



„Reforming a Welfare State How Germany is coping with Globalisation“

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Introduction

From the „Sick man of Europe“ to the „New German Miracle“ Germany as a role model for other countries?

- ▶ What kind of social market economy is successful and sustainable?

Yes, economic model is currently relatively successful

- ▶ Growth among highest in industrialised countries until recently
- ▶ Highest employment level since re-unification (71% up from 64% in mid 90s)
- ▶ Unemployment down from 5 to under 3 million (below former last recession)
- ▶ Government deficit only 1 % in 2011

Yes, success is mainly a result of former reforms

But: Beware of arrogance

- ▶ Many other reform examples: US, UK, NL, DK, S, ...
- ▶ D learnt esp. from flexicurity of northern continental EU countries
(with strong welfare systems)
- ▶ Pathological learning: Reform effort only after crisis
- ▶ To-do list still open, e.g. services liberalisation, skill shortage (OECD)

From the „Sick man of Europe“ to the „New German Miracle“

Starting point - after burst of dotcom bubble in 2000

- ▶ Growth stagnation and rocketing unemployment: “Sick man of Europe”
- ▶ Economic burden of re-unification and lack of reforms in 1990s
- ▶ Challenges of globalisation in a rapidly internationalising economy
- ▶ Demographic challenges

Main gist of reforms and principles

- ▶ Focus on supply side and strengthen market forces to increase growth and employment
- ▶ Revive the Milk Cow
- ▶ Social is what creates employment

From the „Sick man of Europe“ to the „New German Miracle“

Reform aims (to be enlarged upon in the following)

- ▶ Strengthen growth drivers
- ▶ Labour market reforms to bring down employment threshold of growth
 - ▶ Increase lever that transmits growth into employment
 - ▶ Make economy more flexible to meet globalisation challenges

Reduce government debts

- ▶ and burden on future generations

Strengthen Growth Drivers and Market Forces

Investment

- ▶ e.g. via lowering corporate taxation and bureaucracy costs

Employment

- ▶ reforms of labour market and wage policy making

Productivity

- ▶ corporate restructuring

Innovation

- ▶ increase R&D spending, also in corporations

Education

- ▶ many reforms following PISA shock

Competition

- ▶ reduce product market regulations (e.g. crafts)

Labour market reforms

Main gist: Make labour cheaper, more flexible, reduce entry barriers, provide greater incentives to work and improve job agencies

Make labour cheaper – lower relative labour/capital price

- ▶ Wage moderation and working time increase (co-operation from trade unions)
- ▶ Lowering of non-wage cost
- ▶ Opening up of low wage sector - integrate low-skilled workers

Make labour costs and labour use more flexible

- ▶ Firm-level opening-clauses for wage-agreements
- ▶ Increase of working time flexibility (Overtime / working time accounts)

Lower entry barriers into labour market (insider-outsider-view)

- ▶ Liberalisation of temporary work agencies and fixed-term contracts
- ▶ Lowering job protection (firms up to 10 employees (formerly 5) exempted)

Increase incentives for unemployed to take on new jobs

Reduction of government indebtedness

Expenditure cuts: from nearly 49 % in 2003 to 43.5 % of GDP in 2007

- ▶ E.g. Subsidy cuts (Rathenau: „Business complaints about the fierceness of competition are often only a complaints about the lack of ideas.“)

Reform of social system to make it sustainable and to lower labour costs

- ▶ Unemployment insurance reform and deep cuts to contributions
- ▶ Pension insurance reform (extend pension age 67, adjust pension level for life expectancy, ratio of employed/pensioners)

Shift tax burden from income to consumption

- ▶ Tax increases, e.g. VAT, but lower income taxation before

After crisis: Balanced budget rule (structural deficit, corrective mechanism)

- ▶ Rule against policy failure: Frederic Bastiat: “The public household is a household where everyone wants to eat but nobody wants to do the dishes”

What can be learnt from various reform examples?

- ▶ How to make social market economy sustainable?
 - ▶ “Social” is what creates employment (Roman Herzog)
- ▶ Pay-off of supply-side reforms takes time to materialize
 - ▶ Meantime: Schröder-Government broke down under reform burden
- ▶ Reforms have to change expectations and regain credibility
 - ▶ decisive, encompassing (not piecemeal), reliable
 - ▶ Following governments should continue
 - ▶ Merkel-Governments have continued reforms – although at slower pace
 - ▶ Some reversals to counter public reform resentment + improve social cohesion
 - ▶ E.g. minimum wages, tax increase on rich, exc.pension incr.. unempl.duration re-increased >57years
- ▶ Lower relative price of labour (wage moderation, opt-outs, social and tax system)
 - ▶ Strive for co-operative industrial relations
- ▶ Commit to medium term consolidation (Balanced budget rule)
- ▶ Vocational education against youth unemployment
- ▶ Use crisis pressure to break resistance from vested interests

Crisis is also an opportunity!



Thank you for your kind attention !

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How did Germany manage the post 2008 crisis?

After Lehman collapse: massive decline in confidence and demand

Particularly world trade and exports declined

▶ Germany as a very open economy particularly exposed

Imminent danger: shedding profitable jobs and firms with destructive long term effects

▶ Qualification loss of unemployed

▶ Break down of supply chains (esp. automobiles)

Policy reaction: Building a bridge of valley of low demand

▶ Subsidies: Car scrappage premium, short time working subsidies

Co-operative and flexible industrial relations (wage policy)

▶ Trade unions co-operated with wage moderation

▶ Firms co-operated by hoarding labour and providing job security

▶ Short time working schemes and working time flexibility to avoid firing