

IZA DP No. 9325

## **Are There Austerity-Related Policy Changes in Germany?**

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September 2015

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Discussion Paper No. 9325  
September 2015

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## ABSTRACT

### Are There Austerity-Related Policy Changes in Germany?\*

This paper assesses the existence and the extent of austerity-oriented policies in Germany in the aftermath of the 2008-9 recession. In contrast to the intensive phase of labour market and welfare state reforms in the early 2000s aimed at 'welfare readjustment', we do not see austerity policies in Germany, rather a continuation of the path that was adopted earlier. This can be explained by the economic conditions which were, and still are, much more favourable than in many other EU Member States. Most recently, we can identify a partial reregulation of the labour market, most notably the introduction of a national minimum wage, a potential increase in the regulation of non-standard contracts and a reintroduction of early retirement for labour market insiders. These policies can be classified as 'welfare protectionism'.

JEL Classification: J21, J26, J68

Keywords: labour market reforms, Germany, austerity, welfare state retrenchment

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\* Contribution to a project on "Welfare states in the era of EU austerity - the case of labour market policies" organized by the European Trade Union Institute. We are grateful to ETUI for support on this piece of research and in particular to Sotiria Theodoropoulos for helpful comments on an earlier draft.

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## **1. Introduction: The success story of Germany and its Policy Reforms**

Since the turn of the millennium, the German model has been characterised by a period of major reforms followed by a period of remarkable stability and growth in times of global economic crisis. In Germany, austerity-related reforms occurred between 2003 and 2005, when a fundamental restructuring of the welfare system was perceived as necessary in order to ensure international competitiveness and fiscal sustainability in a situation of high unemployment levels and repeated failure to stabilize and ensure economic growth. After the first change of government since reunification in 1998, the new centre-left government was criticized for failing to cope with the economic effects of reunification, globalisation and demographic changes. Germany repeatedly failed to adhere to the fiscal discipline of the European Stability and Growth Pact, which was central to the workings of the EMU. Internal as well as external pressure led to policy reforms and fundamental changes in the pension and unemployment insurance system as well as social assistance schemes. In addition, the German model experienced a relaxation of capital market regulation, accompanied by a reduction of corporate taxes. After these reforms, which were concluded in the mid-2000s, Germany has not continued any austerity strategy in economic or social policy, beyond sticking to fiscal constraint and the debt brake. On the contrary, since the financial crisis hit Europe, the government has responded with policies promoting growth and expansion.

During 2008-9, most of the OECD countries were hit by the financial crash and subsequent crisis and have struggled to recover ever since. Germany, in contrast to most countries, not only managed to quickly respond to the effects of the crisis with fiscal stabilization policies but also managed to reduce unemployment levels to lower levels than before the economic crisis. Germany experienced a severe drop in GDP, of over 5 percent in 2009 but, through various quick policy responses, such as short-term working and the cash-for-clunkers programme, German firms recovered quickly. Ever since, Germany has been experiencing employment growth and the highest average economic growth rate within the Eurozone. In contrast to most of the neighbouring countries, neither economic institutions nor major economic reforms were seen as necessary to stabilise the national economy. The current policy orientation is rather one of moderate reregulation of the labour market and welfare state expansion. However, Germany's strategy challenged other Eurozone members, as the country's rising exports were accompanied by current account deficits in other Eurozone countries.

The academic discourse on welfare restructuring differentiates between two different forms of reform: welfare readjustment or welfare protectionism, which are opposed to each other (Häusermann 2010). Both forms combine elements of retrenchment and expansion between policy instruments that are either categorized as belonging to an 'industrial logic' or a 'needs-based' group. Welfare readjustment strategies are characterised by retrenchment in industrial logic policy instruments, such as passive income support and employment protection (EPL), and expansion in 'needs-based' social policies, such as income subsidies for the working poor or, alternatively, activation mechanisms in labour market policies. In contrast, welfare protectionism entails the expansion of 'industrial' logic instruments and retrenchment in 'needs-based' logic or activation strategies. The strategy of the latter, therefore, protects the old system at the expense

of new participants in the labour market, whereas the former tries to incorporate and protect new participants and groups at the expense of the old system. The differentiation made here is often presented under the theme of labour market dualization or the discourse between insiders and outsiders in the labour market.

With regard to the German case, we will show that the major reforms during the early 2000s can be characterised as welfare state readjustment, whereas the recent changes entail at least some characteristics of welfare protectionism.

## 2. Welfare reforms during the 2000s

The so-called Hartz reforms, initiated in 2002 by the first red-green government and accomplished in January 2005 with the Hartz IV package, marked a significant change in the German welfare state. The Hartz IV reform was introduced as the core activation policy in Germany (Eichhorst/Grienberger-Zingerle/Konle-Seidl 2008, Ebbinghaus/Eichhorst 2009, Hassel/Schiller 2010, Carlin et al. 2014). Initiated in order to simultaneously reduce the increasing level and cost of unemployment, characterised by high structural unemployment and economic inactivity rates in the new federal states and to facilitate access to jobs, the Hartz reforms entailed policy measures that resembled the 'flexicurity' agendas in other countries. The reforms shifted employment risks from the employer to the employee and introduced more flexible forms of temporary or part-time employment. This, on the one hand, increased heterogeneity of employment structures but, on the other hand, these changes led to an increase of fragility in some segments of the labour market, especially in non-standard forms of employment, without questioning the regulatory pattern governing the core of the labour market. Hence, new forms of inequality have emerged within the labour market. The reforms are perceived to have only partially eased the issue of long-term unemployment or the number of beneficiaries of social assistance. The Hartz reforms have created various forms of deregulation that will be outlined here.

One of the primary goals of the Hartz reforms was to reactivate and reintegrate the short-term as well as long-term unemployed. While maintaining contribution-related unemployment benefits for the initial phase of unemployment ("Unemployment Benefit I"), the reform merged the two means-tested schemes of unemployment assistance and social assistance into a single system ("Unemployment Benefit II"), changing the previous system of wage-related income support for those with some employment experience to a flat-rate benefit. The new structure, known as Hartz IV, proposed a single replacement scheme for those unemployed who had never paid contributions to unemployment insurance and those whose contribution-based benefits had expired. In contrast to the previous system, this scheme aimed to prevent poverty for those who received social assistance before, by slightly increasing their level of benefit and simplifying their access to employment services. At the same time, the system no longer secured the previous standard of living of the long-term unemployed, as the old unemployment assistance scheme was abolished, mainly affecting people in East Germany.

In addition, the Hartz reforms entailed substantial activating tools in order to lower the number of unemployed persons. Activation schemes were introduced for those receiving assistance. At the structural level, employment agencies were transformed into so-called jobcentres, entitled to define stricter job suitability criteria and supervise job placements of beneficiaries as well as cut benefits in cases of non-cooperation. Within the framework of 'rights and duties', beneficiaries sign integration agreements with the jobcentres, clarifying the responsibilities of each recipient in order to be reactivated into the job market and, ideally, into regular employment. For this goal, recipients are entitled to receive support in the form of training and additional qualifications, subsidised by the jobcentres. As regards active labour market policies, the reform also entailed wage subsidies or start-ups as an alternative to regular employment as well as reduced social security contribution packages for low-wage employment.

