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# **Adaptation and Influence: The Schumpeterian Perspective on Business-Politics Relations**

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## **Abstract**

This paper introduces Schumpeter's views on the relationship between business and politics and argues that we can discern a distinct Schumpeterian perspective of business-politics relations. Schumpeter's views about the pivotal role of entrepreneurs in economic development attracted substantial interest in economic sociology and in political economy. His views about the role of entrepreneurs in politics have so far however hardly been studied. The paper identifies the following four aspects as central to Schumpeter's perspective of business-politics relations: (a) entrepreneurs and corporations drive economic change, (b) entrepreneurs and corporations are ineffective in defending their political interests and vulnerable to hostile movements, (c) the resulting divergence of the economic and the political impact of entrepreneurs and corporations makes capitalism socio-politically instable, and (d) the relationship of entrepreneurs and corporations to political institutions and public policies is primarily adaptive, rather than causative.

The paper proposes a two-dimensional typology of business-politics relations that combines the Schumpeterian focus on adaptation with the Marxian focus on influence. These two dimensions - adaptation and influence - result in four ideal types: business-dominated social compromise, imposed social compromise, business dominance, and political confrontation. Examples from German welfare state history illustrate these four types. The paper suggests that the Schumpeterian and the Marxian perspective, while in contrast to each other, may be complementary and each perspective valid under different socio-political conditions.

JEL Classifications: P12, P16, H50, H70, J58

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## 1. Introduction

The work of the Austrian economist Joseph A. Schumpeter inspired scholars in different disciplines working on entrepreneurship, in particular its economic, social, and cultural dimensions. Central to the Schumpeterian perspective is its depiction of entrepreneurs and corporations as agents of economic innovation, and thereby also as drivers of economic and social change. If capitalism today is different from what it was, say, one hundred years ago, this is in significant part due to decisions and actions by entrepreneurs and corporations, be they run by their owners or by professional executives. Corporate and entrepreneurial decisions play an important role in many of those social and economic developments that came to characterize the recent past, such as the transnationalization of production and consumption, the precarization of working life, the growth of the service economy, the expansion of information and communication technologies, or the increase in income inequalities, to name just some phenomena affected by entrepreneurs and corporations.

In the Schumpeterian perspective, entrepreneurs and corporations drive forward social and economic change. They are themselves driven by market competition to develop not just new products, but also new production processes and new ways of organizing production. Innovation provides competitive advantages only temporarily, however, as competitors also adopt the new, improved practices, thereby diffusing innovation and gradually eroding the innovator's competitive advantage (Schumpeter 2002 [1912]).

Public policies and state institutions regulate corporate behavior and thereby both enable and constrain corporate innovation. They do for instance ban types of corporate innovation that policy-makers consider socially or politically undesirable. So, for instance, legislation on working time rules regulate what types of work organization corporations can develop. Regulations of financial markets affect how corporations can fund innovations, and so on. At the same time, governments want to foster innovation, perceived as crucial for growth and employment, and provide incentives for instance in the form of tax exemptions for corporate investments in research and development.

This paper aims to introduce Schumpeter's views on business-politics relations and suggests that Schumpeter had developed a distinct theoretical perspective of the role of business interests within capitalist liberal democracies. Much of today's interest in Schumpeter focuses on his views of the role of entrepreneurs as agents of innovation and economic change, while his views on the role of entrepreneurs and corporations in politics received much less attention. In the following section, I introduce Schumpeter's thoughts on the role of business on politics. I identify a focus on adaptation to political constraints and limits to business influence as central to Schumpeter's views of business-politics relations. In section three I propose a typology of

business-politics relations that relates its characterization by Schumpeter to other characterizations in the literature, in particular those inspired by Marxist and elite-theoretical approaches. The fourth section illustrates the four ideal types presented in section three using examples from German welfare state history.

