

# German labour market survey

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The increase in German unemployment has remained low in comparison to the contraction in GDP seen since the end of 2008 (-6.3% y/y in the first half of 2009 – see Chart 1). According to data from the Federal Labour Office, the unemployment rate was 8.1% in October, down 0.1 of a point on September. The number of people out of work had nevertheless climbed by 241,000 since October 2008 (taking it to 3.2 million, compared to 5.1 million in March 2005), with 192,000 being added since the beginning of the year. Employment has also declined since November 2008, with 123,000 jobs lost (see Chart 2).

Faced with a collapse in economic activity at the end of 2008, the German government relaxed the conditions on its partial unemployment scheme. The government now covers half of an employee's social security contributions, or all of them if the worker follows a training programme. The period of time during which companies can take advantage of the scheme has gradually been raised from between 12 and 18 months in November 2008 to 24 months from July 2009. These measures helped limit the rise in unemployment; 1.433 million people were covered by the partial unemployment measures in June 2009, compared to just 39,000 in August 2008.

The relative good health of the German labour market in the face of the recent recession also owes a lot to the reforms carried out earlier this decade.

During the last phase of growth in the German economy, between 2005 and 2008, GDP rose by a total of 11% and 1.4 million jobs were created. The unemployment rate fell by nearly 4 points from just under 12% on average in 2005 to 8% in 2008, reaching

a cyclical low of 7.6% in November 2008. During the previous growth cycle (1999-2001), the unemployment rate did not drop below 9.2%, despite an 8% increase in GDP.

However, Germany now finds itself faced with a sharp rise in temporary jobs and a structural demographic deficit.

## Employment and GDP

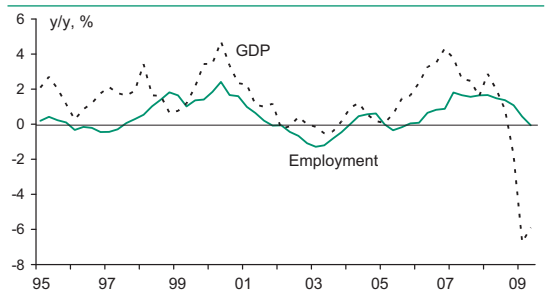


Chart 1

Sources: Federal Labour Office, Bundesbank

## Employment and Unemployment rate

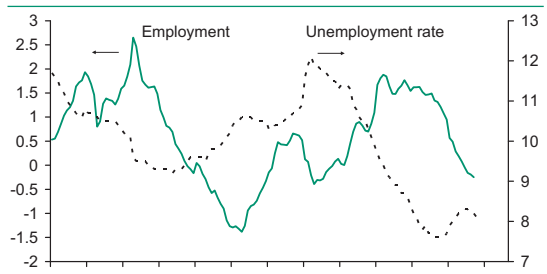


Chart 2

Source: Federal Labour Office

# Labour market reforms during the 2000s

## NAIRU reduced from the middle of the 2000s

Between the beginning of the 1990s and 2005, difficulties in reducing unemployment were illustrated by the increase in NAIRU (Non-Accelerating Inflation Rate of Unemployment), which rose from 6.5% in early 1991 to 8.7% by the autumn of 2005. From there it fell, reaching 8.2% in the second quarter of 2009, (see Chart 3).

The Beveridge curve (which plots the number of unemployed people against vacant posts) also shows a better allocation of work from the middle of this decade, which has allowed a reduction in the structural unemployment rate (see Chart 4). The more efficient the labour market, the lower the rate of unemployment for a given level of vacancies, as the matching of supply and demand is more rapid. Between 2005 and 2006, unemployment rose whilst the number of vacant posts remained stable. Since then, however, the number of vacancies has fallen, as has unemployment.

## The long-term unemployment rate is down

The Hartz reforms profoundly changed the German labour market.

Long-term unemployment (12 months or more) remains a substantial but declining part of the total chart (from 57.3% in 2006 to 53.4% in 2008 according to OECD charts). However, the number of people out of work for more than 12 months fell significantly between 2006 and 2008 (down 35% -- see Chart 5)<sup>1</sup>.

Over the last growth cycle in the German economy (2005 to 2008), people excluded from the labour market, often less well qualified, were able to find work, but the Hartz IV reforms introduced in 2005 have made a considerable contribution to reducing long-term unemployment.

The reduction in benefits, the shortening of the period over which they are paid, from 32 to 12 months, and the follow-up policies adopted have all encouraged the unemployed to return more rapidly to the labour market.