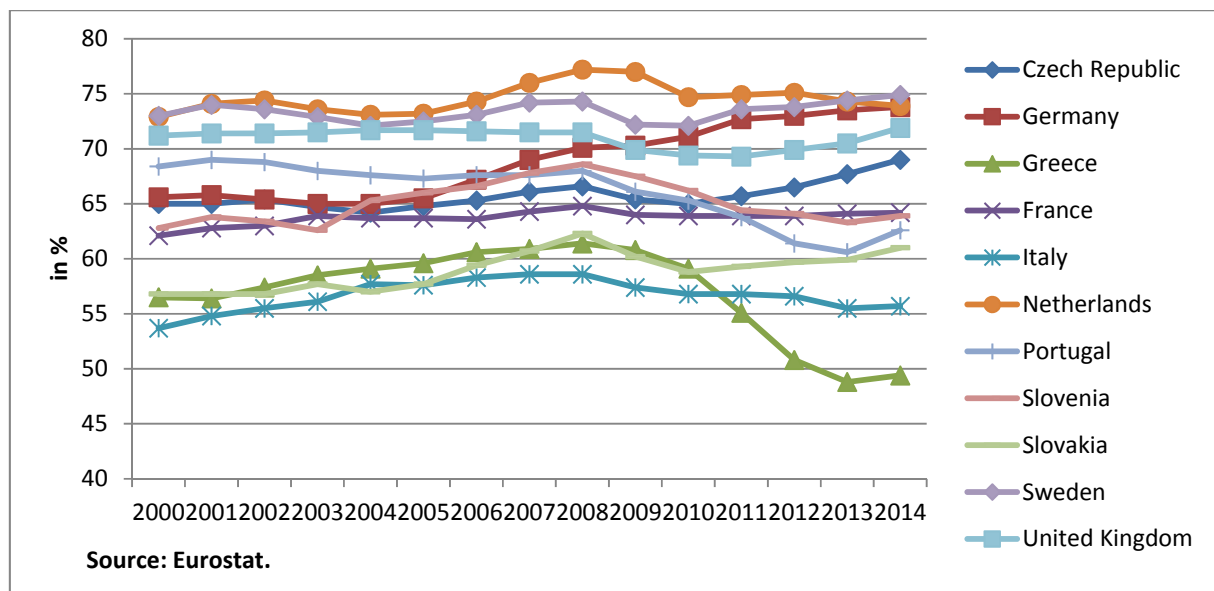
With regard to job creation, the reforms offered different, non-standard employment options, intended as first access possibilities to the job market, such as marginal, part-time work, agency work, or temporary employment alongside a simplified form of self-employment. These forms were intended to lower the barriers for job creation, especially in service occupations, for persons with limited work experience or skill levels. This more dynamic scheme of activation was aimed at linking a lower level of dependency on state benefits to an increase of jobs in the labour market and, in particular, in the service sector (Eichhorst/Grienberger-Zingerle/Konle-Seidl 2008, Ebbinghaus/Eichhorst 2009). Activation strategies aimed at creating a more flexible labour market with new forms of employment but also at creating core changes within pre-existing segments.

One of the biggest changes already occurred in 2003 with the regulation of the marginal part-time segment in the labour market. This change not only lifted the earnings threshold to €400 (€450 since 2013) per month from its previous level of €325, but also suspended the previous restriction of 15 hours per week. In addition, these so-called mini-jobs were allowed as second jobs and were relieved from tax and social insurance contributions and, concomitantly, did not provide social protection. From the employers' perspective, these marginal forms of employment entailed only minimal employers' contributions, as long as the wage stayed below the €400 (€450) threshold. If the wage exceeded €400 (€450), or the employee had more than one of these mini-jobs, full taxation and social insurance gradually applied, which gave more incentive for employers as well as employees to stay under the threshold. Mini-jobs became an attractive supplement for a second job or for secondary earners such as spouses as well as for students and pensioners, as they were exempt from mandatory employee contributions and income taxation. This created an incentive for employers to pay lower gross wages. To what extent employees entering the labour market via mini-jobs and then moving towards full-time employment occurred is questionable. Recent research has claimed that mini-jobs are replacing former regular forms of employment in service sectors, such as the hotel industry and the gastronomy. Evidence shows that employers use the mini-job mechanism to reduce hourly wages and labour costs (Eichhorst et al. 2012, Hohendanner/Stegmaier 2012). Concomitant to the introduction of marginal, part-time work was the reform simplifying social assistance for low-wage earners. Studies show that the number of employees working in marginal, part-time work has increased since 2007, amounting to approximately 30% of the beneficiaries of social assistance (Bruckmeier et al. 2013). Before the

introduction of the minimum wage law in 2013, the clause excluding wages and hours could lead to lower gross wages in the marginal, part-time segment.

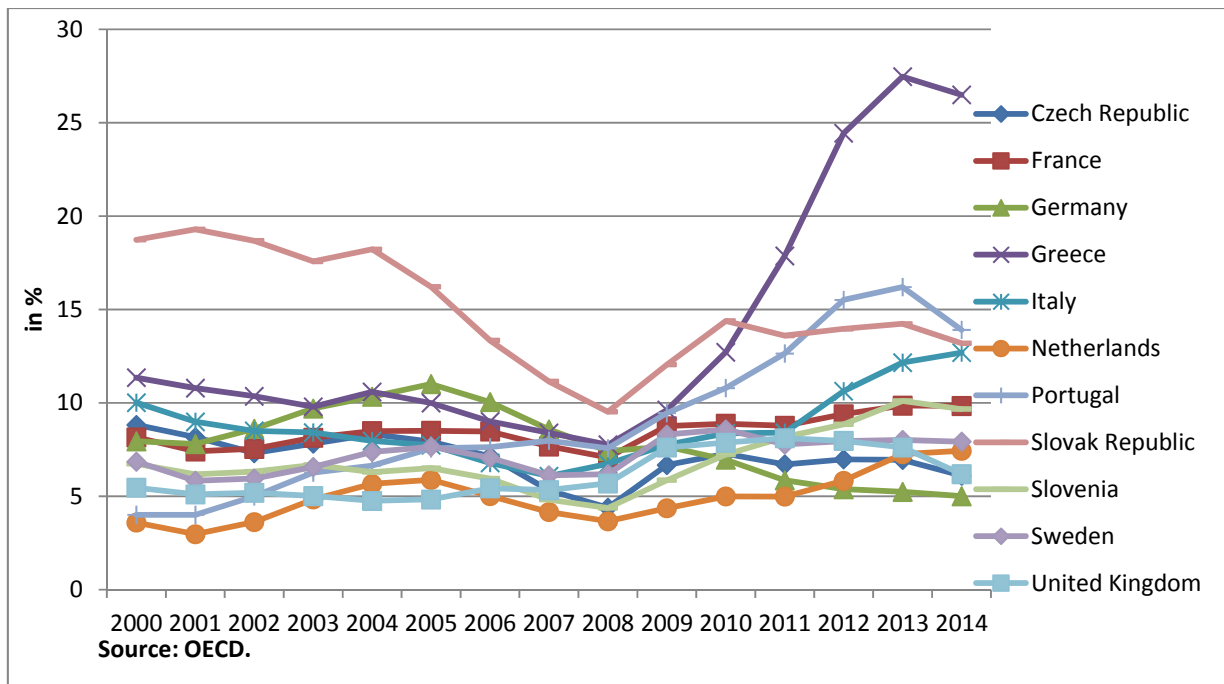
However, the Hartz reforms only marginally touched upon dismissal protection legislation and social protection for permanent and regularly insured employees. The reforms referring to dismissal protection were already introduced during the mid-1990s, narrowing the social selection criteria for fair dismissals. For workers, the maximum duration of unemployment insurance benefits was shortened from 32 months to 24 months. These changes, contributing to an increase in the secondary segment of the market, also created fears that this flexibilisation would contribute to a deterioration of wages and employment stability, although the protection for labour market insiders was hardly challenged. Despite little empirical evidence, these concerns have been readdressed since the mid-2000s and later when the financial crisis opened up the debate on the reregulation of the German labour market.

