

# Comparison of anglo saxon and german capitalism models economics essay



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After the collapse of the Soviet regime the question of types and models of capitalism is widely considered by many economists. All countries have their own approaches and characteristics of the market economy. There are distinguished several models of capitalism on the basis of which the economic policy of the modern states is conducted. This paper focuses on two most common and typical models of capitalism used in modern conditions: Anglo-Saxon and German models. This paper reviews and analyzes two models of capitalism in the sphere of economic relations: corporate governance, financial system, inter-firm relations and the competitive environment, labor relations and employment, workers' training and education, social policy and also innovations.

## **Typologies of Capitalism: Comparison of Anglo-Saxon and German Models**

In modern world economic systems of developed countries, which are called "capitalist" or "market", are not the same and differ politically, socially, and economically. In economic science the question often arises on how many models of capitalism there are? The national economy of any state is unique, but there are general principles of economic organization that help to single out several models. Moreover, these models are called differently by various authors, and their number varies from two to five. But the most studied and recognized are the two models of capitalism: Anglo-Saxon and German. Each of these models of capitalism differs by the types of economic agents, organizational design and approaches to solve socio-economic problems.

The comparison of these models involves studying the model of institutional decisions. How are the relationships between the employee and the

employer regulated? What are the main sources for investment of the firms? Who pays for the employee's skill trainings and their further improvement? Within the limits of economic processes characteristic of economy of any country there are recognized some basic spheres of economic relations. Their institutionalized registration distinguishes one type of capitalism from the other. This paper analyzes two models of capitalism – Anglo-Saxon and German ones, and the main line of comparison here is the scope of economic relations: corporate governance, financial system, inter-firm relations and the competitive environment, labor relations and employment, workers' training and the system of trainings, social policy as well as innovation.

The emergence of the different types and models of capitalism became particularly acute after the collapse of the Soviet regime. The first models of capitalism have been presented in the book of the French economist Michel Albert *Capitalism Versus Capitalism* and later on the typology of capitalism has been more thoroughly explored and substantiated in the book of Peter Hall and David Soskice *Varieties of Capitalism*. According to Hall and Soskice (2001) there are two types of market economy – liberal and coordinated. Liberal economic is inherent in the American model of capitalism, and the coordinated one is in the German model. Hall and Soskice treat in detail each of the two models in the framework of economic agents-firms, they conduct a comparative analysis of American and German companies and consider the main areas of their business. In modern economic science there is a broad classification of models of capitalism on certain grounds. Thus, for example, after M. Albert certain researchers assigned the names of countries to some economic models depending on what country this model is more

characteristic of. Therefore there appeared such terms as “ Anglo-Saxon”, “ Japanese”, “ American”, and “ Rhine” models of capitalism. Hall and Soskice single out a special group of the countries – France, Italy, Spain, Portugal, Greece, and Turkey which they define as “ the Mediterranean” type of capitalism: “...marked by a large agrarian sector and recent histories of extensive state intervention that have left them with specific kinds of capacities for non-market coordination in the sphere of corporate finance but more liberal arrangements in the sphere of labor relations” (Hall & Soskice, 2001, p. 21). M. Orru, N. W. Biggart and G. Hamilton (1997) in the book *The Economic Organization of East Asian Capitalism* consider features of economic systems of the Asian countries and enter the term “ Asian capitalism”. According to the principle of dominance of economic ideology there is distinguished liberal and non-liberal capitalism, the latter one was widely considered at the example of Germany and Japan case in the book of W. Streeck and K. Yamamura *The Origins of Non-liberal Capitalism. Germany and Japan in Comparison*. In terms of economic ideologies Boyer R. underlines the term statism, which belongs to the economies of such countries as France and Italy and is characterized by a large government role played in the economy of the state (Boyer R., 1997). From a position of coordination of economic activities there is distinguished coordinated and uncoordinated market economy. As Soskice noted (1999) in coordinated market economy there is an interaction between economic agents and the state in the course of regulation, but the uncoordinated market economy is characterized by self-regulation of the market. In frameworks of coordinated market economy Hall and Soskice (2001) distinguish industry-based coordination in Germany and group-based coordination in Japan and South

