

Germany's short-time work scheme: can its past success be replicated?

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Germany has avoided a large jump in unemployment in the early stages of the COVID-19 recession, just as it did during the global financial crisis (GFC). One important factor in this success is the well-established short-time work (STW) scheme (Kurzarbeit), whereby the government subsidises wage payments for employees whose hours are cut at companies in temporary distress. Countries such as Austria, Switzerland and Italy have similar established schemes, while others such as the UK, Denmark and Latvia have just recently implemented job retention schemes. A number of questions are pertinent for countries looking to learn from the German experience: how many jobs have been saved by STW, what are the fiscal costs and how much does the scheme's success depend on the specific institutional settings in Germany?

In its current form the scheme functions as an automatic stabiliser, as companies are generally eligible to use STW if they face a major drop in activity for economic reasons or due to extraordinary events, provided the drop is temporary and unavoidable. The application process is fairly streamlined. After notifying the labour agency of the intent and demonstrating the need to use STW, firms are flexible in the actual take-up in terms of both workers and individual work-time reductions. Similar to previous economic crises such as the GFC, exceptional measures to extend the scheme during 2020

could be readily implemented including:

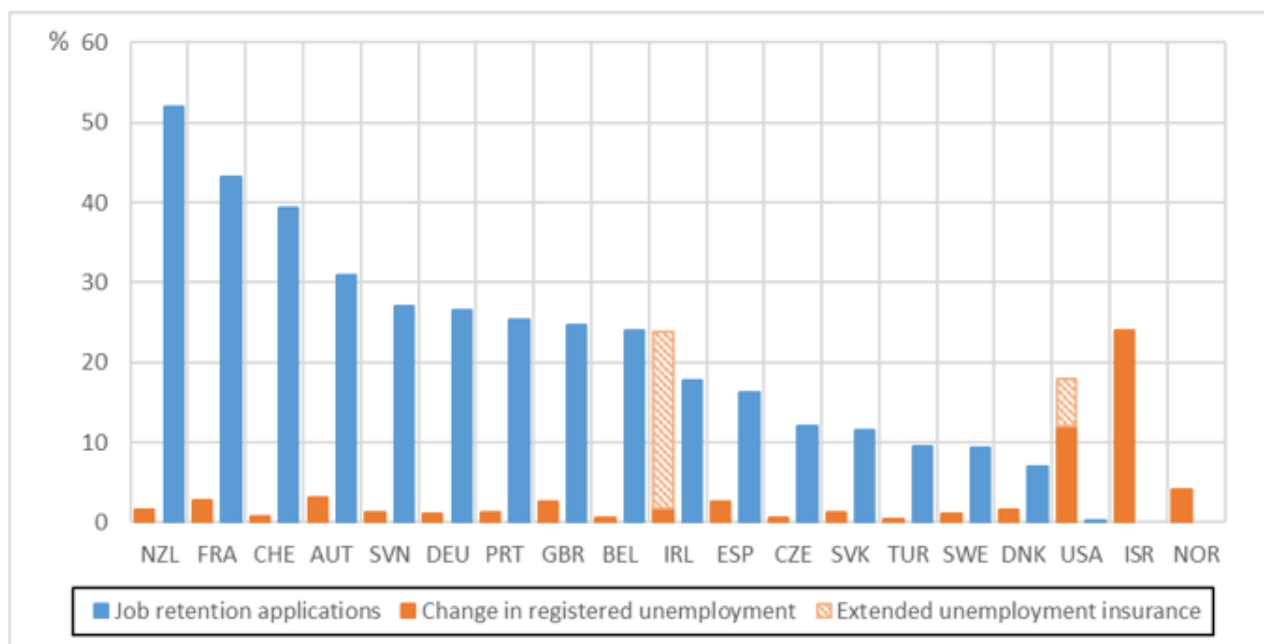
- The eligibility threshold for the share of workers affected by a lack of demand within a firm has been lowered from one-third to 10%, and temporary agency workers made eligible.
- The labour agency reimburses 100% of social security contributions for lost working hours (usually covered by the employer).
- To shield workers from large earnings losses, the replacement rate of lost net earnings is increased from 60% for childless workers and 67% for workers with children to 70% and 77% from the fourth month if they have reduced their working time by at least 50%. In the seventh month, payments are increased further to 80% and 87%.
- Restrictions on taking part-time jobs while on STW have been lifted. The additional earnings are not credited against short-time working benefits as long as the total income does not exceed the previous income.