**Figure 1: Employment rates**





**Figure 2: Unemployment rates**



### 3. Germany during the crisis

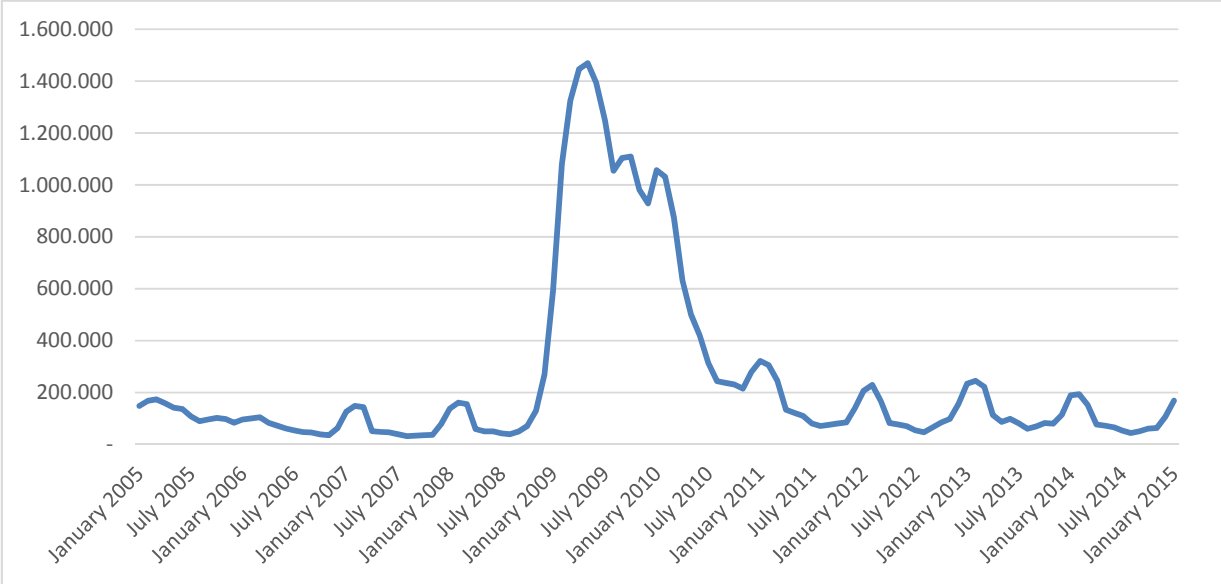
Germany was one of the few countries with declining unemployment and increasing employment during and after the 2008-9 global recession, as figures 1 and 2 show. By now, it is most well-known for its short-time work arrangement, which contributed to the remarkable stability of manufacturing employment during the crisis, which had not been completely predictable by earlier experiences.

In Germany, short-time work has been an established policy instrument for decades, so it was well-known to employers, who had already used it in the past. During the crisis, specific policy action was important, in particular the extension of the maximum duration of short-time work allowance from 6 to 24 months and an increase in the maximum support available to employers. In contrast to the situation up to autumn 2008, employers were entitled to full compensation of social security contributions for hours not worked, starting from the sixth month of short-time work, and from the beginning if training was provided. However, in contrast to the widely shared view, policy reforms regarding short-time work were only one element of internal adjustment. Most of the flexible adjustment via working time reduction occurred at the company level, in particular in the case of reduced overtime work and by using surpluses on working time accounts that had grown for German exporters during the good years before the crisis. This could be done without institutional or policy changes.

All in all, many observers found the smooth development of employment figures in German manufacturing to be quite unexpected. Only a change in employers' behaviour can explain this. German manufacturing employers acted very cautiously during the 2008-9 crisis. Past experience

had taught them that dismissing skilled workers during a temporary downturn can lead to severe skill shortages when demand recovers. This is particularly true in situations of imminent demographic change, which results in smaller cohorts of young workers entering the labour market. In fact, there is evidence that those sectors, in which firms had experienced difficulties in recruiting before the crisis, were the most affected by the crisis, and employers were, therefore, very reluctant to dismiss workers at short notice (Möller 2010). Furthermore, as routine manual tasks had been allocated to temporary agency workers, manufacturing employers could terminate a substantial part of these contracts on short notice as well as not renew some fixed-term jobs (Hohendanner 2010). Hence, the secondary segment of manufacturing workers, on fixed-term and agency work contracts, had to bear a major part of the external adjustment during the crisis – but with the subsequent recovery, employment in agency work picked up again quickly, as shown in table 1. Later on, but earlier than expected by many and stimulated by external demand from outside Europe, regular employment in manufacturing picked up again. Reducing the depth of the value chain in core businesses, while focusing on the most innovative parts, more outsourcing and a longer supply chain, both national and global, can explain this, together with the increased flexibility of employment relations both within the core labour force and the marginal segment. One can argue that the 2008-9 economic crisis led to a dual pattern of adjustment in the German case, with both internal and external flexibility. The general pattern of labour market segmentation in Germany was mirrored during the response to the crisis, as the marginal labour force took a major part of the burden, thus easing pressure on the core workforce, which was also protected by channels of internal adjustment (Hassel 2014; Eichhorst/Tobsch 2013).

**Figure 3: Short-time workers in Germany, 2005-2015**



Source: Federal Employment Agency.

**Table 1: Crisis adjustment in Germany, 2007-2015**

	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015 (forecast)</b>
Real GDP, %	+3.3	+1.1	-5.6	+4.1	+3.6	+0.4	+0.1	+1.5	+1.4
Productivity change per hour worked, %	+1.5	+0.2	-2.6	+2.5	+2.0	+0.6	+0.4	+0.1	+0.5
Hours worked, %	+1.7	+0.9	-3.1	+1.6	+1.6	-0.3	-0.3	+1.4	+0.9
Total employment, %	+1.7	+1.3	+0.1	+0.3	+1.3	+1.1	+0.6	+0.8	+0.6
Total employment, 1,000	40.325	40.856	40.892	41.020	41.570	42.033	42.281	42.622	42.887
Employees covered by social insurance, 1,000	27.134	27.747	27.729	28.008	28.687	29.341	29.713	30.184	30.614
Employees covered by social insurance, %	+2.3	+2.3	-0.1	+1.0	+2.4	+2.3	+1.3	+1.6	+1.4
Unemployment, 1,000	3.761	3.259	3.415	3.239	2.976	2.897	2.950	2.904	2.881
Unemployment rate, %	9.0	7.8	8.2	7.7	7.1	6.8	6.9	6.7	6.6
Temporary agency workers in 1,000	715	761	625	776	882	878	839	n.a.	n.a.
Short-time workers, 1,000	68	101	1.144	503	148	111	124	102	107

Source: Federal Statistical Office, Federal Employment Agency, Fuchs et al. 2015.

## 4. Welfare reforms since 2010: Rather reregulation than austerity policies

In contrast to virtually all other countries, Germany did not adopt severe austerity policies after 2010. Given the robust and improving labour market situation, with the additional revenues collected by the state, a moderate expansion of welfare benefits was implemented, and the last few years have seen a partial reregulation of the labour market. These reforms can be classified as welfare protectionism, in contrast to the welfare adjustment phase in the early 2000s. While reregulatory policies mainly focus on non-standard forms of work and low pay, they indirectly aim at stabilizing the standard employment relationship.

