

Hartz IV and the Consequences: Have Labor Market Reforms destroyed the German Model?

Competitiveness in Europe:
Confronting Italy and Germany –
Residenza Ripetta

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Structure

- What is the German model?
- The Hartz reforms
- Pros and Cons
- Conclusions

What is the German Model?

The (traditional) German model

- Dual training system
- Job protection
- High coverage of collective bargaining
- Strong role of social partnership (and co-determination)
- Generous social benefits
(high replacement ratio and duration)

Implications of the (traditional) German model

- importance of firm-specific human capital
 - vocational training within the firm
 - high tenure
- low *external flexibility*
 - low speed of workforce adjustment (e.g. in face of structural crisis)
- high *internal flexibility*
 - adjustment of working hours
- relatively low wage dispersion

The Hartz Reforms

The rationale behind the German labor market (“Hartz-“)reforms

- high and increasing systemic unemployment since the mid-1970s (ratchet or hysteresis effects)
 - high financial burden through German re-unification
 - low growth, low rates of job creation
 - Germany a laggard in structural change (under-developed service industry)
- Germany the “paradigm of Euroclerosis”
- in the late 1990s the Economist blamed Germany the “sick man in Europe”

The “teutonic turnaround” (M.Burda)

- Chancellor Schroeder in March 2003:
“If Germany refrains from modernizing its labour market institutions then it would be modernized through the brute forces of the global markets leaving barely room for a social protection net.”

Basic elements of the reforms

- reforms in different steps between 2003 and 2005
- key concept for the unemployed “supporting and demanding”
- concrete elements:
 - lower job protection,
 - reduction of the maximum period for unemployment insurance benefits
 - tightening of job acceptance regulations for the unemployed
 - de-regulation for temporary work agencies
- merger of unemployment assistance and welfare (“Hartz IV”)
 - far-reaching consequences!

Consequences of “Hartz IV”

- welfare recipients generally considered to be available for the labour market if being able to work at least for 3 hours a day (→ unintended by-product: 0.5 m increase in unemployment)
- unemployed obliged to accept any reasonable job
- benefits from unemployment insurance means-tested after certain duration (typically one year)
 - social office may access the recipients' private assets
 - pressure for the unemployed to find quickly a new job

General reform effects

- drastic cure
- although not all parts of the reforms well-designed strong effects on the labor market
- extraordinary boom period (2004:Q4 to 2008:Q2) (aggregate economy real production +9.4%; manufacturing +18.8 %)
- from 2005 to the eve of the World Recession unemployment fell from its peak level of more than 5 m to less than 3 m
- ratchet effect was overcome:
 - the unemployment rate at the beginning of the economic downturn (2008:Q3) lower than at the beginning of the previous recession

Specific reform effects

- changes in behavior of the unemployed and the incumbent workforce
- decrease in systemic and long-term unemployment
- better performance of the labor market:
shift of the Beveridge Curve

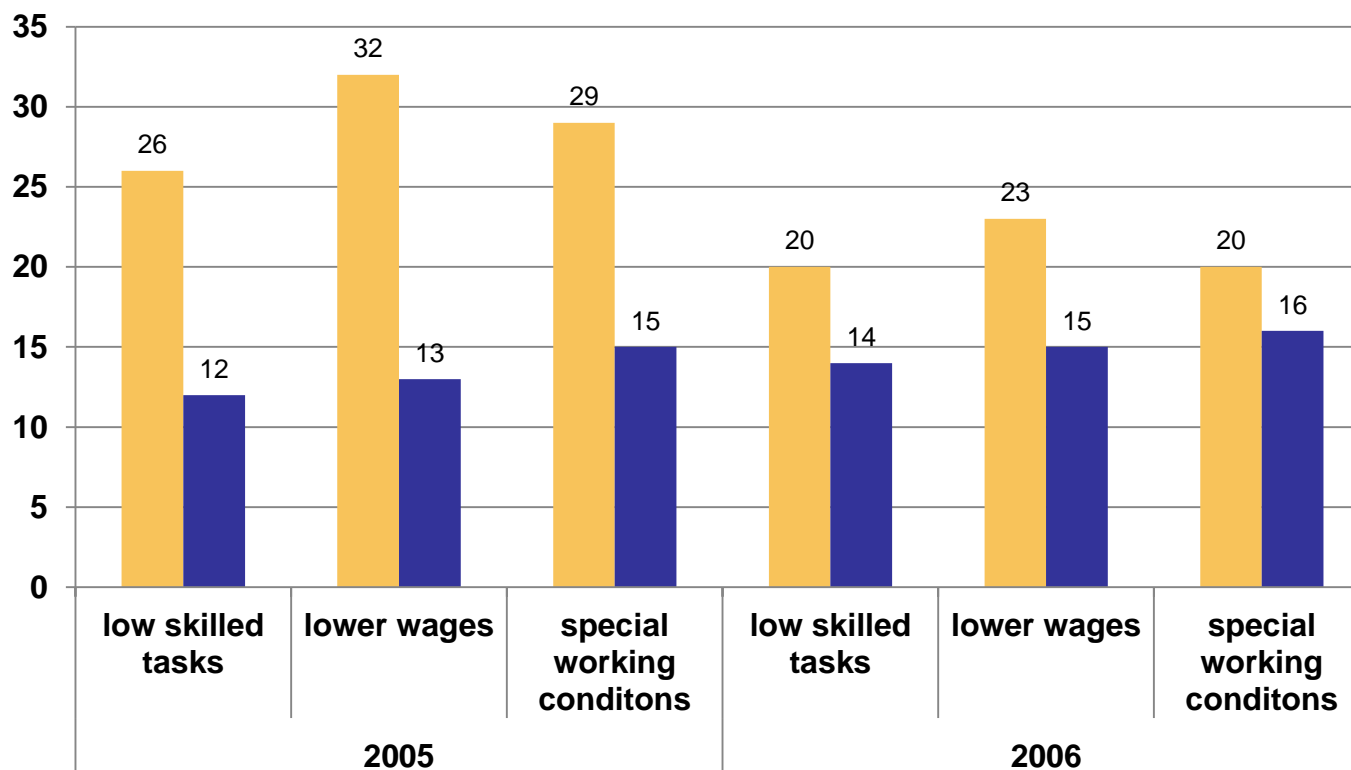
Changes in Behavior

Change in Behavior of Unemployed Jobseekers (relative to previous year)

(firms with job openings within the last 12 months only)

Willingness of jobseekers to accept ...

■ increase ■ decrease



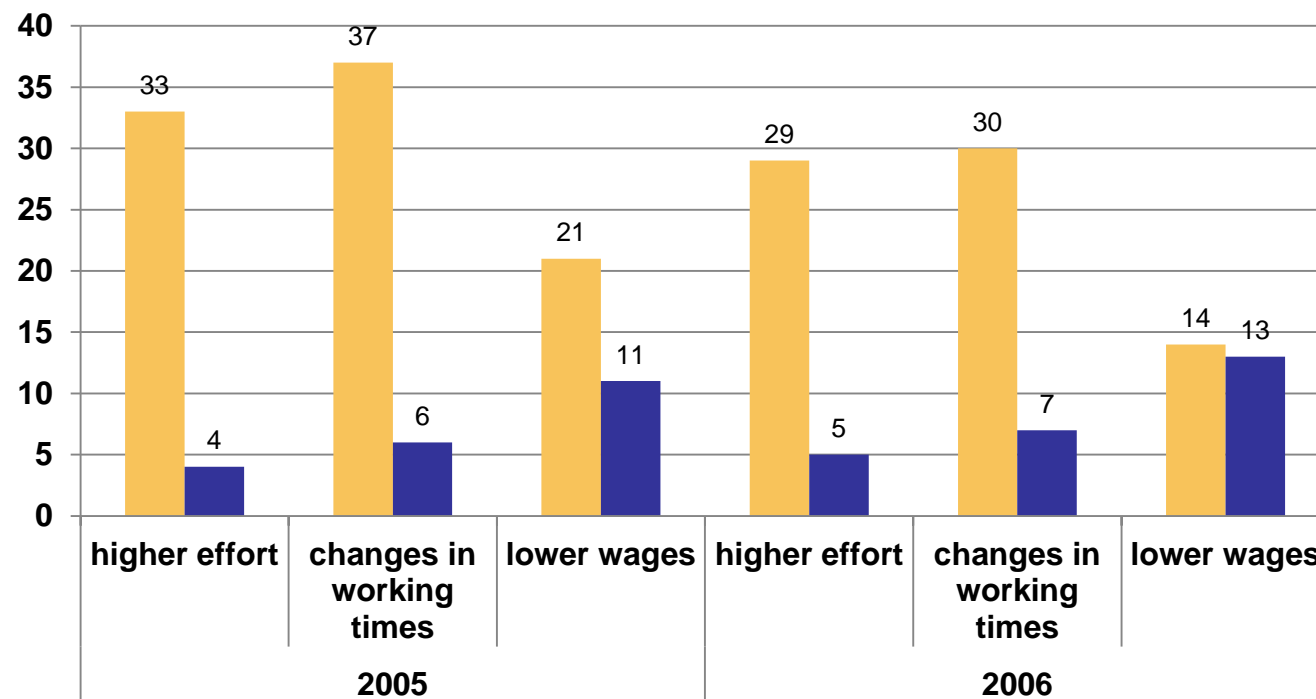
Source: Erhebung des Gesamtwirtschaftlichen Stellenangebots 2005/2006

Change in Behavior of the incumbent Workforce (relative to previous year)

(firms with job openings within the last 12 months only)

Willingness of the incumbent workforce to accept ...

