Unrestricted

BoF Online

7 • 2013

A perspective on the German ‘job miracle’: labour market outcomes and welfare after the labour market transformation

Michaela Schmöller

The opinions expressed in this paper are those of the author and do not necessarily reflect the views of the Bank of Finland.

Bank of Finland
Monetary Policy and Research
26 Aug 2013

Contents

BoF Online

Editor-in-Chief

Jenni Hellström

ISSN

1796-9123 (online)

Postal address
PO Box 160
FI-00101 HELSINKI, FINLAND

Street address Snellmaninaukio
Phone +358 10 8311
Fax +358 9 174 872

Email
firstname.surname@bof.fi
www.bof.fi

Swift SPFB FI HH
Business ID 0202248-1
Domicile Helsinki

List of charts

List of tables

1 Introduction

In the wake of the recent economic crisis, unemployment rates in many countries have notably increased and the question of how to promote employment and combat unemployment has become a central and difficult matter for policy-makers. In the light of these challenges, Germany is commonly considered a role model for tackling the problem of unemployment.

Even as recently as a decade ago, Germany faced persistently high unemployment and its labour market institutions were regarded as a symbol of inflexibility. Today, the unemployment rate in Germany is remarkably low and not even the vast GDP drop in the recent ‘Great Recession’ has hampered this exceptional labour market performance. This striking change in the German labour market even led to the Nobel Prize winner Paul Krugman coining the term ‘German job miracle’ in order to describe the evolution of the German labour market.

The aim of this study is to shed light on this ‘job miracle’ in Germany. To this end, chapter 2 presents the German labour market reforms from 2003 to 2005. It describes the initial situation before the reforms. Moreover, the concrete steps of the reforms are explained in detail, namely the reform of the employment services and the activation of the unemployed as well as labour market deregulation.

Chapter 3 considers in depth the German ‘job miracle’ itself. Section 3.1 outlines Germany‘s transition from the ‘sick man of the euro’ to the ‘German job miracle’. It presents the structural change Germany underwent after the labour market reforms. The most relevant characteristics of the post-reform labour market in Germany are reduced overall and long-term unemployment and increased matching efficiency; a further important observation is a reform-induced decrease in the reservation wage, reflected in a prolonged period of wage restraint and a moderate development in unit labour costs.

Part of the favourable condition of the German labour market nowadays is its resilience in the Great Recession. Labour adjustment to the vast GDP shock was achieved via a decrease in both average working hours and hourly productivity. Moreover, five key factors accounting for the exceptional performance of the German labour market in the crisis are identified: 1) the strong presence of measures of internal firm-flexibility, 2) strong cooperation between the social partners, 3) firms’ willingness to keep their workforce stable, 4) the favourable structure of the economic shock and 5) the sound condition of the overall economy before the crisis emerged.

Despite the favourable overall condition of the German labour market, there have, however, also been adverse developments. This other side of the German ’job miracle’ is presented in section 3.2. The major critical developments in Germany since the labour market reforms are the pronounced presence of non-regular employment, employment limitations for women in mini-jobs, as well as increased inequality and risk of poverty in the country. However, the most problematic aspect can be identified in the presence of the working poor, persons who are living close to or at poverty level despite being employed.

Chapter 4 considers the German ‘job miracle’ in an international context by comparing the German labour market reforms from 2003 to 2005 with the major reform steps implemented in France, Italy and Spain in the recent crisis. A key insight of this country comparison is that the reforms in Germany focused on different means of reducing unemployment than in the comparison countries: whereas Germany focused strongly on the activation of the unemployed, the comparison countries put the emphasis on labour market deregulation as well as the alleviation of the inherent labour market divide between insiders and outsiders. Moreover, this observation appears to be closely linked to the lack of external and internal flexibility measures in the comparison countries as opposed to Germany. Also, the different initial political situation and the overall state of the economy could have played a crucial role for the design of the reforms: Germany implemented the comprehensive structural change in a phase of structural problems and high unemployment and not amid a severe economic crisis with excessive unemployment; this factor might have favoured deregulation over activation in the comparison countries.

Chapter 5 presents the study’s main conclusion.

2 The German labour market reforms (2003–2005)

'We are going to cut the services provided by the state, promote self-responsibility, and we will be forced to demand more individual contribution from every single one of us. All forces of society are going to have to contribute: Employers and employees, the self-employed and also pensioners. We are going to have to make a vast common effort, in order to accomplish our goals. […] Our Agenda 2010 contains wide-ranging structural reforms. By the end of this decade, these reforms are going to bring Germany back to the top in prosperity and labour.' (Excerpt from the government declaration of Gerhard Schröder (14 March 2003); author's own translation; source: Deutscher Bundestag, 2003).

This citation stems from the government declaration of former chancellor Schröder in March 2003, which represented the starting point of 'Agenda 2010', a programme aimed at restoring Germany's competitiveness and welfare. In this speech, Schröder also highlighted that he would 'not accept that solutions founder on individual interests, because of a lack of strength to community' (Deutscher Bundestag, 2003), thereby underlining his commitment to the structural change and the inevitability of reform efforts. Agenda 2010 was a far-reaching reform package implemented by the social democratic-green coalition, comprising, among other things, tax reductions, health and pension reform and a reduction in bureaucracy (Astheimer et al., 2013). The most prominent element of this reform package was the labour market reforms implemented from 2003 to 2005 and intended to tackle Germany's high and persistent unemployment. This was the most comprehensive reform of the labour market and the social state since the foundation of the Federal Republic of Germany (Klinger and Rothe, 2010). Despite the success regarding the key figures of the German labour market in international comparison, the reform steps have been the subject of a highly controversial discussion. Proponents of the reforms attribute Germany's favourable situation nowadays to the reforms, for which Schröder sacrificed his chancellorship. By contrast, the reforms' opponents regard them as a symbol for the aggravation of Germany's social divide and as a betrayal of the social democrats' constituents (see e.g. Volmer, 2013).

This chapter aims at shedding light on the German labour market reforms from 2003 to 2005. Section 2.1 gives an overview of the initial situation in Germany before the reforms.

Section 2.2 presents the labour market reforms in detail. The chronology of implementation is outlined in section 2.3.

2.1 The initial situation

This section provides a brief overview of the situation on the German labour market and in its institutions before the labour market reforms of 2003–2005.

Low employment incentives

Before the reforms, German labour market institutions could be characterized as costly and inefficient in combating the country's high unemployment. Rather than serving as a safety net of last resort, the unemployment benefit scheme aimed at preserving the social status of the unemployed. Benefit payments were based on previous income and employment duration. In addition to the unemployment benefit scheme, there was also a social assistance scheme in place (Jacobi and Kluve, 2007).

(1) **Unemployment benefits** were in general granted for up to 6 months of unemployment – in certain cases up to 32 months – depending on the person's age and employment duration. The payments equalled 67% of the last salary with a ceiling of EUR 4,250 per month. They were financed via unemployment insurance (Jacobi and Kluve, 2007).

(2) **Unemployment assistance** was available after the expiration of eligibility for unemployment benefits. There was no maximum eligibility period. These tax-funded payments generally equalled 57% of the last net income (Jacobi and Kluve, 2007).

(3) Tax-financed **social assistance** provided financial support to households with incomes under a certain threshold, unconditional on previous employment (Jacobi and Kluve, 2007).

In 2004, the replacement rates –the percentage of previous income granted as unemployment benefits – for the long-term unemployed in Germany exceeded those of any other OECD country. Moreover, the tax system reinforced the low employment incentives; this held in particular for the lower-skilled (Jacobi and Kluve, 2007).

In addition to the outlined problems inherent in the unemployment benefit schemes, the respective benefits were unconditional on sufficient search efforts. Furthermore, the public employment agencies offered only limited assistance and monitoring. Job training and public job creation measures were offered. However, the measures were scarcely aimed at direct re-integration into employment, and the programmes were restricted to a narrow customer range. Moreover, the skills and individual situation of a job-seeker were scarcely assessed and the assignment of training programmes was predominantly subject to the discretion of the respective case worker (Jakobi and Kluve, 2007).

Structural problems resulting from German reunification

In the pre-reform phase, Germany was in the process of handling the enormous economic burden of reunification in 1990. Instead of choosing a gradual integration approach, allowing a slow adjustment of the formerly centrally planned East German economy, an approach of rapid, all-embracing unification was chosen: a political, monetary and social union (Bonin, 2005). East Germany's nationalized industry was in a desolate state with a productivity level on average amounting to roughly one third of West German firms (Heilmann et al., 2010). As to the labour markets, the integration of East Germany signified an abrupt increase in the labour force of approximately one third. Additionally, these workers were insufficiently trained and badly prepared for instant employment in an open market environment. Nevertheless, the adjustment of Eastern German wages to Western German levels was a central political goal (Jakobi and Kluve, 2007). This was also in line with the general promise of chancellor Kohl in 1990, to convert former East Germany into 'blooming landscapes' with a high living standard. By 1992, the East German economy had declined by approximately one third (Heilmann et al., 2010). In what followed, eastern Germany faced increasing unemployment and ongoing dependence on transfer payments from the western part of the country. Additionally, the scope for expansive growth policies was limited because reunification also represented an enormous fiscal burden, in particular in view of the Maastricht criteria (Jakobi and Kluve, 2007).

2.2 The reform steps

In order to fight the high and persistent unemployment in Germany, a profound reform and modernization of the labour market was implemented from 2003 to 2005. The commission 'Modern services on the labour market' gave recommendations for the steps to be taken in the reform under the guidance of Peter Hartz – a former member of the board of directors of Volkswagen (Jacobi and Kluve, 2007). The reform's overall goal was a significant reduction in unemployment by affecting the flow variables (Klinger and Rothe, 2010). The reform can be summarized in three main pillars (Jakobi and Kluve, 2007):

1. Reform of the employment services
2. Activation of the unemployed
3. Labour market deregulation

Pillar 1: Reform of the employment services

The main goal of Pillar I – reform of the employment services – was to improve the performance of placement services and policy programmes. This was to be achieved by establishing forms of quasi-market mechanisms and by modernizing and rationalizing the public employment services. Cost-efficiency was to be the main criterion for the selection of programme contents and participants. In order to increase control and accountability of employment agencies, every employment agency was subjected to quantitative individual goals (Jakobi and Kluve, 2007).

Before implementation of the reform, the organization of the employment services was strongly hierarchical. Reform steps were implemented to transform these services into customer-oriented centres offering an extended range of services, such as counselling and the administration of benefit payments. By assigning a specific case worker to each job seeker, the case assignments were to be rendered more individual (Jakobi and Kluve, 2007).

The initiative of creating quasi-market forces with the presence of both public and private providers was intended to create a competitive environment within the field of employment services, and thereby to improve service quality. A voucher system for integration services was introduced. A 'placement voucher' enables the job-seeker to use a private placement service in case of unsuccessful placement. An 'education voucher' allows a free choice of training measure provider (Jakobi and Kluve, 2007).

Additionally, several initiatives were introduced for improving the allocation of measures and resources. In contrast to the pre-reform phase, a highly standardized profiling process of every unemployed individual is now carried out. The person's capabilities, problems and perspectives on the labour market are assessed and the individual is assigned to one of four possible groups of job-seekers. The groups are defined according to perspectives on the job market. Each group is entitled to a corresponding action programme stating the measures available to the unemployed (Jakobi and Kluve, 2007).

Furthermore, the public employment services were given the possibility of outsourcing. For example, ‘Personal Service Agencies’ – temporary employment agencies for the unemployed – could either be conducted by the public employment agencies themselves or delegated to a private temping agency (Jakobi and Kluve, 2007).

Lastly, a strong evaluation mandate was tied to the reforms, in order to enable scientific assessment of their success and continuous optimization. In 2007, over 100 researchers and more than 20 economic and sociological research institutes evaluated the impact of the labour market reforms on behalf of the government (Jakobi and Kluve, 2007).

Pillar 2: Activation of the unemployed

The principle of ‘rights and duties’ – a profound activation strategy – denotes the core element of the German labour market reforms from 2003 to 2005. The reforms were to foster activity and self-responsibility among job-seekers and aimed at their direct re-integration into the labour market (Jakobi and Kluve, 2007). In this section, the various activation measures are outlined.

Subsidy payments

Subsidy payments were introduced in order to further the flows out of unemployment. Start-up subsidies (‘Ich-AG’) for the unemployed were implemented for promoting self-employment. As long as the recipient‘s annual income does not exceed EUR 25,000, the monthly support equals EUR 600 in the first, EUR 360 in the second and EUR 240 in the third year (Jakobi and Kluve, 2007). Furthermore, ‘integration subsidies’ were introduced for firms hiring hard-to-place workers, which aimed at compensating the employer for the person’s lower productivity. These funds were available for 6 to 24 months, whereby the rate of subsidy could equal 50% of the remuneration at most. Priority is given to older and disabled employees. In order to foster employment of older job-seekers, reductions in social security contributions were introduced in the form of an exemption from unemployment insurance contributions for employers hiring a worker aged at least 55 years. Also, ‘wage protection’ – a wage subsidy granted to job-seekers from 50 years upwards – was introduced for those accepting a post with a salary lower than in their previous employment. The payment granted can amount to at most 50% of the wage difference between previous and current employment and is paid for the same period as the remaining entitlement period for benefit scheme I (Jakobi and Kluve, 2007).

Atypical forms of employment

Atypical forms of employment with reduced social security contributions were created. The reforms raised the previous maximum income level for exemption from social security contributions from EUR 325 to EUR 400 (nowadays EUR 450). If this ‘mini-job’, as it’s known, is a person’s only source of income, it is also tax free. Moreover, the concept of ‘midi-jobs’ was introduced; this refers to jobs with reduced social security contributions and covering an income range from EUR 450.01 to EUR 850 (Jakobi and Kluve, 2007; Minijob-Zentrale, 2013).

