

From physically divided to economically divided: The modern effects of the German Divide from 1945 -1989 on current German economics and its implications for doing business in Germany

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From Physically Divided to Economically Divided: The Modern Effects of the German Divide from 1945 -1989 on Current German Economics and its Implications for Doing Business in Germany

Taylor Backhouse

I would like to dedicate this paper to L.G. for helping me with my research and for putting up with all my late nights of writing.

ABSTRACT

Since the war, Germany has struggled to get back on its feet politically, socially, and above all economically. During the division of the nation from 1949-1989, the economic differences between the Federal Republic of Germany (West Germany) and the German Democratic Republic (East Germany) were undeniable. Considering the fact that West Germany operated a free market economy in a western political system, and the East operated a centrally planned economy in a communist political system, there were many economic hurdles come the reunification of Germany in 1989. However, immediately after reunification there was an obvious gap in the economic state of the eastern and western sections of the nation. Thirty years later, despite Germany's economic reputation as a world leader in exports and manufacturing, the gap between the East and West can still be seen in many aspects of German economics. The purpose of this case study is to examine the initial cause of the economic divide as well as to examine the reasons and the severity of the gap as of 2017 and its implications for doing business in Germany.

INTRODUCTION

From War to Wall

In April 1945, the Second World War was coming to an end and a period of recovery in Europe was beginning. With the Russian forces in Berlin and the British, French, and Americans approaching from the west, the Third Reich and all aspects of the German economic, political and social systems lay in ruin. The USSR's quick takeover of Berlin rendered Hitler's successor Grand Admiral Karl Dönitz's plan to capitulate to the British and Americans impossible (Heather, et al., 2017). Growing concerns with angering Stalin led Germany to surrender to all of the allied victors simultaneously.

Following the unconditional surrender of Germany, all governmental authority was now in the hands of the Allies. Differing political ideologies between the communist East and the capitalist West made border negotiations long and laborious and, after one month, Germany was divided into four zones: American in the south, British in the northwest, French in the southeast and Soviet in the East (see Figure 1) (Heather, et al., 2017).

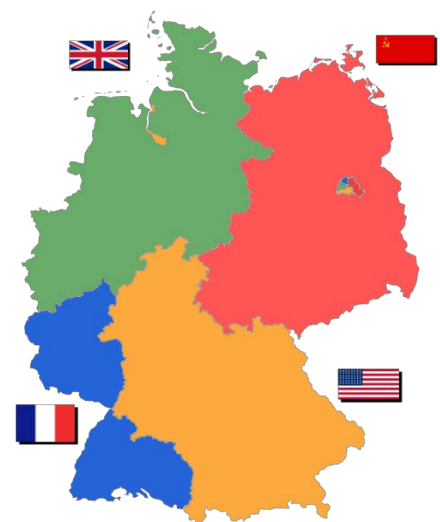


Figure 1. The division of Germany into the American, French, British, and Soviet zones in 1945 (Historiana, 2017)

In 1949, the three western allied sections merged into one revealing two large divided German states: The Federal Republic of Germany (FRG; West Germany) and the German Democratic Republic (GDR; East Germany) (Figure 2) (Heather, et al., 2017). As time went on, the political uncertainty in both the FRG and GDR would cause a social and economic instability. In the east, as the government of the GRD transitioned from a capitalist economy to a communist economy, the business environment became volatile and Germany's largest banks, ministries, and businesses, who were once the pride of Berlin and eastern Germany, began to look westward for survival.

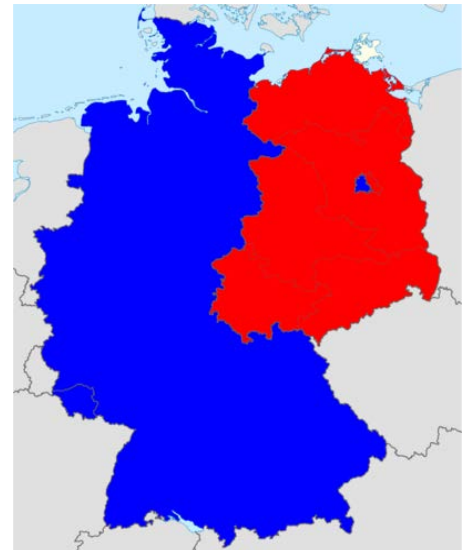


Figure 2. The division of Germany into the FRG (West Germany) and the GDR (East Germany) 1949 (Historiana, 2017)

Banks, Ministries, and Businesses Move West

As the political environment in the GDR began to evolve, Germany's largest and most influential businesses and banks that had their headquarters, in Berlin and Eastern Germany were now looking westward for an opportunity to save their businesses from bankruptcy (Bontje, Musterd, & Pelzer, 2011). In the months to follow, all of the former eastern Germany's large brand name manufacturers, retailers, and banks including Siemens, Daimler (Mercedes Benz), and Deutsche Bank, closed their doors and relocated in the FRG (Bontje, Musterd, & Pelzer, 2011).

The effect of this migration on both states was significant. In the FRG, the immigration brought about a period of "explosive growth and rebirth" for western cities (Heather, et al., 2017). However, for the east the story was quite different. Losing their major industries meant the GDR lost employers, corporate tax payers, and exports. This migration contributed to a further economic downturn in the GDR and was the first step of the establishment of economic disparity between the FRG and the GDR (Heather, et al., 2017).

