

EUROPEAN EMPLOYMENT OBSERVATORY

Post-Assessment
of the National Reform Program
2008/10

Germany

by

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Glossary

Business Foundation Allowance	<i>Gründungszuschuss</i> : New regulation of business foundation support for unemployed UB-I recipients for a period of 15 months at maximum (valid since 1 August 2006). During the first nine months, a lump sum of EUR 300 is paid in addition to UB-I as a contribution to social insurance costs. During the following six months the lump sum is continued to be paid only if the business became the main entrepreneurial activity.
Hartz Reform	Reform of unemployment insurance under the Federal Employment Service (<i>Bundesagentur für Arbeit</i>) and active labour market policies, named after Peter Hartz, principal staff manager of Volkswagen and the president of the “Hartz Commission” established by the German government in 2002. The reform has four parts: Hartz I (2002): introduction of public temporary work agencies (Personnel Service Agencies – PSA) Hartz II (2002): reorganisation of public employment services; mini-jobs, ICH-AG Hartz III (2004): restructuring of public employment services to the Federal Employment Agency Hartz IV (2005): merger of unemployment aid and social assistance to UB-II
Mandatory collective agreement	<i>Allgemeinverbindlicher Tarifvertrag</i> : In sectors with at least 50 % of the employees covered by collective agreements the social partners can apply for an agreement to be declared mandatory. The declaration – undertaken by the Collective Treaties Committee (<i>Tarifausschuss</i>) under the supervision of the Federal Ministry for Labour and Social Affairs – means that all companies of the sector have to adopt the agreement as minimum standards regarding wages and other elements of individual labour contracts. The declaration has to be in the public interest.
Midi-Jobs	Registered employment with monthly wages between 401 and 800 € and reduced social insurance premiums.
Mini Jobs	<i>Geringfügige Beschäftigung</i> : Jobs with monthly incomes up to EUR 400. These can be regular or occasional jobs and jobs in addition to regular employment. Employers pay 30 % of wages to social insurance.
National Training Pact	<i>Nationaler Ausbildungspakt</i> : Agreement between the Federal Government and the employers associations to offer additional dual training places. The pact started in 2004.
Registered employment	<i>Sozialversicherungspflichtige Beschäftigung</i> : Employment contracts subject to public social insurance, i.e. dependent employment with salaries above 400 EURO per month.
Rehabilitation benefit	<i>Eingliederungszuschuss</i> : a wage subsidy for employers who employ long-term or disabled unemployed. Subsidies are limited to 50 % of wages for 12 months. For disabled or older workers the limits are 70 % of wages for a maximum period of 24 months.
Social benefits	<i>Sozialgeld</i> : non-employable persons in a subsistence-based partnership with at least one employable person receive social benefits. Above the age of 16 rates are equivalent to UB-II.
Subsistence-based partnerships	<i>Bedarfsgemeinschaft</i> : These partnerships are defined by the Hartz-IV act as the private income and property units obliged to individual transfers among its members.
UB-I	<i>Arbeitslosengeld I</i> : Regular unemployment benefits for singles provide 60 % of the last net income for 12 months. For parents the rate is 67 %.
UB-II	<i>Arbeitslosengeld II</i> : Means-tested basic income for job seekers, paid after expiration of regular unemployment benefit. The basic rate is 345 EURO per month.
1 € Jobs Auxiliary public jobs	Temporary jobs for UB-II recipients in the field of social and public services. They are remunerated by EUR 1 or 2 in addition to UB-II benefits. Jobs need to be for the public benefit and have to be additional to jobs in the premier labour market.

Executive Summary

Even if the actual banking crises and the danger of a worldwide economic recession can be expected to change the conditions for policy actions considerably, the German NRP sets the right priorities for long-term economic and social development. The focus on a knowledge-based society and economy, the accent on ecological innovation and the continuation of labour market reforms appears to be stringent and conclusive. The reform program is based on the principles of the “social market economy” which appears to be the German flexicurity approach. The NRP therefore did not only identify the right priorities but is strongly linked to the historical roots of the country.

Nevertheless, a series of important aspects are not or not adequately addressed by the NRP:

- the policies to release the educational system from its “class-orientation”
- the introduction of an efficient life-long learning system
- the reduction of the extensive “transition system” for dual vocational training
- the measures to increase the share of university students and human resource investments
- the way to reduce non-wage labour costs not only by lower unemployment insurance rates but by an efficient health care reform

In the area of labour market policies the Hartz Reform has shown positive results and the Federal Government intends fine-tuning rather than a reform. In particular it does not intend a reversal of the reforms – a point which was discussed intensively in recent years.