**Nairu**

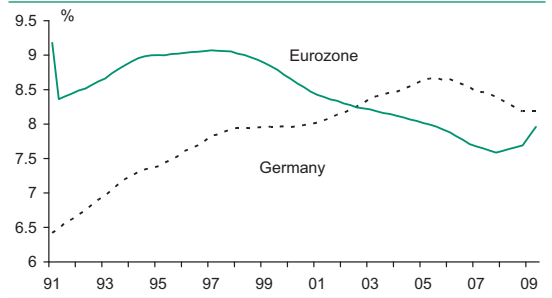


Chart 3

Source: OECD

**Beveridge Curve**

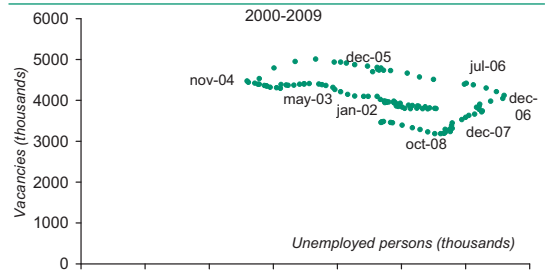


Chart 4

Sources: Federal Labour Office, Bundesbank

**Long-term unemployed persons**

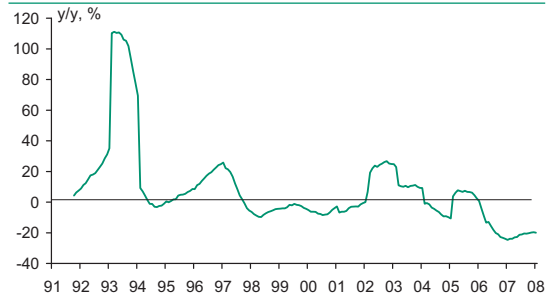


Chart 5

Source: Federal Labour Office

The aim of unemployment benefits was previously to maintain the standard of living of the unemployed person rather than providing emergency support. Since 2005, all household income and assets have been taken into account in calculating the level of benefits to be paid (transport and child benefits are also paid).

People in difficulty, who are available for work, receive benefits under the new Unemployment Benefit II system. This is paid to unemployed people who do not qualify, or no longer qualify, for Unemployment Benefit I payments and also replaces the former social support payments.

Monitoring policies vary according to the ability of the unemployed person to make a rapid return to work, but the demands made of them have been increased significantly. They must actively seek employment and accept any suitable job offered. If they fail to do this, they are subject to financial penalties. They must also take part in training programmes (which may be run by private sector companies), which aim to assess their desire to find a job and build their skills. These programmes last for anywhere between a few days and twelve weeks, and during the training period the job seekers are not included on the unemployment register.

Since 2005, employment agencies have been given quantified targets, which vary depending on the type of agency, but they also have a degree of autonomy in deciding how these are to be achieved. Moreover, if a public agency does not manage to find an unemployed person a job within six weeks they can hand the case over to a private company, which will be paid by results. Support in creating new businesses is also available. Lastly, companies employing someone who has been out of work for some time, and is therefore likely to be less productive, can also receive aid. This support is capped at 50% of wages; the company must not have made anyone redundant in order to employ the unemployed person and must not have employed them in the previous four years.

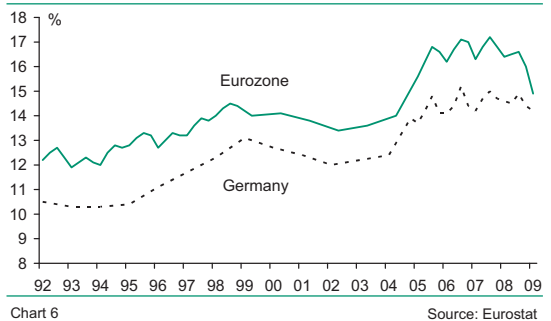
Lastly, the long-term unemployed are increasingly encouraged to take up fixed-term, temporary or part-time posts which public employment agencies are now allowed to offer them.

### Reduction in unemployment driven by greater use of fixed-term and temporary contracts

Temporary and fixed-term contracts are becoming increasingly common in Germany. The 2003 Hartz Act relaxed the limits on the length of such contracts. Fixed-term contracts and those covering temporary work can be for a period of two years, or four years if the employer is developing new businesses. The only restriction is that the same wage be paid for employees working under different sorts of contract or that the employer adheres to an agreement reached with employees.

According to Eurostat figures, the number of employees on temporary contracts rose from 12.4% of the total in 2001 to 15.2% by end-2006<sup>2</sup>. This figure has certainly fallen back again since then. Some employers preferred to use fixed-term contracts – which increase employee motivation and productivity – during the last growth phase from 2005 to 2008. Temporary work was the first area to be hit by the effects of the recession. The share of the total workforce on temporary contracts was 14.9% at end-2008 (compared to 16% for the euro zone as a whole – see Chart 6).

**Total % of employees with temporary contracts**



### Part-time working has also made a contribution

The use of part-time contracts has risen sharply during the 2000s. According to Eurostat figures, part-time jobs made up 25% of total employment in the final quarter of 2008 (against 19.6% for the euro zone), from barely 19% in 2001 (nearly 15% in the euro zone). Thus the number of part-time workers increased by 55% between 1998 and 2008, taking it to 10 million (Chart 7). Measures to relax the rules were introduced in the early part of this decade. These created new types of contract such as “one-euro jobs”, “mini-jobs” and “midi-jobs” which were available to all types of employees and designed to cover secondary employment and non-merchant sectors. A mini-job pays a maximum of €400 per month and a midi-job between €400 and €800 per month. Social security contributions vary according to the level of salary, from zero for salaries of €400 to €400 for salaries of €800. Mini-jobs accounted for 13.8% of total employment in 2007 (having risen 7 percentage points between 1995 and 2005). One-euro-jobs pay between €1 and €2 per hour on top of unemployment benefits. However, only non-profit-making organisations can offer such contracts.