German Economics (1945-1989)

The devastation from the allied bombing campaigns during the Second World War were colossal. It is estimated that over twenty five percent of Germany's housing was destroyed; in cities, the destruction was greater than fifty percent (Leick, Schreiber, & Stoldt, 2017). Furthermore, most of Germany's economic infrastructure and transportation systems had been completely destroyed in 1945. This period of complete destruction became known as Germany's "zero hour" and it represented a period when Germany had to be rebuilt itself from the ground up (Heather, et al., 2017). This, combined with the stagnant economy between 1945 and 1949 caused a domino effect in the nation. The value of the Nazi currency plummeted, millions of Germans were displaced, there was no industry, natural resources had been depleted, and a shortage of food caused widespread malnutrition and disease in the German state (Marketline, 2014). Though this post-war lull had an equal effect on the economy of both the FRG and GDR, overtime they would drift apart economically creating fundamental differences in the economic condition and policies between them.

The German Democratic Republic—East Germany

Prior to the war, eastern Germany was part of a booming capitalist economy (Marketline, 2014). In fact, eastern Germany's GDP per capita was higher than the western and national German average (Marketline, 2014). Their main exports included steel, chemicals, and minerals. However, after the formation of the GDR in October 1949, the German Economic Council formed communist government led by the Soviet Social Democratic Party (SDP) which ruled until its disassembling in 1990 (Gale Cengage Learning, 2014). Their goal was to implement a central planned economy and therefore abolished any sense of capitalism and private property (MacDougall, 2016).

The centrally planned economy is founded on the principle that the economy does not work in the best interest of the people and that instead, a governing authority must to make decisions to meet social and national economic objectives. Unlike a market economy—where citizens and businesses make production decisions and where the interactions between customers and businesses determine the economy—in a centrally planned economy the government or state controls what is produced as well as how resources are allocated. There are also no private businesses in the centrally planned economy as everything is state owned and controlled.

For the GDR, the introduction of the centrally planned economy by the communist government rendered all resources, manufacturing, processing, exporting, and price setting state-controlled. Despite the GDR’s membership in the Council for Mutual Economic Assistance (Comecon)—a program which included all other Soviet satellite states occupied during the post war period, and was created to coordinate the economics of the eastern European countries that comprised the communist bloc—the GDR faced difficulties creating a viable economy as they lacked many of the valuable resources that existed in the FRG (Encyclopædia Britannica, 2017). In addition, the GDR was less than fifty percent the size of the FRG and had one third the population. Furthermore, the war reparations that were imposed the GDR only further dampened the East’s post-war economic recovery since it required far more productivity than it could produce in order to pay back the Soviet Union (Deutsche Welle, 2017). Unfortunately, the repercussions of these actions on the GDR’s economy were immediate; eastern production levels fell, and businesses closed their doors, resulting in an economic decline that would continue late into the 1960s.

In 1955 the Soviet government implemented a five-year plan, with the goal of economically aligning the GDR with the USSR and helping the GDR make up for war losses. The priority was to increase gross domestic product (GDP) from 23 billion GDR Marks in 1950 to 44 billion GDR Marks by 1955 (Statistische Ämter des Bundes und der Länder, 1950). To accomplish this, the government set industry specific growth targets primarily on traditional industries including textiles, machine building, and mining. A full list of the targets can be seen in Table 1. The plan was focused heavily upon industrial output, natural resource extraction, and energy production. However, the industrial sector of the GDR still had not been rebuilt to pre-war levels. This, combined with a limited amount of technological know-how, resulted in the state’s inability to meet the targets and the failure of Five-Year Plan.

Table 1. Government growth targets included in the first Five Year Plan from 1950 to 1955

Industry	Growth Target for 1950-1955 (%)
Cellulose and Paper	49%
Chemicals	82%
Electronics	96%
Engineering and Optics	139%
Food	87%
Light Industry	76%
Machine Manufacturing	121%
Metallurgy	137%
Mining	94%
Non-metallic Minerals	80%
Power Industry	77%
Textiles	101%
Wood Processing	18%

(Statistische Ämter des Bundes und der Länder, 1950)

Throughout the 1960s, 70s, and 80s the GDR continued to see many major economic issues (Deutsche Welle, 2017). Poor working conditions and a lack of available employment created a mass emigration of the labour force to the FRG (Heather, et al., 2017). This resulted in a labour shortage and a further inability to meet the government's production targets. With the financial status of the GDR worsening, the government was forced to act. In 1963, the New Economic System (NOS) was introduced (Marketline, 2014). The primary goal of the NOS was to aid in economic growth by decentralizing economic planning, which is a far cry from the centrally planned economy that had existed (Marketline, 2014).

In 1968, another reform occurred when the government planned to move away from the traditional forms of industry (mining and textile production) and to focus on innovating and producing new technologies. However, both reforms resulted in failure and had little effect on the country's economic problems. In addition, their inability to export goods to the West led to a deficiency of hard currency, which the GDR needed to pay its debts (Marketline, 2014). The Soviets also ceased to provide the GDR with oil at a reduced price, which it formally would export for profit (Heather, et al., 2017). Furthermore, most of their exports went to other Soviet countries, where the margin on goods was significantly less than their western counterparts. This further contributed to the amounting debt. In 1990, political and economic tensions caused political turmoil resulting in the collapse of the GDR and its reunification with West Germany.