The key benefit of STW is moderation of the increase in unemployment during a downturn, with immediate payoffs through avoiding the large wellbeing and scarring costs of unemployment for workers and medium-term gains from maintaining viable job matches. Countries with large STW or job retention schemes have seen substantial take-up of these schemes alongside much smaller increases in unemployment during the current crisis (Figure 1). STW is estimated to have saved in the order of up to half a million German jobs during the GFC when at its peak around 1.4 million workers were in STW (Hijzen and Martin, 2013^[1]; Boeri and Brücker, 2011^[2]). Based on the number of notifications the labour agency estimates that 6 million individuals were in short-time work in April 2020. The flipside is that by subsidising existing

positions, STW can impede labour reallocation, reduce the probability that those without a secure job find work and slow job growth during the recovery (Cahuc, 2019_[3]; Hijzen and Martin, 2013_[1]).

Figure 1. Registered unemployment and applications to job retention schemes such as STW

March to end-May, % of labour force



Note: The change in registered unemployment refers to the difference between early March 2020 and the end of May as a fraction of the total labour force. Job retention applications refers to the workforce covered by applications to national job retention schemes since early March and until end of May, or closest available date. Actual take-up may be lower than the number of applications as only a subset of applying firms actually take up short-time work. Registered unemployment data are not seasonally adjusted, except for the United States. Registered unemployment includes workers on unpaid leave in Israel and on temporary layoffs in Norway. Extended unemployment insurance refers to COVID-19 Pandemic Unemployment Payment in Ireland and Pandemic Unemployment Assistance in the United States.

Source: Schwellnus, Koelle and Stadler, 2020_[4]

Will STW be an efficient instrument in the current crisis?

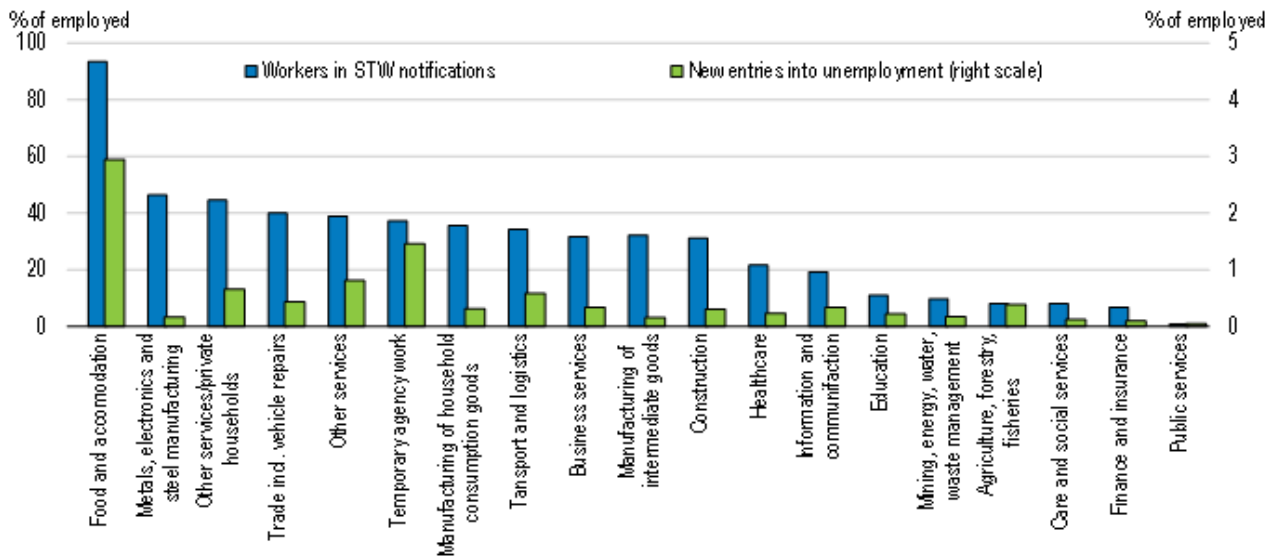
It remains unclear how well STW will perform in the current crisis, but it will be best-suited if there is a relatively rapid economic rebound without substantial changes to the sectoral composition of the economy (Schwellnus, Koelle and Stadler, 2020_[4]). STW was well-suited to dealing with the

downturn in Germany during the financial crisis as the sectoral composition of the economy changed little. No major industry grouping gained or lost more than 1 percentage point in its share of labour between 2008 and 2011, with manufacturing experiencing the biggest decline from 19% of hours worked to 18.2% (OECD, 2020_[5])

Certainly, the current crisis hit the economy faster and more broadly, as many stores and services were required to shut down completely. This is also visible from the concentration of STW notifications and movements into unemployment in those most affected sectors (Figure 2). However, in contrast to the GFC the decline in business activity has been determined by confinement and social distancing rather than pre-existing differences in firm performance, which is mirrored in the so far much greater reliance on STW rather than lay-offs (Weber and Gehrke, 2020_[6]). This suggests that the risk of locking workers in unviable jobs through the use of STW might be less pronounced. Sectoral shifts might be avoided again if the lifting of confinement measures continues and consumers' demand picks up quickly. In addition, Germany entered the current crisis with very low unemployment and a high degree of labour shortages making firms reluctant to lay off valuable workers. Nevertheless, sectors such as tourism, hospitality and aviation might be subject to longer-term interruptions. A fall in demand during the downturn might accelerate structural changes in some industries, such as automotive manufacturing. As a result, reallocation of labour might become more crucial. In this case, relying on STW for an extensive period might be less efficient than implementing measures focusing more directly on job creation.

