

The German Labour Market and Active Labour Market Policies - A Brief Overview

4.1 Introduction

The German labour market is plagued by persistently high unemployment in combination with a clearly separated situation on the labour markets in West and East Germany. After a slight recovery at the end of the 1990s, unemployment rates have risen again to 9.3% in West and 20.1% in East Germany in the year 2003. The Federal Employment Agency ('Bundesagentur für Arbeit', FEA) spends substantial amounts of the fiscal budget to overcome this unemployment problem. A particular emphasis in recent years has been laid on active labour market policies (ALMP), as the spendings of 12.3 bn Euro in West Germany and 8.9 bn Euro in East Germany reflect. The main purpose of ALMP is the permanent integration of unemployed persons into regular employment, i.e. to balance labour demand and supply. Unemployment should be circumvented by an efficient filling of vacancies and the increase of the individual employment chances by upgrading worker's human capital or worker's employability. ALMP were first introduced in Germany in the late 1960s. Since then, the set of programmes has been gradually adjusted to important changes on the labour market, like the oil price shocks during the 1970s or the growth of the labour market after the German Re-Unification. The general tendency to use more activating elements of labour market policies in the 1990s has led to a major reform step which cumulated in the introduction of the Social Code III in 1998 as the legal basis for ALMP. Within that reform, new instruments were introduced, competencies were decentralised and a more flexible allocation of funds has been made possible. Maybe the most important change from an evaluator's point of view was the legal anchoring of a mandatory output evaluation for all ALMP measures. As a consequence, new administrative datasets have been made accessible for scientific research. Evaluation of labour market policies before that was mainly based on survey data like the German Socio Economic Panel (GSOEP) or the Labour Market Monitors of East Germany and Sachsen-Anhalt. Clearly, the main problem

with these datasets was the relatively small number of observations which did not allow to properly take into account effect heterogeneity, e.g. due to individual characteristics like the previous unemployment duration, different skill levels or the age. As we will show later on, this is not a problem for our analysis, since the administrative data we use allows to draw on large groups of participants and examine several sources of effect heterogeneity.

In conjunction with the introduction of the Social Code III, the importance of ALMP rose significantly. The share of ALMP in per cent of the total spending of the FEA rose from 21.7% in 1997 to 30.6% in 2000 in West Germany and from 37.8% to 40.0% in East Germany. Shifting resources from passive labour market policies (PLMP) to ALMP in East Germany was less successful, since unemployment benefits are entitlement programmes, where a rising unemployment automatically increases public spending on passive income support. The unemployment rate dropped from 11.0% in 1997 to 8.0% in 2001 in West Germany, whereas the decrease in East Germany was much lower from 19.5% (1997) to 18.8% (2001). However, following this satisfactory development, the situation worsened again at the begin of the new century, bringing the unemployment rate back to very high levels.

Due to this disappointing situation, the reform process on the German labour market is still ongoing. More reforms, which have become to be known as the ‘Hartz-reforms’, are implemented gradually (see Bundesministerium für Wirtschaft und Arbeit (2003)).¹ Whereas the change from AFG to the Social Code III was mainly characterised by an emphasis on ALMP, the new reforms also tackle the second pillar of labour market policies, namely the unemployment benefits. The tendency is to gradually limit access to unemployment benefits and to lower their level. Since we focus in our empirical analysis on the time period from 2000 until 2002, we are not going to discuss the current reforms here. A good overview of the most relevant issues can be found in Hagen and Spermann (2004).

The aim of this chapter is to present the institutional setup and the most relevant instruments of ALMP for the time period under consideration in our empirical analysis (section 4.2). The focus will lie on job creation schemes since these are the programmes which will be evaluated in chapters 5 and 6. In section 4.3 we will present the previous empirical studies on the effects of JCS both on the micro- and macroeconomic level. Following that we introduce the dataset used for our analysis in section 4.4. Finally, section 4.5 outlines the further steps of our empirical analysis.

¹ Peter Hartz was the chairman of a commission initiated by the Federal Government to provide suggestions for the reduction of unemployment and the reorganisation of the Federal Employment Office (which has been renamed to Federal Employment Agency). The title of the commissions report is ‘Modern Services on the Labour Market’ (Bundesministerium für Wirtschaft und Arbeit, 2003).