

German Economic Reform – Maintaining the Status Quo or a New Beginning?

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Ladies and Gentlemen,

- I'm grateful to the Konrad Adenauer Foundation for giving me the opportunity ...to share with you some thoughts tonighton reforms in Germany, ...a subject which appears to be a suspense-packed movie.
- A movie with much drama and the eventual happy end ...I am sure ...--provided the political protagonists don't lose sight of their role – which is achieving results and not party-political profiling.
- But that is a different matter ...which I do not intend to comment.

- Well, Ladies and Gentlemen, when I came to Washington a year ago ... on my first assignment as Federal Commissioner for FDI ... I compared my country to a vast building site.
- The ongoing process of reforms in Germany, ...I remarked, ...reminded me of all the upheaval that usually goes with any demolition and reconstruction work:

- There is a lot of noise
 - There is a lot of dust
 - And there are lots of onlookers putting their oar in.
- And I concluded my observation by saying: “I am convinced... that after all the dust has settled... we will see a country... that has sharpened its international competitiveness.”

- Now, where do we stand today ...14 months later?
- The snapshot you take is crazy... and breathtaking – virtually in every respect.
- Instead of the upheaval beginning to settle...you can hear more noise see more dust... and there are more piercing voices of onlookers ... than have been before. Noises that seem to drown a truly remarkable success story in the making!
- While the German economy has made a big leap forward... to adjust itself to the challenges of globalization and social reform, ...a political debate on the “mischief of capitalism” has been triggered off ...out of the blue... in view of the forthcoming state elections in North Rhine Westphalia.
- The emotions ...that this short-sighted debate has stirred, ...give proof of the true nature of our subject: It’s political ...and has little to do with the remedial action that has been taken and which is showing first results.

- I think, Jackson Janes, ...the AICGS Executive Director, who is with us tonight, summarized the situation quite aptly:
- He wrote in one of his recent weekly columns - "Germany's Woes: It's not the economy, it's politics!"

- Medicine hardly ever is sweet, Ladies and Gentlemen.
- So, ...people in Germany are feeling the pinch of change... produced by the reconstruction of the social system and changes to the labor market.
- But as the saying goes: if you want the rainbow, you've got to put up with the rain.
- Some people, however, feel ...the rain has turned into a monsoon. Consumer spending is slack and the savings rate is pretty high – 11 percent plus. To a degree.... this is a measure of uncertainty.
- Experts have calculated that Germans have accumulated some 140 billion euros. If that money would be spent, ...we would see an enormous boost of our economy.
- What we need now is more words and deeds of confidence... of political and business leaders. The country and its people can deliver, ...as I will explain.
- The government's Agenda 2010 package shows first results. It is targeting a wide range of issues, such as the labor market, social security, tax and fiscal policies, education and innovation.

- To top it all, the recent summit of chancellor Schröder and opposition leader Angela Merkel also agreed on a program of attractive tax reductions to attract investors.
- So, in spring 2005 the barometer of reforms is tending upwards altogether. The imperative now must be to carry on with the reformsdespite any election fever in view of 2006.
- Most striking, to my mind,... is the enormous rise in Germany's competitiveness... and the greater attractiveness of the country for investors, which you can see now.
- Let me pin that observation on three items – labor, money and geography.

- **Let's begin with labor.** The cost of labor has become a critical issue in almost all industrialized countries.
- Outsourcing and off-shoring are two notions... that occupy many executive's thinking. Quite rightly so, ...because companies need to survive ...in a highly competitive environment.
- Germany has been no exception to that rule. Labor is not cheap.
- The recent expansion of the European Union by ten new member states to 25 countries ...has been used by European industry ...to shift some of their production eastwards ...where labor is extremely cheap.
- This has put pressure on management and unions in Germany... to adapt to a new environment. And,.. indeed,.. Germany has made astonishing progress here.

