

SELF-EMPLOYMENT AND THE LABOUR MARKET IN GERMANY

Introduction

According to no. 21 of the Guidelines for the employment policies of the Member States (Council decision of 12 July 2005), „support for transitions in occupational status, including .. self-employment, business creation ...” is one of the measures that “shall be taken into account in the employment policies of the Member States, which shall be reported upon in the national reform programmes (European Council 2005). High expectations are invested in supporting start-ups as a cure against unemployment. For persons with an innovative business idea and some financial means, setting up one’s own business is always a good option. For unemployed people, it may be a strategy to overcome barriers against their re-entry into the labour market, which may lie in discrimination against age or candidates with a record of long-term unemployment. It remains to be questioned, however, whether boosting business creation is also a viable macro-economic strategy.

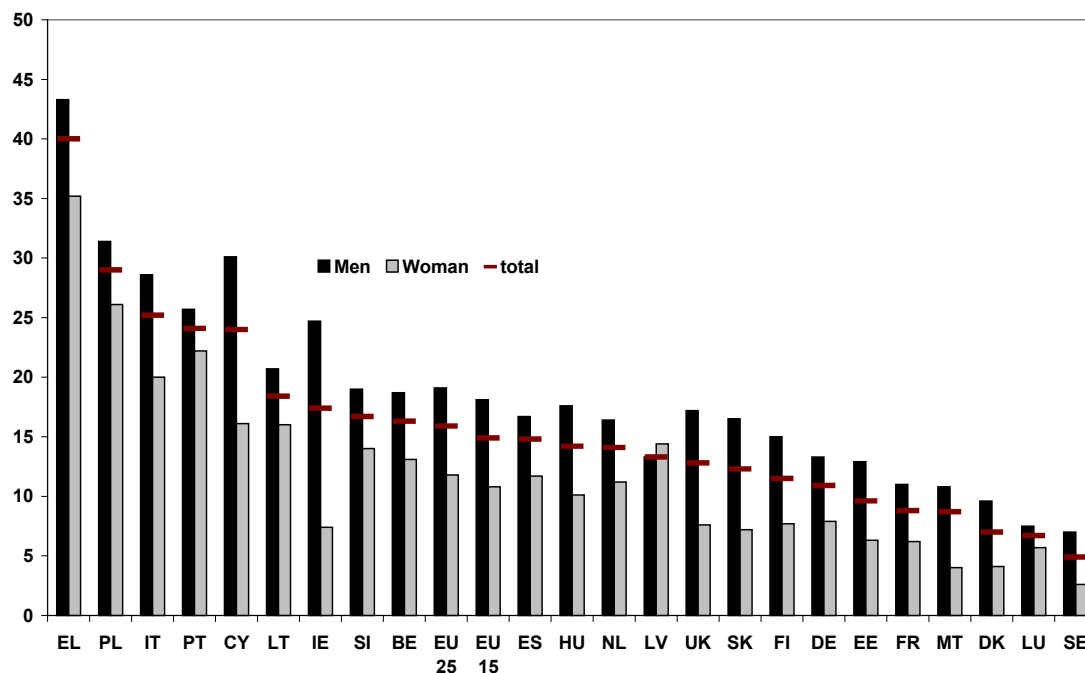
The article is organised as follows: First, the position of Germany with regard to self-employment is assessed in an international perspective, taking account of sectoral structure and prosperity of national economies (chapter 2). Then, the development of business creation and self-employment in Germany is reviewed over time (chapter 3). In chapter 4, the support of start-ups in the context of active labour market policy is critically reviewed. Chapter 5 gives some consideration to the stability of self-employment and the flows between self-employment and unemployment. Finally, chapter 6 attempts a brief conclusion.

Self-employment in an international perspective

According to popular German self-perception, Germany is a society of employees (Arbeitnehmergesellschaft), paralysed by risk-adversity and low entrepreneurial spirit. This notion seems to be confirmed by an EU-wide comparison of the importance of self-employment in total employment (cf. Figure 1): Germany ranks below EU averages of both “EU 15” and “EU 25”, and it exceeds only a few countries like France, Denmark, and Sweden. However, where low shares of self-employment are thought to be linked with poor labour market performance, the ranking of Denmark and Sweden should raise first doubts with regard to this notion right here.