Sanction elements

In order to monitor the search activities and efforts of the unemployed, sanction elements were introduced. Unemployed persons are obliged to accept any suitable post they are offered. Furthermore, a written ‘integration agreement’ is filed for every unemployed person. This agreement contains information about the person’s profile and individual action plan. It also states the services provided and obligations regarding job search activities and programme participation. A violation of the integration agreement or any other lack of cooperation can result in a severe sanction – the temporary cutting of monetary benefits. Moreover, there are several mechanisms for verifying the availability of the unemployed for potential job offers, including compulsory training measures. A further instrument is the ’one-euro job’, a workfare measure, for which the unemployed person receives a very low hourly wage in turn for his/her work in the public sector – typically one symbolic euro per working hour (Jakobi and Kluve, 2007). This is an obligatory measure aimed at providing the unemployed with at least temporary work experience and thereby increasing the possibility of re-integration into employment. This interruption of the unemployment spell with mandatory work is also intended to further the job-search activities of the long-term unemployed.

Reform of the benefits scheme

However, the most relevant and also most criticized reform step undertaken was the wide-ranging change of the former system of unemployment benefits, unemployment assistance and social assistance into a two-pillar benefit model. This reform step is mostly referred to as ‘Hartz IV’, as it was the last of the four reform laws.

As already outlined, benefit entitlement before the reforms was mainly determined by the social security contributions paid before unemployment. By contrast, after the reforms, the most relevant criterion became the individual’s ability to work at least 15 hours a week. Only persons unable to work because of disability, sickness, or care obligations are exempt from participation in the described activation policies and eligible for benefit type II without having to demonstrate any search activities. However, if an individual is classified as capable of work, the eligibility for unemployment benefits is subject to mandatory and active cooperation (Jakobi and Kluve, 2007). The two benefits schemes established by the reforms can be characterized as follows.

Benefit type I is generally available for the first 6 to 12 months of unemployment and is dependent on the contributory period in the previous five years as well as age (Arbeitsagentur, 2009). It amounts to 60% (with children 67%) of the last salary (Klinger and Rothe, 2010). Thereafter, an unemployed person is entitled to **benefit type II**, which is not based on previous earnings, but is a means-tested, flat-rate payment (see Table 1). In addition, persons who never contributed to the social security scheme are eligible for benefit type II (Jakobi and Kluve, 2007). Benefit scheme II can be understood as a provision of basic social security. Consequently, the reforms transformed the previous three-pillar benefit system into a two-pillar scheme by combining the previous unemployment assistance and social assistance into benefit scheme II, roughly at the level of the previous social assistance (Klinger and Rothe, 2010).

Table 1. Benefit scheme II in detail

Non-monetary benefits	
• *Accommodation and heating*	
• *Initial costs of establishing a household (furniture, household appliances)*	
• *One-time payment for clothes*	
Monetary benefits (in January 2013)	
Extent of the benefit dependent on the respective household:	
• *Single persons:*	***EUR 382***
• *Two adults living together (per person):*	***EUR 345***
• *Adults 18 to 24, living with their parents:*	***EUR 306***
• *Children <6 years:*	***EUR 224***
• *Children 6 to 13 years:*	***EUR 255***
• *Children 14 to 17 years:*	***EUR 289***

Author’s own illustration; source: Bundesagentur für Arbeit, 2012.

Pillar 3: Deregulation of the labour market

The German labour market reforms did not aim at an overall liberalization of the labour market. Deregulation focused rather on liberalizing certain areas of the labour market while only implementing minor changes to the protection of regular workers (Eichhorst and Marx, 2009). Deregulation focused on temporary agency work, dismissal protection and fixed-term contracts. The reforms did not change the strongly centralized wage-setting process (Jakobi and Kluve, 2007).

Temporary agency work

Temporary agency work (‘Zeitarbeit’, ‘Leiharbeit’), temping is a practice in which an employee is hired out by his employer (‘temporary employment agency’, or ‘temping agency’) to a third party for a mostly temporary assignment in turn for compensation. This practice has become more and more widespread and serves in some sectors, e.g. manufacturing and certain lower-wage services, as a frequently used means of access to employment. Central to critiques of this approach is the excessive use of temporary agency work to the effect that it does not serve as a bridge into regular employment. This renders finding normal employment increasingly unlikely and hence works to the disadvantage of the employees.

Temping had been gradually deregulated since the late 1990s (Jakobi and Kluve, 2007). However, the Hartz reforms implemented vast changes in the field of temping by abolishing the strong regulations previously in place.

The prohibition of repeated renewals of fixed-term contracts in temporary agency work was suspended. Moreover, the prohibition of re-employment of previously dismissed workers within three months after the dismissal was repealed. Also, the reforms allowed the previously forbidden practice of synchronization – hiring temporary workers only for the period of their assignment in the firm. Furthermore, the former maximum assignment duration (24 months) of temporary workers was suspended (Bräuninger et al., 2013). Given the substantial deregulation, a requirement for the treatment of temps was introduced. This states that temping agencies are either compelled to guarantee equal pay as well as equal treatment of temporary workers and regular workers or to join a collective bargaining agreement (Jakobi and Kluve, 2007).

Dismissals and fixed-term contracts

The reforms also simplified and expanded exemptions from regulations governing dismissals and fixed-term contracts. An important example is the expansion of the exemption from dismissal protection for regular workers: Before the reforms, firms up to a size of 5 employees were exempt from the dismissal regulations; the reforms increased the maximum firm size for this exemption to 10 employees. A further deregulation was undertaken regarding older employees: The minimum age for permission for a repeated renewal of fixed-term contracts was lowered from 58 to 52 years (Jakobi and Kluve, 2007). Moreover, recently established firms were given the possibility of using fixed-term contracts without a valid justification (Eichhorst and Marx, 2009).

2.3 Timeline of the reforms

The reform steps presented in the previous sections were introduced in four different laws, introduced at different dates, referred to as ‘Hartz I to IV’. The following table outlines the timeline for implementation of the laws and their respective contents.

Table 2. Timeline of the reforms

***Hartz I** (January 2003)*

- *Enlarged definition of ‘suitable’ work*
- *Personal integration agreement*
- *Sanctions*
- *Education and placement vouchers*
- *Deregulation of temporary agency work*
- *Deregulation of fixed-term contracts and dismissals*
- *Personal service agency*

***Hartz II** (January 2003)*

- *Atypical employment: mini-jobs and midi-jobs*
- *Start-up subsidies (‘Ich-AG’)*
- *Wage protection*

***Hartz III** (January 2004)*

- *Reformation of the employment agencies*
- *Introduction of job centres*
- *Individual case manager for the unemployed*
- *Integration subsidies*

***Hartz IV** (January 2005)*

- *Reformation of the benefit scheme*
- *One-euro jobs*

(Based on Klinger et al., 2013; Brussig et al., 2006; Klinger and Rothe, 2010)

3 The German 'job miracle'

'Consider, for a moment, a tale of two countries. Both have suffered a severe recession and lost jobs as a result — but not on the same scale. In Country A, employment has fallen more than 5 percent, and the unemployment rate has more than doubled. In Country B, employment has fallen only half a percent, and unemployment is only slightly higher than it was before the crisis.

'Don't you think Country A might have something to learn from Country B?'

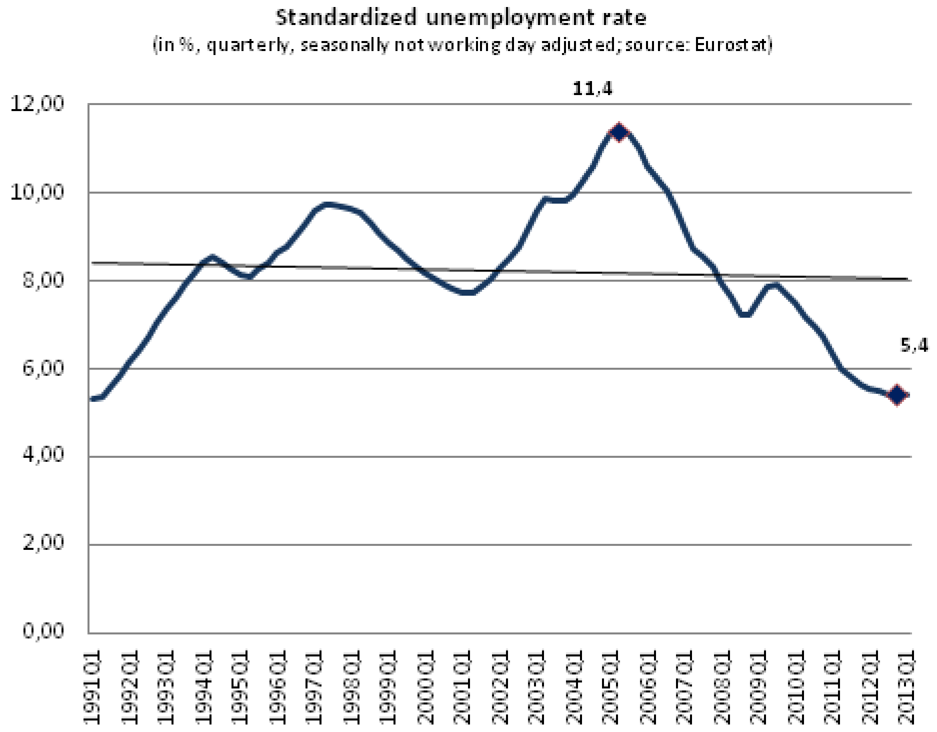
(Source: Krugman, 2009.)

This quotation stems from Paul Krugman's New York Times Blog from 2009. It contains a critical assessment of the labour market performance in the United States ('Country A') as opposed to Germany ('Country B') in the Great Recession. In this column, Krugman also coined the term 'German job miracle', referring to the exceptional developments on the German labour market in the financial crisis (Krugman, 2009). By contrast, roughly one decade ago, the state of the German labour market was very different. Germany was a symbol of inflexibility and poor labour market performance. In 1999, The Economist even referred to Germany as 'the sick man of the euro', hinting at the severe structural problems inherent in the country (The Economist, 1999). These divergent characterizations of the very same country point out that Germany must have undergone a substantial change in recent times. This chapter aims at shedding light on the German 'job miracle'. For this purpose, section 3.1. presents the transition of the German labour market from the 'sick man of the euro' to the 'German job miracle'. It addresses the structural changes of the German labour market as well as its internal flexibility in the Great Recession. Section 3.2 presents the other side of the 'job miracle' by addressing selected critical aspects of the German labour market in recent times which are often omitted when referring to the 'job miracle' in Germany. Section 3.3 presents our conclusions on the German 'job miracle'.

3.1 From the 'sick man of the euro' to the 'German job miracle'

What induced the change from the 'sick man of the euro' to the 'German job miracle'? The explanatory approaches provided by the academic literature are manifold. Some articles addressing the German 'job miracle' consider it a phenomenon limited to the labour market performance in the Great Recession (see e.g. Möller, 2010; Burda and Hunt, 2011). But, as Chart 1 illustrates, the exceptionally good labour market performance already evolved before the financial crisis and has persisted ever since: The unemployment rate peaked at 11.4% in 2005q2 and then, following a dramatic decrease, reached 5.4% in 2013q1.

Chart 1. Quarterly unemployment rate in Germany



This observation suggests the following conclusions. First, the improved labour market performance had already begun in 2005 and hence goes beyond a mere business cycle phenomenon perceptible only in the Great Recession. Second, the overlap of the start of the unemployment decrease and the completion of the reforms in 2005 suggests that the reforms could have induced a labour market turning point. Also, the academic literature identifies several further reform-induced structural changes in the labour market. These structural changes since the Hartz reforms are presented in the following section, 3.1.1. However, there are further important features of the German labour market that were already in place before the reforms and greatly contributed to the resilience of the labour market in the Great Recession and thereby to the favourable condition prevailing nowadays. These elements and their relevance in the financial crisis are outlined in section 3.1.2.

3.1.1 Structural changes after the reforms

This section provides an overview of the structural changes in the German labour market after the labour market reforms.

Substantial reduction in unemployment

As previously described, unemployment has decreased substantially since the reforms: from 2005q2 to 2013q1, the unemployment rate dropped by roughly 6 percentage points. Also, long-term unemployment (12 months or more) in terms of the share of the active population declined significantly from 6% in 2005 to 2.5% in 2012, as illustrated in Chart 2. Also, a decrease in the share of long-term unemployed in the total unemployed from 2005 to 2012 of roughly 7.5 percentage points is discernible. This suggests both shorter unemployment spells and more successful re-integration in the labour market after the reforms. Klinger et al. (2013) confirm the strong decline in long-term unemployment and emphasize the notable increase in the probability of returning to employment. Accordingly, even though the subsequent employment relationship has not always been sustainable, the decrease in long-term unemployment is nonetheless an important improvement, since the shortened unemployment duration and the reduced risk of short-term becoming long-term unemployment helps avoid both negative impacts on labour market participation and the social costs of long-term unemployment.

Chart 2. Long-term unemployment in Germany

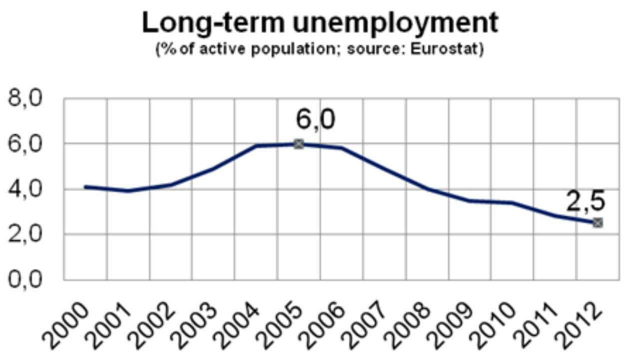
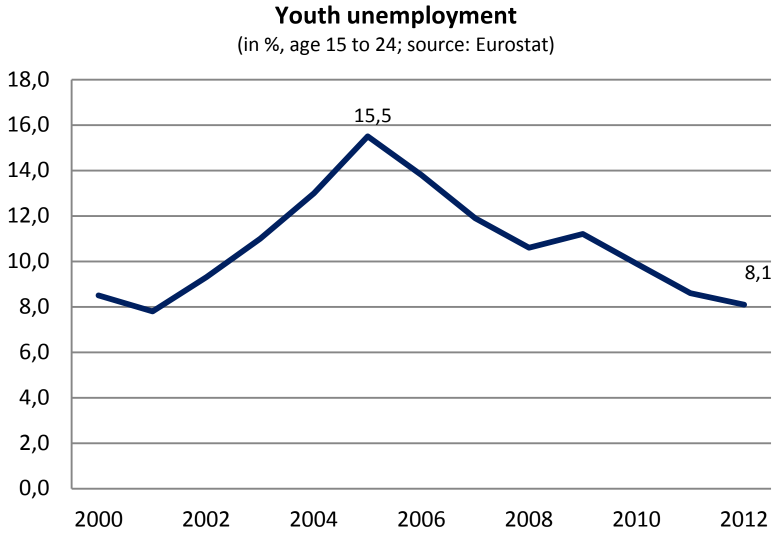


Chart 3 demonstrates that also youth unemployment substantially decreased following the reforms, from 15.5% in 2005 to 8.1% in 2012.