## 2. Schumpeter's views on business-politics relations

Given the pivotal role that Schumpeter attributed to entrepreneurs as agents of capitalist development it seems natural that he would have attributed a pivotal role to entrepreneurs also in politics. In fact, the opposite is the case. He thought that entrepreneurs lacked political clout. Schumpeter outlined his thoughts on business-politics relations mainly in his book *Capitalism, Socialism, and Democracy*, where, unlike in his earlier work, he did not limit himself to the economics of entrepreneurship, but expanded his arguments to the political and social pre-conditions of capitalism and of entrepreneurial innovation. Albeit his treatment of the political and sociological conditions of capitalism is speculative and frequently polemical, his arguments do amount to a coherent theoretical perspective.

What is this perspective? In Schumpeter's view, capitalism is a success in economic terms, but a failure in political terms. He saw capitalism as vulnerable to the influence of hostile intellectuals and entrepreneurs as both unwilling and unable to defend capitalism against its opponents.

He viewed the bourgeoisie as politically inept and unfit to defend its own interests. He lamented the ways in which business interests behave when challenged:

They talk and plead - or hire people to do it for them; they snatch at every chance of compromise; they are ever ready to give in; they never put up a fight under the flag of their own ideals and interests - in this country [the United States, TP] there was no real resistance anywhere against the imposition of crushing financial burdens during the last decade or against labor legislation incompatible with the effective management of industry (Schumpeter 2010 [1942], 144).

Moreover, for Schumpeter 'the bourgeoisie is politically helpless and unable not only to lead its nation but even to take care of its particular class interest.'(Schumpeter 2010 [1942], 123). Its success in transforming the economy produces anti-capitalist sentiments, while capitalists, often indifferent on political issues, tend to back down and accept anti-capitalist policies. In short, the very success of capitalism ultimately generates its own collapse (Schumpeter 2010 [1942], 130).

Schumpeter emphasized the adaptive character of business attitudes towards politics and policies: 'The attitudes of capitalist groups toward the policy of their nations are predominantly adaptive rather than causative' he argued (Schumpeter 2010 [1942], 47). Entrepreneurs and corporations primarily adapt to the institutional and political context, much more so than what

they are able to shape that context. They tend to be politically passive, concerned more with the fortunes of their own firm, rather than with the wider social and political environment, and, when they get involved in politics at all, they do so in response to hostile initiatives, rather than in a pro-active manner. Even then, however, they often seek compromise, not confrontation.

In short, the view of the relations between business and society that emerges from the work of Schumpeter is thus one of business as an active agent of change in the economic sphere, but as passive and ineffectual in the political sphere. As a result, the future of capitalism seemed vulnerable to Schumpeter, as the social group upon whose agency the capitalist system relies lacks both the ability and the will to defend that system. Moreover, rather than trying to defend the free enterprise system that Schumpeter cherished, entrepreneurs would put up with political chains and act in a despondent way, making the survival of capitalism itself seem in doubt to him.

What is there to commend the Schumpeterian perspective on business-state relations? Does it enjoy empirical support? Schumpeter wrote *Capitalism, Socialism and Democracy* during the period of Roosevelt's New Deal reforms, reforms which he was firmly opposed to and which indeed most business people in the United States at that time opposed as well (see e.g. Allen 1991, 687; Hacker/Pierson 2002; Mizruchi 2013, 34). Moreover, during the 1930s, the view that capitalism would be bound to collapse was not particularly uncommon. As the Soviet Union weathered the Great Depression better than the West and given the collapse of liberal democracy at the hands of authoritarian and fascist regimes in many places, Schumpeter's views about the collapse of capitalism were fully in tune with the *Zeitgeist*, nor is it clear whether he genuinely believed in them or intended them merely as a sophisticated polemic.

Nevertheless, we cannot reduce Schumpeter's views of business-politics relations to a mere product of the gloomy age he lived in, but we need to see them as a coherent theoretical argument that deserves to be considered on its own. The Schumpeterian perspective contrasts clearly with a large body of scholarship that either starts from the premise that business is politically powerful or that intends to document business influence in politics, its sources and forms. Building either on arguments about the structural dependence of the state on investment decisions by businesses (Lindblom 1977; Poulantzas 1978 [1973]) or on "instrumental" forms of business influence, like lobbying or campaign donations (e.g. Hacker/Pierson 2010; Miliband 1973 [1969]), such studies investigate the extent and the sources of business influence in politics. In contrast, Schumpeter, emphasized the dependence of business on social and political conditions it cannot produce or secure itself, without the support of other social groups.