One also comes to wonder why countries like Greece, Poland, Italy and Cyprus should be leading the rank order. It soon turns out that self-employment per se is not a good indicator since, in most European countries, agriculture is a sector of small family businesses so that gross shares of self-employment to some degree reflect the remaining importance of agriculture within a nation’s employment market.

Figure 1. Shares of self-employment in total employment by gender, Europe 2004



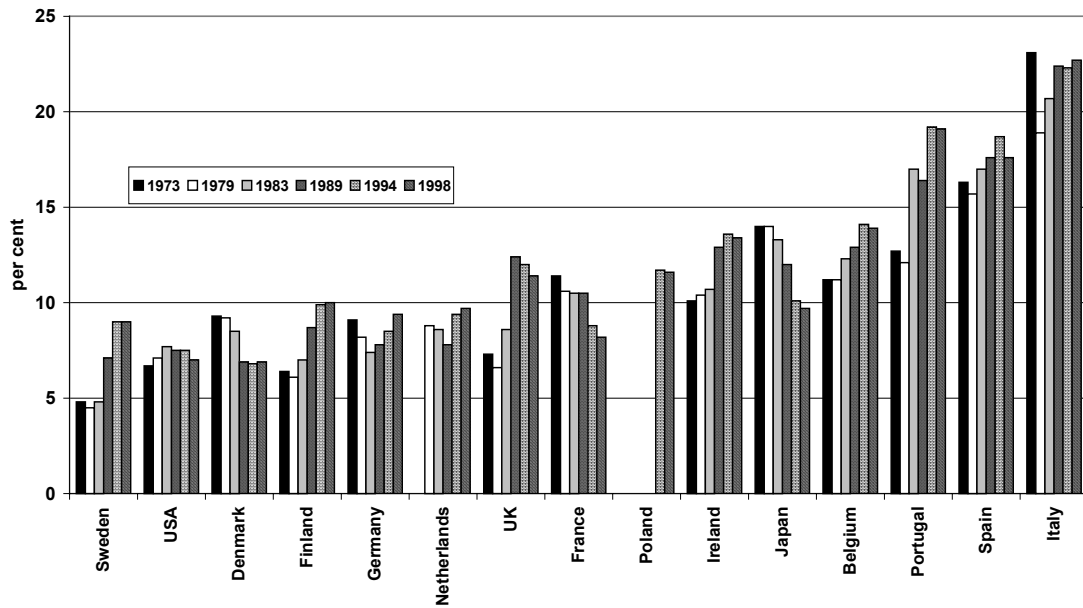
Source: Employment in Europe 2005: 50

Non-agricultural self-employment and overall labour market performance

Fortunately, the OECD provides data on shares of non-agricultural self-employment, which also include non-EU countries and which show developments over a time span of 25 years (cf. Figure 2). What comes as the first striking surprise here is that the US, considered as the classic homeland of the 'self-made man', ranks lower than Germany, and with a downward tendency since the mid-eighties. For the same period, Germany shows an upward trend. For most countries, the magnitude of change over a period as long as 25 years appears quite modest.