Education and training policies attract the strongest attention as this appears as the most important parameter for future development. The complex structure of policy decision within the German federal system appears as an important barrier for a consistent policy. An open process of coordination between Federal and Länder Governments is therefore suggested to overcome these limitations.

1. Introduction

The updated National Reform Program (NRP) for Germany continues the reform path defined by the previous 2005/08 program, addressing six priorities:

- (1) promoting the knowledge society and innovation
- (2) fostering open markets and competition
- (3) improving the framework conditions for entrepreneurial activities
- (4) establishing stable public finance, sustainable growth and social security
- (5) using ecological innovation as comparative advantage, safeguarding energy supply and combating climate change
- (6) adjusting labour markets to new challenges and demographic change

Even if the actual banking crises and the danger of a worldwide economic recession can be expected to change the conditions for policy actions considerably, the German NRP sets the right priorities for long-term economic and social development. The focus on a knowledge-based society and economy complies with traditional specialisation patterns of Germany and is based on the experience that this strategy works effectively. The accent on ecological innovation is irreplaceable facing the challenges of climate change. The continuation of labour market reforms appears to be stringent, considering the dominance of welfare state principles and attitudes among the German population. The reform program is based on the principles of the “social market economy” which appears to be the German flexicurity approach. The NRP therefore did not only identify the right priorities but is strongly linked to the historical roots of the country.

Based on this general appraisal this post-assessment of the German NRP will concentrate on measures related to the European Employment Strategy. These are policy actions promoting the knowledge society (Priority 1), reforming of the social security system (Priority 4) and continuing of labour market reforms (Priority 6). Before addressing these issues, however, a brief look at present economic trends appears to be necessary.

2. Facing economic recession

The German NRP was written at a time when the severity of the world financial crises was not fully visible yet. Economic forecasts still assumed the continuation of growth in 2009 at rates between 1.0 and 1.5 % (QR II/2008). These expectations have been revised meanwhile and Germany is seen at the border of recession. The latest business cycle forecast by the Project Group Business Cycle Forecasts¹ published on October 13 results in 0.2 % GDP growth for 2009 in the base-line scenario and -0.8 % in the risk scenario.

The deepness of the financial crises and its impacts on the “real” economy still remains unclear. What started as the US sub-prime crises transformed into a liquidity crisis and now into a solvency crisis of the world banking system. While governments are counteracting with equity funds and financial guarantees, it is evident that this will affect European economies. The question is only to what extent. Experience from the financial crises in Sweden (1992) showed that the economy was 5 % below its former capacity utilisation, two years after the start of the crises. In Japan (1994) however the economy was 18 % below its trend four years later. This reveals how important adequate policy reactions are at the moment.

Regarding the financial scope hard times have to be envisaged for public expenditures – not only for labour market policies but NRP actions in total. This means both, the shrink-

¹ The co-operation between the leading economic research institutes in Germany.

age of financial resources for reform policies and the rising need to counter-act unemployment. Usually social security systems are under threat in recession times as revenues decline and expenditures increase. Except unemployment insurance, none of the other social security branches accumulated sufficient resources for a recession.

Among the anti-depression measures actually discussed by the Federal Government, the suggestion is supported to make health insurance premiums tax-free. This measure was planned for 2010 but should now be brought forward to 2009 and would bring a tax advantage of 9 billion EURO to German consumers. Moreover, public expenditure programmes are discussed.

3. Promoting the knowledge society and innovation (Priority 1)

The NRP is strongly aware that skill needs are continuously rising in both, the production of high-tech manufacturing goods and the provision of services. In parallel, demographic change will reduce the number of young persons. It concludes that the conditions for education, research and innovation will have to be improved and investments are needed (NRP, Paragraph 6).

As a major critique, the PISA studies repeatedly stated that the probabilities to pass the German educational system strongly depend on social origin (*Pre-Assessment, p. 8*). The NRP however does not address this issue, not as part of the planned reform measures for education and training and not as part of the plans for life-long learning. For an economy which is strongly based on human resources, however, a status-based selection does not only waste parts of its resources, but prolong labour market segmentation and reduce the effectiveness of integrative measures. The issue should be one of the top priorities of educational reforms in Germany.

3.1. Life-long learning

In parallel, the NRP does not include a section on life-long learning. While child care, vocational training and university training are addressed in detail (Paragraph 8 to 12), life-long learning is only listed as an item of the Skills Initiative (*Qualifizierungsinitiative*) without giving any details of a policy approach (Paragraph 7).

