

Summary of the research project:

**“Entwicklung von Erklärungsmodellen für Arbeitsmarktpolitiken”
(Explaining labor market policies)**

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Principal investigator: PD Dr. Michael Neugart

- Unemployment insurance: the role of electoral systems and regional labor markets, *European Journal of Political Economy* 21, 815-829, 2005;

Abstract: Levels of insurance against unemployment vary considerably across countries. Replacement rates, the ratio relating income from unemployment to what people earned when they were employed, are higher in countries with proportional electoral systems than in countries with majoritarian systems. Also, replacement rates are positively correlated with per capita income and negatively correlated with the countries' unemployment rates. I develop an electoral competition model that replicates these stylized facts.

- Why German labour market reform has begun, *Economic Affairs* 28, 11-16, 2005;

Abstract: The current German government has levied a battery of labour market reforms that were previously seen as impossible to launch. I discuss why we have seen those reforms and what we should expect in the intermediate future. Will policy makers go on tuning the German model of labour market institutions, or might we see a reversal of what has been done so far?

- Pensions with early retirement and without commitment, *Applied Economics Letters*, forthcoming

Abstract: In this paper it is shown that more generous early retirement provisions as well as lower employment lead to lower steady state pension rates if governments weigh the welfare of the older persons relatively strongly. A relatively stronger weight on the welfare of the young reverses the results. The driving forces behind those findings are governments that cannot commit to pension policies and consequently take into account future governments' policies when maximizing electoral support from the currently young and old constituencies.

- The choice of insurance in the labor market, *Public Choice*, forthcoming
 Employment protection and unemployment benefits are considered the most prominent insurance devices for workers to protect themselves against the risk of unemployment. It occurs that societies either choose a high level of employment protection relative to unemployment benefits or vice versa. This paper explains where countries locate on this trade-off. It is argued that higher coverage of voters out-of-the labor force with intra household transfers yields a politico-economic equilibrium with relatively high employment protection and relatively low unemployment benefits. Cross country data and survey data on voters' preferences are presented that corroborate the outcomes of the model.
- Labor courts, nomination bias, and unemployment in Germany (with Helge Berger), revised version of CESifo Working Paper No. 1752, 2007
 Abstract: Labor courts play an important role in determining the effective level of labor market regulation in Germany, but their application of law may not be even-handed. Based on a theoretical model of the legal process and a new panel data set, we identify a nomination bias in labor court activity – that is, court activity varies systematically with the political leaning of the government that has appointed judges. In an extension, we find a significant positive relation between labor court activity and unemployment, even after controlling for the endogeneity of court activity. The results have potentially important policy implications regarding the independence of the judiciary and labor market reforms.
- Shocks and endogenous institutions - An agent-based model of labor market performance in turbulent times (with Christian Martin), mimeo
 Abstract: We develop an agent-based model of labor market regulation to study the consequences of employment protection legislations for labor market performance. Unlike most of the existing accounts of labor market regulation we endogenize the institutional setting. Workers cast their vote on labor market regulation depending on the past payoffs that accrued to them when one of two competing parties with different labor market policy platforms was in power. We find that employment protection systems per se do not harm employment in the long-run. However, we identify important interaction effects with exogenous shocks. In more turbulent times, employment protection systems affect labor market performance for some periods even after the shock has subsided.

- Labor market regulation and the legal system (with Carsten Hefeker), revised version of the CESifo Working Paper No. 2041

Abstract: When enacting labor market regulation governments face courts that interpret and implement the legal code. We show that the incentives for governments for labor market reform increase with the uncertainty that is involved in the implementation of legal codes through courts. Given that judges have more discretion in common as opposed to civil law systems more reform activity as a response to crises should be observed in the former system. This finding is backed by evidence from a panel of OECD countries.

- Asymmetric information and oversized coalitions (with Carsten Helm), mimeo

Abstract: Empirically oversized coalitions – those where a coalition government would still hold the majority of seats even after losing one of its partners – play a major role in democratic societies. While this observation is at odds with some of the standard explanations for government formation, we propose an argument where it is fully rational for a party that already holds a majority to invite an additional party to form a coalition and make a policy proposal within a referendum. Our argument builds on ideologically motivated parties being better informed about the true state of the world than voters. As in these cases the true motivation of policy proposals is hard to judge by the electorate a party may consider to form a coalition to signal the voter the true state of the world even if it already holds a majority.