» Opinion

Germany's New Labor Market Miracle

The worst global recession in post-war history has understandably raised fears of surging unemployment rates around the world. And indeed, employment has dropped dramatically in many countries. In Germany, as well, many observers started to see dark clouds over the labor market by the end of last year. Most forecasts expected a substantial rise in unemployment in 2009. However, after an increase during the first months, the unemployment rate went down again in the spring.

Klaus F. Zimmermann

With the arrival of summer came new forecasts that unemployment would rise substantially – to a rate of over 4 million this year and more than 5 million in 2010. These assessments were largely based on the observation that many firms have an excess workforce, are burdened by enormous business costs, and have introduced short-time work. With long-term stagnation of the German economy on the horizon, this situation cannot continue forever, the argument goes. And once the companies run out of breath, they will sooner or later have to dismiss their excess workers.

Against the background of these predictions, it really seemed like a miracle that the labor market situation has remained calm during the summer and into the fall – although this is precisely what I had predicted in early summer. Another miracle was the fact that the free fall of the economy could be stopped in the second quarter, when first signs of a slight upswing appeared. In the third quarter, Germany's economy has again picked up considerably. The impact of the crisis was therefore much less pronounced than was expected for 2009. The growth outlook for 2010 can be even more optimistic. That the unemployment rate will hit 4 million by the end of the year has become mathematically impossible. It is also most unlikely that unemployment will reach 5 million in 2010, as many had feared. Today's forecasts for 2010 are well below 4.5 million.

But a miracle is only a miracle until the causes are fully explained. Some claim that the stimulus packages have led to the fast recovery. But this ignores that most stimulus programs did not start before mid-2009 and that their real impact will not be felt until 2010, if at all. Short-time work aside, it was only the controversial "cash for clunkers" program that went into force earlier this year. But the limited scope of this program alone could not have caused the swift recovery. Now is the chance to discuss how to channel the public funds into sectors like education and infrastructure, where they would be invested most effectively and sustainably.

The past months have shown that the German labor market is in a strong position even in times of crisis. Political reform, union wage restraint and corporate restructuring have done their share in making this possible. Wage income has fallen behind capital income for a long time now. Moreover, the crisis has particularly hit skilled workers in the export-oriented investment good industries. But employers try to retain highly qualified staff as long as possible – and at almost any cost. Therefore, the short-time work policy is certainly the most effective component of Germany's economic stimulus package.

High employment rates and low energy prices strengthen the economy because they stimulate consumption. In fact, the crisis has not really hit private households in Germany. It has mainly affected corporate profits and investment income. Thus, the crisis essentially served to correct long-term trends in redistribution. Considering that the economies of Germany's most important trading partners have also started to recover, there is reason to hope that the "miracle" will continue.

Institute for the Study of Labor
I Z A

Editor: Prof. Dr. Klaus F. Zimmermann
Managing Editors: Mark Fallak, Holger Hinte
Address: IZA, P.O. Box 7240, 53072 Bonn, Germany
Phone: +49 (0) 228 - 38 94 223
Fax: +49 (0) 228 - 38 94 180
E-Mail: compact@iza.org
Web: www.iza.org
Graphics/Photographs: IZA
Printing: Güll GmbH, Lindau
Layout: IZA