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Similar but different? Comparing economic policy responses to the Corona Crisis in the UK and Germany

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Abstract

This paper presents a comparative political economic analysis of the policy responses to the Covid-19 crisis in Germany and the UK. These two countries responded to this symmetric economic shock with similar furlough and business loan schemes to stabilize both the demand and supply side of the economy. However, highly different political-economic structures in both countries meant these *a priori* similar policies produced different results. We argue that this divergence can best be explained through the lens of Varieties of Capitalism's 'institutional complementarities'.

Keywords: political economy, economic policy, Europe

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1. Introduction

The Covid-19 health crisis has hit the advanced capitalist world hard. In early 2020, only weeks after the first cases were detected in Europe, many workplaces closed, especially in the manufacturing sector. While service workers were able to work at least part of the time from home, that was impossible in industry, where the physical presence of both labor and capital are crucial. Global as well as regional supply chains ground to a halt, factories were mothballed, workers furloughed, and sales points significantly reduced.

The Covid-19 crisis is a tragic but revealing natural experiment to evaluate some of the claims that different schools in comparative political economy, and particularly comparative capitalism studies, have made over the last three decades. It constitutes a symmetric shock to the economic system, eliciting highly similar expansive macroeconomic policy responses, including very similar microeconomic policy instruments such as furlough schemes topping up wages to stabilize the labor market, and grants or inexpensive long-term loans to stabilize the business sector.

At first glance, this suggests that Covid-19 has become the great equalizer. If we could still credibly claim that origins of and responses to the financial crisis followed, at least to some extent, different paths in different countries (Hancké 2013; Johnston, Hancké and Pant 2014; Höpner 2018), the new world after the pandemic seems to play by a single set of rules. All countries were hit the same way, 'best practice' prescribed a shutdown of the economy despite the economic pain, workers were furloughed and/or told not to enter workplaces to avoid contagion, and businesses were shut and kept on life support everywhere. Where, one could ask, is the fabled diversity in capitalism now? Surely looking for variety is, under the circumstances, a bit like re-arranging the deck chairs on the Titanic – not quite a marginal footnote, perhaps, but essentially insignificant given the similarity in the adaptation strategies adopted everywhere, for the same reasons and with the same intended effects.

In this paper, we suggest that this view is wrong. In fact, what is remarkable given the magnitude of the symmetric shock and the similarity of policy responses across the advanced capitalist world, is the significant diversity in the actual processes and outcomes of economic policies. While it is certainly too early to gauge the long-term economic performance effects of the policies, the review of processes, actors, and implementation that we examine in this paper produces one incontrovertible surprising finding: some of the advanced capitalist countries might just as well have been living in vastly different universes. We do not refer here to the obvious incompetence in some governments' initial responses to the pandemic, and to the disparities in health and economic performance (in the UK, in any case, Brexit is certain to throw a massive spanner in the works regardless – see Sampson 2020). Instead, we examine those economic policy responses that were *the same* everywhere because they were considered 'best practice': the active intervention by governments, sometimes against their own ideological predilections or against the underlying logic of their 'model' of capitalism, to stabilize labor markets, employment and wages, and the cash injections for businesses that were stopped from trading.

In the UK and Germany, the two countries at the empirical center of this paper (and prototype liberal market economies LME and coordinated market economies CME in the familiar Hall and Soskice 2001 formulation; Howell 2003), the initial shock was the same, economic policy responses were very similar in almost all relevant respects, but implementation and effects were very different. Foreshadowing our conclusions, the UK's furlough scheme, both the initial one and the revised version of autumn 2020, targeted aggregate unemployment figures and postponed slightly but far from eliminated mass layoffs. Similarly, the business support schemes failed to reach many of their addressees, largely because UK banks lacked the basic knowledge and regulatory arrangements to provide ailing firms with emergency funding. Many businesses ended up closing their doors by the end of summer 2020 regardless of the initial financial aid.

In Germany, the same policies played out differently. The inherent flexibility of German manufacturing and the ability to deploy workers in jobs that had a similar skill basis to produce different goods (what Piore 1986 called *functional* as opposed to *numerical* flexibility), allowed businesses to quickly retool to start producing essential, usually health-related products, and thus remain operative while contributing to the national health effort. The *Kurzarbeit* furlough scheme, in turn, secured employment and, most importantly, allowed businesses to reopen immediately after the downturn with the same highly skilled workforce. Rather than just stabilizing employment levels, the German scheme was an instrument to safeguard the investment in skills by both workers and employers (a skill retention scheme, rather than a job retention scheme). Similarly, banks rapidly dispensed funding to local small and medium sized companies, because they had developed very close relations with them over the years and did not face information and regulatory obstacles as a result (Zysman 1983; Yamamura and Streeck 1993; Deeg 2010). The world for workers and businesses in both countries, which had seemed similar when the virus hit in early 2020, was a very different one indeed on the other side of the pandemic.

These outcomes were so unexpectedly different because of the articulation of the policies with the existing institutional frameworks in labor and financial markets. This goes well beyond the 'weak state' view in Varieties of Capitalism (Wood 2001; Howell 2003). We look at areas where strong governments, with an almost unlimited fiscal and political mandate, adopted what everyone thought of as the gold standard responses to the crisis. In both the UK and Germany these policies significantly ran against the prevailing macro or microeconomic consensus: Germany normally abhors deficits and activist fiscal policy, while ever since the Thatcher era, the UK prefers market forces to sort out an economic crisis. The stage was set for very similar outcomes, yet the opposite happened.

We build this argument on an essential though sometimes downplayed theoretical point in the *Varieties of Capitalism* (VoC) framework: the notion of institutional complementarities (see Hall and Soskice 2001). Tightly interlocking elements in the institutional framework increase or decrease the performance of policies, even if each one individually may be considered perfect or, conversely, sub-optimal. Translated into the case here, the institutional frameworks of both economies powerfully shaped the effects of the policies by refracting them, as it were into different substantive outcomes. The divergence was, in other words, not primarily due to different initial positions in Covid-related health (it was far from clear in February 2020 which country would be hit hardest, a sad price that initially went to Italy with one of the best-funded and organized health care systems in Europe); neither to the incompetence of government (since all governments adopted fundamentally similar policies and the reputation of the British civil service is broadly equal to that of the German administration); nor to differences in industrial structure (German manufacturing was, on paper at least, as much a sitting duck as London's coffee shops; in fact, much of the service sector in the UK stayed in business because of widespread work-from-home arrangements).

The balance of this paper is organized as follows. We start with a review of debates on the broader issue of economic policy responses, in light of the varieties and commonalities of capitalism, and sketch the methodological contours of our study. We will then present the detailed case material, which relies on a combination of public and official statistics, and press material. Labor market policies are our first area, since they offered the template for the economic support policy measures adopted in other areas. A final section brings out the salient issues in the comparison between the UK and Germany and concludes.

