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EUROPE PROPS UP JOBS, US PROPS UP WORKERS

Wage subsidies keep the EU's official unemployment rate lower than the US's, but could hold it back in long run.

By Tom Fairless and David Harrison
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Karren Madere and Andrea Knebel are both victims of the Covid-19 recession. Ms. Madere was laid off in June from her job at a travel-management company, where she negotiated hotel-room rates for corporate clients. Ms. Knebel was sent home in April from her job as a business consultant at an auto-parts factory.

Ms. Madere, 61 years old, has since applied for nearly 200 jobs. She spends her days looking for jobs online and follows the news, hoping Congress will agree on another economic-relief package for laid-off workers.

By contrast, Ms. Knebel's lifestyle hasn't changed all that much. She spends her time cycling around the picturesque valley where she lives, buying items for her house, and meeting friends for virtual breakfasts and lunches. She isn't looking for work. She doesn't worry about how to pay for health care, unlike Ms. Madere, who expects to go without health insurance for a few months.

The difference: Ms. Madere lives outside Baton Rouge, La.; Ms. Knebel lives close to the Black Forest, in southern Germany. Their circumstances reflect the divergent policies the US and most of Europe have used to support their labor markets.

Like tens of millions of Europeans, Ms. Knebel is on furlough from her job at engineering group Robert Bosch GmbH. Though she didn't work for nearly four months, and now works only some days, she continued throughout to receive roughly 90 percent of her normal salary, two-thirds of it paid by the German government.

"I don't feel that I lost that much financially," said Ms. Knebel, 54, who lives with her teenage daughter.

In Louisiana, Ms. Madere received 13 weeks of severance pay after being laid off and this month started getting unemployment benefits of $222 a week. She enrolled in Medicaid, the federal low-income health-insurance program, but is at risk of becoming ineligible because, with the unemployment benefits, her income may not be low enough.

"Hopefully things will change. Hopefully things will get better," she said.

Unemployment has risen far more in the US than in Europe this year. But this isn't the result of a deeper recession in the US or less-aggressive fiscal response. US gross domestic product has contracted less than Europe's, and its fiscal stimulus has been larger as a share of GDP.

Rather, it reflects different approaches to the labor market. European governments have paid companies tens of billions of dollars to keep idled workers such as Ms. Knebel on payrolls. Under the continent's so-called short-time work programs, the state reimburses workers who have lost income because they are working fewer hours. Around a quarter of all workers in Germany, France, Italy and Spain were tapping such programs in May, receiving between 60 percent and 85 percent of their lost income, according to Pimco, an investment manager.

The US has enacted some wage subsidies: Congress established the Paycheck Protection Program in March, which gives small employers loans that are forgiven if they retain their workers.

The program boosted employment at eligible firms by around 3.25 percent, or roughly 2.3 million jobs, according to research by economists at the Federal Reserve, the Massachusetts Institute of Technology and ADP, a payroll-processing company. Congress also offered tax credits of as much as $5,000 to support the wages of each employee retained by a business hurt by the pandemic.

But most US support went directly to the unemployed. Federal lawmakers added an additional $600 a week to payments, extended the duration of benefits and made gig workers eligible. Most workers received more from the enhanced benefits than they did from the job they lost, according to a University of Chicago study. At the peak in June, nearly 33 million workers—about 20 percent of the labor force—were receiving benefits, according to the Labor Department. The extra payments ended on July 31, and Congress is divided over how to extend them.

If all workers using short-time work programs were classified as unemployed, Europe's jobless rate would have been around 33 percent in May, compared with 15 percent in the US, according to Pimco.

There are advantages and risks to both approaches, economists say.

By effectively freezing their labor markets, European governments hope to keep viable businesses alive. Companies retain valuable skills and relationships, enabling them to quickly fire up as the economy recovers. Workers get paychecks and job security, which should support consumer spending.

Short-time work programs "actually prevent unemployment, which we see the US has to go through," Markus Soeder, Bavaria's minister-president, said in an interview with German public television. German Finance Minister Olaf Scholz on Aug. 16 proposed extending the program from 12 months to 24 months, which would cost the government an additional €10 billion ($11.8 billion).

Some economists worry Europe's wage subsidies could delay adaptation to longer-term changes and increase the share of unproductive "zombie" companies, which don't make enough profit over time to cover their debt-servicing costs. In Germany, the share of such companies is likely to increase to 15 percent of all businesses this year from 7 percent last year as a result of government subsidies, according to Creditreform, a credit agency. Their survival hurts healthier competitors by undercutting prices while preventing the flushing out of weak companies and bad loans that typically happens after downturns. That hurts overall productivity.

Millions of furloughed employees might ultimately be fired anyway. Around a third of British businesses expect to lay off staff by October, when their job-furlough program will be wound down, according to the Chartered Institute of Personnel and Development and

Adecco, a staffing group. German manufacturers expect to shed staff over the coming months, according to the Ifo think tank.

“We have learned from the last three recessions that shrinking sectors such as finance never recovered,” said Giuseppe Moscarini, a labor economist at Yale University. “People learn they can live without some things and they like others. These are times to restructure these sectors and automate.”

Europe’s approach partly reflects the rigidity of its labor market. Layoffs are costlier and job creation weaker than in the US German workers average around a decade in the same job, compared with 4.2 years for Americans, according to Deutsche Bank.

Germany places one of the highest tax burdens on labor in the world, to help finance the nation’s social-safety net. A single German worker with no children earning the average wage takes home roughly 50 percent of the amount their employer pays to employ them, including social-security contributions. A similar American worker takes home around 70 percent, according to data from the Organization for Economic Cooperation and Development.

Germany’s short-time work program, called Kurzarbeit, dates back to 1910, when the German Reich subsidized workers hurt by reduced production of potash. During the 2008-09 global financial crisis, short-time work kept German unemployment much lower than in other rich countries. It enabled exporters to quickly restart as demand picked up, grabbing market share.

But the program also hurt labor productivity, according to a 2017 study led by Russell Cooper at Pennsylvania State University. More productive companies struggled to expand because fewer workers were available.

Ms. Knebel and Ms. Madere both work in industries expected to shrink or change shape even after the pandemic.

The auto sector, which employs almost a million workers in Germany, is wrestling with a protracted drop in demand, in part due to a shift toward fuel-sipping hybrid and electric vehicles.

“Short-time work is currently masking large strains in employment,” Hildegard Müller, president of the German Association of the Automotive Industry, said earlier this month. “Manufacturers and suppliers are under enormous pressure…We unfortunately have to reckon with a further decline in employment.”

Bosch recently informed employees at Ms. Knebel’s factory that it wants to cut as much as 30 percent of the workforce of around 4,200. The company plans to move some production and development of auto parts to a low-cost location, probably Serbia. To avoid layoffs it is asking workers and managers to work fewer hours for less pay, or to take early retirement.

But Ms. Knebel, who has a Ph.D. in biology, says she isn’t looking for other work. Last month, she helped organize a workers’ march through the local town to protest the job cuts.

By contrast Ms. Madere is heeding the warning that travel may not come back. “I’m not going to be able to find a job in my field,” she said. She has thought about taking real-estate courses, even though she’s daunted by the idea of going back to school. She’s thinking about car-rental agencies, or office work for home health-aide companies.

"I'm 61 years old and I've been doing this since I was 25," she said. "And it's like, what do you do?"