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Korea (p. 34). The questions of standardization, technology, and labor relations in Germany are solved by business associations and trade unions, which according to Hall and Soskice (2001), "...are organized primarily along sectoral lines...by contrast, the business networks of most importance in Japan are built on keiretsu, families of companies with dense interconnections cutting across sectors..." ( p. 34). Thus, in Japan and South Korea economic questions are solved within business – groups.

Corporate governance is carried out by managers and employees of the company in order to achieve effective operation of the company and ensure their own interests. Corporate governance in the Anglo-Saxon model is conducted in the interests of shareholders. It aims at maximizing the profits of the company. In the Anglo-Saxon model the structure of ownership is greatly diversified and blurred; the small shareholders dominate. A large proportion of shares ownership belongs to individuals. In the German model the interests of not only shareholders but also other interested groups are taken into account, i. e. managers, employees of the firm, the state, and also business partners who the firm cooperates with. If in the Anglo-Saxon model the governance is in a dispersed ownership, i. e. the owners of shares are not only small shareholders, but also institutional investors – insurance, retirement, investment and other funds, then in Germany owners of shares are the major shareholders who are directly involved in the management of a company (Hall & Soskice, 2001). " Thus the types of investors generally taking smaller share-holdings account for 80 per cent of shareholdings in Britain" – indicate Hall and Soskice (2001, p. 342). Small shareholders are interested primarily in maximizing their own dividends, which does not

always correspond to the needs of the company for successful development. If we compare the activities of American companies that develop business which primarily take into account the interests of shareholders, the companies in Germany operate on the basis of social responsibility for the employees which is the hallmark of the German model of capitalism.

The financial system is a set of institutions and plays a major role in financing businesses. Financial institutions include banks and stock markets, which act as intermediaries in the transformation of monetary assets in the investment. In German model the financial system is focused mainly on banks, in Anglo-Saxon model it is focused on the share markets. Even during the 1980s the concept of “one firm – one bank” relationship existed in Germany (Allen, 1994, p. 11). So as Vitols S. (2001) informs the share of the banking system in total financial assets of the economy is 60-70% in Japan and Germany, while in the U. S. it is less than 25% ( p. 173). Unlike American companies, in German companies the main sources of financing are long-term bank loans. In German model, as claims Allen (1994), “the financial system – has been dominated for years by a small number of huge universal banks (Deutsche, Dresdner, and Commerz are the largest) – universal because they perform all financial functions...” (p. 11) In the Anglo-Saxon model the enterprises depend more financially on securities markets, “where dispersed investors depend on publicly available information to value the company. This applies both to bonds, share issues, and bank lending” – explain Hall and Soskice (2001, p. 28). The stock market is more liquid than the market of promissory notes. The efforts of managers are mostly focused on increasing the market value of shares of the company as the main

criterion for success of the company is the growth rate of shares. In the Anglo-Saxon countries the stock market, as a rule, is the market of small shares that affects the volume of trade in equity securities and their liquidity. The main disadvantage of targeting the stock markets is that the stock markets are not always able to objectively evaluate the financial condition of the firm - the problem of asymmetric information.

