

PRESS RELEASE

New Research Study suggests **Growing Wage Inequality in Germany**

In Germany, wage inequality has been rising since the late 1970s. Throughout the 1980s, all workers experienced a real wage growth, but wages grew substantially faster for workers at the top of the wage distribution. In contrast, in the 1990s and early 2000s, i.e. after reunification, real wages continued to rise at the top, but started to decline for low income groups. These are the findings of a recent study conducted by IZA Research Fellows Christian Dustmann and Uta Schönberg in cooperation with Johannes Ludsteck from the IAB, funded by the Anglo-German Foundation and the Deutsche Forschungsgemeinschaft. The study suggests that the rise in inequality among high wage earners is primarily due to technological change, whereas the real wage losses of low wage earners are partly due to a decline in union coverage. These findings are relevant in the light of the current debate on the minimum wage.

The recent study analyzes the changes in the West German wage structure since the late 1970s. Christian Dustmann (University College London), Johannes Ludsteck (Institute for Employment Research, IAB), and Uta Schönberg (University of Rochester) show that the common perception that Germany's wage structure remained largely stable over this period is inaccurate. In the 1980s, wages grew throughout the distribution, but substantially more so at the top end than at the low end. In contrast, between 1991 and 2001, wages of earners at the 5th percentile dropped by 12 percent, while earners at the 85th percentile experienced a positive wage growth of about 10 percent.

Hence, contrary to what is commonly believed, the US, the UK, and Germany experienced similar changes in wage inequality at the top of the wage distribution throughout the 1980s and 1990s. However, the increase in wage inequality among low income groups occurred in Germany about 10 years later than in the US and the UK.

The study argues that the increase in upper tail inequality is predominantly due to the diffusion of new technologies that became available in all major industrial nations at roughly the same time, and that favoured highly skilled workers. In contrast, the rise in lower-tail inequality is better explained by episodic events, such as the weakening of union power. These events happened in Germany a decade later than in the US or the UK. "It is not a coincidence that the gap at the lower end of the German wage distribution widened in the 1990s," explained IZA Research Fellow Christian Dustmann. "For instance, this decade saw a rapid decline of the German unions – a process that the United Kingdom and the United States had already experienced in the 1980s."

The share of workers who are covered by an industry- or firm-level agreement in Germany decreased by 16 percentage points between 1995 and 2004. According to the study, if unionization had remained constant at its 1995 level, wages in 2004 would have been 8% higher for the low-wage group (5th percentile), but only 0.5% higher for high-income earners (85th percentile). De-unionization contributed to roughly one third of the wage drop for low wage earners over the period 1995 to 2004. This suggests that the large wage losses at the lower end could have been partly avoided had unionization not declined.

The authors' findings suggest that the currently debated introduction of a legal minimum wage in Germany might indeed contribute to preventing a further increase in lower-tail inequality. However, such a policy may come at a price, in particular for the low-skilled who could experience a higher unemployment risk. Also, the decline in wages at the lower end of the wage distribution may have enhanced competitiveness of the German industry and therefore fuelled the current economic boom.

More information about the research

Professor Christian Dustmann
Department of Economics
University College London
Gower Street
London WC1E 6BT
U.K.
Phone: +44 20 7679 5832
Mobile: +44 7818 048 380
Fax: +44 20 7916 2775

More information about the Anglo-German Foundation

Annette Birkholz
Press and Publications
Anglo-German Foundation
Hackescher Markt 1
10178 Berlin
Deutschland
Phone: 030 2063 4985
Email: ab@agf.org.uk

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For more information on the initiative see:

<http://www.agf.org.uk/currentprogramme/CreatingSustainableGrowthInEurope.php>

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For more information on the program see

http://www.dfg.de/aktuelles_presse/information_fuer_die_wissenschaft/schwerpunktprogramme/archiv/info_wissenschaft_20_03.html

The full text of the study (Christian Dustmann/Johannes Ludsteck/Uta Schönberg: Revisiting the German Wage Structure. IZA Discussion Paper No. 2685.) is downloadable from the IZA website at <http://ftp.iza.org/dp2685.pdf>

