

MUTUAL LEARNING PROGRAMME:
PEER COUNTRY COMMENTS PAPER GERMANY

**‘Kurzarbeit’ – the revival of
a traditional labour market policy instrument**

Peer Review on “Employment measures to tackle the economic downturn: short time
working arrangements / partial activity schemes”

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A paper submitted by
Kurt Vogler-Ludwig (Economix Research & Consulting)
in consortium with GHK Consulting Ltd and CERGE-EI

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1 LABOUR MARKET SITUATION IN THE PEER COUNTRY

This paper has been prepared for a Peer Review within the framework of the Mutual Learning Programme. It provides information on Germany's comments on the policy example of the Host Country for the Peer Review. For information on the policy example, please refer to the Host Country Discussion Paper.

Regulation

Short time work (STW) in Germany can be dated back to 1910 when the potash industry was restructured. It has played an important role ever since, particularly during economic downturns. In the recent economic crisis it became a major instrument of employment policies.

There are three types of short time work:

- cyclical STW to compensate cyclical downturns;
- seasonal STW to reduce the effects of seasonal fluctuations in labour demand;
- transitional STW to help the restructuring of the labour force.

This paper is on cyclical STW only.

Eligibility for cyclical STW is regulated in the Social Code III (SGB III, § 169 ff.). Companies can apply for STW benefits if (parts of) their workforce face a reduction of gross wages of more than 10%. The envisaged loss of employment has to be substantial and unavoidable, but transitory.

All employees subject to unemployment insurance are covered by the programme, including agency workers. Working time reductions can range between -10% and -100%. The support is provided for a maximum period of 18 months.

Employees receive 60% to 67% of the wage reduction as benefit. The higher rate is for beneficiaries with children.

Employers have to pay full social security contributions for short-time workers but – according to recent regulations – receive 50% of the employers' share as subsidy. This is around 10% of the gross wage reduction. If STW lasts for more than six months or if training is provided during STW which last at least 50% of the reduced working time, employers receive 100% of the social security contributions for STW.

STW is part of unemployment insurance. Companies apply for STW at their regional labour office of the Federal Labour Agency. The application has to include a statement by the works council as far as this exists.

Impact

The strong reduction of GDP, which culminated at an annual change of -7.1% in the second quarter of 2009, was only translated into a minor decrease of employment around -0.3% in the following quarters (see Chart 3). This was mainly achieved by the reduction of working hours which peaked at -5.1% in the second quarter of 2009. In the following quarters, working hours started to recover rapidly and increased by a year-on-year rate of 1% in the first quarter of 2010. This shows the great importance of working time flexibility in the course of the crisis.

STW has proved to be an efficient labour market policy instrument. However, in this context, it was only one of the instruments. It financed the reduction of working time (by 32.5%) for 1.5 million short time workers at the maximum. This amounts to 4% of all employees, and their working time reduction contributed only 1.4 percentage points to the

total reduction of working time. This is only one seventh of the decline in working times between III/2008 and II/2009.

Why has STW been so important for the stabilisation of employment? There are several reasons:

- The measure concentrated on those industries and companies which needed public support most urgently. Mechanical engineering, the car industry, and metal production were among the sectors using STW frequently. Moreover, it concentrated on medium and big companies.
- It compensated the reduction of working hours rather than jobs in general or companies in trouble.
- The measure requires financial contributions by employers and workers. The selection of companies and of jobs within the company, for which STW is requested, is therefore restricted: from the employers' side as they have to pay parts of the social security contributions and other benefits for short time workers; from the workers side as they lose parts of their income (see Chart 2).
- More generally, the measure is a temporary insurance against unemployment helping companies to preserve their staff and giving staff at risk the perspective to stay in employment.

