

# How Do Business Interest Groups Respond to Political Challenges? A Study of the Politics of German Employers

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## Abstract

Social scientists dealing with business and politics have tended to focus mostly on the power of business and less on the political challenges and constraints that business interest groups face. This paper analyses how business interest groups respond to political initiatives that challenge their interests, using four episodes of political conflict in Germany. The paper elaborates a model of response strategies and their likely impact on political outcomes. The model suggests that business interest groups can respond to political challenges in two ways: by seeking confrontation or by pursuing adaptation. The paper illustrates these two response strategies with four episodes of political conflict in the political-economic history of Germany: (i) the adoption of social insurance under Bismarck, (ii) the adoption of unemployment insurance in the 1920s, (iii) the adoption of board-level codetermination in the early 1950s, (iv) and the Agenda 2010 labour market reforms of the early 2000s. These four case studies show that adaptation facilitates social compromise, while confrontation results in a bifurcated outcome, producing either dominance or defeat of business interests, depending on what side government takes. Furthermore, the analysis finds that confrontation tends to be associated with unity of interests within the business community, while adaptation tends to be associated with fragmentation of interests. The discussion emphasises that the role of business in politics should not be seen solely in terms of business ‘influencing’ politics, but also as potentially adaptive.

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This paper addresses the following question: How do business interest groups deal with political challenges? Most research on the political role of business (a short form for business interest groups) focuses on the mechanisms, causes, and forms of business influence in politics. In this vein, there are numerous studies of how business interest groups exert political influence and how successful they are in getting what they want (for example, Bell and Hindmoor 2013; Bell and Hindmoor 2014; Block 1987; Culpepper and Reinke 2013; Fairfield 2010; Marsh and Lewis 2013; Svallfors 2016; van Apeldoorn 2000; Vogel 1989). Business enjoys considerable power, and this power is derived from both structural sources, the dependence of society on investments by private firms, and on instrumental sources, such as lobbying and donations.

Even though business interest groups are powerful, they do however not always get what they want. Business interest groups confront demands by other political actors endowed with power resources, demands that may or may not conflict with how the business community, or segments within it, sees its interests. Thus, the preferences of business interest groups, while influential, do as a rule not determine political decisions.

The most important constraint on business influence is democracy. One major goal of political parties is to win elections. Business people, that is, the owners and senior executives of private firms, constitute a minority of the electorate. Political parties and governments face incentives to comply with business demands – due to the structural and instrumental power of business – but they also face the potentially conflicting incentive of satisfying voter preferences. When preferences of a large share of voters conflict with the preferences of the business community or a large segment of it, policy-makers and parties need to decide whether to side with the respective business interest group or with the respective voter segment. In short, while business interest groups enjoy considerable resources to ensure political influence, both instrumental and structural, other social groups enjoy other sources of influence, in particular those that stem from their larger electoral size. Governments do not necessarily or invariably give precedence to business interests when those conflict with voter preferences. Business interests may therefore possibly be undermined or soundly defeated by large voter segments.

Recent research on business power and influence has focused on factors that may either enhance, undermine or reduce business influence. These factors include the state of the economy and the incidence of economic crises (Vogel 1989; Vogel 1996), the credibility of exit threats (Bell and Hindmoor 2013; Bell 2012), the extent of informational advantages enjoyed by business over policy-makers (Bernhagen 2007), the extent of regulatory competition across polities (Hacker and Pierson 2002), and the salience of policy issues to the public (Culpepper 2011).

These studies provide valuable insights into the sources of variation of business influence. Yet the impact of business interest groups on political decisions depends not only on their influence but also on whether, and if so how, they adapt to the goals of those actors who pose a challenge to their interests, actors whom I call ‘challengers’. The purpose of this paper is to analyse how business interest groups deal with situations where their political clout is weakened by actors who challenge their interests. What do business interest groups do when political challengers are sufficiently strong to constrain business interest groups’ ability to get what they want? How do they respond to these political challenges?

This paper suggests that business can respond to political challenges in two ways: *confrontation* or *adaptation*. Hence, business interest groups might become more assertive and intensify their activities to achieve their goals. If challengers are strong, this will lead to confrontation. Alternatively, business interest groups may assess that an uncompromising attitude is likely to lead to defeat, and may thus moderate their demands; in this case compromise and political accommodation will be viewed as the politically more expedient strategy. The choice of response strategy, confrontation or adaptation, has important consequences for the viability of social compromise, in so far as adaptation facilitates compromise on both sides.

The paper explores the effects of these choices on political outcomes. I argue that these effects will depend on the intensity of the political constraints. The paper proposes a two-dimensional typology: The two dimensions are (a) the intensity of political constraints faced by

business, and (b) the response strategy chosen by business (adaptation/confrontation). The combination of these two dimensions results in a cross-tab with four possible outcomes (see table 1). The paper illustrates this typology with examples taken from the historical development of the welfare state and institutions of codetermination in Germany.

The empirical analysis shows how business' choice of response strategy affects political outcomes. The outcomes possible are modelled as either defeat of business, forms of social compromise, or victory of business. When German business interest groups adapted to political constraints, this often resulted in social compromise where business could shape certain policy details but also had to make concessions. In cases where business opted for confrontation, the political outcome depended on the strength of these constraints. Hence, if the constraints were strong, a confrontation strategy failed and business interests were defeated; if the constraints were weak, confrontation resulted in victory.