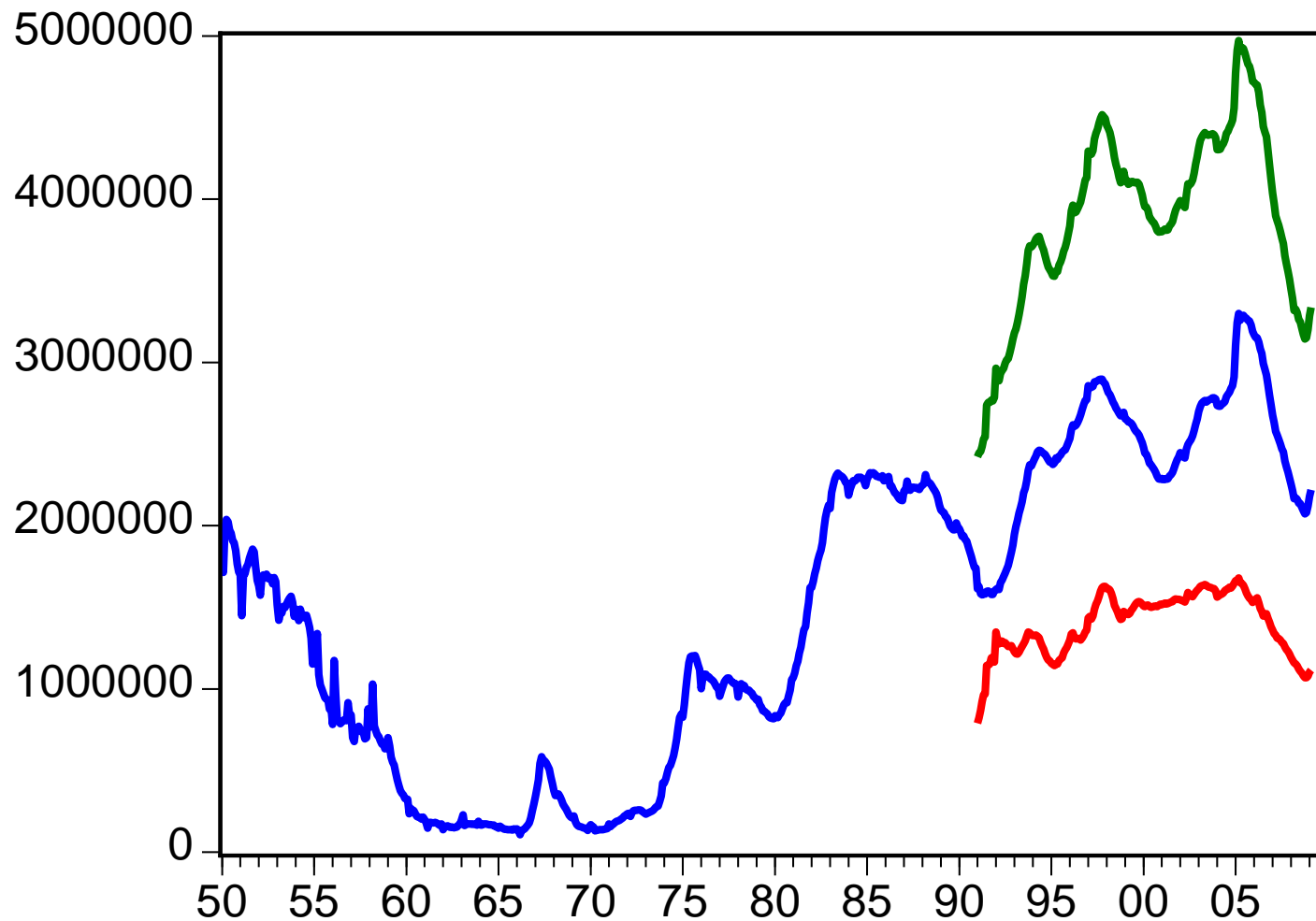
■ increase ■ decrease



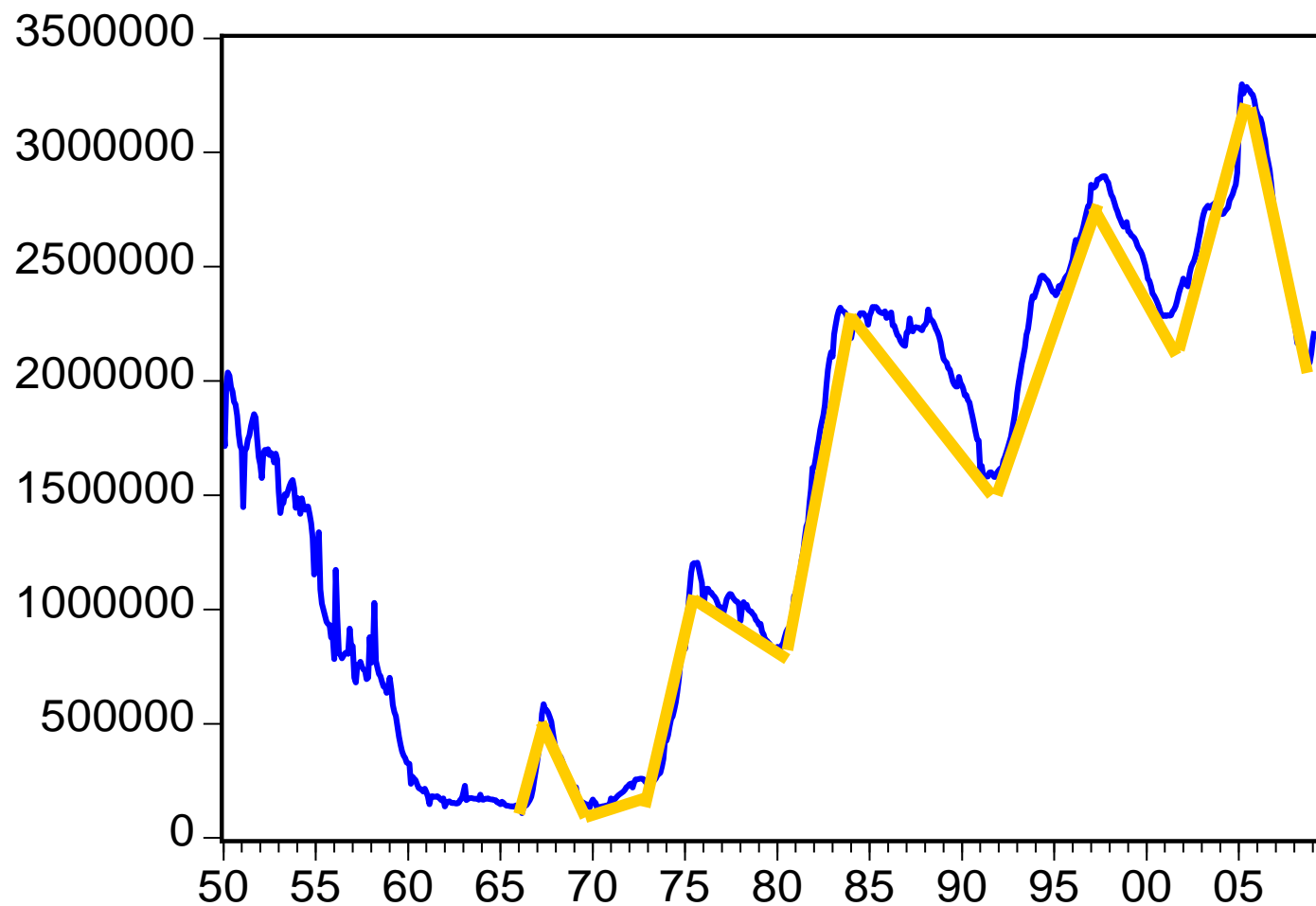
Source: Erhebung des Gesamtwirtschaftlichen Stellenangebots 2005/2006

