, Germany's physical assets, such as factories and equipment, suffered a large degree of destruction and loss. But its scientific and technological strength, production organization and management strength, skilled workers are basically still in existence. Under such circumstances, production can be quickly resumed and developed if the necessary production funds and raw material supplies are obtained. Thanks to the strong support of the United States and the interplay of other favorable conditions at home and abroad, west Germany's industrial production, from the monetary reform of 1946 to 1950, recovered to the pre-war level of 1936 in just a few years, and agricultural production exceeded the pre-war level by 2%. Since then, West Germany continued to vigorously strive for "return to the world market", and its national economy entered a period of further development, developing at a faster speed among the big countries. By 1950, Industrial production in FRG had returned to pre-war levels. From 1950 to 1977, industrial production increased by 4.04 times, with an average annual growth rate of 6.2%, only lower than that of Japan in the same period, but higher than that of the United States, France, Britain and other countries. In 1955, FRG surpassed Britain and France in industrial output, second only to the US, and was not overtaken by Japan until the 1970s. It can be seen that such a growth rate in Post-war West Germany is also rare in German history. During the same period, GNP increased more than tenfold from DM 118.6 billion to DM 1.23 trillion. [5] All economic and technical indicators are among the top in the world.

FRG, with its remarkable economic and political achievements, demonstrated to the world the success of another kind of market economy besides the United States and Britain: the social market economy. Originally, the development of German capitalism before the war showed the world a different path from the western countries such as Britain and the United States: from the backward free economy of Weimar period to the national political economy of the Third Reich. Based on this, FRG embarked on the path of economic development that balanced market vitality and social balance. Generally speaking, this model focuses on balancing the market and equilibrium. On the one hand, like other Western countries, it pursues a market economy and advocates free competition. On the other hand, it sees that free competition has its antisocial side. Social market economy advocates state intervention to minimize the possible negative effects of free competition. Set out from the country, establish the frame order of economic activities, attack the appearance of negative factors; Both directly support and support the disadvantaged groups in free competition through redistribution. This balanced system enjoys broad support in German society. Therefore, state intervention is not a limit to market vitality, but a guarantee of free competition. Under this system, not only did free competition not become savage competition, but social policy became consistent with the market economy.

At the beginning of the 19th century, German economy emphasized order while promoting free competition. In the course of development, we pay attention to the construction of strong economic fields and advantageous economic structure. Technology and quality have always been in a leading position, and export has become the main driving force of economic growth. After the interruption of the two world wars, the German economic system, the core elements of which were order liberalism and coordination, was finally pushed to completion.

### 3. The economic situation of east and West Germany after unification

In terms of time alone, although Germany and Germany achieved political unification in a short period of time, the integration of the two different systems was a difficult and tortuous process. Economically, the fundamental motivation for East Germans to pursue German reunification was an immediate improvement in economic conditions. However, this wish has not been fully realized. Even after reunification for a long time, the substantial social and economic integration of east and west Germany has not yet appeared.

#### 3.1 The situation in the east

Germany introduced a new economic constitution in a very short period of time through "shock therapy" and completed the transformation of east Germany's economic system. In addition, in order to promote the economic development of eastern Germany towards the direction of unification, the federal government adopted policies such as "Solar Energy Convention", "Unification Fund" and "Eastern Revival Plan" to promote the construction of eastern Germany. The Modrow government optimistically assumed that the value of GDR enterprises and real estate in the market economy was about DM 400 billion, but this was not the case. East Germany's production potential is estimated at 12-13% of west Germany's, and is mostly obsolete, with only 10% of its equipment capable of producing goods that are competitive in the international market, and with a workforce half as productive as west Germany's, and only a third of the country's businesses profitable. In 1990 the national budget deficit will reach \$120 billion market and the external debt will reach \$35 billion. However, due to the above-mentioned large financial assistance and related measures, the period of economic "maladjustment" caused by the system transition in East Germany was significantly shortened, which promoted the rapid economic growth for three consecutive years. According to statistics: "In 1990, federal aid to the East amounted to DM 150 billion, increased to DM 170 billion in 1991, and reached DM 218 billion in 1992." In the fifth year after the transition, the total amount of funds spent on social security alone was more than half of Germany's GROSS social product, compared with "32% in the United States and 39% in the United Kingdom".

