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# How the Deutsch Mark Swallowed Up East Germany's Economy

Thursday 29 October 2020, by [BALHORN Loren](#), [TRÖGER Mandy](#) (Date first published: 3 October 2020).

**After the Berlin Wall's fall, the introduction of the West German currency was widely presented as the East's path to prosperity. But the result was a fire sale of East German industry to Western businesses — a massive destruction of jobs and public property whose harmful effects are still felt 30 years after reunification.**

"The social market economy has turned out to be nothing more than ordinary capitalism." Just two years after German reunification, erstwhile East German premier [Hans Modrow](#) used these words to welcome readers of *Offenes Blatt* magazine into 1993.

The disillusionment felt by Modrow — the last member of the Socialist Unity Party (SED) to lead the German Democratic Republic (GDR) — hadn't come from nowhere. As who one Green politician called the "honest administrator" of the initial "transition process in the GDR," Modrow experienced firsthand how the state's attempts at reform were nipped in the bud by West German political elites. Critics on both sides of the inner-German border were dismissed as traitors to the cause of reunification.

Later a member of parliament in the reunified Germany, Modrow became one of the sharpest critics of West German chancellor [Helmut Kohl's](#) policies. The Christian Democrat Kohl's strategy was built around the deutsch mark and the "free market." But it turned out to have disastrous consequences for all of Germany — ones that continue to be felt thirty years later. Still today, East-West relations in Germany are shaped by relations of inequality and dependency — as we can better understand with a look at the transition of 1989-1990.

## Reform Over Unity

Calls for economic reform had been growing louder in the GDR already in the fall of 1989, before the fall of the Wall on November 9. As the staff of the progressive newspaper *Der Morgen* had written in an internal memo as early as October, "many of the problems that have to be tackled in our country have to do with straight-up economic matters." Economic policy was thus to be the cornerstone of all reform efforts in the GDR.

This was recognized at the highest levels of government. On November 1, 1989, shortly after long-serving leader Erich Honecker was deposed, the new chairman of the Council of State, [Egon Krenz](#), traveled to Moscow. According to the minutes of a confidential conversation he conducted with Soviet leader Mikhail Gorbachev, he admitted that decisions taken at the ninth SED party congress were not "based on a real assessment of the situation." "In the solutions to economic issues," he remarked, "subjective opinions" had been taken as the point of departure. The party had drawn conclusions that completely bypassed national and international realities, and now the catastrophe in the country was almost unstoppable. Eight days later, [the Berlin Wall fell](#).

The very next day, over in West Germany, a seventy-five-page report was circulated in the Federal Agency for All-German Affairs, summarizing the goals of the most important GDR opposition groups. All of them adhered to the “unique existence of the GDR,” such as “a vision of a democratic socialism with guaranteed civil rights to be established on German soil.” Every opposition group agreed on the continued existence of a reformed GDR — a fact that is often forgotten today.

Economic reform, in this context, meant the “creation of a mixed system,” in other words, “the incorporation of market elements into a de-bureaucratized [state] planning framework subject to democratic control.” Proceeding from “radical-democratic and socialist ideas,” the state was to be purged and social justice returned to the forefront of a democratized social and economic policy.

On December 1, the East German parliament, or Volkskammer, rescinded the SED’s monopoly on power, and two days later Krenz, the Politburo, and the entire Central Committee resigned. Hans Modrow, an early critic of Honecker in the SED leadership, became de facto head of state. On December 7, the oppositional grassroots-democratic “Round Table” was formed. Though ignored by Modrow at first, it later cooperated with him in a “school of democracy.” Nevertheless, the general thrust remained the same: [democratic reforms, not reunification](#).

Views on reunification looked quite different in the Federal Republic, i.e., West Germany. Already in mid-November 1989, the leadership of the liberal Free Democratic Party (FDP) declared that “the demand for self-determination for Germans in the GDR is absolutely correct,” but “before that, it should be stated that the FDP strives for the reunification of the two German states.” Kohl’s ten-point program, announced in late November, also foresaw a gradual reunification. For FDP leader Otto Graf Lambsdorff, this meant the GDR giving a “clear ‘yes’ to the market economy.”

During a debate in the West German parliament in mid-January 1990, the head of the federal chancellery, Rudolf Seiters, called for a “contractual community” between the East and West with the goal of German unity. Reform forces in the GDR and critics of the Federal Republic objected to this proposal and pleaded for more time. GDR reformers wanted to maintain an independent state, while critics in the West opposed what they saw as a united Germany with dismal future prospects. The Round Table, for instance, discussed the possibility of a contractual community based on the 1972 Basic Treaty on German-German relations, as well as a confederation between the two states.