Changes in Systemic and Long-term Unemployment

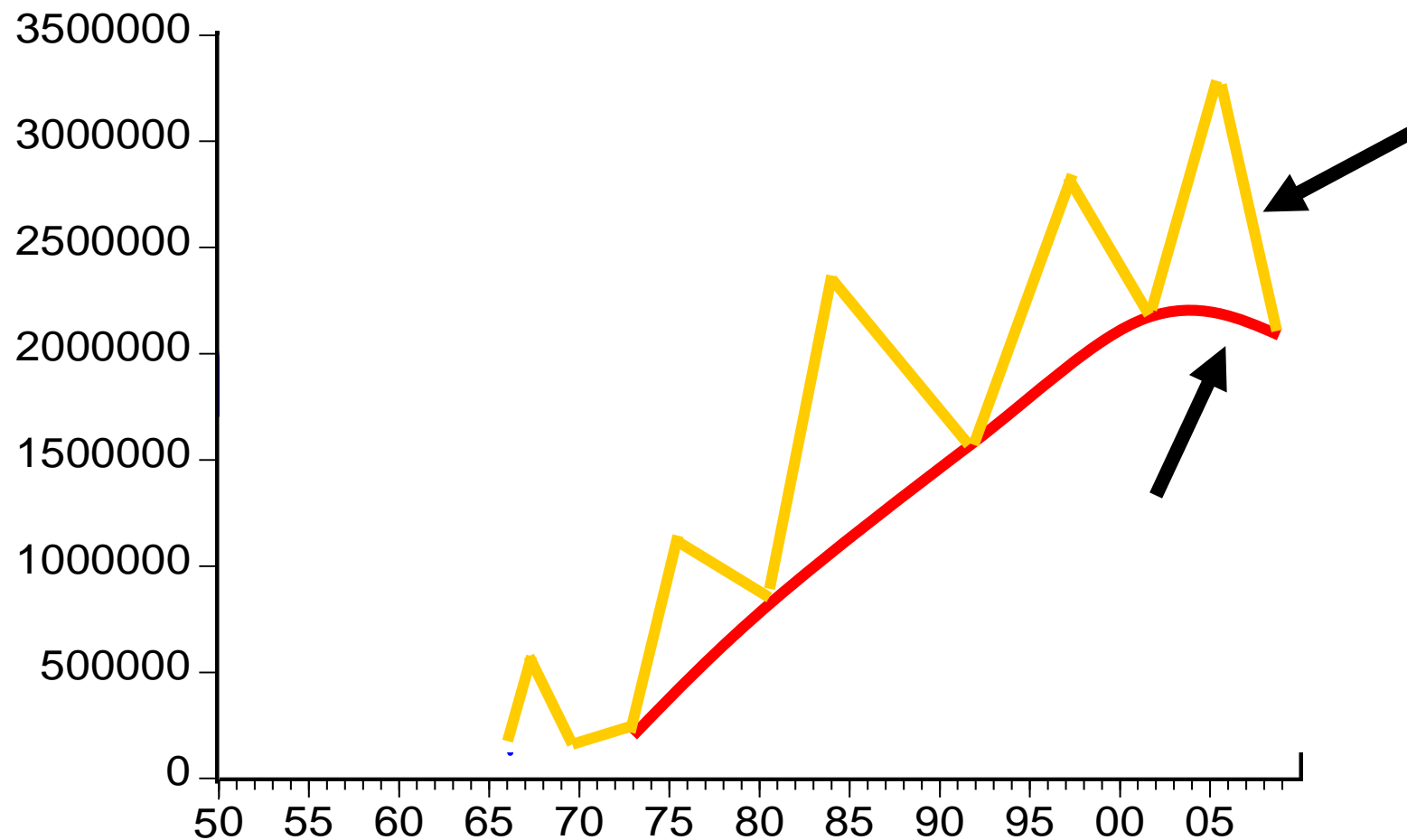
Unemployment: Long-run development



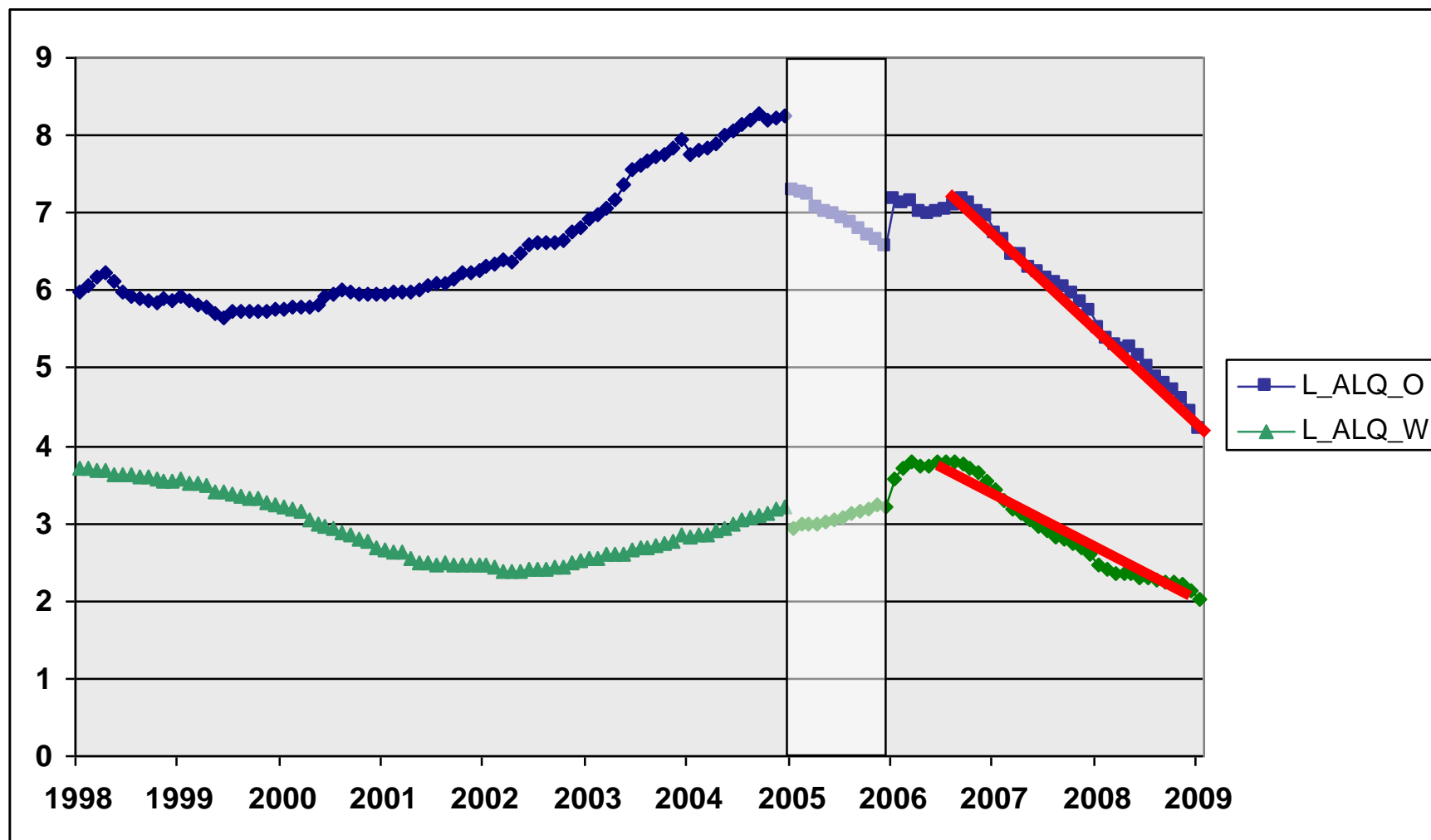
Unemployment – The ratchet effect (1)



Unemployment – The ratchet effect (2)