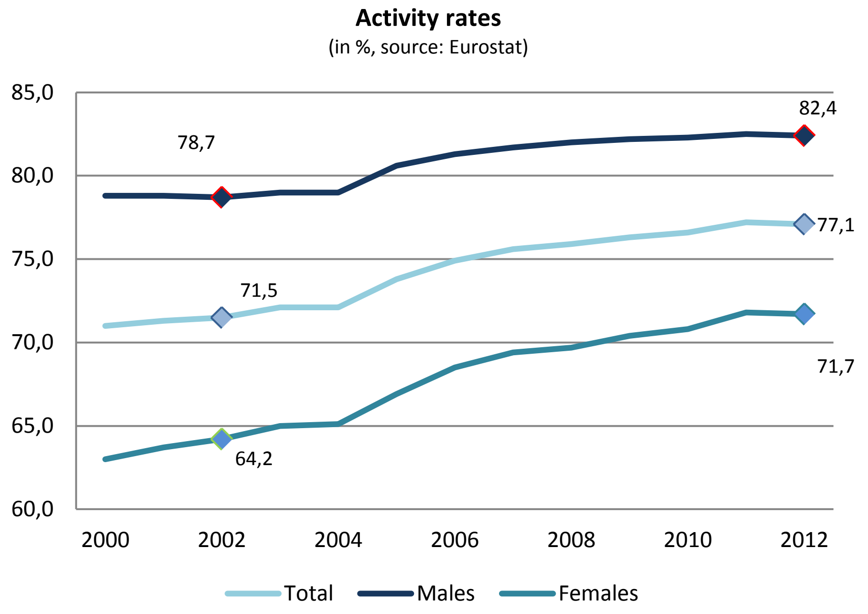
Chart 3. Youth unemployment in Germany



Higher labour force participation

Another favourable development is the increase in labour force participation (see Chart 4). The activity rate of the total population in 2012 exceeded the respective value in 2002 by roughly 5.6 percentage points. The increase in the activity rates of women (7.5 percentage points) was more pronounced than for men (3.7 percentage points) over this period.

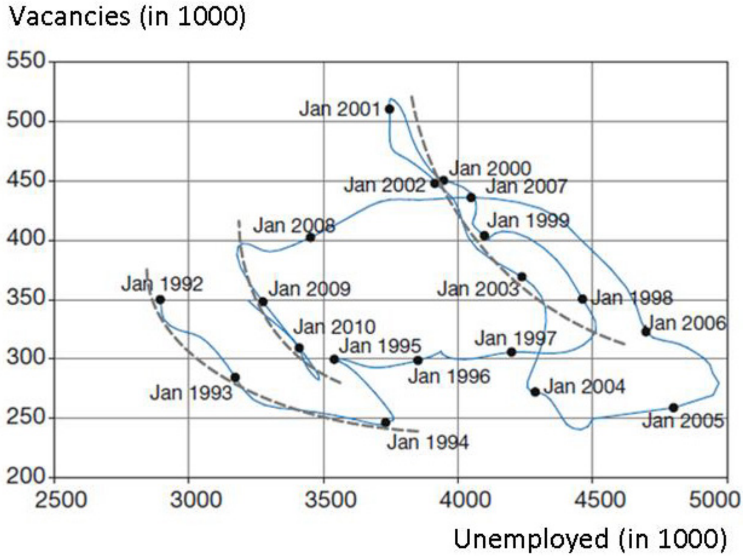
Chart 4. Labour force participation in Germany



Increased matching efficiency

Since the labour market reforms, improved matching efficiency is discernible. This is suggested by shortened search processes. Also, the Beveridge curve shifted inwards after 2005 (Chart 5).

Chart 5. Pre- and post-reform Beveridge curves



Source: Gartner and Klinger, 2010

Thus, matching efficiency increased, since the same amount of vacancies is now coupled with lower unemployment (see Klinger and Weber, 2012; Gartner and Klinger, 2010). Moreover, Klinger et al. (2013) confirms the positive effect of the German labour market reforms on matching efficiency via a semi-logarithmic model. According to this study, the matching of the long-term unemployed was especially improved.

More favourable labour adjustment over the business cycle

Furthermore, based on the business cycle dating presented in Table 3, labour adjustment over the business cycle has changed since the reforms. The volume of work grew more intensely in the post-reform upswing (‘upswing II’) than in the pre-reform upswing (‘upswing I’). This holds despite a stronger employment increase in the pre-reform upswing, since it was to a large extent realized in minor employment, whereas in upswing II mainly full-time jobs were created (Gartner and Klinger, 2010). Even more substantial differences are perceptible concerning recessions. Despite a comparatively small GDP decrease, employment fell strongly in the pre-reform recession; by contrast, employment was hardly negatively affected at all in the Great Recession, even though there was an enormous drop in GDP. In sum, the post-reform labour market appears to be more successful in creating employment in upswings and to be more resilient against negative employment effects in recessions (Gartner and Klinger, 2010).

Table 3. Recent business cycles in the German economy

Upswing I	Recession I	Upswing II	Recession II	Upswing III
1998–2001	2001–2004	2004–2008q1	2008q2–2009q1	since 2009q2

Source: Gartner and Klinger, 2010

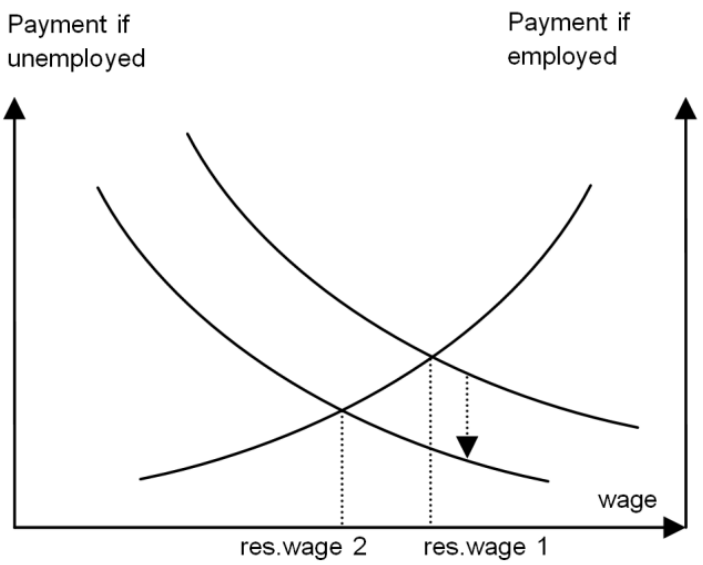
Wage restraint after the reforms

Both economic theory and recent empirical findings indicate that the German labour market reforms, and in particular the more restrictive design of the unemployment benefit scheme, curbed wage development in Germany.

The theoretical considerations regarding the effect of the reforms on wage setting are based on the search model of Diamond, Mortensen and Pissarides, which enables statements about the conditions under which an individual is willing to accept a job and how firms take into account the reservation wages of future employees. An individual makes a rational decision about accepting or rejecting a post by comparing its position in case of unemployment and immediate employment. The latter position is characterized by the monetary value of immediate employment and the former position by the value of all payments including possible future wages. The individual takes into account the expected wage level, expected unemployment benefits, as well as the possibilities of finding an alternative job and returning to unemployment. The key concept for analysing the effect of a reduction in unemployment benefits on wage setting within this model framework is the reservation wage. This is the wage level for which the position in case of unemployment is equal to the position when being employed and thus renders an individual indifferent between the two alternatives (Arent and Nagl, 2011). Hence, it corresponds to the minimum wage an individual has to be offered in order to accept a job offer.

Chart 6 illustrates the theoretical effect on the reservation wage of a reduction in unemployment benefits. The payment function of employment increases and the payment function for unemployment decreases with the wage level. The reservation wage equals the wage level in the intersection point of the curves (Arent and Nagl, 2011).

Chart 6. Unemployment benefits and reservation wage

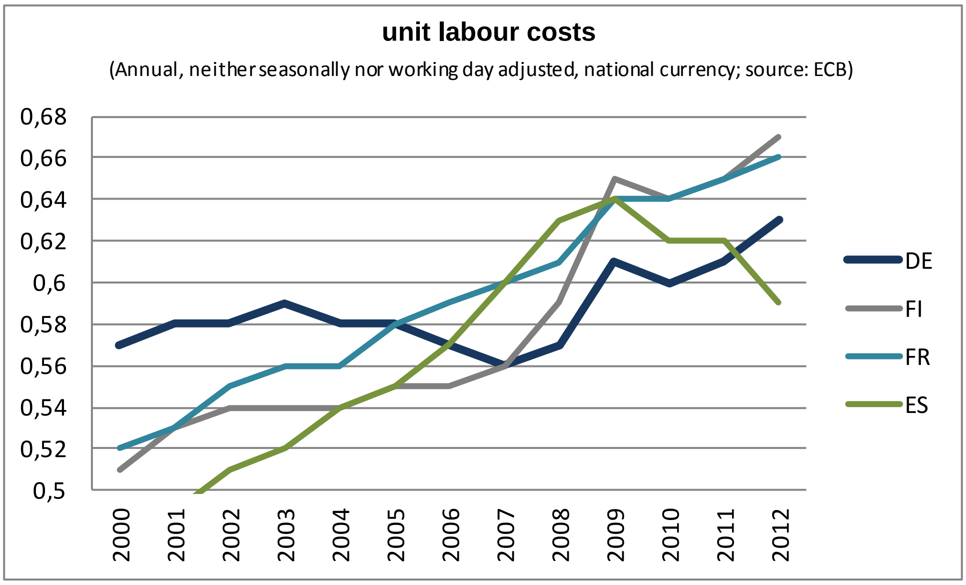


Source: Arent and Nagl, 2011

A reduction in unemployment benefits induces a downward shift of the payment function in case of unemployment, since the payout for this scenario decreases. Thus, the option 'employment' is rendered more attractive. The new reservation wage is lower than in the initial situation (Arent and Nagl, 2011). In sum, a reduction in unemployment benefits induces a reduction in the reservation wage and hence in the minimum wage level firms have to offer for a post to be accepted. All in all, this theoretical model predicts a negative effect on wage levels of a reduction in the unemployment benefit scheme, as implemented by the Hartz reforms. Arent and Nagl (2011) confirmed the wage-curbing effect of the German labour market reforms econometrically.

An observation in line with this reasoning is the weakened negotiating position of labour unions in collective bargaining since the reforms. This is due to workers' increased fear of social decline, which is closely linked to the redefinition of appropriate job offers to a job-seeker, the reduction in benefit payments and entitlement periods, and the combination of unemployment and social assistance into the merely means-tested benefit scheme II (Gartner and Klinger, 2010). In other words, the willingness of workers to make concessions in return for job security was increased. Consequently, the maximum claims labour unions made in collective bargaining were substantially lower, as maintaining employment has become the most relevant goal.

Chart 7. Unit labour costs in Germany and other euro area countries



The series on unit labour costs (Chart 7) provides further evidence for the wage-curbing effect of the reforms: The development of unit labour costs has been particularly modest since the start of reform implementation in 2003. In addition, this wage restraint discernible in Germany after the reforms had two important consequences:

1. It favoured increased employment in the upswing after the reforms, since labour costs fell substantially short of workers' productivity (Gartner and Klinger, 2010).
2. It represented a buffer for firms in the Great Recession, which enabled employers to avoid large-scale dismissals, keep the workforce stable and even utilize it at lower productivity (Gartner and Klinger, 2010).

3.1.2 Resilience in the Great Recession

As outlined previously, the recent favourable developments in the German labour market are to a substantial extent related to the labour market reforms. Nevertheless, there are further important characteristics of the German labour market, in particular certain labour market instruments, which already existed before the reforms. These measures made a major contribution to avoiding large-scale job losses in the Great Recession and thereby also contributed substantially to the favourable labour outcomes today. These key characteristics as well as their relevance in the Great Recession are outlined below.