Figure 2. Degree of STW and unemployment varies across sectors

Cumulative share of employees within sector mentioned in notifications of STW in March and April 2020 & share of previously employed individuals entering unemployment



Note: New entries into unemployment measure the cumulative number between the cut-off dates of mid-March and mid-May in comparison to the previous year. In line with the calculations of the share of workers mentioned in STW notifications by the Bundesagentur für Arbeit, the number of entries into unemployment are also relative to the number of employees within each sector at the end of September 2019. Source: Bundesagentur für Arbeit; own calculations.

Some current additional measures increase the efficiency of the scheme. For example, expansion of STW to allow part-time working in a second job is positive as it facilitates reallocation towards sectors with a temporarily higher labour demand. On the other hand, deadweight effects might increase with the full reimbursement of social-security contributions as it makes it less costly for firms to hold on to workers even if their job is not viable and they will be laid off eventually (Crimmann, Wießner and Bellmann, 2010^[71]).

How much does it cost?

The fiscal costs from STW are generally low relative to the number of jobs saved. The costs to the labour agency of saving around half a million jobs during the GFC amounted to about EUR 4.6 billion in 2009 and EUR 3.1 billion in 2010

(Bundesagentur für Arbeit, 2011_[8]). Based on the estimate of 6 million workers in STW in April 2020, labour agency budget estimates suggest costs could have been running at almost 2% of GDP recently, with the increase in unemployment payments roughly a degree of magnitude smaller. By comparison, increases in unemployment benefits under expanded coverage were costing US governments around 5% of GDP in early May (including substantial increases in payment generosity) and the Israeli government just over 3% per cent of GDP in April.

The generosity of German STW payments is aligned with unemployment benefits, but may cost the government more upfront if it pays for reductions in hours for workers who would have been kept on anyway. Conversely, STW offers fiscal benefits because the government saves on the cost of helping those who become unemployed to find work. Compared with job-saving alternatives, STW schemes such as the German one have a lower cost per job (Cahuc, Kramarz and Nevoux, 2018_[9]). By allowing for a partial hours adjustment, the fiscal cost per worker covered is lower than job retention schemes that subsidise workers who stop work altogether. They are also better targeted than wage subsidies.

Can Germany's successes with STW be readily replicated?

There are some institutional settings that favour working time adjustments in Germany and may limit applicability to other countries. Stringent rules about layoffs make STW more pertinent to firms. Germany, like some other countries with extensive STW programmes such as France and Italy, ranks in the top 10 OECD countries for protection of permanent workers against dismissal (OECD, 2020_[10]). Protection includes notice

periods, during which the regular salary would have to be paid, and in some cases severance payments. Total costs averaged across different tenures reach almost 22 weeks of salary, among the highest in the OECD (World Bank, 2020_[11]).

Similarly, firing and re-hiring is more costly for firms that require specific qualifications such as technology-intensive production. At the time of the GFC, the turnover costs for low-skilled workers were around EUR 7000 in Germany whereas they were almost five times that high for qualified workers (Bach and Spitznagel, 2009_[12]). OECD research shows that technology- and skill-intensity is positively related to labour-hoarding tendencies during economic downturns (OECD, 2010_[13]). In this context, the relative importance of technology- and skill-intensive manufacturing in Germany may help to explain the modest response of employment to the decline in output during crises.

In addition, internal flexibility measures such as working hour accounts and reductions in weekly hours or overtime play an important role in working time adjustments in Germany and help cushion the effects of cyclical downturns. Such internal flexibility measures are often covered through collective bargaining agreements or agreed between the social partners, which might not be easily transferred to other countries.

What's to be learned?

In sum, the German experience shows that an established, flexible and quickly accessible STW scheme can help reduce the labour market effects of an economic crisis and save viable job matches when the downturn is short-lived, the sectoral

composition of the economy is not affected, and costly firing and hiring by firms might slow the recovery. For the German case, it remains to be seen whether COVID-19 will trigger the need for substantial reallocation of labour, undermining the benefits of keeping employees in their current jobs. Moreover, any such scheme needs to be tailored to country-specific institutional settings and the eligibility for different types of workers and their share in the economy have to be carefully considered. For example, even when they are eligible for STW it might still be easier for firms to lay off workers on fixed-term contracts, which across European OECD countries on average constitute around 8% of all workers in sectors hit heavily by the COVID-19 crisis (OECD, 2020_[14]). During the GFC, take-up of STW in Germany was lower in firms with a higher share of fixed-term contracts (Boeri and Brücker, 2011_[2]). Similarly, the self-employed cannot use STW and might need different support programmes. Many countries including Germany have established special funds for the self-employed. Finally, as STW is targeted at keeping incumbent workers in employment, it needs to be recognised that potential new hires such as young graduates and those currently unemployed do not benefit and may lose out if subsidised jobs hinder their own entry into the labour market. Rates of transition from unemployment to employment during April and May 2020 were the lowest ever recorded for those months, worse even than as unemployment approached its 2009 peak during the GFC (Bundesagentur für Arbeit, 2020_[15]).