2. The inevitability of global capitalism

The Covid-19 crisis is, in terms of (comparative) political economy, perhaps best understood as the latest manifestation of the idea that attention to variety within capitalism has led us to ignore its many commonalities. The latter approach obviously goes back to Marx and Engels (1848), who developed an evolutionary notion of capitalism from primitive forms of accumulation to Britain as the most advanced nation in the world (in the Communist Manifesto, Ch. 1). In the last few decades, however, it has received a new lease on life, first through Susan Strange's (1986; 1998) critiques that comparing different forms of capitalism in the era of *Casino Capitalism* is concentrating on the trees for the forest, and Wolfgang Streeck's recent writings on the commonalities (and imminent demise) of capitalism (Streeck 2016). The basic idea of these approaches is simple yet powerful: In many ways the capitalist political economy cannot be 'tamed'. There may be marginal variations that reflect the historical development of institutions governing labor and financial markets, but as capitalist economies are ever more integrated into the global economy, they take on functional forms that reflect, first, their position in the hierarchical division of labor (with US capitalism at the apex) and, second, increasingly begin to resemble the basic logic of that US-centered system.

Ignoring for a moment the implicit teleology in this argument, most striking is the notion that the international economic order (or disorder, as many of these authors would argue) inevitably trumps the national, often democratically negotiated, economic orders that arose from the social compromises after the first and second world wars. In that light, the financial crisis of 2008-09 was the first sign on the wall. The severity of the crisis was rooted in the fact that all financial systems had, as it were, been sucked into the US-originated orbit; it then threatened the very survival of the global financial system, both the EU and Monetary Union in Europe, pushed up unemployment (and reduced growth) everywhere and generally exposed the fallacy of institutionalist approaches to capitalist variety. Once the tsunami came, even the best swimmers drowned.

In that light, the Covid-19 crisis is simply the second instalment of the same process, only with more of an analytical vengeance. Covid-19 was a massive symmetric shock producing vast uncertainty: It was unclear in February 2020 if Germany, the USA or Greece would be the hardest hit by Covid-19. 'Social distancing' was introduced everywhere, leading to the closure of practically all organizations that require a physical presence for the good or service to be produced: much of the public sector, hairdressers, restaurants, schools and, of course, manufacturing. Only work of this kind that was considered essential could be performed more or less as normal, while the rest of us worked from home or were furloughed, keeping our job but paid a replacement income as long as that job could not be performed. Manufacturing output collapsed as a result, local or regional supply chains dried up and, since the epidemic had reached global proportions very quickly, global value chains lost much of their, well, value. The world, especially the rich OECD countries at first, experienced a sudden stop as a result of a simultaneous supply and demand shock. Global capitalism had suffocated all economies in its immediate sphere of influence, and by summer 2020, was making its way into more peripheral regions such as Latin America and Africa.

The initial symmetric shock of the pandemic elicited symmetric economic policy responses everywhere: macroeconomic 'stimulus' by central banks and finance ministries, wage subsidies and furlough schemes to prop up household incomes and prevent unemployment, and grants or cheap loans to keep businesses afloat. The ECB, the Federal Reserve, and the central banks of Japan and the UK embarked on quantitative easing activities on a scale that dwarfed the bail-out packages the financial sector had received a decade earlier (Cavallino and De Fiore 2020). Finance ministries, even those that up until recently had ignored the negative real interest rates on government debt and insisted on consolidating their fiscal position or imposed austerity, suddenly rediscovered the Keynesian virtue of countercyclical spending.

Germany, Austria, Denmark, Belgium and the Netherlands, some of the coordinated market economies, introduced wage subsidy schemes at a massive scale, as did France, Italy and Spain. Most surprisingly, perhaps, in March 2020, barely a few weeks after the first cases emerged in the UK, the Johnson government also decided to hand out massive wage subsidies, and even the Trump administration in the US installed a furlough scheme – in both cases for a limited time, but soon extended for a few months when it became obvious that the pandemic was not a short-lived crisis. Business grants became the norm everywhere, despite their obvious anti-competitive nature; and state aid schemes for large companies in sectors such as air transport and automotive were introduced, often explicitly ignoring WTO fair trade rules or EU competition policy.[1]

There is no escaping the conclusion, therefore: All advanced capitalist economies, be they CMEs, LMEs or MMEs, faced the same crisis, and they all responded with the same instruments to curb its effects. Covid-19 had finally flattened the world (in

[1] See the Economist "Europe's habit of propping up firms may outlast the pandemic", 28 May 2020 (https://www.economist.com/europe/2020/05/28/europes-habit-of-propping-up-firms-may-outlast-the-pandemic).

Thomas Friedman's 2005 expression), even in those areas where political degrees of freedom had, perhaps, remained most resilient and adverse to change. The attention to diversity within capitalism, with its pinnacle in the *Varieties of Capitalism* school (Hall and Soskice 2001; Hancké et al. 2007) was now revealed to be the misguided attempt at comparative political economy that it had always been. Global forces had eliminated the institutional 'wrinkles' in the domestic make-up of political economies, and a decade after the Great Financial Crisis, the first instalment of crisis-prone global capitalism, Covid-19 and its repercussions sealed that development. A big symmetric, systemic shock yielded symmetric, systemic policy responses. Thus the new conventional wisdom.

There are two important problems with this view, however. The first is 'puzzling evidence': the way these policies played out in practice diverged rather dramatically almost immediately. As we will document below, German banks provided companies quickly with access to emergency loan schemes, while similar efforts materialized much more slowly and were considerably less targeted in the UK. In late summer 2020 the UK's fiscal agency HMRC also reported £3.5bn in furlough fraud and error (about 10% of the total sum spent[2]), while no significant cases of fraud seem to have emerged in Germany. In addition, short-term economic indicators suggest a steeper collapse in the UK (minus 20.4% versus minus 10.1% in Germany[3]), higher unemployment and bankruptcies and (almost certainly) a more difficult recovery.

These outcomes, secondly, are related to a powerful but often underestimated feature of capitalist economies. They are truly 'systems', in the sense that different elements

[2] See the Guardian "Watchdog warns over UK furlough fraud and government contracts", 16 September 2020 (https://www.theguardian.com/uk-news/2020/sep/16/watchdog-warns-over-furlough-and-government-contracts).

[3] See the Office for National Statistics (ONS; https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpfirstquarterlyestimateuk/apriltojune2020) and Statistisches Bundesamt "Pressemitteilung Nr. 287", 30 July 2020

in it have to work in tandem to be effective: Policies that government actors introduce therefore have to be at the very least compatible with the pre-existing systemic elements. Technically this idea is derived from the theory of 'institutional complementarities' (Hall and Soskice 2001; Milgrom and Roberts 1992). The interaction of two mutually reinforcing elements of a particular capitalist system can produce performance effects that are superior to the sum of the performance effects of each of these elements individually, and vice versa – sensible policies may fail in the absence of supporting elements in the institutional make-up. Cherry-picking economic policies therefore does not work in the absence of underlying institutional frameworks that support them. In this particular case, very similar furlough and business grant schemes have fed into different systemic structures in the UK and Germany, which produced these diverging results. In sum, despite the global crisis with similar policy responses everywhere, their effects – understood here as their processual outcomes, not performance – diverged because of these complementarities. Capitalism does seem to come with a manual, in other words (pace Blyth 2003): New batteries in the machine only work if the operator also knows how to use it.