Does the Schumpeterian perspective of business-politics relations have empirical relevance? Is it able to better explain empirical phenomena compared to accounts that emphasize business dominance and influence? I argue it is not. Nevertheless, the Schumpeterian focus on

political adaptation and accommodation by business can usefully complement the focus on influence and power that characterizes much of the literature on business and politics, at least if we accept that business influence varies greatly and that therefore both views – the Marxian business dominance thesis and the Schumpeterian business adaptation thesis – apply under different conditions.

In the remainder of this paper I will try to illustrate the usefulness of combining a focus on business *influence* with a focus on business *adaptation*. If we see both concepts as variables, rather than as premises that we should take as universally valid, we can indeed combine the Marxian and Schumpeterian perspective and see both as applying to different scenarios, which are based on conditions that we need to specify. I will illustrate the usefulness of combining the two perspectives by drawing on my own, published research on the impact of employers’ organizations on formative social policy reforms in Germany (Paster 2009; Paster 2011; Paster 2012b; Paster 2013; Paster 2010).

**3. A typology of business-politics relations**

We can combine the two dimensions of influence and adaptation into a cross-tab (Table 1). The dimension of adaptation can be simplified into two political stances: accommodative to political constraints or no. The political influence of business can be strong or weak. The two dimensions thus result in four conceptual scenarios, shown in table 1 below.

**Table 1: Two dimensions of business-politics relations: influence and adaptation**

	Strong business influence	Weak business influence
Stance of business adaptive	Business-led social compromise (I)	Imposed social compromise (II) <i>Schumpeterian prediction</i>
Stance of business not adaptive	Business dominance (III) <i>Marxian prediction</i>	Political confrontation (IV)

Source: own elaboration.

The concepts in the cells of table 1 present hypotheses about what the political outcome is likely to be for each of these four possible scenarios. If organized business enjoys strong political influence and is willing to accommodate to demands of other actors we can expect what I call a *business-led social compromise (I)*. A business-led social compromise is a policy arrangement that is shaped by the needs and expectations of the business community, and that incorporates demands by labor and other social groups on the terms of the business community (I). An *imposed social compromise (II)* results if the political strength of other political actors and an accommodative

attitude by organized business combine to produce a policy arrangement whereby business accepts policy features it does not want in turn for concessions and in order to avert unilateral government action that would be even further removed from its preferences. In other words, this is the type of outcome Schumpeter saw as empirically prevalent.

Business dominance (III) results if business influence is strong and business is not willing to take an accommodative stance. In this case the adopted policies will not reflect the outcome of a political compromise but will reflect primarily the preferences of the business. In other words, this is outcome reflects the Marxian expectation of the capitalist state as being an instrument of the needs and interests of capitalists. *Political confrontation* (IV) is the fourth scenario envisaged in our cross-tab: it results if a politically weak business community combines with a non-accommodative stance, that is, if business is unwilling to give in despite being in a weak position.

We can expect the two dimensions, political influence and adaptation, to correlate inversely. The stronger organized business is, the lesser will be its willingness to accommodate political constraints. The weaker the political influence of business is, the more willing business will be to accommodate to constraints. As a consequence, we can expect that imposed social compromise (II) and business dominance (III) will be the most frequent outcomes. In comparison, business-led social compromise (I) and political confrontation (IV) are far less likely.

#### **4. Some illustrations of the typology from German welfare state history**

In the remaining sections of the paper I will illustrate the advantages of this perspective drawing on research on welfare state development in Germany published in my recent book (Paster 2012b). I will provide only a minimum of empirical detail here, as the reader can find more detailed accounts of the reform episodes mentioned in the book. My intention here is to illustrate the added value of a perspective that takes into account the adaptive role of organized business groups, as compared to a perspective that pays attention only to their influencing role. Theoretical accounts that focus only on mechanisms and strategies of business influence in politics tend to neglect the extent to which those are shaped by the political context, and may, as a result, attribute a greater causal role to the political agency of organized business than justified.