By 1999, productivity in the east was about 32 percent higher than it had been in 1991. After the completion of the economic system transition, east Germany gradually optimized its industry and adjusted its industrial structure, forming a new economic structure dominated by automobile industry, chemical industry and electronic industry. In addition, east Germany's infrastructure was strengthened, especially housing construction and urban construction in East Germany. Infrastructure is being rebuilt at a state-of-the-art level in the five new states and many of the country's ultra hightech investments are being located there.[6] In the early days of German reunification, Kohl promised the East German people that he would seek to bring economic prosperity to the region in a short time. Although system transition has made the above achievements in economic development, its disadvantages are also obvious. The reunification took place in less than a year, and in such a short period of time, it was bound to be radical, leaving a legacy in areas such as national health insurance, education, housing and social security.

Although the GDP of the eastern region had a higher growth rate in the years after reunification, the economy declined after 1994 and had dropped to around 2 %by 1996. Under east Germany's planned economy in the past, employment in East Germany remained at a high level. However, the transition from a planned economy to a market economy has led to the loss of hundreds of thousands of jobs, with the unemployment rate rising from 15.9 %in 1996 to 18 per cent in 1997, averaging 19-20%. Unofficial unemployment estimates for the five new states remain in the 40 to 50 %range, and transfer payments continue to sustain living standards throughout the region.[7] In addition, the difference in wages between East and West Germany was large. For example, civil servants in east Germany earned 10% less than those in west Germany, and processing workers about 15% less than those in West Germany. Wages in east Germany as a whole were only 60 per cent of those agreed in the west. Large numbers of young workers moved from east to west to raise income levels. In the early years of German unification, more than two million people moved from east to west. In the east,

in addition to bustling shopping malls, there are devastated villages. Fast growth zones formed around Leipzig, Erfurt and Dresden, while regions such as Mecklenburg were moribund.

### **3.2 The situation in the west**

All the federal government has done for the east is based on the national income of the west. Excessive care for the east is bound to sacrifice a considerable part of the interests of the west, resulting in increased burden on the west and reduced welfare. Estimates from the Institute for Urban Construction in Bonn and the Cologne Institute for Economic Research suggest that between DM 1.5 trillion and DM 2 trillion are needed to bring eastern production income, employment, environmental protection and quality of life close to those of West Germany. [7] This will not only increase the financial burden of the government, but more importantly, it will be based on the national income of the west, which will inevitably sacrifice part of the interests of the west. Although the Kohl government had previously promised west Germans not to raise taxes, they felt heavy pressure from the government would eventually fall on them. This will not only increase the financial burden of the government, but more importantly, it will be based on the national income of the west, which will inevitably sacrifice part of the interests of the west [8]. Although the Kohl government had previously promised west Germans not to raise taxes, they felt heavy pressure from the government would eventually fall on them [9]. In order to maintain social stability, restore the economy of the eastern region and maintain the sustained economic growth of the western region, the German government adopted the strategy of "high wage – high technology" in the eastern region, in order to gradually reduce the westward migration of the eastern German labor force and reduce the employment pressure in the western region [10]. Achieving this strategy will require trillions of marks to be spent over a considerable period of time, which is not an easy task. In the process of reunification, the government poured 1.1 trillion marks into the east by the end of 1997, eroding its surplus financial base.