The increase in part-time working between 1998 and 2008 was spread across all age groups. This said, some 60% of part-time posts are occupied by people aged between 35 and 54. The rapid growth in use of these contracts has modified the structure of the labour market and helped reduce the unemployment rate. The use of part-time working gives companies greater flexibility, particularly in the service sector, in which nearly 85% of part-time workers are employed.

Part-time contracts tend to offer low wages and less job protection. This is due, in particular, to the dominance of relatively unskilled work. In 2008, 22% of part-time workers did not have any professional qualifications, compared to 13% for the workforce as a whole.

Half of all part-time workers have two such jobs and 23% indicated that they have been unable to find full-time work (13% in 1998); 65% of them are in the former East Germany.

### Greater flexibility in setting wages

Labour market reforms have given companies greater flexibility. They have also contributed to helping dampen down wage growth during the 2000s by allowing companies to make use of a broader range of employment contracts.

Moreover, the method of negotiating wage settlements began to change in the late 1990s. Companies were able to negotiate certain terms to help protect or increase competitiveness.

For example, in 1997 the chemicals sector was able to introduce a “corridor” for wage settlements that came into force in 1998. With the agreement of all social partners, this covered a 10% reduction in the number of hours worked and in wages relative to the levels set in previous settlements.

Some variable elements of wages, such as the thirteenth month, may now be negotiated downwards. In banking, profit-related bonuses were introduced in 2002. Some companies also increased the number of hours worked in 2004, with the working week increased from 35 hours to 39 hours without any increase in salary.

### Part-time employment

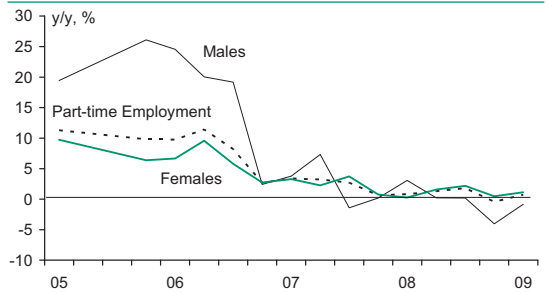


Chart 7

Source: Eurostat

### Compensation of employees (in % of VA)

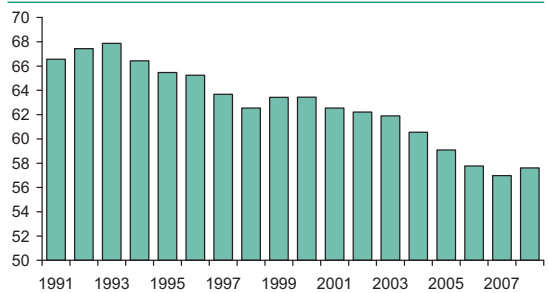


Chart 8

Source: Eurostat

Having risen by 4.6% y/y in 2000 (for inflation of 1.5%), employee remuneration fell 0.5% y/y in 2005 (when inflation was 1.4%). This was followed by an acceleration in wage growth up until 2008 (4.2% y/y) at a time when inflation ran at 2.7%.

The share of value added taken by wages fell from 67.9% in 1993 to 57.6% by 2008 (Chart 8). Similarly the margin rate (gross operating profit over value added) rose from 31.8% in 1993 to 41.2% in 2008 (having hit 41.9% in 2007). The good financial health of German companies allowed them to protect employment during the period of growth from 2005 to 2008 but also to face up to the recent crisis. They have thus been able to retain staff with the appropriate training, meaning that they will avoid the costly process of recruiting new staff once the recovery is firmly in place.

## The Hartz Acts

Between 2002 and 2005, the Agenda 2010 programme implemented the main proposals of the Hartz Commission's August 2002 report. The Hartz I and Hartz II Acts of 2002 led to:

- The creation of one-stop Job Centres to manage unemployment benefits and help the unemployed to find work;
- The creation of temporary staffing agencies (PSA) within local agencies;
- Provision of financial support for casual work ("Mini-jobs" and "Midi-jobs");
- Support for new business creation.

The Hartz III Act, which came into force on 1 January 2004, covered the transformation of the former Federal Labour Office into the Federal Employment Agency. The distribution of benefits was devolved to local agencies.

The main changes introduced under the Hartz IV Act of 1 January 2005 were:

- Prior to the introduction of this Act, unemployment benefits were paid for 32 months at a rate equivalent to 67% of previous income. From 1 January 2004, benefits were paid at this level for 12 months and then were reduced significantly. However, payments were adjusted with bonuses, reflecting family circumstances and other sources of income, to prevent income levels from falling too abruptly.

- The Act also required the long-term unemployed to accept a less well paid job or face reductions or removal of benefits. "One-euro-jobs" were introduced, as were new business support for the unemployed, who are required to accept jobs that allow them to top up their benefits. Failure to do so results in the cancellation of benefits.