- Wage freezes,.. a partial return to the 40-hour week,.. lower entry wages and shop contracts... that allow more flexible working in line with market demand: ...– all this is happening... and reflects the new realities.
- That would have been unheard of... only a couple of years ago. Germany is definitely on the move!
- At a recent luncheon with executives of leading US companies in Germany... I was pleased to learn... how they are able to adjust working hours to the actual volume of work today.
- Hewlett Packard, ...for instance, ...tell their workforce at short notice ...by a brief SMS message on mobile phoneswhether they will be required to turn up for extra work or not.
- Others operate flexible working hoursup to 12 a day.
- A few weeks ago, a U.S. car component manufacturer in Germany concluded a new contract ...extending weekly working hours from 40 to even 44 hours with no extra pay.
- So, ...you will find a great readiness by local shop committees to come to tailor-made agreements.
- Co-determination at shop floor level works.
- “Stop moaning and get on with it”..... that message, ...I believe, ...is now widely understood.

- **My second point is money.** Germany's comparative advantages in the euro zone have grown remarkably.

- An article published by the British magazine “The Economist” the other weekrevealed that the euro area may have a single currency, ... but it still has many different real exchange rates.
- That is stunning news.
- When the single currency was born, ...Germany’s unit labor costs were the highest in the euro area. But since 1999 ...they have fallen by 10 percent relative to the average.
- In contrast, ...relative unit labor costs have risen by 9 percent in Italy, Spain and the Netherlands.
- Economists at ABN Amro were quoted as estimating that Germany’s labor costs are now lower than Italy’s.
- Ireland and Portugal have also lost competitiveness.
- In the past five years Germany has boasted faster growth in labor productivity ...than the euro area average.
- The same analysts conclude ...that Germany’s real trade-weighted effective exchange rate against the dollar ...has risen only 4 percent since early 2002.
- By the same token, ...France’s real exchange rate has gone up by 9 percent, and that of Italy and Ireland by 17 percent.
- The economists arguethat Germany’s modest rise in the real trade-weighted exchange rate explains the country’s success as the world’s leading exporter– a result of a remarkable improvement of the terms of trade.
- Also, ...Goldman Sachs, ...the investment bankers, ...stated in a report a few weeks ago that Germany’s competitiveness has improved dramatically and was now on par with the rest of the Union.

- So, Germany is good for many a pleasant surprise!

- **The third point is geography.** Since May last year, ...the European Union has had 25 rather than 15 member states.
- And Germany has become the geographical heartland of the European Union... now a market of 454 million consumers.
- This is an important message for all those people who seek a centrally based production platform or rely on supply logistics. Germany is an excellently placed turntable.
- No wonder, the country has become a winner of the EU expansion ...according to the DHIT, ...the confederation of German chambers of commerce.
- Wages may be lower in the new member states,... but suppliers prefer the close proximity to the major markets, ...which they find in Germany.
- You cannot be more centrally placed in Europe and linked up with the world ...than you are in Germany. That surely is an asset, ...which investors recognize.

- I think,Ladies and Gentlemen, ...these three points are worth remembering.

- They reflect important developments over the past 24 months that should not be overlooked when judging the status of reform in Germany.
- Confidence in Germany as a business location is growing... even against the background of the cheap labor markets in the new E.U. member states which I mentioned.
- The other day, Frankfurter Allgemeine carried a headline saying: "Berlin is cheaper than Bratislava".
- The story was about Germany's chemical giant BASF.
- They were looking at an ideal European location for a new service centre for their foreign operations. And they decided in favor of Berlin. 500 to 600 jobs are involved.
- BASF also considered Krakow in Poland... and Bratislava in Slovakia. But these places only finished as runner-ups.
- Management concluded that labor costs were only part of the equation. Flexibility, training and skills of the workforce... are at least equally important. On these scores Berlin won.
- The BASF case does confirmwhat the American Chamber of Commerce in Germany statedin their recent survey on Germany's position as a business location:
- Germany remains the first choice for U.S. companies as regards service and competence centers and R&D in Europe.
- 71 percent of U.S. companies operating in Germany... expect more turnover this year. 40 percent want to increase their capital expenditure... and 21 percent plan to hire more staff.

- I think this is a pretty convincing token of confidence in Germany as a business location. The economy is in quite a positive shape.

- Ladies and Gentlemen: You have asked me, ...are we maintaining status quo or do we see a new beginning ...concerning economic reform?
- My answer is positive: Yes, we do see a new beginning. We are not marking time. Nor are we beating the retreat.
- But the task is by far not completed. The need for reform is long term. That is an important point to communicate.
- All political parties know thisand they must carry on the work initiated by Chancellor Schröder in his Agenda 2010beyond the 2006 election yearwhoever will be in power then.
- Thank you!