

1 Introduction, Summary, and Conclusions

1.1 Basic Conditions in Germany: A Stylized Review

Germany's job market is in a deep crisis.¹ Economists are in general agreement that unemployment in Germany is not the result of economic cycles but is, instead, rooted in structural causes. The original German model of social market economy (*Soziale Marktwirtschaft*) emphasized the principle of subsidiarity and thus self-help. However, the development of unions and employer associations, and the resulting actions of political parties interested in the patronage of such entities, have changed the original German model into one of an all-embracing welfare state that guarantees individuals their acquired standard of living. This evolution is partly due to Germany's history of being a protected industrial society where labor agreements could be negotiated between employers and employees that promised noncompetitive wages regardless of the employees' productivity, a situation particularly true for unskilled and semi-skilled employees. Employers profited from conflict-free relations with their employees and thus from relatively few strike days. Individuals who remained unemployed due to non-market-clearing wages and excessive individual reservation wages did not suffer much, if at all, due to the elaborate welfare state that guaranteed them a high standard of living. In fact, there was very little incentive to seek full- or even part-time employment.

The world has changed dramatically in the last couple of decades, however. Globalization is on the steady increase due to improvement of transportation infrastructure and communication, increasing international capital mobility, and the collapse of the Eastern Bloc, as well as the reduction of trade barriers (e.g., the European Union). Enterprises are increasingly under pressure from international competition. Companies use their connections and networks to shift labor-intensive production to areas of the globe that can offer competitive wages, a situation that has had an espe-

¹ As the following analyses widely refer to West Germany (except for chapter 3), this short review will not focus on East-German-specific problems.

cially strong impact on low-skill jobs in the home country. In contrast, at least in Germany, capital-intensive production is not affected by shifting employment to low-cost countries. Rather than cheap labor, a highly developed infrastructure and a great degree of legal certainty are more important and beneficial to capital-intensive production. However, in the wake of the eastern enlargement of the European Union, even these factors will not be able to keep business in Germany as its neighbor states will also be able to guarantee these conditions.

Under these circumstances, it is no surprise that the promotion of business start-ups has been the focus of economic policy. The goal is to encourage employment-effective macroeconomic development. It is believed that innovative business start-ups, especially in the service sector, will create employment for those individuals whose jobs have been lost, particularly the secondary-sector employees. In addition to these direct job-creating effects, innovative business start-ups are expected to induce growth impulses (supply-side effects) due to the intensified competition they will engender, thus leading to efficiency gains and more innovation (cf. Fritsch and Mueller 2004; Fritsch et al. 2005).

It is the emergence and survival of these new businesses that is the subject of this introductory chapter, which proceeds as follows. Section 1.2 provides a short description of the data and the methods of analysis applied in this book. Section 1.3 summarizes the growth and employment effects of new business formation. Chapter 2 and 3 will treat these effects more extensively. Section 1.4 gives the main findings of chapters 4 through 6 on the determinants of the emergence and survival of new businesses. Section 1.5 summarizes the main theses of this book and draws some policy conclusions.

1.2 Data and Methods of Analysis

Direct, comprehensive data on new business formation are unavailable in Germany. However, it is possible to extract this sort of information from the German Social Insurance Statistics of the Federal Employment Services.² These statistics began to be collected in West Germany in 1973 and are derived from public health, pension, and unemployment insurance reports. Each business with at least one employee subject to social security receives a unique, permanently assigned code number; the code number is thus an identifier for the business. Thus, a code number occurring for the

² See Fritsch and Brixey (2004) for a description of this data source.