The next section presents detailed empirical material to support this argument. We start with the wage subsidy schemes that set the tone for most other support programs, and then pivot to the business loan and grant schemes. Starting from the obvious similarities, we will, when unpacking their actual operation, slowly edge toward a view of fundamentally different effects because of how these schemes were articulated with the existing institutional settings in labor markets and systems of corporate financing.

3. Tales of the unexpected

On 11 March 2020, the WHO declared Covid-19 a pandemic – a dangerous epidemic that rapidly crossed national borders, engulfed entire continents and required dramatic and strict population confinement arrangements. Two weeks later, governments in practically all OECD economies (with the exception of the US) had imposed measures to curtail the spread of the virus. Because of the particular nature of the virus, infection was difficult to detect, often not until it was too late. Fighting contagion thus implied a complete preventative lockdown of close to entire societies and economies. In a few months' time, GDP fell 10-15% on an annualized basis in most advanced capitalist economies.

Here we examine the economic policy responses in Germany and the UK to this unprecedented social shock. Germany is a prototype Coordinated Market Economy (CME) in the Varieties of Capitalism scheme (Hall and Soskice 2001), the UK a Liberal Market Economy (LME). We expect that in these two countries, policies that are essentially the same in all relevant respects, will lead to different modes of implementation, with substantially different outcomes. We attribute this divergence to the institutional frameworks that govern labor and financial markets and show that this interaction between policies and institutions was guided by their mutual articulation. The test of our argument is simple, therefore: If the results of essentially identical policies are very similar in both countries, capitalist variety would at best be a thin veneer; if they are different, however, and if we can link those differences to structural, systemic elements in the domestic economy, varieties of capitalism remain alive and well.

3.1 Labor market policies in the UK and Germany

In response to the symmetric shock of Covid-19, workplaces in both economies quickly shut down, depriving workers of wages and households of income. Governments in both countries responded by offering wage subsidies to businesses so wages were stabilized even if the company was unable to trade. However, as we will demonstrate, in their actual implementation these policies differed significantly, and their effects therefore diverged as well. In the UK, the initial wage subsidy scheme was generous but ultimately short-lived, and as a result many companies planned mass layoffs in the autumn of 2020. While they stabilized household income to some extent, they had relatively few effects beyond (the admittedly very important goals of) keeping unemployment low and consumption relatively high in the comatose Covid economies. In Germany, the labor market policies were based on the existing 'short-time work' (*Kurzarbeit*) scheme, which allowed for part-time employment and enticed employers to think of ways to retain and hone existing or new skills, since on-the-job training and retraining was permitted under the program. Thus, they not only attempted to stabilize employment and household income, but also supported the development of the skills basis of the German economy.

The schemes looked very similar at the outset. In the UK, if a company shut down or saw its business significantly reduced as a result of the Covid shock, government subsidies would pick up 80% of the gross wage, capped at £2500 (about $3300) as part of the *Job Retention Scheme*, the official name of the program. Applying to the scheme was relatively simple and unbureaucratic. In the UK, the company paid the worker who was not working and asked the government to refund 80% of that salary, while in Germany the company also applied for the difference between the salary paid and the salary covering time worked. The standard was that up to 60% of the salary was paid. Neither country required detailed documentation of financial problems.[4] For its

[4] See Wired "The UK's coronavirus furlough scheme, explained by experts", 29 July 2020 (https://www.wired.co.uk/article/uk-furlough-scheme-job-protection) for a concise and transparent description of the UK scheme. HMRC. 2020. "HMRC Coronavirus (COVID-19) Statistics." London, UK: HMRC (https://www.gov.uk/government/collections/hmrc-coronavirus-covid-19-statistics) gives statistical details on the schemes. A description in English of the German scheme can be found in Bloomberg "Explaining Kurzarbeit, or Saving

furlough scheme, Germany relied on the *Kurzarbeit* model, developed in response to the 2008-09 financial crisis, which allowed for partial wage subsidies if a company retained its workforce in part-time employment. In the UK, in contrast, the subsidy was all or nothing (at least until 1 July 2020, when partial wage subsidies were introduced for companies already in the scheme). Unsurprisingly, these schemes had the support of business organizations and trade unions in both countries (see Coulter 2020 for the UK) and even the opposition (on the left in the UK and on the right in Germany) agreed that the schemes were necessary for at least the immediate future.

Relatively small differences between the schemes, often deeply embedded in the institutionalized employment systems of both countries, mattered significantly for their implementation and effects. The German *Kurzarbeit* scheme is more than just a temporary arrangement to avoid unemployment. Employers are supposed to keep their workers on the books after the wage subsidy scheme runs out; in fact, in August 2020, *Kurzarbeit* was extended until late 2021 on existing terms to make that outcome a quasi-certainty. UK employers are under no such obligation: The scheme was – as its name suggested – a job retention scheme but nothing else. Chancellor (i.e. Finance Minister) Sunak explained ending the scheme in October 2020 by stating that it might create false hopes of stable jobs.

In addition, because of the strict (some would say 'rigid') working time arrangements in Germany (Locke and Thelen 1995), which are carefully monitored by employee representatives, it was relatively easy to calculate part-time employment. The part-time wage subsidies under *Kurzarbeit* therefore were a transparent and collectively policed possibility. The flexible working time arrangements in the UK, negotiable between individual employees and employer, particularly outside the regulated public sector, made such a calculation of working time percentage very difficult. In

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Jobs the German Way", (https://www.bloomberg.com/news/articles/2020-04-03/how-germany-pays-workers-when-their-work-dries-up-quicktake).

order to avoid the inevitable potential for fraud, the scheme, somewhat bluntly, only accepted 100% furlough requests.

Implementation of furlough schemes

By the summer of 2020, when the British scheme in its initial form ended, about 9.6m workers were furloughed, spread over 1.16m companies or 61% of eligible employers. The hospitality sector has had the highest furlough rate of 77%, while the retail sector furloughed the highest number of workers (all data from the official website of the fiscal agency; HMRC 2020). The German numbers are comparable. Half of all companies in the country had applied for wage support, covering about 10m workers or roughly 25% of the workforce. In some industries, such as hospitality, automobiles and aviation, over 90% of employees found themselves in *Kurzarbeit* schemes.[5]

The two labor markets were not the same, of course, even before we examine the effects of regulatory and institutional frameworks. Self-employment is considerably higher in Britain, for example. An estimated 17.9% of the UK workforce fell in this category[6], which were compensated under the business loan and grant schemes that we discuss later in this paper. In addition, since working times are fixed through collective negotiations in Germany, companies could flexibly request partial wage subsidies while production continued. However, with only a high upper ceiling of 48 hours in the UK, requesting part-time wage subsidies was impossible because it was not easily enforceable. The gross sums spent in the UK wage schemes were therefore

[5] See Deutsche Welle "Why Germany's reduced hours scheme won't work long term", 11 May 2020 (https://www.dw.com/en/why-germanys-reduced-hours-scheme-wont-work-long-term/a-53377212).

