
THE TRUE COST OF AUSTERITY AND INEQUALITY

Germany Case Study

Germany's economic and social development since the financial crisis is quite distinct to the other economies of the Eurozone. Although the country suffered a sharp decline in growth, falling from 3.4 per cent in 2007 to 0.9 per cent in 2008 and -5.1 per cent in 2009, the recovery came fast with a positive growth rate of 4 per cent in 2010 and 3.1 per cent in 2011. In 2012 it slowed again to 0.9 per cent with a forecast of 0.3 per cent for 2013, while the Eurozone as a whole remains in recession.¹

The German Federal Government, like many other European Union member states, took measures to bail out insolvent banks and stimulate the economy to prevent its collapse. As a result of these actions, public debt rose from 65.4 per cent of GDP in 2007 to 82.5 per cent in 2010. But, unlike some countries in southern Europe, interest rates for German bonds remained at historically low levels, thanks to a side-effect of the Eurozone crisis: with many other Eurozone countries in trouble, Germany represents a safe haven for investors. As a result, it has been relatively easy for Germany to service its debt. At present, the net cost for the bailouts will be at least €70bn and, according to the International Monetary Fund (IMF), public debt will fall to 68.7 per cent of GDP by 2018.²

The unemployment rate in Germany was 7.8 per cent in 2008 and increased only slightly to 8.1 per cent in 2009. It then fell back to 7.7 per cent in 2010 and dropped to 5.5 per cent in April 2012.³ In part, this was the result of special flexibility measures in labour law that were already in place before the crisis, such as supplementing the wages from temporary short-term work through public subsidies. These measures were able to give the labour market a higher level of resilience. In 2013, however, unemployment has again begun to rise and had reached 6.8 per cent in May,⁴ but this is still half the rate of the Eurozone as a whole (12.4 per cent).

Alongside this, low levels of household debt and inflation⁵ suggest that Germany has not suffered as severe a crisis as other parts of Europe.

The idea has emerged that Germany could serve as a model to other European countries in dire economic straits; however, in order to understand the special dynamics of Germany after 2008 it is important to consider the deeper mechanisms of the country's 'success story'.

Competitiveness – the core of the 'German model'

The main reason both for the sharp decline in 2009 and the fast recovery is the German economy's strong reliance on exports. In 2012, 41.5 per cent of German GDP depended on exports. This represented a dramatic increase of more than a third over the previous decade, from 30.5 per cent in 2002.⁶ It has led to an enormous trade and current account surplus of 6.3 per cent of GDP (second only to China in size) between 2008 and 2012, while the average for advanced economies in this period was a deficit of 1.5 per cent.⁷ When the global economy stumbled as a result of the crisis, Germany was hit hard, but when the global economy went up again, thanks to the recovery in China and other emerging economies, German exports became again the locomotive for growth.

However, the competitiveness of the German economy has also two strongly negative sides:

- it is a driving factor behind the economic imbalances within the Eurozone and hence is adding to the difficulties faced by crisis-affected countries as they seek to recover;
- it has a high social price to be paid by the majority of the population.

This increased competitiveness lies partly in structural competitive advantages such as a large share of manufacturing, advanced technologies, and a skilled labour force. But it also has its roots in a set of neo-liberal reforms undertaken since 2002, the so-called *Agenda 2010*. This was a neo-liberal reaction to the poor performance of the German economy after re-unification. At its core were labour reforms ('*Hartz IV laws*') introduced by the coalition government of the Social Democrats and the Green Party under Chancellor Gerhard Schröder.

These reforms consisted of sharp cuts in unemployment benefits, making labour more flexible by weakening the trade unions, applying heavy bureaucratic pressure on the jobless, reducing social security, such as pensions, and raising the age of retirement from 65 to 67. Real wages fell on average by 1.6 per cent a year from 2002 to 2012, falling fastest once the reforms were introduced, with the years between 2002 and 2007 seeing a drop of 3.9 per cent.⁸ Only since 2010 has there been an increase in real wages of 2.85 per cent which continued until 2012. The gender gap in wages remained more or less the same throughout the decade at 19.4 per cent in 2010.⁹

The reform package was accompanied by a wave of privatizations of public services, such as water and public transport, along with tax reductions for corporations and those in high-income bands, while VAT was raised from 16 to 19 per cent in 2007.

In other words, the neo-liberal austerity policies, which now dominate the European crisis management, had already been implemented in

Germany before 2008. Taken as a whole, the Schröder reforms shifted the balance of power between capital and labour considerably in favour of capital.