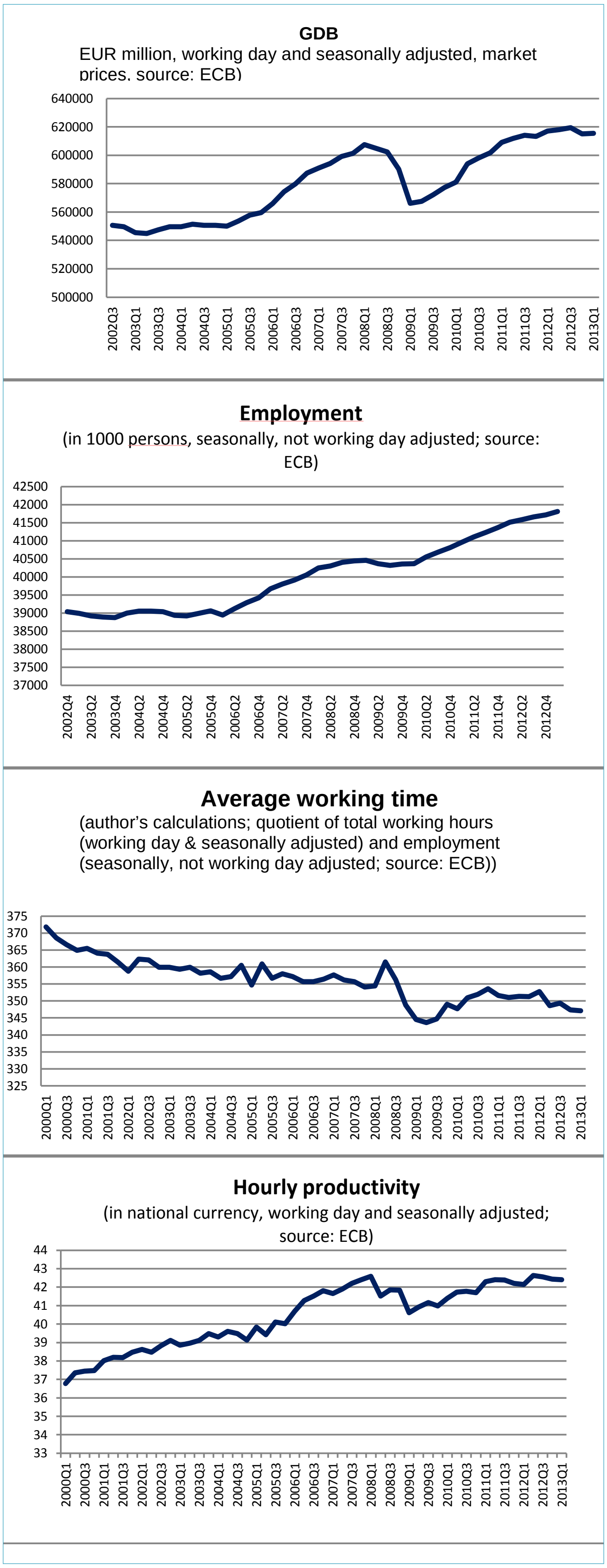
Labour adjustment in the Great Recession

For understanding the resilience of the German labour market in the Great recession, the series on GDP, employment, average working time and hourly productivity are useful tools (Chart 8). Germany experienced a vast drop in GDP from 2008q2 to 2009q1. By contrast, employment hardly decreased, it merely stagnated. What explains this minor response of employment to the drop in GDP? The series on average working time and hourly productivity demonstrate that labour adjustment to the GDP shock was realized via two channels other than dismissals:

1. An intense reduction in average working time
2. A substantial drop in hourly productivity

This observation suggests the strong use of internal flexibility measures within firms, which allowed for the adjustment of individual working time to the firms' economic condition as opposed to external labour adjustment via dismissals. However, it also demonstrates the willingness of the firms to keep their workforce stable, since each worker was not only utilized at lower working time, but also at lower hourly productivity.

Chart 8. Labour adjustment in Germany during the Great Recession



The main factors for the resilience of the German labour market in the Great Recession are presented next.

Five key factors behind the German labour market‘s resilience in the Great Recession

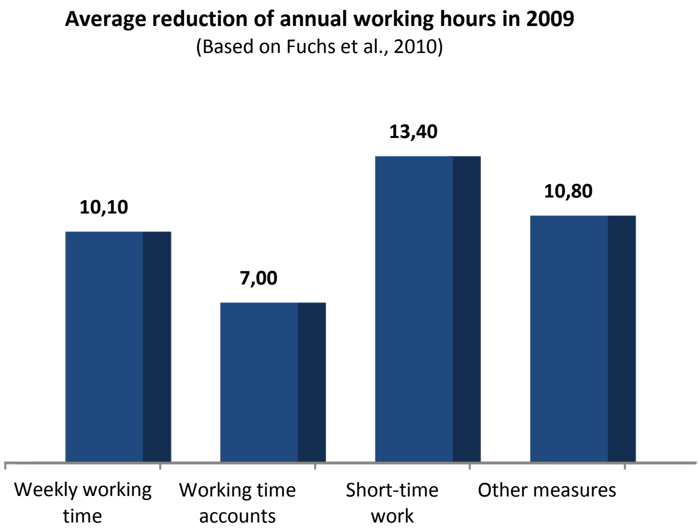
1. **Strong use of internal flexibility measures**

As outlined previously, average working time was decreased drastically during the financial crisis, whereas employment was hardly affected, suggesting the intense use of internal flexibility within firms.

The design of working time accounts in Germany favours an initial internal labour adjustment as opposed to dismissing employees in firms where these working time accounts are used. These accounts allow firms to use overtime without having to pay an overtime premium. However, the accumulated overtime on the working time account has to be reduced by an equal degree within a certain time frame. Dismissing workers with high working time balances is linked to high costs since the accumulated overtime has to be compensated in this case including an overtime premium (Burda and Hunt, 2011).

Chart 9 sheds light on the use of the various internal flexibility instruments in this period. The average working time in 2009 was 41.3 hours lower than in 2008. The main components of this decrease in average annual working time were the reduction in agreed weekly working hours (–10.1 hours), the reduction in working time account balances (–7.0 hours) and the practice of short-time work (–13.4 hours) (Fuchs et al., 2010). This illustrates both the variety of internal flexibility instruments at the disposal of German firms and the intensity of their use in the crisis. Moreover, since the decrease in average annual working time in 2009 exceeded the general weekly working time of one full-time employee, this also demonstrates the extent to which dismissals could be prevented in the Great Recession.

Chart 9. Internal flexibility instruments in Germany



2. Strong cooperation between the social partners

Favourable labour market conditions were created by the strong cooperation between labour unions and employers. Important examples of this practice are the formation of 'alliances for jobs' and the agreement on opening clauses in collective agreements (Möller, 2010). This strong cooperation enabled the internal flexibility in the first place.

3. Firms' willingness to keep their workforce stable

As already outlined, average working time was substantially reduced by firms' use of internal flexibility measures in the Great Recession. However, the firms also accepted a decrease in hourly productivity in this phase. Thus, the willingness of the firms to keep the workforce stable must also have played a decisive role.

The academic literature provides several explanatory approaches for firms' motivation for conducting this large-scale labour hoarding strategy. One argument is that the previously outlined wage restraint provided a buffer for firms and enabled them to utilize labour at both lower working hours and lower hourly productivity, and by doing so dismissals could be avoided (Gartner and Klinger, 2010). A further theory is that the firms were able to avoid large-scale dismissals in the Great Recession because of their reluctance to hire in the pre-crisis upswing: Firms hired fewer employees than predictions based on the economic conditions would have suggested. According to this theory, a major explanation for this reluctance to hire was employers' pessimism regarding future economic conditions during the upswing before the Great Recession (Burda and Hunt, 2011). Another theory states that a perceived shortage of skilled labour, in particular in manufacturing, could have played a role. The workforce in these firms is highly specialized and trained. Thus, a reduction in the workforce correlates with an enormous loss of firm-specific human capital. Moreover, when hiring new employees after the recession, there would have been high costs of search, hiring and training, while firms' production capacity in the ensuing recovery would also have been. For these reasons, firms might have been reluctant to lay off workers (Möller, 2010).

4. Favourable structure of the economic shock

The fact that the firms with a strong economic performance in the pre-crisis phase were also excessively affected by the Great Recession also accounts to an extent for the resilience of the German labour market as a whole in the financial crisis. The Great Recession hit hardest the export-oriented manufacturing sector. However, these manufacturing firms were the 'growth engines' of the pre-crisis upswing with a strong economic performance. Table 4 illustrates both the higher growth in the pre-crisis phase and the more drastic GDP drop in the crisis of manufacturing as opposed to the economy as a whole (Möller, 2010).

Table 4. GDP change (in %) in the total economy and in manufacturing

	Total	*Manufacturing*
Upswing 2004q4–2008q1	*9.4*	*18.8*
Recession 2008q2–2009q2	*–5.9*	*–19.3*

Source: Möller, 2010.

5. Sound overall condition of the German economy

For explaining the resilience of the German labour market in the Great Recession, the fact that the German economy was in a sound overall state before the crisis erupted in 2008 also plays a decisive role. Budgetary consolidation was in progress and employment increasing. Germany was neither confronted with a stock market nor a housing price bubble. There was strong demand for German products by customers in both traditional and emerging markets. Furthermore, structural advances in the field of the labour market had been implemented before the crisis emerged. A prolonged phase of wage restraint had rendered Germany more competitive, since it enabled a considerable decrease in real unit labour costs, in particular relative to Germany's main competitors. Also, signs of a re-accelerating convergence process in eastern Germany were discernible. All in all, full employment was a realistic perspective for more and more German regions (Möller, 2010).

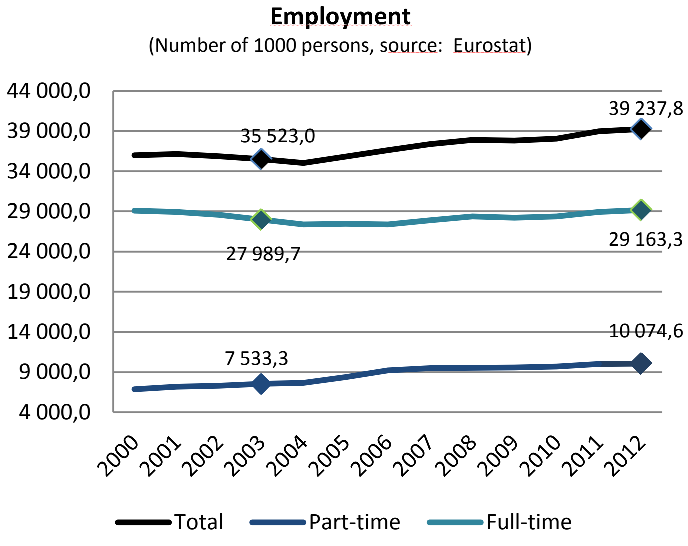
3.2 The other side of the 'job miracle': critical perspectives on the German labour market

The previous section presented the major reform-induced changes in the German labour market as well as further factors for its resilience in the Great Recession. However, there are critical perspectives on the German labour market that cannot be ignored when analysing the German 'job miracle'. These go beyond market performance and require us to take a closer look at the employment structure in Germany and potential social side-effects of the success suggested by the key indicators addressed previously. These critical perspectives are outlined below.

Presence of non-regular employment

As Chart 10 illustrates, full-time employment has increased notably since the labour market reforms. However, a substantial proportion of the total employment increase has been realized through part-time employment. This strong increase in part-time work since the labour market reforms suggests that the German 'job miracle' is presumably to an extent related to the practice of job sharing.

Chart 10. Part-time and full-time employment



Furthermore, the share of part-time work in total employment (Eurostat) in Germany in 2012q2 (25.8%) exceeds the euro area average by 4.8 percentage points. Also, this share clearly exceeds the respective figures for France (17.9%), Italy (17.0%), Spain (14.8%) and Finland (13.9%). The share of women in part-time employment (45.0%) in 2012q2 is substantially above the euro area average (35.9%) and notably higher than before the reform (39.2% in 2002q2). This observation could be related to the labour force entry of previously passive women due to the introduction of mini- and midi-jobs.

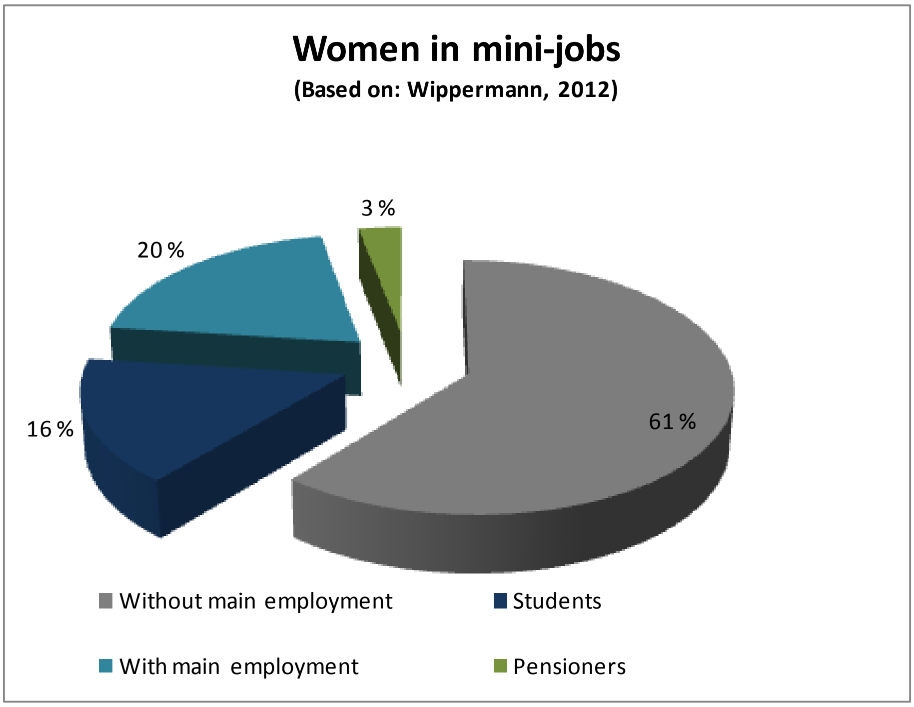
The share of fixed-term contracts (source: Eurostat) in 2012 is low in Germany (13.8%), below the euro area average (15.2%) and notably less than in countries such as France (15.2%) and Spain (23.6%). Nonetheless, the share of fixed-term contracts was even lower before the reform (12.0% in 2002).

Women in mini-jobs

A problematic development in line with the presence of non-regular employment is the over-representation of women in mini-jobs. For evaluating mini-jobs, it is crucial to understand their initial intention. Mini-jobs were initially designed to fulfil a bridging function, enabling transition into regular employment. They were intended to be of limited duration. The main target groups of this instrument were the long-term unemployed and women with employment interruptions due to family obligations. In addition, mini-jobs were also aimed at persons already under social security coverage, such as students, pensioners or persons already in regular primary employment. For this group, mini-jobs – due to their uncomplicated design – were to facilitate additional earnings exempt from taxes and social security contributions in a non-bureaucratic manner. Furthermore, the introduction of mini-jobs was intended to alleviate the incidence of unreported work (Wippermann, 2012).

