Political and Economic Impacts of German Reunification

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Abstract. This article aims to provide a holistic and comprehensive summary on the political impacts as well as economic impacts of the Reunification of Germany in 1990 due to the fact that politics and economics are inter-linked.This article analyses political impacts through linking the reunification with other geopolitical changes in the world that took place afterwards, and discovered that the reunification did not effectively eliminate the division between Eastern and Western Germany and strengthened right-wing extremism in the East, yet contributed to the easing of global tensions, the dissolution of the Soviet Union and the integration of Europe. This article analyses economic impacts mainly through the comparison of various macroeconomic indicators, including annual GDP growth rate, unemployment rate, and inflation rate, of the German Democratic Republic(GDR) and the Federal Republic of Germany(FRG) before reunification and western and eastern Germany after reunification, and discovered that the reunification had in general negative domestic economic impacts, and that the economic disparity between eastern and western Germany has not been eliminated yet.

Keywords: Political impact; economic impact; German history; reunification of Germany.

1. Introduction

The official reunification of the German Democratic Republic (East Germany) and Federal Republic of Germany (West Germany) took place on 3 October 1990. The "Unification Treaty" became effective on that day, dissolving East Germany and integrating it into West Germany. Although this geopolitical shock happened over thirty years ago, different political systems and economic structures of East and West Germany resulted in various problems which remain unresolved in today's Germany. There are numerous studies separately on the political impacts and economic consequences of the reunification, such as the development of "Ostalgie", a general feeling among East Germans that life was better before reunification, and the deterioration of Eastern Germany's economic performance in 1990s even with enormous amount of aid from the West. Nevertheless, there seems to be a lack of comprehensive analysis of the interaction of politics and economics during and after reunification, which is why this article helps to provide a clearer picture of how geopolitical changes and government policies affected domestic, European and global economy, and how the economic trends in turn influenced geopolitics and government policies.
This article consists of three parts. In the first part, historical background will be introduced and briefly analysed, demonstrating how the political and economic developments in East and West Germany paved way for reunification and sowed seeds for future problems.

In the second part, by using various recordings from archives and existing secondary sources, political impacts will be analysed and it will be shown how the reunification, instead of elimination East-West Germany division, actually strengthened it, which consequently led to the rise of right-wing extremism in Eastern Germany. Moreover, reunification will be linked at international scale, to the developments of the end of the Cold War and the integration of Europe, and it will be shown that the reunification of Germany contributed to the dissolution of the Soviet Union and that the formation and enlargement of the European Community was partially a result of the reunification.

In the third part, through comparing macroeconomic indicators of West and East Germany before and after reunification, domestic economic impacts will be analysed, and it will be shown that economic performance of Germany as a whole deteriorated greatly immediately after reunification, and the disparity between the more developed West and less developed East remains visible today.

2. Historical Background

2.1. Political Differences between East and West Germany

2.1.1 Political structure and diplomatic relationship

West Germany was a federal parliamentary constitutional republic, with elections held every four years, whereas East Germany was a Marxist-Leninist one-party socialist state, where the citizens did not have actual suffrage. West Germany did not restrict general freedom of speech, resulting in a more diverse political atmosphere. Coalition governments were common, and there were also radical political groups such as the Red Army Faction. However, for East Germany, all political parties were subservient to the ruling party——Socialist Unity Party of Germany (SED). The secret police, *Stasi*, monitored East German citizens and freedom of speech were largely limited. This caused the East Germans to be politically conservative even after reunification. Nevertheless, the ruthlessness of Communist government and the worsening standard of living resulted in much dissatisfaction and criticism among East Germans, which consequently led to multiple demonstrations in the late 1980s and was a strong motivation for reunification.