### 4.1 Reregulation of temporary work

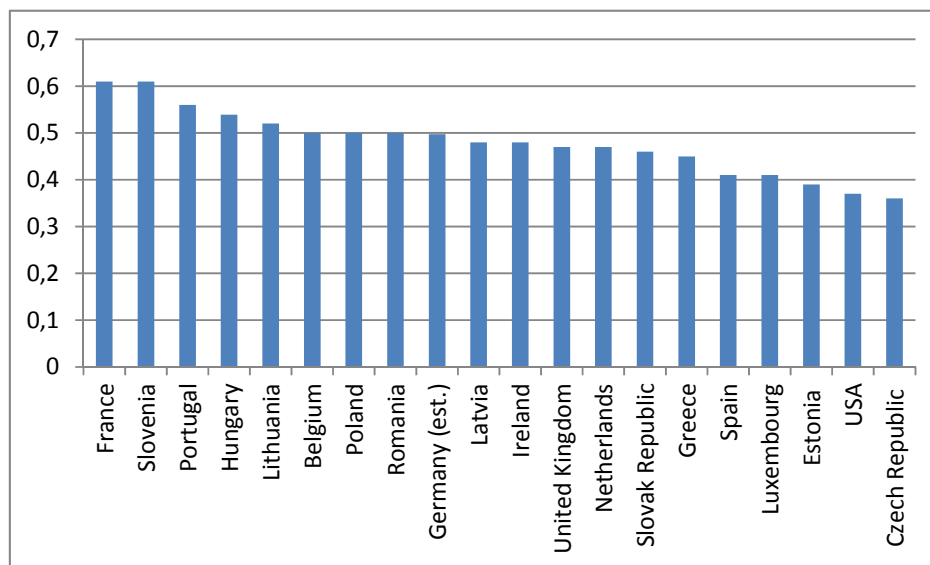
As with fixed-term employment, temporary agency work has also been liberalized progressively over the last few decades, with the most important deregulatory step being taken in 2003. Since then, virtually all restrictions regarding agency work have been lifted, such as the maximum duration of assignments, the ban on synchronicity between employment contract and individual assignments or the ban on rehiring. At the same time, equal pay and equal treatment were laid down by law as a general principle governing the temporary agency work sector. However, deviations were allowed for initial periods of employment after phases of unemployment and, most importantly, by way of collective agreements. This led to a virtually full coverage of the agency sector by collective agreements – however, the wages set were significantly below those of major user sectors such as the metalworking sector (see Baumgarten et al. 2012; Jahn 2010; Jahn/Pozzoli 2013).

While the original intention of promoting temporary work agencies was to strengthen placement capacities for the unemployed, the labour market reforms actually implemented in Germany led to the creation of a peculiar wage gap between direct employees in manufacturing and temporary agency workers performing similar tasks, as wage scales differ and assignments can be made for an indeterminate period of time. This has led to competition between directly employed staff and agency workers, in particular in the low and medium-skilled segment of manufacturing. Where trade unions and works councils were strong, they could achieve agreements with employers on a step-by-step closure of the wage gap, by way of earnings supplements and on a better transition from a temporary agency work contract to a direct employment relationship with the user company (Spermann 2013). As these changes cannot be established on a general basis throughout the German labour market, due to the weakness of trade unions in some sectors, the current government has announced a reregulation of temporary agency work by law in the near future. This would mean the reintroduction of a maximum assignment period of 18 months and equal pay after nine months of service with a user company. Agency work would then be more restricted again, compared to the situation in the recent past.

## 4.2 Introduction of the minimum wage

By the beginning of 2015, Germany had introduced a statutory minimum wage of €8.50 gross per hour, about 50 percent of the median wage, which is in the medium range of EU Member States' minimum wages (see figure 4). The introduction of a general minimum wage is certainly the most important labour market reform of the current decade so far. It is remarkable that Germany now has a minimum wage that basically covers all workers and that it was introduced without much political struggle with the current government, as it was backed by all major parties and the trade unions as well as a large share of the electorate. The introduction of a minimum wage in Germany can only be understood when taking into account the prior history of collective bargaining and low pay sector expansion.

**Figure 4: Minimum wage in percent of median wage of full-time workers, 2013**

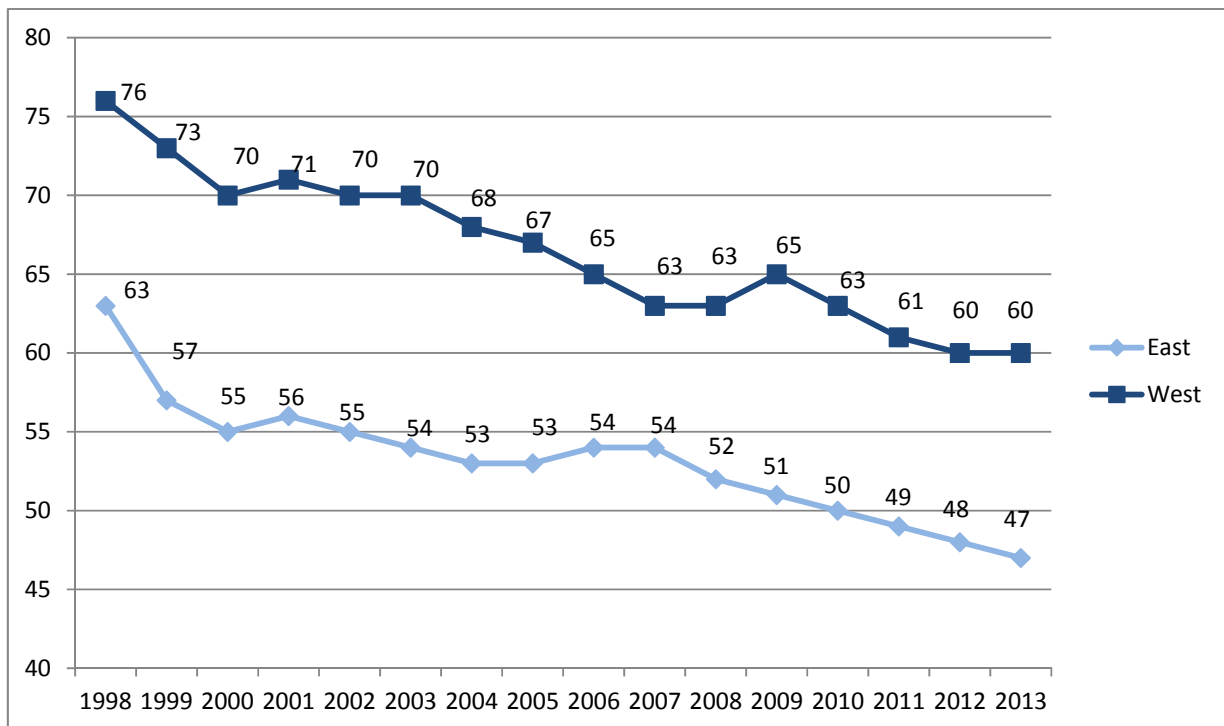


Source: OECD online database, estimated value for Germany.

For many decades, trade unions in Germany were not interested in having a statutory minimum wage, as collective bargaining coverage was high enough to regulate wages in major parts of the labour market. Over the last 20 years or so, this has changed: first, with lower and declining bargaining coverage rates in East Germany and second, with a general problem in establishing wage agreements in major private service sectors (see figure 5). With the move towards a more flexible labour market in the early 2000s, this led to a massive increase in wage dispersion and low pay employment shares. Collective bargaining was not able to reverse this trend, as

bargaining structures were either nonexistent or too weak in many of the crucial segments of the labour market. This led to growing public attention to low pay and to a reversal of the position of major trade unions, in particular those representing service sector occupations. As a consequence, they started campaigning for a statutory minimum wage, an initiative supported by the Social Democrats. Even before the adoption of the national minimum wage, more and more collectively agreed minimum wages (where they could be set) were extended, in order to cover non-organised employers and employees.