The German STW programme therefore appears to have strong multiplier effects. The financial offer of public unemployment insurance to support jobs at risk worked as a trigger for further adjustments. Companies avoided redundancies by cutting overtime, the expansion of part-time work, the use of working time account buffers, and even wage cuts. Workers largely accepted these measures in the face of the crisis. Moreover, companies stopped recruitment, reduced costs and expanded marketing activities. Nevertheless, rising labour unit costs and declining profits were accepted by shareholders and owners. As a result, only 11% of the German companies which saw themselves as being affected by the crisis, made workers redundant as a response to the crisis¹.

The strong preference of German companies for keeping workers in their jobs, is related to the experiences during the previous upswing. During this long growth period German companies restructured in many respects: product portfolios, production technologies, organisation of work, international labour division, etc. This had strong effects on the composition of skills and competences of the workforce which – by itself – was the major source of efficiency gains and company profits. For the first time, therefore we got the evidence of human-capital driven growth which brought the skills and competences of the workforce into the centre of economic competition.

Having a clear understanding of this context, companies in Germany were very sensitive about disturbing the efficiency of their work organisation by making workers redundant. They also had the experience of rising skill shortages in 2007 and 2008 and thus feared recruitment problems in the following upswing. Thus they invested into the preservation of their staff even at the expense of lower short-term profits. Another reason why the STW programme was successful relates to the expectation of a short recession. Policy actors, managers and workers, were convinced that there would be a rapid recovery. This was due to the former experience of improving international competitiveness which supported the feeling of a strong 'real' economy. But it also has to be addressed to the determined policy commitments included in the public anti-crisis programmes. The high employment level which resulted from these reactions avoided the panic of rapidly increasing unemployment and kept consumer trust at high levels. Together these circumstances created a positive

¹ The type of company adjustments to the crisis were surveys within the German Job Vacancy Survey in II/2009. More detailed results are published in Heckmann, Kettner, Pausch, Szameitat, Vogler-Ludwig (2009): Wie Betriebe in der Krise Beschäftigung stützen. IAB-Kurzbericht 18/2009.

long-term perspective which gave a good reason for accepting short-term losses. STW therefore appears to be important as a measure to improve the general economic climate rather than preserving a great number of jobs. In this regard, the German programme has been very efficient.

2 ASSESSMENT OF THE POLICY MEASURE

The French situation appears to be different. As the Host Country Report reveals, companies used 'almost all the tools at their disposal to cut costs' rather than reducing working times substantially. The adjustment of labour input to the comparatively moderate GDP decline was mainly achieved by the reduction of fixed-term contracts, agency work and regular employment. The full-time equivalent of overtime work decreased only marginally (-6%) while agency work shrunk by 25%. With such a cost cutting strategy, French companies did not allow labour unit costs to rise or productivity to decrease to the same extent as in Germany. Similarly profit shares did not decline in parallel to other countries.

It can be assumed that the institutional and regulatory environment plays an important role. The French minimum wage regulation, the working time act, and other legal settings create a different framework which may not allow for internal adjustment strategies – or reduce the incentives to select such strategies.

A second reason may be found in the segmentation of the labour market which is mentioned in the report. This appears along two major dimensions. One dimension is the segmentation of peripheral jobs in fixed-term contracts or agency work from core jobs in open-ended contracts. The other dimension is the segmentation of subcontracting firms from their main contractor. Both forms raise the speed of labour adjustment by externalising risks. Fixed-term contracts are not renewed, agency work is stopped, and subcontracts are cut. Such adaptation strategies improve the flexibility at least in the dependent segments of the labour market, but weaken the long-term orientation of these economic actors. As the dependent segments have to carry a heavier adjustment load compared to the core segments, the chances to survive a severe crisis are much lower than under the condition of a more or less equally distributed adjustment pattern.

The host country report also refers to the observation of labour hoarding, particularly among larger companies (page 5). This however came to an end in mid 2009. It would be interesting to know why this happened. One explanation might be that cost cutting measures – including working time adjustments – were not sufficient to preserve jobs. As a result companies switched to job cuts. Another explanation may be found in medium-term business expectations. If companies did not have the perspective of a speedy recovery, adjustments in the number of jobs appeared unavoidable.