West Germany adopted "Ostpolitik" in 1969, aiming to normalise the relationship between West Germany and Eastern European states, particularly East Germany. The Basic Treaty was signed in 1972, which established formal diplomatic relationship between the two Germanies. Between 7 and 11 November 1987, East German General Secretary Erich Honecker visited West Germany, becoming the first ever East German head of state to set foot on West Germany. Therefore, it can be shown that before reunification, the official connection between the two Germanies were restored to a certain extent.

In November 1989, after Egon Krenz succeeded Honecker as the leader of East Germany, he pledged to carry out political and economic reform, in order to create a more liberal democratic, but nonetheless socialist nation [1]. The idea was welcomed by some of the reformists in East German government, but eventually, the merger of the two Germanies was completed through the absorption of East Germany by the capitalist West Germany. This led to disappointment among some East Germans, especially when the economy collapsed after the merger.

2.1.2 Social welfare

West Germany conducted multiple rounds of social welfare reform. Universal index-linked pension system was implemented, free medical service at hospital was offered to 9 million West Germans that were qualified for social relief, and subsidised medical service was provided for 23 million patients under the national healthcare insurance scheme [2]. East Germany, on the other hand, had a very low original pension, which was gradually increased by political leaders on important occasions such as major party congress. The welfare system was used as a way to gain public support and approval for the communist regime, and the improvement each time was relatively small [3]. As a result, welfare system in East Germany were considerably worse than that of the West Germany. However, it cannot be ignored that if reunification were to take place, it would be a heavy financial burden for the government to establish the same welfare system in the less developed Eastern Germany.

2.2. Economic Development Differences between East and West Germany

West Germany adopted capitalism market economy, and after World War II, it recovered rapidly and created an economic miracle——"*Wirtschaftswunder*". The currency reform in 1948 halted hyperinflation and decontrol of prices stimulated producers as higher prices together with more valuable new currency incentivise sellers to supply more goods and services. As a result, West Germany reconstruction was achieved at an astounding speed, and by 1989, West Germany had a GDP per capita of Intl$18690, over three times as high as that of East Germany which was Intl$5100 (Table 1).

East Germany adopted command economy which was similar to that of the Soviet Union. The rigid command economy structure resulted in an inefficient system where the prices were controlled by central government and hence could not serve as a signal to producers to increase or decrease supply. This led to frequent over-production or under-production of consumer goods, undermining citizens' standard of living as well as slowing down economic growth (Table 2) [4]. Apart from the rigid economic system, the Soviet Union claimed most of East Germany's heavy industry as war reparation, which seriously weakened the economic recovery of East Germany. Thus, the stagnant economic development triggered public dissatisfaction towards the Communist government and resulted in a series of protests in 1980s.

Table 1. Comparison of GDP per capita between GDR and FRG from 1936 to 1991

	GDR			FRG			
	GDP (1990 Intl$, millions)	Population(thousands)	GDP per capita ($)	GDP (1990 Intl$, millions)	Population(thousands)	GDP per capita ($)	East GDP per capita as a percantage of the West
1936	74,652	15,614	4,781.09	192,911	42,208	4,570.78	105
1950	51,412	18,388	2,795.95	213,942	49,983	4,280.30	65
1973	129,969	16,890	7,695.03	814,786	61,976	13,146.80	59
1990	82,177	16,111	5100.68	1,182,281	63,254	18,690.69	27
1991	85,961	15,910	5,402.95	1,242,096	63,889	19,441.47	28

Data Source: Maddison, Angus. The World Economy. Development Centre of the Organisation for Economic Co-operation and Development (OECD), Paris, 2006, p. 178.

Table 2. Comparison of annual GDP growth rates between GDR and FRG (%)

	GDR	FRG
1950-1960	6.7	8.0
1960-1970	2.7	4.4
1970-1980	2.6	2.8
1980-1989	0.3	1.9
1950-1989	3.1	4.3

Data Source: Sleifer, Jaap. Planning Ahead and Falling Behind: The East German Economy in Comparison with West Germany 1936–2002. Walter de Gruyter GmbH, Berlin, 2006, p. 53.