## **Kohl and the Deutsch Mark**

These discussions took place against the backdrop not only of an unstable situation in the GDR, but also of several meetings between Modrow and Kohl. While preparing for Kohl’s visit to Dresden, on December 19, 1989, Modrow noted that “there must be no disappointment about this meeting, for it would risk increasing social unrest as a result of political and social insecurity.” The impression could not be given “that West Germany is waiting for instability in the GDR rather than providing effective, i.e., rapid, support.”

There was a long list of concerns: the precarious economic situation, rising emigration, and the dire gap between the currencies in East and West. This latter problem, Modrow argued, would soon be directed against the GDR. With the introduction of visa-free travel at the beginning of 1990, it would lead to an “increased flow of speculative money back into the GDR . . . including the consequences of illegal employment.”

Modrow’s plan was, therefore, a contractual community and some form of compensation for the reparations which only the GDR had paid to the Soviet Union after World War II. West Germany was expected to cover its share with a payment of 15 billion deutsch marks in 1990 and 1991. In return, the GDR would commit its production to primarily servicing the West German market. Kohl

promised help at the subsequent meeting with Modrow. Both agreed on the creation of German-German expert groups on political and economic problems.

Shortly thereafter, in January 1990, Modrow warned that the deteriorating situation in the GDR was “worrying.” The political interests of individual groups in East and West Germany had to be subordinated to the goal of social stabilization. Modrow attempted to pull the opposition — of which the Round Table remained the organized institution — into government. He participated in three of its meetings and appointed eight of its members as ministers. One consequence of this cooperation was the first free GDR elections, which were held early, on March 18, 1990. Nevertheless, by the end of January, Modrow had also adopted a four-step plan for the “formation of a unified German state.”

At the second meeting between Modrow and Kohl in Bonn in early February, the West German chancellor emphasized that he anticipated an accelerated unification process. In light of recent developments, he argued, the idea of a contractual community was outdated — and a monetary and economic union was now needed. There would be no stabilization without a quick currency union, Kohl declared in a one-on-one discussion with Modrow. According to the minutes, Kohl was mainly concerned with one thing: “The deutsch mark should be used as the strongest ‘asset’ to calm the situation. That requires decisive economic reforms in the GDR in order to introduce the social market economy.”

Modrow and the Round Table opposed this — arguing that the goal could not be a hasty *Anschluss*, or annexation, of the East. GDR citizens had to retain their rights and sovereignty. Despite repeated public promises, Kohl had provided no support. He had thus both disappointed the high expectations he had created amongst East Germans and, in so doing, heightened insecurity in the country. According to Modrow, whether intentionally or not, these “stalling tactics” and Kohl’s propagation of a rapid monetary union had pushed public opinion toward a hasty agreement.

According to reports on the meeting, it was “obvious to the Round Table that some forces in the Federal Republic are currently angling for a deliberate intensification of the problems in the GDR” in order to protect their own interests. It again warned against a hasty monetary union — the GDR must first and foremost find its own solutions for economic reform. This, Modrow emphasized, represented “the unanimous will of the government and the Round Table.”

But this will was ignored. In March 1990, journalist Walter Süß wrote in the left-leaning West German newspaper *die tageszeitung* that the federal government in Bonn showed a “demonstrative disregard of the Modrow government.” In this same newspaper, Antje Vollmer was critical that the GDR government was being treated “as if it no longer existed.”

On February 7, 1990, the West German government stipulated that the adoption of the West German economic and legal system would be the prerequisite for any monetary union with the GDR. Accordingly, the federal minister for economic affairs Helmut Haussmann (FDP) demanded the GDR’s “unrestricted commitment” to “purebred private property” and rejected Modrow’s criticism. “Coming back with the deutsch mark in your luggage is one of the greatest gifts,” Haussmann pontificated. Expert meetings on monetary and economic union began the following week.

### **Ignored Criticisms and the “Second Economic Miracle”**

Critical voices were few and far between. West German politicians were, as *die tageszeitung* wrote, “appallingly optimistic.” They expected, like Social Democratic financial expert Ingrid Matthäus-Maier, a “second economic miracle.” Only a few experts, like the Marxist professor of political science at the Free University of Berlin, Elmar Altvater, warned of the “economic consequences of

the GDR's hasty annexation to the Federal Republic." The German Council of Economic Experts, a nonpartisan group tasked with preparing an annual report on the German economy dating back to the 1960s, expressed its strong opposition to the monetary union. In a letter to Kohl dated February 9, 1990, it stated that the rapid introduction of the deutsch mark would not bring long-term advantages for the East, but the opposite. In an open letter, Altvater and other experts warned:

The rapid economic annexation of the GDR would be an adventure not with an uncertain, but rather a highly certain outcome: the collapse of large parts of the GDR economy, which without the protection of its own currency with a low exchange rate would not be internationally competitive. Evidently, it is being deliberately calculated that it will be possible to blame the enormous social costs of a rapid annexation on the old system.