The Federal Republic of Germany—West Germany

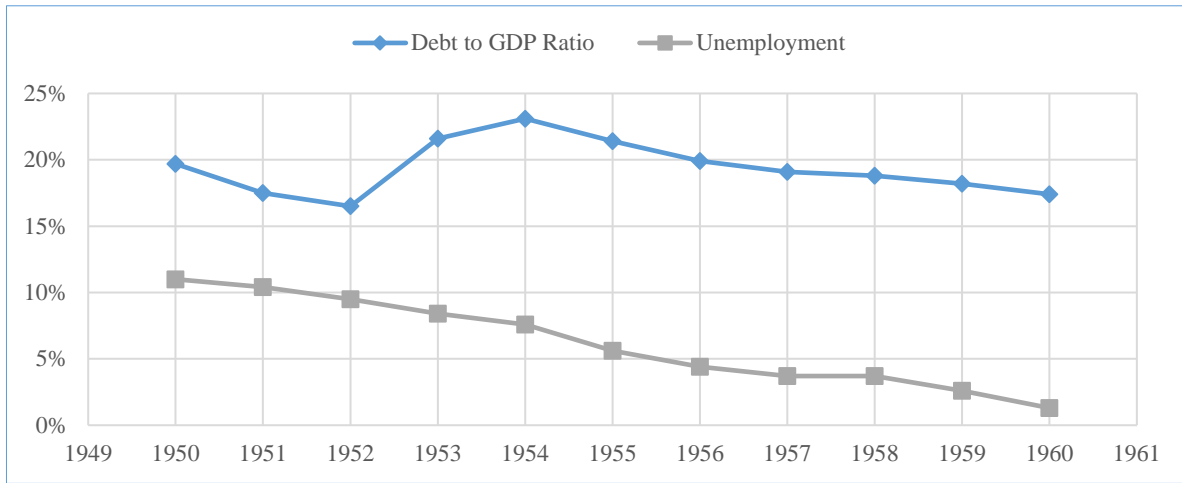
Germany, immediately after the end of the Second World War, was undoubtedly a suffering nation, and the West was certainly not exempt from these conditions. West Germany's industrial capacity was at an all-time low due to the intensive bombings and the killing off of the majority of the labour force (Leick, Schreiber, & Stoldt, 2017). In addition, harsh war reparations, imposed by the Western Allies, created a declining economy. For example, between 1944 and 1946 the FRG's economic output decreased at a rate of 37.6% per annum, while at the same time, the population grew by 20%. This effectively meant that their per capita output fell by almost 50% (Marketline, 2014). Though it was not uncommon to see economic decline following the war, when you compare the 50% decline in GDP per capita in the FRG to Britain's mere 7%, one can understand exactly how desperate the situation was (Marketline, 2014). However, in 1947, in effort to help the economy of the FRG, the Marshall Plan was introduced.

The Marshall Plan, created by General George Marshall, was established to help the western European nations recover from the destruction of the war. Marshall knew that Germany, despite its history, would be essential to re-establish the European economy (Heather, et al., 2017). The Plan provided hundreds of millions of dollars to the FRG in order to rehabilitate the damaged cities and industrial sectors (Heather, et al., 2017). Ultimately, the Marshall Plan gave the FRG the economic push it needed to establish its industrial presence in post war Europe.

After the introduction of a new currency, an influx of foreign labour, and a push towards competition and consumerism, West Germany's "Wirtschaftswunder" –or economic miracle—occurred (Marketline, 2014). This miracle was in part created by the large labour force of unemployed workers. In addition, West Germany benefited heavily off of its joint economy with the British, French, and American zones from which its currency reformation and the Marshall Plan were born. In the years to follow, this economic miracle would continue. Between 1950 and 1960 West Germany saw an average GDP growth rate of 7.96% —double the rate for Britain, France, and the United States (Heather, et al., 2017). As seen in Figure 3, the FRG's debt to GDP ratio decreased and its unemployment fell below two percent. To put this into perspective, the debt to GDP ratio of the UK during the same time was 107%, the unemployment rate was 1.5% and their average GDP growth rate for the decade was 2.85% (Eichengreen & Ritschl, 2008). Part of the reason for this was the healthy trade surplus. Another contributor for the FRG's success was the reputation that it had built for itself in the world of manufacturing. At this time, and even today, a label stating "Made in Germany" was synonymous with quality and superior engineering (Heather, et al., 2017). This

excellence in engineering combined with their capacity surplus allowed them to become one of the world’s leading exporters.

Figure 3. Changes in debt to GDP ratio and unemployment in the FRG from 1950-1960 (%)



(Eichengreen & Ritschl, 2008)

For the FRG, the automotive industry became particularly important. German car companies such as Mercedes Benz, Porsche, BMW, and Volkswagen, who had moved their headquarters to the West, were now a key component of the FRG’s success (Hajdu, 2013). Their desirability and reputation allowed them to charge a premium for their products which brought hundreds of millions of Deutsche Marks into the state (Hajdu, 2013). The success of the automotive industry in West Germany contributed to the continuous GDP growth and allowed them to become an ‘Economic superpower’ and the world’s third largest economy up until 1990 and Reunification (Marketline, 2014).

Reunification—From Two States to One

As the FRG’s economy continued to grow, in the late eighties the economic crisis continued to deepen in the GDR. During the summer of 1989, thousands of people had fled the GDR for the FRG through the newly sovereign states of Hungary and Czech Slovakia (New World Encyclopedia, 2015). At the same time, the GDR’s communist government was growing increasingly powerless. Then, on the evening of November 9, 1989, a member of the Communist Party mistakenly released news in which the government stated that it would allow East Germans to go to the FRG at any time without a visa (Heather, et al., 2017). Crowds immediately gathered at the edge of the Berlin Wall and demanded that the guards let them pass into the West. That night, tens of thousands of East Germans made the journey over the Wall.