**Figure 5: Collective bargaining coverage, in percent of all workers**



Source: Hans Boeckler Foundation Tarifarchiv.

Regarding the statutory minimum wage, there are a few exemptions, in particular interns, young people below the age of 18, apprentices and the long-term unemployed for a maximum of six months after taking up a job. Furthermore, transitory exemption clauses exist for seasonal workers and for those sectors where there are binding collectively agreed minimum wages below €8.50; they only have to apply the statutory minimum wage of €8.50 by 2017. While the initial minimum wage level was set politically, and basically reflects the position of the trade unions, in the future, a bipartite commission of employer associations and trade unions will negotiate the adaptation of the minimum wage, taking into account the development of collectively agreed wages and the situation in the labour market. Academic experts will be consulted.

The minimum wage will certainly change the rules of the game in some segments of the German labour market. Occupations, regions and employment types dominated by low wages will be strongly affected. This holds true in particular for activities such as hairdressing, taxi driving,

waiters, for smaller establishments, for East Germany and for marginal, part-time work (Arni et al. 2014). Although it is still too early to have gathered any evidence on the effects of a minimum wage, we can expect a mixture of employment restructuring, maybe some job losses, with price increases and a certain tendency to circumvent the minimum wage, e.g. by informal unpaid overtime or by moving to freelance or self-employment. In a more general perspective, the minimum wage will certainly reverse some of the wage dispersion trends observed in Germany over the last ten years or so, in particular in service occupations relying on mini-jobs.

**Table 2: Low pay below the minimum wage in Germany**

<b>Employees... (ordered by share level)</b>	<b>Share of concerned employees</b>	<b>Average required wage increase to match minimum wage</b>
In marginal employment	58	43
Aged up to 24 years	37	45
In firms with 4 employees or less	35	44
With few or no qualifications	35	41
In East Germany (and Berlin)	23	39
	⋮	
In firms with 2000 employees or more	8	33
In full-time employment	8	27
In financial services	4	31
With high qualifications	3	39

Source: Brenke 2014.

### **4.3 Activation, income maintenance and long-term unemployment**

Changes to the labour market and social policies were at the heart of the government's agenda in 2003. The Hartz reforms I-IV changed not only the institutional structure of the Federal Labour Agency and the interplay between local level poverty relief and national unemployment insurance, but also the general policy approach towards mobilizing the long-term unemployed. While in the past, skilled workers were largely protected from the expectation to retrain and were rather encouraged to keep their primary skills in a particular trade during spells of unemployment,

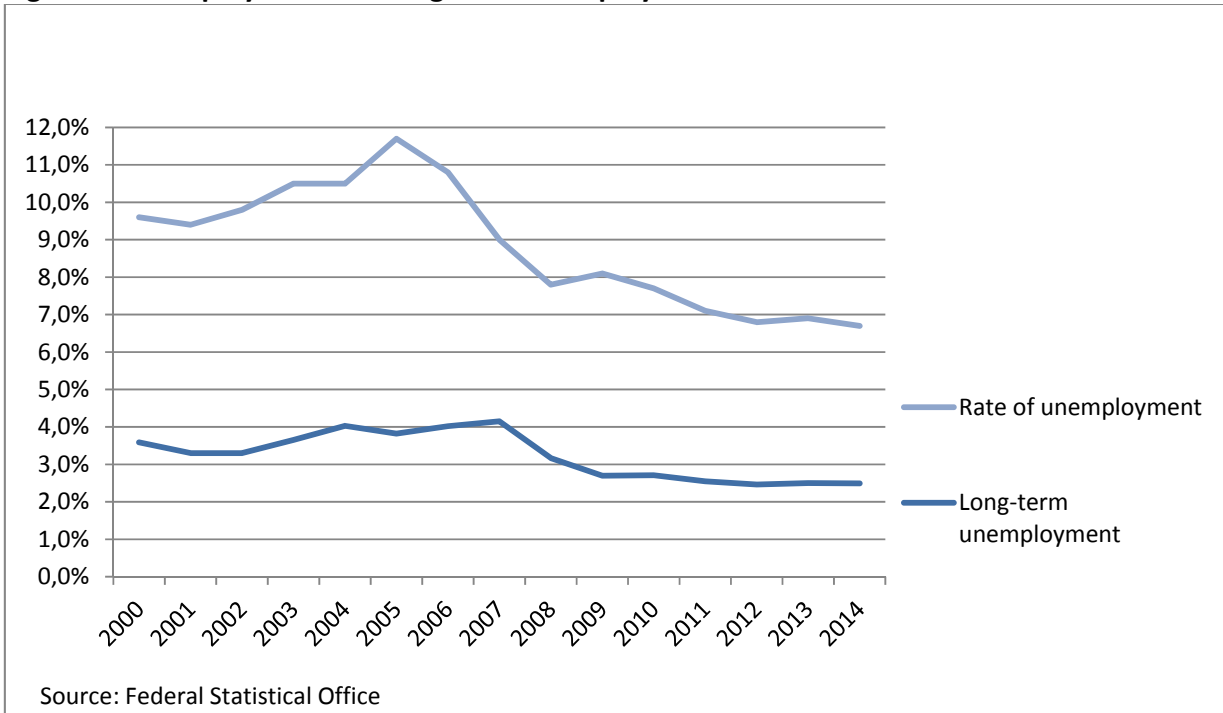


the emphasis shifted to retraining and getting back to work more quickly if they were about to become long-term unemployed after one year (Hassel and Schiller, 2010). In particular, the focus was on the activation of the (long-term) unemployed through a cut in benefits for long-term recipients of unemployment assistance, mainly relevant in East Germany, and an increase of activation efforts towards job searches, also in less attractive segments of the labour market. The reform of the unemployment insurance system involved a cut in benefits for the long-term unemployed who moved to social assistance levels after a period of 12 to 18 months of unemployment. This had a psychological effect on those at the risk of being transferred to social assistance. At the same time, a kind of negative income tax was introduced by enabling workers with low-paying, part-time jobs to draw benefits to make ends meet. These reforms were highly contentious at the time they were introduced yet, despite some political pressure from the left, they have not been reversed. Amendments addressed many details, however, affecting both welfare benefits and activation measures.

