# '1:1 — with some risk' from the Süddeutsche Zeitung (24 April 1990)

**Caption:** On 24 April 1990, the Bavarian daily newspaper Süddeutsche Zeitung comments on the decision taken by Helmut Kohl, Chancellor of the Federal Republic of Germany (FRG), to apply the exchange rate of one East German mark to one West German mark.

**Source:** Süddeutsche Zeitung. Münchner Neueste Nachrichten aus Politik, Kultur, Wirtschaft und Sport. 24.04.1990. München: Süddeutscher Verlag. "1:1 - mit Risiko", auteur:Thoma, Franz , p. 4.



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## 1:1 — with some risk

by Franz Thoma

That all went rather quickly — the Chancellor is clearly in decisive mood! Even if he is guided more by desirability than feasibility, by a sense of what is politically *opportune*, and above all by the chance on the home front to throw the SPD's foolish talk about breaking promises back in its face. The Chancellor has virtually brushed aside the Bundesbank's well-founded objections. And for the opposition they were never valid anyway. 1:1 is the name of the game —Kohl's general recipe for converting East German Marks into West German Marks, a recipe extending to wages, which is clearly a risk. Kohl has however found something of a currency policy alibi as regards savings, where he has heeded concerns expressed by the central bank.

To date only the 1:1 rate for pensions has gone unchallenged. The split conversion rate for savings and cash is roughly in line with thinking at the Bundesbank in Frankfurt. It would no doubt have been problematic for Helmut Kohl to have completely ignored the currency policy views of the Bundesbank, an institution held in high regard by the citizens of the Federal Republic, if rather less so by its politicians.

The pension conversions, even if they are raised to 70 % of the most recent withdrawals, and the split conversion of savings should prove manageable. The real problem lies firstly in *wages* and secondly in the *high debt levels* of DDR undertakings, a fact which has become increasingly apparent in recent weeks. Even assuming that the new DDR Government's almost reckless proposal that wage levels first be corrected upwards and only then converted at 1:1 is taken no further, the full conversion on which the SPD also looks favourably will impose life-threatening costs on undertakings in the DDR, which are already facing an uphill struggle. They will after all be required to take over half the debt burden. That represents debts (excluding housing) of 125 thousand million marks. Just looking at the arithmetic it ought to be possible to cope with a 1:1 wage conversion, bearing in mind that wage levels across the border are about a third as high as those in the Federal Republic, while productivity stands at barely half. And current rates of productivity as a measure of prosperity may however rise sharply with the introduction of the Deutschmark in so far as process bottlenecks can be expected to disappear.

But what do such calculations really mean? Even if, as is to be hoped, productivity rises sharply, thereby gradually creating scope for upward adjustments of wages, undertakings in the DDR will be required as from Day 1, which can be no earlier than 1 May but should be no later than 1 July, to compete with products from the Federal Republic. This they cannot do. However hard people in Zwickau and Eisenach may work building their Trabants and Wartburgs, they will have no chance of shifting them against hard currency as from Day One, and from Day One only hard currency will count. This factor and the need to pay off debts and interest will increase the threat to jobs in the DDR, however good the 1:1 rate may at first appear. (Yet what would the alternative have been — a new flood of immigration at 2:1?). That in turn will increase the demand for unemployment funding — or perhaps for temporary wage subsidies.

Citizens in West Germany, though more than ready to adopt a sympathetic stance, are being driven to a measure of scepticism by the demanding tone coming out of the GDR and are now asking above all: What will all this cost? And does it threaten the *value of the Mark*? There exists no historical model for the shift from a command economy with a non-convertible currency to a market economy with hard currency. Everything depends on how national income in the GDR evolves. Our fear is that the 300 thousand million Eastern Marks will not become 300 thousand million Western Marks, because many GDR concerns will be incapable of competing even if they were to be surrounded by tariff walls for a transitional period. If the GDR were to receive for the initial period the sum of about 20 thousand million Marks in Central Bank money, the effect would be to increase by 9 % the amount of cash circulating in the Federal Republic; this could be handled without inflationary impact if the GDR social product were to remain at least at today's level. The risk of price inflation driven by additional demand from the GDR would be rather greater; this is why a split rate is appropriate in the case of savings deposits.

When the West German citizen is viewed as a taxpayer rather than as a saver, the additional loads imposed by the GDR really begin to pile up. The Federal Government will have not only to scrape together every single Mark of additional tax revenues but also to subject the budget to a severe shake-up (spending on defence and road-building, support for frontier areas and Berlin). This will call for thousands of millions to be spent. And while it is true that not everything has to be done from one day to the next, there being some things that could be funded through loans, Bonn should nevertheless take care not to decide obstinately in advance that everything can be managed without tax increases, though admittedly this must be a last resort. The conversion offer which has now to be negotiated with East Berlin is too generous to maintain such a position. Lothar de Maizière has every reason to be satisfied. He will try all the same to gain a little more ground on savings accounts.

And yet the GDR side would also be well advised not to take leave of their common sense, as some politicians in the Federal Republic have apparently already done. If that were to occur, the Federal Republic would be left carrying a huge burden of new debts and would lose virtually all power of movement. The currency shift will in the first instance be a *heavy load*. Let us now do what we must to carry that load — there is no other way.