The opening of the Berlin Wall was a fatal blow for the GDR and would ultimately lead to its demise. When the election took place in March 1990 the Communist Party, now renamed the Party of Democratic Socialism, was defeated by a party that promised a “speedy reunification of Germany” and thus a new Eastern government was formed (Heather, et al., 2017). Threatened by a continuous stream of refugees leaving East Germany, the new government was forced to expedite the negotiations. In July, a monetary union was created which meant that now East German’s had the same currency as their western counterparts (Heather, et al., 2017). The unification treaty was signed and came into effect in early October 1990 and resulted in the merger of the German Democratic Republic and the Federal Republic to form the unified Republic of Germany. As the East joined the West, the western systems of banking, education, social security and welfare, justice and regulation all directly replaced those from the East (Heather, et al., 2017). However, little was done to help the economic state of the former GDR or to

help create economic equality between the two states. This resulted in the development of an economic gap between the East and West that has only continued to get worse as time has passed.

Research question

Just over 25 years later, Germany is the centre of European economics once again. Although there were periods of economic downturn during the “Dot Com Bubble” and the 2007 financial crisis, it has remained one of Europe’s largest economies. One would expect, based on Germany’s current economic success, that any economic gap created by the reunification period had been fully bridged. However, upon closer inspection, you can see that there is still great inequity between the economic state of western and eastern Germany. Though it may seem, from an outsider’s view, that this be extremely unlikely, upon closer inspection, the economic gap between the East and West is visible in infrastructure, household income, GDP, unemployment rates, and housing prices. After looking into this phenomenon further, it is clear that the divided period of Germany, and the steps taken by the government during the reunification process, are continuing to have a lasting effect on Germany economic equality. Thus, we must consider what caused this gap; why this gap still exists and to what extent it affects the economic state of the nation; and what implications it has on modern day business activities within Germany.

DISCUSSION

The Origins of the Economic Gap—Reunification

Economically, reunification posed several difficulties and consequences for Germany—many of which would have a long-lasting effect on the country. As we have seen, the FRG and the GDR operated polar opposite economic policies. The GDR’s centrally planned economy, state-controlled enterprises, and set prices held it back from economic growth. In contrast, the FRG’s free market model, which followed a free price system, allowed it to recover quickly from its post-war destruction. Although, one can argue both in favour of and against each of the economic principles when considering divided Germany, the fact is that one state prospered while the other one lay on the verge of collapse.

As seen in Table 2, the FRG was far outperforming the GDR up until the reunification (Marketline, 2014). For example, the FRG’s gross national product was almost 600 percent higher than that of its Eastern counterpart. This divide made reunification a grandiose and problematic undertaking economically speaking (Marketline, 2014). The core problem was the state of the eastern German economy, which was much worse than anyone had thought. With the East’s obsolete technology, crumbling infrastructure, and a lack of capitalist experience, West Germany’s government faced numerous decisions. These included: raising money for infrastructure; how to privatise eastern firms; how to handle the exchange rate; and how they planned to allocate the funds in the East—whether it be on investment or consumption (Hunt, 2006).

Table 2. Key economic indicators compared between the German Democratic Republic and the Federal Republic of Germany in 1990.

Indicator	German Democratic Republic	Federal Republic of Germany
Gross National Product (\$ bill)	159.50	945.7
GNP per capita (\$)	9,679	15,300
Budget Revenues (\$ bill)	123.5	539
Budget Expenditures (\$ bill)	123.2	563

(Marketline, 2014)

The infrastructure in eastern Germany was also something that had to be dealt with. There were complaints about energy shortages and many factories and production facilities that required complete demolition and reconstruction (Hunt, 2006). In addition, the transportation network, including the Nazi-era Autobahns, almost needed to be completely rebuilt. To tackle this the West German government began to invest heavily in eastern Germany (Heather, et al., 2017). These funds were primarily allocated to infrastructure and investment. Though it is difficult to track and estimate the exact amount of money that western Germany poured into the East, records suggest that, during the first three years following reunification, it surpassed DM 350 billion (Hunt, 2006). Following this period, it is estimated that an additional DM 150 billion flowed eastward (Hunt, 2006). From 1991-2003, 4-5 percent of the West’s yearly GDP was spent on the East (Heather, et al., 2017). Yet few of these investments provided increased economic benefit to the East.

To tackle the problem with the currency exchange, the Finance ministers of the former FRG and GDR approved a legislation that promised a common currency between the reunified states (Marketline, 2014). On July 1, 1990, citizens of the previous GDR could exchange their DDR Mark for the new western Deutsche Mark (DM). The conditions for the exchange depended on the age of the person and the amount of money they had. On average, the rate was 1.8:1 (DDR Mark to DM) (Marketline, 2014). Loans and other liabilities were transferred at a rate of 2:1, while salaries and pensions were exchanged at 1:1 (DDR Mark to DM). It is important to note however that these rates only applied to citizens of the former GDR. Foreigners and companies outside of the GDR were able to exchange at a rate of 3:1 (Marketline, 2014).