Moreover, this gap in economic development would become an enormous burden if an economic merger were to take place, as the more developed West Germany would have to invest a tremendous amount of resource in the less developed East Germany in order to erase the disparity, paving way for a series of problems in the future and leaving many hidden dangers.

3. Political Impacts

3.1. Domestic Impacts

3.1.1 "Ostalgie" and East-West division

After the reunification of Germany, the invisible psychological division between West and East Germany persisted. The reunification was completed by Federal Republic of Germany absorbing five East German states. Thus, FRG social and economic institutions dominated the former East Germany. East German products disappeared, for the western distributors of consumer goods assumed control over the eastern market; East German factories were sold to westerners at next to nothing; school, streets and buildings were renamed to erase their Communist marks; socialist memorials and monuments were toppled; education system, especially universities, were restructured [5]. These

swift changes of society left many East Germans, especially the older generation, at a loss, as they no longer had sense of belonging to the new nation. As for the young, this uncompromising campaign which aimed to erase all traces of the old GDR era from eastern German states severely challenged their original way of life [5]. Therefore, although for different reasons, the effects of the rapid changes on eastern Germans were similar: East German consumer goods, such as Trabi cars and Kittel smocks, were seen to be bought and used by eastern Germans again in the 1990s. Producers and vendors also restarted the reproduction and commercialisation of East German goods. This "Ostalgie" can be seen as East Germans' attempt to restore and re-ascertain the foundation of their identity and personhood.

Furthermore, the economic disparity between GDR and FRG and the conservative mindset of eastern Germans led to discrimination and mutual suspicion. Stereotypes emerged, that "Ossis"—— eastern Germans were racist, lazy and self-pitying, and that "Wessis"—— western Germans were self-centred, money-obsessed and arrogant. The division remains visible today, as in a poll commissioned by German government in 2019, 57 per cent of eastern Germans claimed that they felt like citizens of second class compared with western Germans. Only about 38 per cent of respondents in the East regarded reunification as a success. Among people under the age of 40, the percentage decrease to around 20 per cent [6].

In addition, the deterioration of eastern German economy immediately after reunification also caused the wish of eastern Germans to return to GDR era. After reunification, unemployment rate of eastern Germany soared from around 10 per cent in 1991 to 20 per cent in 2004 [7], whereas in the old GDR, sufficient jobs were provided by the central government. This job insecurity caused disappointment and depression among eastern workers, and thus creating soil for this nostalgia for East Germany.

3.1.2 Rise of right-wing extremism in eastern Germany

After reunification, eastern Germany's economic development continued to lag behind the western part. Economic production of GDR is a third lower than that of FRG, and the average income is 10 per cent lower [8]. This is partially because the privatisation of former GDR industry resulted in a loss of capital and labour to western Germany, as Western Germans seized control of most privatised East German firms and eastern German labour moved west for employment opportunities. Thus, eastern Germans' resentment towards the unfair treatment during reunification led to them supporting far-right political parties as an act of protest to the dominant central government.

Another reason for the rise is immigration. During the GDR era, the government signed agreement with other socialist states such as Vietnam, Mozambique and Cuba to allow their nationals to work in GDR. With the increasing unemployment after reunification, these immigrants were blamed by eastern Germans for stealing their jobs. Thus, right-wing extremism creeped in due to xenophobia, evident by the Rostock-Lichtenhagen riots in 1992, where hundreds of right-wing extremists attacked asylum seekers, throwing stones and petrol bombs at their apartment block. This extremism continued as eastern Germany remained to lag behind the West economically, and in the Bundestag election of 2021, the far-right Alternative für Deutschland party performed strongly in eastern Germany, coming in first place in former East German states of Saxony and Thuringa [9].