[6] See Office for National Statistics "EMP14: Employees and self-employed by industry", 11 August 2020 (https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/datasets/employeesandselfemployedbyindustryemp14).

higher than they needed to be and probably the collapse in output was also higher because a company was either operating at 100% regardless of the actual orders, and therefore paid full wages but lost a part of the revenue as a result of lower output, or closed entirely, which meant that its contribution to GDP fell to zero.

Finally, the 'rigid' labor market in Germany paradoxically proved an excellent basis from where to start when companies decide to shift production to what were seen as 'essential products', usually associated with the health sector. In late April 2020, the manufacturing company *Viessmann*, for example, started producing portable ventilators, mobile care units and face masks instead of their usual heating units. They did so in close cooperation with doctors from local hospitals and academic experts from the prestigious local technical university RWTH Aachen – a form of cooperation that is far from unusual in Germany (Viessmann 2020).[7] In a parallel case in the UK, which offers an almost perfectly matched comparator, such a conversion proved much more difficult: While many observers rightly lauded *Dyson*, the manufacturer of high-end vacuum cleaners, for being able to design a functioning ventilator in ten days[8], in their idolatry they ignored that the actual retooling of the plants and the concomitant conversion of the workforce was considerably less successful (surprisingly, the Daily Mail, usually among the more nationalist voices in the UK, was the only one to raise this counterpoint[9]). Unable to gain the contract, *Dyson* ended the project a few weeks

[7] In addition to Viessmann's press release, see Handelsblatt "Heizgeräteehersteller Viessmann baut nun auch Beatmungsgeräte", 20 April 2020 (https://www.handelsblatt.com/unternehmen/mittelstand/familienunternehmer/familienunternehmen-gegen-corona-heizgeraeteehersteller-viessmann-baut-nun-auch-beatmungsgeraete/25752624.html?ticket=ST-2272808-aybJrtDWpjwSwhpbJ03W-ap2).

[8] See two related articles in the Financial Times "Dyson to produce 15,000 ventilators from scratch 'in weeks'", 25 March 2020 (https://www.ft.com/content/4cc667f2-6ee2-11ea-89df-41bea055720b); and "Muddled thinking punctures plan for British ventilator", 17 April 2020 (https://www.ft.com/content/5f393d77-8e5b-4a85-b647-416efbc575ec).

[9] See Daily Mail "Could Dyson and Rolls Royce REALLY make ventilators to treat coronavirus victims? Experts warn converting production lines to build life-saving equipment will take 'many months'", 16 March 2020 (https://www.dailymail.co.uk/sciencetech/article-8117847/Dyson-JCB-Rolls-Royce-face-problems-making-ventilators-experts-warn.html).

and £20m later. The upshot was that while many German manufacturing firms, especially among the famous *Mittelstand*, stayed in business in new product lines, many of their British counterparts closed their doors and sat out the lockdown under the tight distancing rules.

Sectoral coverage was quite similar in both cases but, again, with very different effects. Large parts of the manufacturing sector were affected by closures, as were bars, cafés and restaurants. All of these were closed in the UK lockdown, making about 200,000 workers in the hospitality sector technically unemployed (HMRC 2020).[10] While restaurants and bars did not formally close in much of Germany, the drop in trade resulting from the lockdown meant that over 90% of businesses in the sector applied for wage subsidies. The reliance of the British economy on services is often seen as the driver of the greater fall in output and higher rise in unemployment. Inasmuch as this refers to low-productivity, low-wage service companies with intensive face-to-face contacts, such as bars, restaurants, hairdressers and personal beauty care, this seems correct. But in other service sectors, usually associated with higher value-added activities such as consulting, finance and law, distancing proved less of a problem – definitely less than in manufacturing, which requires physical presence of both worker and machine, especially in the sophisticated high value-added manufacturing sector for which the country is internationally famous. Thus, all other things equal, manufacturing would have been among the worst hit sectors in this pandemic, and Germany should have been on its knees very quickly. However, because of the intrinsic *functional* flexibility of the German manufacturing sector, what should have been a catastrophe turned into a relative success, while Britain's high employment

[10] See data from the Office for National Statistics, not seasonally adjusted.

numbers in low value-added sectors that were unable to trade significantly increased unemployment.

Mass redundancies provide an area with highly consequential differences in the institutional background of labor market policies. In the UK, the lay-off procedure is basically governed by individual labor law. An employer announces redundancies and unless there are collectively negotiated deviations, the law stipulates how much notice every worker needs to be given, and what the redundancy package entails. The arrangement is far from generous, especially by continental standards: One week of notice pay if employed for less than two years, and an extra week of notice pay for every year with the same employer. The flexible labor market in the country leaves the initiative, with very few constraints, entirely to employers. Since many UK companies, especially SMEs, often live hand to mouth with very low savings, the path of redundancies is usually the fastest, 'tried and tested' way to cut costs; larger companies do so because of shareholder pressures. The overall effect is that significant drops in economic activity are almost immediately reflected in rising redundancies and unemployment. Ultimately, employees and the welfare state have paid the cost of the economic downturn associated with Covid-19.

Arrangements in Germany follow a fundamentally different logic. Collective redundancies are always subject to wide consultation with the works council, collective negotiations with trade unions, or some form of bargaining with other workforce representatives. Importantly, the costs of the social plan that follows these negotiations are in principle borne by the company, and because of the power of the unions and works councils inside the companies they usually entail quite generous redundancy packages. Coupled with the possibility of applying to *Kurzarbeit* schemes, the calculation for individual employers is almost the exact opposite of their UK counterparts: instead of unilaterally deciding on mass redundancies, German employers prefer the wage subsidy schemes. These allow them to retain their skilled workforce at a reduced cost (which, therefore, also entices worker and employer to jointly invest in skills; Hassel 2007).

Making sense of the differences in wage subsidy programs

The most intriguing conclusion of this detailed analysis of different aspects of the ostensibly very similar wage subsidy schemes is that even after only a few months of implementation, their effects appeared to diverge significantly. To a large extent, these different effects are embedded in the different institutional frameworks of the labor market. The absence of strict and closely monitored working time patterns in the highly flexible UK labor market has made part-time wage subsidy schemes very difficult to organize. Preventing fraud meant that companies either worked full-time or were closed full-time. It was very difficult to organize a program that sat between these two extremes. In Germany, in contrast, the rigid working time patterns across the economy, which are policed by works councils and trade unions, have not led to a total collapse of the economy due to insufficient flexibility. They have actually been the foundation of the successful *Kurzarbeit* scheme, which have allowed companies to produce on a part-time basis without increased costs for them and wage losses for workers.