The French STW regulation seems to be complicated. Three different levels were distinguished, and as far as can be understood, the amount of public support to employers is uncertain. For example, the third level regulation mentions that the allowance paid by the employers '...can be partly funded (50%) by the government below a certain ceiling, which is very often exceeded' (page 7). This appeared to be a rather vague perspective for an employer who wants to use this instrument. With this experience, French employers might be cautious in using the new regulation (APLD).

It can also be questioned whether the new regulation is generous. According to table 1, employers pay 58% of the employee compensation during STW if the employee earns 1.5 times the minimum wage. The remaining 42% comes from government subsidies. This appears to be a substantial burden as the employer would save 100% if he makes the

worker redundant.² These facts may be one of the reasons why STW did not achieve a high level in France and why STW expired rapidly in 2009.

3 ASSESSMENT OF THE SUCCESS FACTORS AND TRANSFERABILITY

STW is not a panacea for business downturns. Its usefulness strongly depends on the economic perspective, in particular how long the recession can be expected to last. STW makes sense only in the short term. If there is a need for long-term restructuring of the economy and of labour markets, STW would be counterproductive and wasted money. If STW support is granted for too long, it may hamper economic restructuring and preserve less competitive jobs. The German 24 months which were applied during the first phase of the crisis appear to be significantly too long. As the statistical data show, such long support periods are only used by a minority of companies (Chart 4).

Long-term perspectives however, are the matter of companies rather than policies. Companies have to assess the rationale of preserving staff or cutting jobs. This is best guaranteed if public money covers only parts of the overall costs. A relevant contribution has to come from the employers. This sets the right incentives to keep STW short and select only those companies and workers who need public support.

Nevertheless, the experience shows that employers strongly react to the level of subsidies. This was the case in Germany where the government previously set the rule that employers have to pay social security contributions for the short time workers. STW did not play an important role during that time. In the moment however, when the rule was changed and the government supported social security payments, the revival of the STW started. In France, the employers also reacted positively to the new regulation and extended the use of STW. The substantially higher cost burden for employers in France compared to Germany, may explain the lower rate of short time workers and the shorter STW periods.

The trade-off between a low financial share of government support and a sufficient use of STW, therefore needs to be carefully considered. The relevant counterfactual situation which can be used for the comparison is unemployment. This applies to employers, workers and governments.

- Employers have the option of keeping workers in jobs with the help of STW or making workers redundant. STW would preserve the human capital basis but afford certain labour costs. Redundancies would save labour costs but require write downs on the human capital basis in the long-run.
- For workers, the attractiveness of STW depends on the risk of becoming unemployed and the envisaged amount of income cuts. Workers with a low propensity to become unemployed will be less inclined to enter STW programmes. Workers with a high propensity will have a stronger motivation. Workers also have to be included in the cost sharing model. This guarantees that STW is kept as short as possible, also with the help of workers representatives.
- Governments have the option to support STW or to finance unemployment. As mentioned above, a rapid rise of unemployment may not only have direct financial effects but deteriorate the economic climate considerably. The risk of becoming unemployed may have substantial behavioural effects among the workforce which negatively affects organisational efficiency. This could justify a certain public

²In contrast to table 1, line 'employers', no cost savings for employers is evident as the counterfactual situation is not to keep the workers employed but to make them redundant.

preference for STW arrangements. However, this may be compensated by negative long-term effects which reduce the speed of restructuring in the economy.

As all three groups of actors may profit from the introduction or application of STW, a concise and adequate form of burden sharing is necessary. This strongly depends on the institutional and historical relations between the groups.