More generally, through this analysis, the paper intends to show that a focus on how business responds to political challenges results in a better understanding of the role of business in politics, as compared to an approach that takes business dominance in politics as the norm and challenges to business dominance as insignificant. Taking into account that the strategic choices made by business interest groups are affected by the political challenges they face provides us with a more nuanced understanding of business-politics relations. This understanding takes into account both the power business enjoys, as well as the constraints it faces, with the outcome dependent on a combination of the strategic choices business makes and the political constraints it faces.

The paper is organised as follows: the next section revisits theoretical debates on the role of business in politics, arguing that a focus on response strategies and adaptation complements and improves existing approaches. The third section presents the typology of business-politics relations and spells out its theoretical implications for our understanding of how business and politics interact. The fourth section shows the utility of this typology by applying it to several key policy-making episodes in the development of welfare state and codetermination legislation in Germany. The final section offers a conclusion and discusses possible reasons why business sometimes pursues confrontation, and sometimes adaptation.

## **2. Theoretical debates on business-politics relations**

To understand the role how business interest groups affect the politics and policies in liberal democracies, we need to briefly revisit debates about the nature of relations between business and politics. We can identify two strands of thinking in these debates: power elite theories and pluralist theories. The first strand sees power in politics as located in a coherent, tightly connected social elite that shares a common worldview, an elite within which the owners and senior executives of large corporations form an important part. The second strand of thinking views power structures in democracies as characterised by competition among a multitude of social interest groups, with no one group being able to permanently monopolise power.

We can trace back the intellectual pedigree of these two strands to Karl Marx and Joseph Schumpeter, respectively. In their *Communist Manifesto*, Marx and Engels famously declared that '[t]he power of the modern state is merely a device for administering the common affairs of the whole bourgeois class' (Marx and Engels 1971 [1848]). From the 1960s, a strand of Marxist work emerged that theorises, and to some degree tried to empirically document, the dominance of capitalist interests in politics (Poulantzas 1978 [1973]; Poulantzas 1969; Miliband 1973 [1969]; Jessop 1983). Arguments about business dominance in politics are central also to non-Marxist versions of power elite theory, notably the work of the sociologists Wright Mills (1999 [1956]), Useem (1984), and Domhoff (Domhoff 1996; Domhoff 1990; Domhoff 1967).

The pedigree of pluralist perspectives goes back to the work of the economist Joseph A. Schumpeter and the theory of democracy he developed in Part IV of his book *Capitalism, Socialism, and Democracy* (Schumpeter 2010 [1942]). Central to Schumpeter's view of democracy is the importance of competition for power through a struggle for votes (Schumpeter 2010 [1942]).

According to Schumpeter, the rise of democracy is causally connected to capitalism (Schumpeter 2010 [1942]). Schumpeter emphasised the inability of business interest groups to control democracy because of popular demands of an anti-business character and the empowerment of these demands by democracy (Schumpeter 2010 [1942]).

The pluralist perspective also inspired a rich body of empirical work. Important examples of work in the pluralist tradition are, in particular, the work by David Vogel on the impact of business interest groups in the United States during the 1960s and 1970s in the fields of consumer protection, environmental policies, and occupational health and safety (Vogel 1987; Vogel 1983; Vogel 1989); or the study by Gerhard Braunthal of the Federation of German Industry during the 1950s (Braunthal 1965). Scholars working in the state autonomy or historical institutionalist traditions also utilise a pluralist perspective, often implicitly (Skocpol 1980; Hacker and Pierson 2002; Steinmo 1993; Immergut 1992).

As noted earlier, more recent research turned to variation in business influence and to the identification of the sources of that variation (for example, Bell and Hindmoor 2013; Woll 2014; Culpepper 2011). These studies thus turned away from framing the question of business power as an either/or issue; that is, power elite vs. pluralism; and towards a more empiricist perspective on business power. They suggest a view of business as sometimes, but not always, dominating political decisions. Yet, these studies also maintain an analytical focus on the influence of business on politics, and do not systematically look at the constraints that business has to confront. In this approach, the causal arrows go from business to politics but never vice versa. In reality, business does not always get what it wants. Hence, we lack an understanding of whether and if so, under what conditions, business interest groups adapt to other actors and their demands.

The insight that business sometimes adapts to political opponents, instead of fighting them, first emerged in research on welfare state history. Studies of the social policy legislation of the New Deal era in the United States in particular showed how some segments of business adapted to changes in the political context by trying to influence the planned legislation rather than fight it, although the importance of adaptation and the decisiveness of business involvement for political outcomes remains disputed (key contributions to this debate are in particular Skocpol and Amenta 1985; Hacker and Pierson 2002; Swenson 2002; Gordon 1994; Quadagno 1984; Jenkins and Brents 1991; Domhoff and Webber 2011).

A related strand of research on business and politics shifted the focus from questions of power to questions of preferences. Studies in this strand focus on what business wants, rather than on how successful it is in getting what it wants. The literature on Varieties of Capitalism (VoC), inspired by the framework by Hall and Soskice (Hall and Soskice 2001), provided a major stimulus to this strand. Hall and Soskice expected that in coordinated market economies, major segments of employers will support institutions that underpin coordination among firms, whereby they see social policies as complementing such institutions (Hall and Soskice 2001; see also Rhodes 2005). Others expect that employers in coordinated market economies will support the adoption of social programs because of the type of skills they require (for example, Estévez-Abe et al. 2001). In political economy, Germany is often seen as an archetypical case of coordination (for example Streeck 1997), which makes the country also a crucial case for testing VoC-inspired arguments.

