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Article

Short-time work schemes in the eurozone: flattening the curve

Unemployment in the eurozone has barely increased so far, mainly due to the massive take-up of short-time work schemes. This smooths out the unemployment shock, but as the recovery is unlikely to be V-shaped, unemployment is destined to rise in the recovery phase

Content

Short-time work schemes to the rescue

The mother of all labour market shocks has had an extremely varied effect on unemployment across advanced economies so far. In the US, the number of people that have filed for unemployment since the start of the lockdowns has surpassed 40 million and the unemployment rate reached 14.7% in April (before declining to 13.3% in May). In the eurozone, April unemployment was just 0.1% higher than in February, at 7.3%. While in the US this is the highest unemployment rate ever recorded, the current eurozone unemployment rate is the second lowest ever seen. There are several reasons for the large difference. One is that eurozone labour markets are, in general, more rigid due to stricter hiring and firing regulations, another is that inactivity is going up as people stop looking for work, but the most important factor is that government support through short-time work schemes is suppressing the unemployment rate massively at the moment.

Soon after the lockdowns were implemented, short-time work became a staple of fiscal emergency packages across the zone. This followed the German example of the Great Financial Crisis, when the scheme was considered to be a large success. The schemes incentivise employers to keep workers on the payroll by subsidising their pay for a pre-determined amount of time. In this crisis, the tool seems particularly fit for purpose as it helps companies bridge a limited period without revenues or with lower revenues, and supports it in the recovery phase.

Short-time work schemes across Europe: where are we?

	DE	FR	IT	ES	NL	BE	AT	PT
% of employment on ST work	16%	48%	29%	19%	24%	19%	32%	5%
% of employees on ST work	17%	55%	38%	22%	28%	23%	32%	5%
% of salary subsidized by ST work	60-87%*	70%**	80%	70%*	90%	70%	80-90%*	67%
Duration of ST work in months	12	12	12	6	7	6	6	6

Source: ING estimates on national data, ETUI Policy Brief No7/2020.
Note: latest available data differs per country; in some countries estimates of short-time workers reflect total number of applications; *% of net as opposed to gross salary; **min 85% of net salary & 100% of net salary for those receiving minimum wage

By country, the schemes are rather similar, but they differ in length and percentage of salary that is subsidised. More generous schemes pay up to 90% of wages, like in the Netherlands and Austria, while in Portugal, the payout is only two-thirds of the total salary. The length of the scheme differs substantially as well with Germany, France and Italy offering support for 12 months and other large eurozone countries just half a year. In France, there are discussions on lengthening the scheme to 24 months, while in Italy concerns about funding raise doubts about whether the 12 months of support can be achieved. Here, support through the EU's new SURE programme could help, as this is specifically designed for countries to borrow cheaply to fund short-time work programmes.

The take-up on the measures is huge. In most larger member states, the schemes cover between 15 and 30% of workers and in France, short-time work has been applied to more than half of all employees (with the caveat that this is not the actual number of employees currently being subsidised yet). It is evident that this makes a massive difference to the number of unemployed. This does not mean that all of these people would be otherwise unemployed though, there are many people on the schemes as precautionary measures so the counterfactual unemployment rate would be far lower than simply adding up the number of unemployed and the number of people on short-time work.