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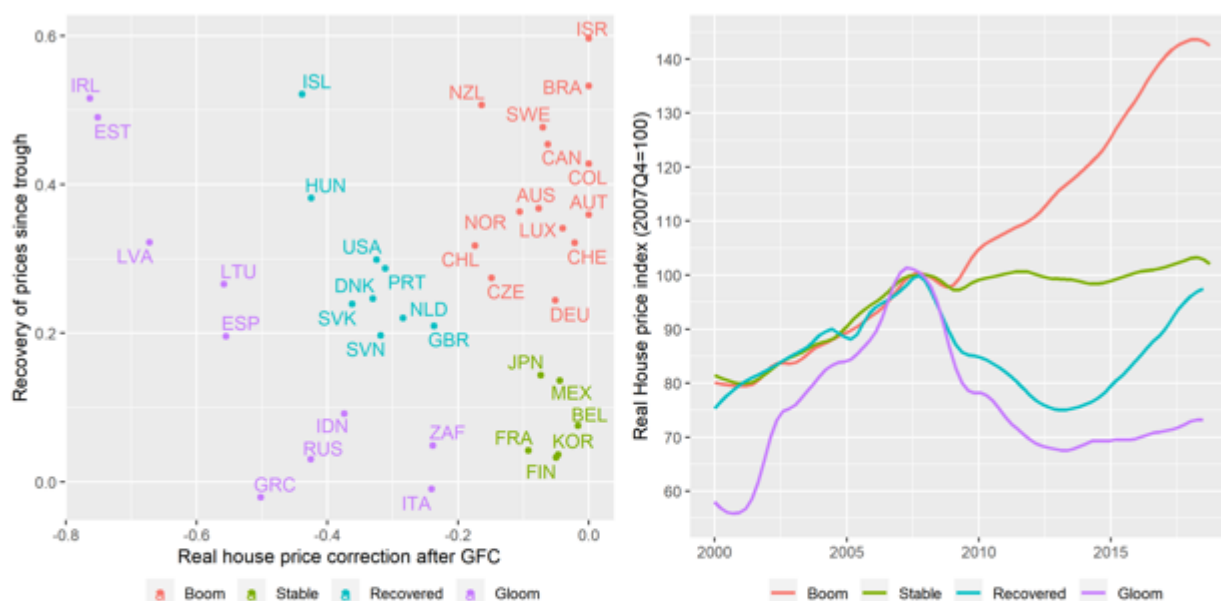
Are there ways to protect economies against potential future housing busts?

by Boris Cournède, Maria Chiara Cavalleri, Volker Ziemann, OECD

Housing, a large and volatile sector, is often at the centre of economic crises, as a trigger or amplifier. The current situation, which is characterised by house prices approaching or exceeding pre-crisis levels in many countries, raises questions as to whether these price levels may be indicative of a possible impending correction and what can be done to

reduce housing-related macroeconomic risks.

Figure 1. House price developments since the global financial crisis



Note: The right panel depicts average price movements per country group using local regression techniques. "Boom" and "Stable" countries encountered a limited price correction (<20%) during the global financial crisis. The former witnessed sharp increases thereafter (>20%) and the latter did not. "Recovered" and "Gloom" countries experienced a major real house price correction during the crisis (>20%). The former benefited from an equally strong rebound while the latter did not.