##### **4.1 Business-led social compromise: Bismarck's social reforms**

The introduction of social insurance during the reign of Bismarck resembles a business-led social compromise. The reforms consisted of the adoption of three new public programs: accident insurance, health insurance, and old-age and disability pensions. An alliance between heavy industry and the national government promoted and shaped the reform project, with a view to

pacify workers and to weaken the appeal of the social democrats.

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 bills (Bueck 1903). Bueck called the social reforms “a work of civilization of the highest order, which, as a model for all times, will bring [the Empire] honor” (Bueck 1905, 792).

The interests of industry focused primarily on work injury insurance, less on the other two programs. The adoption of work injury insurance was shaped by lobbying by heavy industry, which at that time was the politically dominant segment within the German business community. The adoption of new employers’ liability legislation 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 November 2<sup>nd</sup>, 1880, the executive director of the heavy industry group *Bochumer Verein*, Louis Baare, assembled a group of like-minded industry representatives to work out a draft for a new work injury insurance program (Breger 1994), which the executives then sent to the Ministry.

Opinions in the broader business community on the adoption of work injury insurance were mixed: A survey by the Prussian Statistical Office in 1881 found that 53 per cent of all regional Chambers of Commerce backed the draft, while 39 per cent were critical of it (Francke 1881). Yet, heavy industry was the dominant group within industry. It had cooperated with Bismarck already earlier in the debate about trade protectionism in the 1870s and, unlike other sectors, could rely on a strong organization, in particular the Central Association of German Industry (*Centralverband deutscher Industrieller, CDI*).

The adoption of social insurance programs during the era of Bismarck thus has the characteristics of a business-dominated social compromise. Labor unions and Social Democrats had little influence on the adoption of the reforms. Although the reforms were motivated by a fear of the rise of the labor movement, the organizations of the labor movements were still very weak at that time, compared to later periods. The growth of the labor 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 policy-making, the Social Democrats never held more than 12 per cent of the seats in parliament. Heavy industry exercised an authoritarian approach of labor management (Büren 1934, 60-74) and were not yet constrained by any collective agreements. In short, the political influence of heavy industry was at its peak during the Wilhelmine Empire, and much stronger than during later periods. The fear of a potential future strengthening of the labor movement and an intensification of class conflict motivated heavy industry to promote social reforms, rather than the actual strength of organized



labor. 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 short, the adoption of work injury insurance, health insurance, and old-age pensions under Bismarck was a business-dominated project. Key segments of the business community; heavy industry in particular, had actively backed this project and had shaped the details of the new policies. 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 the new programs. One employer representative remarked for instance that “the best way to weaken the power of the Social Democrats is to fulfill that part of their demands that every philanthropist must accept as legitimate” (Oechelhäuser 1889, 109).

#### **4.II Imposed social compromise: the adoption of unemployment insurance**

An imposed social compromise is a compromise accepted by the key segments of business under the impression of a parliamentary majority against the policy preferences of business. In other words, an imposed social compromise constitutes what rational choice theorists call “a second-order preference,” an acceptance of a policy option as a lesser evil. German welfare state history provides us with a number of examples of imposed social compromise. The adoption of unemployment insurance in 1927 is one example of a political compromise that was accepted by the main peak business federations in the absence of more favorable options.

The initiator of the unemployment insurance bill was the ministerial bureaucracy and its Minister, Heinrich Brauns, a priest and member of the Catholic Center Party. The democratization of the political system with the Weimar constitution (1919) and the inclusion of the Social Democrats and the Center Party, two parties with a pro-welfare stance, in government had resulted in a parliamentary majority for the adoption of unemployment insurance, something that had been absent before 1918. Moreover, the labor unions, which initially supported a Ghent model rather than public insurance, came to back a public program after 1918, when the unions’ own compensation schemes became financially unviable.

During the period of the Wilhelmine Empire (1871-1918) all groups of employers had been staunchly opposed to any public support to the unemployed, primarily because they feared an erosion of work incentives and an increase in workers’ reservation wage (e.g. Zahnbrecher 1914; Reiswitz 1904). In short, they suspected that unemployment insurance benefits would produce a premium for laziness. After the 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 extended indefinitely after the war. Second, a new parliamentary majority in favor of supporting the unemployed made the

dismantling of this program unfeasible.

