

– Presse release –

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The German Council of Economic Experts (*Sachverständigenrat zur Begutachtung der gesamtwirtschaftlichen Entwicklung*) is today publishing its

Annual Report 2006/07

with the title

CONFLICTING INTERESTS – MISSED OPPORTUNITIES.

One year ago the new grand coalition government entered office with a resolute air and an ambitious agenda. The broad parliamentary majority which it commanded constituted an exceptionally propitious basis for launching far-reaching reforms in key economic policy fields. Yet following some highly promising initial steps, such as the raising of the retirement age and the adoption of the first stage of the reform of Germany's federal structure, the policymakers got bogged down in the mire of conflicting interests. This is exemplified by the reform of the method of funding the statutory health insurance scheme, which can only be labelled a failure. Nor is the forthcoming reform of business taxation now likely to represent any bold breakthrough, although comprehensive proposals had been elaborated for this. In February, for example, the German Council of Economic Experts itself submitted a blueprint for reforming income and business taxes by way of a dual income tax. All in all, the economic policy record after the first year of the grand coalition government can, at best, be termed patchy.

Any hope of making real advances must therefore be focused on efforts to improve the employment situation of the low skilled and the long-term unemployed. In August the German Council of Economic Experts presented an outline for an effective wage subsidy model to this end. Other measures that are overdue are the need to reform the statutory long-term care insurance scheme and to continue reforming Germany's federal structure, for which proposals have already been submitted.

Should the political decision-makers manage to unblock the impasse of their own making caused by the conflict of interests, the continuing bright macroeconomic outlook in 2007 represents a favourable foundation for re-embarking upon the path of economic policy reform and for resuming the forward march initiated by the promising steps taken at the start of the current legislative period.

This year the German economy grew surprisingly robustly at the rate of 2.4 per cent. Whereas previously the economic recovery had been driven mainly by external demand, domestic demand, too, picked up perceptibly in 2006. It was fuelled not least by private investment and, although this was overstated by exceptional factors, private consumption. One particularly pleasing feature is

that, for the first time in a long while, the economic upturn has also reached the labour market and has led to a trend-change in employment subject to full social security contributions. Although clearly restrictive impulses may be expected to emanate from fiscal policy in 2007 as a result of the increase in the standard rate of VAT and insurance tax by 3 percentage points and the further curbing of tax breaks, the underlying dynamics of economic activity are unlikely to falter in the year ahead. Rather, the conditions are in place for an ongoing – albeit somewhat more muted – upturn, as the German economy will move into the new year with a well filled order book and a remarkably buoyant momentum. As a result, gross domestic product is set to grow by 1.8 per cent in 2007.

Key economic data for Germany

	Unit	2003	2004	2005	2006 ¹⁾	2007 ¹⁾
Gross domestic product	% ²⁾	-0.2	1.2	0.9	2.4	1.8
Total domestic demand	% ²⁾	0.6	0.0	0.5	1.8	1.0
Investment in machinery & eq.	% ²⁾	-0.1	4.2	6.1	6.9	6.0
Construction investment	% ²⁾	-1.6	-3.8	-3.6	2.5	1.7
Other investment	% ²⁾	2.5	1.2	4.7	4.1	3.5
Consumption expenditure	% ²⁾	0.0	-0.3	0.2	0.9	0.3
Private households ⁴⁾	% ²⁾	-0.1	0.1	0.1	0.9	0.3
General government	% ²⁾	0.4	-1.3	0.6	0.9	0.5
Exports of goods and services	% ²⁾	2.4	9.6	6.9	10.2	6.6
Imports of goods and services	% ²⁾	5.4	6.9	6.5	9.9	5.3
Employment (domestic)	million	38.72	38.88	38.82	39.05	39.30
Registered unemployed	million	4.38	4.38	4.86	4.53	4.27
Employees ⁵⁾	million	27.01	26.56	26.24	26.33	26.62
Unemployment rate ⁶⁾	%	10.5	10.5	11.7	10.9	10.2
Consumer prices ⁷⁾	% ³⁾	1.1	1.6	2.0	1.7	2.3
General government balance ⁸⁾	%	-4.0	-3.7	-3.2	-2.2	-1.5

1) 2006: own estimate, 2007: forecast. - 2) Price-adjusted; changes against previous year. - 3) Change against previous year. - 4) Including private non-profit institutions. - 5) Employees subject to social insurance contributions. - 6) Share of registered unemployed in total civilian labour force (dependent civilian employed persons, self-employed, family workers). From 2003 to 2005, source: Federal Labour Office (Bundesanstalt für Arbeit). - 7) Consumer price index (2000 = 100). - 8) Fiscal balance of central government, state government, local government and the social security funds, as defined in the national accounts, in relation to nominal gross domestic product.