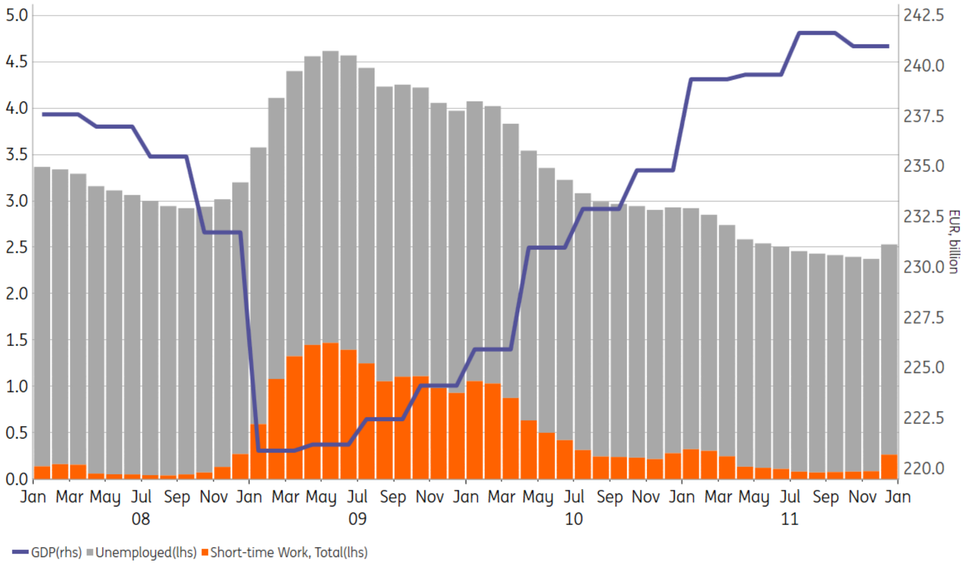
Still, the current unemployment rate is absolutely no reflection of the current state of the eurozone economy. The downsides to the measures are that they increase public debt and reduce restructuring among companies that could boost the longer run productivity of the economy. On the other hand, it is beneficial to the economy in the recovery phase. For one, consumers retain their income, which is helpful as lockdowns are gradually lifted and people can go out and consume again. Moreover, businesses can retain their workers through the period of economic fallout, meaning that the knowledge about production remains in house for when orders return. Both of those factors should speed up the recovery phase, but don't expect any miracles either.

Lacking a V-shaped recovery, short-time work cannot prevent unemployment from rising

It is hard to extrapolate the small impact of the coronavirus crisis on unemployment right now as the recovery path is highly uncertain and the impact of the schemes clouds the expected unemployment picture as well. Looking back at the success of Germany's short-time work scheme in the aftermath of the 2008 recession, we note that the increase in unemployment was relatively mild during the crisis, with short-time work absorbing a significant part of the labour market impact from the downturn. Even though unemployment increased from 7.6 to 8.3% and took close to two years to recover, that can be considered a success given the severity of the recession. This was mainly related to the surprisingly quick recovery of the German economy and the duration of the scheme, which was long enough to cover both the downturn and the recovery phase. The German experience from 2008/9 also shows that short-time work schemes are a powerful tool to bridge a short period with weak demand when the economy doesn't really suffer from any structural weakness. The fact that Asian economies were barely hit by the financial crisis and returned quickly to growth boosted German exports. Arguably, short-time work schemes would not have had the same positive impact in Spain or Greece, which went through a longer period of structural adjustment.

Short-time work absorbed a lot of the labour market impact during the Great Financial Crisis

Germany



Source: ING Research, Macrobond

Looking at the current economic crisis, we see that the downturn is even deeper than in 2008. After a 3.6% decline in 1Q, we expect the eurozone economy to contract by 14% in the second quarter, making the decline just over 17% in total. This means that even though the take-up of the schemes is massive, we can still expect an increase in the unemployment rate in the coming months. What's more, we don't expect a recovery to the pre-corona level of economic output until 2023. It took Germany just three years to fully recover from the 2008 crisis. According to our expectations, the period in which output is lower than at the start of the crisis will be more than a year longer. With most countries currently having short-time work schemes in place for either six or 12 months, there will be years of substantially lower output than before the crisis without excess employees being subsidised.

All of this indicates that while short-time work has benefits in times of a severe and short labour market shock, it will not prevent unemployment from rising substantially over the course of the downturn and recovery. While the US unemployment rate is already coming down from record high levels, unemployment in the eurozone has only just started to rise and will likely do so for some time to come, with surges likely as the schemes expire. Where the two regions end up depends largely on the speed of the recovery, but with a V-shaped move out of the question now, the eurozone's jobless rate will be substantially above the current rate of 7.3%.

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