During the early years of Weimar, employers initially maintained their opposition to unemployment insurance, but over time came to realize that opposition was pointless, given the parliamentary majority (Paster 2011). The main employer peak federations eventually decided to cooperate with the government and the unions in hammering out the details of a bill for unemployment insurance. This way, they hoped to be able to at least take the edge off the planned program and shape those details they particularly cared about, such as a close link of benefit rights to employment record, the link of the program to public labor 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 a bill based on the draft worked out by unions and employers in June 1927, it had the support of the Social Democrats, the Center Party, and two smaller center-right parties (German People's Party and the German Democratic Party), which together held 57 per cent of the votes (Paster 2012b, 98).

The strategic motives of the business federations are documented through archival sources. On 16 December 1929, the social policy committee of the Federation of German Industry (*Reichsverband deutscher Industrie*, RDI) decided to abandon opposition to unemployment insurance, with 16 votes in favor of abandoning opposition, and five votes against. 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, he considered a dismantling of unemployment assistance without substitute as unrealistic, and thus, unemployment insurance as the lesser evil (RDI 1921). Similarly, the social policy committee of the Federation of German Employers' Associations (*Vereinigung deutscher Arbeitgeberverbände*, VDA) decided in a meeting on 27 January 1925 that a continuation of opposition would have "no reasonable chance" of success (VDA 1925).

In short, the adoption of unemployment insurance resulted from a compromise between employers and unions that was imposed on employers. Employers grudgingly cooperated because they knew that a majority in parliament backed the introduction of unemployment insurance and that the government would go ahead with its plans even without business consent. The adoption of unemployment insurance was thus an imposed social compromise that was made possible by a combination of political weakness of business and the willingness of the main business federations to adapt their stance and strategy, rather than to dig in their heels.

#### **4.III Business dominance: labor market reforms in the 2000s**

The third type in the typology is business dominance (III). Business dominance results if business

finds itself in a position of strong political influence and sees no need to adapt to demands and preferences of other political actors. The literature on business and politics discusses a range of factors that may explain variation in business influence. Among these factors belong, for instance, capital mobility, the political strength of actors that may challenge business dominance, asymmetries of information between business and policy-makers, the state of the economy, and variation of salience of policy issues (see Paster 2015, 7-9).

We may think that the willingness of business to adapt will decline with the extent of business influence. In other words, the greater the influence of business, the less likely it is to adapt. Yet, we have seen above (I) that even under conditions of political dominance business does sometimes adapt, if it considers adaptation as necessary to maintain and protect its politically dominant position. If no such political challenge is imminent, however, we can expect political influence to be associated with absence of political adaptation.

The labor market reforms in Germany during the early 2000s provide an example of business dominance. In the face of high unemployment, the government of Social Democrats and the Green Party initially aimed at negotiated reforms of labor market regulations through a tripartite body, known as the Alliance for Jobs, formed in 1998. These talks failed to produce substantive reforms due to deadlocks between unions and employers. The employers threatened to leave the talks, because they thought that the proposals discussed did not go far enough towards meeting their demands for lower labor costs and liberalized labor markets (Der Spiegel, 1 March 199: 26).

After the failure of the Alliance for Jobs talks, the Schröder government set up an expert committee mandated to work out proposals for job-creating labor market reforms. Business representatives played a prominent role in the committee, which was chaired by the personnel director of Volkswagen Peter Hartz. Unlike in the Alliance for Jobs talks, the unions held no veto right in the new committee. The proposals of the committee centered on work incentives, activation, and employability, that is, supply-side reforms that were fully in line with the agenda of the employers' federations (Kinderman 2005, 435; Menz 2005, 199-200). Its most controversial component was the partial replacement of unemployment insurance by a means-tested benefit program (*Arbeitslosengeld II*) for the long-term unemployed.

