

Hartz IV reform did not reduce unemployment in Germany

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The Hartz IV reform of the German labor market has been one of the most controversial reforms in the history of the reunited Federal Republic of Germany. It has been widely seen as the end of the welfare state leading into poverty. At the same time, Germany has been able to reduce its unemployment rate over the last years more than almost any other European or OECD member country. What role did the Hartz reforms, and the Hartz IV reform in particular, play in this success story? A recent publication by Junior Professor Andrey Launov and Professor Klaus Wälde of Johannes Gutenberg University Mainz (JGU) shows that the Hartz IV laws had indeed no noteworthy impact on the decrease of unemployment in Germany. Just in contrast to that, the Hartz I to Hartz III reforms appear to have been more helpful.

Throughout decades [unemployment](#) benefits continue to remain an important tool used by policy makers to regulate performance of the labor market. In the recent past many economists have argued that too high [unemployment benefits](#) in the most of the European countries have led to too rigid and inefficient labor markets. They reduce incentives of unemployed workers to look for jobs and largely contribute to high and persistent unemployment. With unemployment rates crossing the benchmark of 10 percent in nearly all major European economies between the early 1990s and the early 2000s, a number of European governments have responded with various labor market reforms. Not surprisingly, a reduction of unemployment benefits has become the core part of these reforms.

Germany was not much different from its European neighbors. Between 2003 and 2005 it implemented a series of so-called Hartz reforms of the labor market. Among these the notorious Hartz IV reform of 2005 was reducing unemployment assistance benefits for the major part of the German workforce. It was also cutting the time period during which unemployment insurance benefits were to be paid. While the government aspired to curb unemployment, the danger of Hartz IV was obviously in hurting the least socially protected, such as for instance the long-term unemployed with low chances of finding a job. Indeed, the reform has quickly assumed a negative image in the perception of the general public. It was widely felt that Hartz IV is really "the end of the welfare state" and overall harmful to workers.

The new study by Launov and Wälde, published in the renowned *International Economic Review*, looks into various impacts of the Hartz IV reform on the entire German labor market and on the different groups of workers. This study finds that contrary to initial aspirations the contribution of the Hartz IV reform to reducing unemployment in Germany as a whole has been exceptionally low. In fact, the reform can explain only 0.1 percentage point of the post-Hartz decline of the [unemployment rate](#).

The reason for that is to be seen in the reform's changes to replacement of employment income. The threat of ending up with lower unemployment assistance benefits once [unemployment insurance](#) expires is very low for high- and medium-wage earners. These workers as a rule find new jobs much faster than they would need to face the benefit cuts arranged under Hartz IV. So for them Hartz IV was virtually inessential. For low-skilled low-wage earners, who constitute the main part of long-term unemployment, the difference between their benefits before Hartz IV ("Arbeitslosenhilfe") and after Hartz IV ("Arbeitslosengeld II") turns out to be often too small to make any impact. Objective difficulties with regard to the employability of such workers make the benefit reform

even less useful.

The reform has scored a stronger impact on the labor market in the East Germany compared to West Germany, though even here it was lagging behind the initial expectations.

Nevertheless, unemployment in Germany has sharply fallen after the whole set of Hartz reforms became legally effective. Launov and Wälde point out that the impulse to this success comes most likely from the earlier packages of the reform, such as for instance from restructuring of the Federal Employment Agency as part of the Hartz III reform. The creation of job centers, the introduction of a single contact address for all claims by unemployed, the lowering of the number of unemployed per case worker, and other actions and measures under arrangements of Hartz III helped to reduce the unemployment rate by 1,3 percentage points. The reform of the Federal Employment Agency as such was thus considerably more effective than the reduction of benefits by Hartz IV. The Mainz economists conclude that the [labor market](#) indeed needed reforms but the particular composition of such reforms is the most crucial element of their success. "It has been proven that aspects such as a reduction of unemployment assistance benefits, which is difficult to deal with in terms of distribution policy, have brought us to rather negligible consequences," emphasize Launov and Wälde.

More information: Andrey Launov, Klaus Wälde, Estimating Incentive and Welfare Effects of Nonstationary Unemployment Benefits, *International Economic Review*, 25 October 2013 [DOI: 10.1111/iere.12032](#)

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