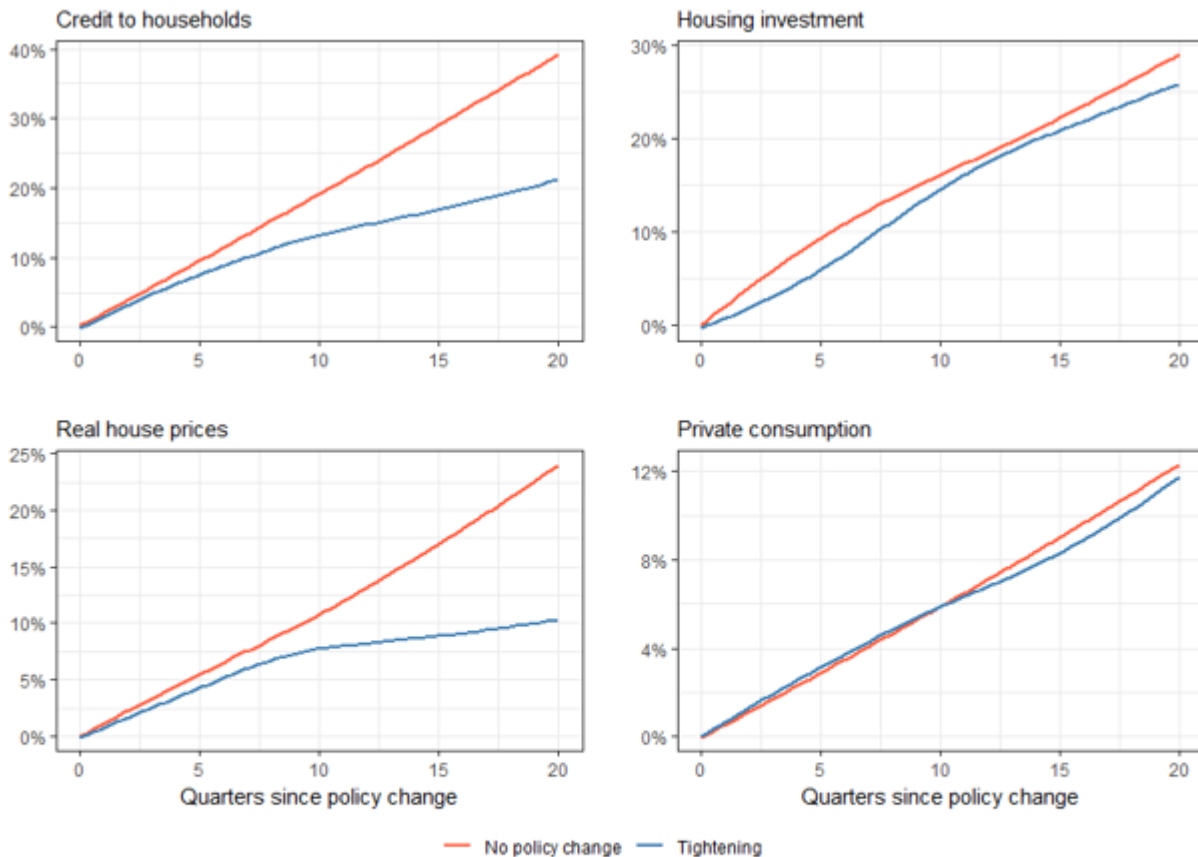
Source: Cavalleri, M. C., B. Courmède and V. Ziemann (2019), "Housing Markets and Macroeconomic Risks", *OECD Economics Department Working Papers*, No. 1555, OECD Publishing, Paris.

The OECD has been developing models that allow assessing to which extent economic trends associated with housing booms, such as steep house price increases or strong debt expansion, can fuel the risk of a severe economic downturn (Turner, Chalaux and Morgavi, 2018). About half of the countries covered by the models are estimated to face real yet limited risks (above 20% but below 30%) of experiencing a severe downturn over the medium term, with housing trends playing a significant role." Model results suggest that housing booms can fuel crisis risk domestically but also across borders as a consequence of international financial links (Cavalleri, Courmède and Ziemann, 2019).

Countries can reduce housing-related risks in particular by:

- Capping the size of loans relative to house prices. New evidence suggests that such caps are capable of containing house prices and mortgage lending incurring limited economic cost (Figure 2): housing investment is only marginally reduced and there is very little effect on consumption. Tighter loan-to-value ratios are also linked with a lower risk of severe downturns.
- Limiting the size of loans relative to income. This measure holds promising potential but has been seldom used so far, which means there is little scope yet to evaluate it ex post.
- Tightening bank capital requirements for riskier housing loans. Measures of this nature are linked to more moderate output fluctuations and stronger recoveries after downturns.
- Reducing the tax advantages given to housing assets. Higher effective taxation of housing assets (which can come from higher property taxes or lower income tax breaks for housing) favours smoother housing cycles.

Figure 2. Effect of tightening LTV caps



Note: The treatment group consists of episodes where countries tightened their LTV caps at time=0. The control group comprises episodes where countries did not implement such a policy change although their conditions were otherwise similar. This treatment group has been determined by propensity matching techniques using a probit model with real and financial variables as covariates. The lines show averages for each group.

Source: Cournède, B., S. Sakha and V. Ziemann (2019), "Housing Markets and Economic Resilience," *OECD Economics Department Working Papers*, forthcoming, OECD Publishing, Paris.