When analysing the patterns of women in mini-jobs (Chart 11), it becomes apparent that only in a minority of cases does the mini-job serve as an additional source of income, i.e. for students, pensioners or in addition to a regular primary job. For the majority of women in mini-jobs (61%), this is their only source of income. Moreover, the share of women among all persons only employed in a mini-job exceeds two-thirds. Given the relatively low female labour participation rates, this suggests a notable over-representation of women in this category (Wippermann, 2012).

Chart 11. Patterns of women in mini-jobs



This observation seems to be closely related to the disincentives in place due to the common taxation of spouses in Germany. It allows an income exempt from taxes and social security contributions for the second earner – very often the wife – up to an income of EUR 450 per month (Wippermann, 2012). Thus, there are disincentives to take up part-time work with higher working hours or even full-time employment. 82% of the women only working in a mini-job are married. Moreover, 88% of the partners of the married women with just one mini-job are employed full-time and are thus responsible for the family's main income (Wippermann, 2012).

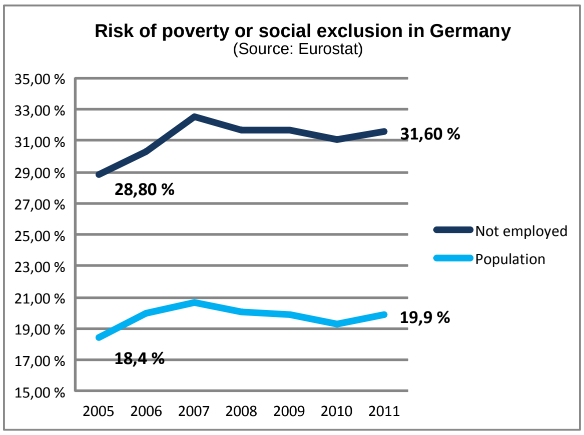
Besides their over-representation, the labour market prospects of women after having entered a mini-job are particularly poor. Only a very small share manage the transition into part-time (26%) or full-time employment (14%), whereas the majority (60%) exit the labour market into non-participation. Also, the average employment duration of women in mini-jobs equals 6 years and 7 months and is thus by no means of limited duration. Furthermore, mini-jobs were found to exert a 'stigmatizing' effect, attributable to employers' interpretation of being employed in a mini-job as a sign of insufficient qualification for regular employment. Moreover, women's probability of regular employment decreases with the duration of employment in a mini-job. In sum, instead of fulfilling the bridging function, mini-jobs rather act as a ‘trap’, rendering the transition into regular employment unlikely in the first place and even more and more unlikely the longer the duration of the mini-job (Wippermann, 2012).

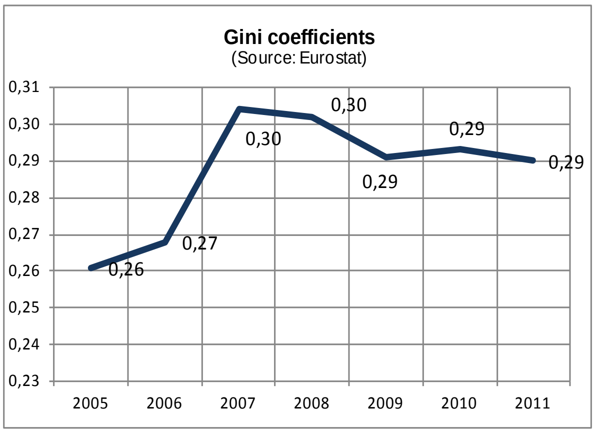
Statements about to what extent working only in a mini-job is a voluntary choice are difficult. However, there is evidence suggesting that this employment situation is not in line with the expectations of many women working in mini-jobs. For example, a survey on women’s motivation for entering a mini-job demonstrates that among the top four motives of these women are the attainment of material and emotional independence and the improvement of their own financial provision for old age. Moreover, even after having been employed in a mini-job for more than 5 years, women still hope that their contracts will be converted into regular employment (Wippermann, 2012).

Rising poverty and inequality

Chart 12 illustrates the development of the risk of poverty as well as inequality in Germany since the labour market reforms. The risk of poverty or social exclusion (Eurostat) in Germany has risen since 2005, the year the labour market reform reached completion. In 2011, this measure exceeded the corresponding value in 2005 by 1.5 percentage points for the whole population. The corresponding change in the group of non-employed is 2.8 percentage points higher, which presumably reflects the substantial modification in the field of unemployment insurance and benefit payments.

Chart 12. Risk of poverty and inequality in Germany





The risk of poverty or social exclusion of both non-employed persons and the population as a whole is still below the euro area average (2011). However, the risk of poverty or social exclusion of the population in Germany (19.9%) is higher than in many other countries, such as Finland (17.9%), Austria (16.9%) and the Netherlands (15.7%). Also, inequality, measured by the Gini index (Eurostat), experienced an increase after 2005. Inequality in Germany in 2011 (0.29) was under the EU average (0.31) but higher than in countries such as Belgium, the Netherlands, Austria and Finland (for all these countries around 0.26). The ranking of Germany as to inequality was very different in 2005, when the German Gini-index (0.26) was on the same inequality level as Finland and Austria and even lower than the respective values for Belgium (0.28) and the Netherlands (0.27). Of course, the labour market reforms are not necessarily the only factor accounting for the negative development of poverty and inequality. However, the change of the institutional setting of the labour market – in particular the promotion of atypical employment and the change in the unemployment benefit scheme in a more restrictive direction – may have had a significant impact.

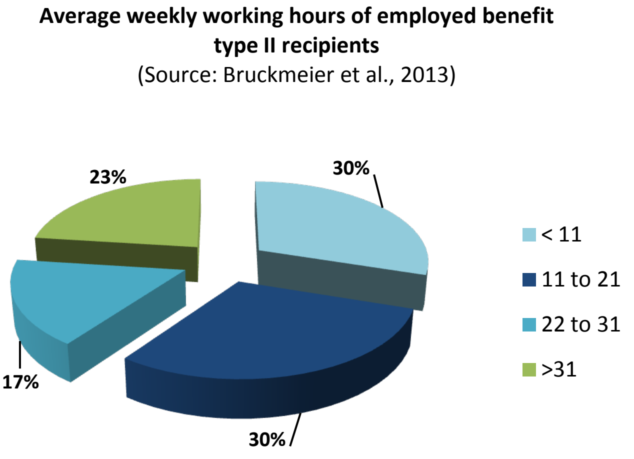
The working poor

Are the ‘working poor’ a current phenomenon on the German labour market? The Eurostat measure ‘Risk of poverty at work’ provides evidence for its presence in Germany. The risk of poverty at work in Germany (7.0%) exceeds the euro area average. Only a few countries display higher values and the difference is substantial relative to the Netherlands and Austria (4.5% each), Belgium (3.2%) and in particular Finland (2.0%).

Also, the number of persons with a second job has increased enormously since 2003, the year of the introduction of mini-jobs. By 2012, the number of persons with a second job had more than doubled compared with 2005. An increasing number of persons with a second job is also observable in the euro area, but at a very different intensity than in Germany. For example, the growth rate in the number of employees with a second job from 2003 to 2012 equals roughly 37% in the euro area, 36% in Finland, 25% in both Italy and France. However, the excessive increase in employees with a second job in Germany does not necessarily provide evidence for ‘working poor’, since, for example, as addressed previously, the mini-job instrument also enables a tax-free income gain in addition to regular employment.

By contrast it is notable that among the 4.5 million benefit type II recipients in April 2012, 1.3 million were in employment. This means that 1.3 million employed persons are dependent on transfer payments from the state despite being employed. The weekly working time of these employed benefit type II recipients is presented in Chart 13. According to this, the majority (60%) of employed benefit type II recipients works less than 21 hours per week and their lack of sufficient financial means is thus presumably coupled with a too low weekly working time. However, a substantial share of employed benefit type II recipients, namely 23%, work at least 31 hours per week (Bruckmeier et al., 2013).

Chart 13. Average weekly working time of employed benefit type II recipients

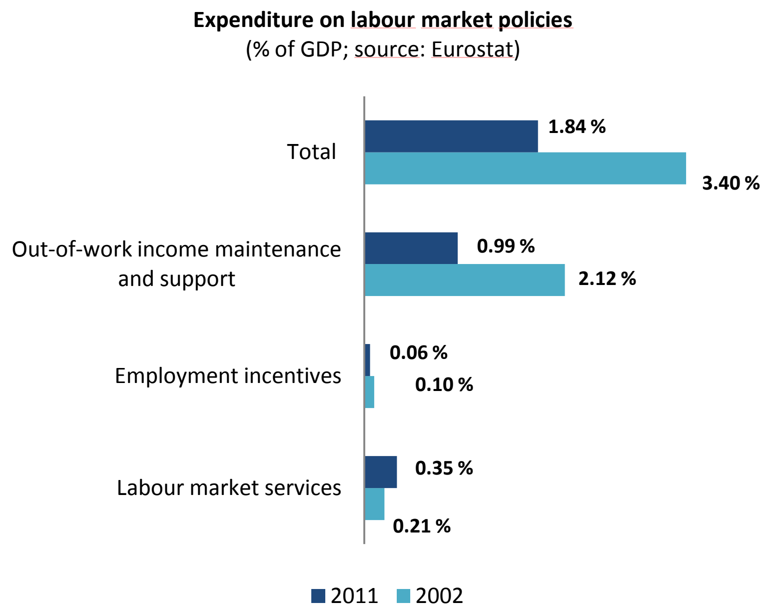


Nevertheless, the average hourly gross wage of these employed benefit II recipients (EUR 6.20) suggests the presence of working poor in Germany. By contrast, the average wages of regular employees is EUR 16.76 (western Germany) and EUR 13.54 (eastern Germany) (Bruckmeier et al., 2013).

Fiscal sustainability

In light of this presence of income subvention of low-wage incomes, it is necessary to ask if the German ‘job miracle’ is sustainable in fiscal terms. A comparison of the spending on labour market policies in 2002 and 2011 (Chart 14) does, however, demonstrate that a strong decrease in the total spending on labour market policies is perceptible.

Chart 14. Expenditures on labour market policies in Germany



This decrease has been realized especially via a reduction in expenditure on out-of-work income maintenance and support, i.e. unemployment benefits. However, the decrease in spending on these measures has also been favoured by the strong decrease in unemployment. Nevertheless, Germany's expenditure on labour market policies is among the lowest in the euro area.

3.3 The German 'job miracle' – in conclusion

This chapter has demonstrated that the German labour market has undergone a substantial change in the past decade from a former symbol of inflexibility and poor labour market performance to a labour market with favourable overall labour outcomes and institutions that are considered a possible role model for many other countries. The following structural changes are discernible. Unemployment and long-term unemployment decreased substantially, while labour force participation increased. The average unemployment duration is shorter after the reforms and matching efficiency improved significantly. Moreover, the post-reform German labour market displays signs of increased employment creation in upswings and stronger resilience of employment in recessions. A further relevant observation is a phase of wage restraint after implementation of the reform, discernible among other things by means of the moderate development of unit labour costs since 2003. This is in line with the prediction of economic theory regarding reservation wages (Diamond, Mortensen and Pissarides), which states that a reduction in unemployment benefits, as implemented in the German labour market reforms, exerts a negative effect on wages. In practice, this observation can be attributed to a weakened negotiating position for labour unions in the aftermath of the reforms, due to workers' enhanced fear of social decline in case of unemployment. The maintenance of employment appears to have become a more relevant goal for employed insiders than increasing wages.

Moreover, the resilience of the German labour market in the Great Recession is substantially responsible for its overall favourable condition today. During the financial crisis, Germany faced a vast drop in GDP, whereas employment hardly changed. This is due to the high degree of internal flexibility in the German labour market: instead of dismissing workers, individual working hours were drastically reduced and even hourly productivity declined substantially. The following five key factors account for this resilience in the Great Recession. First, the strong use of internal flexibility measures. Second, the strong cooperation between the social partners. Third, the willingness of firms to keep their workforce stable, potentially motivated by the wage restraint before the crisis, reluctance to hire in the pre-crisis upswing or a perceived shortage of skilled labour. Lastly, the favourable condition of the firms most severely affected by the GDP shock was significant, as was the sound overall state of the German economy before the Great Recession set in.

However, the German 'job miracle' also has a reverse side, as there have also been more negative developments discernible in recent times. To begin with, non-regular employment is now a fact of life in Germany. In particular, the share of part-time employment has substantially increased since the reforms. Also, mini-jobs scarcely serve as a bridging function into regular employment for women, rather hindering their regular employment opportunities. Poverty and inequality are on the increase in Germany. In particular, the share of employees with a second job has notably increased since the labour market reforms. However, the most problematic development is the presence on the labour market of the working poor. A substantial number of employees require state support in addition to their earned income in order to make ends meet. Some of these employed benefit type II recipients have working hours close to or even at full-time level with a substantially lower wage than average. Nonetheless, in fiscal terms, the German 'job miracle' is sustainable: overall expenditure on labour market policies is notably lower since the reforms.

4 Country Comparison: Labour Market Reforms in the Euro Area

This chapter compares the labour market reforms in France, Italy and Spain in the recent crisis with the labour market reforms in Germany from 2003 to 2005. Section 4.1 gives an overview of the labour market situation in the comparison countries in the recent crisis. Section 4.2 presents a cross-country comparison of the most relevant labour market reform steps in France, Italy and Spain with the German labour market reforms from 2003 to 2005. Section 4.3 presents conclusions from the cross-country comparison.