The Federal Skills Initiative will be discussed at an “Education Summit” with the Länder at 22 October in Dresden. The Federal Government expects approval for a series of measures:

- Voluntary internships in technical and natural science studies.
- Research-oriented education by Kindergarten and primary schools
- National pact for promoting female participation in natural science and technical studies
- Promotion of female professorships
- Promotion of female academics during parent phase
- Initiative for the development of regional life-long learning structures (in cooperation with foundations)
- Foundation of an alliance for life-long learning in cooperation with social partners, Länder and municipalities targeting at a rise of participation rates.
- Introduction of an education award including direct transfers, support of education-oriented savings and provision of training credits.

Regarding life-long learning, the program includes important measures to develop the approach. However, this appears as the promotion of existing practices rather than the creation of a new system. The proposals might also be characterised by the concern to

restrict financial commitments at the Federal level and to ensure the contributions of social partners, Länder governments and regions (see Pre-Assessment, page 9).

The principles of an effective life-long learning system are not yet visible. These should include

- The function of life-long learning as part of the education and training system and the linkages to initial training
- The combination of training modules by a system of training credits or other types of certification
- The definition of minimum standards for training measures and training providers
- The integration of activities financed by companies and the Federal Labour Agency regarding training standards and training levels
- The creation of a financial support system for adult learners

3.2. Child care

In the area of child care, the Federal Government is much more resolute, having now decided on the child promotion act (*Kinderförderungsgesetz*) on 26 September 2008. This will bring child care services for 35 % of the children below three. From 2013 onwards parents will have an entitlement for child care services and parents who don't use these services will receive a monthly allowance.

While this program appears to remove important barriers for female labour participation, it remains unclear why this measure is included in Priority 1. This would mean that parents in general are less able to educate their children in young years than public child care institutions. Research evidence about this question remains unclear.

3.3. Vocational training

The dual vocational training system shows a positive balance for the training year 2007/08 with a slight surplus of training places over applications. This couldn't be observed for many years and can be attributed to the upswing of labour demand but also to the policy initiative under the National Training Pact.

The great number of disadvantaged young persons who are less competitive on dual training markets forced the Federal Labour Agency and other public authorities to establish a voluminous "transition system" of non-company-based training with the target to compensate their disadvantages through preparatory training. While 540,000 new training contracts were signed during the training year 2007/08, 338,000 young persons were in preparatory measures for vocational training financed by the Federal Labour Agency (April 2008). In addition school-based measures are provided. The estimated size of the "transition system" is 550,000 persons (*Bildung in Deutschland 2008*). These figures indicate a less favourable balance of the training situation in Germany as it reveals that the demand for training measures is considerably higher than measured by training balances.

The success of these measures, however, remained limited. Only one third of the participants were engaged in dual training 15 months after leaving the preparatory measure, and one sixth were in school-based training. The National Education Report for 2008 therefore recommends questioning the effectiveness of the transition system (*Bildung in Deutschland 2008, p. 167*).

The NRP does not include these arguments in spite of the fact that the Federal Government is responsible for dual training in general and many of the policy measures undertaken by the transition system. The solutions of the problems with disadvantaged young

people are certainly multifaceted. Without going into the details of this debate, the main suggestions refer to

- The reform of the *Hauptschule* (secondary level I school without access to higher education) which appears as a dead-end for the educational career of many pupils
- The creation of vocational training modules rather than three-year training courses
- The choice of less-demanding or shortened dual training courses

Many of these suggestions were debated for years but were obviously unable to find their way into the NRP. The fact that Länder governments did not contribute to the reform proposals appears as one of the general shortcomings of the present NRP, and is particularly evident in this Priority.

3.4. University education

A major point addressed by the recent OECD “Education at a Glance” study (2008) was the low participation of German youth in tertiary education. Only 21 % of an age cohort attends a university in comparison to 37 % among all OECD countries. This is partly attributed to the strong role of dual training in Germany: 84 % of the 25-34 aged completed vocational training in Germany while this share is only 78 % on OECD average. However, the share of university students increased much less in Germany (+3 percentage points since 2000, compared to +9 percentage points in all OECD countries). This reflects the weakness of public investments into education and training during this decade (*Pre-Assessment, p. 8*).

Raising the number of students therefore is an important issue on the educational reform agenda in Germany, considering in particular the recent debate on skills shortages in engineering and natural sciences. The NRP however does not refer to this point.