### **3.3 Solution**

#### **3.3.1 Adjust the industrial structure and improve the quality of pillar industries**

Germany's industrial structure is unbalanced. At present, Germany's primary and secondary industries in the PROPORTION of GDP is declining. The primary industry accounted for only 1% and the secondary industry less than 30%. The tertiary industry is its leading industry. At the same time, the growth of Germany's tertiary industry is obvious, but its tertiary industry export rate is not high. The industrial structure model driven by the tertiary industry will always be Germany's choice." [11] The value added of Germany's manufacturing industry, which is typically represented by machinery and automobiles, accounts for the highest proportion of its GNP in the world. Among them, luxury cars "made in Germany", such as Mercedes-benz, BMW and Audi, are sold all over the world, and 3/4 of Germany's mechanical products are sold to the global market. The current economic situation means that traditional automobile manufacturing, machinery and equipment manufacturing, electrical and electronic industries, construction and energy industries are facing the pressure of technological upgrading and transformation, and the industrial and supply chains must be integrated and optimized. In addition, as the mainstay of The German economy and accounting for 99% of the total number of German enterprises, SMES are facing great challenges in their development mode under the three major trends of global scale economic effect, accelerated optimization and integration of industrial chain and Internet technological innovation. In view of the large number of small and medium-sized enterprises in Germany, the German government can consider providing targeted assistance to some enterprises leading in the industry or involved in emerging industries, so as to give full play to the advantages of the social market economy system and enhance the competitiveness of enterprises.

#### **3.3.2 Adjust “expanding export strategy” and consolidate and stimulate domestic demand**

Limited by the size of its domestic market, Germany relies heavily on foreign trade, and is a typical export-oriented country. Its exports are mainly automobiles, mechanical equipment, chemical

products and electrical products. In 2018, Germany's total trade volume reached 2.41 trillion euros, including 1.32 trillion euros in exports and 1.09 trillion euros in imports, with a trade surplus of 228 billion euros. According to the statistics of The German Federal Statistics Office, 1/4 of German domestic enterprises depend on foreign export, and 92% of the total amount of German industrial finished products are exported to the international market. Therefore, foreign trade is a crucial part of German economic development. At present, the global economic recovery is weak, Germany's foreign trade bears the brunt, exports continue to decline to record lows. Net exports accounted for at least two-thirds of Germany's GDP growth over the past decade, more than in any other big economy. But such growth is not stable. To maintain its share of GDP, Germany's trade surplus must rise every year. Germany's external surplus reflects a long-term problem: domestic demand is as weak as external demand is strong. Consumer spending has grown by just 0.3% a year over the past decade, weighed down by extended wage restrictions and high household savings. An ageing country like Germany should save more than it invests, creating a balance-of-payments surplus so that it can save in foreign assets to pay for future pensions as its Labour force shrinks. However, Germany's external surplus is too large, and a lot of funds are not used properly and there are problems of waste, such as buying us subprime bonds. So Germany should "reasonably" sell its TREASURIES and invest its foreign currency in more stable emerging markets in search of higher returns.

### **3.3.3 Attaching importance to trans-regional economy and strengthening China-Germany economic and trade cooperation**

In Germany's foreign trade, EU countries occupy an important position, Germany's exports to EU countries account for more than 50% of its total foreign trade. In 2018, Germany's top ten trading partners, except China and the United States, are the Netherlands, France, Italy, the United Kingdom, Poland, Austria, Switzerland and the Czech Republic, all of which are MEMBERS of the European Union except the United Kingdom. In 2018, The total trade volume between China and Germany reached 199.3 billion euros, making China Germany's largest trading partner for the third consecutive year. From luxury cars to the machinery needed to make China the workshop of the world, German companies produce products that meet the needs of the booming Chinese market. Both As suppliers and demanders of globalization, China and Germany have room to expand cooperation. In addition, in the long run, China and Germany should strengthen exchanges in some basic aspects of cooperation, such as talent cultivation and education. There is great potential for cooperation in areas that are more frontier and future industrial directions, such as the environment and energy.