The nature and organization of skills is another area where superficially small differences led to big consequences. The intrinsic functional flexibility of highly skilled German workers (Piore 1986) has made possible the rapid and successful adjustment of companies in response to collapsing product markets and the emergence of new demand. In the UK, in contrast, top-level product engineers redesigned products to meet the same goals in a matter of days; yet, reorganizing the company and the workforce to actually start making the new products proved too high a mountain to climb.

Similarly, the different organization of mass layoffs has meant that German employers think again when production falls, lest they face social conflict, a high redundancy bill and the loss of valuable skills. British employers, faced with the end of the Job Retention Scheme, were subject to almost diametrically opposed incentives and laid off large parts of their workforce to cut costs in attempt to balance the books.

The short-term economic outcomes were very different as well. German employment and economic growth fell considerably less than in the UK. The flexible labor market in the UK was unable to alleviate the crisis situation. In fact, without wanting to push this point too far, key elements of that same flexibility seem to have exacerbated the already quite tenuous situation that Britain found itself in during and after the lockdown of spring 2020. And in a case of deep irony, key elements in the same dimensions but mirroring the British ones, allowed Germany to adapt quite successfully to the rapidly shifting economic environment.

As time has gone on, these differences have, arguably, only become clearer. In late September 2020 faced with a second Covid-19 wave and rapidly rising unemployment as a result of renewed lockdowns, UK Chancellor Sunak introduced a new version of the furlough scheme that was scheduled to run out in its current form at the end of October. It is copied directly from and is even closer to the German *Kurzarbeit* program than the original furlough scheme. It introduces a part-time wage subsidy for companies that have planned to retain workers but are uncertain about being able to work at 100% of capacity. The state will pick up a maximum of 22% of the salary (with a monthly cap of about £700/month – about $1000), down from 80% initially and 60% in the final stages of its predecessor, with a monthly maximum of £2500. Employees forego a third of their wages – 30% part-time work being the floor at which the scheme kicks in; and employers contribute the remainder, which is about 55% of the monthly wages, up from about 20% under the old scheme. The projected savings for the Treasury is about two-thirds compared with the initial scheme, or several billions of

Pounds Sterling per month, in large part by shifting the financial burden onto employers.

Since the wage subsidy scheme now looks almost exactly like the German one (but with a high relative contribution by employers) we are even better able to isolate those elements that are necessary to make such a scheme work. Three crucial differences at the basis of the German success stand out – and their absence in the UK does not herald well for the new scheme. Firstly, the German set-up combines juicy carrots and heavy sticks in the background. Employers have invested significantly in the skills of their workforce, which makes them reluctant to see those go. *Kurzarbeit* is, in that sense, as much a job retention scheme as a program to retain and develop skills. The stick is given by the highly institutionalized and, therefore, expensive mass lay-off procedure discussed earlier. Incentives for employers are therefore heavily skewed in favor of participation in Germany. Secondly, often ignored in the debate on the German system, in large part because it is such an organic element of the current industrial relations set-up, is the highly organized form of micro-corporatism in German companies. Workers and employers jointly negotiate and organize the actual operation of the scheme, even though the employer applies to the Ministry of Labor for funding. Finally, a similar point can be made for the macro-level 'embeddedness' of these measures: in many CMEs, with corporatist national labor market institutions, discussing such schemes in response to a crisis is standard practice, while in LMEs the introduction of such schemes is the result of *ad hoc*, topical negotiations *during* the crisis, not before, and crucially dependent on government initiatives.

Combined, these three elements – the incentives, the micro-corporatist and the macro-corporatist structures – are prominent in the German case (and many other North-West European political economies), but almost entirely absent from the UK scheme. Skill development remains the Achilles Heel of the British training system, while employers can hire and fire more or less at will; company industrial relations remain adversarial and mired in mutual distrust; and the encouraging signs of agreement between social partners at the start of the crisis (Coulter 2020) may well turn out to be a simple temporary alignment of short-term interest once the shift in the financial burden is absorbed.

The next section undertakes a parallel analysis of the business loan and grant schemes, which were introduced for similar reasons to the wage schemes – the inability to trade – in both countries in very similar ways. Like our analysis of the wage schemes, the finance scheme suggests that something that looked quite similar at the outset ended up working in very different ways in both countries, and to large extent this had to do with the position of the financial system in the political economies of the UK and Germany.

3.2 The institutional underpinnings of business emergency loans

Once the extent of the Covid-crisis had become clear, governments throughout Europe were quick to prepare their fiscal arsenal in order to safeguard domestic business from an unprecedented downturn. In Britain and Germany, governments turned to the complex mix of tax cuts and deferrals, employment and welfare support, and direct grants and business loan support schemes. Here we analyze the implementation and effects of these business support schemes. In the first six months of the crisis (between early March and August 2020), the UK has directly loaned or guaranteed about £53bn while the figure in Germany stands at around €54bn. What is more, these programs have resembled each other in terms of substance as well. Despite these similarities, however, there have been substantial differences in their implementation, target groups and, as a result, their effectiveness.

Comparing business support schemes

At the heart of British and German efforts lay fundamentally similar business support policies that offered cheap and easily accessible credit to help firms weather the Covid storm. In mid-March 2020, the German government announced its widely targeted *KfW-Unternehmerkredit* (company credit supplied and underwritten by the public investment bank *KfW*) while the British Treasury launched two separate schemes with the Coronavirus Business Interruption Loan Scheme (CBILS) for SMEs and the Covid Corporate Finance Facility (CCFF) for large companies. Both countries then complemented these initial policies with another wave of initiatives targeting firms that struggled to access credit under the first round of schemes. The UK introduced the Coronavirus Large Business Interruption Loan Scheme (CLBILS), the Future Fund and its Bounce Back Loans, while Germany initiated the *KfW-Schnellkredit* ('instant loan' program).

The British and German flagship policies, CBILS and *KfW-Unternehmerkredit* respectively, resembled each other in many ways. Both schemes allowed businesses access to cheap credit by providing banks with substantial government guarantees while allowing generous repayment periods. In Germany, the government backed 80-90% of business loans depending on firm-size, with a two-year grace period on repayments. The British Treasury, in turn, provided a fixed 80% guarantee in addition to covering fees and interest-payments for the first 12 months. In both cases, the policies were implemented through government-backed investment banks in partnership with local banks. In Germany, the *Kreditanstalt für Wiederaufbau* (*KfW* – literally 'Credit Agency for Reconstruction') assumed its long-standing role as provider and guarantor of special loans. These were processed by the house banks (or *Hausbanken* in German; henceforth, we will use this term to designate all banks that have long institutionalized relations with firms of all sizes) of the applicants. In much the same vein, the British Business Bank (BBB) administered the government's business lending programs. However, rather than accepting applications from any UK-based bank the BBB organized a pool of accredited lending institutions (initially 40, expanding to 102) to take part in the scheme.