As the OECD states, the problem can be solved by two principal approaches:

- The Nordic countries in Europe expanded public expenditures for both, universities and scholarships
- The Anglo-Saxon countries raised tuition fees but provided scholarships and study credits to less privileged students

In addition to higher investments into tertiary education, scholarships appear to be particularly important for German students as this could help overcoming the strong status-based origin of university graduates. The prevailing system of training credits (*Bundesausbildungsförderungsgesetz, BAFöG*) therefore needs to be reviewed regarding effectiveness, social impacts and costs.

3.5. Governing and financing education

Considering the rising importance of human resources and life-long learning, the Federal Government would be the first institution to present its ideas and promote policy actions. However, its legal competences in the field of education and training were recently restricted in favour of Länder governments. This appears as an irritating decision compared to the changes at company level where human resource development meanwhile is the authority of the top management.

The complex structure of the German education and training system – with Länder governments as the main actors but important contributions by the Federal Government and private companies – makes clear and stringent solutions very difficult. Given the legal conditions, an open process of coordination in the field of education and training policies was suggested in the pre-assessment, bringing Federal and Länder governments together

in a structured procedure of targets, monitoring, and recommendations (*Vogler-Ludwig: Pre-Assessment of the German NRP 2008/10, page 13*).

This would help developing a broad consensus on educational policies not only with respect to financial investments but also the structure and functionality of the education and training system. Länder governments would have to open their systems for evaluation and reforms, and they would have to contribute to the nation-wide performance of the system rather than defending traditional principles.

Financing still is one of the unsolved questions of education and training policies, in particular with regard to life-long learning but also vocational training at the intermediary level. While general education is free-of-charge and university training is burdened with small tuition fees, dual vocational training is partly financed by companies and the public support for life-long learning is restricted to unemployed persons. This creates diverse incentives for the involvement of students, companies and governments. Moreover it is an important reason for the inflexibility of the systems as all changes are associated with costs. Also from this point of view, clear financial commitments by all partners are needed before negotiations start. Moreover, a stronger involvement of the Federal Government in education and training policies appears to be adequate.

4. Social security (Priority 4, B)

Only the strong rise of employment and the corresponding decline of unemployment allowed keeping total social security contributions below the level of 40 % of gross wages. The major contribution came from unemployment insurance which will reduce rates from 3.3 to 2.8 % by 2009. While this was a considerable decline since 2006 when the rate was 6.5 %, all other parts of the social security system increased their demands in recent years:

- Pension insurance from 19.5 to 19.9 %
- Care insurance from 1.7 to 1.95 %
- Health insurance from below 15 to 15.5 %

By the beginning of 2009 therefore, the overall contribution rate will be 39.95 % – and this in an exceptionally favourable employment period.

From this point of view it appears as one of the most severe shortcomings of German social security policy that it was unable to restrict expenditure growth of the public health care system. The continuous rise of health care costs means that – in spite of continuous reforms – the inefficiencies of the system are not removed and the chance to promote employment through lower non-wage labour costs is missed. During the expected downturn of the German economy this would be particularly helpful decelerating employment decline.

Among the reform measures for health insurance, the introduction of a standard contribution rate and the centralisation of financial flows by a national health fund will help balancing financial revenues among insurance institutions rather than expenditure risks. It will therefore hardly re-enforce efficiency demands. This could be achieved by tendering procedures with providers of health care services and pharmaceuticals. This instrument however is hardly applied until now. The tax contribution to the national health fund for the purpose of non-insurance related transfers is also important to reduce burdens but does not comprise more than one tenth of the estimated volume of these transfers.

5. Adjusting labour markets to new challenges and demographic change (Priority 6)

The NRP Section for this Priority underlines the principles of German labour market reforms in recent years and suggests further fine-tuning of various elements rather than a principal reform. Considering the valuable contributions of the Hartz Reforms to both, the performance of public labour market services and job search behaviour of unemployed, this appears as the adequate strategy. In particular, the NRP does not indicate any reversal of previous reforms.

The following assessment of labour market policies is limited by the fact that the evaluation results for the Hartz Reforms are not yet fully available. The latest publications date from 2006. Other but much more limited research findings therefore have to be used.

5.1. Flexicurity approach

As indicated by the pre-assessment, Germany applies a very specific type of flexicurity. Traditionally, the principle of the “social market economy” (*Soziale Marktwirtschaft*) can be seen as an early application of flexicurity as it guarantees both, the freedom of markets and the social responsibility of employers and public institutions. The trade-off between these elements, however, is solved in a different way than in Denmark. Flexibility is directed on the adaptability of existing working places, and security is focused on stabilising employment. The Danish model therefore does not serve as a benchmark (*Vogler-Ludwig: Pre-Assessment of the German NRP 2008/10, page 9*).