## **4. Implications for the development of Northern Ireland**

Compared with the "golden age" of economic growth in continental Europe under the Marshall Plan after the second world war, Northern Ireland's growth rate is unsatisfactory. The UK's weakness in capital markets, taxation, industrial relations and training systems has led to weak innovation and slow improvements in Labour utilisation. [12] The political turmoil at the beginning of the century made the economy of Northern Ireland suffer a heavy blow. Ethnic, religious, political and other issues affect the economic development of Northern Ireland. Although the Northern Ireland issue is fundamentally different from the reunification of Germany, the economic policies of the Federal German government for the new federal states in the east after the reunification of Germany can give some enlightenment to the economic support of Britain for Northern Ireland:

### **4.1 Expand investment in Northern Ireland to improve employment**

According to the Statistical Research Institute for Northern Ireland, the employment rate in Northern Ireland is consistently about two percentage points below that of the UK as a whole. After being above the UK average in the wake of the 2008 financial crisis, the unemployment rate in Northern Ireland fell below the average again in 2018, to 2.5% in 202. [13] This shows that Northern Ireland faces a problem of underemployment. Considering the economic structure of Northern Ireland, the British government should encourage manufacturing enterprises to invest in Northern Ireland, so

as to expand the employment area of Northern Ireland and encourage people to find jobs. Germany's experience suggests that blindly boosting employment is not an option. A similar strategy of "high wage and high technology" is needed to improve the income of people in Northern Ireland. It is imperative to raise the minimum wage and introduce high-tech industries. A notable example is the complementarity of the pharmaceutical industry in Northern Ireland with local universities, which has directly contributed to the development of Queen's University Belfast's Medical School, which is one of the leading pharmaceutical majors in the UK.

#### **4.2 Construction and renewal of infrastructure to realize the redevelopment of the tourism industry**

The UK government could subsidise infrastructure in Northern Ireland to help improve it. Spending on public infrastructure in Northern Ireland has risen steadily over the past five years, according to the Northern Ireland Institute of Statistical Research. The construction industry is the focus of positive growth, which is self-evident in promoting the manufacturing industry in this region. [14] Tourism has become an important economic driver in Northern Ireland since the ceasefire in the late 1990s. Major tourist attractions include historic cities such as Belfast and Londonderry, as well as the Giant's Causeway in the north. The number of people visiting Northern Ireland before the COVID-19 pandemic also showed a steady increase year on year. Good infrastructure lays a good foundation for the development of tourism. During the pandemic, new and refurbished infrastructure can contribute to the recovery of the tourism industry in the gradual opening up of the post-pandemic era.

#### **4.3 Expand investment in higher education and continue to cultivate high-level talents**

Northern Ireland has only one top-ranked university in the world, a figure that compares poorly with England. According to Queen's University Belfast, there are 10 subjects in the top 200 in the world (QS World University Rankings 2021). Three of those subjects are in the World Top 100 (QS World Rankings by subject 2021).[15] Excellent higher education can drive the rapid development of local economy. The UK government should continue to invest in higher education in Northern Ireland, such as increasing financial support for other local universities and promoting exchanges between excellent universities and ordinary universities, so that the higher education community in Northern Ireland can continue to export high-quality talents.

In a word, when governing Northern Ireland, the British government should focus on fundamentally improving the low productivity of Northern Ireland and coordinating regional development through economic policies, so as to increase the cohesion of various regions.

### **5. Conclusion**

The process of German reunification was tortuous and repeated. From the beginning of the allied countries' occupation of Germany, The German nation once again embarked on the road of unification, which has not been completely finished yet. Up to now, the economic problems behind the unification of Germany are still worth exploring. Some valuable experience can be summarized from the negative influence of the unification of Germany and Germany: before the unification of Germany and Germany, due to the differences in political and economic system and other aspects, as well as the disparity of economic strength, a series of social problems appeared after the reunification, which affected the economic development and social stability of Germany after the reunification to some extent. A series of macroeconomic measures by the federal government have solved many of these problems. Although these policies have the limitations of The Times, they can still be used as a reference for many countries in areas with strong centrifugal force in governance and assistance.

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