Unfortunately, implementing the unified currency negatively affected the wealth of the former GDR citizens. The so called “great exchange” did not bring about what many East Germans had hoped. Instead, many saw their spending power decrease dramatically. This created an immediate economic divide. To demonstrate the effect of the exchange rate of the well-being of the former citizens of the GDR we will look at the average salaries of citizens from both the GDR and the FRG. According to the Statistics Office of the GDR 1989, the average gross salary for a citizen of the GDR was 2194 DDR Mark. In comparison, Federal Republic of Germany’s data show that the average gross monthly salary was DM 3,358.00 (Marketline, 2014). According to these numbers, at an exchange rate of 1:1, GDR citizens were already DM 1144.00 worse off than the West Germans per month (Marketline, 2014). In addition to this, there were significant increases in the price of goods in the GDR after the DM was adopted. Consider the pre-unification price of potatoes for example (Table 3). At a 1:1 exchange rate, the price for 5 kilograms of potatoes in the FRG was almost 480 percent higher than the GDR pre-reunification. If you couple this with the fact that most Eastern Germans’ salaries were converted at a rate of 1:1 post-reunification, the effect of the exchange rate can easily be seen—the price of many essential goods rose astronomically, sometimes hundreds of percent, making easterners immediately worse off.

Table 3. Product pre-unification prices

Product	Cost in GDR	Cost in FRG
Potatoes (5Kg)	0.85	4.94
Rye Bread (1 Loaf)	0.52	3.17
Beef (1Kg)	9.80	17.20
Tram Ticket	0.20	2.07
Electricity (1kWh)	0.08	0.42
Rent (per Month)	75.00	411.00
Coffee Beans (1Kg)	70.00	17.86
Washing Machine	2,300.00	981.00
Fridge	1,425.00	559.00

The currency conversion also affected production costs. Before reunification, production costs in the GDR were already at a European high. After the introduction of the DM, wages rose far above the productivity level and production costs skyrocketed. As a result, many Eastern firms once again fled to the West as the labour was cheaper and production costs were lower (OCED, 1989).

Another challenge was privatizing former state-owned firms in the GDR. Early in the unification process, the FRG government decided that privatizing the GDR economy was a priority (Ghaussy & Schäfer, 1993). To do so, the western government took over the Treuhandanstalt (Trust Agency; TA) which was previously established by the GDR to take over the East German firms and turn them over to the Soviet state (Ghaussy & Schäfer, 1993). The new, western managed TA had the task of privatizing the eastern firms. Their goal was to match firms in the same industry with western industry experts (Dyck, 1997). The TA decided which companies would continue to operate and which would cease to exist. Considering that some eastern communities were dependent on the companies that operated within them, the TA also decided which communities would prosper and which would not. In total, 75 percent of the firms were taken over by western firms and family business operators, 6 percent were purchased by foreign buyers, and only 20 percent remained in the hands of eastern business owners (Dyck, 1997). The effect of this was the establishment of a network of western own subsidiaries in eastern Germany, many of which would be closed or bankrupt in the years to follow. By the time of the Treuhandanstalt's dismemberment in 1994, it had privatized around 14,000 businesses and 44,000 plants which accounted for 45 percent of the East German workforce (Carlin, 1994). In the end, the TA privatization had resulted in DM 193 billion in net losses (Brada, 1996).

Foreign investors that were aware of the Treuhandanstalt's work were also extremely wary about investing in eastern Germany. Less than 5 percent of all investments in the East were foreign and out of that, most were from West Germany (Ghaussy & Schäfer, 1993). Because of the fact that western Germany had control over a majority of the reunification process, most of the remaining companies in eastern Germany were mere subsidiaries of western companies. Many of these firms were purchased on a "stand-by" basis, meaning that they were purchased and prepared for production, but never actually put to use. In addition to this, most of the East's financial assets were purchased and controlled by the main German banks of the West.

As a result, the economy of eastern Germany suffered immensely during the reunification process. Within a year, unemployment in the East rose above 3 million and industrial output fell well below half of the previous output (Marketline, 2014). In fact, in 1991, the entire production of eastern Germany accounted for less than 8 percent of the entire nation (Marketline, 2014). Even though this was the case, western Germany experienced two years of booming growth with rates of over 5 percent. Meanwhile, eastern GDP fell 15.6 percent in 1990 and 22.7 percent in 1991 (Marketline, 2014).

Though some may dispute that there were any long-lasting effect of the German divide and the reunification, the truth is, even today the economic divide still exists. If key metrics are compared between eastern and western Germany including household income, GDP, unemployment rates and housing prices it is obvious that there is an unbalance of economic prosperity. Of course, it is easy to say, from an outsider's view, that Germany's economy is thriving, but only from within the German border can it be seen that the ongoing economic inequity between the East and the West has created long-term negative side effects. However, the outlook for the East isn't all that bleak, since the economic disparity creates many opportunities for both growing and established businesses.