This paper suggests a somewhat different perspective, one which explains employers' support for social programs as a result of adaptation to changing political challenges and constraints, rather than of the needs of production. Germany provides a difficult case for testing this approach in so far as, according to the VoC approach, the institutional framework in Germany is favourable to the dominant segments of business. Hence, we can expect that business in Germany may have to adapt less to political constraints than in other countries.

In the following subsection, the paper presents a typology of business-politics relations that models how different response strategies by business will facilitate different outcomes.

### **3. How does business deal with political challenges? Two alternative strategies**

This section proposes a model for how to categorise business responses to political challenges, as well as the effects of these responses on political outcomes. As suggested earlier, business interest groups can respond to political challenges in two ways: confrontation and adaptation. Confrontation refers to efforts by business interest groups to push back or to defeat initiatives by political challengers. Confrontation can involve a variety of activities, for instance, public campaigning, lobbying, and donations to allied parties. Its defining characteristic, however, is that it attacks the policy proposals and arguments of a challenger head on in order to defeat them.

Adaptation, in contrast, refers to the accommodation of political challengers by making concessions to them. Business interest groups may pursue adaptation in order to exert influence in negotiations where the adoption of a policy cannot be stopped entirely or to pursue prioritised, overarching political goals, such as political stability and social peace, where confrontation would endanger these goals. In subsequent sections, we will analyse the implications of this choice for political outcomes, but first we need to turn to the concept of political challenges.

In this paper, the term ‘political challenges’ is used as an umbrella term for all initiatives by political actors that conflict with what business or a segment of it see as their interests. Political demands that challenge the interests of business can come from diverse agents: labour unions, social movements or political parties, for instance. The existence of such challengers does not in itself pose a threat to the political dominance of business interest groups. What is decisive is the stance taken by the government, that is, whether in a conflict government sides with business or with the challengers. Government itself can also be a challenger or a part of an alliance that acts as a challenger. Within government, it will typically be the ministers in charge, the senior staff in the ministries, and the parliamentary deputies of the governing parties, that decide on what stance the government shall take. Political challenges warrant a response by business only if government sides with the challengers or if government is itself the challenger. Therefore, I call a challenge ‘strong’ if the government sides with the challenger or is itself the challenger, and ‘weak’ if the government does not (that is, if government either remains neutral or sides with business against a challenger).

This argument raises the question: What is business? I use the term ‘business’ as a short form for business interest groups. Business interest groups are political actors that explicitly represent the interest of private corporations, including their owners, shareholders and senior executives. Business interest groups can represent individual firms or groups of firms or even the entire national business community. The representativeness of business interest groups for the entire business community, all private firms in a country, will vary empirically, and a homogenous position for an entire business community cannot be assumed.

The interests of the business community can be homogenous or heterogeneous, depending on the character of the policy issue. On some issues, the business community may be divided, with different segments in conflict. On other issues business may act as a uniform actor. Different interests may also lead to different strategies. Some groups may opt for confrontation, others for adaptation. To give an example, calls by environmentalist groups for stricter emission standards for cars generally pose a challenge to manufacturers of gasoline-driven cars, while producers of electric cars may expect to gain a competitive advantage due to higher costs being imposed on their competitors. In this case, we can expect the two groups to pursue different response strategies, and the outcome to be affected by the balance of political strength among these producers.

This paper treats divisions within the business community as an empirical question rather than theorizing these divisions. We will return to the issue of divisions in the empirical sections and in the discussion (section IV). For the purpose of laying out the basic argument, we will assume in the following section that a dominant segment within the business community exists, one whose influence on government is greater than that of other segments.

#### *3.1 The impact of business strategy on political outcomes: a two-dimensional typology*

We now turn to the question of how the choice of strategy by business is likely to affect political outcomes. The previous section introduced two strategies, confrontation and adaptation, and argued that these two strategies represent alternative responses by business to political challenges. This section presents a fourfold typology of political scenarios, based on these two strategies.

I argue that the effect of the two strategies on policy decisions will differ depending on whether or not the challenger enjoys the support of the government. In principle, we can think of the possible outcomes of a conflict between business and a challenger as a continuum ranging from an outright defeat of business on the one end of the continuum to business dominance on the other end, with variants of political compromise in between.

Which outcome prevails will depend on a combination of two factors: (1) the strategy chosen by business in response to a challenge (adaptation or confrontation); and (2) the stance taken by the government, siding either with business or with the challenger. The interaction of these two sets of factors results in four possible ideal-typical scenarios, which can be represented as a cross-tab (table 1). I call these four scenarios (I) business-led social compromise, (II) imposed social compromise, (III) business dominance, and (IV) business defeat.

[TABLE ONE ABOUT HERE]

These four concepts represent hypothetical political outcomes for each of these four possible scenarios. If government sides with business and business decides to adapt we can expect variant I, what I call a *business-led compromise*. A business-led compromise is a policy arrangement that is engineered by the government and that reflects the preferences of the dominant segment of the business community; however, the business-led compromise also includes some concessions to the challengers, although on terms acceptable to business.