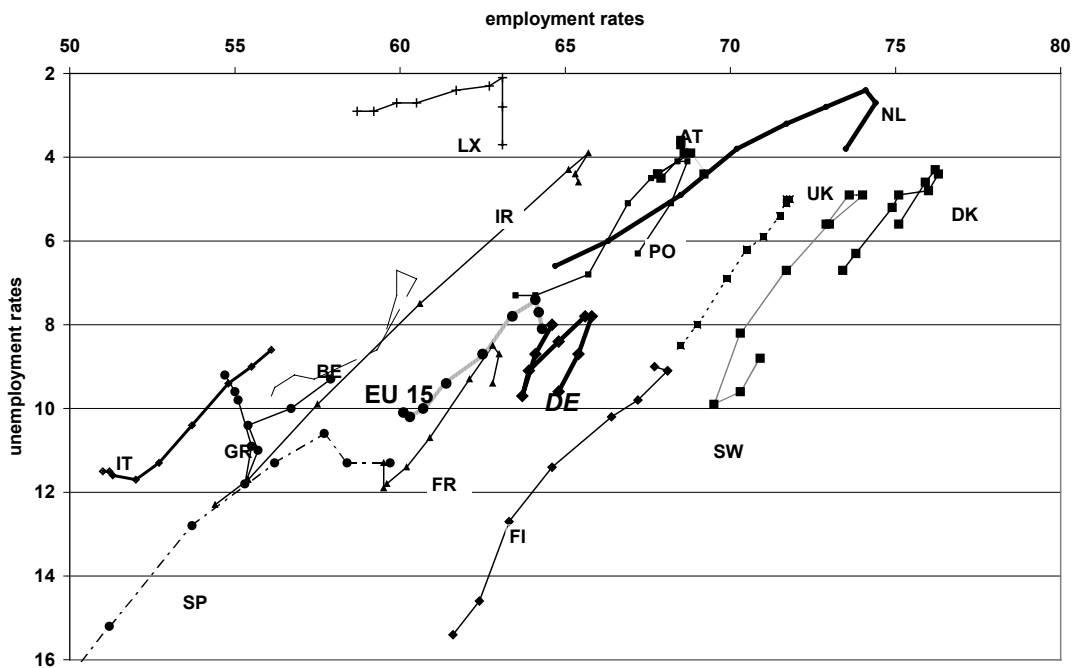
Without agriculture, Poland is no longer at the top but somewhere in the middle. Spain has moved up, and it is only Italy and Portugal that occupy high ranks in both counts (Figure 1 and Figure 2). Grouping countries by their trends in self-employment and their general labour market performance (cf. Figure 3) yields no clear picture. Denmark and the UK show a decline in self-employment while recently improving their labour market performance, while Germany and Belgium experienced a rise of self-employment in times of poor labour market performance. There seems to be no clear pattern indicating whether self-employment is favourable or unfavourable for boosting employment rates and lowering unemployment rates. It does stick out, however, that the Mediterranean Countries seem to combine high shares of self-employment even without agriculture with poor overall labour market performance.

Figure 2. Percentage of non-agricultural self-employment in selected OECD countries, 1973–1998¹, ordered by average level of years given