The labor market reforms of the red-green governments headed by Gerhard Schröder reflect implicit business dominance. The business federations (i.e. the *Bundesvereinigung deutscher Arbeitgeberverbände*, BDA, and the *Bundesvereinigung Deutscher Industrie*, BDI) did not play a pivotal role in the reforms; the government bureaucracy was the main initiator (Hassel/Schiller 2010). Yet, the reforms were fully in line with the preferences of the business federation – that is, they strengthened work incentives and reduced social expenditures - even though they did not go far

enough in these regards in the view of the business federations. As the reforms had the backing of a parliamentary majority and the unions were sidelined, business had thus no need to adapt to constraints or to offer concessions. Instead, the activities of the business federations focused on public campaigns intended to mold public opinion in favor of the reforms, such as the Initiative New Social Market Economy, a pro-reform think tank sponsored by the employers of the metalworking industry (Kinderman 2014).

In short, the labor market reforms of the early 2000s were characterized by an implicit dominance of business interests. The thrust of the reforms was fully in line with the preferences articulated by the business federations, but the reforms were not primarily the outcome of political interventions by these federations. Instead, a set of factors created a political context amenable to business-friendly reforms, most important among them, a high level of problem pressure created by high unemployment, the perception of international competition and globalization ruling out alternative paths, and a government committed to labor market reforms. Given this context, the business federations had neither reason to seek confrontation nor to adapt to constraints (Kinderman 2014).

#### **4. IV Political confrontation: the legislation of board-level co-determination**

Political confrontation is the fourth type of business-politics relations. It results from a combination of political weakness and lack of adaptation. Political weakness of business does not automatically result in social compromise. In addition, a willingness of business to adapt to political constraints needs to be present for social compromise to occur. If business persists on its position despite being politically weak, the outcome will thus be political confrontation.

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

The legislation of mandatory parity codetermination met with massive resistance by industry, both from heavy industry as well as from other industries. Industrialists saw board-level codetermination as a piecemeal strategy of expropriation and nationalization. Walter Raymond, the president of the Federation of German Employers' Associations (*Bundesverband deutscher Arbeitgeberverbände*, 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 advocates of codetermination, that is, the labor unions, themselves saw it as a tool to gain control of the economy. For the unions, board-level codetermination was just one element of the broader program of economic democracy, by which they meant the democratic control of economic decisions at all levels, from the plant level, via the sectoral and regional level, to the national level. The de-concentration of ownership and centralized economic planning at the regional and national levels were further key components of economic democracy (Van Hook 2004, 258; Naphali 1928).

Why did union demands for codetermination make it to the national political agenda in the immediate post-war period? The answer lies in decisions by the Allies and the interest of the German government to get the unions to consent to the Western integration of the newly created West German state. The Allies had confiscated the large heavy industry combines in the Ruhr area and in light of the role played by the heavy industry in enabling Hitler’s war, wanted to re-organize ownership structures in the coal and steel industry. The North German Iron and Steel Control (NGISC) was the Allied agency in charge of re-organizing heavy industry and decided to seek union cooperation in support of its plans. As a concession to German unions, the iron and steel firms controlled by the NGISC had to introduce parity co-determination in 1947/48. The unions viewed this step as a mere intermediate success, as they wanted codetermination to become mandatory in all sectors, the nationalization of big firms, and centralized economic planning (cf. Paster 2012a; Paster 2012b, 141-148).

The legislation of mandatory parity codetermination in heavy industry was a political compromise to ensure unions’ consent to the conservative government’s broader economic and foreign policies, policies that conflicted with the unions’ own economic policy program. The conservative-liberal government, headed by Chancellor Adenauer, wanted to return the heavy industry firms to their old owners. At the same time, the Allies had in the meantime lost interest in a re-organization of heavy industry and were willing to grant the German government autonomy on domestic economic policy, as long as the conflict over codetermination would be resolved. Therefore, the broader goals of nationalization and centralized economic planning were now off the agenda. Adenauer urged industry and unions to find a compromise on codetermination but the protracted negotiations, which had started in May 1950, came to no result due to industry intransigence.

The unions threatened with a general strike and both sides called on Chancellor Adenauer to mediate. In January 1951, Adenauer intervened personally and held separate consultations with both sides. With the mediation by Adenauer, unions and industry reached a compromise at the end of January 1951, which parliament then passed into two laws. The compromise consisted of

the institutionalization of mandatory parity co-determination 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. This weaker form meant that employees had one third of the votes in the supervisory board. In short, the unions succeeded in protecting parity codetermination in heavy industry, but failed to extend it to other sectors.