A second possibility is an *imposed compromise* (II), which results if government sides with the challenger and business adapts to that constraint. This is likely to produce a compromise whereby business accepts some policies that it does not favour while also obtaining some concessions or managing to avert actions that would be even less favourable. Imposed compromise differs from the business-led compromise in that the concessions imposed on business are more substantial.

The third possible variant is *business dominance* (III), which results when business seeks confrontation with challengers while government sides with business. In this scenario of offensive confrontation, the adopted policies will not reflect the outcome of a political compromise but solely the preferences of business. In so far as government is subservient to business in this case, this outcome reflects the Marxian thesis of the capitalist state as being an instrument of the needs and interests of capitalists.

Finally, the fourth scenario, *business defeat* (IV) results if business pursues confrontation even though political challengers are strong. In this scenario of defensive confrontation, government sides against business, and business is unwilling to give in despite being in a position of political weakness. The result is a defeat for business.

The typology shows that for business, confrontation is a more risky strategy than adaptation, as confrontation can lead to defeat, and is thus a high-gain/high-risk strategy; while adaptation will result in some form of compromise, thus making extreme outcomes less likely. Confrontation can lead to outright defeat because it excludes the possibility of influencing details of policies through consultations and negotiations, while adaptation, precisely because it requires concessions by all sides, is unlikely to result in outright defeat. For business interest groups that prioritise predictability of political outcomes, there are incentives to opt for a strategy of adaptation. However, confrontation can be a more promising strategy for business either if political opponents are weak (offensive confrontation) or if the stakes are very high for business (defensive confrontation).

Critics of this typology might argue that empirically, business dominance (cell III) is the most prevalent outcome and that those instances in which business confronts intense political challenges are empirically rare. However, the four episodes discussed in this paper, focusing on social policy and industrial relations in Germany, provide evidence of all four types of responses.

The two dimensions, political challenge and response strategy, may be correlated. Business may be more likely to adapt if constraints are strong. We can thus expect that cells II and III will be more populated. While the empirical analysis of this paper documents instances of all four types, the limited number of cases studied does not allow us to make conclusive statements about the empirical distribution of the four types. What we can document, however, is that business adaptation to political challenges occurred in Germany under some conditions, and that the choice of response strategy, adaptation or confrontation, had important consequences for the political outcomes.

#### **4. Political challenges and business response strategies in welfare state history: A case study of Germany**

This section applies the typology described above to four reform episodes from the development of social programs and industrial relations in Germany. The section shows the effect of business interest groups' choice of strategy on political outcomes. Four reforms episodes are presented, two of which are examples of adaptation and two of confrontation. The episodes are: the adoption of work injury insurance in the 1880s (an instance of adaptation), the adoption of unemployment insurance in the 1920s (adaptation), the adoption of mandatory board-level codetermination in 1950/1951 (confrontation), and the reform of labour markets in the early 2000s (confrontation). The analysis will seek to show how the choice of strategy by business, together with different levels of constraints, led to different outcomes, resulting in either a success for business, a defeat of business or a social compromise.

The four episodes are taken from very different historical periods, and we therefore need to ask how the different strategies relate to differences in historical context. The Wilhelmine Empire, the Weimar Republic, and the post-war Federal Republic provided very disparate settings for business-politics relations and for the opponents of business to launch challenges. The Wilhelmine Empire can be described as a semi-democratic monarchy, with free elections but unequal voting rights, whose government was accountable to the Emperor, rather than to the parliament. Relations between the dominant sectors of industry, heavy industry in particular, and the government were friendly and close (see Kaelble 1967), and anti-socialist legislation, in place from 1878 to 1890, limited mobilization by socialist organisations. This was a context where business was in a dominant position and where opponents could hardly launch strong challenges.

The Weimar Republic provides a very different context. Industrialists were now in a much weaker political position. Democratization had enabled the Social Democrats and the Catholic Centre Party to enter government, and unions and collective bargaining were now institutionally protected, in contrast to the Empire. In Weimar, works councils were also now legally mandatory. Business was thus much more constrained. Parts of industry never fully accepted the enhanced role of unions. After World War II, similar constraints continued in the Federal Republic, but the dominant groups in industry were now willing to accept an institutionally protected role for the unions.

The following subsections will document how differences in the strength of political challenges combined with different response strategies by business to produce different outcomes in terms of the degree of business dominance, leading to defeat, compromise or victory for business interests.

##### **4.1 Adaptation to a weak challenge: Bismarck's social reforms**

The introduction of social insurance in Germany during the 1880s was an initiative by the government in cooperation with dominant segments within industry. The reforms consisted of the adoption of three new public programs: accident insurance, health insurance, and old-age and disability pensions.

The dominant segments within business supported these reforms. The large firms in heavy industry were worried about worker militancy. An alliance between heavy industry and the national government drove and shaped the reform project, with a view to pacifying workers and

weakening the appeal of the social democrats. The heavy industry sector had initially wanted to protect its own company welfare programs, but it later agreed to shift responsibility to publicly run programs, seeing a public social policy as a more effective way to secure political stability. Heavy industry's support for public insurance thus reflected an adaptation to the need for political stability. In contrast to the heavy industry sector, German manufacturers were less supportive of the reform, but they lacked political clout since they were still small and less well organised.