Source: OECD Employment Outlook 2000: 158

Figure 3. Employment and unemployment rates of EU 15, 1995–2003



Source: Employment in Europe 2004 – □ = 2004 values

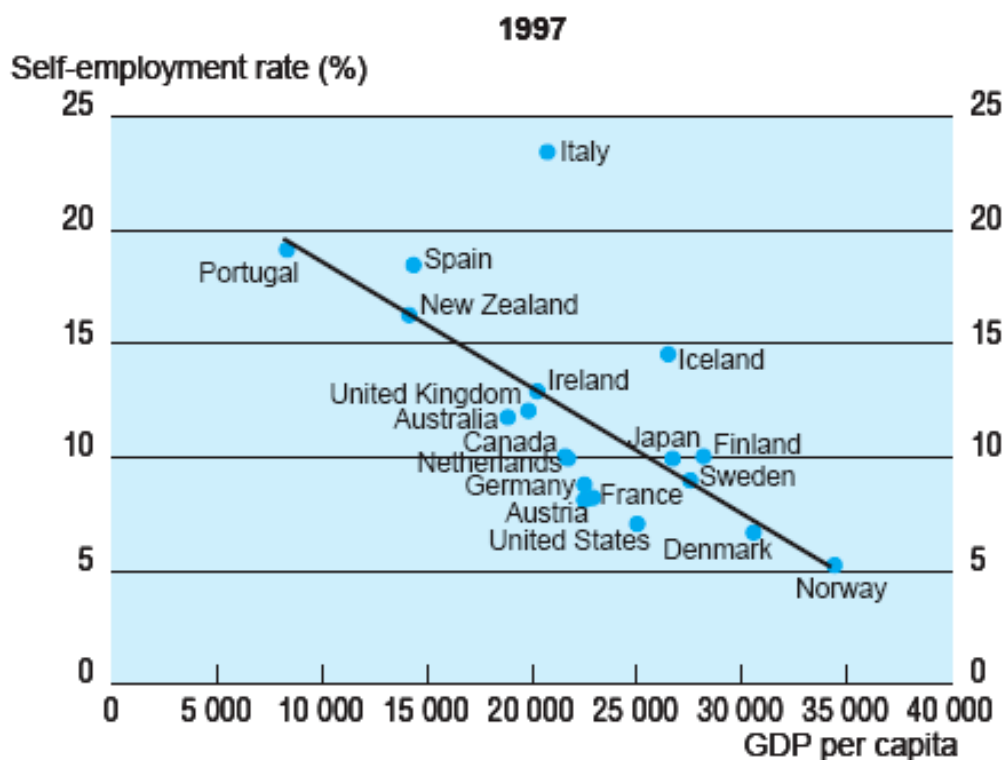
Self-employment and prosperity

Shifting our attention from labour market performance to overall economic prosperity, the relationship between the rate of self-employment and GDP per capita actually appears to

¹ Poland and Portugal: Last values are for 1997 instead of 1998.

be negative (cf. Figure 4). Self-employment may be an option for unemployed people with no other possibilities to find work, and it is also unquestionable that a dynamic economy needs the continuous creation of new businesses in order to compensate for those that have failed. However, there is no indication that boosting self-employment as such offers a way out of economic stagnation, insufficient employment growth or persistently high unemployment.

Figure 4. Non-agricultural self-employment rate and GDP per capita in some OECD countries, 1997



a) The self-employment rate is defined as the ratio of self-employment to civilian employment, excluding the agricultural sector and unpaid family workers. Countries shown are those where data are available for 1979, 1990 and 1997. GDP per capita is in US\$ and exchange rates of 1990.

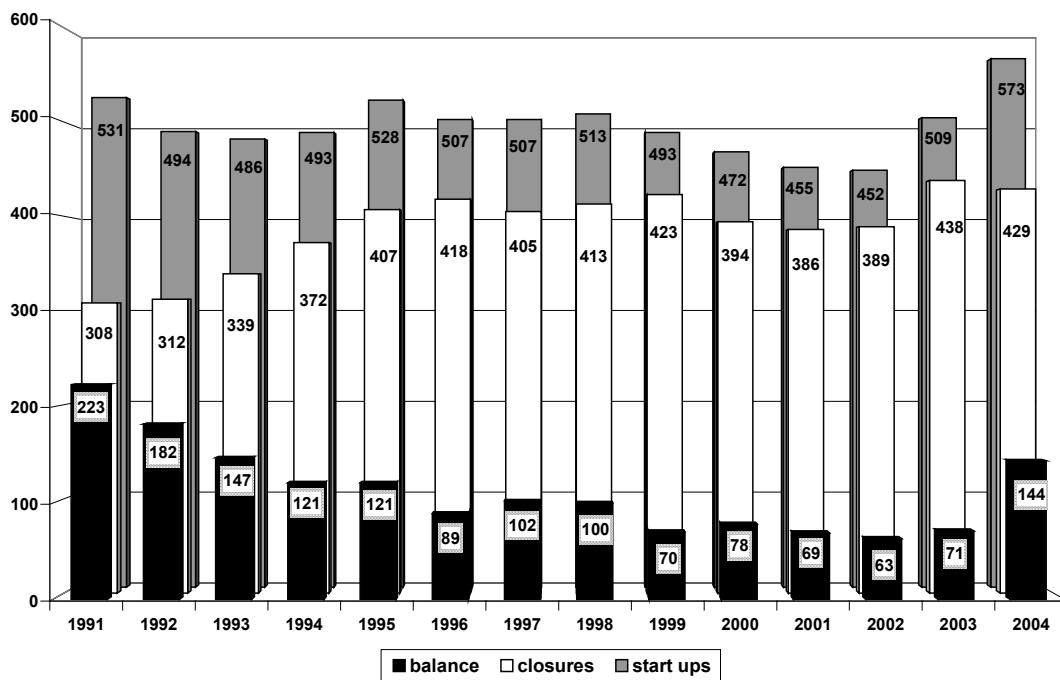
Sources: OECD database on annual labour force statistics; OECD database on national accounts.