## The German labour market under the microscope

Whilst labour market reforms have reduced the unemployment rate and increased employment across all categories of worker, the conditions of access to work continue to vary.

Youth unemployment is lower in Germany than in the euro zone as a whole, but there are growing problems

The unemployment rate for the under-25s has risen steeply since the end of 2008; it stood at 10.7% in August 2009 (under the ILO definition<sup>3</sup>), having reached a cyclical low point of 9.3% in August 2008 (Chart 9). Companies have little incentive to recruit inexperienced workers and young apprentices against a background of a deterioration in the labour market.

They also have greater scope for reducing the number of young employees, as their trial periods last two years during which the employer can fire them at any time and re-employ them six months later.

Unemployment rate



Chart 9

Source: Federal Labour Office

## ***Any return to strong growth will come only gradually***

*German GDP grew by 0.3% q/q in the second quarter of this year. This rise, the first since the first quarter of 2008, followed quarter-on-quarter falls of 2.4% in the fourth quarter of 2008 and 3.5% in the first quarter of this year (Chart 10). GDP contracted by 5.9% year-on-year. Net exports made a positive contribution to growth (1.6 of a point in Q2 2009) due to a fall in imports that, at 5.1% q/q, was greater than the 1.2% q/q drop in exports. International demand has, however, been feeding company order books for several months. Having collapsed since the end of 2008, exports of goods fell 1.8% m/m in August but grew by 6.1% m/m in June and 1.7% m/m in July. The upward trend in new orders for manufactured goods (up 17.1% between February and August 2009) thus suggests a recovery in output in the second half. Indeed, industrial production rose by 1.7% m/m in August (having fallen 1.1% m/m in July). However, this was primarily a technical recovery. Companies had run down inventories in the early part of the year, which had a strong negative effect on growth in the second quarter (-1.9 points after 0 points in Q1 2009). They will now need to satisfy demand through an increase in production.*

*Investment in capital goods and machinery fell by only 0.5% q/q in Q2 2009 (compared to -18.5% q/q in Q1 2009). It is likely to grow only slowly over the next few quarters, given the tightening of lending conditions and the low capacity utilisation rate. However, construction investment (up 0.2% q/q in Q1 2009 and 1.4% q/q in Q2 2009), boosted by government support, will go some way to offsetting weak company spending. As a result, total investment, which rose 0.8% q/q in the second quarter (0.2% q/q in Q1 2009), will remain just within positive territory over the next few months (Chart 11).*

*Growth has however been boosted by increases in public and private consumption (0.4% q/q and 0.7% q/q respectively).*

*The fall in inflation and the €2,500 subsidy on new car sales have helped bolster consumer spending against the background of a limited deterioration of the labour market. Since last summer, inflation has been running at record lows. Favourable comparison effects on energy prices and, to a lesser extent, lower prices in the food sector have put strong downward pressure on prices. German inflation (on the basis of the CPI consumer price index) was thus 0% in October (from -0.3% in September). However, the basis of comparison effects will gradually drop out of the equation over the next few months. This is because oil prices peaked in the summer of 2008 before collapsing. Price rises will nevertheless remain modest given the easing of underlying inflation. The low capacity utilisation rate and the slowing of consumer spending over the next few quarters will continue to put downward pressure on prices.*

*Economic activity has thus reached its cyclical low point. Various indicators published in recent months suggest that growth will accelerate between now and the end of the year before easing back to a more moderate rate. The IFO business confidence index recorded its seventh consecutive monthly rise in October (to 91.9), putting it at its highest level since September 2008. Although business leaders are expecting an upturn in growth over the next few months, they are also demonstrating a degree of caution.*

## GDP

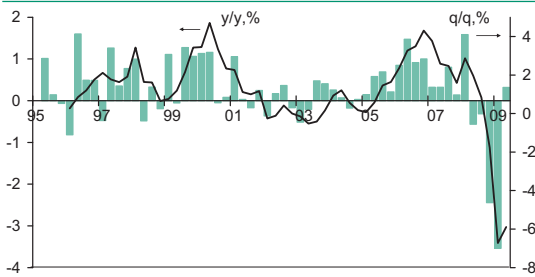


Chart 10

Source: Bundesbank

## Investments and exports

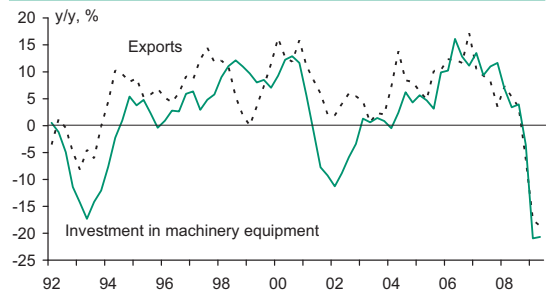


Chart 11

Source: Bundesbank

At 0.6 of a point, the increase in the IFO index was modest compared to those of previous months. The results of the PMI survey confirm those of the IFO report. The composite PMI index rose by just 0.2 of a point, to 52.6, in October. Having reached a cyclical low of 32 in January 2009, the industrial PMI index has moved back above 50, thus signalling growth in activity over the next few months (51.1 in October from 49.6 in September). In contrast, the services PMI index fell by 1.1 points (from 52.1 in September to 50.9 in October), reflecting, in particular, the slowdown in private sector consumption.

