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# Hysteresis in Unemployment Rates? A Comparison between Germany and the US

By Uwe Hassler, Frankfurt a.M., and Jürgen Wolters, Berlin\*

JEL C14, C22, E24

Unemployment, hysteresis, fractional integration, change in persistence.

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## Summary

In this paper we compare the unemployment dynamics of the US and Germany with monthly data up to 2008. With data from 1971 on the evidence is mixed when applying descriptive methods or formal unit root tests. When allowing for fractional integration, however, we find similar results to the literature in that shocks to US data seem to be transitory while having permanent effects on German unemployment. This difference in hysteresis, however, depends on the sample. Using recursive and rolling techniques we observe that shocks in US subsamples until the mid-nineties are clearly more transitory than in more recent subsamples. We conclude that hysteresis has turned into a dominating feature also on US labour market more recently.

# **Wage Adjustment, Competitiveness and Unemployment – East Germany after Unification**

**By Werner Smolny, Ulm\***

JEL E24, O11, O52, P2

Wages, competitiveness, unemployment, economics of transition.

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## **Summary**

Nearly 20 years after unification large differences of the labor market situation in East and West Germany persist. Wages are still considerably lower, the unemployment rate is about twice of the West German level, and the competitiveness of the East German economy seems to be low. This paper analyzes the process of (relative) wage adjustment in East Germany and the resulting development of competitiveness and unemployment differentials. We present estimates of the wage adjustment in East vs. West Germany based on wage convergence and effects of unemployment on wage growth. The central focus of the paper is the empirical analysis of the interaction of the development of competitiveness and the labor market situation. The results reveal large equilibrium gaps for wages and unemployment which are based on the wage-setting process, the behavior of competitiveness and the adjustment of unemployment.

# Oil and Unemployment in Germany

By Andreas Löschel, Mannheim, and Ulrich Oberndorfer, Berlin\*

JEL Q43, E24

Oil price, unemployment, Germany.

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“...for those who have yet to be convinced, I hereby renew the forecast – sometime again within the next ten years, turmoil in the Middle East will produce another major disruption to world petroleum supplies. The crisis will produce a recession”.

*Hamilton (1996)*

## Summary

In this paper, we analyze oil price impacts on unemployment for Germany. Firstly, we survey theoretical and empirical literature on the oil-unemployment relationship and relate them to the German case. Secondly, we illustrate this issue within the framework of a vector autoregression (VAR) approach for Germany. For this purpose, we use three different specifications in order to adequately address the uncertainty related to the construction of an adequate oil variable. Using monthly data from 1973 to 2008, we show that oil price increases induce a rise in unemployment in the German labor market. Moreover, for a restricted sample period for post-unification Germany, we oppose claims that the oil to macroeconomy relationship has weakened since the 1980s. However, our results suggest that it has become more important to construct adequate measures of oil price variables.

## **Living Standards in an Aging Germany: The Benefits of Reforms and the Costs of Resistance**

**By Axel Börsch-Supan and Alexander Ludwig, Mannheim\***

JEL J11, J21, D13, E27, H55, F16, F21

Aging, pension reform, labor market reform, labor supply reactions.

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### **Summary**

The extent of the demographic change in Europe and especially Germany is dramatic and will deeply affect future labor, financial and goods markets. The expected strain on public budgets and especially social security has received prominent attention, but aging poses many other economic challenges that threaten growth and living standards if they remain unaddressed.

This paper investigates the potential benefits of pension and labor market reform for growth and living standards, taking into account behavioral reactions to specific reforms. Which behavioral reactions will strengthen, which will weaken reform policies? While Germany has a large unfunded pension system and vulnerable labor markets, Germans show remarkable resistance against pension and labor market reform. Can Germany maintain its standard of living even if behavioral reactions offset some of the current reform efforts? The paper uses a novel modeling approach to distinguish between exogenous and endogenous components of labor supply in order to shed light on these questions.

## **Choosing from the Reform Menu Card – Individual Determinants of Labour Market Policy Preferences**

**By Friedrich Heinemann, Mannheim, Ivo Bischoff, Giessen and  
Tanja Hennighausen, Mannheim\***

JEL J48, D63, C42, A13

Labour market reform, economic beliefs, fairness preferences, ALLBUS.