3.2. International Impacts

3.2.1 European integration

International opinions on German Reunification were not completely positive, even for some of West Germany's allies. Considering the fact that Germany initiated two World Wars, which resulted in tens of millions of casualties, there were worries that a reunified Germany would pose a threat to the balance of power in Europe, endangering European stability. British Prime Minister Margaret Thatcher expressed her strong opposition, as she believed that reunification would make Germany "simply too big and powerful to be just another player in Europe" [10]; similarly, French President François Mitterrand said to Thatcher that a united Germany could "make more ground than even Hitler had" [11]. Thus, as a show of non-aggressive and co-operative political stance, German

Chancellor Helmut Kohl promised that the reunification of Germany would remain in the European Community and the NATO. West Germany had been an active participant in European integration, co-founding European Coal and Steel Community(ECSC) in 1951, European Atomic Energy Community(Euratom) and European Economic Community(EEC) in 1957. After reunification, Helmut Kohl contributed greatly to the Maastricht Treaty, which marked the birth of European Union(EU). Throughout the three decades since the formation of EU, Germany continues to be the largest net contributor to EU budget, showing its willingness for European cooperation; Germany also supported the establishment of the Economic and Monetary Union(EMU) as well as the creation of Eurozone. Therefore, it can be concluded that German Reunification helped to accelerate the process of political and economic integration of Europe, because without the support from a major European power, the European Communities would not be able to exert considerable influence over much of the continent, severely hindering the positive effects of the integration.

3.2.2 The end of the cold war and the dissolution of soviet union

The democratisation of East Germany and the subsequent German reunification are widely considered to be a symbol for the end of the US-Soviet confrontation. Shortly after the fall of the Berlin Wall on 9 November 1989, US President George H. W. Bush and Soviet General Secretary Mikhail Gorbachev convened in Malta. Although no agreement or treaty was signed, it was considered as a mark for the end of the Cold War confrontation as the US and Soviet Union abandoned the old image of enemies [12]. The Berlin Wall was one of the most famous symbols of the Cold War, as it was a visual demonstration for the Iron Curtain, separating Germany's capital city. Now that the symbol for division was erased and the once separated nation became reunified again, it was a clear signal to the Europe and the world that the East-West confrontation had come to an end. Thus, the reunification of Germany helped to significantly ease the tense global atmosphere since Soviet invasion of Afghanistan brought an end to Détente.

The reunification of Germany also stimulated the centrifugal-disintegrative process within the Soviet Union. Inspired by the Germany example, nationalist movements intensified in the republics of the Soviet Union. On 12 June 1990, the largest republic of the Soviet Union, Russian Soviet Federative Socialist Republic(RSFSR) declared sovereignty, and its leader, Boris Yeltsin, resigned a month later from the Communist Party of the Soviet Union(CPSU). Following Russian footsteps, other republics such as Ukrainian SSR, Byelorussian SSR and Kazakh SSR proclaimed sovereignty in 1990 as well. After a failed coup by conservatives to re-establish a strong central government in August 1991, the dissolution of the Soviet Union became inevitable. Although it was predicted by some dissident thinkers that the Soviet system was "slowly decaying and had no future", the rapid collapse of the Soviet Union was not considered as an immediate possibility [13]. The reunification of Germany, together with the collapse of Communism in other Eastern European states, exerted a domino effect on the Soviet Union, which accelerated the process of dissolution by setting examples of initiating peaceful nationalist revolution and secession from the control of Moscow.

4. Economic Impacts

The domestic impacts on Germany after reunification were immediate: the economy plunged. Throughout the 1990s and 200s, the Germany struggled with the astronomical cost of reunification for two decades, and the recovery came only after the Global Financial Crisis 2007-2008.

4.1. Deterioration of economy from 1990s to 2000s

After reunification, the FRG government invested over 2 trillion marks in eastern Germany [14] to assist its transition to market economy, and to subsidise East Germans at employment, pensions, transportation, education and housing. This resulted in tremendous government expenditure, and Chancellor Kohl decided not to raise taxes, but to go into deficit. The Bundesbank had to increase interest rates as a response to the inflationary pressure of the government deficit. The inflation reached the highest point of 5.2 per cent in 1992 and gradually returned to normal level below 3 per cent

(Fig.1). Annual GDP growth rate plunged to a negative one per cent in 1993 (Fig.2) and continued to stay in a rather low level below 2.5 per cent for most years from 1993 to 2021.