Despite their many similarities, there were some clear differences between the CBILS and *Unternehmerkredit*. Interest rates, for example, were set at a fixed rate in Germany while British banks operating under the Coronavirus Business Loan Interruption Scheme were free to set their own rates. Moreover, the *Unternehmerkredit* scheme allowed firms of any size to participate and offered loans of up to €100m. CBILS, by contrast, was specifically aimed at businesses with a maximum turnover of £45m, with loans of up to £5m only. After initial pushback, the British Treasury balanced its SME-focused CBILS by organizing the Covid Corporate Finance Facility (CCFF) in cooperation with the Bank of England (BoE). CCFF targeted large investment grade corporations by having the BoE directly buy up commercial paper issued by corporations. The minimum issuance, in this scheme, stood at £1m with a maximum maturity of one year.

In addition to these initial programs, both the German and the British government further bolstered their fiscal support for businesses with new schemes during the months that followed. Already in early April 2020, Germany introduced the *Schnellkredit* catered to smaller and younger businesses that struggled to access credit under the *Unternehmerkredit.* In contrast to the latter, this new program offered lines of credit up to €800,000 at a fixed 3% interest rate with a full 100% guarantee from the *KfW*. The UK, similarly, introduced the so-called Bounce Back Loans (BBL) targeting micro-firms with loans between £2,000 and £50,000 at 2.5% interest and a 100% guarantee to address the problem of mounting credit hold-ups for small firms. The British government supplemented this scheme with the announcement of the Future Fund and Coronavirus Large Business Interruption Loan Scheme (CLBILS). The Future Fund specifically aimed at providing direct liquidity to start-ups which could not access existing schemes stipulating that businesses needed to show profitability.

The Coronavirus Large Business Interruption Loan Scheme, on the other hand, expanded CBILS to include firms with a turnover above £45m as it soon became clear that a substantial share of businesses could neither access CBILS nor CCFF.

The effects of loan schemes in Germany and the UK

While these financial support packages were tailored to help certain groups of businesses, they also left others out of the reckoning. This is particularly the case for the UK where the initial policy response along the lines of CBILS and CCFF explicitly excluded two types of firms. On the one hand, businesses that were not (yet) profitable remained outside the schemes' purview, as the Treasury was apprehensive about artificially propping up already struggling firms.[11] Many profitable medium and large enterprises, on the other hand, also had nowhere to turn to because CBILS support capped annual turnover of applying firms at £45m while CCFF targeted the very largest companies in the UK, few of which would have struggled to access funding in the first place. While the introduction of the Coronavirus Large Business Interruption Loan Scheme in April 2020 did appease this previously neglected group, the Bounce Back Loans clearly signaled that the government's priorities lay with the two extremes in the size distribution – the very big corporations and the very small shops on the local high street.

This outcome contrasts sharply with what happened in Germany. First of all, German stipulations of pre-Covid profitability were more lenient, only making it a hard condition for loans *exceeding* €800,000. Moreover, the *Unternehmerkredit* was a more broadly oriented instrument. Not only did it not make any stipulations regarding firm

[11] See reports in The Daily Telegraph "Germany's 100pc guarantees highlights shortcomings of UK loan scheme", 8 April 2020 (https://www.telegraph.co.uk/business/2020/04/08/germanys-100pc-guarantees-throw-spotlight-ailing-uk-loan-scheme/); and Daily Mirror "Coronavirus-hit firms get 100% backing for loans in major government U-turn", 27 April 2020 (https://www.mirror.co.uk/news/politics/breaking-coronavirus-hit-firms-100-21934344).

size, but the wide range of available loans made it an attractive proposition to businesses of all sizes. Most importantly, the close ties between firms and their *Hausbank*, the financial institution that they would normally do business with and which had detailed knowledge of the company's credit situation, significantly simplified the emergency loan application process.

Yet some firms in Germany initially struggled to access the liquidity necessary to stay afloat. After the introduction of the *Unternehmerkredit*, SMEs and their representative associations complained that they were facing insurmountable obstacles trying to convince banks to guarantee 10% or 20% of the share of loans that were not covered by the *KfW*.[12] This was especially the case for those firms that had made significant investments in the run-up to the Covid crisis and had been temporarily in the red as a result, as well as for those whose business models were most affected by the economic shutdown. In addition, recently established firms were also shut out as businesses that had spent fewer than five years on the market were not eligible. The government reacted to these concerns with the introduction of the *Schnellkredit*, providing fully covered loans, but capped at €800,000 per application.

As a result, though very similar on paper, the effects of British and German business support programs almost perfectly mirrored each other. In the UK, those firms that required help most urgently, also seemed to struggle most to get it as CBILS proved highly ineffective. In fact, in the first week of implementation only 983 out of 130,000 applications were approved, amounting to a grand total of only £90m in cash disbursements.[13] In April 2020, the British Chamber of Commerce polled that only 13%

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[12] See Wirtschaftswoche "Corona-Kredite: Das 10-Prozent-Problem", 3 April 2020 (https://www.wiwo.de/my/unternehmen/banken/hilfe-fuer-unternehmen-corona-kredite-das-10-prozent-problem/25711258.html?ticket=ST-1256727-ciu0zmaJCznCfvu52Nxa-ap6).

[13] See The Guardian, "130k inquiries, 1k loans: why UK government had to tweak help to small firms", 2 April 2020 (https://www.theguardian.com/business/2020/apr/02/130k-inquiries-1k-loans-why-uk-government-had-to-tweak-help-for-small-firms).

of applications had been successful while the remaining were either left unprocessed or denied.[14] Data on SME business lending during March and April 2020 support this conclusion: while lending among large corporations spiked in March, a similar surge for SMEs only emerged at the end of April.[15] Finally, low numbers of total applications indicate that not only were many firms unsuccessful with their applications, more importantly, many were simply ineligible for the support schemes in the first place. This included businesses exceeding £45m in turnover but not in the top 100.

In Germany, the situation of these medium-sized firms was much more favorable. Supported by their house banks, applications were submitted swiftly and passed on to the *KfW* where automated assessments guaranteed extremely high acceptance rates. In stark contrast to the UK, however, the smallest firms, especially those with fewer than 11 employees – making up 89% of all businesses[16]– and the self-employed faced an uphill battle. They were excluded from the *KfW Schnellkredit* and had to apply for emergency grants from their local governments in the *Länder* instead. Given caps on the size of programs, the bureaucratic cost of applications in many cases far exceeded

14 See the British Chamber of Commerce "BCC Coronavirus Business Impact Tracker: Loan schemes still slow to help many cash-strapped firms – but furlough scheme preventing redundancies", 29 April 2020 (https://www.britishchambers.org.uk/news/2020/04/bcc-coronavirus-business-impact-tracker-loan-schemes-still-slow-to-help-many-cash-strapped-firms-but-furlough-scheme-preventing-redundancies).