Change in the Long-term Unemployment Rate 1998-2009

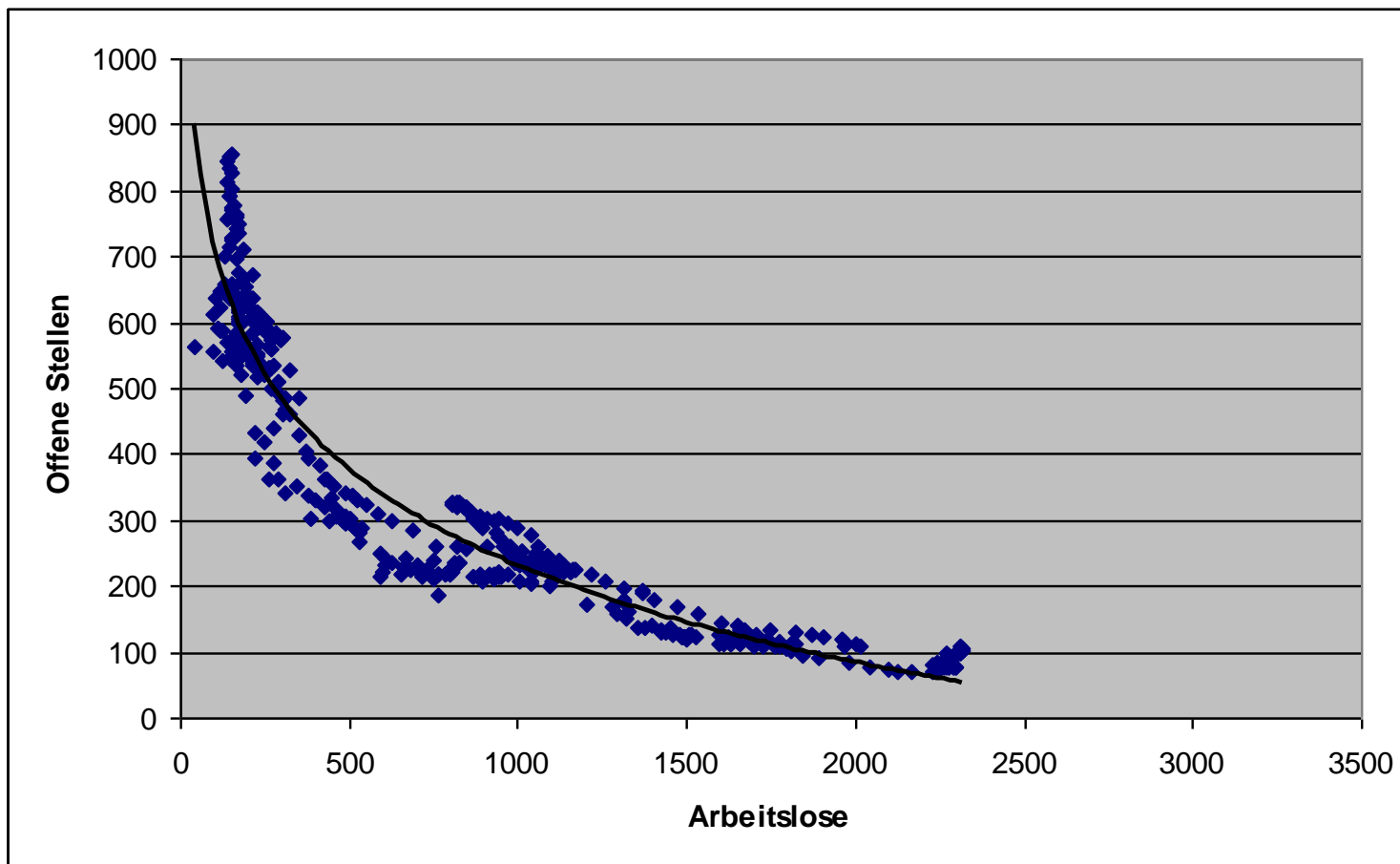


Eigene Berechnungen; Langzeitarbeitslose in Prozent der zivilen Erwerbspersonen, saisonbereinigte Werte, Daten für 2005 wegen Bruchs in der Statistik nicht interpretierbar

A Shifting Beveridge-Curve ...

Die Beveridge-Kurve 1950:M1 bis 1985:M6

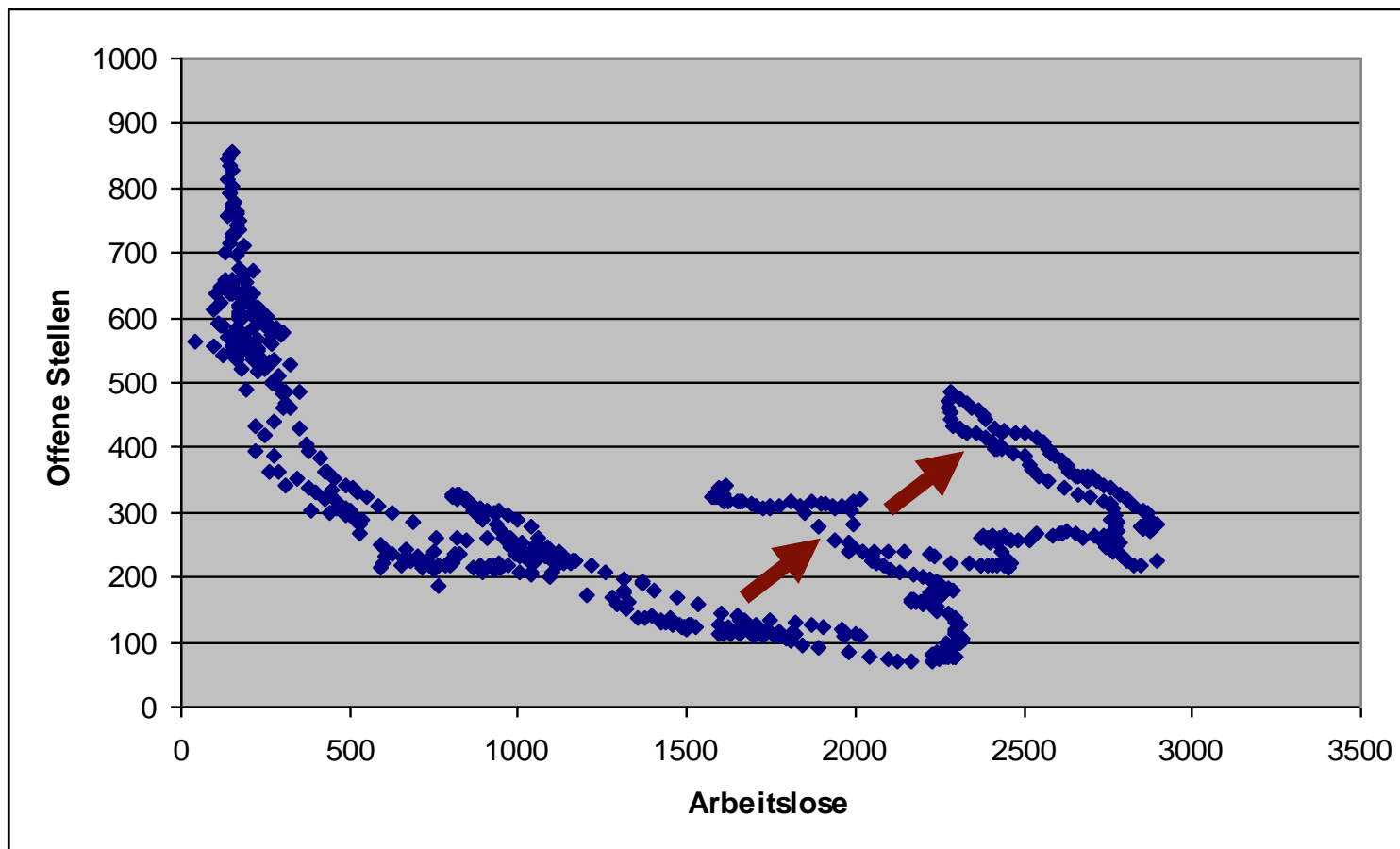
(Registrierte Arbeitslose und offene Stellen, saisonbereinigte Monatswerte)