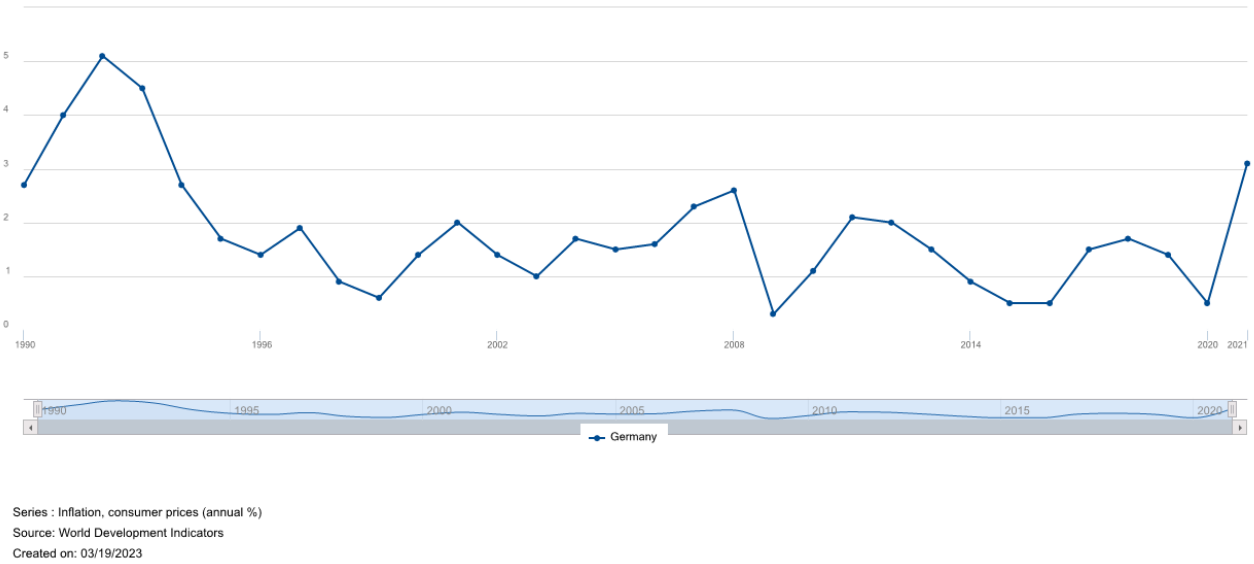


Fig. 1 Germany Inflation Rate (Consumer Prices)1990-2021

Data Source: World Development Indicators, Databank, The World Bank, 2023. Cited on 19 March. https://databank.worldbank.org/reports.aspx?source=2&series=NY.GDP.MKTP.KD.ZG&country=DEU

Furthermore, from 1996, the contribution of Germany's domestic demand to production began to decrease and the growth of national income was mainly stimulated by exports [15]. Under these conditions of shrinking domestic demand and the switch of the main driver of growth from domestic demand to fast increasing exports, the procurement of the excessive production capacity of eastern Germany and a considerable increase in the total labour, were neither needed nor desired. Additionally, the privatisation of former Communist public properties that resulted in the closing down of many acquired East German companies and factories led to the unemployment of millions of qualified workers. Unemployment rate rose sharply from 1991, staying above 7.5 per cent from 1993 to 2008 (Fig.3).