Although the IFO and PMI indices point to a perceptible improvement in the German economy, their slower rate of progress suggests that the economy will make only a gradual return to lasting growth. We therefore expect GDP to contract by nearly 4.7% for this year as a whole, despite the upturn in growth at the year end.

The unemployment rate amongst young people in Germany remains lower than that in the euro zone as a whole. In August 2009 this stood at 19.7% on the ILO definition, having hit a cyclical low of 14.5% in March 2008. However, the German figure is now trending towards the euro zone average. A gap of more than 8 points in 2000 narrowed to 3.5 points in 2005 and 5.5 points in 2008.

The apprenticeship system is falling into disuse. This system allows young people to receive professional training within a company. However, there seems to be decreasing interest in this option amongst the young at a time when the tertiary sector is taking on a growing importance in the German economy.

Amongst other things, the apprenticeship system lead to a high level of specialisation which can negatively affect the mobility and adaptability of young workers if a particular sector gets into difficulties. In addition, companies are increasingly unwilling to bear the costs of apprenticeships, even though they are often able, once the training period has finished, to pay apprentices at below the market rate.

Lastly, educational achievement amongst young people in Germany is below the euro zone average. Eurostat figures show that the proportion of those aged between 20 to 24 having completed at least upper secondary level education has also been below the euro zone average since 2003. In 2005, the figures were 71.5% for Germany and 73.5% for the euro zone.

## Increased employment levels amongst older people

The unemployment rate amongst those aged 55 or over began to fall in the late 1990s, but has seen a particularly steep decline so far this decade. The OECD estimated that the unemployment rate for those aged 55 to 64 was 15.3% in 1997, a figure that had fallen to 12.7% in 2005 and 9.7% in 2007.

Since 2006, companies have had the possibility to offer fixed-term 5-year contracts, without the need for additional justification, to workers aged over 52 who have been unemployed for more than 4 months (temporary contracts must normally be for a period of less than 2 years). The period for which unemployment benefits are paid to the over-50s has also been cut to 18 months. If the unemployed person accepts work on a lower wage than they previously received they also receive a top-up payment equal to 50% of the difference for a period equal to that during which they received unemployment benefits. This payment is then cut to 30% of the difference. Companies employing someone aged over 50 who has been unemployed for more than 6 months can also claim assistance of between 30% and 50% of the salary paid for a 36-month period.

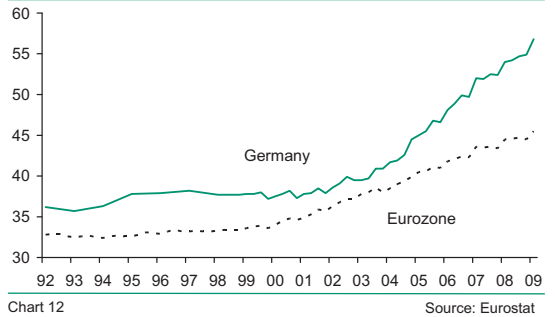
Germany has already significantly exceeded the Lisbon Treaty targets set in 2007 of boosting the employment rate for those aged 55 to 64 to at least 50% by 2010. According to Eurostat figures, this figure rose from nearly 38% at end-2000 (just under 35% in the euro zone) to nearly 57% in the second quarter of 2009 (compared to around 46% in the euro zone – see Chart 12).

The educational level of the baby-boomer generation, which was higher than that of the generation before, has allowed it to adapt more easily to the requirements of the labour market.

The government also adopted various incentive measures in 2005 and 2007 as part of the “50-plus Initiative”, which have made a considerable contribution to supporting employment amongst older workers, particularly for those with fewer educational qualifications.

Some measures which had previously encouraged early retirement of older employees have been gradually

Total employment rate (55-64 years)



phased out. Employees aged over 55 can still take advantage of part-time working schemes, under a system that allows them to halve their working hours.

In general the employees concerned continue to work full time for five years, and then stop work altogether, receiving benefits until the retirement age of 65. The employer is obliged to pay, in the form of a bonus, 20% of wages (not subject to tax and social security contributions) plus 70% of the former net salary received. They must also pay pension contributions on 80% of the original salary. These costs are reimbursed by the Federal Employment Agency if an unemployed person or an apprentice is recruited to replace the retiree. However, this system of part time working for older employees will only be open to new entrants until December 2009. Given the deterioration of the labour market, the Employment and Social Affairs minister of the previous coalition had planned to extend the scheme until 2014. However, this would be unlikely to have much effect on the unemployment rate in the short term given the desire of older workers to continue in full-time employment before taking early retirement.

Lastly, older workers face even greater incentives to remain in the labour market in view of a tightening of retirement conditions. The retirement age will gradually be raised from 65 to 67 between 2012 and 2029 (although an individual will be able to claim a full pension from the age of 65 provided that they have 45 years of contributions).