Rapid annexation would conjure up a "(bi-)national disaster," and unification would degenerate into an "uncontrolled large-scale experiment," the experts claimed. The costs would be in an order of magnitude "that could hardly be managed." Kurt Hübner, an openly critical political scientist, warned that an immediate monetary union – which would eliminate the protective mechanisms to counteract economic degradation and social polarization — would result in the immediate decline of the East German mark. The opening of the market would "hit the GDR economy like a shock" and result in a collapse of industry, low wages, and "a situation of dependent development".

According to critics, promised capital transfers from West Germany would lead to the takeover of GDR property by private companies from the West. Therefore, the acceleration of the *Anschluss* would "only be in the interest of the speculators" who were trying to "cut the best slices out of the GDR cake." If any "investment boom" whatsoever was possible, then only if the GDR economy remained intact and was "restructured under social control." Possibilities for such an approach included a fiscal equalization scheme or a development fund, as well as "targeted economic protection measures" with a secure GDR currency.

In retrospect, Hübner remarked that such scenarios and analyses had, indeed, garnered public attention at the time but were "perceived by political parties ... as a betrayal of German unity." This snuffed out criticism from the outset, causing Kohl's agenda — in Modrow's view, a product of the Chancellor's "superficial political ambition" — to appear to be the sole alternative. Lacking an actual concept for its economic policy, the West German government relied entirely on the market and placed its hopes in the goodwill of West German capital in the East German economy. It, thereby, left the populations of both East *and* West in the dark about the full extent and long-term consequences of German unification.

### **Living With the Consequences**

As critics predicted, the introduction of the market economy on July 1, 1990 (through the so-called "Economic, Monetary and Social Union") and Germany's subsequent political unification on October 3, 1990, abruptly exposed the hitherto insulated East German economy to international competition. It quickly became apparent that industrially manufactured GDR products could not compete with their Western counterparts in terms of features, quality, or price. Previously, goods exported to the West had been sold at significantly reduced prices. Now, it was virtually impossible to sell East German products on Western markets.

At the same time, Eastern European markets — which had until that point been secure sales markets for the GDR — suddenly collapsed due to the socio-economic transformations going on there. Following German unification, industry-wide wage levels were also raised quickly. This further worsened the cost situation for East German companies, not least due to their traditionally high levels of staffing characteristic of enterprises under state socialism. According to economist Joachim

Ragnitz, it was “therefore obvious that a large part of the existing GDR companies would have to exit the market sooner or later.”

Between 1989 and 1991, East German industry experienced a dramatic decline with correspondingly negative effects on the labor market. By 1991, the number of jobs in the manufacturing sector had fallen from 3.3 million to 1.7 million. By 1995, industrial employment had fallen by a further 800,000 and thus shrunk to around one-quarter of pre-1990 levels. According to calculations by the Institute for Employment Research, more than 2.5 million people lost their jobs in eastern Germany between 1989 and 1991, while the total number of employed people fell from almost 9 million to around 6.7 million.

This was followed by mass-scale labor migration and thus a demographic shift. Those who could went to work in West Germany. The public sector reacted with extensive transfer payments and the implementation of complex labor market policy measures, the costs of which were borne by the taxpayers of the old West German states. However, this did little to counteract the massive structural rupture across eastern Germany.

Like many other analysts, however, Ragnitz concludes that this development was inevitable. Following the introduction of the market economy, the East German economy collapsed due to “a lack of modernization of businesses in the GDR and the initially poor infrastructural conditions.” Mistakes in the unification process were made but “to a small extent,” such as the “hasty introduction of the Deutschmark.”

But looking back on the events of 1989-90 today, a different picture emerges. The economic catastrophe in eastern Germany in the 1990s was the logical consequence of the West German government’s unification policy, which was based on the strictures of the market and demanded the wholesale adoption of the West German political-economic order. The West German government’s priority was to retain the established structures of the Federal Republic, rather than build an independent and thus competitive economic region in the former East.

Ultimately, the Federal Republic thus became the benchmark against which the GDR’s reforms were measured. To dismiss the consequences of this as *inevitable* fails to do justice to the historical reality — especially given that structural dependencies still determine relations between the former East and West today. This can be seen, for example, in higher levels of unemployment in the East alongside higher levels of ownership and corporate shareholding in the West.

In this context, a critical examination of the economic and political interests that conditioned German reunification at the time — and the ongoing consequences of those interests — remains essential to understanding the deep inequalities in Germany today.

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