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### **Summary**

This contribution empirically explores the drivers of labour market reform acceptance for the individual level in Germany. For that purpose we make use of the representative German General Social Survey (ALLBUS). This survey offers data to which extent individuals support benefit cuts, longer working years, cutting subsidies to declining industries, phasing out of employment programmes, or a liberalisation of employment protection. Our theoretical considerations suggest that self-interest, information, fairness judgements, economic beliefs and other individual factors such as socialisation under the communist regime in the former German Democratic Republic drive individual reform preferences. Our empirical results support this notion: While we find self-interest to be an important driving force, our results show that a number of factors well beyond the narrow scope of self-interest strongly shape individual reform preferences.

# Employment Adjustments on the Internal and External Labour Market – An Empirical Study with Personnel Records of a German Company

By Knut Gerlach and Olaf Hübler, Hannover\*

JEL J63, M51

Personnel records, overtime, promotion, job mobility, cancellation agreement, transfer organisation.

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## Summary

Firms are affected by the product demand. This leads to employment adjustments. In the literature we find only very few contributions investigating the issue whether internal adjustments are linked and which relationships exist with external adjustments. Are they of a complementary or substitutive nature? Furthermore, it is of interest to find out, whether we can observe an obvious trend and whether the adjustments are driven by cyclical movements.

For this study we have an extensive data set of a large German manufacturing company, which supplies innovative products for the domestic and international market, provided on a monthly base from January 1999 to December 2005. The empirical analysis starts with descriptive statistics. We find that the employment adjustment cycle coincides only to a certain degree with the macroeconomic cycle. Internal and external adjustments are more characterized by complementarity than by substitution. Over the observed period we cannot detect analogous wage adjustments. It is noticeable that in 2003 compared with the years before the number of employees is substantially reduced. The econometric investigation is based on a two-stage approach. We start with a bivariate probit estimation in order to extract the relationship between the probability of overtime and of promotion. Unobserved variables have opposite effects on the former and the latter adjustment instrument. Furthermore, we detect a negative trend of internal employment adjustments. Cyclical effects are ambiguous. The next step, the determination of external adjustments with respect to overtime and promotion adjustments, is split into two estimates. On the one hand we do not distinguish between the type of external employment adjustment and on the other hand we use this information separating between quits, layoffs, workers with a cancellation agreement and with a transition into a transfer organisation. The first approach demonstrates that a promotion reduces the probability to leave the firm while overtime is positively associated with an external job change. This pattern holds generally speaking in the second, more detailed estimates. Quits are the exception. In this case we observe opposite effects. Finally, we cannot detect any influences of promotions on cancellation agreements.

## Can a Task-Based Approach Explain the Recent Changes in the German Wage Structure?

By Dirk Antonczyk, Bernd Fitzenberger, and Ute Leuschner, Freiburg\*

JEL J24, J31, D31, C43

Wage inequality, occupations, tasks, skill biased technical change, polarization.

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### Summary

This paper investigates the changes in the German wage structure for full-time working males from 1999 to 2006. Our analysis builds on the task-based approach introduced by Autor et al. (2003), as implemented by Spitz-Oener (2006) for Germany, and also accounts for job complexity. We perform a Blinder-Oaxaca type decomposition of the changes in the entire wage distribution between 1999 and 2006 into the separate effects of personal characteristics and task assignments. In line with the literature, we find a noticeable increase of wage inequality between 1999 and 2006. The decomposition results show that the changes in personal characteristics explain some of the increase in wage inequality whereas the changes in task assignments strongly work towards reducing wage inequality. The coefficient effect for personal characteristics works towards an increase in wage inequality at the top of the wage distribution. The coefficient effect for the task assignments on the contrary shows an inverted U-shaped pattern. We conclude that altogether the task-based approach can not explain the recent increase of wage inequality in Germany.

# Firm Heterogeneity and Wages under Different Bargaining Regimes: Does a Centralised Union Care for Low-Productivity Firms?

By Nicole Guertzgen, Mannheim\*

JEL C23, J31, J51, L13

Wage-setting structure, unions, oligopoly, linked employer-employee data.

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## Summary

This paper studies the relationship between wages and the degree of firm heterogeneity in a given industry under different wage setting structures. To derive testable hypotheses, we set up a theoretical model that analyses the sensitivity of wages to the variability in productivity conditions in a unionised oligopoly framework. The model distinguishes centralised and decentralised wage determination. The theoretical results predict wages to be negatively associated with the degree of firm heterogeneity under centralised wage-setting, as unions internalise negative externalities of a wage increase for low-productivity firms. We test this prediction using a linked employer-employee panel data set from the German mining and manufacturing sector. Consistent with our hypotheses, the empirical results suggest that under industry-level bargaining workers in more heterogeneous sectors receive lower wages than workers in more homogeneous sectors. In contrast, the degree of firm heterogeneity is found to have no negative impact on wages in uncovered firms and under firm-level contracts.