Source: OECD Employment Outlook 2000: 173

Business creation and self-employment in Germany

Where an increase in self-employment occurs during periods of deteriorating labour market performance, as we saw for some countries in Figure 2, it appears that new businesses may be created as a result of economic distress rather than as a sign of prosperity. There is some support for this hypothesis in the German development of start-ups and liquidations, (cf. Figure 5). In 1994 and 1995, and again 2003 and 2004, both start-ups and liquidations went up. Actually, these years marked downturns of the business cycle. There is also some indication of the same mechanism working in the opposite direction: The years of 1999–2002 brought some economic recovery, and during these times of the much-hailed “New Economy” both liquidations and new start-ups went down.

Figure 5. Enterprise start-ups and liquidations in Germany, 1991–2004



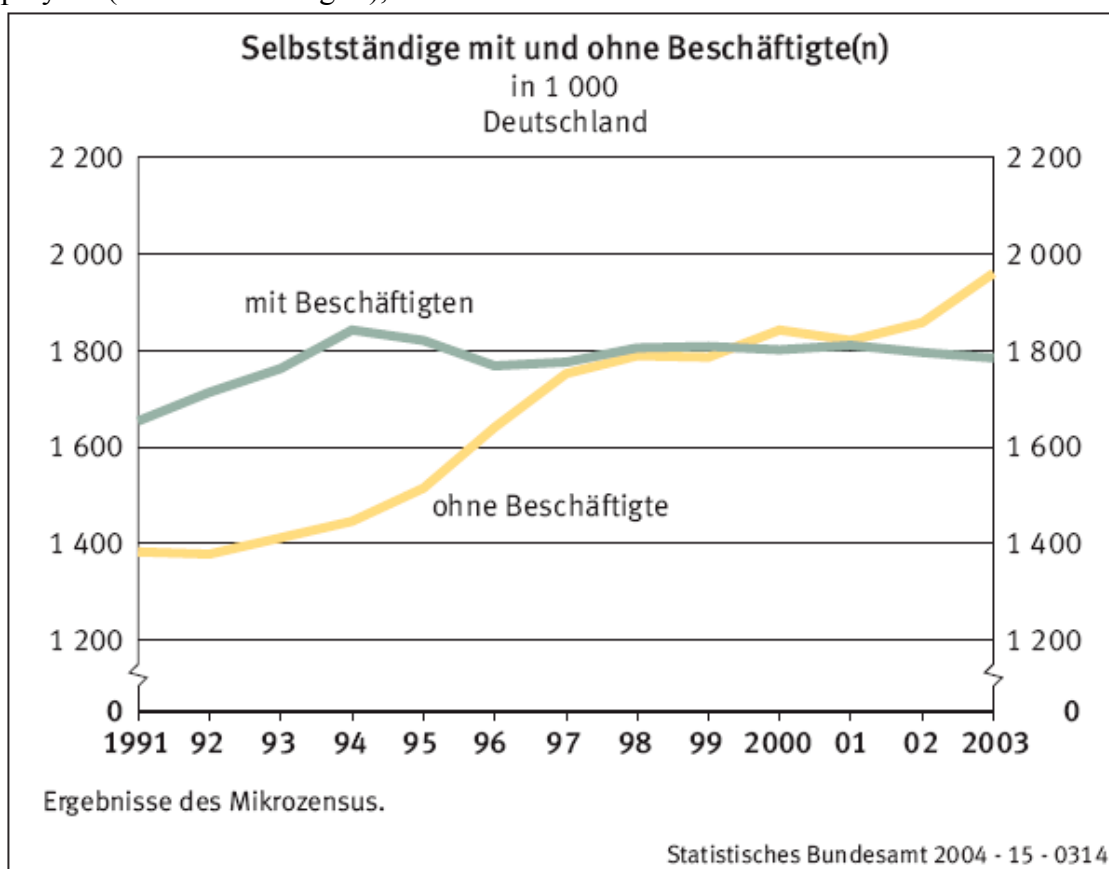
Source: Institut für Mittelstandsforschung