Datenquelle: Deutsche Bundesbank, lange Zeitreihen; nur Westdeutschland

Die Beveridge-Kurve 1950:M1 bis 2004:M12

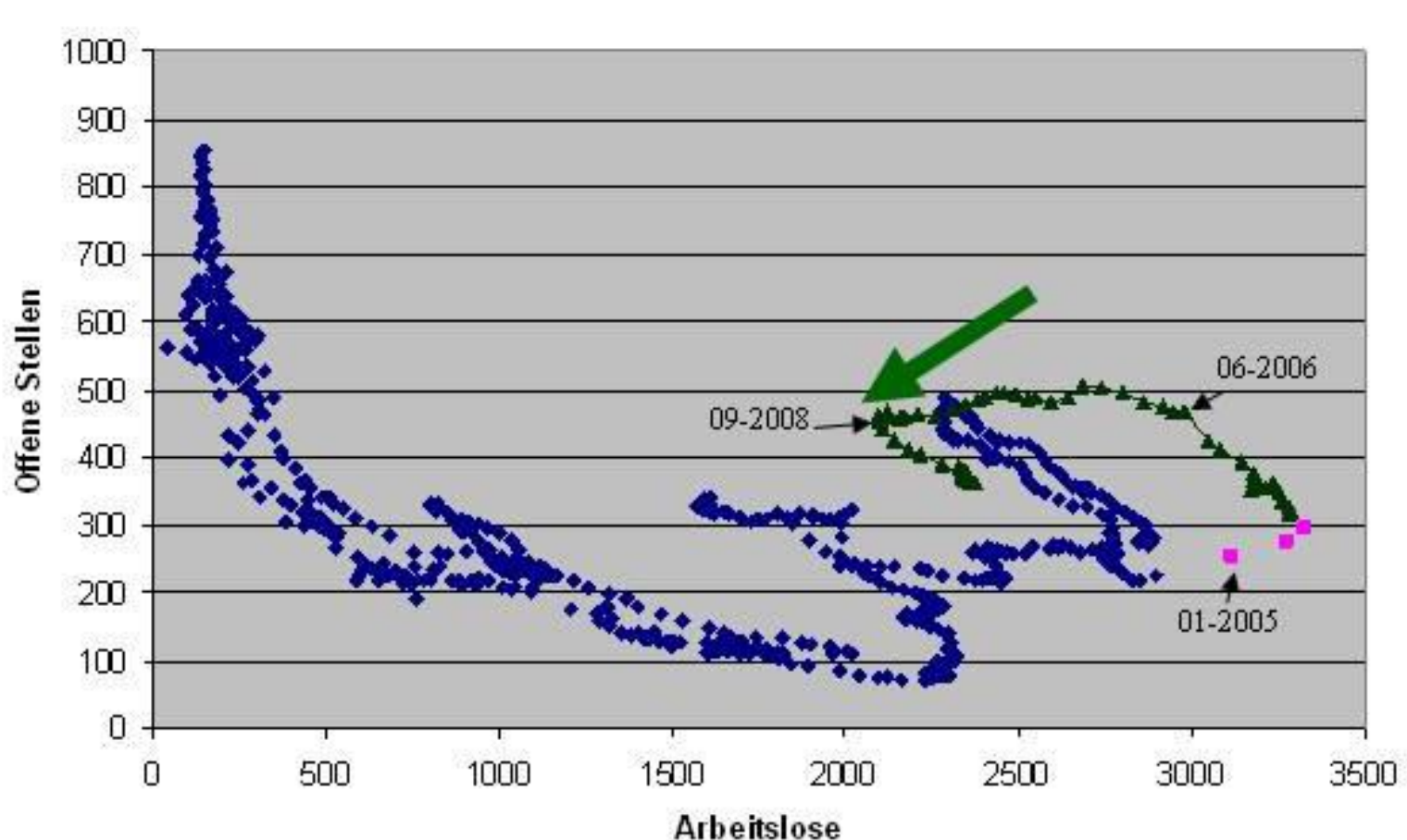
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Datenquelle: Deutsche Bundesbank, lange Zeitreihen; nur Westdeutschland

Die Beveridge-Kurve 1950:M1 bis 2010:M3

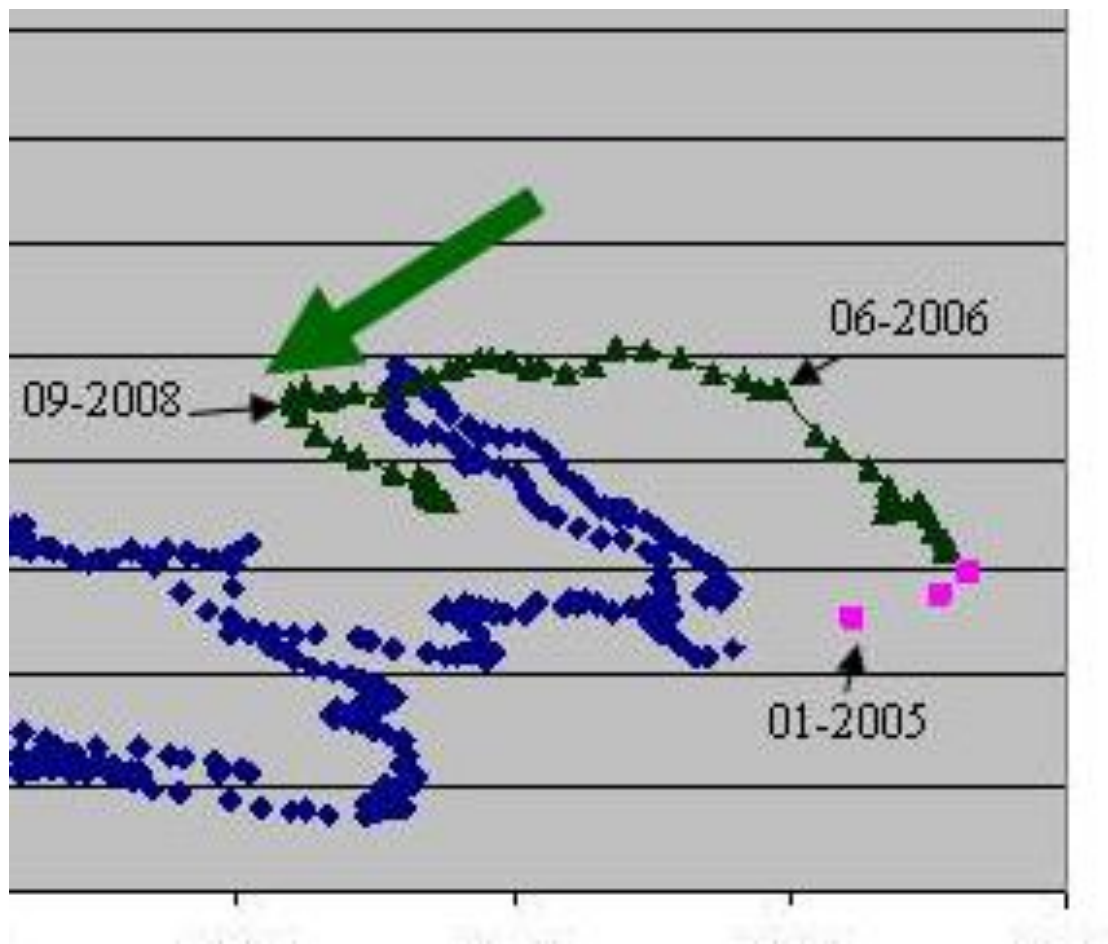
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Datenquelle: Deutsche Bundesbank, lange Zeitreihen; nur Westdeutschland

Die Beveridge-Kurve 1950:M1 bis 2010:M3

(Registrierte Arbeitslose und offene Stellen, saisonbereinigte Monatswerte)



Datenquelle: Deutsche Bundesbank, lange Zeitreihen; nur Westdeutschland

Drawbacks

Drawbacks of the reform

- increasing segmentation of the labor market
 - decrease of normal employment
 - wage inequality/ working poor
 - job instability (for some groups)
- limits of activation
 - right balance between “supporting” and “demanding”?
 - instruments of active labor market policy do not fit the individual needs adequately