This view is expressed by the German NRP when it says that “... measures serve the necessary flexibility at the labour market and rapid integration into working life and simultaneously promote job security and social protection” (Point 67). Flexicurity measures therefore concentrate on activating unemployed persons and improving public placement services on the one hand, and regulating minimum standards by labour law and social transfers on the other.

With the Hartz Reforms Germany has undertaken important measures to raise the flexibility of labour markets and reduce the negative impact of income transfers on job search behaviour. This contributed to reduce the share of long-term unemployed and increase labour participation of women, young and older workers, and migrants.

The Hartz Reforms will come under threat with the expected down-turn of the German economy. The activation principle of labour market policies requires a sufficient number of vacancies. Otherwise the efforts of preparing for a new job and finding new employment will remain idle. Facing such a situation, it will be particularly important to raise the flexibility of labour supply and thus exploiting all job potentials at regional and occupational labour markets. Moreover, working time flexibility will be able to contribute to a broader job sharing – a demand which is mainly addressed to employers.

5.2. Re-organisation of labour market services

With a new regulation of public labour market services the Federal Government intends shortening placement periods and extending placement services. This was already the problem at the beginning of the re-organisation of the Federal Labour Agency and obviously was difficult to implement. Further progress – in particular through a reduction of administrative burdens of placement staffs – appears to be important.

One of the central problems of the re-organisation is the decision of the constitutional court that the administrative cooperation of the labour agencies (as part of the Federal Labour Agency) and municipalities is not constitutional. This was the major part of the decentralisation approach of the Federal Labour Agency, which proved to work sufficiently well according to the Conference of the Ministers for Labour and Social Affairs in Germany. The Federal Government therefore plans to include this type of cooperation in the constitution.

Regarding the decentralisation of labour market services to municipalities (without involvements of the Federal Labour Agency) first unofficial results of the evaluation of these measures indicate that the performance of municipal services is not better than that of centralised services.

5.3. Low-skill and low-wage employment

The problem of low-skill employment was discussed from the perspective of wages rather than skills in recent years. While statistics reveal that there is a big difference between the two aspects – 64 % of the low-wage employees terminated vocational training – the majority of these workers are engaged in low-paid jobs with restricted job profiles. The labour market devaluated previous training and job experience at the disadvantage of these workers.

Recent studies show that in 2005 22 % of the German workforce were employed in low-wage jobs (including part-time jobs and mini-jobs)² (*Weinkopf 2006*). Only 12 % of the low-wage group were able to earn a wage above the low-wage threshold within six years (comparisons between 2000 and 2005). Most of them were young male workers with comparatively good qualification. About one third was still employed on a low-wage job after six years (*Schank et al. 2008*).

These results reveal that combating low-wage employment is a matter of age and qualification. Low-wage employment has to be addressed in young years mainly through education and training. This would reduce the probability to be part of the low-wage sector in the long-run.

The Federal Labour Office achieved positive results with its “integration allowance” (*Eingliederungszuschuss*), which compensates disadvantages of unemployed by an employer subsidy. 70 % of the promoted UB-II recipients were in regular employment 20 months after starting the promotion, compared to 30 % of non-promoted unemployed. Fine-tuning of allowances according to the individual disadvantages would help increasing the effectiveness of the instrument (*Bernhard et al. 2008*).

The German NRP applies a selective approach for integrative labour market policy measures. Considering the results of the previous studies, the approach could be used even more specified through the individual customisation of support measures. The intention to give more time to placement services would help proceeding on that route.

5.4. Minimum wages

An important element of the flexicurity strategy was the introduction of minimum wages for a restricted number of sectors. This appeared to be necessary as the reduction of transfer incomes (UB-II benefits: 351 EURO per month for a single person) opened a

² Low-wage workers earn less than two thirds of the median wage.

downward spiral of wages in some branches. The differentiated approach selected by the Federal Government was already characterised as adequate by the pre-assessment.

Recent research literature shows, that the instrument of minimum wages has to be treated with caution, if negative employment effects should be avoided. The introduction of minimum-wages in the construction sector showed significant negative job effects in particular in Eastern Germany where the minimum wage was rather close to average wages of workers (*König, Möller 2008*). The further handling of the minimum-wage instruments recently introduced therefore needs to consider such effects precisely (Point 70).

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