4 QUESTIONS

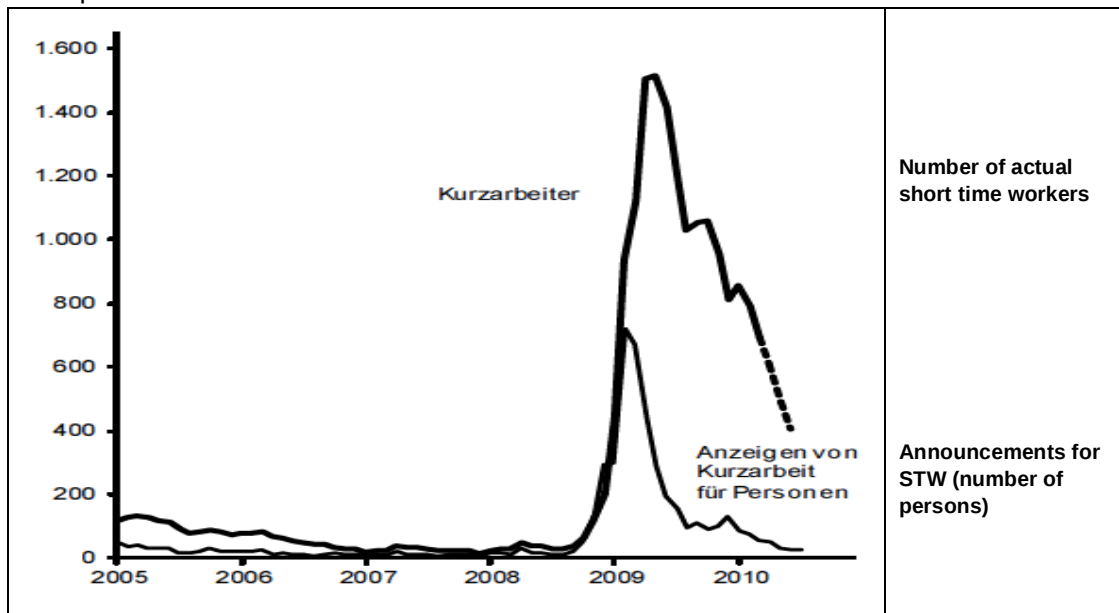
1. Why did French companies follow a cost cutting strategy with the adjustment of employment rather than working hours?
2. Why did labour hoarding stop in mid 2009?
3. Why did average compensation of employees continue to rise during the crisis?
4. Does the new APLD substitute the previous STW programmes?
5. Do workers remain covered by social security (health insurance, pension insurance etc)?

ANNEX 1: SUMMARY TABLE

Labour market situation in the Peer Country
• STW has a long tradition in Germany and has become a major instrument in combating the financial and economic crisis. • It proved to be efficient by stabilising employment and avoiding a rapid rise of unemployment. It was also efficient in preserving the human capital basis of the companies. • The strong preference of German companies for STW is related to the rising importance of human capital and the experience of skills shortages in the recent past.
Assessment of the policy measure
• France has a less generous (and more complicated) system of STW which has not the same importance like in Germany. • Companies preferred cost cutting strategies rather than working time reductions. Labour market segmentation may be an important reason for this.
Assessment of success factors and transferability
• STW is not a panacea for business downturns. Its usefulness strongly depends on the probability of a rapid recovery. • Employers strongly react to the amount of subsidies. • As all groups may profit from STW, a concise and adequate form of burden sharing is required.
Questions
• Why did French companies follow a cost cutting strategy with the adjustment of employment rather than working hours? • Why did labour hoarding stop in mid 2009? • Why did the average compensation of employees continue to rise during the crisis? • Does the new APLD substitute the previous STW programmes? • Do workers remain covered by social security (health insurance, pension insurance, etc.)?