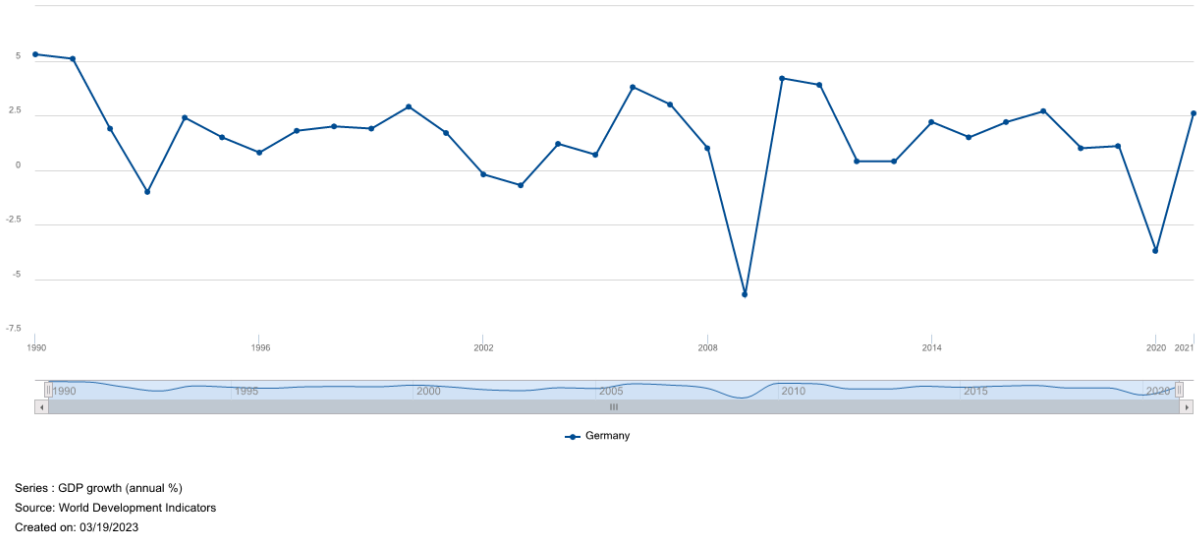


Fig. 2 Germany GDP Growth Rate 1990-2021

Data Source: World Development Indicators, Databank, The World Bank, 2023. Cited on 19 March.
https://databank.worldbank.org/reports.aspx?source=2&series=NY.GDP.MKTP.KD.ZG&country=DEU

High unemployment and low economic growth posed heavy pressure on Germany's welfare system. Citizens, especially high-skilled employed workers and capital owners had to pay a higher tax as the number of applicants for unemployment insurance increased, which discourages private investment [16]. This reduced the overall contribution of the capital owners to the welfare system, right when the government needed to increase welfare expenditure, setting up the vicious cycle. As a result, investment and output per capita decreased, which led to a slow-down in economic growth.

