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How to deal with this?

Germany's successful "Bounce Back Strategy" during crises

"New Zealand, be calm, be kind, stay at home", announced Prime Minister Jacinda Ardern on the 25th of March. It was the day when the Government suddenly shut down the country in order to contain a worldwide spreading virus and to save lives. The Government promised to cushion the effects this lockdown has on the economy and released a 12.1-billion-dollar support package (4.5 per cent of NZ´s GDP) only to realise very soon after that this won´t be enough to ease the economic downturn. The big question is: How to manage a global crisis on a scale never seen before in modern history? It´s a situation no-one has ever dealt with as the lockdown caused a sudden stop in terms of economic production – not just a slowdown. Senior economists are already predicting scenarios that range from higher unemployment rates to the fact that the pandemic will be far more economically damaging than even the Global Financial Crisis or the Great Depression.

Now, every country in the world has to find its own way through this new kind of crisis. Although it´s hard to compare different states and different economies it turns out that some applied better strategies than others to overcome crises in the past. In this regard, it might be helpful to take a closer look at how the strongest economy in Europe has successfully dealt with their biggest economic and financial challenges: Germany.

How Germany overcame the Global Financial Crisis 2008/09

Germany´s economic system is a "social market economy". A concept that promotes free-market capitalism and is based on a specific relationship between state and market, and between capital and labour.

While most other European countries are still dealing with the aftermath of the 2008-9 financial crisis, Germany´s economy emerged with revitalised export industries and a record-low unemployment rate. The keys to success were structural reforms and strict economic management, combining fiscal conservatism and structural reforms of welfare and the labour market. The country experienced a deep but short recession (Q2 2008 – Q1 2009). According to Christian Dustmann, a German economist and Professor of Economics at University College London, the most distinctive feature of Germany´s recession was that unemployment hardly increased. Dustmann states that this was achieved because employment reduction was distributed between workers, employers, and tax payers. The precondition to this solution was the specific governance structure and a unique collaboration between Policy Makers, Unions and Industrialists. The export-led growth was the result of adjustments in business and labour relations that revitalised German industries.

Even long before the Global Financial Crisis Germany implemented change within three specific economic key areas:

1. Decentralisation of wage setting
   - Governance structure of the German system of industrial relations is not rooted in legislation and not governed by the political process, but laid out in contracts and mutual agreements between trade unions, employer associations, and works councils
   - Institutions allowed for decentralisation of wage setting process, from an industry- or region-wide level to the level of the single firm
   - Sharp decline in share of workers covered by union agreements
   - Increase in opening clauses that strengthened the role of firm-based works councils in wage determination relative to trade unions

2. Manufacturing sector improved competitiveness
   - Inputs from domestically provided non-tradable and tradable services
   - Productivity increases outpaced wage increases. This meant a decline in unit labour costs but increase in real wages
   - Increased use of trade integration with Eastern European countries through inputs imported from abroad
   - Introduction of "Hartz Reforms" (2003) that reduced and limited the benefits of workers while unemployed, liberalized agency work, reformed "active" labour market policies, and reorganised the Federal Labour Agency

3. Great flexibility in labour market
   - Opening of central and eastern European countries: unique opportunity for German industry to move production abroad. This changed balance of power between unions and employers and strengthened work councils

During the recession, Germany also released two economic recovery plans (2008 and 2009). An important part of the stimulus programs was the introduction of short-time working. Employees received a short-time compensation of up to 67 per cent of their net salary for a maximum of two years. This was highly beneficial for the employer as the business didn´t continue to pay wages but staff could stay on and were ready to work full time again as soon as the crisis was over. The costs were covered by the Federal Employment Agency (Bundesagentur für Arbeit, BA) which is attached to the German Federal Ministry for Labour and Social Affairs. During the Global Financial Crisis, Germany invested 8 billion Euros in short-time working compensation. In May 2009, nearly 1.5 million employees took advantage of this support scheme.

Germany's emergency package during the Coronacrisis

Germany immediately kicked into "crisis mode". The Government decided on very tight rules to contain the spread of covid-19 and to adequately support its economy. The position Germany was in before the Coronacrisis was beneficial for two reasons:

- Since Chancellor Angela Merkel took office the Government followed a strict "black zero" fiscal policy which only allows the country only to take new debt in special crisis situations so it won´t end up with the burden of a colossal debt.

- Germany already had mechanisms in place that allow businesses to stay afloat during crisis times. These mechanisms were installed during the Global Financial Crisis in 2008/09.

The extensive economic stimulus packages that were applied during the Global Financial Crisis instantly kicked into gear: liquidity support, easy access to short-time working compensation for employees and additional state aid. The German reaction to the coronavirus pandemic has been straight forward and very pragmatic. They immediately broke with their strict "black zero" fiscal policy, which characterised chancellor Angela Merkel´s era, and took 156 billion Euro (about 10 per cent of Germany´s GDP) of new debt to fund additional social spending and to support liquidity for self-employed people in a coordinated effort to prevent deeper economic disruption. According to German Finance Minister Olaf Scholz, economic fiscal management in the past had brought Germany´s debt-to-GDP ratio to below 60 per cent (equivalent figure in Italy: 134.8 per cent) giving them now the financial scope to deal with this crisis. The support package to cushion the economy totals more than 750 billion euros. It also includes a 600 billion-euro Economic Stabilisation Fund (WSF) that consists of 400 billion euros in guarantees, 100 billion euros for equity stakes in companies and 100 billion euros for state-backed loans. According to the Financial Times the WSF "will not only underwrite companies' debts but also recapitalise those experiencing financial difficulties due to the coronavirus turmoil, effectively paving the way for a wave of partial state takeovers."

Germany's and New Zealand's powerful answer to fight the lockdown effects

As in the slogan "a lot helps a lot" Germany had learned its lessons in the past and knows how beneficial a generous financial boost by the state helps the economy to land on its feet again. Very similar to Germany, New Zealand was in a very good state before the Coronacrisis. In fact, there is a lot of parallels: both countries made provisions in order to be able to increase debt, and both immediately decided to lace up a comprehensive economic support package. New Zealand´s debt is about 20 per cent of NZ´s GDP - low by international standards, and not only the result of the current Government´s work. Former Finance Minister Sir Michael Cullen got debt down to virtually zero even before the Global Financial Crisis hit, forcing subsequent Finance Ministers to ramp up borrowing. By 2017 debt was once again falling. Now, New Zealand is going even further than the UK and the US with a $12.1 billion economic package that is not a "one-off package" as Finance Minister Grant Robertson stressed, saying to government would spend more if needed.

NZ´s wage subsidy scheme is also similar to the German one. However, instead of the state covered short-time working model in Germany, New Zealand businesses are negotiating altered working conditions including voluntary pay cuts with their staff to ensure that employees can be retained during the extreme downturn in economic activity.

Senior economists believe that a drop in the dollar would help those who are still able to keep exporting and that being a world leader in selling food during this time is also an advantage.

The lockdown is very much a “drive by sight” situation at the moment but businesses in Germany and New Zealand would at least like to know for how long they have to endure it, as there is no openly discussed exit strategy yet.