The conflict over parity codetermination flared up again in the 1970s. Unions had renewed their campaign for an extension of parity codetermination to the rest of the economy, demands that the Social Democratic-led coalition government that came to power in 1969 was willing to take up. The new Codetermination Law, adopted in 1976, introduced a new form of codetermination: all firms with more than 2000 employees now needed to have parity codetermination, albeit the capital representatives would elect the chair and the chair has the swing vote in case of an impasse. In addition, senior managerial staff now had their own representatives in the supervisory board. In short, thus the 1976 law extended codetermination rights, but fell short of full parity between capital and labor.

The industry federations campaigned fiercely against this extension of codetermination rights, arguing that it would result in an undue concentration of power in the hands of the unions and led to a 'union state.' The employer federation (BDA) filed a constitutional complaint against the law based on the argument that the law violates private property rights (BDA 1979). The Federal Constitutional Court rejected the complaint in 1979 and confirmed the constitutionality of the law (Wiedemann 1980).

In sum, the conflicts over the legislation of mandatory board-level codetermination in the post-war period are an example of political confrontation. Rather than adapting to political constraints, business in this case decided to stand firm and fight. Both sides resorted to public campaigning and lobbying. Unlike in the case of unemployment insurance, discussed in the previous section, employers did not decide to seek a compromise or to cooperate with policy-makers, even though the political odds were against them in both cases.

Thus, the theoretical lesson from this case is that business does not always adapt to constraints. Political weakness does not necessarily induce adaptation. Why did German business not accommodate to political constraints in the case of codetermination, while it did so in other cases, like the adoption of unemployment insurance? The most likely reason the difference in *salience*. Codetermination goes to the core of business control over firms. In contrast, unemployment insurance merely raises labor costs and may weaken work incentives, but it does not intervene with corporate governance and the control of firms. Codetermination thus affects the core of owners' control over firms, while social programs do not. More generally speaking, the greater the salience of a policy issue is to entrepreneurial control over firms the less the

willingness of business to adapt to constraints will be.

## 5. Conclusions

Schumpeter's prediction that capitalism would collapse because of capitalists' inability to defend their own interests has not materialized. Yet, his emphasis on the adaptive role of business in politics was spot on. A focus on adaptation complements the focus on business influence and business power. Although the role of business in politics may not primarily be an adaptive one, as Schumpeter thought, it is at least sometimes adaptive.

The two-dimensional typology proposed in this paper intends to show the analytical value of looking not only at the political influence and power of business, but also its adaptation to political constraints. I have argued that different combinations of these two dimensions are likely to result in four different types of business-politics relations: business-dominated social compromise, imposed social compromise, business dominance, and political confrontation. The examples from German welfare state history illustrated these four types. The typology is applicable also to other policy fields.

The typology provides a corrective to approaches that focus only on the influence of business, and neglect adaptation. While it does not allow us to make predictions about adaptation – about when, how, and how much business will adapt to constraints – it does point us to new questions. In particular it points to questions of how influence and adaptation relate to each other. In particular, is business more likely to adapt when its political influence is weak? Does weak influence induce adaptation or confrontation? I have alluded in the discussion on the adoption of unemployment insurance (4.II) that adaptation may happen as a response to weakness. Yet, at the same time, we have seen that adaptation can happen when business has a dominant position in politics and when it has not. We have also seen that adaptation does not automatically happen in response to weakness.

In other words, the empirical discussion raises questions about the empirical frequency of the four cells. Are all combinations of adaptation and influence - that is, all four types -equally likely? If so, what determines the occurrence of each type? If not, how do adaptation and influence correlate? We have not answered these questions in this paper. Yet, the typology proposed enables us to see questions like these, questions we would likely not see if we only look at influence alone. Clearly, the Schumpeterian focus on adaptation can not substitute for an analysis of the sources and extent of business influence and business power in capitalist democracies; yet, it has the potential to complement research on business influence in a way that sheds light on the conditions under which business power and democracy can be reconciled.

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