



## **Climate Change, Digitisation and Globalisation – does the Social Market Economy need Renewal?**

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- › In light of current challenges – particularly climate change, digitisation, globalisation and not least the COVID-19 pandemic – the Social Market Economy faces calls for renewal.
- › The founding fathers of the Social Market Economy – particularly Alfred Müller-Armack – regarded the Social Market Economy as an evolving economic and social order that can and must constantly be adapted to current challenges.
- › Even though the Social Market Economy could not account for present-day challenges at the time of its initiation, it is possible to derive policy recommendations from its values and principles. Its detailed elaboration is part of a societal negotiation process.
- › The Social Market Economy is capable of addressing economic and societal challenges. A renewal of the Social Market Economy is necessary in the sense of adapting the free regulatory framework – its values and principles are yet timeless.

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## Introduction

The Social Market Economy has proven to be a stable and successful economic and social order. In light of current challenges, however, there are increasing calls for a renewal of the Social Market Economy. This has come out most clearly in discussions on climate change: some claim that the Social Market Economy would need to be refined to a “Eco(logical)-Social” Market Economy to be able to address climate change.

Whether climate change, digitisation, globalisation and addressing a pandemic – the key debate is whether the Social Market Economy is up to date viz. in a position to address economic and social challenges of our time. This paper argues that the instruments of the Social Market Economy must be adapted to current challenges – yet the values and principles of the Social Market Economy are timeless. The exact policy design is up to societal negotiating processes.

## Part I: Foundations of our economic and social order: Social Market Economy as a free, evolving order

The conceptualisation of the Social Market Economy as an economic and social order mainly took place in the 1940s to 1960s. At the time, many of the present-day challenges such as climate change, digitisation and globalisation were not yet foreseeable in their current magnitude. Yet a closer look at our economic and social order shows that the Social Market Economy is timeless and adaptable.

The Social Market Economy is not merely a free market economy with a “social appendix”, but rather a normative model where human beings and their freedom take centre stage. The purpose of this economic and social order is to “link the principle of freedom on the market with that of social balance”.<sup>1</sup> Human beings are regarded as God’s creation and thus entitled to freedom and responsibility. Human dignity constitutes and limits human freedom: the state should trust its citizens to develop their freedom and empower them to do so, but at the same time prevent them from harming others. This requires the state to set rules and ensure compliance. The state is, so to speak, both rule-maker and referee. A democratic state is most capable of this task.

The concept of Social Market Economy is based on Ordoliberalism and Christian social teaching.

At the economic level, the model outlined above is best realised in a market economy in which a strong state ensures and protects competition. Competition satisfies the (material) needs of consumers most efficiently and creates “prosperity for all”: competition between suppliers ensures good quality at reasonable prices and rising wealth for everyone. In the long term, competition leads to innovation, quality improvements and falling prices. The luxury of today

The role of competition

becomes the standard of tomorrow. A good example of this is the development of the mobile phone: whilst the first phones were rather big, unaffordable and not very mobile, the smart-phone of today has become an affordable mass product. Competition played a major role in this evolution as producers developed ever better, more functional and more affordable models to please their customers.

By contrast, concentrations of market power and lack of competition tend to hamper progress and cause higher prices. The state has to set a regulatory framework for competition within which economic actors can act freely – it sets the rules and ensures their compliance as a neutral “referee”. Walter Eucken’s constituent principles of competitive order are the corner stone for a functioning competitive order that creates wealth; his regulatory principles define occasions and rules for state interventions in case of market failure or distortions of competition.<sup>2</sup>

The role of the state

The regulatory principles – i.e. the tasks of the state – include the preservation of competition via monopoly control and the internalisation of external effects. External effects are third party effects that are not included in the price. The state should internalise these effects – i.e. integrate them into the price mechanism. Further tasks of the state include empowering people to freedom and responsibility – e.g. via education – so that individuals can assert themselves on the labour market and make a living.