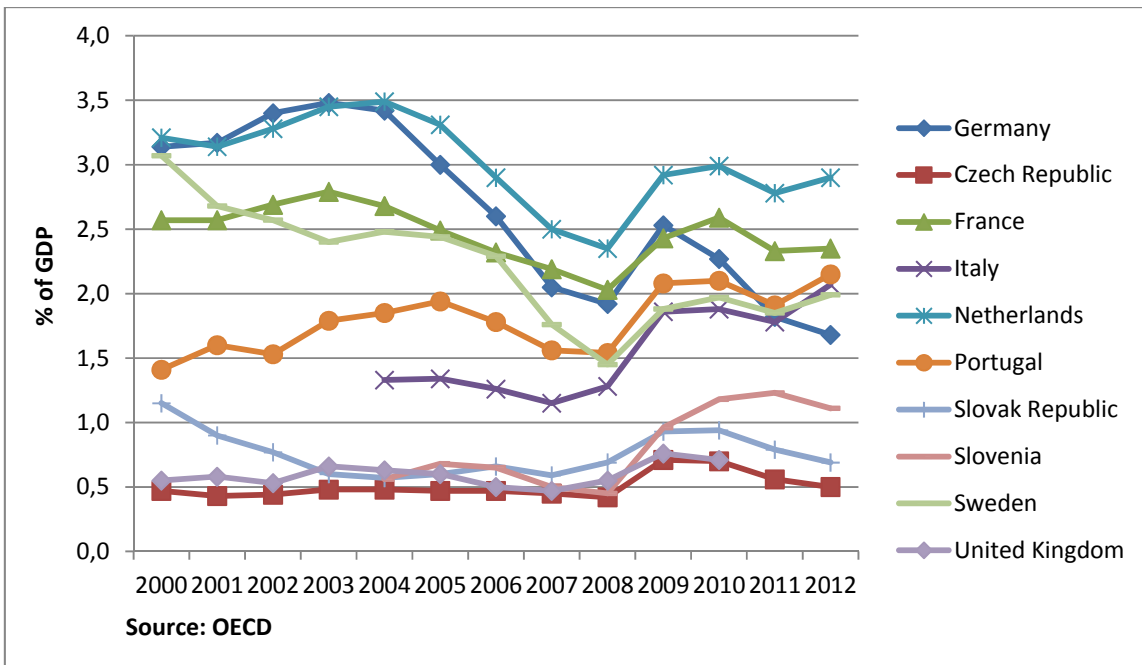
One of the most debated issues concerns the generosity of the minimum income support scheme in Germany, both for adults and children. The method for setting the benefit level was challenged politically and legally, resulting in a judgment of the Federal Constitutional Court in 2010. This led to a refinement of the calculation, as laid down in formal legislation, but not to a general change of the system. There has neither been a major retrenchment nor an increase in benefit generosity. For adults, minimum income support is determined based on the consumption patterns of low-income earners, allowing for some arbitrary adjustment. For children living in needy households, the new rules resulted in a slight increase in benefit levels. In addition to cash benefits to cover the cost of living, the German minimum income support scheme covers appropriate housing and heating as well as specific needs and support for school children. The evolution of the level of minimum income support in Germany is related to the development of net earnings and consumer prices, so that welfare benefits can keep pace with them.

What has changed over time is the number of benefit recipients, both under the unemployment insurance and the minimum income support scheme.

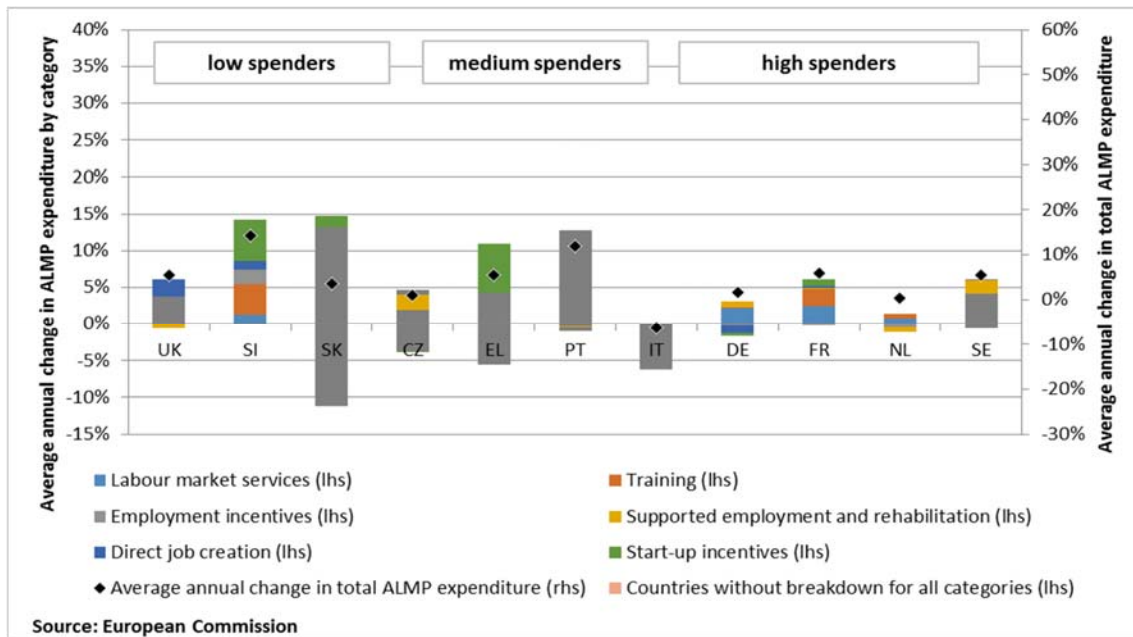
**Figure 6: Unemployment and long-term unemployment**



**Figure 7: Expenditure on ALMPs as a percent of GDP**



**Figure 8: Expenditure on passive labour market policies as a percent of GDP**



Some issues remain: one is the relatively large group of people combining income from work with receipt of social assistance. About 1.3 million have some income from work, but do not leave the benefit system. While, at first glance, this suggests a large number of working poor, the actual situation is not unambiguous, as the majority of those ‘working unemployed’ work part-time, so that their income from work is under no circumstances sufficient to raise them above the breadline. Here, the main issue is that some people only have very weak incentives to move from part-time work, or marginal part-time work, to longer working time, in particular full-time work.

The most important reason for that is that the policy is based on an earnings disregard clause that allows minimum income support beneficiaries to earn a limited amount before benefits are withdrawn; hence, increases in earnings would result in a progressive loss of benefits without any improvement in net income. The second concern is the lack of child care support and other services for those taking care of children, in particular single parents, who rely on minimum income support to a very large extent. Of course, there are also full-time workers receiving additional benefits, in particular if they have large families. Data show, however, that their hourly wages are not particularly low.

The second major issue is the persistent problem of unemployment. The improvement of the labour market situation in Germany since mid-2005, even during and after the 2008-9 crisis, has

helped reduce unemployment, including long-term unemployment, as figure 6 shows. However, the most disadvantaged have not benefited that much from the stronger demand for labour. This is the most difficult task: to integrate the remaining long-term unemployed into gainful employment, as they lack the relevant skills and work experience, have health problems or other obstacles to employment. It would require tailor-made services addressing the specific needs of the target group, and, formally, the German legislation on active labour market policies for the long-term unemployed allows for a very flexible use of different instruments, including training, hiring incentives for employers, job search assistance, personalized assistance and work experience programmes. Yet, there seem to be significant issues with the implementation of such policies (Spermann 2014). A reform in 2011 has simplified and reduced the number of instruments, allowing for a more flexible use in local offices of the public employment service, but this reform also resulted in a reduced available budget for those most dependent on support (see figures 7 and 8), affecting, in particular, public employment schemes and start-up support (Gesetz zur Verbesserung der Eingliederungschancen am Arbeitsmarkt).

Currently, a new initiative to combat long-term unemployment is under debate, including employer subsidies, an integration pathway via part-time work and personal assistance to the long-term unemployed. There has also been a debate about limiting the use of negative sanctions. Negative sanctions are only one element among others, and they are certainly not the best way to address the most vulnerable groups.

#### 4.4 Vocational training

The Vocational Training (VET) system ‘appears to be undergoing a period of subtle but significant change’ (Thelen and Busemeyer, 2012, 89). Vocational training is still the dominant form of training after secondary education, with more than 50 percent taking up some form of apprenticeship. It is a highly structured approach towards training, in which firms employ apprentices and train them on the job; they also attend school for part of the time. The licensing of training, the content and the examination of apprentices are organized and supervised by the local chamber of commerce. German-style vocational training has always been seen as a highly successful way of training young school leavers below the level of tertiary education. It has consistently produced low levels of youth unemployment and high levels of specialized training.