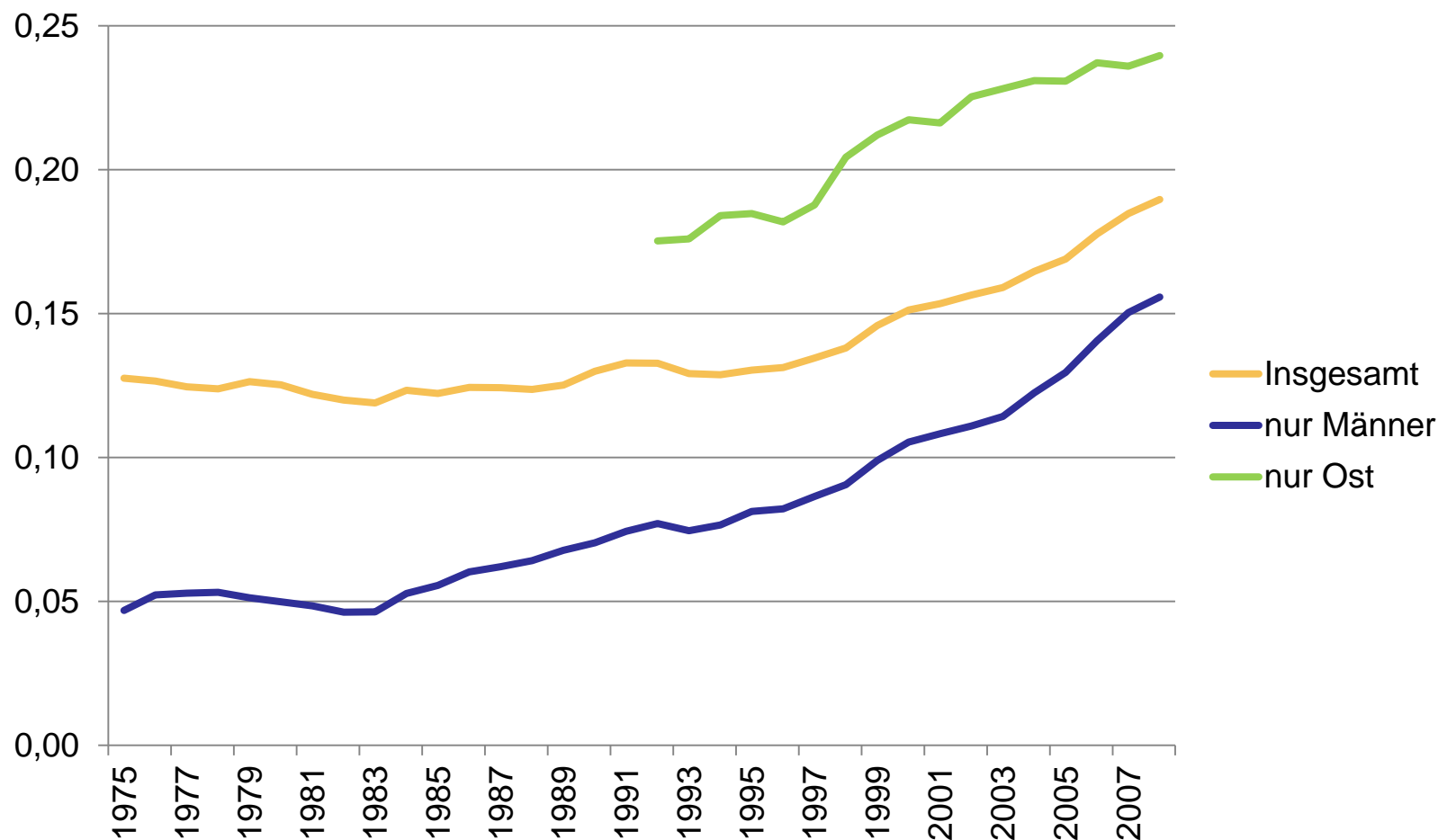
Wage inequality

Share of normal employment* by age and skill level

	1991	1999	2007
Age			
15-24	56,2%	35,9%	28,1%
24-49	75,0%	70,4%	63,9%
50-64	73,9%	69,4%	65,3%
Skill level			
low	54,9%	46,9%	34,0%
intermediate	77,0%	71,0%	64,8%
High	75,7%	71,9%	67,5%

full-time, permanent contract with social contributions; working with the same employer (no temps)

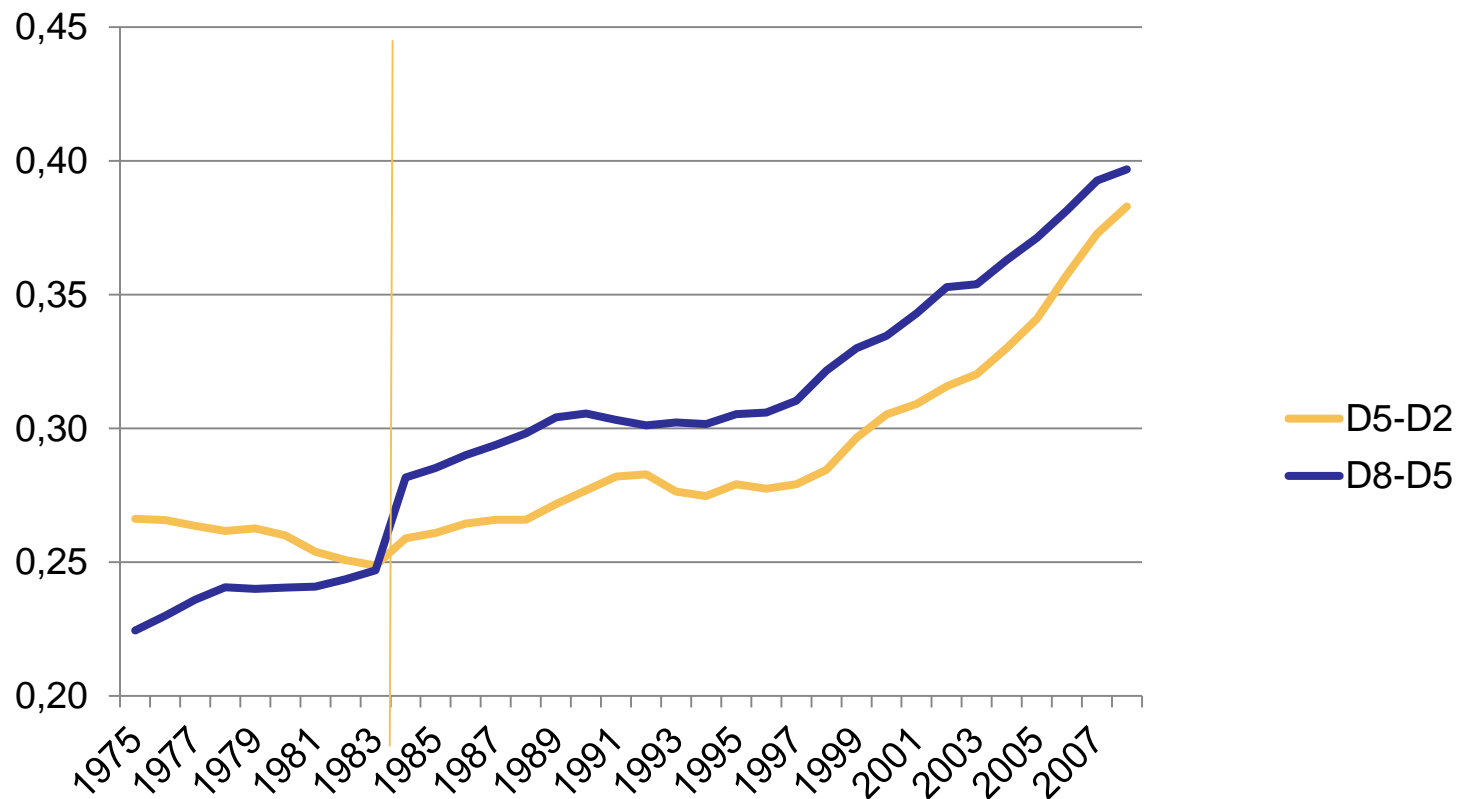
Share of low-pay employment*



* 2/3 of the median; full-time workers only; age 25 und 55; Source: Own calculations with SIAB

Inequality measures 1975-2008

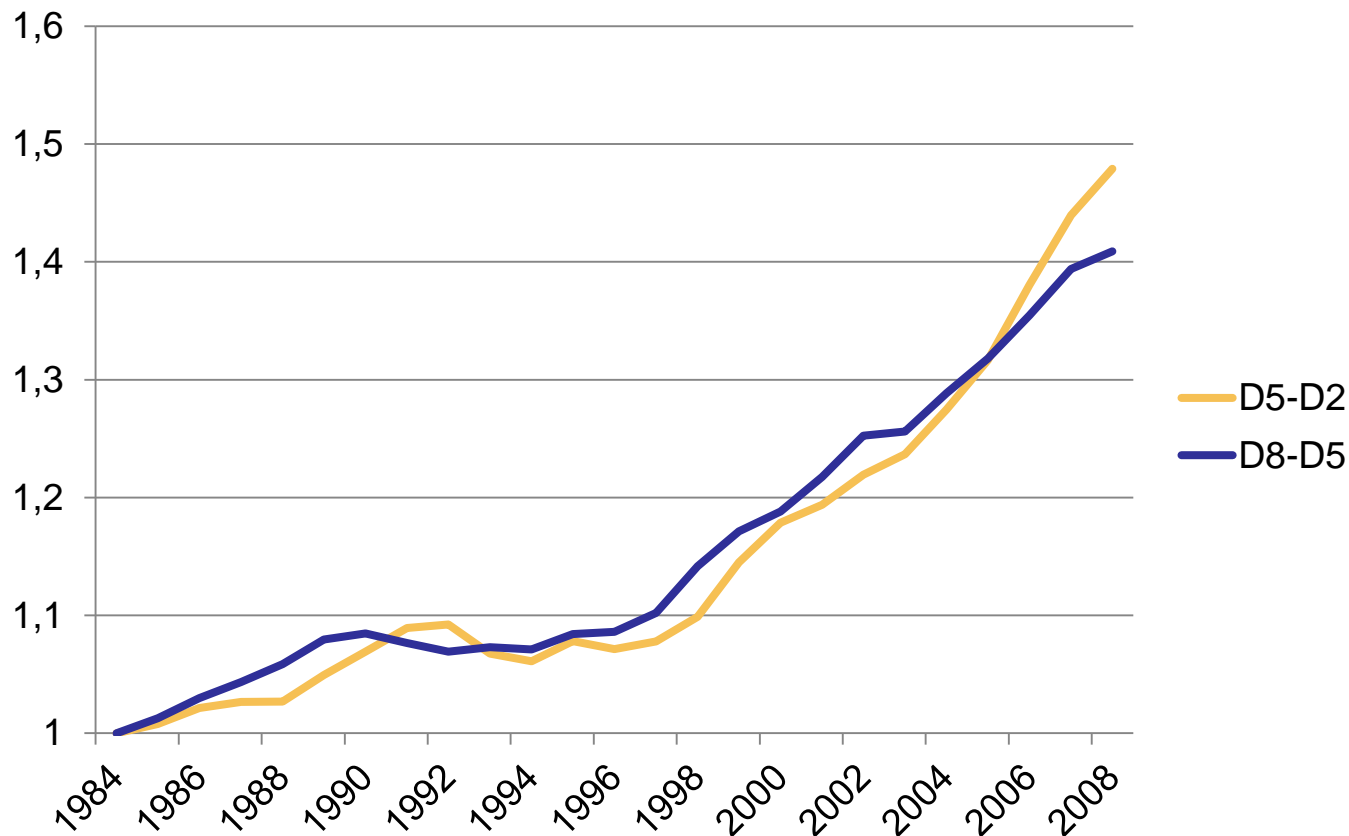
(Log. decile distance in the upper (D8-D5) and lower (D5-S2) tail of the distribution¹⁾)