Chart 1: Cyclical STW, Germany

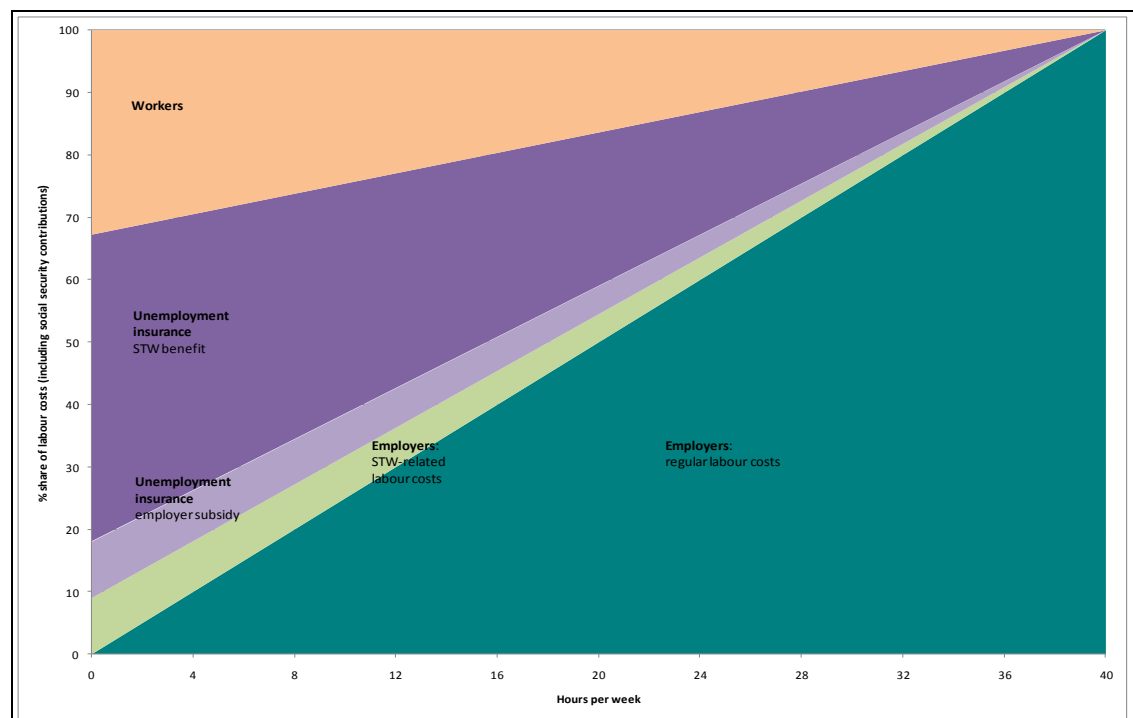
'000 persons



Source: Bundesagentur für Arbeit, Monatsbericht August 2010.

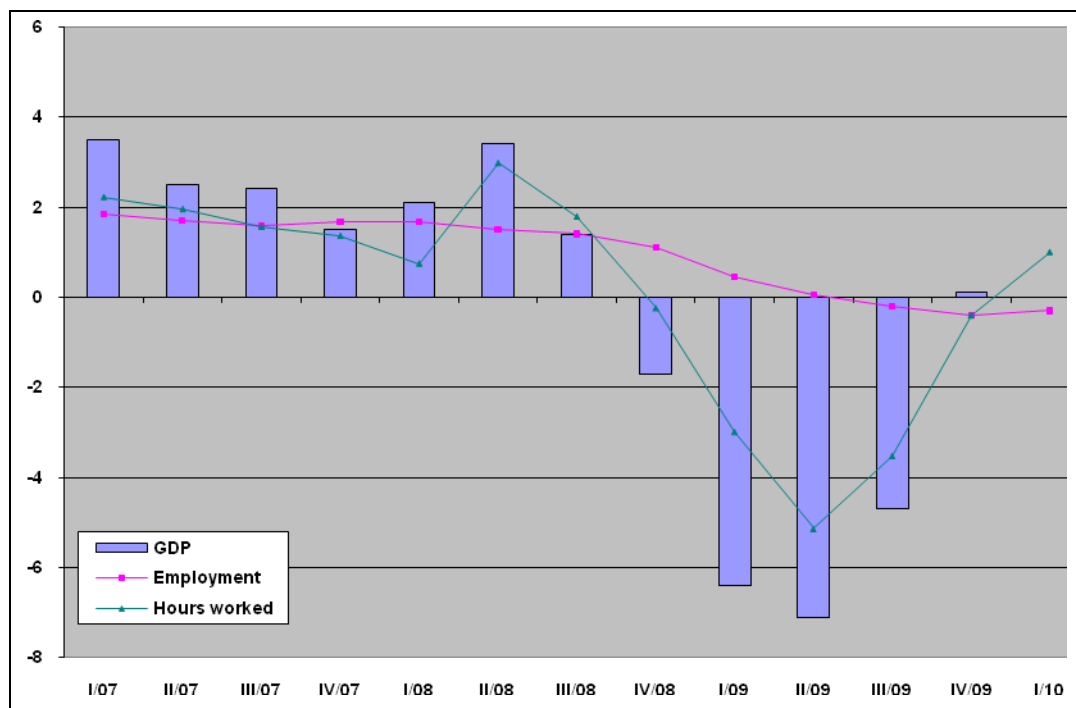
Chart 2: Cost sharing of STW programme, Germany