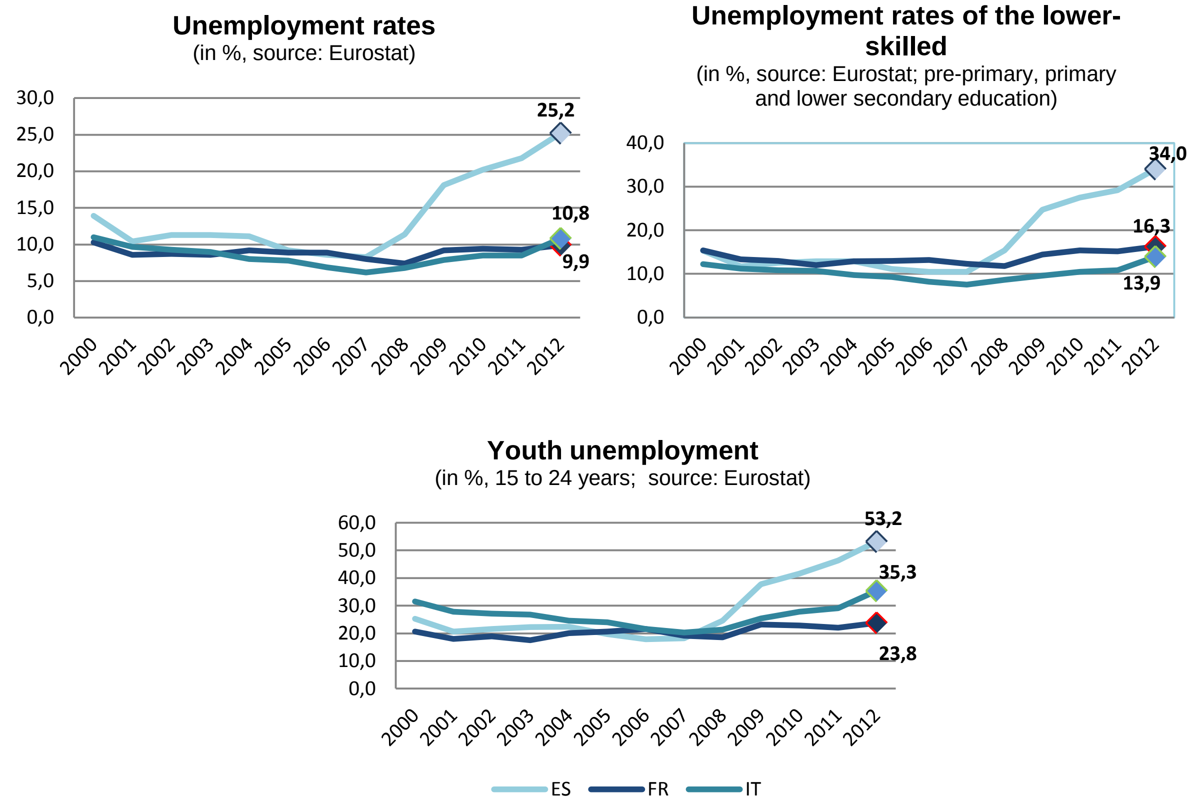
4.1 The labour markets of France, Italy and Spain in the recent crisis

This section outlines the initial situation on the French, Italian and Spanish labour markets. The comparison countries face two common, major problems, which are illustrated in Chart 15. First, their very high and partly excessive unemployment rates. Second, their excessive unemployment rates for both youth and the lower-skilled. These groups apparently carry an over-proportional share of the labour adjustment to the economic situation. They are particularly affected by an inherent labour market dualism, with strongly protected insiders and high entry barriers for outsiders.

France

Labour market duality in France is closely linked to high labour taxes and minimum labour costs. Also, the labour market is rigid. Youth and low-skilled workers face limited job opportunities and fixed-term contracts are particularly prominent among this group.

Chart 15. Unemployment rates in Spain, France and Italy



Disincentives to work at older ages are pronounced in France: The retirement age is notably low, as is the minimum contribution period for full pensions, while the unemployment benefit scheme can be characterized as generous for older unemployed. The consequences are low return rates of older unemployed into work. High real wages hinder firms' capacities for innovation and maintenance of international competitiveness (Cheng et al., 2013; OECD_a, 2013; OECD_b, 2013). The European Commission states that the real compensation of employees has risen more rapidly than productivity. Moreover, France has the highest relative minimum wage as opposed to the median wage among all EU countries, with corresponding negative employment effects. Temporary contracts represent the main route of labour market entry for young workers in France and scarcely serve as a bridge into regular employment – only 14% of all fixed-term contracts are converted into permanent contracts. Another negative feature is the lack of both internal and external flexibility in French firms (European Commission, 2013).

Italy

Italy, too, has a strongly divided labour market. Entry barriers for outsiders are high and employment can be precarious, particularly for young people. The outcomes of the Italian education system are problematic. The training content of apprenticeships are insufficient, and the transition from an apprenticeship to a permanent contracts is inefficient. Temporary contracts are subject to abuse and generate disincentives for investment in human capital. By contrast, permanent contracts are highly protected. They are characterized by high dismissal costs, and legal processes after dismissals can be costly. Moreover, the costs of collective dismissals in Italy are the highest within the OECD. The degree of internal flexibility within firms is low. Wage and productivity development are not sufficiently linked. The share of firm-level contracts is low and the tax system puts a high tax wedge on incomes. Italy's social safety net is fragmented, complex and uneven, contributing to the inefficient reallocation of workers. Employment services are fragmented with respect to region, and active labour market policies are often ineffective and poorly funded. Labour participation rates for both women and young people are very low (Lusinyan and Muir, 2013).

Spain

As illustrated in Chart 15, Spain faces the highest unemployment rates within the comparison countries. Unemployment is excessively high, particularly among young people and the lower-skilled.

Labour market dualism in Spain has its origin in strict employment protection for permanent employees and a large share of temporary contracts among newly hired workers. Spain has the highest share of temporary workers in the OECD and also very high dismissal costs for permanent workers (Wölfl and Mora-Sanguinetti, 2011). Moreover, wages can scarcely respond to unemployment due to the design of collective agreements. The severe lack of internal flexibility within firms in Spain is reflected in, among other things, the rise in individual working time since 2007, in contrast to a decline in most other OECD countries. Problematic is also the automatic extension of collective wage agreements to the entire province/industry, very limited opt-out clauses, and substantial wage indexation (IMF, 2012).

Comparison of the initial situation in Germany and the comparison countries

When comparing the initial situation in Germany and the comparison countries, the following observations can be made. First, as outlined previously, Germany faced marked labour market problems. These problems were work disincentives due to the design of the unemployment benefit scheme and the tax system, inefficient and unsystematic re-integration measures, as well as a regional unemployment problem in eastern Germany after reunification. Thus, Germany faced considerable structural problems before the implementation of reform. However, the German reforms from 2003 to 2005 were not implemented amid a severe economic crisis, in contrast to the labour market reforms in the comparison countries.

Also, the condition of the labour markets in Germany and the comparison countries before reform implementation appears to differ substantially with regards to flexibility within firms. The German labour market had been gradually deregulated since reunification (see e.g. Feil et al., 2008). Also, internal flexibility measures had already been established since the mid-1980s (Eurofond, 1998). By contrast, firms in France, Italy and Spain had hardly any means of external or internal flexibility at their disposal before the reforms.

A further important difference is that labour market dualism was apparently not a problem in Germany before the labour market reforms, whereas the divide between permanent and fixed-term contracts represented a major challenge for the comparison countries.

4.2 Cross-country comparison

This section presents a comparison of the German labour market reforms from 2003 to 2005 with the most relevant reform steps implemented in France, Italy and Spain in the recent crisis. For this purpose, the major reform steps implemented in the comparison countries are assessed and categorized into four possible categories. Three of these categories represent the pillars of the German labour market reforms, namely *reform of the employment services, activation of the unemployed* and *labour market deregulation*. In addition, an extra category is introduced in order to capture reform steps not comparably implemented in Germany.

4.2.1 Reform of the employment services

Table 5 provides an overview of the reform of the employment services. As already outlined, this was an important pillar of the German labour market reforms. Notable reform steps were implemented in order to improve the quality and cost-efficiency of labour market services. For example, the formerly strongly hierarchical employment offices were transformed into more customer-oriented ‘job centres’. Quasi-market forces were established in order to improve the quality of the public services, such as the introduction of voucher systems, which aimed at creating a competitive environment with both public and private training and placement service providers. In addition, the public employment services were given the possibility of outsourcing. A highly standardized profiling process of the unemployed was introduced to improve the allocation of resources and re-integration into the labour-market. Finally, a strong evaluation element was introduced to enable assessment of the reforms' success and their continuous optimization.

Table 5. Comparison of employment services reforms

Germany	France	Italy	Spain
Transformation of the strongly hierarchical employment offices into customer-oriented 'job centres' *Quasi-market mechanisms with both public and private service providers via voucher systems* *Possibility of outsourcing certain employment services* *Establishing a highly standardized profiling process* *Inclusion of a strong evaluation element in the reforms*	*none*	*Measures for alleviating regional fragmentation and efficiency differences in the employment services* *Imposition of a minimum level of employment services offered per region* *Some liberalization of placement services*	*Personalized back-to-work paths for the unemployed* *Temping agencies used as employment agencies*

In comparison, the reform attempts of France, Italy and Spain in this category appear to be less pronounced. However, the relevance of reform of the employment services varies substantially from country to country.

Italy implemented reforms to alleviate the inherent regional fragmentation and efficiency differences in employment services. A minimum level of employment services offered per region was imposed and placement services to an extent liberalized (Lusinyan and Muir, 2013).

Spain established personalized back-to-work paths for every unemployed person – a reform comparable to the personal integration agreement introduced in Germany. Also, temporary employment agencies were permitted to act as employment agencies in order to reduce average search times for the unemployed and to improve matching (Bentolila et al., 2012; Ministry of Economy and Competitiveness, 2012). In recent times, France has not reformed its employment services.

4.2.2 Activation of the unemployed

This section compares the elements of activation policies in Germany, on one hand, and France, Italy and Spain, on the other (Table 6). Sub-categories for the comparison are introduced based on the German activation strategy: namely 'reform of the benefit scheme', 'subsidy payments', 'atypical forms of employment' and 'sanction elements'.

Reform of the benefit scheme

As already elaborated, the unemployment benefit scheme was drastically reformed in Germany. This presumably represents the most comprehensive change of the Hartz reforms. The formerly relatively generous system of unemployment benefits, unemployment assistance and social assistance was transformed into a more restrictive two-pillar system. This meant the unification of unemployment and social assistance into just the means-tested benefit scheme II, roughly at the income level of the former social assistance. Only disabled and ill persons are exempt from the severe activation policies and job-search obligations.

In Spain, the fragmented unemployment insurance was reformed. The minimum age for the unemployment protection programme was raised from 52 to 55 years. Some benefits for longer-term unemployed were reduced from 60% to 50% of previous income (Garrigues_c, 2012).

Italy, too, changed its benefit scheme. In particular, distortions and abuses of the existing legislation were to be restricted, while implementing a more expansive and equitable protection scheme in case of involuntary job loss. The most relevant reform step is the introduction of AspI ('Assicurazione Sociale per l'Impiego') – the social insurance for employment. The aim of this new social insurance was to simplify the complex, unequal and exclusive unemployment insurance system previously in place. An upper limit was introduced for benefit payments, at EUR 1,119.32. Furthermore, benefit payments were rendered duration-dependent, as they decrease by 15% after six months and by a further 15% after 12 months (Clauwaert and Schönmann, 2012).

France abolished the job-search exemption for older unemployed over 55 years of age (OECD_b, 2013). Moreover, the possibility of accumulating unclaimed rights to unemployment benefits was introduced. This reform step was aimed at promoting early return into employment while increasing employee protection (Libération, 2013).

Subsidy payments

As explained previously, the German labour market reforms introduced various forms of subsidy payments in order to facilitate the integration of hard-to-place job-seekers in the labour market. Start-up subsidies (‘Ich-AG’) were designed to promote self-employment of the unemployed. For employers hiring a hard-to-place worker, integration subsidies were provided as compensation for the worker’s lower productivity. The instrument of wage protection was put forward to facilitate the re-integration of older job-seekers.

The activation measure ‘subsidy payments’ was also strongly represented in the activation strategy of the comparison countries.

France implemented ‘emplois d’avenir’, a measure intended to combat unemployment among lower-skilled young people. These subsidized employment contracts are reserved for persons from 16 to 25 years of age without formal qualifications in problematic or rural areas. The state subvention generally equals 75% of the minimum wage, which corresponds to EUR 1,069.25 for a full-time post. It is paid for one to three years, and these jobs are primarily created in non-profit sectors. Moreover, an ‘inter-generational contract’ was introduced in order to provide incentives for the employment of older people (aged at least 57 years) and young people (under 26 years). Its maximum duration is three years and firms with less than 50 employees are entitled to the subvention, which equals EUR 2,000 per year.

Table 6. Comparison of the reforms to the benefit scheme and the introduction of subsidy payments

Germany	France	Italy	Spain
Reform of the benefit scheme			
Shorter entitlement periods *Lower benefit payments* *Benefit payments strictly conditional on job-search activities* *Transformation of the previous three-pillar social safety net into a two-pillar scheme (Elimination of unemployment assistance)*	*Accumulation of un-employment benefits* *Abolition of job-search exemption for older unemployed*	*Reform of the strongly fragmented safety net towards a more uniform scheme (e.g. Aspl)* *Introduction of a ceiling for unemployment benefits* *Duration-dependent unemployment benefits*	*Partial reform of unemployment insurance* *Increase of the minimum age for unemployment protection* *Reduction of some long-term unemployment benefits*
Subsidy payments			
Start-up subsidies for the unemployed *Integration subsidies for hiring a hard-to-place worker* *Wage protection for older employees*	*'Emplois d'avenir': subsidized youth employment* *Inter-generational contract: tax incentives for employment of younger and older workers* *Social security incentives for permanent employment of young persons*	*Tax incentives for hiring young workers, apprentices and older workers* *Special company type for young entrepreneurs with simplified requirements*	*Tax and social security contribution incentives for start-ups – in particular for the unemployed* *'Prepara Plan': a vocational retraining programme for registered unemployed with family obligations* *Contract for training and learning: training and work experience for young persons*

If a collective agreement exists, larger firms (up to 300 employees) are also entitled to the subvention (Lacan, 2013; Direction de l'information légale et administrative, 2013). Furthermore, the French reforms was aimed at fostering permanent employment of young people by introducing exemption for firms from social security contributions for three months in turn for hiring young people on open-ended contracts (Lacan, 2013).