1) full-time male workers only; age 25 und 55;; West Germany; structural break in 1983/84; Source: Own calculations with SIAB

Inequality index (1984=1) 1984-2008

(Log. decile distance in the upper (D8-D5) and lower (D5-S2) tail of the distribution¹⁾)

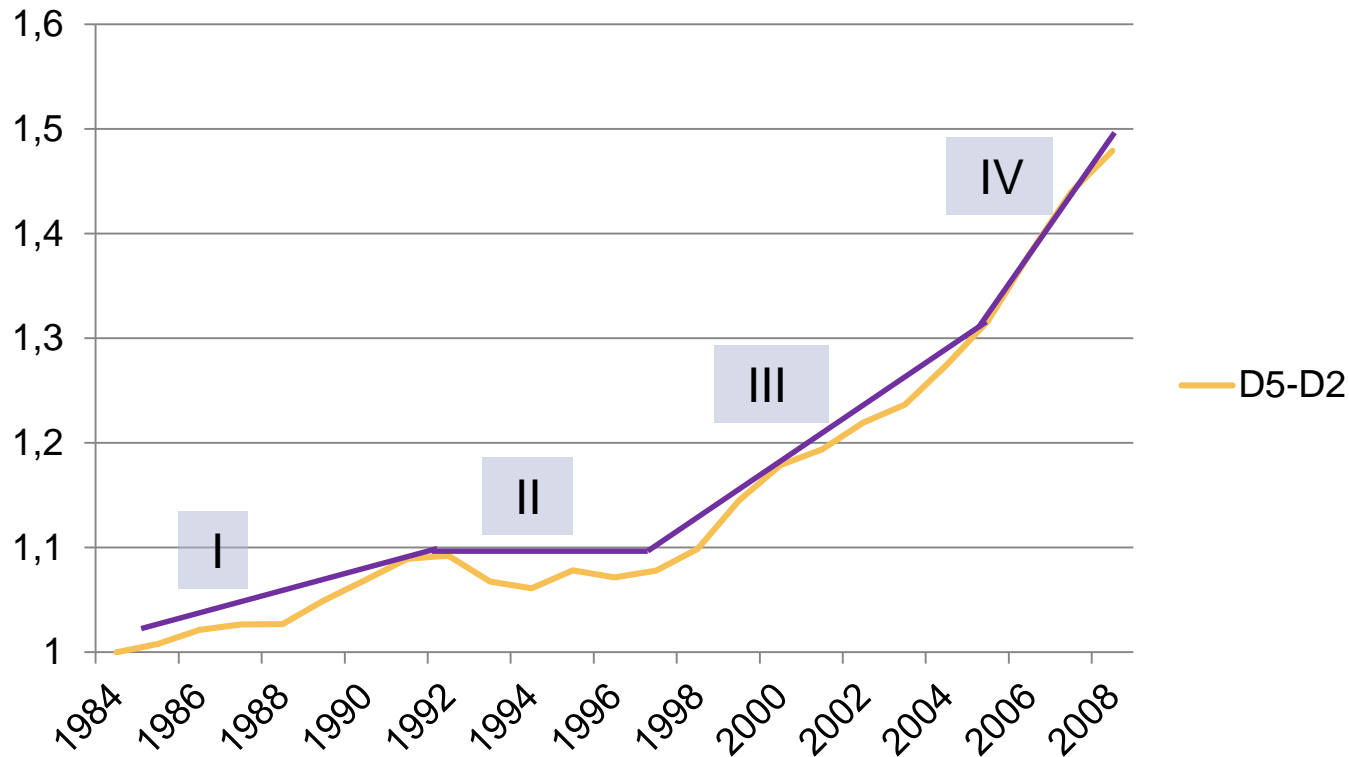


1) full-time male workers only; age 25 und 55;; West Germany; Source: Own calculations with SIAB; Quelle: S-IAB

Inequality Index (1984=1) 1984-2008

(Log. decile distance in the lower (D5-S2) tail of the distribution¹⁾)

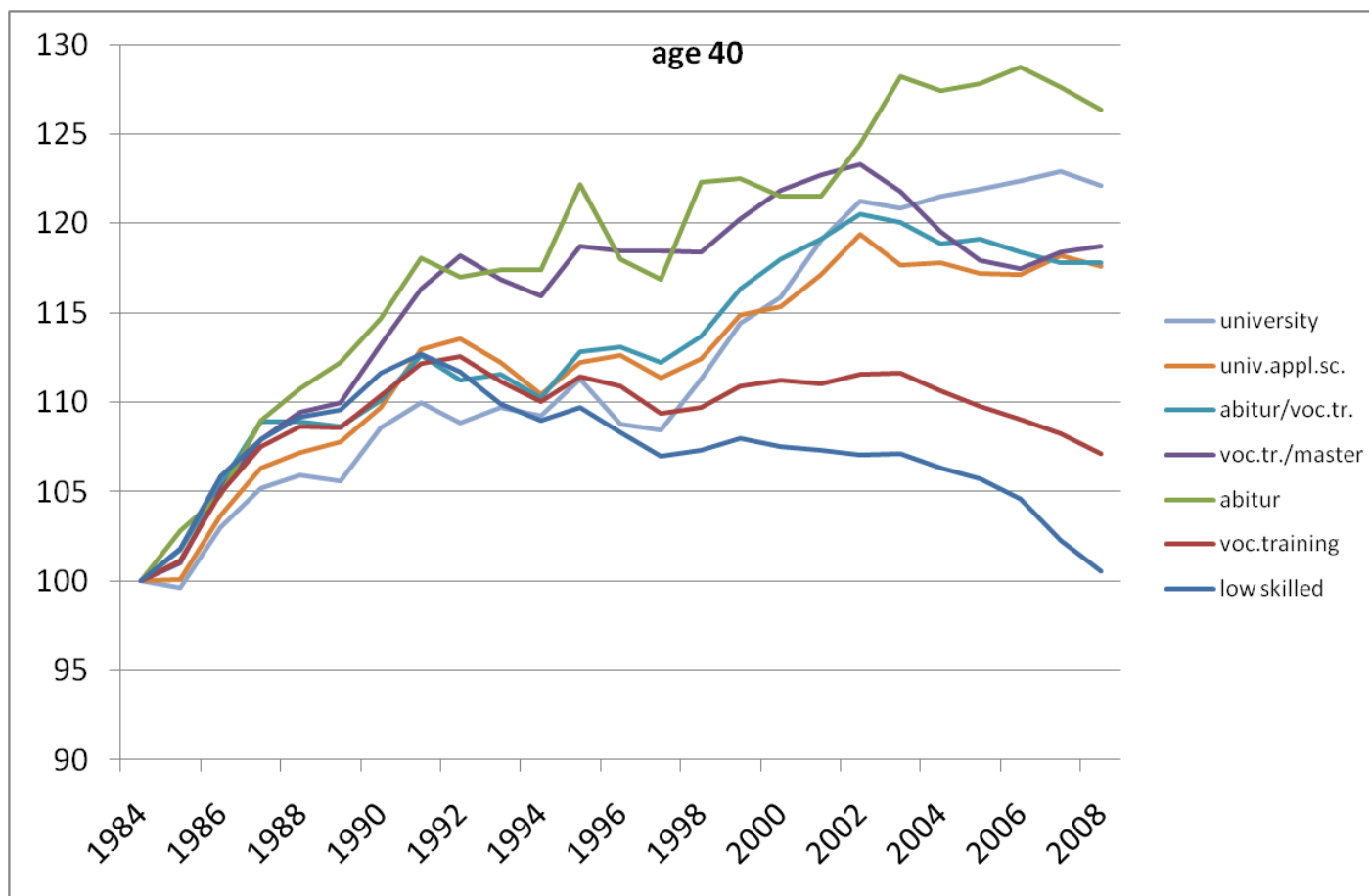
D5-D2



1) Full-time male workers only; age 25 und 55;; West Germany; Source: Own calculations with SIAB; Quelle: S-IAB