The Central Association of German Industry (Centralverband deutscher Industrie, CDI) which was dominated by heavy industry, played an important role in the drafting of the German social insurance bills (Bueck 1903). The executive director of the CDI, Henry Axel Bueck, called the reforms 'a work of civilization of the highest order, which, as a model for all times, will bring [the Empire] honour' (Bueck 1905).

The attention of heavy industry was focused primarily on work injury insurance and less on the other two programs. Lobbying by heavy industry played an important role in the adoption of work injury insurance. The adoption of an employers' liability law in 1871 had created a wave of lawsuits by injured workers against their employers and had fuelled industrial conflicts. The work injury-prone heavy industry thus looked for a way to defuse this source of conflict and to shift the costs of compensation to the broader business community. On 2 November 1880, the executive director of the heavy industry firm *Bochumer Verein*, Louis Baare, assembled a group of like-minded industry representatives to draft a new work injury insurance program (Breger 1994) that would replace employers' liability. The government bill was based largely on this industry-led proposal.

Opinions on the adoption of work injury insurance among the broader business community were mixed. A survey by the Prussian Statistical Office in 1881 found that 53 per cent of all regional Chambers of Commerce backed the government draft, while 39 per cent opposed it (Francke 1881). Yet it was heavy industry that remained the dominant actor within industry. It had cooperated with Bismarck already earlier in the debate about trade protectionism in the 1870s and, unlike other sectors, heavy industry could rely on unified and powerful organizations, particularly the aforementioned CDI.

The adoption of social insurance programs during the Bismarck era shows characteristics of a business-government alliance. The success of this alliance was made possible by the adaptation behaviour of dominant parts of business to the plans of the government and the perceived need to do something about 'the worker questions'. While the reforms were certainly worker-friendly, German labour unions and Social Democrats had little influence on the actual adoption and design of these programs. Although the reforms were motivated by a fear of labour militancy, the organizations of the labour movements were still very weak at that time, compared to later periods. The growth of the labour unions did not start before the 1890s, and anti-socialist legislation, adopted in 1878, stifled political mobilization by the newly founded Social Democratic Party. During the entire period of reform (1878-1889), the Social Democrats never held more than 12 per cent of the seats in parliament.

Heavy industry exercised an authoritarian approach of labour management (Büren 1934) and was not yet constrained by a collective bargaining system. The political influence of heavy industry was at its peak during the Wilhelmine Empire and would never again achieve such strength in later periods. Heavy industry's fear of a potential future strengthening of the labour movement and an intensification of class conflict motivated it to promote social reforms rather than the actual strength of organised labour. In pre-empting organised labour, heavy industry also succeeded in shaping many details of the new laws, such as the exclusion of union funds from the new public health insurance program.

In sum, the adoption of work injury insurance, health insurance, and old-age pensions under Bismarck was the product of a business-government alliance, and both sides responded to the perceived challenge of labour militancy. Key segments of the business community; heavy industry in particular; actively backed this reform project and shaped the details of the new social



programs. The character of the reforms as a social compromise was implicit, as industrialists expected workers to acquiesce and to turn away from the Social Democrats as a result of better social protection. One employer representative, for instance, remarked that ‘the best way to weaken the power of the Social Democrats is to fulfil that part of their demands that every philanthropist must accept as legitimate’ (Oechelhäuser 1889).

In short, the political challenges to which business adapted were more imagined than real. The perceived challenge of labour radicalism united government and the dominant segments within industry to cooperate in the formation of social insurance programs.

#### **4.2 Adaptation to a strong challenge: the adoption of unemployment insurance**

The adoption of unemployment insurance in 1927 is one example of a political compromise that was accepted by the main business federations in the face of a clear parliamentary majority in favour of the reform. Initially, all business interest groups strongly opposed unemployment insurance. When it became clear that the passing of the law could not be stopped, the main business federations decided to cooperate with government elites to hammer out details of the bill. By supporting a compromise, German business could secure concessions on details that mattered to them.

The initiative for the bill came from the Ministry of Labour and its head, Heinrich Brauns, a priest and member of the Catholic Centre Party. The democratization of the political system with the Weimar constitution (1919) and the participation of the Social Democrats and the Centre Party in government had resulted in a parliamentary majority for the adoption of unemployment insurance. This situation was in stark contrast to the period before 1918, when no such majority existed. Moreover, the main unions backed a public insurance program after 1918, when the unions’ own compensation schemes (known as the ‘Ghent model’) became financially unviable.

During the Wilhelmine Empire (1871-1918), all groups of employers had been staunchly opposed to any form of support to the unemployed, primarily because they feared an erosion of work incentives due to an increase in workers’ reservation wage, that is, the wage level below which unemployed workers are expected to refuse a job offer (Zahnbrecher 1914; Reisswitz 1904). Employers suspected that the possibility to obtain unemployment benefits would induce laziness and reduce labour supply. After the First World War, the political context had changed for several reasons: first, during the war, a means-tested program for assisting the unemployed had been introduced, initially only for the period of the war, but effectively made permanent after the war. Second, the pro-welfare parliamentary majority and the participation of pro-welfare parties in government made the dismantling of this program unfeasible.