Those who are not able to make a living – e.g. due to age or illness – should be able to lead a dignified life through social benefits (solidarity principle). The state or the community provides educational and social benefits for those in need via redistribution of tax revenue. A progressive, fair tax system based on merit is essential: strong shoulders should also bear a comparatively higher tax burden and thereby support the community; those who merit more should, however, still have more disposable income. This form of solidarity is however strictly limited to those who cannot provide for themselves and their families (subsidiarity principle). Freedom, responsibility, subsidiarity, solidarity and orientation towards the common good represent timeless values of the Social Market Economy; Eucken’s principles of competitive order lay the foundation for the economic order.

Solidarity and  
subsidiarity principle

Despite these values and principles, the Social Market Economy is not a “closed”, set-in-stone concept that can be applied mechanically. Alfred Müller-Armack, who coined the term Social Market Economy, regarded this economic and social model as “a progressive style, an idea waiting to be given shape”:<sup>3</sup>

The evolving character of the Social  
Market Economy

*“According to its conception, the Social Market Economy is not complete; it is not a patent medicine that, once it has been prescribed, can be used in the same way for all time. It is an evolving order in which, besides the firm principle that everything has to take place within the framework of a free system, it is continually necessary to emphasise different things, in accordance with the requirements of a changing time.”<sup>4</sup>*

The Social Market Economy must therefore be constantly adapted to new challenges. In other words, the state has to adapt the regulatory framework to current challenges on the basis of the fundamental values and principles of the Social Market Economy.

The Social Market Economy is hence explicitly able to address social problems which go beyond economic issues. Alfred Müller-Armack spoke of a “second phase” of the Social Market Economy, in which economic policy is a means to reaching societal goals beyond satisfying people’s material needs. Among these goals he numbered – back in the 1960s – environmental policy, European integration and development assistance.

The “second phase”  
of the Social Market  
Economy

A further aspect of this “second phase” of the Social Market Economy is, according to Alfred Müller-Armack, “social irenics” – i.e. the reconciliation of capital and labour, e.g. on the basis of partnership in collective bargaining. Ludwig Erhard, too, aimed to reconcile the interests of interest groups in a concept he called “formed society” – and to prevent politics from being captured by single interest groups. According to him, (economic) policy should be based on the interests of society as a whole as opposed to satisfying contradictory particular group interests. He saw the “formed society” as consisting no longer of classes or groups with contradictory goals, but rather as consisting of common interests and cooperation agreements. Yet “only on the foundation of a healthy economy can society fulfil its actual and ultimate goals”.<sup>5</sup> Economic aspects of the Social Market Economy must be taken into account when striving for societal goals and overcoming current challenges.

## Part II: The adaption of the Social Market Economy in view of ecological, digital and global challenges

### 1. Ecological challenges

The evolving character of the Social Market Economy puts it in an ideal position to address present challenges without neglecting its values and principles. The challenge of climate change illustrates this point. Experts largely agree that pricing greenhouse gas emissions is necessary for reaching climate targets. This approach conforms to the Social Market Economy: Walter Eucken’s regulatory principle of “economic calculation” prescribes internalising external effects into the price mechanism. Greenhouse gas emissions constitute external effects as they pollute the environment, cause climate change and thereby impact on third parties. Yet these social costs are not included in the market price. Accordingly, the state should give greenhouse gas emissions a price tag by integrating them into the price mechanism, making environmental impacts of economic activities visible.

Which carbon pricing model is most suitable, however, cannot be derived from this principle. It is still questionable whether carbon pricing on its own is sufficient to cope with climate change or whether other policies such as state research policy must be added. Regardless, these objections do not undermine the appropriateness of our economic and social order, but rather illustrate the need for a societal negotiating process in accordance with the “second phase” of the Social Market Economy that takes economic, ecological and social aspects into account.

Ludwig Erhard’s reminder that social goals like a sustainable and greenhouse gas-neutral economy can only be realised on the basis of a healthy economy illustrate the necessity of considering economic aspects when fleshing out the regulatory framework. Equal consideration must be given to economic, ecological and social aspects. Furthermore, it is necessary to remember the reconciling [irenic] character of the Social Market Economy – the Social Market Economy can reconcile the “economic” and the “ecological”, something that appears particularly important in the current polarised debate. The Social Market Economy is thus *per se* sustainable through involving and reconciling economic, ecological and social aspects – and does not need to be conceptually extended to an “Ecological and Social Market Economy”.