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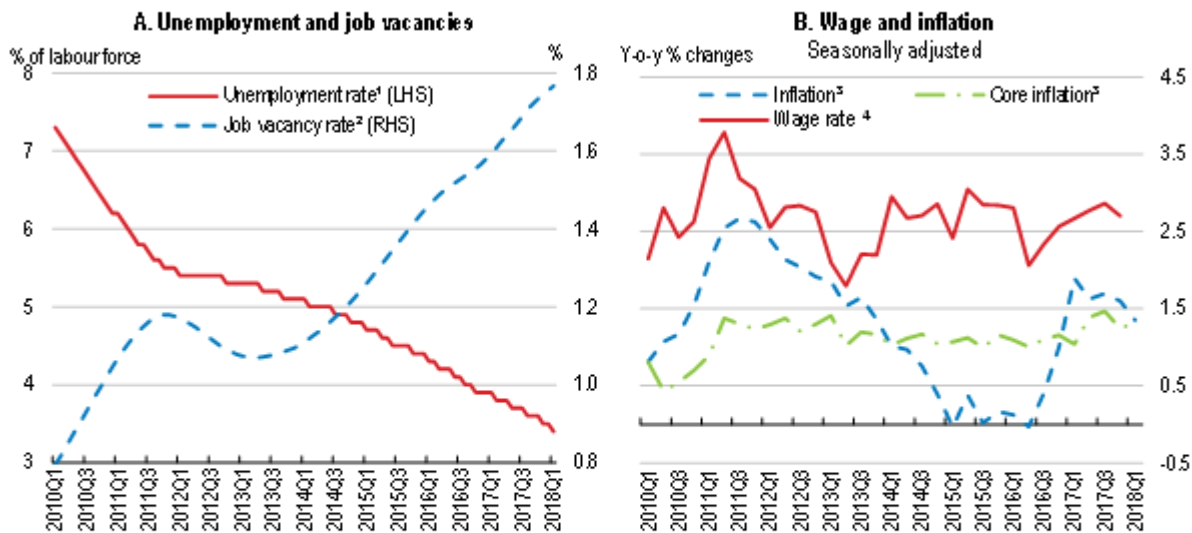
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Economic growth is strong and wellbeing is high but challenges lie ahead

by Andres Fuentes Hutfilter and Naomitsu Yashiro, OECD Germany Desk

Germany's strong and steady growth is set to stay – real GDP is projected to grow by 2.1% this year and next. Strong domestic demand and exports drive growth. As a strong exporter of capital goods, Germany is benefiting from the global recovery of trade and investment and the recovery in the euro area. Low interest rates and immigration boost residential construction. At 3.4% unemployment is record low, allowing wages to grow above inflation (Figure 1). Wages have grown across the board, breaking the trend of rising inequality and allowing private consumption to expand steadily. Germany also provides many jobs to immigrants, now mostly from Europe. Poverty is lower in Germany than in most OECD countries. But many workers are still on low wages, especially among women, the low and the middle-skilled (Figure 2). This may hold back growth if workers have little chance to move out of low-wage jobs. During the years of strong performance the government and businesses have reduced debt. Households also continue to save, in part for old age. The external counterpart of this is the large current account surplus.

Figure 1. The labour market is tight but nominal wage growth has remained broadly stable



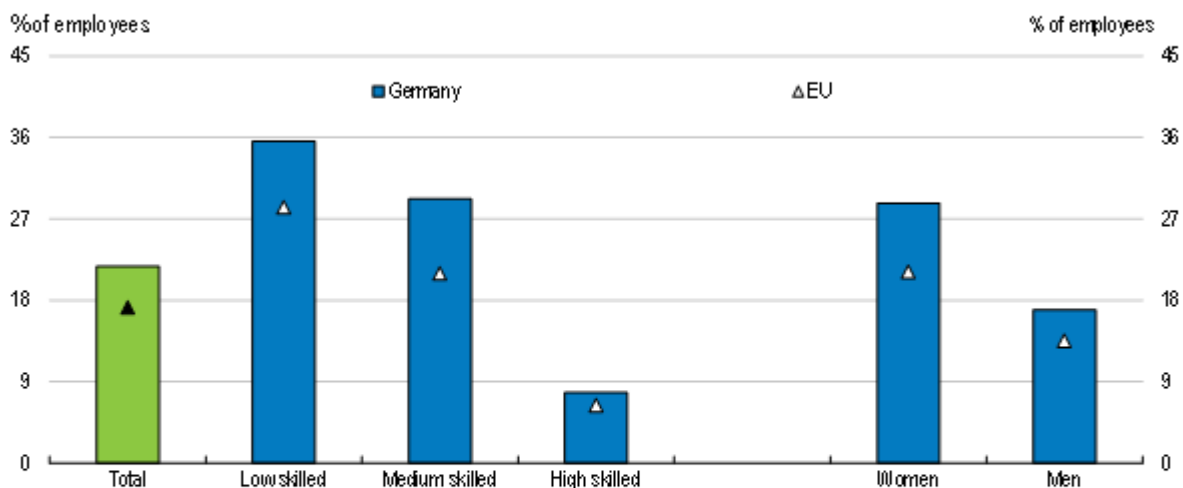
1. Population aged 15-74 years. Based on the German labour force survey.
2. Percentage of unfilled job vacancies relative to total employment.
3. Harmonised consumer price index (HICP). Core HICP excludes energy, food, alcohol and tobacco.
4. Average nominal wage per employee.