During the early years of Weimar, employers initially maintained their opposition to unemployment insurance. Over time, however, they came to realise that opposition was pointless. The two main employer federations, the Federation of German Employer Associations (VDA, Vereinigung deutscher Arbeitgeberverbände) and the Federation of German Industry (Reichsverband deutscher Industrie, RDI), eventually decided to cooperate with the ministry and the unions in hammering out the details of a bill for unemployment insurance. With this strategy, the two employer federations hoped to be able to dilute some of the more unpleasant aspects of the planned program and influence those provisions of the bill they particularly cared about, such as making benefits conditional on employment record, control of benefit recipients by the public labour exchanges, and the involvement of the employers’ associations in the administration of the new program. In all these respects, employers got their way.

Parliament passed the bill based on the draft worked out by unions and employers in June 1927. The bill had the support of the Social Democrats, the Centre Party, and two smaller centre-right parties (German People’s Party and the German Democratic Party), which together held 57 per cent of the votes.

The strategic motives of the business federations are documented in archival sources. On 16 December 1929, the social policy committee of the RDI, by a vote of 16 to 5, decided to

abandon its opposition to unemployment insurance. The chair of the committee, Hubert Hoff, pointed out that unemployment insurance would be the lesser evil compared to unemployment assistance, because 'if ...unemployment assistance continues, the employer has no influence over the use of the funds.' At the same time, Hoff considered a dismantling of unemployment assistance without any replacement as unrealistic; thus, unemployment insurance was seen as the lesser evil (RDI 1921). Similarly, the social policy committee of the VDA, in a meeting on 27 January 1925, decided that a continuation of opposition would stand 'no reasonable chance' of success (VDA 1925).

The adoption of unemployment insurance resulted from a compromise between employers and unions, engineered by the ministry, in the shadow of a clear majority in parliament. Employers grudgingly cooperated because they knew that a majority in parliament supported the introduction of unemployment insurance and that the government could thus go ahead unilaterally. The business federations thus adapted to political majorities and the government's plans, thereby enabling a compromise solution.

#### **4.3 Confrontation of a weak challenge: labour market reforms in the 2000s**

The labour market reforms in Germany during the early 2000s provide an example of business choosing confrontation and succeeding in its goals due to weak political constraints. Many economists attributed high unemployment in the 1990s to tightly regulated labour markets and high non-wage labour costs associated with high social expenditures (for example Sinn 2003). During the 1990s, academic and journalistic observers of German politics diagnosed a deadlock in the reform efforts due to the semi-sovereign character of the German state with its many veto points (for example Streeck and Trampusch 2005).

Nevertheless, the reforms were ultimately enacted. The Social Democrats came to power in 1998 with a promise of lowering unemployment. The Government, consisting of Social Democrats and the Greens, initially aimed to hammer out a negotiated reform of labour markets through a tripartite body, known as the Alliance for Jobs, formed in 1998. These talks failed due to deadlocks between unions and employers. The employers threatened to leave the talks, stating that the unions' proposals did not go far enough to lower labour costs and liberalise labour markets (*Der Spiegel*, 1 March 1999: 26). Employers and unions both supported financing of social insurance through payroll taxes, but the two sides were at odds on the issue of deregulating labour markets and facilitating new forms of less protected low-wage employment.

After the failure of the Alliance for Jobs talks, the Schröder government set up an expert committee mandated to work out proposals for labour market reforms intended to create jobs, known as *Agenda 2010*. Business representatives played a prominent role in the committee, which was chaired by the personnel director of Volkswagen, Peter Hartz. Experts from the business consultancies of Roland Berger and McKinsey were among the members. Unlike in the Alliance for Jobs talks, the unions held no veto rights. Only two of the twenty-one members came from the unions.

The proposals of the committee focused on strengthening work incentives, activation of the unemployed, and expansion of low-wage work, that is, supply-side reforms that were fully in line with the demands advanced by the Federation of German Employer Associations (BDA 2005; BDA 1998). The most controversial component of the committee's proposals was the partial replacement of unemployment insurance for the long-term unemployed with a means-tested benefit (*Arbeitslosengeld II*).

During the 1990s, the employer associations had begun to conduct and finance public campaigns to deregulate labour markets; one example are the activities of the employer-funded think tank 'Initiative New Social Market Economy' (Kinderman 2005; Menz 2005; Kinderman 2016). Campaigns like these aimed at increasing public support for labour market liberalization and lower labour costs.

In this case, the political constraints were weak. The measures proposed by the Hartz committee were in line with the demands issued by the Federation of German Employers

Associations (Bundesvereinigung deutscher Arbeitgeberverbände, BDA), the Federation of German Industry (Bundesvereinigung Deutscher Industrie, BDI) and other employers' associations.

Opposition to the reforms came from the left wing within the SDP and from some of the unions. The unions were divided into a traditionalist camp, led by the metalworkers (IG Metal), and a modernizing, reform-minded camp, led by the chemical and mining workers (IG BCE). Thus, the government, under the impression of high problem pressure, decided it could afford to ignore the opposition to the reforms (Hassel and Schiller 2010). In parliament, a broad coalition that included the Christian Democrats and the Free Democrats, both in opposition, backed a deregulation of labour markets. In short, the Agenda 2010 labour market reforms were a case where the government ended up siding with the declared preferences of the dominant segment within the business community. This emboldened employers to pursue a strategy of confrontation of the opponents of the reform, and at the same time the need for adaptation was weak.

