

German minimum wage drove workers to more productive firms

The introduction of the minimum wage for the first time in Germany in 2015 drove workers from smaller to larger and more productive businesses that pay higher wages, according to a UCL and Institute for Employment Research (IAB) Nuremberg study.

The study, published today as CReAM Discussion Paper No. 07/20, which is the most comprehensive analysis of the wider implications of Germany's minimum wage policy, also showed that wages of low-paid workers increased relative to that of high-paid workers without lowering employment rates.

By boosting wages, but not reducing employment, the minimum wage helped reduce wage inequality across individuals and regions.

“Contrary to concerns that characterised the debate in the run up of Germany's introduction of a nationwide minimum wage, we do not find that it reduced employment. On the contrary, our research suggests that the minimum wage increased overall production efficiency, by reallocating workers from less to more productive firms,” said co-author Professor Attila Lindner (UCL Centre for Research and Analysis of Migration, CReAM).

In January 2015, the German government introduced a uniform minimum across all 16 of the country's federal states, requiring firms to pay €8.50 per hour. It cut deep into the wage distribution, with 15 per cent of workers earning a wage below €8.50 six months before the minimum wage came into effect.

Using administrative records from the Federal Employment Agency's Statistics Department processed for research purposes at the Institute for Employment Research (IAB), the study investigated the wage and employment effects of the policy by comparing workers who earned less (treated group) and considerably more (control group) than the minimum wage before and after its introduction.

The researchers found that workers who earned a wage of less than €8.50 at baseline experienced an unusually high wage growth (6.7%) following the introduction of the minimum wage, bringing their wages up to the level of the minimum wage.

While hourly wage growth of workers earning slightly above the minimum wage at baseline - between €8.50 and €12.50 - was also slightly higher (2.3%) in the post-policy than in the pre-policy period.

Post-policy wage growth was very close to pre-policy wage growth for workers earning more than €12.50 at baseline. Yet, despite concerns raised about the impact a national wage would have on employment rate and business stability, the minimum wage did not harm employment prospects of low wage workers.

However, the minimum wage caused some small businesses to exit the market. Noticeably, the number and share of small businesses with less than three employees declined, with medium and large firms absorbing the workers previously employed in smaller businesses.

The analysis showed that low-wage workers (but not high-wage workers) move to businesses that offer more full-time jobs, employ a more skilled workforce, pay a higher

wage premium to the same type of worker, and are larger and more stable in response to the introduction of the minimum wage.

This trend of low-wage workers upgrading to ‘better and bigger’ businesses accounted for 25% of the wage increase brought about by the introduction of the minimum wage.

First author of the study, Professor Christian Dustmann (UCL Centre for Research and Analysis of Migration, CReAM), adds: “One needs to keep in mind however that the minimum wage was introduced when the German economy was doing well. Our findings do not necessarily generalise to other labour markets, or other time periods”.

Notes to editor

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Dustmann, Christian., Lindner, A., Schönberg, U., Umkehrer M. and vom Berge, P. ‘*Reallocation Effects of the Minimum Wage*’, is available at [https://www.cream-migration.org/publ uploads/CDP_07_20.pdf](https://www.cream-migration.org/publ/uploads/CDP_07_20.pdf)

The calculations are based on administrative records from the Federal Employment Agency’s Statistics Department processed for research purposes at the Institute for Employment Research (IAB).

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