During the 1990s and 2000s, three main developments have created pressure within the vocational training system (Thelen and Busemeyer, 2012, 76-78): first, the share of firms that engage in vocational training declined from 35 to 25 percent, which reflected the downswing of the business between the mid-1990s and the mid-2000s. Second—and related to the decline of firm participation—the demand for training by school leavers could not be met. Young school leavers at the lower end of school qualifications found it increasingly difficult to find training places. As the German government is committed to providing training up to the age of 18, many of those ended up in a kind of ‘transition system’ (Baethge et al., 2007) of state-sponsored training. Third, the attitude of large firms towards the training needs of school leavers has changed. While in the past, firms increased training capacities beyond their business needs in order to meet demand, this form of corporate social responsibility has significantly declined over

the last decade. Firms are more reluctant to train just in order to fill the gap. Outsourcing, restructuring and fierce competitive pressure have introduced a new emphasis on cost-cutting that does not allow for voluntary training.

With regards to policy change, some incremental adjustments were made. In particular, shorter training courses (two-year apprenticeships) were introduced and some of the content was removed. The government also introduced short training courses for school leavers with low skills. As school leavers increasingly either drop out of low-quality training or cannot meet the expectations of high-quality training, a school-based training regime evolved alongside the firm-based VET system. The content of apprenticeships has also become more modular and flexible. Some of these developments took place in the context of increasing Europeanization in training standards. Even though training is not part of the core EU competencies, the European Qualifications Framework has introduced a credit system which should make VET in Germany more compatible with other countries.

While, on the whole, we can see institutional stability, many training features and content are markedly different today, compared to the beginning of the period. However, given the onsetting, rapid demographic change and rapidly declining numbers of school leavers, there is an expectation among policymakers and firms that the remaining school children will increasingly be pushed towards higher levels of training (Thelen and Busemeyer, 2012).

In 2014, the German vocational training system was repeatedly discussed in policy circles as well as in public debates. Various observers perceive the system to be in a crisis, because both the number of training contracts is decreasing and the number of young people without an apprenticeship is growing. At the same time, employers complain about unsuitable applicants and unoccupied vocational training vacancies. The most recently published Annual Report on Vocational Education by the Federal Government in April 2014 notes a decline in training contracts by 20,000 to 530,000.

The government and social partners responded by forming an "Alliance for Education and Training" (Allianz für Aus- und Weiterbildung), consisting of political representatives from the national and state level, trade unions and employers. The Alliance is the successor to the "National Pact for Training and Skilled Manpower Development" (Nationaler Pakt für Ausbildung und Fachkräftenachwuchs). It agreed on various measures to improve the situation in vocational training. One of the objectives is to create additional vocational training positions. Moreover, it introduced a programme called "Assisted Training", which supports weaker candidates in finding an apprenticeship and finishing their training successfully.

Although some problems of the educational system are currently noticeable, the overall diagnosis of a "crisis" should be handled more carefully. In the past, there have been repeated phases in Germany, in which the number of vocational training positions has been decreasing. Moreover, in the vocational training and labour market, imbalances between supply and demand occur on a regular basis. Due to the regional distribution of open positions and the limited geographical mobility of potential applicants, it could be the case that vacant apprenticeships in South

Germany confront young people from East Germany, who haven't found training positions. In addition, there are significant differences in the ratio of vacant training positions and applicants between different professions. International comparisons indicate that the German vocational training system generally works well and generates very low youth unemployment. It prevents polarized structures of low-skilled school and university graduates, as exist in Spain, for example. Vocational training offers a good entry into the labour market and career opportunities in professional curricula, decent working conditions and promising perspectives for permanent employment, ensuring financial security and an acceptable standard of living. Hence, this path of professional qualifications is generally valued among employers and within society.

However, the vocational training system is currently shrinking and losing an increasing share to higher or academic education. More and more school graduates decide against vocational training and for a university degree. This is, on the one hand, problematic because, for example, artisanal professions face increasingly difficult challenges in finding prospective candidates and endanger, at some point, jobs and businesses. On the other hand, industries and large companies primarily employing university graduates welcome, and actually require, increasing levels of academic training in employees. However, since the prerequisites in many occupations for vocational training are constantly increasing, weaker candidates, for which universities are not an option, also have difficulties in finding a vocational training position. The background to these developments is a structural change within the economy towards more complex tasks and higher qualifications.

The problems could be addressed through minor changes and a better connection between the two systems: if more combinations between training and university would be offered and universities would be more available for training graduates, this would improve the attractiveness of the vocational training system. Future trainees would benefit from double degrees, further education, practical experience and improved possibilities of job and career entries. Companies would benefit by filling vacant training positions, qualified trainees and their embedding into the companies. In addition to improving the link between vocational training and higher education, weaker candidates looking for an apprenticeship should be individually counselled and supported, even if this entails financial support from employment agencies. The strengths of young people should be determined and linked to matching vocational training positions. At the same time, it is important that working conditions in occupations with low numbers of applicants and high drop-out rates - as in the hotel industry and the gastronomy - are improved by adjusting wages or working time. Finally, guidance and information on vocational training before and after graduating high school could be improved. Only through realistic information about the requirements at university and vocational training, and the respective professional opportunities, could wrong decisions and the resulting drop-out rates be reduced. Although existing programmes placing university drop-outs into apprenticeships are feasible, these initiatives are diversions that cost money and time and should be prevented in the first place.

However, political target setting to increase the number of vocational training positions should be evaluated critically, as they might result in the artificial creation of jobs without a necessary

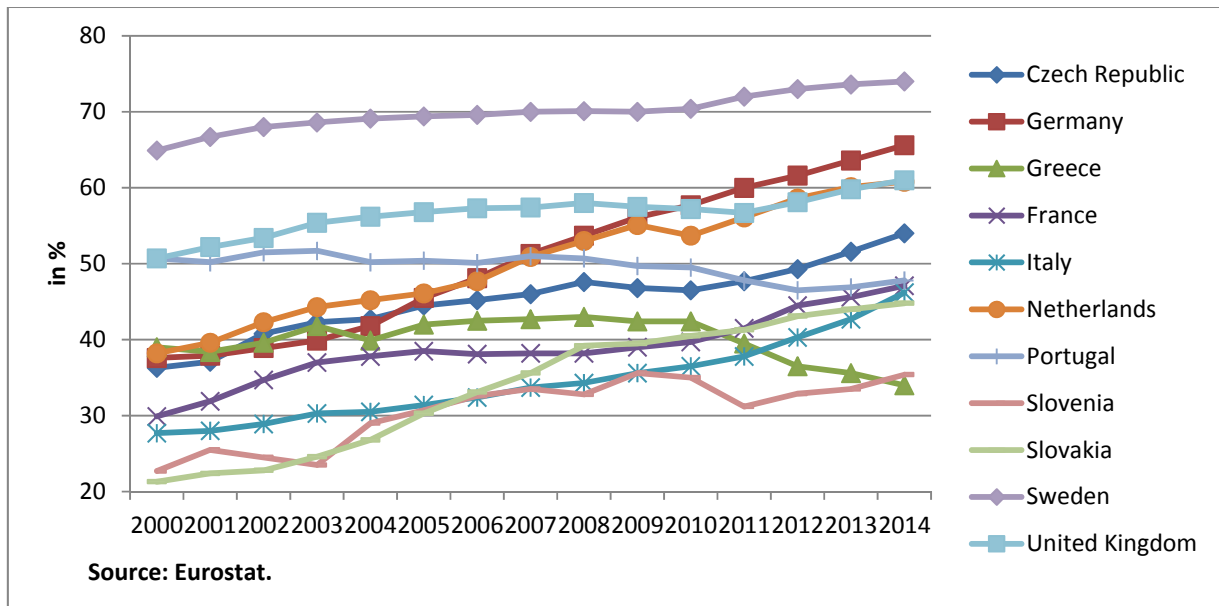
long-term perspective. The market of vocational training is rather a market to be controlled by the social partners as well as the apprentices.