Finally it should be noted that for the whole period since the 1990ies, the annual net balance of the creation and destruction of businesses in Germany was positive. Nevertheless, these years were characterised by low growth rates and increasing unemployment, and the employment peak of 1992 was never reached again.

If this sounds contradictory, some of the riddle may be solved by introducing another empirical distinction that is often missing in the literature. It does obviously make a decisive difference whether a self-employed person employs only her- or himself, or whether she or he creates jobs for other people. This difference is crucial for the impact of self-employment on overall employment, and it is also relevant for the social characteristics of self-employed people: Are they entrepreneurs in the Schumpeterian sense, or are they only selling their individual labour power under a form different from waged or salaried employment?

For Germany, the result of this distinction is quite revealing (cf. Figure 6): The previous increase of self-employed persons employing other people has come to a standstill since 1994, the beginning of the German stagnation after the unification. On the other hand, the increase of the self-employed without employees was stronger in economically hard times than during the weak recovery between 1998 and 2001. It has recently become quite strong, and we will soon see one factor contributing to this development.

Figure 6. Self-employed in Germany with employees ('mit Beschäftigten') and without employees ('ohne Beschäftigte'), 1991–2003



Source: Federal Bureau of Statistics

Business start-ups as an instrument of active labour market policy

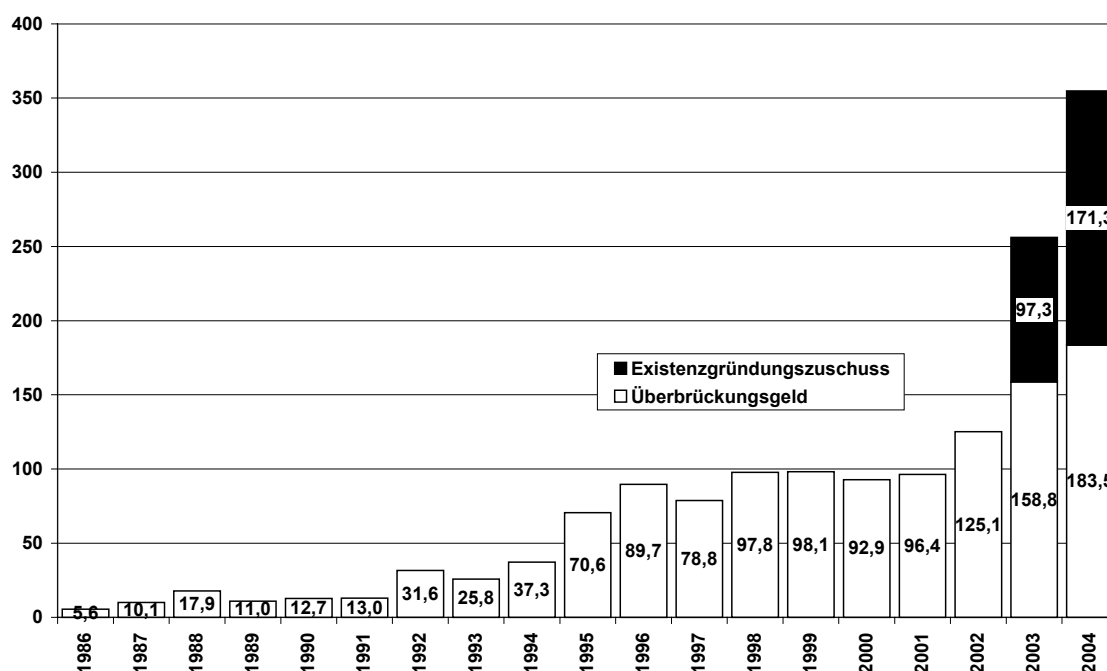
Germany was relatively late in discovering start-ups as a way out of unemployment that should be supported by labour market schemes. The reasons for this may be seen in the “Bismarckian” tradition of the German unemployment insurance system, which also finances active labour market policies. By becoming self-employed, a formerly dependent worker is ‘lost’ as a payer of unemployment insurance contributions. Supporting this move from the unemployment insurance fund was seen as adverse to the insurance system.