## GDP growth components

	2008	2009*	2010*	Q109	Q209	Q309*	Q409*	Q110*	Q210*	Q310*	Q410*
GDP q/q				-3.5	0.3	0.9	1.0	0.1	0.0	0.1	0.2
GDP y/y	1.0	-4.7	1.4	-6.7	-5.9	-4.8	-1.4	2.3	1.9	1.1	0.4
Private consumption y/y	0.2	1.4	-0.8	-0.1	1.2	1.6	2.7	1.0	-0.4	-1.5	-2.3
Public consumption y/y	2.0	2.6	3.1	2.5	2.2	2.6	3.0	3.5	3.3	3.0	2.8
Fixed investment y/y	2.3	-7.8	2.0	-11.2	8.3	-7.6	-3.8	4.8	2.9	1.1	-0.5
Stocks (contribution to growth)	0.5	-1.3	0.6	0.0	-1.9	-0.5	0.0	1.0	0.3	0.1	0.0
Exports y/y	2.4	-14.2	7.4	-17.5	-18.6	-16.1	-3.5	9.5	10.8	7.8	2.1
Imports y/y	3.9	-8.3	7.6	-7.6	-11.0	-12.2	-2.3	6.8	12.0	9.4	2.6

Table 1

\* BNP Paribas Forecasts - q/q quarter-on quarter change - y/y year-on-year

### A narrow gender gap in unemployment

In September 2009 the unemployment rate amongst women (on the ILO definition) was 6.9% and that for men was 8.3% (Chart 13). However, the number of women without work rose by 1.1% between its low point in November 2008 and September 2009, whilst the figure for men jumped by 15.9% between October 2008 and September 2009.

Although unemployment amongst women was greater than that amongst men during the last period of growth in the German economy, the gap went into reverse from January 2009.

Although women benefited less from the rapid growth in industrial exporting sectors and in banking and insurance, which are traditionally weighted towards men, male employment also suffered much more from the collapse in economic activity from end-2008<sup>4</sup>. In addition, the working female population has grown at a stronger rate than the male population since the third quarter of 2008 (Chart 14).

Women (some 85% of whom are employed in service sectors) occupied nearly 80% of temporary posts in 2008. The number of women working part time increased by 45% between 1998 and 2008 and by 11.6% between 2005 and 2008. For men, part time

posts have doubled since 1998, with an increase of over 27% between 2005 and 2008.

According to Eurostat data, the employment rate for women remains significantly below that for men, at 66.2% compared to 75.2% in the second quarter of 2009. There remain many obstacles that discourage women from remaining in the labour market. The lack of suitable infrastructure (such as crèches) proves a particular disincentive to a return to work after the birth of their first child. Thus the employment rate for women with one child was 67.5% in Germany in 2008, compared to 74.4% in the euro zone.

### Unemployment amongst foreign workers remains structurally higher than the national average

Foreign workers in Germany were the first to be hit by the collapse in economic activity and the adjustments to staff numbers carried out by companies. On the whole such workers occupy a greater number of temporary and part-time posts. As a result, the unemployment rate amongst foreign workers began to rise steeply from the end of 2008, jumping from 15% in November 2008 to 17.3% by April 2009. Despite falling somewhat since then, it remained at 16% in October 2009 (Chart 15).