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Carbon pricing as a regulatory approach to cope with climate change

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The Social Market Economy as a compass to a sustainable society

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Sustainability as a component of the Social Market Economy

## 2. Digital policy challenges

The case of digital platform monopolies also illustrates that the Social Market Economy is still up to date and is able to give guidelines for addressing current challenges. The market power of large digital platforms (which is sometimes abused) confronts economic policy with new challenges. Although platforms – particularly comparison shopping websites – can intensify price competition between providers or innovative competitors, digital platform markets tend towards enormous concentration of market power and have “winner takes it all” characteristics – to the point where single platforms obtain monopoly status or comprise the entire market.<sup>6</sup>

The fundamental values and principles of the Social Market Economy still exist in digital platform markets. Big platforms only increase prosperity as long as they have to compete with other players. As soon as they abuse their market power, set up entry barriers and “swallow up” smaller competitors in order to prevent competitive and innovative pressure, state interventions in digital markets become necessary. In particular, regulators need to stop market dominating platforms from taking over innovative competitors and to adapt competition law accordingly – e.g. through broadening the assessment basis by access to data. The current amendment of the Act against Restraints of Competition (“GWB-Novelle”) has already implemented this step at the national level. The disclosure of anonymised user data to create a level playing field would likewise lower digital barriers to entry and foster digital competition.

Walter Eucken considered it “necessary to prevent the formation of powerful players, not only to combat individual abuses of market power”.<sup>7</sup> This seems to apply particularly to platform markets. Current research suggests that the predominance of powerful platforms in “winner takes it all” markets is practically irreversible. Regulators thus need to check whether *ex ante* regulation on top of the *ex post* regulation is necessary – in other words, whether competition authorities should regulate platforms *before* they reach a position of market dominance. An adaptation of the regulatory framework along these lines would be in line with the Social Market Economy.

## 3. Global challenges

The cases of climate policy and the regulation of digital platform monopolies show that the national level alone is no longer sufficient to meet international and global challenges. Global challenges call for global solutions. According to the subsidiarity principle, competences should remain as close to the individual as possible – yet if a problem cannot be resolved at the individual, family, municipal, regional or national level, the global community comes into play. Phenomena like climate change require European and global solutions.

At the same time, we observe a weakening of multilateralism: protectionism and economic nationalism are gaining ground, global organisations are undermined or by-passed. In particular, the blocking of the Appellate Body as part of the Dispute Settlement System of the World Trade Organisation (WTO) undermines a key pillar in the international trade system.<sup>8</sup> This also seems to constitute a challenge for the Social Market Economy: protectionism undermines open markets and fair competition as principles of a functioning competitive order. A “strong state” is necessary for legislation and law enforcement as pillars of the rule of law, but it is lacking at the global level.

Regardless, the principles of the Social Market Economy serve as guidelines. Even without a strong “global state”, commitment to multilateral, rule-based trade is indispensable for prosperity. It is necessary to strengthen international organisations in order to achieve a better enforcement of law and, as second best, to implement the rule of law at the global level. More precisely, Germany and other states could form a “coalition of the willing” to initiate

Social Market Economy and digitisation: platform monopolies

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The regulatory principles remain relevant

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Adapting the regulatory framework: time for *ex ante* regulation?

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Globalisation and Social Market Economy: building blocs of a global order

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Multi- and plurilateralism as regulatory responses to global problems

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the necessary reforms of the WTO and, if necessary, seek plurilateral solutions.<sup>9</sup> European integration or coordination as part of the “second phase” of the Social Market Economy also offers a possible regulatory solution: only a strong EU can appropriately represent German and European interests in a globalised world. The fundamental values and principles of the Social Market Economy thus remain valid in the context of globalisation and offer solutions to resolving global problems.