## **Crime and the Labour Market: Evidence from a Survey of Inmates**

**By Horst Entorf, Frankfurt a.M.**

JEL C83, J38, K42

Inmates survey, recidivism, labour market, illicit drug use.

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### **Summary**

In this paper data from a survey of 1,771 inmates conducted in 31 German prisons provide microeconomic evidence on the relationship between individual anticipated labour market opportunities and the perceived probability of future recidivism. Results show that inmates with poor labour market prospects expect a significantly higher rate of future recidivism. Having a closer look at subgroups of prisoners reveals that drug and alcohol addiction cause adverse effects. Thus, improving prisoner health care by installing effective anti-drug programmes would be one of the most effective measures against crime.

# **The Creative Class, Bohemians and Local Labor Market Performance**

**A Micro-data Panel Study for Germany 1975–2004**

**By Joachim Möller, Regensburg, and Annie Tubadji, Nürnberg**

JEL Z10, C23, R1, O1, O3

Culture, regional development, Bohemians, creative class, dynamic panel methods.

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## **Summary**

The paper aims at testing Florida's concept of the Creative Class using panel data for 323 West German regions for the time period 1975–2004. Applying a dynamic system approach based on GMM, we find that the local concentration of the Creative Class has predictive power for the economic development of a region and tends to outperform traditional indicators of human capital. However, our results do not support Florida's assertion that the creative workers flock where the Bohemians are. According to our findings, the Creative Class is attracted by favorable economic conditions as indicated by employment growth or an increasing wage bill.

## **Spatial Implications of Minimum Wages**

**By Thiess Buettner and Alexander Ebertz, Munich\***

JEL J6, R12, J3

Minimum wages, urban poverty, spatial wage structure, mobility, economies of agglomeration.

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### **Summary**

This paper addresses possible consequences of a minimum wage in a spatial context. An empirical analysis utilizing German data shows that a significant spatial wage structure exists and that, as a consequence, the share of workers earning wages below a minimum wage will be particularly high in rural counties even if we control for educational and occupational differences. A theoretical analysis discusses the implications for the spatial structure of the economy and shows that while the wages in the countryside will be affected positively, wages will decline in the city, where employment and population rise. Workers in the city will further suffer from an increase in housing costs. This supports concerns that urban poverty might increase as a result of the introduction of a minimum wage.

# The Impact of Innovation on Employment in Small and Medium Enterprises with Different Growth Rates

By Volker Zimmermann, Frankfurt a.M.\*

JEL J23, O33, C21

Labour demand, innovation, small and medium enterprises.

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## Summary

This article examines the impact of innovation on employment growth in innovating small and medium enterprises. In contrast to existing studies, which typically use the least squares estimation technique, quantile regressions were carried out to analyse the data. This method allows one to examine the effects of innovation at any desired point on the distribution function – for example, in firms experiencing positive or negative growth – providing a more complete picture of the relationship between innovation and employment growth than the standard method of viewing deviations in the average effect. The key finding of the study is that innovation has a positive effect on employment in both growing and shrinking small and medium enterprises. In addition, innovation has a much stronger impact on employee headcounts in companies that are already experiencing strong growth than in their slower growing or shrinking counterparts. When differentiating between product and process innovations, the analysis shows that the introduction of new or improved processes has a larger impact on employment than product innovations. Thus, positive employment effects of innovations are not restricted to narrow segments of the economy. Economic policy aimed at bolstering the innovative strength of firms is thus a strong encouragement to employment on a broad basis.

# Do Older Workers Lower IT-Enabled Productivity?

## Firm-Level Evidence from Germany

By Irene Bertschek and Jenny Meyer, Mannheim\*

JEL J14, J24, O33

Labour productivity, information technology, older workers.

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### Summary

The paper provides empirical evidence for the question whether firms' IT-enabled labour productivity is affected by the age structure of the workforce. We apply a production function approach with heterogenous labour to firm-level data from German manufacturing and services industries. We find that workers older than 49 are not significantly less productive than prime age workers, whereas workers younger than 30 are significantly less productive than prime age workers. Older workers using a computer are significantly more productive than older non-computer users. The positive and significant relationship between labour productivity and IT intensity is not affected by the proportion of older workers.