Consequently, even after the invention of “Überbrückungsgeld”, a support measure by which the former unemployed continues to draw unemployment benefit for six months while setting up his new business, this kind of support remained marginal in practice. It did not really come off the ground until the mid-nineties when ‘entrepreneurship’ became ideologically favoured. The far-reaching reforms of German labour market policy that were prepared by the so-called Hartz Commission in 2002 created an additional instrument, “Existenzgründungszuschuss”, which became available in 2003. It is paid as a degressive flat rate for up to three years, as long as the income earned in self-employment does not exceed 25,000 Euros per year. This is well below average annual earnings of waged and salaried employees, which characterises the new instrument as one for the support of ‘small businesses’ without employees.

Paradoxical as the creation of two competing instruments may appear, the initial warnings of critics that the new instrument would crowd out the old were not confirmed in practice. Quite contrary, both instruments grew impressively in entrant numbers (cf. Figure

7). More than 350,000 formerly unemployed people supported in setting up their own business is quite an impressive figure, and even with unemployment around five million it helps to reduce the unemployment count considerably, at least temporarily. Ongoing evaluations do not yet allow a clear assessment of the sustainability of these new businesses, but they already cast a shadow of doubt. A large proportion of these ‘entrepreneurs’ lack a clear business plan, and many appear to have entered entrepreneurship out of necessity or even opportunism (Bundesregierung 2006: 190f.). For unemployed people approaching the end of their period of eligibility for benefits, pretending to set up a business is a way to continue the reception of some benefit. Local Employment Agencies may collaborate in this sham because it cuts down on their unemployment count and contributes to achieving their ‘business targets’. But in the end, these entrepreneurs will return as unemployed jobseekers.

Figure 7. Entries into labour market policy support for setting up one’s own business, 1986–2004, in thousands