15 See the Bank of England, Monetary financial institutions' loans to UK small and medium-sized enterprise.

16 See Statista "Anzahl der rechtlichen Einheiten in Deutschland nach Beschäftigtengrößenklassen im Jahr 2018" (https://de.statista.com/statistik/daten/studie/1929/umfrage/unternehmen-nach-beschaeftigtengroessenklassen/#:~:text=Rechtliche%20Einheiten%2F%20Unternehmen%20nach%20Beschäftigtengrößenklassen%202018&text=Im%20Jahr%202018%20gab%20es,statistischen%20Unternehmensregisters%2F%20Registerstand%3A%2030).

the utility of the grants available to them and cases of fraud further hampered the efficacy of the support schemes.[17]

Thus, the puzzling result when comparing the effects of business support schemes in the UK and Germany is that the very companies that fell through the cracks in the UK experienced the strongest support in Germany *and vice versa*. While SMEs from Germany's famed *Mittelstand* faced only very limited challenges in applying for emergency aid, the traditional high street shop was left out.

The institutional foundation of diversity in business support schemes

Why did these two largely similar emergency loan programs in the UK and Germany produce such different outcomes? The answer lies largely in the organization of the domestic financial systems. In the UK, two fundamental problems effectively shut out medium-sized businesses: an information and an incentive problem. Private banks that wanted to participate in the emergency loan programs had to apply and register with the British Business Bank. Given unclear risk and cost structures, this limited the number of banks participating in the schemes and created a bottleneck from the outset. Many applicants that were in dire need of financial support therefore could not work with their usual credit institution, while those lenders that had most expertise in working with SMEs were unable to act as facilitators, which left many SMEs in the uncomfortable position of having to convince anonymous lenders of their creditworthiness. For CBILS in particular, these credit assessments were automated through centralized application platforms that were plagued by glitches and resulted in very high denial rates. In addition, the British Business Bank approved lenders on a rolling basis, which resulted in swift approvals of the UKs largest private institutions,

[17] Note that business grant schemes are independent from the government-backed loan schemes in substance and practice. The former concerns direct transfers from the government to firms and does not rely on banks acting as intermediaries. The higher degree of anonymity might serve as an explanation why Germany saw relatively more instances of fraud in the grant scheme than in the loan programs; see Financial Times "Germany cracks down on coronavirus aid fraud", 19 April 2020 (https://www.ft.com/content/c2123b10-2fa5-4fe7-9422-44de8541f527).

principally Barclays, HSBC, NatWest and Lloyds. These four banks together ended up dispensing 89% of the funds under the Coronavirus Business Interruption Loan Scheme. While they provided the government with scale and capacity, these banks also relied most on standardized application processes with the least granular information on SMEs.

These information problems were exacerbated by gravely misaligned incentives, which put private banks in a difficult position. As the government did not set fixed interest rates for the loan programs, the costs to banks of emergency loans were mounting and, in many instances, eligible applicants were nudged into regular loan products which were more profitable to private lenders. Moreover, at the outset of CBILS much uncertainty prevailed over the right of banks to demand collateral in the form of personal assets from applicants. Many applicants, particularly smaller firms, thus were priced out of loans during the early weeks of the program. These problems were effectively tackled only when the government introduced the Bounce Back Loans scheme that guaranteed 100% of the loans at a fixed 2.5% interest rate while expanding eligibility criteria, making it virtually impossible for banks to demand collateral. Unsurprisingly, data indicate that the Bounce Back Loans program has by far been the most popular support scheme in the UK: by mid-August 2020, BBL had lent over £35bn compared to £13.5bn under CBILS. The 'Malthusian' high-street shops received most political attention and support after the initial failures of the program, and policy emphasized protecting unemployment statistics that were certain to explode when support schemes turned out to be ineffective in stabilizing these very small and micro businesses.

In Germany, the institutional preconditions of the financial system were very different. Most importantly, banks of all sorts and sizes were in principle eligible and motivated to participate as facilitators in the support schemes. At the micro-level, relational lending constitutes a deeply institutionalized element of Germany's post-war financial system (Zysman 1983; Deeg 1998; Hall and Soskice 2001). Small and medium-sized businesses in particular have maintained close personal relationships to their *Hausbanken*, which do not only hold significant knowledge about their clients' credit history, but also about their business models, market position, and long-term strategies. [18] At the meso-level, the publicly guaranteed *KfW* implemented the government's support schemes. Established in 1948, *KfW*'s founding purpose laid in supporting reconstruction efforts by facilitating and distributing funds from the Marshall Plan. Over the course of its 70-year long history, the *KfW* has specialized in distributing its AAA-rated government-backed capital by providing affordable loans to domestic and international clients, often facilitated through local *Hausbanken*.

When Covid-19 struck, this allowed the German government to fall back on a deeply institutionalized system of bank-to-business and bank-to-bank links that could easily be deployed as a public utility. Data on the share of *Unternehmerkredit* and *Schnellkredit* by bank type illustrate this point. For both kinds of programs, public savings banks and cooperatives shouldered over two-thirds of the volume of loans while holding a total market share of only around 30%. Furthermore, banks were actively incentivized to participate in the loan programs by being promised an interest margin of 0.2% and a one-off payment of €1,000 per application while taking on no or very low credit risks.[19] The combination of these conditions resulted in extremely high acceptance

[18] One might reasonably suspect that the dependence on the close ties between *Hausbanken* and firms invited fraud. *Hausbanken* could be much too positively predisposed towards ailing SMEs to be trustworthy facilitators. But there are currently no registered cases of fraud in the business loan programs. Given the critical attitude of the opposition parties – notably the Greens and the liberal FDP – to the business loan schemes, such cases would quickly have surfaced if they existed. The main reason for this absence of fraud seems related to the residual 10-20% that banks have to cover from their own funds – at least for the *Unternehmerkredit* scheme – the grave reputational costs to banks, and ultimately the severe penalties, including up to five years jail.

[19] See FinanzSzene "Banken erhalten je KfW-Schnellkredit 1000 € plus 0,2% p.a.", 13 April 2020 (https://finanz-szene.de/banking/banken-erhalten-bis-zu-2600-euro-je-kfw-schnellkredit/); and Handelsblatt "EU gibt grünes Licht für KfW-Schnellkredit", 13 April 2020

rates of 99.95% of all loan applications that passed the initial assessment stage at the *Hausbank* level. Compared to the informational hold-ups experienced in the UK, this swift exploitation of the infrastructural position of the *Hausbanken* to distribute loans shows that the public utility function of Germany's secondary banking sector remains a central aspect of the German political economy.

Yet, all that glitters is not gold, even in Germany. Critics from the ranks of Germany's opposition parties, most notably Green party representatives, have voiced increasing concerns about Germany's emergency loans program.[20] They suggest that exceptionally high acceptance rates indicate a lack of credit risk assessment which may provide the basis for the rise of so-called 'zombie firms', that is, failed businesses on life support.[21]

While it is too early to evaluate this risk, arguably more worrisome than those businesses receiving help that they do not deserve, are those that need it most but cannot access funding. As with every deeply institutionalized system, it seems to work well for insiders but discriminates against those who lack access. In contrast to the UK, the very smallest firms in Germany have struggled to get the help they needed. As discussed earlier, businesses with fewer than 11 employees, including the self-employed, were *a priori* excluded from *KfW* loan programs. These could not rely on the infrastructural support and reputation of a *Hausbank*, and when lacking relevant collateral, they had only the state financial authorities to turn to. Many of the smallest

(https://www.handelsblatt.com/finanzen/banken-versicherungen/coronahilfen-eu-gibt-gruenes-licht-fuer-kfw-schnellkredit/25735270.html?ticket=ST-1689716-RWK9hIUGs6RAzbZbzN2G-ap4).