The employer associations pursued a strategy of confrontation from a self-aware position of strength. This strategy took the form of vociferous public campaigning for lower labour costs, easing of regulations to create low-wage jobs, more flexible types of employment, and stricter job search requirements for the unemployed. Given the favourable context, this strategy of confrontation was successful. A recent study by Kinderman finds that after public opinion had shifted to the left following these reforms, the employer associations toned down their confrontationist stances on labour market and social policy issues (see aKinderman 2016). In this case, employers' perception of their strength induced them to pursue confrontation rather than to adapt to the demands of the unions by offering concessions.

#### **4.4 Confronting a strong challenge: the introduction of board-level co-determination**

The legislation of mandatory parity codetermination in heavy industry, enacted in 1951, provides an example of political confrontation under strong political constraints. Parity codetermination refers to the representation of employees in the supervisory boards of large firms, with employees having the same number of seats as owners. The *Montan Codetermination Law* of 1951 made board-level codetermination mandatory for all firms in coal mining, as well as iron and steel production. Employees received the right to appoint half the seats in the supervisory board, as well as the right to appoint one member of the executive board, the labour director.

Industry vehemently opposed the introduction of mandatory parity codetermination. Industrialists saw board-level codetermination as a piecemeal strategy of expropriation and nationalization. Walter Raymond, the president of the Federation of German Employers' Associations (BDA) argued that codetermination's 'decisive characteristic is its aim of abolishing private property as the means of production' (quoted in Bunn 1958). Industrialists' view of board-level codetermination as 'socialism in disguise' is not surprising, because the unions themselves saw it as a tool to gain control of the economy. For German unions at that time, board-level codetermination was just one element of a more comprehensive program of economic democracy. In this program, economic decisions at all levels; the plant, the sectorial, and the national level; would ultimately be governed by bipartite corporatist bodies (Van Hook 2004; Napthali 1928).

Why did union demands for codetermination make it to the national political agenda at that time? The answer lies in decisions by the Allies and the interest of the German government to secure the unions' support for the political-economic integration of the newly created West German state into the Western capitalist economies and the institutions of the European Community. The Allied occupation authority had confiscated the large heavy industry combines in the Ruhr area and had plans to re-structure ownership. The North German Iron and Steel Control (NGISC), the Allied agency in charge of re-organizing heavy industry, decided to seek the cooperation of German unions. As a concession, the NGISC, in 1947, offered board-level codetermination in the iron and steel firms it controlled. The management and former owners of

the affected firms were excluded from the talks between the unions and the NGISC (Thum 1982).

Two years later, the newly elected conservative-liberal government, headed by Adenauer as Chancellor, decided to make parity codetermination in heavy industry permanent. The government's goal was to ensure unions' consent to the government's broader economic and foreign policies, policies that conflicted with the unions' own economic policy program, specifically the decision to abandon all plans for nationalization and centralised economic planning. The government wanted to return the heavy industry firms to their old owners. In the meantime, the Allies had lost interest in a re-organization of heavy industry and decided to grant the German government autonomy on these issues, as long as the conflict over codetermination would be resolved.

The government, needing the cooperation of the unions, decided to ignore the industrialists on this issue. Adenauer urged industry and unions to find a compromise on codetermination, but the protracted negotiations, begun in May 1950, came to no result due to the intransigence of the industry representatives. The president of the Federation of German Industry, Fritz Berg, declared that 'industry sees in these negotiations, which take place under the threat of a political strike, a fatal shock to the authority of the state' ((quoted in Berghahn 1985).

The unions threatened a nationwide strike and both sides called on Chancellor Adenauer to mediate. In January 1951, Adenauer held separate consultations with both sides. By the end of the month, unions and industry had reached a compromise, which parliament then passed into two laws. The compromise consisted of the institutionalization of mandatory parity codetermination in heavy industry (coal mining and iron and steel production), and a weaker form of codetermination in firms with more than 500 employees outside of heavy industry, by which employees had only one third of the votes in the supervisory board.

The conflicts over the legislation of mandatory board-level codetermination in the early post-war period (1947-51) are an example of political confrontation. Rather than adapting to political constraints, business in this case decided to stand firm and fight, even though the odds were against it. Both sides resorted to public campaigning and lobbying. Unlike in the case of unemployment insurance, employers did not seek a compromise or cooperate with state elites, even though the political odds were against them in both cases.

The case of codetermination thus shows that political constraints do not always induce business to adapt. Why did German business choose not to accommodate to political constraints in the case of codetermination, while it did so in the case of Bismarck's reforms and of unemployment insurance? The most likely explanation lies in the difference in importance of the policy issues at stake. Codetermination goes to the core of business control over firms. In contrast, social insurance programs, while they may raise labour costs and may weaken work incentives, do not infringe on the fundamental autonomy of entrepreneurs. They are costs of doing business, but not threats to business ownership as such. The analysis suggests that the willingness of business to adapt to political challenges correlates inversely to the importance of the policy issue for business. The more central the policy issue (in the view of business), the lesser the willingness to adapt and thus the greater the likelihood that business will deploy confrontation to defend its interests.