Real Earnings 1984-2008 by Qualification (1984=100, male full-time

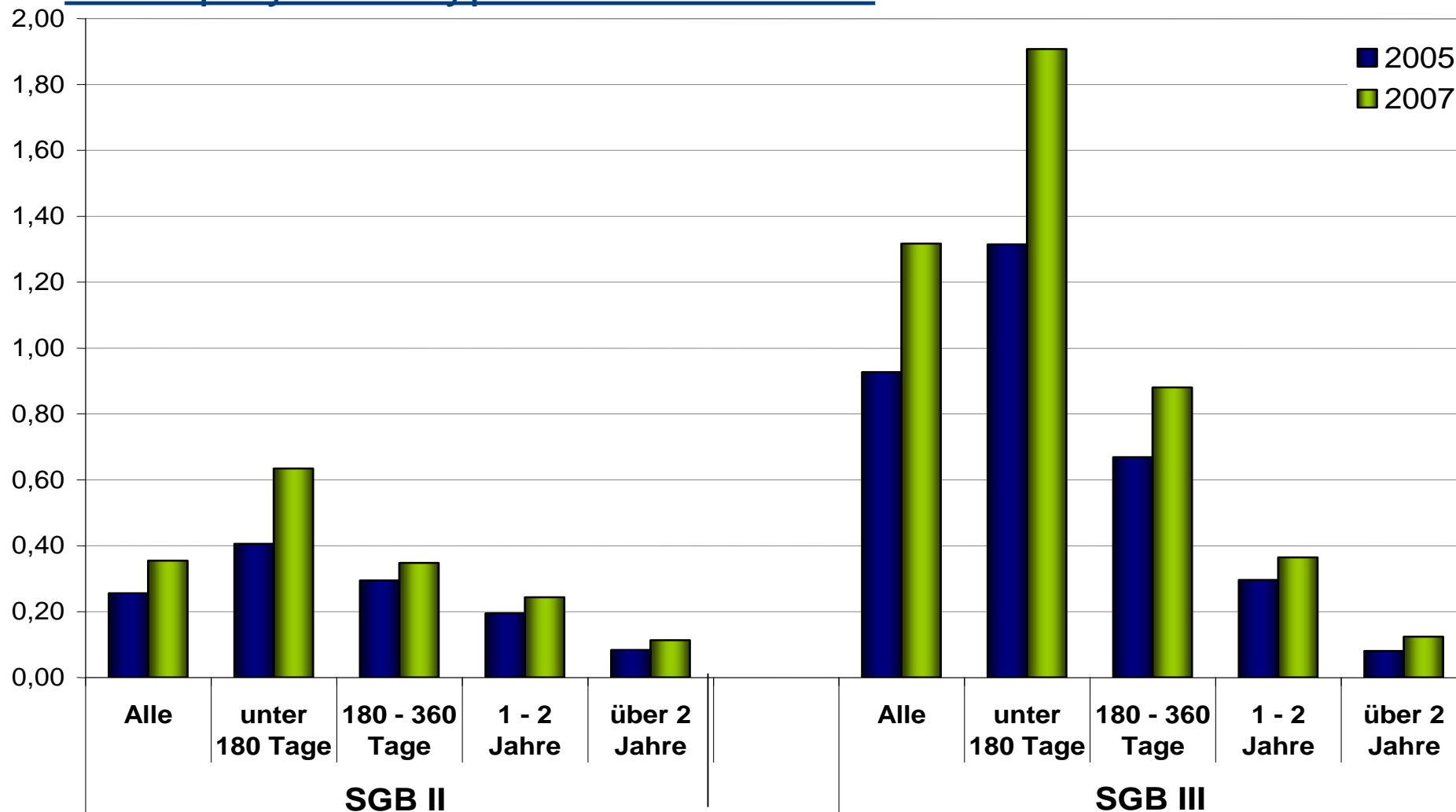
worker West, age 40)



Quelle: Eigene Berechnungen auf der Grundlage einer ökonometrischen Schätzung einer logarithmischen Lohnfunktion ; erklärende Variablen: Konstante, sechs Dummy-Variablen für Qualifikation, Alter, Alter², alle Interaktionen; Datenbasis: S-IAB

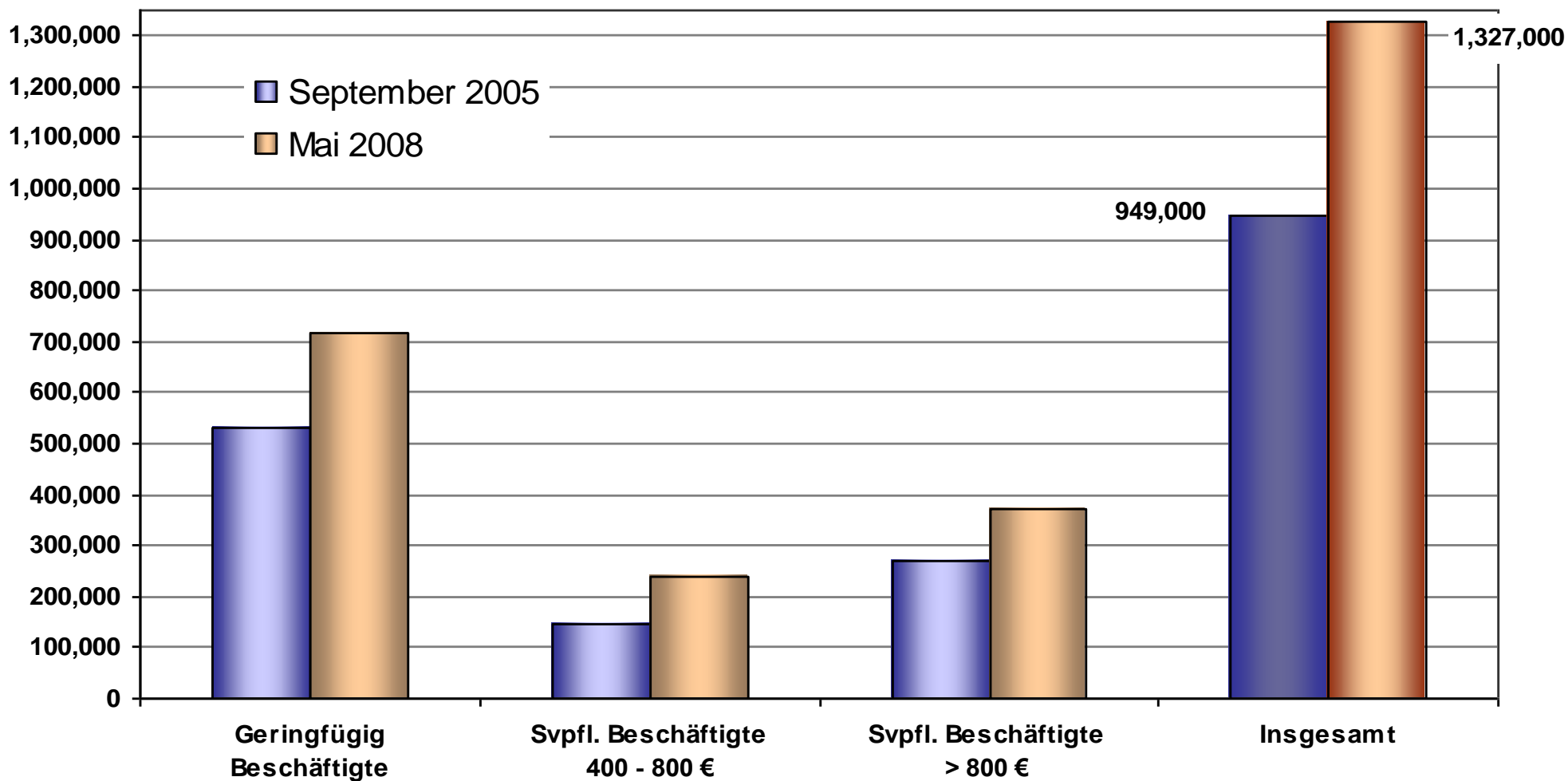
Limits of Activation

Transition Rates to Employment by Unemployment Duration and Unemployment Type 2005 und 2007



Working Poor

Working Poor by Type of Employment (2005 und 2008)



Conclusions

Answer to the Initial Question

Did the Hartz-reforms destroy the German model?

→ No! But ...

Prince of Salina in Visconti's *Leopard*:

“Everything must change if everything is to remain the same.”

Reform of the reform?

Improvements necessary with respect to ..

- the precise fitting of active labor market instruments → more qualified case workers
- limiting inequality → minimum wage
- the control logic of labor market policy → fostering job stability, especially for temps

Employment and Unemployment over the Life Cycle (Birth Cohort 1950)

		Employ- ment	Unemploy ment	Not in labor force
A	# Spells	9.9	10.6	15.9
	ØDuration (Da	332	343	162
B	# Spells	3.9	1.1	3.9
	ØDuration (Da	1677	167	731

Group A: High-risk group (5% of cohort, 50% of unemployment days)

Group B: Rest

Effects of reforms on Germany's job miracle?



BIP-Schock
und
Veränderung
der
Arbeitslosigkeit
in den OECD-
Ländern
2008, Q2 bis
2009, Q2

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