In Italy, too, tax incentives for hiring young workers and apprentices as well as older workers were introduced. Moreover, a special company type with simplified requirements was established with the aim of promoting entrepreneurship among the young (Clauwaert and Schönmann, 2012; Lusinyan and Muir, 2013).

Spain also implemented start-up subsidies, in the form of tax reductions. The tax exemption is particularly pronounced for unemployed persons. Additionally, newly self-employed person under 30 years of age is granted exemption (worth EUR 50) from social security contributions for the first 6 months of self-employment (Stability Programme Update Kingdom of Spain 2013–2016, 2013). Furthermore, the ‘Prepara Plan’ was introduced. The target group for this vocational retraining programme is people registered unemployed with family obligations. Benefit recipients receive financial assistance equal to 75% of the public income indicator for a maximum duration of 6 months. The programme will continue until the unemployment rate falls below 20% (Garrigues_a, 2012; La Moncloa, 2013). Moreover, the contract for training and learning should provide young persons (up to 30 years) with work experience and training, and in particular alleviate the impact of early school dropout (Ministry of Economy and Competitiveness, 2012).

Atypical employment and sanction elements

As described in the chapter on the German labour market reforms, a crucial part of the German activation strategy was the introduction of atypical forms of employment and sanction elements. Atypical forms of employment were mini- and midi-jobs intended to serve as a bridge out of unemployment and increase labour participation. The sanction elements are substantial and put a strong focus on job-search activities by the unemployed. Job-seekers are generally obliged to accept any suitable job offer and to strictly follow a written ‘integration agreement’. The sanction itself is the temporary cutting of benefit payments. Mandatory participation in training measures and compulsory one-euro jobs were introduced as a tool for verifying job-seekers’ availability for potential job offers. In the comparison countries, no substantial measures in the field of atypical employment and sanction elements were introduced.

Table 7. Atypical employment and sanction elements

Germany
Atypical forms of employment ♦ *Mini-jobs* ♦ *Midi-jobs* ***Sanction elements*** ♦ *Cut of benefit payments* ♦ *Obligation to accept any suitable job offer and to strictly follow a written integration agreement* ♦ *Verification of the availability for job offers via mandatory participation in training measures and 'one-euro jobs'*

4.2.3 Labour market deregulation

This section contrasts the labour market deregulation in the German labour market reforms with the deregulation implemented in the comparison countries (Table 8).

As already outlined, Germany did not implement an overall deregulation strategy but merely deregulated certain segments of the labour market. Temporary agency work was strongly deregulated by allowing repeated renewals of fixed-term contracts in this category, re-employment, synchronization as well as an unlimited assignment duration. Deregulation measures were also introduced concerning dismissals and fixed-term contracts. For example, the maximum firm size for exemption from dismissal protection was increased from 5 to 10 employees. Also, the use of fixed-term contracts without the need to provide justification was permitted for recently established firms. The minimum age for which a repeated renewal of fixed-term contracts is legitimate was lowered from 58 to 52 years.

The deregulation strategy in the comparison countries was very different to the German approach. Instead of implementing exceptions to the existing regulation, deregulation in the comparison countries aimed at providing the firms with more external and internal flexibility. These reform steps are presented below.

External flexibility

In France, Italy and Spain, reform steps to provide the firms with external flexibility were implemented. This deregulation took place in the field of dismissal regulations and collective agreements.

Dismissal regulation

The French labour market reform facilitated dismissal procedures by lowering the regulations for the generation of social plans as well as legal challenges thereto. This measure was aimed at providing firms with both a gain in time and legal security. Accordingly, two possible routes for social plans were established: either via a collective agreement, approved by the public authorities within 8 days, or via an unilateral agreement which requires administrative approval within 21 days (Le Figaro, 2013). Also, the period for contesting the respective decision has been lowered from 12 to 3 months (Libération, 2013).

Both the Spanish and Italian labour market reforms were strongly focused on alleviating the problems of costly and excessive court procedures and compensation payments. In Italy, out-of-court settlement was encouraged and processes for dismissal litigation accelerated (Lusinyan and Muir, 2013). Moreover, reinstatement claims were restricted. The Italian labour market reforms also aimed at harmonizing the regulations for collective dismissals with those for individual dismissals (Lusinyan and Muir, 2013). The Spanish reforms redefined the term 'dismissal for economic reasons'. Additionally, firms are no longer obliged to deliver objective proof of economic stress, but merely some evidence for the claim that the dismissal decision was needed to maintain the firm's current or future market competitiveness. Moreover, the severance pay for objective dismissals was reduced from 45 to 20 days' wages per year of seniority (Wölfl and Mora-Sanguinetti, 2011). Severance pay for unfair dismissals was also unified and limited (Jimeno et al., 2012), while the notice period for objective dismissals was reduced (Wölfl and Mora-Sanguinetti, 2011). Also, 'procedural wages' – wages paid during court proceedings – were scrapped (De Guindos, 2012). Moreover, the approval of the public authorities is no longer required for collective dismissals (Jimeno et al., 2012). The Spanish labour market reforms also introduced the possibility of dismissals on objective grounds in public administration (Garrigues_b, 2012). A reform step towards more external flexibility for Spanish firms was the introduction of a new type of permanent contract for small firms with less than 50 employees that entails a one year trial period. They are promoted via a tax bill reduction of EUR 3,000 euro when hiring the first worker on this type of contract, including special incentives for hiring previously unemployed persons (Ministry of Economy and Competitiveness, 2012).

Collective agreements

The labour market reforms in Spain and Italy implemented changes in the field of collective agreements. In Italy, an agreement was made to further the decentralization of wage bargaining. Moreover, tax incentives were provided for productivity-based contracts (Lusinyan and Muir, 2013).

The Spanish labour market reforms established the general priority of firm-level collective agreements. Also, opt-out clauses were introduced to allow firms to exit from higher-level collective agreements in order to better adapt to market conditions. Furthermore, 'ultra-activity' – the unrestricted extension of collective agreements beyond their expiration in case no new agreement is made – was abrogated and the maximum validity of an agreement beyond its expiration was set at two years (Ministry of Economy and Competitiveness, 2012).

No substantial changes concerning collective agreements were implemented in France.

Internal flexibility measures

As outlined previously, the internal flexibility measures were already at firms' disposal before the Hartz reforms were implemented, whereas before the recent labour market reforms in France, Italy and Spain these measures seemed to be hardly available to firms. The German labour market reforms did not introduce any additional means of internal flexibility within firms, whereas internal flexibility played an important role in the comparison countries.

In Italy, firms were granted the possibility of extending the contracted period of fixed-term contracts in order to complete the activities captured in the contract and meet the firms' organizational needs. The possible extension period equals 20 to 30 days for contracts shorter than 6 months and 30 to 50 days for longer contracts (Clauwaert and Schönmann, 2012). Moreover, the wage guarantee funds were expanded (Lusinyan and Muir, 2013).

The French labour market reforms implemented several measures aimed at increasing firms' internal flexibility in case of economic problems. Firms can adjust the salary and or working time in return for job security. Firms' entitlement to these measures depends on the approval of labour unions representing at least 50% of the employees. The maximum duration for this practice is two years (Lacan, 2013). Uncooperative employees can be dismissed for economic reasons (Libération, 2013). Furthermore, regulation of mobility agreements was made more restrictive (Libération, 2013; Le Figaro, 2013).

Table 8. Labour market deregulation

Germany	France	Italy	Spain
Temporary agency work:		***External flexibility***	
		Dismissal regulation	
Repeated fixed-term contracts *Re-employment* *Synchronization* *Unlimited assignments* ***Dismissals and fixed-term contracts:*** *Rise of the firm size exempt from dismissal protection to 10 employees* *Use of fixed-term contracts for recently established firms*	*Social plans: facilitation of their regulation and limitation of legal challenges*	*Encouragement of out-of-court settlement* *Restriction on reinstatement claims* *Harmonization of the rules for collective dismissals with those for individual dismissals*	*Broadened definition of 'dismissal for economic reasons'* *Unification and limitation of severance pay* *Reduction of the notice period for dismissals* *Elimination of 'procedural wages'* *Abrogation of the approval of public authorities for collective dismissals* *Dismissals on objective grounds in public administration* *New type of permanent contracts for small firms, including a trial period*
		Collective Agreements	
Reduced minimum age for repeated fixed-term contracts to 52 years	*none*	*Promotion of the decentralization of wage bargaining* *Provision of tax incentives for productivity-based contracts*	*General priority of firm-level agreements* *Opt-out clauses from higher-level collective agreements* *Elimination of 'ultra-activity'*
		Internal flexibility	
	Decrease in salary and/or working time in turn for job security *More severe framework for mobility agreements*	*Extension of fixed-term contracts for organizational needs* *Expansion of wage guarantee funds*	*Adjustment of wages, working time, work schedule* *Possibility of temporary suspension of contracts*

The Spanish labour market reforms also established more flexible working conditions, allowing adaption to fluctuations in firms' activity. This includes the adjustment of salaries, working hours and work schedules. The suspension of employment contracts is a further temporary adjustment mechanism (Ministry of Economy and Competitiveness, 2012).

4.2.4 Reform steps not implemented in Germany

This section presents major reform steps implemented in France, Italy and Spain which are not observable in the German labour market reforms.

Measures tackling labour market dualism

Tackling their severe labour market dualism was a central aim of various reform steps in the comparison countries. Since Germany did not face a labour market duality before the labour market reforms, no measures in this area were implemented.

France implemented disincentives for fixed-term contracts in the form of increased social security contributions. The contribution rates were increased from the previous 4% for all contract types to 7% for contracts shorter than one month, 5.5% for contract durations from one to three months and 4.5% for remaining fixed-term contracts (Libération, 2013).

The Italian labour market reforms also imposed tax disincentives for fixed-term contracts. Moreover, disincentives for the repeated use of fixed-term contracts were imposed by enlarging the obligatory intermediate period from 10 to 60 days for contracts shorter than 6 months and from 20 to 90 days for longer fixed-term contracts. A general upper limit of 36 months was established for fixed-term contracts. After this period, a contract must be converted into a permanent contract, taking into account any work relationship with the same employer. Another reform step was the automatic conversion of fixed-term contracts lacking formal justification into permanent contracts. Affected employees receive subsequent compensation equal to 2.5 to 12 months of their previous salary (Clauwaert and Schönmann, 2012). Tax incentives were introduced for promoting apprentices. The firms' allowance for hiring new apprentices was made conditional on the conversion of past contracts into open-ended positions: For three years after the reforms at least 50% of apprentice contracts have to be converted into permanent contracts; after that, the rate of conversion must equal 30%. If a firm does not fulfil this criterion, only one additional apprentice can be hired. Firms with a firm size up to 10 employees are exempt from this regulation. Additionally, the generally applicable maximum ratio of apprentices to skilled workers was in generally raised to 3:2 (previously 1:1). Also, a minimum duration of six months was introduced for apprenticeships (Clauwaert and Schönmann, 2012).

The Spanish labour market reforms increased employee compensation upon the termination of a fixed-term contract from 8 to 12 days (Wölfl and Mora-Sanguinetti, 2011). For temporary employment on specific projects or services ('contratos de obra y servicio') an upper limit of three years was set (Wölfl and Mora-Sanguinetti, 2011).

Country-specific measures

This section presents measures established in the comparison countries which have only been implemented in the respective country. This type of reform step is discernible for France and Italy.

One of these measures is at the same time one of the most relevant reform steps implemented in France: the 'tax credit for competitiveness and employment' (CICE), which is available to all French firms. This provides financial support for firms in order to enhance their competitiveness and further, among other things, their activity in investment, innovation and recruitment. In 2013, the tax-credit amounts to 4%, and from 2014, 6% of the wage bill, with only wages up to 2.5 times the minimum wage taken into account (Le portail de l'Économie et des Finances, 2013). France also aimed at improving the dialogue between social partners by establishing employee representation on the supervisory board for firms with more than 10,000 employees worldwide, or 5,000 employees in France (Le Figaro, 2013). Furthermore, France aimed to foster training by introducing a 'personal account for education'. This measure entitles both unemployed and employees to 20 to 120 hours of education per year (Le Figaro, 2013). Moreover, any employee with at least two years of seniority in a firm with at least 300 employees is entitled to a temporary change of job type within the firm or the temporary change to another firm in order to be trained in a new field or to develop certain competences. After this phase, the employer is obliged to offer a comparable position as before the training period, whereas the employee is not obliged to return to the initial employer (Libération, 2013; Le Figaro, 2013). Moreover, the French reforms intensified the regulation of part-time work by establishing a general minimum working time of 24 hours per week and increasing overtime pay by 10% (Le Figaro, 2013).

The Italian labour market reforms were aimed at increasing female labour participation. For this reason, tax incentives for hiring women were introduced. In order to improve the compatibility of family and working life, baby-sitting vouchers were introduced. Also, protection mechanisms for women were established against the phenomenon of 'blank resignation letters' (Lusinyan and Muir, 2013).

4.3 Conclusion

This section summarizes the main conclusions concerning the comparison of the German labour market reforms with the recent reforms of the labour markets in France, Italy and Spain.