## 5. Discussion

The four cases studied have illustrated two different strategies of German business interest groups in responding to political challenges: adaptation and confrontation. In the case of the adoption of work injury, health insurance, and pensions under Bismarck and the adoption of unemployment insurance in the Weimar Republic, business interest groups adapted and were willing to accept policies that they had initially opposed. In contrast, business sought confrontation during the adoption of codetermination and the labour market reforms of the early 2000s. The motives behind this confrontation, however, were very different in the two cases. In

the case of codetermination, confrontation was defensive. It was the attack on ownership control that induced confrontation. In the case of the Agenda 2010 reforms, confrontation was offensive. Its goal was to change public opinion in order to achieve the desired reforms. In other words, in the case of codetermination, business was clearly on the defensive, while in the case of the Agenda 2010 reform, business was in an advantageous position and used confrontation to strengthen its hand further.

The main factor behind why business pursued adaptation in some cases and confrontation in others appears to be importance of the policy issues on the agenda to the interests of business. Policy proposals that challenge the interests of business more thoroughly than others are deemed more important, while other policy issues, of lower priority, lend themselves toward more compromise and adaptation. In the cases described above, proposals for board-level codetermination restricted the decision-making powers of owners by requiring them to share this power with employees. In contrast, the adoption and expansion of social programs does not interfere with decisions by individual firms. Social programs may raise labour costs or reduce labour supply, but these issues are less central to business than questions of ownership and control. The analysis thus suggests that a determination of whether business will pursue adaptation or confrontation will depend on the importance of policy issues to business.

The analysis also finds changes in business strategy over time. Actors may alternate between confrontation and adaptation, rather than sticking with only one of the two. One pattern identified empirically is a shift from confrontation to adaptation in the course of the policy-making process. Confrontation may appear to business as the right strategy in the early stages of a conflict, while adaptation may appear more effective at later stages. This is because confrontation may achieve a shift in the broader political agenda, while adaptation can only shape details. The attitudes of German business toward the introduction of unemployment insurance provide an example. Business interest associations initially campaigned forcefully against unemployment insurance, while in the later stages of policy-making, the major federations adapted. As the analysis has shown, this shift of strategy was a response to changes in government and in parliamentary majorities. In the struggle over codetermination, in contrast, business did not switch to adaptation, despite similar constraints. As suggested earlier, the persistence of a confrontation strategy reflects the fact that ownership is less negotiable for business than labour costs.

The case studies also point to the relevance of heterogeneity in the political strategies of business. In the case of the Bismarckian social reforms, heavy industry and textiles pursued a strategy of adaptation: industrial actors went along with the government plans to offer social protection to workers. In contrast, the manufacturing sector was less supportive of public social insurance (Ullmann 1979). In the case of unemployment insurance, the major national federations shifted to adaptation, while some groups, representing smaller firms and agriculture, remained in confrontation mode. In the two cases of confrontation, codetermination and the Agenda 2010 labour market reforms, intra-business heterogeneity did not play a major role. It thus appears that adaptation is more likely to induce disunity within business. Confrontation involves the perception of a common opponent and may thus help to mollify internal disagreements. In contrast, adaptation often involves a difficult weighting of costs and benefits, where some segments may see the benefits of adaptation as outweighing the sacrifices, while others may perceive the concessions required as too costly. In the case of the Bismarckian reforms, the manufacturing sector, being more vulnerable to price competition due to a larger of competitors and smaller firms size, was more sensitive to cost increases than heavy industry, as cartels and syndicates limited price competition in the later sector. Similarly, in the case of unemployment insurance, larger firms were better able to shoulder the costs of adaptation and the larger firms dominated the employer federations.

What implications does the analysis presented here have for debates about business power? Our findings suggest a modified version of pluralism, one that acknowledges that business interest groups enjoy power and influence, while at the same time recognizing the significance of

variation in business influence. The four cases taken from German history show that the ability of business interest groups to prevail in political conflicts varies considerably. Proponents of the business dominance thesis may challenge this perspective in two ways. First, they might argue that an analysis of four reforms taken from one country is insufficient to document the empirical prevalence of variation and that an analysis of a larger number of cases would show business dominance (cell III) to be the most frequent outcome. There is clearly a need for testing the relevance of the model presented in this paper in other countries. Nevertheless, the studies discussed in section 2 suggest that variation in business influence is also significant in other countries. This suggests, in turn, that differences in response strategies by business are not simply a German affair, but are likely to take place elsewhere.

Second, one might argue that the variation across the two dimensions is limited due to the structural character of business power in which the range of policy options that are politically viable are limited. This is without doubt true, as no government can ignore the expectations of firms and investors at will, as Lindblom and others have argued (Lindblom 1982). Yet, this structural dependence merely poses limited conditions. It does not determine the influence of business on political decisions. Investigating how business interest groups respond to political challenges can produce a more nuanced and more precise understanding of how these responses affect political outcomes. The outcome of conflicts between business and other political actors is not pre-determined. Business does not always get what it wants. The extent to which business interests prevail in political conflicts is affected by both the political strength of these challengers and the response strategies business decides to pursue.

**Table 1. Two dimensions of business-politics relations: challenge and response strategy**

Strength of challenge (columns):	Weak challenge (government sides against challengers of business)	Strong challenge (government sides with challengers of business)
Type of response strategy (rows):		
<b>Adaptation</b>	Business-led compromise (I)	Imposed compromise (II)
<b>Confrontation</b>	Business dominance (III)	Business defeat (IV)

Source: own elaboration.

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