The system of industrial (labor) relations includes institutions that are involved in hiring employees and the use of labor. The German model is characterized by the big role of trade unions played in regulation of industrial relations. The collective negotiations at branch and national levels are conducted between trade unions and employers. Thus, unions act as the representatives of the working class and respect their interests. One of the most important tasks in the sphere of labor and social relations for a social market economy is to avoid the process of turning a person, as a factor of production in the economy, into a tool. It is necessary to observe and improve the personal non-property and moral rights in the process of economic activities. Therefore, the order of labor and social relations requires the protection and care of health, human dignity and the right to self-realization. All above mentioned is governed by the norms of social protection. For example, there are rules concerning assurance with regard to working time and space, safety, protection from hazards, etc. There are two parallel systems that regulate labor relations between workers and employers in Germany. According to Allen (1994, p. 7), these are institutionalized and legally enshrined systems that allow employees to participate in the ownership and management of enterprises, and also the

system of strategic “codetermination”, which means representation of employees in the supervisory board. These systems apply to all employees, regardless of their belonging to trade unions, and workers’ representation on the board can reach half of its composition. In Germany institutes regulating labor relations are represented by such organizations as Federal Association of German Industry, Federal Association of German Employers, and the Chamber of Commerce (Allen, 1994). The body representing the interests of hired workers – work council – is also established. The Anglo-Saxon model of capitalism is characterized by flexible labor markets and the provision of an individual employee’s salary, at the same time there is a high differentiation between the wages of employees and senior staff – managers of the company. As Hall and Soskice explain (2001):

In the industrial relations arena, firms in liberal market economies generally rely heavily on the market relationship between individual worker and employer to organize relations with their labor force. Top management normally has unilateral control over the firm, including substantial freedom to hire and fire (p. 29).

Thus, unlike the German model the Anglo-Saxon one is characterized by the decentralization of labor relations, short-time hiring of the employees and weak acting of trade unions and work councils.

Forms of inter-firm relations determine the nature of competition in the market. The German model known for its non-liberal views on the economy is characterized by closer inter-firm linkages, long-term cooperation, and coordinated interaction. In Germany and other European countries business



self-regulation function is carried out by professional associations, while in countries with liberal capitalism the inter-company relations, as Hall and Soskice argue (2001) “ are based, for the most part, on standard market relationship and enforceable formal contracts” (p. 30). In Germany banks are involved in the ownership and management of enterprises, and in the United States it is prohibited by law. The Anglo-Saxon model is the model of liberal capitalism, which treats businesses and companies as independent, autonomous economic agents characterized by highly competitive relationship in the market. U. S. firms carry out one-time deals, avoiding long-term commitments. Therefore, the labor market is more flexible in the conditions of changing market, and is also characterized by larger turnover of staff.

With the emergence of modern capitalism, with the development of market relations the role of social protection increases and new institutions appear that provide social protection of the citizens. Polanyi argued “ that social protection rescues the market from itself by preventing market failures” (as cited in Hall & Soskice, 2001, p. 145). In the XX century in the modern market economies there takes place the establishment of the welfare state, which represents a set of institutions whose primary purpose is to provide social protection of population through the redistribution of income. The Danish sociologist Gosta Esping-Andersen has developed a general typology of models of the welfare state; along with liberal and conservative models he also highlights the social-democratic one. According to him in Sweden, Finland, Norway, Denmark and the Netherlands there is a social-democratic model characterized by high costs from the state, redistribution of the

incomes to the poor by maintaining a strong fiscal policies to equalize incomes of population (Esping-Andersen, 1990). Attitude to social protection radically differs in two models of capitalism: Anglo-Saxon and German. In the Anglo-Saxon model the degree of social protection is at the minimum level, contemporary liberals see the violation of the laws of the market and individual freedom in the excessive social protection. Therefore, the state's role played in the social protection of citizens is minimal, and is directed only towards the neediest. And as a consequence the liberal countries have a high level of social stratification of the population. Achieving wealth is generally provided by maintaining an efficient economy in the country and the development of systems of private insurance. The German model is a model with a socially oriented market economy. Unlike the Anglo-Saxon model the special attention is paid to the social protection, since it is a basic prerequisite for effective economic policy and mechanism for investment in human capital. Such countries as Germany, Austria, France, Italy and others are characterized by a large differentiation in rendering social assistance, for example, depending on seniority, or the industry which the employee is engaged in (Esping-Andersen, 1990). The social market economy in the German case has demonstrated its effectiveness and we can say with certainty that it provides a more technical, civilized, economic and social progress than any other less free and socially-oriented economic structures.