## Conclusion and outlook

In conclusion, the Social Market Economy still lives up to current challenges. It offers solutions to issues of our time – be it climate change, digital platform monopolies or growing protectionism.<sup>10</sup> As far as the Social Market Economy’s need for renewal is concerned, it is true that an adaptation of the regulatory framework is necessary. Yet the principles of the Social Market Economy set out an economic, ecological and socially acceptable course. Its actual implementation – e.g. whether greenhouse gas pricing will be by a tax or emissions trading – is subject to societal and democratic negotiation processes. There is hence no need for a new economic and social order – the regulatory framework merely requires adaption that is based on the values and principles of the Social Market Economy. The Social Market Economy is more relevant than ever.

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- 1 Müller-Armack, A. (1976) *Wirtschaftsordnung und Wirtschaftspolitik* (Bern: Haupt): 243.
  - 2 For a full explanation see M. Schebesta (2018) *Monitor Ordnungspolitik: Grundlagen* (Berlin: Konrad-Adenauer-Stiftung e.V.). [https://www.kas.de/documents/252038/253252/7\\_dokument\\_dok\\_pdf\\_52829\\_1.pdf/542e0117-7bd4-cdfc-1bd3-639e5bfab04c?version=1.0&t=1539647304933](https://www.kas.de/documents/252038/253252/7_dokument_dok_pdf_52829_1.pdf/542e0117-7bd4-cdfc-1bd3-639e5bfab04c?version=1.0&t=1539647304933) (last accessed on 13.02.2020).
  - 3 Müller-Armack, A. (1976) *Wirtschaftsordnung und Wirtschaftspolitik*: 12.
  - 4 Müller-Armack, A. (1956) “Soziale Marktwirtschaft”, in *Handwörterbuch der Sozialwissenschaften*, vol. 9 (Stuttgart/Tübingen/ Göttingen: G. Fischer u.A.): 390.
  - 5 Erhard, L. (1957) *Wohlstand für Alle* (Bern: Haupt Verlag): 140.
  - 6 For a full account see M. Schebesta (2018) “Digitale Plattformen in der Sozialen Marktwirtschaft”, in: Konrad-Adenauer-Stiftung (ed.) *Analysen & Argumente*, No 312 (August 2018). [https://www.kas.de/wf/doc/kas\\_53371-544-1-30.pdf?180820075144](https://www.kas.de/wf/doc/kas_53371-544-1-30.pdf?180820075144) (last accessed on 23.03.2020).
  - 7 Eucken, W. (2008 [1947]) “Über die zweifache wirtschaftspolitische Aufgabe der Nationalökonomie”, in N. Goldschmidt & M. Wohlgemuth (eds) *Grundtexte zur Freiburger Tradition der Ordnungsökonomik* (Tübingen: Mohr Siebeck): 148.
  - 8 For more background see D. Gregosz & O. Wientzek (2019) “WTO in der Krise – aber nicht am Ende”, in: Konrad-Adenauer-Stiftung (ed.) *kurzum*, No 55 (December 2019). <https://www.kas.de/documents/252038/7442725/WTO+in+der+Krise+-+aber+nicht+am+Ende.pdf/b097c058-1a8f-3f5e-9056-bbf747879d10?version=1.1&t=1579093761629> (last accessed on 23.03.2020).
  - 9 On the WTO reforms see D. Gregosz (2018) “Macht Trump die WTO bald obsolet?” in: Konrad-Adenauer-Stiftung (ed.) *kurzum*, No 19 (August 2018). [https://www.kas.de/documents/252038/253252/7\\_dokument\\_dok\\_pdf\\_53484\\_1.pdf/10c07f62-1dfc-e039-7ffc-d58dbc414826?version=1.0&t=1539647004861](https://www.kas.de/documents/252038/253252/7_dokument_dok_pdf_53484_1.pdf/10c07f62-1dfc-e039-7ffc-d58dbc414826?version=1.0&t=1539647004861) (last accessed on 23.03.2020).
  - 10 A study covering all aspects of the challenges mentioned was not completely possible in this setting.

## Imprint

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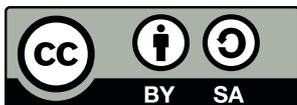
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Publisher: Konrad-Adenauer-Stiftung e. V., 2020, Berlin  
Design and typesetting: yellow too, Pasiek Horntrich GbR / Janine Höhle,  
Konrad-Adenauer-Stiftung e. V.

ISBN 978-3-95721-707-3



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