Source: OECD (2018), *OECD Economic Outlook: Statistics and Projections* (database) and Statistisches Bundesamt.

StatLink <http://dx.doi.org/10.1787/888933737381>

Figure 2. The incidence of low-pay employment is high

Low-wage earners by education and gender, 2014



Note: Low-wage earners are defined as those employees earning less than two thirds of the median gross hourly earnings. Low skilled, medium skilled and high skilled are defined respectively as educational attainments of below upper secondary (ISCED 0-2), upper and post-secondary (ISCED 3-4) and tertiary (ISCED 5-8). All employees excluding apprentices working in enterprises with 10 or more than 10 employees and which operate in all sectors of the economy except: agriculture, forestry and fishing (NACE Rev. 2, section A); and public administration, defence and compulsory social security (NACE Rev. 2, sections O).

Source: Eurostat (2018), *Employment and working conditions* (database).

StatLink <http://dx.doi.org/10.1787/888933737248>

In this context, policy makers in Germany must ensure that strong social and economic outcomes are sustained in the

future and inequality and poverty risk are reduced further, in the light of several challenges: Trend productivity growth has slowed, in Germany and elsewhere. As elsewhere in the OECD, productivity across firms has increasingly diverged between leaders and other firms. In Germany SMEs are 20 to 30% less productive than large firms and business creation has slowed. New technologies must be exploited more to benefit the whole society, and to realise strong growth consistent with the low-carbon transition. Entrepreneurship should be fostered through a more flexible insolvency regime, good e-government services and better access to high speed Internet. At the same time, technological change requires workers to adapt to new and changing jobs throughout their life time by updating skills. Across the OECD, middle-skill jobs have been the most affected by changes in tasks and automation. Technological change requires workers to adapt throughout their life time. The strong fiscal position provides room in the near term to fund spending priorities that will raise growth and wellbeing durably. Boosting investment in skills and technology and employability at higher age can also help reduce the current account surplus. The new government's coalition agreement contains welcome steps in this direction.