Insecurity, poverty and inequality – the flip side of the ‘German model’

The social costs of this shift have been high. Germany is experiencing a new phenomenon: a dramatic increase in precarious jobs with extremely low wages (creating what is otherwise known as the ‘working poor’), little or no social security or protection of workers’ rights. The number of jobs of this type has increased from 4.3 million in 2001 to 7.8 million in 2010, accounting for one-third of the total wage labour force.¹⁰ The gender gap in this area is particularly high: 34.1 per cent of women are working in these jobs compared to only 12.3 per cent of men.¹¹

The Schröder government’s reforms also exacerbated the trend of rising poverty.¹² The level of poverty in Germany increased significantly from 11.8 per cent in 2000 to 15.2 per cent in 2007. Since then, there has been a slight increase to 15.8 per cent in 2010.¹³ Women are most affected: in 2010, 16.8 per cent of women were poor compared to 14.9 per cent of men. There are marked differences between western and eastern Germany. In 2010, 14.3 per cent of the population in the west were poor compared to 22.2 per cent in the east.

The impact on the wealthy

Inequality both in income and wealth distribution is also increasing. In 1991, the GINI coefficient (the measure of inequality within a country¹⁴) for real household market income was 0.41. It peaked in 2005 at 0.48, before falling to 0.47 in 2010. This high level of market income inequality has prompted considerable efforts to reduce net income inequality – after taxes and transfers – which is currently 0.29. Indeed, the redistributive impact of household taxes in Germany is among the highest in the OECD.¹⁵ While net financial assets have increased across Germany from €1.19 trillion in 1991 to €3.39 trillion in 2010, ten per cent of the population now own 60 per cent of these assets, while 50 per cent have practically no assets at all.

Socio-economic development in Germany is broadly characterized by neo-liberal policies. It is therefore not surprising that Official Development Assistance (ODA) is also coming under pressure. Whereas, in the past, ODA was always growing, in some periods considerably, for instance from \$5bn in 2001 to \$14.1bn in 2011,¹⁶ it has since remained comparatively low at 0.38 per cent of GNI.¹⁷ Moreover, there is an unprecedented move ahead: in 2014 resources for German development cooperation will be cut by €245m, and another cut of €160m is planned for 2015.¹⁸

NOTES

- ¹ IMF (2013) 'World Economic Outlook 2013', Washington: IMF, <http://www.imf.org/external/pubs/ft/weo/2013/01/>
- ² IMF (2013) *op. cit.*
- ³ The unusual fact, that the unemployment rate among German women is lower than for men is due to a generally lower employment rate of women compared to other advanced economies. Hence, it does not reflect a progress but a lagging behind.
- ⁴ 'Zahl der Erwerbstätigen im April 2013 erneut um 0,7 % höher als im Vorjahr', Statistisches Bundesamt, https://www.destatis.de/DE/PresseService/Presse/Pressemitteilungen/2013/05/PD13_180_132.html
- ⁵ IMF (2013) *op. cit.*
- ⁶ 'Foreign trade', Statistisches Bundesamt, <https://www.destatis.de/DE/ZahlenFakten/GesamtwirtschaftUmwelt/Aussenhandel/Handelskennzahlen/Tabellen/Exportquote.html>
- ⁷ IMF (2013) *op. cit.*
- ⁸ Aggregated decline for this period
- ⁹ 'Persistenz im Zeitverlauf', WSI, <http://www.boeckler.de/39135.htm>
- ¹⁰ Arbeitsgruppe (2013): 'Memorandum 2013: Umverteilen – Alternativen der Wirtschaftspolitik', Cologne: PapyRossa, http://www2.alternative-wirtschaftspolitik.de/uploads/memorandum2013_tabellen.pdf
- ¹¹ DGB Abteilung Sozialpolitik (2012) 'Licht und Schatten im Beschäftigungssystem', Arbeitsmarkt aktuell, Berlin: DGB Bundesvorstand, http://www.sozialpolitik-aktuell.de/tl_files/sozialpolitik-aktuell/Politikfelder/Arbeitsmarkt/Dokumente/Licht%20und%20Schatten.pdf
- ¹² According to EU definition of poverty line: 60 per cent of median income
- ¹³ Bundesministerium für Arbeit und Soziales (2013) 'Der Vierte Armuts- und Reichtumsbericht der Bundesregierung', Berlin, P. 461, <http://www.bmas.de/DE/Service/Publikationen/a334-4-armuts-reichtumsbericht-2013.html>
- ¹⁴ The Gini coefficient ranges from zero to one, with zero as the complete absence of inequality and one as complete inequality.
- ¹⁵ OECD (2012) 'Income inequality and growth: The role of taxes and transfers', OECD Economics Department Policy Notes, No. 9, <http://www.oecd.org/eco/public-finance/49417295.pdf>
- ¹⁶ OECD (2012) 'Development: Aid to developing countries falls because of global recession', <http://www.oecd.org/newsroom/developmentaidtodevelopingcountriesfallsbecauseofglobalrecession.htm>
- ¹⁷ OECD (2013) 'Aid to poor countries slips further as governments tighten budgets', <http://www.oecd.org/newsroom/aidtopoorcountrieslipsisfurtherasgovernmentstightenbudgets.htm>
- ¹⁸ 'Bundeshaushalt', VENRO, <http://venro.org/themen/haushalt/>

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