Although the German system of vocational training seems to be in a crisis, the extent is still limited. It remains attractive for many businesses to employ apprentices, as these are often motivated and productive, do not cause large costs and potentially stay in the firm in the long term. Through the proposed reforms, this interest could be strengthened. In addition, the focus of young people can be increasingly redirected to vocational training as an education system with benefits. Presumably this will be achieved in particular through mixed forms of vocational training and academia. In addition to a merger of these two systems, permanent shifts in the size and importance of the individual systems would eventually be acceptable as long as, in the final outcome, enough young people are professionally qualified.

#### **4.5 Bringing early retirement back in**

Germany had adopted a long-standing path towards later retirement since the late 1990s, basically abolishing all options of a generous early exit from the labour market e.g. publicly subsidized old-age, part-time work ('Altersteilzeit') and moving the statutory retirement age step-by-step to 67. This policy was phased in in 2012 and mainly affects younger and prime-aged workers. It was primarily seen as a policy to stabilize the public budget, both with respect to the first pillar of pension insurance and to the tax-funded general budget, as well as to avoid the premature loss of skilled labour in a rapidly ageing economy. As regards labour market performance, since the late 1990s, the employment rate of older workers has increased significantly in Germany and much more strongly than in many other European countries, as figure 9 shows.

**Figure 9: Employment rate of workers aged 55-64**



As companies could not shed older workers as smoothly and cheaply as before, and as they had a stronger need to continue employment to a later stage in life, the rise in employment rates of older workers was mainly driven by the longer tenure of workers who would have retired earlier in the old regime. Despite some criticisms raised by trade unions and welfare associations, the general paradigm shift seemed to be largely accepted. Against this backdrop, a quite unexpected policy change occurred. After the last general election in 2013, Germany introduced a new form of early retirement, namely the option, for those born in 1952 and earlier, to receive a full pension without any deduction when retiring at the age of 63, after at least 45 years of employment with pension insurance contributions. For younger people, this would be smoothly phased out again. This reform was mainly pushed for by the German trade unions in association with the Social Democrats, as a policy to pave the way to an early exit for a core group of trade union members, i.e. skilled workers with a vocational training degree and long employment biography. This can be seen as the most explicit case of welfare protectionism, favouring labour market insiders. The Christian Democrats did not oppose this, given the general popularity of early retirement policies in a situation of apparently affluent public revenues, on the one hand, and the need for political support for their own pet project: a pension bonus for mothers. Retirement at 63 increases the generosity of the public pension scheme. It leads to a loss in revenues from taxes and pension contributions and to additional expenditure within the welfare state. Implicitly this is a



redistributive policy, from those not fulfilling the requirements of retirement at 63 to those who can benefit, i.e. medium-skilled workers with long employment experience and a decent wage who are mostly active in manufacturing or the public sector. Those with a shorter or more unstable employment biography do not have access to this specific arrangement. In fact, since the legislative change, more older workers have applied for early retirement than was initially expected. Up to spring 2015, about 300,000 have filed for a pension at 63, implying a significant decline in the employment rate of those aged 63 to 65.

## 5. Conclusion

Our paper tries to assess the existence and the extent of austerity-oriented policies in Germany in the aftermath of the 2008-9 recession. In contrast to the intensive phase of labour market and welfare state reforms in the context of the Hartz reform package that pointed towards 'welfare readjustment' during the early 2000s, we do not see a clear pattern of austerity policies in Germany. In general, the path that was adopted earlier was continued after 2005 and also during and after the crisis. This holds for the deregulated situation of non-standard contracts such as marginal, part-time work and temporary agency work as well as the activation policies addressing both short-term and long-term unemployed people. The stability of policies can be explained by the economic conditions which were, and still are, much more favourable than in many other EU Member States. Hence, apart from some cuts in active labour market policies, we cannot see welfare state retrenchment. Most recently, we can identify a partial reregulation of the labour market, most notably the introduction of a national minimum wage, a potential increase in the regulation of non-standard contracts and a reintroduction of early retirement for labour market insiders as well as the potential expansion of active labour market policies. These policies can be classified as mostly 'welfare protectionist'. The reregulation of the low pay sector and non-standard contracts, while directly addressing the more disadvantaged groups of workers, also limits pressure on wages and working conditions of the core of the labour market.

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**Table A1: Labour market developments in Germany, 2000-2014**

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Employment rate (15 to 64 years)	65.6	65.8	65.4	65	65	65.5	67.2	69	70.1	70.3	71.1	72.5	72.8	73.3	73.8
Unemployment rate (15 to 64 years)	8	7.9	8.7	9.8	10.5	11.3	10.3	8.7	7.5	7.8	7.1	5.9	5.5	5.3	5.0
Full- time equivalent employment rates of men and women															
In Total	65.6	65.8	65.4	65	65	65.5	67.2	69	70.1	70.3	71.1	72.5	72.8	73.3	n.a.
Men	72.9	72.8	71.8	70.9	70.8	71.3	72.8	74.7	75.8	75.4	76	77.3	77.6	77.7	n.a.
Women	58.1	58.7	58.9	58.9	59.2	59.6	61.5	63.2	64.3	65.2	66.1	67.7	68	68.8	n.a.
Employment rates by age group															
15 to 64 years	65.6	65.8	65.4	65	65	65.5	67.2	69	70.1	70.3	71.1	72.5	72.8	73.3	73.8
15 to 24 years	47.2	47	45.7	44.2	41.9	41.9	43.5	45.4	46.6	46	46.2	47.9	46.6	46.8	46.1
25 to 54 years	79.3	79.3	78.7	77.9	78.1	77.4	78.8	80.3	80.9	80.8	81.5	82.8	83.2	83.3	83.5
55 to 64 years	37.6	37.9	38.9	39.9	41.8	45.5	48.1	51.3	53.7	56.1	57.7	59.9	61.5	63.5	65.6
Employment rates by educational level															
All levels	65.3	65.7	65.4	64.9	64.3	65.5	67.2	69	70.1	70.3	71.1	72.5	72.8	73.3	73.8
Pre-primary, primary and lower secondary education	55.3	44.9	43.6	42.6	40.7	42.3	44.1	44.8	45.6	45.3	45.4	52.7	52.7	53.2	46
Upper secondary and post-secondary non tertiary education	69.9	69.9	69.8	69	68.2	69.4	71.2	73.1	74	73.9	74.7	76	76.4	76.9	77.7
First and second stage of tertiary education	83	83.2	83	82.9	82.6	82.8	84.2	85.3	85.7	86.3	86.7	87.6	87.6	87.5	87.7
Unemployment and Long-term Unemployment															
unemployment	8	7.9	8.7	9.8	10.5	11.3	10.3	8.7	7.5	7.8	7.1	5.9	5.5	5.3	5.0
long- term unemployment	4.1	3.9	4.2	4.9	5.9	6	5.8	4.9	4	3.5	3.4	2.8	2.5	2.4	2.2

Source: Eurostat.