Schumpeter in the Economist on Lessons from Germany

GERMANY'S midsized manufacturers, collectively known as the Mittelstand, are often praised as a group for providing the backbone of the world's fourth-largest economy. Individually, they are world leaders in hiding their light under a bushel. They tend to be family-owned, tucked away in small towns and familiar only to the businesses that buy their specialised machinery and components. "We are not digging for gold," says Joachim Kreuzburg, the boss of Sartorius, a maker of laboratory equipment. "We are selling shovels to the gold-diggers."

Increasingly, though, Germany's hidden champions are enjoying a measure of international celebrity. Officials and businesspeople from the world over are making pilgrimages to Germany to learn from the Mittelständler, much as they flocked to Japan in the 1970s to study Toyota. Mario Ohoven, president of the BVMW, a trade body for the Mittelstand, says that wherever he goes these days, he is pressed to explain the secrets of his members' success. Recent suitors include Iran and Egypt.
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Germany's economic strength in recent years is the most obvious reason why other countries want to emulate it. But the Mittelstand also appears to offer a solution to some of the biggest worries haunting the capitalist system. One is about inclusiveness: some countries worry that too much economic activity is becoming concentrated in a small number of giant companies and in a few megacities. Another is youth unemployment: millions of young people remain idle while bosses complain of skill shortages. Winfried Weber, a professor of management at the University of Mannheim, explains that the combination of medium-sized companies with deep local roots and a strong apprenticeship system means that in Germany only 7.8% of those aged 25 or under are unemployed, compared with 22.1% in Sweden and 54% in Spain. Mittelstand firms inspire extraordinary loyalty in their workers: on average only 2.7% of them leave each year, compared with the 30% turnover at some big American companies.

Of the stream of pilgrims who come to study Germany's midsized marvels, the most devoted are from South Korea. Moon Kook-hyun, a former boss of Yuhan-Kimberley, a maker of disposable nappies, has argued for years that his country is too dependent on a handful of giant conglomerates, the chaebol, and must focus on improving its small and medium-sized family firms. He is so passionate about his cause that he set aside his business career to serve in parliament and, in 2007, to run for president. He got only 5.7% of the vote. But his message that companies do not have to be big to be world-class is resonating. South Korea's current president, Park Geun-hye, recently took a group of would-be Mittelständler to visit their role models in Germany. South Korea has also set up German-style Meister schools, to teach bright youngsters to become masters of a technical trade.

Mr Moon is now taking his crusade to China. Every year he lectures to thousands of heads of Chinese family firms that Germany has more than 1,000 companies that have been in the same family for generations but can compete with the world's best. Again, his message is hitting home, and China is also now sending delegations to Germany. However, some of its canny capitalists have concluded that the best way to understand the Mittelstand firms is to own one. Among those recently bought by the Chinese are Putzmeister, a maker of concrete pumps, and Preh, which makes various electronic innards for cars.

Before announcing the triumph of the Mittelstand, it is worth bearing two things in mind. The first is that business models can never be transported lock, stock and barrel. The German system depends on delicate relationships between schools and companies, and capital and labour. It is hard to see this being reconstituted in South Korea, with its adversarial industrial relations, or the United States, with its enthusiasm for labour mobility. The British have been trying to learn from the German apprenticeship model since the late 19th century, with limited success.

The second is that the Mittelstand is changing rapidly: just as the world is trying to learn from its companies, they are busy learning from the world. The Freudenberg Group, a maker of filters, seals and lubricants, has been owned by the Freudenberg family for eight generations. But its chief executive, Mohsen Sohi, is an American who spent his first 20 years in Iran. Mittelstand firms are realising that they can no longer just stay in small-town Germany. To stay competitive they need to produce their goods globally and service them wherever their customers are—and to help them with this, they are hiring growing numbers of foreigners. Sennheiser, which makes headphones and microphones, recently passed to a new generation of Sennheisers, Andreas and Daniel, who stress the importance of "being global in everything we do". They want to learn from "innovative customers" around the world: the Japanese are particularly demanding when it comes to sound, and Americans when it comes to fashion.

However, this does not mean that the pilgrims are visiting Germany in vain. It is a vivid example of the fact that manufacturers in rich, high-wage countries can prosper from globalisation if they invest in human capital and focus on sophisticated products. The West's industrial companies learned from lean manufacturing without importing Japan's system of managed capitalism. German companies such as Freudenberg are embracing globalisation without losing their roots: Mr Sohi has learned German and praises his company's "Mittelstand spirit". Management science has always progressed by picking up ideas from all over the world and remixing them into more productive combinations. Germany is assuming its rightful role as one of the world's leading laboratories for this mixing.