Costs per short time worker as % of weekly labour costs



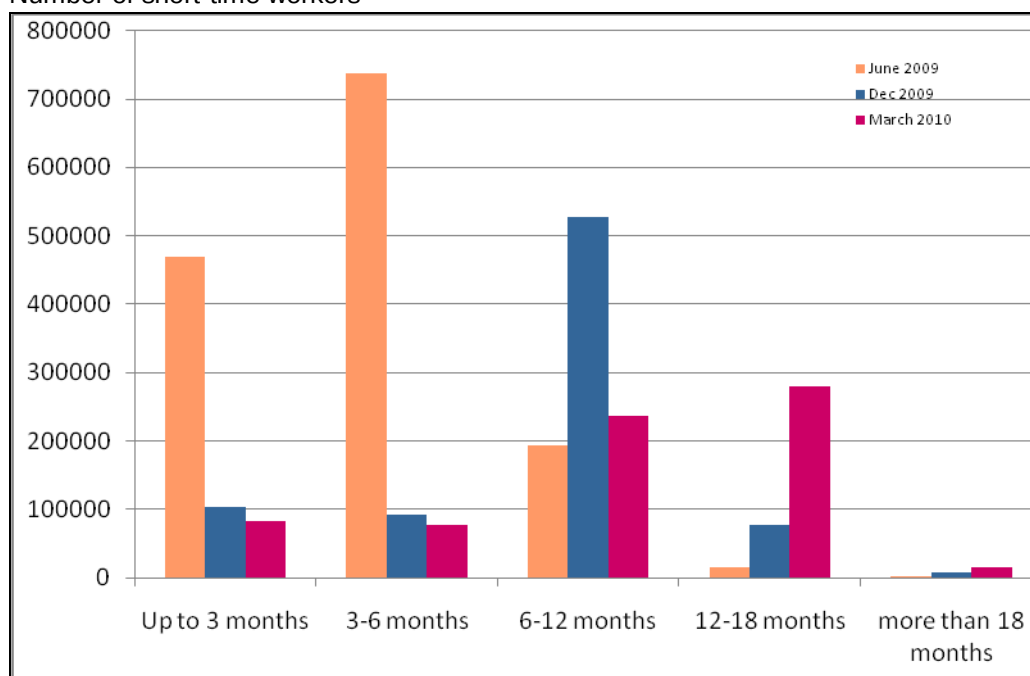
Source: Economix

Chart 3: Hours worked, growth and employment. Germany
% change to previous year



Source: Statistisches Bundesamt

Chart 4: Current length of STW, Germany
Number of short-time workers



Source: Bundesagentur für Arbeit