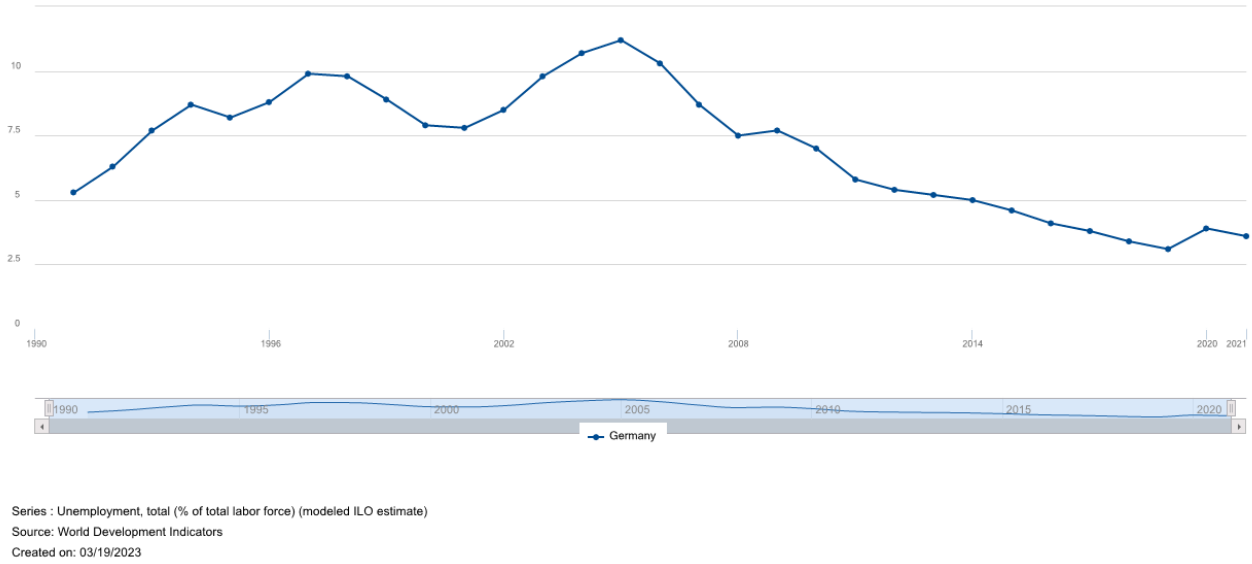


Fig. 3 Unemployment Rate of Germany 1991-2021

Data Source: World Development Indicators, Databank, The World Bank, 2023. Cited on 19 March.
https://databank.worldbank.org/reports.aspx?source=2&series=NY.GDP.MKTP.KD.ZG&country=DEU

4.2. Struggle of Eastern Germany

Although FRG government provided astronomic financial aid to eastern Germany, the economic development of the East still lags behind after three decades. The pattern of Treuhand privatisation starting from 1990 led to unbalanced distribution regarding the headquarters of companies across Germany, with the result that the eastern Germany is virtually void of headquarters of large firms in any category [15]. This was because firm owners and managers from West Germany were more experienced in running private business and had first-hand information from acquaintances in the Treuhand Trust about the privatised asset, and many former East Germany factories and companies were seized by western Germans. This consequently led to migration of skilled eastern German workers to western Germany for more better-paid employment opportunities. These problems during privatisation, along with the deteriorating German economy overall and the lower productivity of eastern Germany compared with the West, resulted in eastern Germany lagging behind western Germany economically for three decades. In 2019, GDP per capita in the West was €43,449 while that of the East was €30,027, which was 69% of the West; unemployment rate in the West was 5.1 per cent while that of the East was 7.1 percent; as for gross annual income, eastern Germany with €31,347 was only 83 per cent of western Germany with €37,844[17]. Thus, although the economy of eastern Germany did improve over the decades, its gap with the former West Germany still has not

been eliminated. This largely contributed to the resentment of eastern Germans towards the West and accounted for the rise of far-right political parties such as AfD, as they promise voters that they would provide more employment through expelling immigrants and refugees, and through withdrawing from European integration to protect domestic firms.

5. Summary

In conclusion, the reunification of Germany was a geopolitical shock that produced long-lasting impacts on Germany, Europe and the world. This article discovered that the reunification did not erase the East-West division, as different life experiences had resulted in different national identities between West Germans and East Germans. The deterioration of economy also gave rise to right-wing extremism and xenophobia in eastern Germany, which continues to be a problem for the government throughout the decades. Thus, despite the fact that reunification was warmly welcomed and celebrated by both sides, long-term domestic political impacts were negative. This article also discovered that the reunification pushed Germany towards economic difficulties. The enormous expenditure on financial aid to the East became a heavy burden on government budget and led to rising unemployment and inflation. Moreover, the very foundation of the privatisation process of former East German assets caused various problems, including rising unemployment in the East and national economic recession. It also resulted in the weak performance of eastern German economy, as the foundation of economic productivity for eastern Germany was damaged during privatisation. This article provides a cross-referral comparison between political and economic impacts of the reunification, thus depicting more clearly the interconnection between the two kinds of influence. In this way, the article hopes to offer some insights to future researchers on the consequences of German Reunification, which are still affecting the world today.

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