The Divide Today

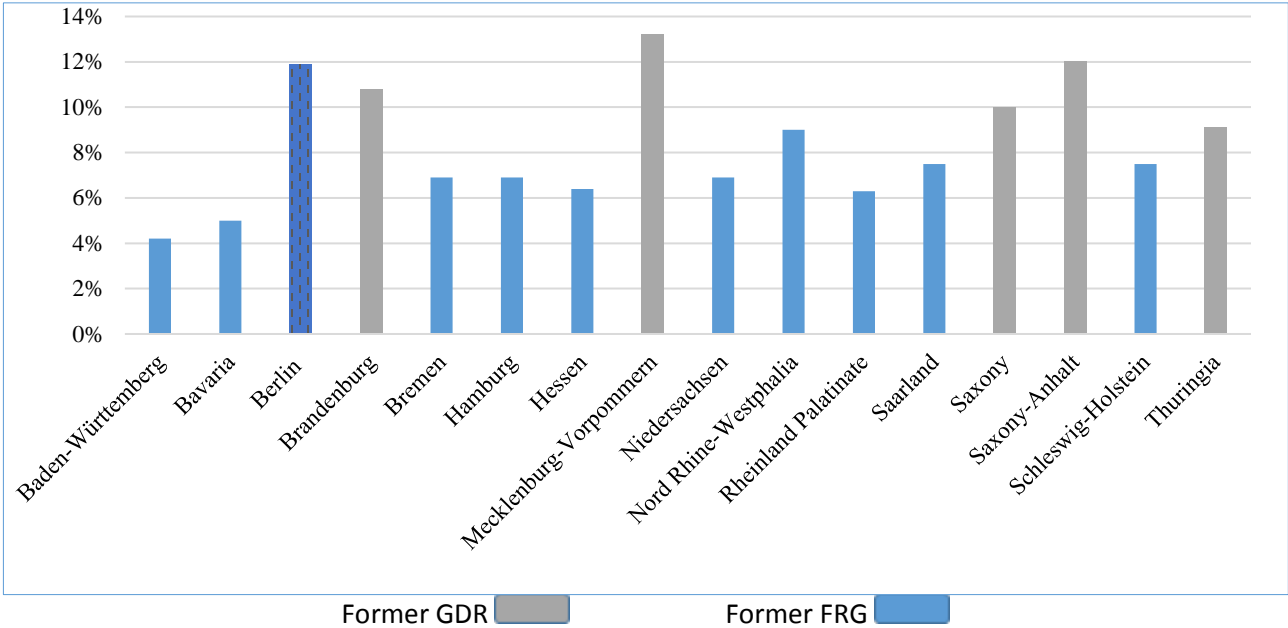
As of 2017, the German economic gap is still prevalent. The Economist's article "Still not Over the Wall," and Rick Noack's article "The Berlin Wall fell 25 years ago, but Germany is still divided," outline the reality of Germany's underlying economic problems (Berlin & Jena, 2014; Noack, 2014). Today, the West's dominance over eastern Germany is visible in many demographics. Whether it be unemployment rates, monthly income, or social services the West seems to continuously outperform the East. According to Oliver Johnmann, the gap today can largely be

attributed to western Germany’s head start both during the denazification process and the prevalence given to it during the reunification process (Johnmann, 2017). In addition, other factors such as the emigration of bright East German minds to the West, the adoption of the Deutsche Mark, and the privatization process played a large role in East Germany’s economic position (Johnmann, 2017). The following will compare the East and West on key present-day indicators.

Unemployment

To explain the modern gap, we will first look at unemployment. There is a lot of debate about unemployment in Germany as many people consider it to be proof of the success or unsuccessfulness of reunification. However, statistics show that an undeniable variance exists between the East and West. From Figure 4, we can see that the highest rates of unemployment, excluding Berlin, exist in the new states that once were territories of the GDR (Statistisches Bundesamt, 2016). Moreover, according to the Statistische Landesämter the former FRG state, Nord Rhine Westphalia, which currently has the highest unemployment rate in the West, still has a rate that is 9 percent lower than any of its former GDR counterparts (Statistisches Bundesamt, 2016). The fact that all states are former GDR members, demonstrates that the problem is not related to any specific state or geographic area, rather that this problem is related to the long-term effects of political turmoil and reunification decisions in the GDR.

Figure 4. Unemployment rate in Germany by state as of 2016 (%). Berlin has been separated due to the fact that it was both a state of the GDR and FRG.



(Statistisches Bundesamt, 2016)

This issue is in part due to the wave of mass migration of labourers, who were seeking higher pay and more promising job prospects that occurred during and after reunification. This had a deep effect on the economy of the region since there were no skilled labourers to work in the few remaining and operative production facilities (Marketline, 2014). Today, there is still a growing concern with potential investors when it comes to investing in new and continuing business ventures in the East and consequently, eastern Germany has failed to evolve economically.

Upon closer inspection, it would appear that the unemployment in eastern Germany has created a vicious cycle that prevents it from repairing the unemployment issue. For example, the lack of available work is driving, rather

pushing, people westward to the enterprise centres of the West. As a result, eastern cities are perceived as having less employment potential for the workers and less return potential for investors. This returns the attention to the West of Germany where the funds and labour are eventually allocated. This phenomenon has created an everlasting threat to cities and states of eastern Germany as their populations, productivity, and wealth are continuing to decline.

Income and Wealth

To continue, a second metric that should be looked at is household income. In 1980, there were obvious differences in the average salaries between former West and East Germany and this is still evident today. Mean income inequality is an ongoing issue particularly for the states that made up the GDR. As seen in Table 4, people in this region are earning less, saving less and therefore are having less disposable income (Statistisches Bundesamt, 2016). If we look at gross and net household income for example, there is a difference of 25% and 23% respectively (Statistisches Bundesamt, 2016). The same pattern can be noted for gross annual salary and disposable income per month. Although these differences are large, the East has taken steps to tackle them which include lowering the cost of goods and housing.

The inequities in wealth between the old GDR and FRG are very transparent. According to Kate Connolly (2015), out of the 500 richest Germans, a mere 21 are in the East, and of those, 14 are in what used to be West Berlin and of the 20 most financially successful cities, only one is in the East. To continue, Madeline Chambers from 'Business Insider' (2015) suggests that western states are considerably richer and households in the East own less than half of the wealth accumulated by those in the West.