### Unemployment rate for females

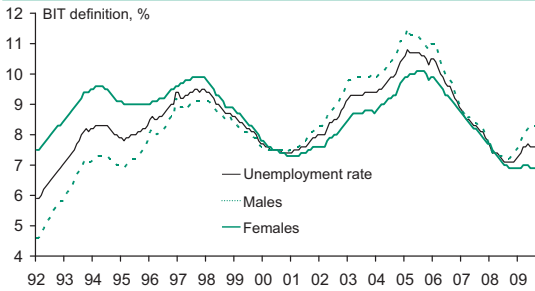


Chart 13 Sources: Federal Labour Office, Eurostat

### Unemployment rate-Western Germany

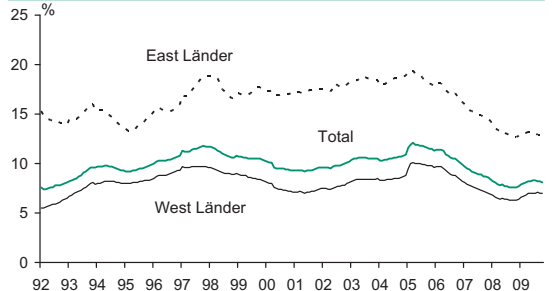


Chart 16 Source: Bundesbank

### Labour force

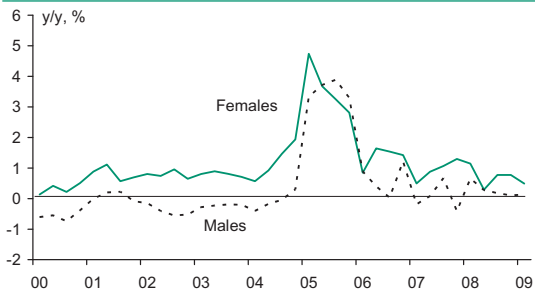


Chart 14 Source: OECD

### Unemployment rate-Eastern Germany

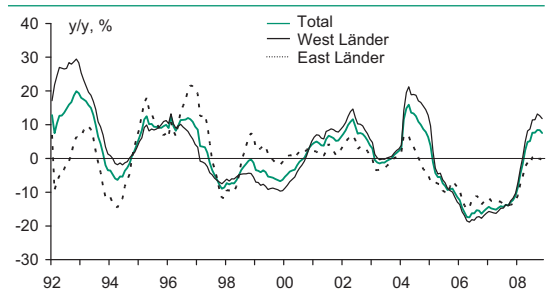


Chart 17 Source: Bundesbank

### Unemployment rate-foreigners

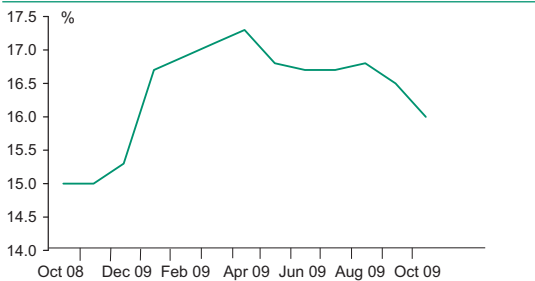


Chart 15 Source: Federal Labour Office

### German population

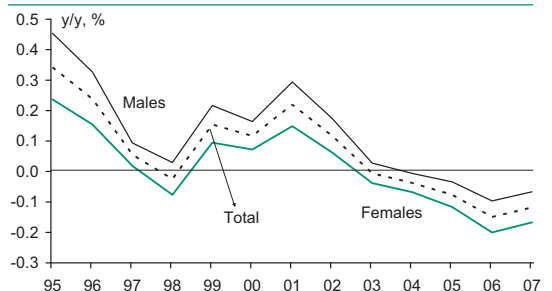


Chart 18 Source: Federal Office of Statistics

The unemployment rate rose only slightly at the beginning of this year in the former East Germany, but it remains well above the rate in the West

Unemployment has only increased slightly in the former East Germany, rising just 0.6% between its low point in November 2008 and October 2009; over the same time, the former West Germany saw an increase of around 12% (Chart 16). The number of employees covered by the partial unemployment scheme also rose less in the East. Between August 2009 and June 2009, the number of people in this scheme increased by a factor of 25 (to 175,000) in the East, but by a factor of 38 (to 1,244,000) in the West. A higher proportion of companies in the East are in services sectors and as a result, suffered less from the collapse in manufacturing activity at the end of 2008.

With Germany celebrating the twentieth anniversary of the fall of the Berlin Wall this year, unemployment remains structurally higher in the East, despite a 6.7 point fall in the unemployment rate between March 2005 and November 2008, that took it to 12.7% (Chart 17).

To a large extent the origins of this situation lie in the economic and social decisions taken at the time of reunification. Immediately after this, wage negotiations were conducted mainly by unions and employers from West Germany, who wanted an increase in wages in the East in order to limit the flow of workers from East to West and of companies in the opposite direction.

In addition, the introduction of regulations to protect job security discouraged companies from creating new jobs (companies retained their existing posts but did not create new ones).

In addition, subsidies were available to support relatively unprofitable companies, meaning the creators of new businesses had fewer resources. Given the level of wages, weak productivity and the subsidies allocated, companies invested in businesses that created few jobs, providing little incentive for East Germans to get the training to attract the companies that would create jobs. Young graduates therefore moved west, whilst the least “employable” section of the labour force (older and with fewer skills) remained in the East.

## Germany faces a new challenge: the demographic shift

Increased employment rates partially offset a falling population

The total labour force grew rapidly in 2005 and 2006 (by 3.6% and 1% respectively), before settling into more sedate growth rates from 2007 (0.5% in 2008), which went some way to offsetting the decline in total population. The fall in unemployment from the middle of the current decade probably encouraged a number of people to stay in, or return to the labour market. In addition, the introduction of temporary and part-time contracts regularised employment that had previously formed part of the black economy. The increase in the active female population was particularly rapid (1.2%, 3.6% and 1.4% in 2004, 2005 and 2006 respectively). In addition, the baby-boomer generation is more active than their predecessors due to higher levels of education which allowed them to meet the needs of the labour market. According to the OECD, the overall employment rate for people aged 15 to 64 thus rose from 71.1% in 2000 to 75.6% in 2007.

The increase in the employment rate will not, however, be enough to offset the shock of the withdrawal from the labour market of the baby boom generation over the next few years. Although the retirement age will be raised to 67, the German population, which has seen growth slowing since the mid-1990s, contracted by 0.1% per year, despite an increase in life expectancy from 75.3 years in 1990 to 79.8 years in 2006. Moreover, this period has also seen an even faster decline in the female population, which has contracted by an average of 0.2% per year.

The natural growth rate has been negative for three decades. It stood at -2.624 in 2008 (4.599 for the euro zone as a whole). The fecundity rate in 2007 was 1.37 children per woman (1.33 in 2006, 1.53 for the 27-member European Union) a figure which has changed little in recent years. A lack of facilities makes it difficult for women to balance professional and family commitments. Many women, particularly those who are highly educated, are now deciding not to have children.