[20] A term famously coined by Germany's finance minister Olaf Scholz (SPD).

[21] See Financial Times "Germany haunted by spectre of zombie companies", 20 August 2020 (https://www.ft.com/content/5d5d1bc1-61a3-46a9-915c-1a1e6f2e5fd2?shareType=nongift).

businesses therefore complained that financial aid was not provided fast enough and that they felt abandoned during the process.[22] Whereas British policies seemed to protect its smallest and largest firms but not its SMEs, the German schemes ended up protecting the latter, the heart of the country's economic model, but did so at the expense of the former.

In sum, despite initiating ostensibly similar business loan programs, the effects of these financial interventions in Germany and the UK could hardly have been more different. Not only did the British programs suffer from comparative inefficiencies during their first weeks, the Treasury's policies targeted a different set of firms compared to the plans implemented by their German counterparts. The German programs sought to stabilize the country's industrial base of *Mittelstand* firms while the British government targeted very large and very small firms at either extreme of the scale. This puzzling gap between the similarity of the formulation of these policies and their diverging outcomes is a function of variation in the supply-side institutions in Germany and the UK. In the former, the crisis programs are an extension of deeply institutionalized relations between firms, banks and the state. These institutional legacies allowed German banks and the *KfW* to overcome information asymmetries regarding firms' solvency. The German banking sector thus could do what it has done so well for decades – act as the key cog in business-state relations to facilitate industrial development. Instead of ending up in the dustbin of history with the large commercial banks (Hardie et al. 2013), relationship banking, the model at the core of the German system, showed its strengths during the Covid-19 crisis.

In the UK, on the other hand, financial support for businesses is a purely countercyclical tool. In its essence, the Coronavirus Business Interruption Loan

[22] See FinCompare "Zu wenig Hilfe für den Mittelstand", 31 July 2020 (https://www.barkowconsulting.com/wp-content/uploads/2020/08/200811-FinCompare-Studie_-Die-Corona-Hilfen-kommen-nicht-im-Mittelstand-an-2.pdf).

Scheme is a rerun of the 2009 'Enterprise Finance Guarantee' designed to stabilize during the last credit crunch. Whereas the German government explicitly decided to work through the *KfW*, the UK had no choice but to engage with commercial banks. Lacking the institutional resources available to Germany, the Treasury ended up introducing Bounce Back Loans to overcome the limitations of CBILS. It should be no surprise, then, that Bounce Back Loans have ended up functioning as the most important funding line for British business while the comparable *Schnellkredit* has, at best, been a residual measure for Germany.

4. Conclusion: Varieties of Capitalism's revenge

News of the death of capitalist variety may have been exaggerated. The debate in comparative political economy after the great financial crisis of the late 2000s had taken a distinctly non-comparative turn. Global capitalism was raising its ugly head again: the postwar era of seemingly tamed capitalism, subjected to a variety of national, domestic political and institutional arrangements, had come to an end by the turn of the century, dramatically exposed in the 2008-09 financial and economic crisis, the dress rehearsal for the economic chaos in the wake of the Covid-19 pandemic.

Crises such as Covid-19 offer a window into the key mechanisms that make a political-economic system tick: what could be disguised under a thin layer of normality in other periods, forces itself to the forefront in such moments of high tension. A detailed analysis of the responses of governments in two very different varieties of capitalism, the CME Germany, and the LME UK, to the economic fall-out of the health crisis at first glance seems to confirm the theory of institutional convergence. A similar shock in different systems led to essentially the same economic policy responses, carried by different government coalitions but with similar support from business and labor. A more nuanced analysis of the economic policies as part of a set of mutually reinforcing institutional arrangements – ‘complementarities’ in the VoC jargon – suggests a very different conclusion. Both the furlough and the business support schemes were implemented in very different ways in both places, and with diverging effects. In combination with other elements in the institutional set-up, furloughs schemes minimized unemployment but also, importantly, preserved high, specific skills in Germany while mainly acting as a short-term buffer to unemployment shocks in the UK. Small and medium-sized enterprises did well out of the loan schemes in Germany but not in the UK, while the very largest and smallest companies benefited in the UK but considerably less so in Germany. Wherever we look, policies that appeared to be part of the same broad family of fiscal responses ended up producing very different effects – mainly as a result of how they interacted with underlying systems and strategies on the supply side of the economy. Varieties of capitalism are alive and well, in other words, in Berlin and London – and therefore almost certainly elsewhere as well.

As a consequence, our findings also hold important implications for the vibrant debate on the reach of global financialization and the convergence of national financial systems (Van der Zwan 2014). There is no doubt that the German banking system – once the hallmark of Zysman’s (1983) ‘bank-led’ system – has become more ‘market-led’ as a result of increased disintermediation and exposure to global financial markets (Hardie et al. 2013). Even some of the more conservative savings banks, it seems, are not immune to the lure of new financial products and services (Schwan 2020). But these developments should not hide the fact that existing institutional arrangements tend to be quite durable and that as a result, both, financialized and relational styles of banking can co-exist.

In fact, the swift exploitation of the infrastructural position of the *Hausbanken* to distribute loans shows that the public utility function of Germany’s secondary banking sector remains as central to the system as ever. While large commercial banks did indeed turn to Wall Street, most of the smaller local banks remained true to their traditional role of providers of industrial credit and served as the gatekeepers to business support schemes during the crisis. Deeg (2009; 2014) suggested, in fact, that this process of institutional bifurcation has effectively protected large parts of the German financial system from the pressures of international markets, rather than absorb them into the global financialization vortex. Our findings suggest that most banks in coordinated market economies still seem to have the capacity to serve as active intermediaries and engage not mainly or exclusively with other financial actors, but also – and crucially so – with the real economy. Our results demonstrate that, more than simply retaining its institutional features, this system is still very much alive in a functional sense as well.

That, then, brings us to the final point of this paper, which is addressed to policymakers. If the effects of policies are as dependent on underlying, often deeply rooted, institutions as we suggest here, simply introducing policy elements developed elsewhere becomes very difficult, if not impossible. Their effectiveness depends to a large extent on the existence of institutions that may be hard to construct or manipulate. Policies need to be compatible with these underlying institutional frameworks and the incentives they produce for actors operating within them, else they run the risk of failure, or worse, make a bad situation worse. This is not only a call for care with policy innovation, it is also a call to heed the unintended (but not necessarily unpredictable) interactions between different elements in a political economy.

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