Table 4. Comparison of key economic matrices between former East Germany and former West Germany as of 2016

	Former FRG	Former GDR	Difference in Percent of former GDR
Gross Household income per month (€)	4,090	3,080	-24.7%
Net Household income per month (€)	3,144	2,425	-22.9%
Gross Annual Salary (€)	30,881	24,580	-20.4%
Monthly Disposable Income (€)	3,213	2,465	-23.3%

(Statistisches Bundesamt, 2016)

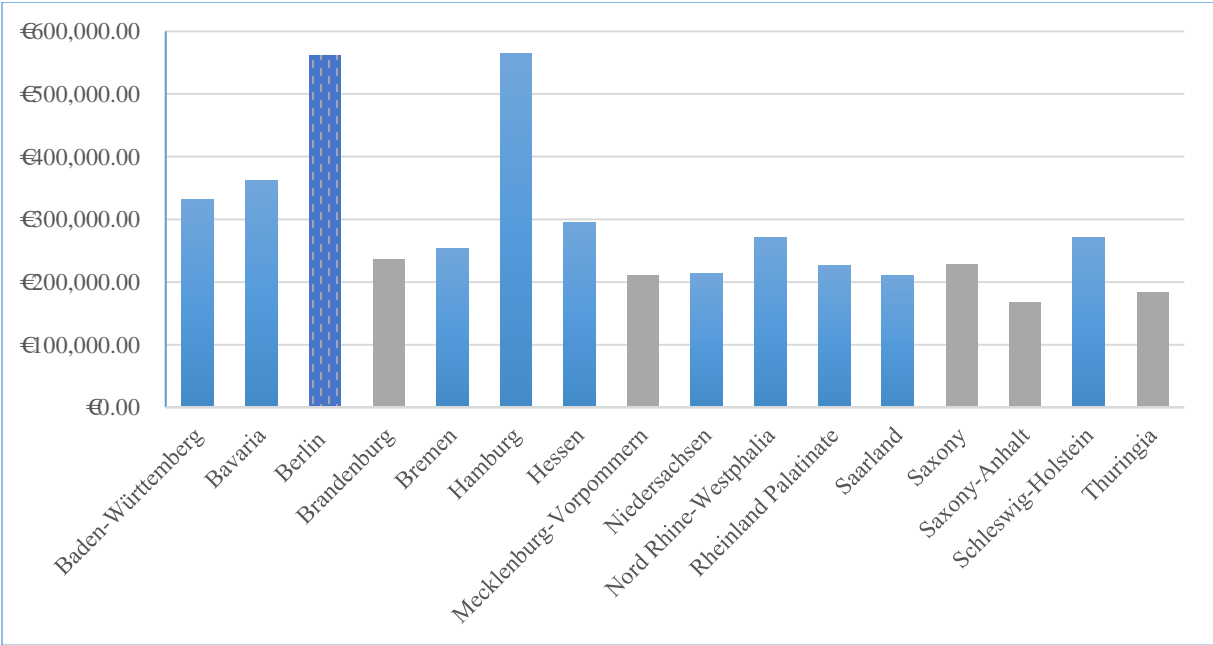
To put it into perspective, let's consider the average wealth of a person in the west and east. The average wealth of a westerner is approximately €154,000 per person (Chambers, 2015). However, if an easterner were to have net assets of €110,000 they would be considered to be in the top 10% of richest eastern adults (Chambers, 2015). The factors that continue to add to these inequities include: the fact that wages in the former GDR are almost €2,800 per month lower than those of their eastern counterparts; pensions were transferred from DDR Mark to DM at a rate on 1:1 whereas savings accounts were transferred at a rate of 2:1, meaning that savings accounts were decimated; and that property in the East is almost worth half as much of that of the West (Chambers, 2015; Connolly, 2015).

Housing Prices

It is fair to say that, for most people, the largest purchase that they will make in their lives, is their homes. Although the price of most goods in the former GDR have adapted to the lower incomes of those in the East, a great difference can be seen between the cost of housing between the East and West. As seen in Figure 5, the average price of homes in the East is much lower than those in the West (Immowelt, 2017). There are many external factors that

are influencing the housing prices including available employment, crime rate, and the quality of the education system (Marketline, 2014). However, when we compare these metrics between eastern and western Germany, some of the eastern states rank in the top five when it comes to their education system and the absence of crime (Marketline, 2014). This implies that neither educational issues nor crime rate problems are to blame for the low housing prices and rather that they are a product of the local, worse-off eastern economy.

Figure 5. Differences in Housing Prices in Each German State in 2016.



(Immowelt , 2017)

Consumption

After the fall of the Berlin Wall, western consumer goods such as Milka chocolate bars, Walkman, and Levi jeans became extremely popular and sought upon goods by easterners (Connoly, 2015). Immediately after reunification western goods such as these flooded the shelves of retailers in the East. However, even today, few products from eastern Germany have infiltrated the western retail scene (Connoly, 2015).