## Germany makes little use of immigration

Faced with these demographic trends, Germany has recently changed its immigration policy.

The German government has sought to facilitate immigration of foreign graduates (doctors, engineers, teachers, etc.). A law introduced on 1 January 2005 simplified the administrative processes involved<sup>5</sup>.

Even so, many restrictions remain. New immigrants must have a concrete job offer and a qualified immigrant from outside the European Union must show that he or she will receive an annual income of €85,000. Immigrants must also know at least 200 to 300 German words. There are therefore still considerable obstacles to immigration.

The number of non-naturalised immigrants from outside the 27 EU member states arriving to work in Germany was just 40,324 in 2007. Although this was twice the number in 2006, the figure fell by nearly 118,500 between 2000 and 2007. Thus the net migration rate has fallen significantly since the early 1990s. According to the OECD it was 2.2 in 2001 (1.2 for the 27-member EU) and 0.5 (3.8) in 2008 (Chart 19).

Lastly, Germany is experiencing difficulties in recruiting qualified labour, particularly in new technology sectors.

Immigration rate (1000 inhabitants)

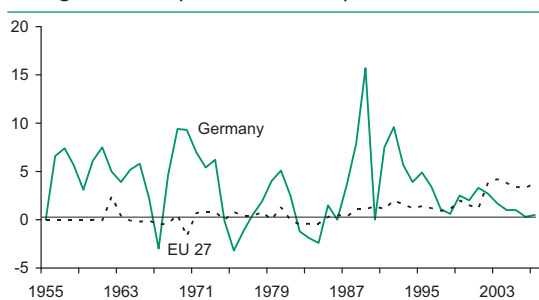


Chart 19

Source: OECD

The Hartz Acts (in conjunction with wage restraint) have given companies more flexibility and allowed them to become more competitive. These reforms thus helped support German growth over recent years which in turn resulted in the creation new jobs. As a result, the increase in the unemployment rate has been relatively modest when set against the scale of the collapse in economic activity at the end of 2008.

The flip-side of this picture is the fact that the decline in international trade since the end of last year has highlighted the German economy's dependence on exports, which have been the main engine of growth in recent years.

Labour market reforms, by encouraging increased use of temporary and part-time contracts, have made some employees more vulnerable, and limited wage growth has held back consumer spending in recent years. Although stimulus measures for consumers and lower inflation have both boosted private consumption, their effects will gradually drop out of the equation, whilst exports will make only a very gradual return to strong growth.

The measures set out by the new coalition of the CDU/CSU and the liberal FDP created after the recent elections could, however, help boost consumer spending and consolidate business competitiveness. There are plans to increase family allowances, reduce income tax and cap social security contributions.

The labour market will therefore have suffered little relative to the collapse in economic activity, and the reforms carried out in recent years will allow Germany to take full advantage of a return to growth in its main export markets.

29 October 2009

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## NOTES

<sup>1</sup> Long-term unemployment represents a considerably greater part of the total than for the 15-member EU (approximately 38.6% in 2008 from 44.7% in 2006). The 15-member EU consists of: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the United Kingdom.

<sup>2</sup> 14.5% in 2001 and 17% at the end of 2006 in the euro zone.

<sup>3</sup> According to the International Labour Organisation (ILO), an unemployed person is someone of working age (15 or over) who meets three conditions:

- is out of work, that is to say has not worked even for a single hour during a reference period of one week;
- is available to take a job within 15 days;
- has actively sought employment in the preceding month or has found employment that is due to begin within three months.

<sup>4</sup> Total employment was down by 0.1% in the second quarter (having grown 0.4% in Q1 2009 and 1.4% in 2008). Job losses were however concentrated in the industrial sector (excluding construction) which employed 20% of workers in 2008. Despite the recent rally at the end of the summer, the collapse in industrial activity since the end of 2008 (-17.4% y/y in August) has forced companies to cut staff numbers. As a result, employment contracted by 0.6% and 1.8% q/q in the first and second quarters respectively, having risen by 1.5% in 2008. Conversely, service sector employment rose by 0.4% q/q (0.8% q/q in Q1 2009 and 1.5% in 2008). This sector accounted for 72.5% of jobs in 2008. In particular, employment continued to grow in the fields of health, education and personal services, areas in which there are many part-time jobs. Thus the number of unemployed people in the domiciliary services sector and in other health professions fell by 4.5% and 1.8% respectively between January and August, with the number of social assistants rising 2.8%. In the construction sector (5.4% of total employment), employment was down 0.9% q/q (after -0.2% q/q in Q1 2009 and -0.7% in 2008). These disparities help explain the divergent unemployment trends between men and women and also the differences between the former West Germany and East Germany.

<sup>5</sup> Immigrants from outside the EU can now obtain residence and work permits directly from the German embassy in their country of origin, and the two permits can now be issued simultaneously. A permanent residence permit is granted to applicants who have had a residence permit for five years. Foreign students who have studied in a German university have one year to find work. Under some circumstances permanent residence permits can be granted immediately to a graduate immigrant if other members of their family also receive work permits.

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