The system of education and training is an important element in the economic sphere and is responsible for training of workers and professionals. As the system of educational institutions, it provides the economy with the necessary skill formation. In the German model of capitalism, the education

system is characterized by strong vocational training of staff and their acquiring all necessary knowledge and skills within the firm. The vocational training sphere also includes standardization and certification of skills within branches. According to Hall and Soskice (2001) " Germany relies on industry-wide employer associations and trade unions to supervise a publicly subsidized training system" (p. 25). In the Anglo-Saxon model the education system has formal character when it is possible to receive general professional skills (Hall & Soskice, 2001). They are available to everybody and are well represented in the labor market characterized by high turnover of labor. Therefore, in liberal countries, employers are not interested in investing in their employees so that they could obtain special education. This is a personal initiative of the employee interested in his/her professional growth and further promotion. Thus, unlike the German model which is characterized by a restricted vocational training of the employees, by the high proportion of investment by firms and enterprises, the Anglo-Saxon model is characterized by getting generic skills through formal education. Investments into educational preparation of the worker are made by personal investments of the individual.

Organization of the innovation process plays an important role in the economic policy of modern states. Within Anglo-Saxon model the management system is focused on radical innovations which entail high risks. In such fast-growing and high-tech industries such as corporate finance, telecommunications, advertising, entertainment, biotechnology, semiconductors, computer soft and others it is characteristic to use radical innovations, which are implemented in countries with liberal economies (Hall

& Soskice. 2001). Realization of business ideas in innovative process is carried out at the expense of venture financing. It seems to be one of the reasons that can explain a large proportion of venture capitalists in these countries. The German model is characterized by orientation to the long-term projects, which results in the development and application of improving innovations. At the same time the introduction of improving innovations is effective in manufacturing technology, equipment and long-term use goods. In the process of realization of improving innovations the workers and employees of the enterprises are also involved along with other interested parties.

Thus, on the basis of the comparative analysis mentioned above it is possible to list distinctive features in the process of management between the German and Anglo-Saxon models of capitalism. The Anglo-Saxon model is primarily a public company with lots of small shareholders, where the corporate governance is conducted in the interests of minority shareholders in a dispersed ownership. This model is characterized by risk-taking decisions, less business dependency on the state, open economic borders, great significance of the stock market in financing businesses. At the same time the financing depends on market conjuncture. Stand-alone companies are focused on one-off transactions in inter-firm relations. Other features are the maintenance of intense competition and the application of antitrust actions governed by the law. In sphere of industry relations there is a high level of decentralization, short-term hiring, and flexible labor markets. Vocational training of workers is carried out at the level of general knowledge and skills obtained within the limits of formal education. The

further specialization of employees depends on the individuals themselves and their possibilities to invest in their own education. The basic difference is the minimum role of the state played in social protection, and also a low level of activity of the basic institutes of the welfare-state. The innovative and scientific process is carried out by radical methods and is concentrated basically in highly developing and hi-tech branches.

The German model is a non-liberal, coordinated and socially oriented model of capitalism. Within the firm the corporate governance is carried out both in interests of shareholders, and interested groups – hired workers, business partners, local communities, the state, etc. In financing the enterprises the main role is played by the banks, meanwhile the central bank has the full autonomy. In the sphere of inter-firm relations business – associations and business networks play the important role in definition of the character of the competitive environment.

German firms differ by high level of cooperation. The characteristic feature is the regulation of labor relations by the developed institutes, in particular trade unions, and social norms. The big role is assigned to vocational training of employees. The enterprises are interested in financing of education and the further specialization within the limits of professional preparation of the employees. Innovative process is focused on improvement of available technologies. The German model differs by the socially focused economy, strong social policy, developed systems of social protection of citizens and high level of redistribution of incomes.