Productivity

As far as productivity is concerned, the East is only 73% as productive as the West. Western cities such as Munich and Stuttgart remain world leaders in automotive manufacturing with companies such as Mercedes Benz, Porsche, and BMW (Marketline, 2014; Connoly, 2015; Heather, et al., 2017). Frankfurt remains home to the headquarters of the country’s largest banks and is considered to be the financial capital of Germany (Marketline, 2014). In Bonn, the old capital of the FRG, resides the headquarters of the country’s postal service, telecommunication, and rail services (Heather, et al., 2017). In addition, out of the top thirty companies making up the German Stock Exchange (DAX) all of them are headquartered in the West (Sharp Trader, 2017). This is in part due to the politically controlled economy of the GDR and the fact that the East is home to industries that are synonymous with a less developed economy. Productivity is an important indicator of economic growth since increased productivity allows businesses to produce greater output for the same amount of economic input (DCED, 2017). This in turn, creates higher revenues, and more gross domestic product (DCED, 2017). The fact that all major industry migrated to the West just prior to the divide, remains, to a large extent, the reason why western Germany continues to exhibit economic growth and why the former GDR continues to fall behind economically.

The Gap's Implications on Doing Business in Eastern Germany

It is obvious that the economic gap between the former GDR and FRG still exists. This divide has created hardships for both the economy of eastern Germany and the people who reside there. While at the same time, the gap provides numerous opportunities for new and current business models to thrive in. To examine both the opportunities of doing business in eastern Germany, the political, economic, and technological environments will be examined.

The Political Environment

Though in the beginning, the transfer of the West's political institutions to the East was detrimental to their economic position, since then, they have been heavily invested in bettering the economic conditions of the former GDR. They provide ample funding and tax breaks to new and existing businesses in effort to attract them to the former GDR. In 2015 alone, over 3.1 billion euros were invested in these companies (MacDougall, 2016). In addition, the government introduced a 5.5% tax on western states that is transferred to promote the economic growth of the East. These conditions provide the perfect foundation for both new and established businesses.

The Economic Environment

Since reunification, eastern Germany and its previously Soviet occupied eastern European counterparts have been considered the "emerging markets of the first world" and according to the Germany Trade and Investing Association (2016), eastern Germany is "one of the world's most attractive investment locations (Caprio, Folkerts-Landau, & Lane, 1994). But nowhere has the former GDR economy grown faster than in its industry. A massive reindustrialization program, has made the East one of the most advanced and equipped yet untapped industrial areas in Europe. This is one of the benefits of the present divide. The inequities between the former GDR and FRG provide businesses with the opportunity to enter an untapped market and get in on the ground floor of the economic boom of the region. Thus far, eastern Germany's economy has been radically overhauled and is ready for industry to infiltrate its facilities and cities. Some businesses like Porsche and BMW have already taken advantage of this (with production facilities in the eastern city Leipzig) yet many are unaware of the benefits that the eastern economy can offer (BMW, 2017; Porsche, 2017). These include, but are not limited to: lower production costs, lower cost of materials, lower shipping costs, lower taxes, and cheaper labour. East Germany has also caught the attention of foreign direct investment (FDI) because of its tax breaks, unemployment rate, and low start-up and production costs (Günther & Gebhart, 2005).

The Technological Environment

Though the technological environment of eastern Germany has been considered to be lagging because of its communist past and little available capital, there are several features that actually provide opportunities for business who decide to operate in the East. First, their extensive railway and freight lines, make it possible to reach over 300 million consumers across eastern Europe in under 24 hours. This in itself provides a huge opportunity for production-based companies. In addition, scientific research institutes are driving the rapid development of a number of new industry sectors that are waiting for investment and business know-how to make them thrive. Eastern Germany has also become a leader in the renewable energy, biotechnology and healthcare sectors (MacDougall, 2016). In fact, the East's Research and Development GDP share is significantly higher than the European Union, and almost equivalent to the US', at 2.5%. These reasons are in part what make the former GDR one of the most attractive markets in the world for investment.

The technological environment of eastern Germany also has attracted a thriving entrepreneurial community. Start-up activity is playing an essential role in the East's economic development. New ventures bring innovation, jobs, and most of all investment to the former communist state and Germany recognizes the benefits of this. The

presence of internationally renowned universities, research centres, and business accelerators makes eastern Germany very attractive for new investment and new enterprises. In addition, the East has an extensive start-up investment program through which it provides financial aid and industry know-how (Cassala, 2016).

All in all, the evidence provided by the analysis of the political, economic, and technological environment of eastern Germany suggests that there are numerous business opportunities in the former GDR. For new businesses and tech start-ups, the East provides some of the lowest rent and corporate tax rates, heavy government funding, and a network of technological research centres (Cassala, 2016). For large corporations, eastern Germany offers low production costs, low goods acquisition costs, and well-connected transportation network that allows them to transport to all of eastern Europe and western Asia. In addition, there is also the opportunity for businesses to act with a social cause. Since the East has been suffering economically for the past 30 years, businesses that invest within this region have the opportunity to offer jobs, bring new industry, raise the living standards, and ultimately help the East bridge the gap between their western counterpart.

CONCLUSION

Overall, the political differences between Soviet-controlled East Germany and Western-controlled West Germany created numerous economic challenges during the division from 1945-1989. Upon reunification, many believed that the economic disparity between the two states would be bridged and that Germany would become one economic entity. However, this was not the case and the economic divide of Germany is still prevalent today, and it is not getting any better. The differences between the former GDR and FRG exist in almost all facets of the German economy, and though Germany as a whole is the economic superpower of the European Union, the East is still struggling to get back on its feet. For businesses, this presents an untapped opportunity. Low production, labour, and material costs combined with ample government funding, a social purpose, and many leading research and business facilities, create a perfect opportunity for a new or existing business to thrive. Therefore, it is imperative that when businesses or investors are considering Germany, that they look and heavily consider the former German Democratic Republic.

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