1. Different focus of the reform strategies

The comparison made clear that the focus of the labour market reforms in Germany was different from those in the comparison countries, despite some differences within this latter group. The reform of the employment services was a substantial part of the German reforms. By contrast, it only played a minor role in Italy and Spain and was not addressed at all in France. The activation of the unemployed was the most relevant and most pronounced pillar of the German labour market reforms and also an important element of the reforms in the comparison countries, if far less relevantly than in the Hartz reforms. The opposite holds for labour market deregulation. Even though notable reforms were implemented in Germany, no overall deregulation was implemented. However, labour market deregulation was a major pillar in France, Italy and Spain. The labour market reforms aimed at establishing both external and internal flexibility on the part of firms. Furthermore, measures not implemented in Germany predominantly addressed the labour market duality inherent in France, Italy and Spain.

Consequently, the labour market reforms in Germany focused on the activation of the unemployed, whereas the focus of the labour market reforms in the comparison countries was deregulation and the alleviation of labour market duality.

2. The different strategy focus reflects different initial problems

As emphasized in this chapter, the German labour market had been gradually deregulated since reunification. Moreover, internal flexibility measures were already at the disposal of firms before the reforms. By contrast, the unemployment benefit scheme in combination with the German tax system provided substantial disincentives for taking up employment. This initial situation is also reflected in the clear focus on the activation of the unemployed, whereas deregulation was less prominent in the reforms.

This observation also holds for the labour market reforms in the comparison countries. Firms had hardly any means of external or internal flexibility at their disposal. Moreover, the countries faced a substantial divide between permanent and fixed-term contracts. This is clearly reflected in the reforms' focus in these countries: deregulation and the alleviation of labour market duality.

3. The different reform strategies presumably reflect the countries' initial economic and political conditions

When considering the economic and political conditions in Germany and the comparison countries, the following facts stand out. Before 2003, Germany certainly faced marked structural problems with persistently high unemployment. However, the condition of France, Italy and Spain before the labour market reforms can be characterized as a lot more severe than the problems inherent in Germany before the Hartz reforms. These countries were in a severe economic crisis and faced excessive unemployment. This applies in particular to Spain. These different degrees of economic and political problems before the reforms may have also significantly shaped the design of the labour market reforms themselves. Being confronted with excessive unemployment, activation policies might have been perceived as both less effective and socially more painful in the comparison countries. This could have possibly favoured deregulation as opposed to activation in France, Italy and Spain.

5 Conclusion

What can be learned from the German experience? The German labour market reforms were both profound and comprehensive. In retrospect, it becomes apparent that the reformers from 2003 to 2005 showed foresight, courage and responsibility by implementing these bold reforms. The decision for the labour market reforms and for restoring Germany‘s competitiveness before an actual severe economic crisis made them necessary was voluntary, suggesting that Germany was among the few countries who took the Lisbon strategy for 2010 seriously.

The reformers of the last decade kept their promise: the reforms brought Germany back to the top in prosperity and the labour market. The reform-induced structural change combined with the strong cooperation between the social partners made the German labour market internationally highly competitive by keeping unit labour costs at a moderate level.

In addition to these factors, the strong internal flexibility of German firms made the labour market highly resilient against temporary fluctuations in economic activity – not even the Great Recession induced a substantial increase in the unemployment rate in Germany. Thus, the overall performance of the German labour market is indeed exceptional and has insights to offer in the context of sustainable economic performance.

This study also demonstrated that Germany‘s transition had a certain cost. The reforms had a substantial political impact. Not only did Schröder lose his chancellorship, the party‘s former main supporters, the working class, has considered the reforms a ‘betrayal’ towards them, contributing to record-low votes for the Social Democrats and a change in the political map of Germany.

It appears that the success of the many – the labour market in its entirety – came to an extent at the cost of the few, those at the lower-end of the income scale who carried a disproportionate burden in Germany’s transition to new-found competitiveness. The reforms seem to have contributed to the enlargement of the social divide and reshaped the general significance of work in the country.

From this perspective, it remains to be seen if the reforms will also bring Germany to the top in the field of welfare. Given the outstanding state of the overall economy, especially compared with many other European countries, it is striking how many people live in fear of social decline and close to or even at poverty level.

Drawing the conclusion that the labour market reforms were a mistake is nevertheless wrong. The developments in France, Italy and Spain emphasize what could have been a potential different path for Germany: high protection for the few employed insiders and continuous unemployment, lack of perspective and hardship for the unprotected rest. This would surely not have been a better alternative. The reforms in Germany were clearly an overall success, and given their immense magnitude – representing a substantial change of the German economy and its institutions – it is not surprising that some of the implemented measures exerted unexpected and distortive effects. It could be argued that a mistake in Germany was to refrain from a profound continuous optimization of the labour market reforms – despite a high level of research and available information on their effects.

Thus, for the development of the labour market to be deserving of the term ‘miracle’ also with regards to welfare and for it to be perceptible also at the lower end of the income scale, corrections would have to be implemented, as it has become clearer that the reduction of unemployment is of a structural nature. These changes would not necessarily have to be vast but should move the German labour market away from the American model by, for instance, controlling the excessive use of temporary agency work. Also, a re-design of the tax system in a more egalitarian direction would be helpful in furthering more independent employment paths for women.

All in all, even though an important insight from the German experience is that the success of the labour market has entailed sacrifices, that is not to say that other countries should refrain from rendering their labour markets more efficient and competitive. On the contrary, Germany’s example gives a clear indication that it is possible to solve the problem of unemployment and restore competitiveness via structural reforms.

Thus, Germany’s experiences can serve as a source of inspiration for increasing the overall performance of the labour market while at the same time avoiding the excess costs some groups have carried in Germany.

References

Arbeitsagentur (2009): 'Dauer des Anspruchs', http://www.arbeitsagentur.de/nn_25638/Navigation/zentral/Buerger/Arbeitslos/Alg/Dauer-Anspruch/Dauer-Nav.html.

Arent, S. and W. Nagl (2011): 'Löhne und Arbeitslosengeld: Wie haben sich die HARTZ-Reformen auf die Lohnentwicklung ausgewirkt?', ifo Dresden berichtet, 3/2011.

Astheimer, S. et al. (2013): '10 Jahre danach: Die Agenda 2010 – eine Bilanz', Frankfurter Allgemeine Zeitung, 13 March 2013.

Bentolila et al. (2012): 'Europe's Labour Markets And The Crisis', CESifo DICE Report, 2/2012.

Bonin, H. (2005): 'Tarifpolitik, Entgeltflexibilität und Beschäftigung in Ostdeutschland', Zeitschrift für Arbeitsmarkt Forschung, vol. 38(2/3).

Bräuninger, M. et al. (2012): '10 Jahre Hartz-Reformen', HWWI Policy Paper 73.

Bruckmeier, K. et al (2013): 'Aufstocker im SGB II: Steinig und lang – der Weg aus dem Leistungsbezug', IAB Kurzbericht, 2013(14).

Brussig, M. et al. (2006): 'Zielstellung, Förderstrukturen und Effekte der 'Entgeltsicherung': Erfahrungen mit einem Kombilohn für ältere Arbeitnehmerinnen und Arbeitnehmer', Zeitschrift für Arbeitsmarkt Forschung, Jg. 39 (3/4).

Bundesagentur (2012): 'Arbeitslosengeld II / Sozialgeld', http://www.arbeitsagentur.de/Navigation/zentral/Buerger/Arbeitslos/Grundsicherung/Alg-II-Sozialgeld/Alg-II-Sozialgeld-Nav.html.

Burda, M.C. and J. Hunt (2011): 'What Explains the German Labour Market Miracle in the Great Recession?', Brookings Papers on Economic Activity, 42(1).

Cheng, K.C. et al. (2013): 'France: Selected Issues', IMF Country Report No. 13/3.

Clauwaert, S. / I. Schönmann (2012): 'The crisis and national labour law reforms: a mapping exercise', ETUI Working Paper 2012.04.

De Guindos, L. (2012): 'The Spanish Economy – Facts that Cannot Be Overlooked', http://www.thespanisheconomy.com/SiteCollectionDocuments/en-gb/Economic%20Outlook/The%20Spanish%20Economy%20facts%20that%20cannot%20be%20overlooked.pdf.

Deutscher Bundestag (2003): Plenarprotokoll 15/32, March 14 2003.

Direction de l'information légale et administrative (2013): 'Emplois d'avenir: mise en place au 1er novembre 2012', posted 2 November 2012, http://www.service-public.fr/actualites/002507.html.

Eichhorst, W. and P. Marx (2009): 'Reforming German Labour Market Institutions: A Dual Path to Flexibility', IZA Discussion Paper, No. 4100.

Eurofound (1998): Provisions on working time accounts in collective agreements; http://www.eurofound.europa.eu/eiro/1998/03/feature/de9803255f.htm.

European Commission (2013): 'Macroeconomic Imbalances – France 2013', European Commission Occasional Papers, No.136.

Feil, M. et al. (2008): 'Arbeitsmarkt- und Beschäftigungspolitik nach der Wiedervereinigung', Zeitschrift für Sozialreform, Vol. 54(2).

Fuchs, J. et al. (2010): 'Prognose 2010/ 2011: Der Arbeitsmarkt schließt an den vorherigen Aufschwung an', IAB Kurzbericht 18/ 2010.

Garrigues_a (2012): 'Royal Decree-law 23/ 2012, of August 24 2012, Extending the Vocational Retraining Programme for Individuals Exhausting Their Unemployment Benefit

('Prepara Plan')', Garrigues Updates Labour 12-2012. http://www.garrigues.com/en/Publicaciones/Novedades/Documents/Updates-Labour-12-2012.pdf.

Garrigues_b (2012): 'Law 3/2012, of July 6, 2012, On Urgent Measures to Reform the Labour Market', Garrigues Updates Labour 9-2012, http://www.garrigues.com/en/Publicaciones/Novedades/Documents/Updates-Labour-9-2012.pdf.

Garrigues_c (2012): 'Law 3/2012, of July 6, 2012, On Urgent Measures to Reform the Labour Market', Garrigues Updates Labour 9-2012, http://www.garrigues.com/en/Publicaciones/Novedades/Documents/Updates-Labour-9-2012.pdf.

Gartner, H. and S. Klinger (2010): 'Verbesserte Institutionen für den Arbeitsmarkt in der Wirtschaftskrise', Wirtschaftsdienst (11), 90. Jahrgang, November 2010.

Heilmann, D. et al. (2010): 'Teure Wiedervereinigung: Das Billionen-Projekt 'Blühende Landschaften'', Handelsblatt, October 10 2010.

IMF (2012): Spain 2012 Article IV Consultation, IMF Country Report No. 12/202.

Jacobi, L. and J. Kluve (2010): 'Before and After the Hartz Reforms: The Performance of Active Labour Market Policy in Germany', Zeitschrift für Arbeitsmarkt Forschung, 1/2007.

Jimeno, J.F. et al. (2012): 'Reforming an insider-outsider labour market: the Spanish experience', Presentation at Banque de France Labour market Conference, 15. November 2012.

Klinger, S. and T. Rothe (2010): 'The impact of labour market reforms and economic performance on the matching of short-term and long-term unemployed', IAB Discussion Paper, 13/2010.

Klinger, S. and E. Weber (2012): 'Decomposing Beveridge curve dynamics by correlated unobserved components', IAB-Discussion Paper 28/ 2012.

Klinger, S. et al. (2013): 'Makroökonomische Perspektive auf die Hartz-Reformen: Die Vorteile überwiegen', IAB Kurzbericht, 11/2013.

Krugman (2009): 'Free to Lose', New York Times, Nov 12 2009, http://www.nytimes.com/2009/11/13/opinion/13krugman.html?_r=0.

Lacan, A. (2013): 'France: des avancées sur le front de l'emploi', Eco Focus Crédit Agricole S.A., Apériodique 13/04.

La Moncloa (2013): 'President of the Government announces automatic extension of 'Prepara Plan' until unemployment falls below 20% ', http://www.lamoncloa.gob.es/IDIOMAS/9/Presidente/News/2013/20130124_PG_Peru.htm.

Le Figaro (2013): Ce que change le texte sur la sécurisation de l'emploi, March 6 2013, p. 5.

Le portail de l'Économie et des Finances (2013): 'Qu'est-ce que le Crédit d'impôt pour la compétitivité et l'emploi?', http://www.economie.gouv.fr/ma-competitivite/quest-que-credit-dimpot-pour-competitivite-et-lemploi.

Liberation (2013): La flexibilité au nom de la compétitivite; March 6 2013, p.5.

Lusinyan, L. and D. Muir (2013): 'Assessing the Macroeconomic Impact of Structural Reforms: The Case of Italy', IMF Working Paper, WP 13/22.

Minijob-Zentrale (2013): 'Besteuerung des Arbeitsentgelts aus geringfügigen Beschäftigungen', http://www.minijob-zentrale.de/DE/0_Home/01_mj_im_gewerblichen_bereich/18_steuerrecht/node.html.

Ministry of Economy and Competitiveness (2012): 'Labour Market Reform, February 2012', http://www.thespanisheconomy.com/SiteCollectionDocuments/en-gb/Economic%20Policy%20Measures/120517%20labour%20market%20reform,%20brief%20description.pdf.

Möller, J. (2010): 'The German Labour Market Response in the World Recession – de-mystifying a Miracle', Zeitschrift für Arbeitsmarkt Forschung, 42(4).

OECD_a (2013): 'OECD Economic Surveys: France 2013', OECD Publishing.

OECD_b (2013): 'Economic Policy Reforms 2013: Going for Growth France'.

Stability Programme Update Kingdom of Spain 2013–2016 (2013).

The Economist (1999): 'The sick man of the euro', The Economist, 3 June 1999.

Volmer, H. (2013): 'Die zwei Erzählungen der 'Agenda 2010' – Land gerettet, Land gespalten', http://www.n-tv.de/politik/Land-gerettet-Land-gespalten-article10264791.html.

Wippermann, C. (2012): 'Frauen im Minijob – Motive und (Fehl-) Anreize für die Aufnahme geringfügiger Beschäftigung im Lebenslauf', Bundesministerium für Familie, Senioren, Frauen und Jugend.

Wölfl, A. and J. S. Mora-Sanguinetti (2011): 'Reforming the Labour Market in Spain', OECD Economics Department Working Papers, No. 845, OECD Publishing.