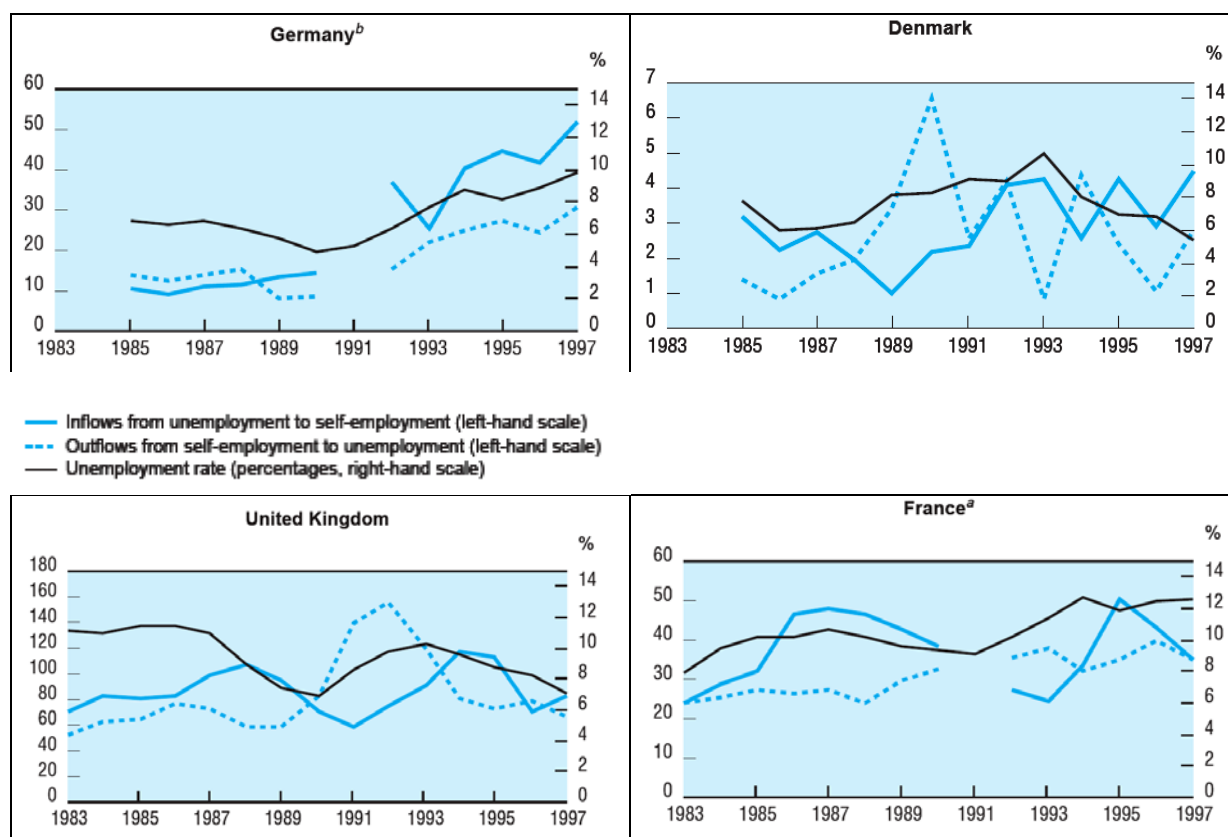


Source: Federal Employment Agency

Self-employment and unemployment

In countries otherwise so different with regard to their employment models like Germany, Denmark, the UK, and France, the relative magnitude of flows between self-employment and unemployment appears remarkably similar (cf. Figure). Germany, however, is the one country among these four with the most clearly marked upward tendency of these flows, which corresponds with the upward tendency of unemployment (the equally increasing level of self-employment being controlled for using it as the base for the percentage). In other words, as self-employment is increasingly being used as a cure against unemployment, self-employment itself becomes less stable while the stock of unemployment is not reduced. Like other methods of individual ‘activation’ of unemployed people without macro employment growth, the push for business creation only creates higher unemployment turnover.

Figure 8. Flows between unemployment and self-employment in selected countries, 1983–1997 (thousands and as percentages of self-employment)



Source: OECD Employment Outlook 2000: 165

Conclusion

Germany is not in a high position with regard to the share of self-employment in total employment. According to conventional wisdom, this is an indication of a weak spirit of entrepreneurship and one of the causes of insufficient job creation. Boosting the setting up of new businesses then seems to be the cure.

However, international comparisons do not support the idea that high shares of self-employment are correlated with higher overall employment, lower unemployment or higher prosperity. If there is any pattern at all, the national share of self-employment seems to be negatively correlated with an economy's overall performance. This stands out also in a longitudinal perspective: increases of self-employment seem to occur more likely during recessions than during upturns.

In Germany this can be clearly seen in the recent recession. Self-employment has been growing, but only among free-lancers without employees. The job creation effect of these start-ups is thus very limited. To some degree, this recent development is due to increased support for start-ups by unemployed people. The sustainability of these one-person-enterprises is still open to question. In any case, the mobility between unemployment and self-employment is growing. It appears, then, that increasing percentages of self-employed are more related to variegation of the forms of employment and to increasing volatility of people's employment careers than to entrepreneurship and employment growth. Entrepreneurship that would increase the 'wealth and work of nations' (to combine the wordings of Adam Smith and Robert Reich) is not a question of quantity but of quality.

Unfortunately, the latter appears to be in decline in Germany.

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