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Germany 's

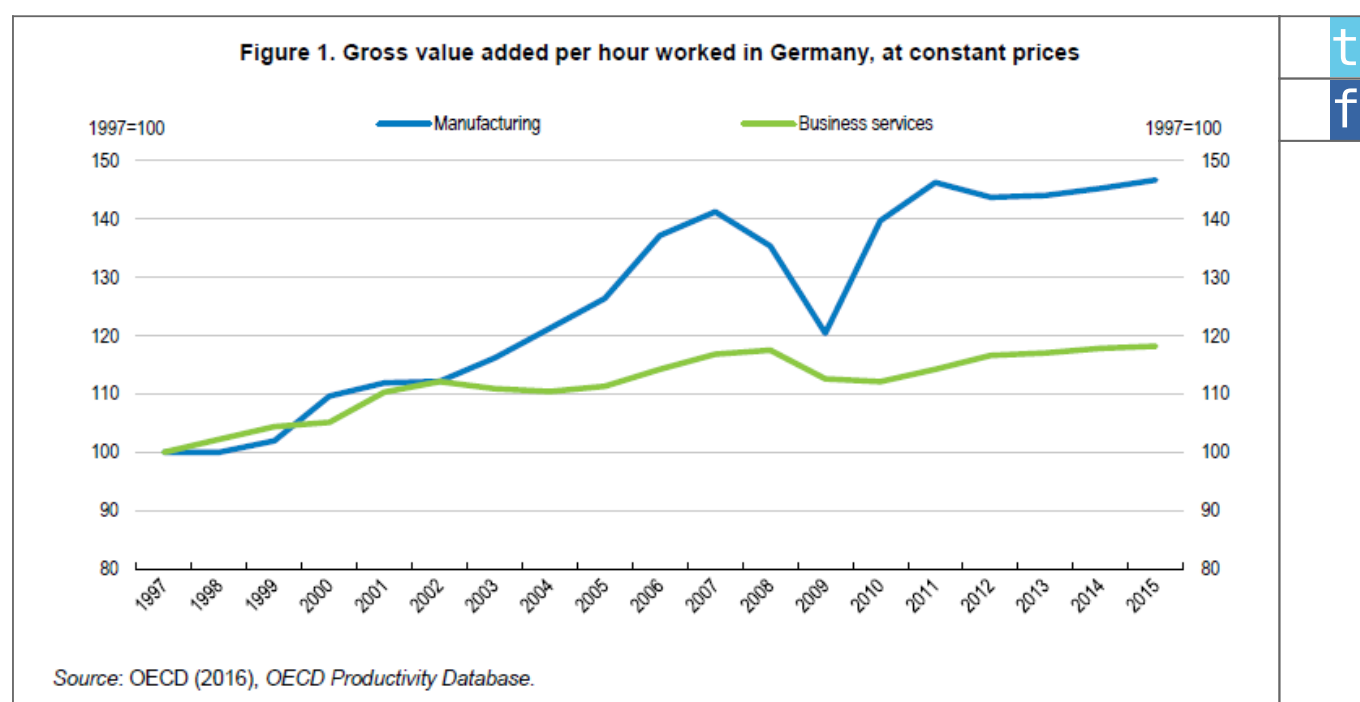
economic

performance is strong but productivity and investment need a boost

By Andres Fuentes, Head of German Desk, OECD Economics Department

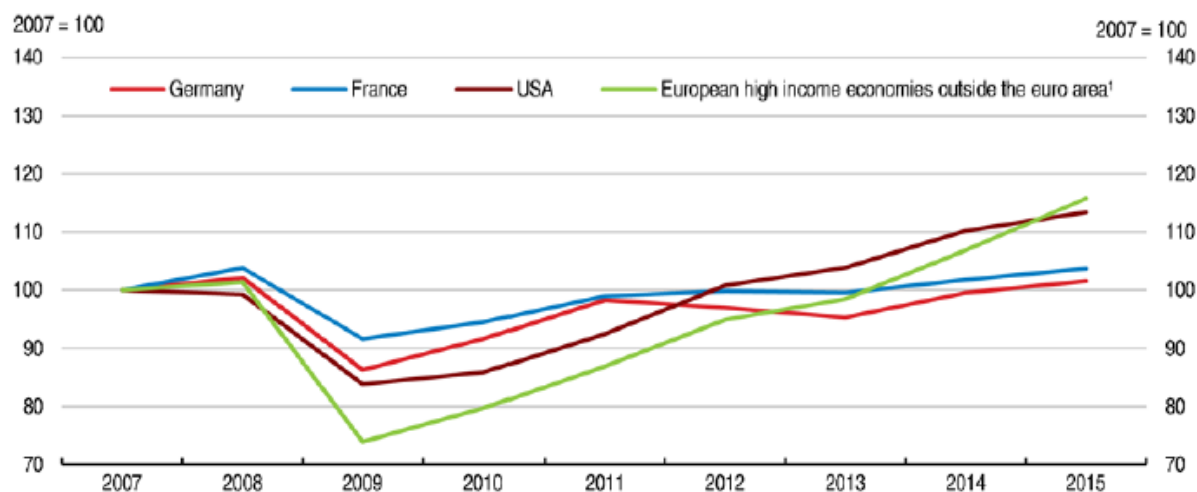
The German economy has steadily recovered from the 2008 global crisis. Thanks to past reforms, the labour market has proved strong and export performance has been impressive. The unemployment rate is now the lowest in the European Union. On the back of rising wages, private household demand has strengthened. Germany has lower income inequality than most OECD countries and scores well in most dimensions of well-being. The recently introduced minimum wage has improved the income situation of many low wage earners.

So economic performance has been excellent. But there is a weak spot: Labour productivity has grown little since the outbreak of the crisis (Figure 1) and is relatively low in the services.



In part this is because business investment has been weak in both physical assets, like machinery, and knowledge based capital (KBC, like intellectual property and software) (Figure 2).

Figure 2. Business investment has grown little in recent years



1. Includes Denmark, Sweden, Switzerland and the United Kingdom. They are weighted on the basis of investment spending in 2011. Source: OECD (2016), OECD Economic Outlook: Statistics and Projections (database), and OECD calculations based on OECD Economic Outlook: Statistics and Projections (database) and on Main Economic Indicators Database.

Demand is a key determinant of business investment. Weak demand conditions in geographically close export markets and increased uncertainty, notably in the euro area, have been particularly damaging to investment. Policies that improve stability and growth prospects in the euro area would therefore raise German investment and its economic potential. Reinvigorating investment in Germany would also reduce its large current account surplus, and thereby promote more balanced global growth.

Reducing regulatory barriers to competition and market entry stimulates business investment and improves productivity. In Germany investment in KBC is particularly low in the services. Some regulations in professional services and the network industries are too restrictive, and easing them would boost productivity throughout the economy because these services are inputs to downstream economic activities (IWU, 2015). For example, restrictions on advertising and firm ownership should

be eased. In broadband networks, technologies which supply the fastest speeds, notably “fibre to the home”, have barely been deployed. This has held back IT investment and the greater use of IT as a productivity generator.

Policies to avoid incumbents’ interests disproportionately affecting the design of regulation can raise innovation and productivity. Germany has made significant improvements to its regulatory policy system, but the administration could focus more strongly on the analysis of the economy-wide impacts of policies, rather than on sector-specific impacts, and on efforts to improve transparency of lobbying.

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