



# 2015 Annual Economic Report

## Investing in Germany's and Europe's future

### Summary

1. The German economy is in good shape. Employment is at a record level, unemployment is falling, and the development on the labour market is creating scope for appreciable wage rises. This year, the public-sector budget will again be close-to-balance, and there will be a slight structural surplus. A steady and reliable debt limitation policy is creating confidence amongst companies, employees and investors, and also provides an important platform for future investment and growth. Investment is a key to higher competitiveness, lasting prosperity, and a better quality of life for people in Germany and Europe. The Federal Government has therefore set itself the target of strengthening private-sector and public-sector investment in Germany and Europe.

2. Following a strong first quarter, economic growth tailed off appreciably in the course of 2014. The level of corporate investment fell below expectations against the backdrop of a disappointing global economic development and the uncertainties caused by increased geopolitical risks. The last few months of the year did however see a recovery driven by a strong labour market and strong consumption. The recovery is also reflected in improved business sentiment.

3. This development is likely to continue in 2015. For 2015, the Federal Government expects an annual average increase in gross domestic product of 1.5% (cf. Overview 1). Over the course of the year, i.e. from final quarter to final quarter, the German economy will grow more strongly in 2015 than last year. The dynamism of the domestic economy will mainly be driven by the sharp rises in incomes and the ongoing expansion of employment. Additional employment will chiefly be created in the services sectors. The positive development in wages and employment will boost the disposable income of private households. Economic policy measures like the minimum wage, and the increase in and broadening of pension payments, will also raise disposable incomes. In view of geopolitical tensions and the ongoing weak

growth in the eurozone, the external economic environment remains difficult. The lower oil price is likely to stimulate growth. Overall, a moderate increase in exports can be expected. This will gradually improve the investment climate in the export-oriented German economy. Due to the falling prices for crude oil, Germany's current account surplus will be higher this year than last year.

4. The pick-up in growth is likely to result in a clear improvement in corporate profits this year. Unit wage costs will mark a moderate rise. In terms of the overall economy, no inflationary tensions are expected. Low oil prices are resulting in a moderate development of the price level. There are no signs of deflationary tendencies for Germany.

5. A central assumption for the projection is that the financial sector will remain stable and there will be no negative developments in the eurozone or the world economy which will cause a significant rise in uncertainty.

6. Germany's Social Market Economy is rooted in the understanding that, if a society is to enjoy lasting economic success, it needs to be open, competition-oriented and fair, and show solidarity. The Social Market Economy therefore needs a shared understanding of the balance between individual responsibility and solidarity. The Federal Government would like to further deepen this shared understanding via dialogue, transparency and broad opportunities for all citizens to participate.

7. Like last year's budget, the 2015 federal budget will not require any net new borrowing. This boosts the ability of the state to act and enhances business and public confidence, and thereby also helps to stimulate higher private-sector investment. This means that the Federal Government's budget and fiscal planning are providing a clear signal for higher investment. Furthermore, it is significantly lowering the burden on the Länder and the municipalities, and thus boosting their scope for investment.

8. The Federal Government also aims to open up greater scope for private-sector investment, to further strengthen the innovative capacity and competitiveness of the companies – particularly in the industrial sector – and to foster public acceptance of this in a dialogue with all the stakeholders. The Federal Government is taking a comprehensive approach toward achieving this, including:

- maintaining public infrastructure and expanding it in a targeted fashion,
- boosting innovative capacities and backing German commerce, and particularly the industrial sector and small and medium-sized enterprises, in the context of the digital transformation,
- continuing the energy transition in a successful and cost-efficient manner, creating a secure policy environment for investment, and setting incentives for businesses to invest in efficiency technologies,
- investing more in education in order to ensure a supply of skilled workers, strengthening labour market integration and broadening the possibilities to participate, and
- stabilising and deepening economic and monetary union in Europe.

9. The German economy is facing the challenges of accelerated technological change and an ageing society. This means that innovation and investment in future capabilities are of crucial significance for Germany. Since the

development in investment has been restrained for quite some time, there is a need to strengthen public-sector investment and to improve the environment for private-sector investment. Here, it is necessary

- to improve the policy environment for private-sector investment by reducing existing impediments to investment. This is particularly the case for young companies; their investment is declining and is below the international average.
- to boost the funding of the maintenance and expansion of public infrastructure in a targeted fashion and to develop new concepts for funding it. Here, the aim is to include possibilities for private-sector finance and to stick to the path of fiscal consolidation. One focus here is to be on efficient transport routes and municipal infrastructure.

10. The Federal Government sees a need for substantial efforts to be made in the field of public-sector investment in the next few years. From 2014–2017, it is already providing an additional €5 billion for the maintenance and expansion of federal transport infrastructure. From 2016–2018, it will provide a substantial amount of further funding, totalling €10 billion, for public-sector investment, particularly in infrastructure and energy efficiency.

11. The Federal Government will also expand the level of funding generated by the users. The HGV tolls will be extended as of 1 July 2015 to a further approx. 1,100 km of four-lane federal roads, and as of 1 October 2015 will also apply to HGVs with a maximum permissible gross

### Overview 1: Selected key figures for macroeconomic trends in the Federal Republic of Germany<sup>1</sup>

	2013	2014	annual projection 2015
	Percentage change on preceding year		
<b>Gross domestic product (GDP), output approach</b>			
GDP (real)	0.1	1.5	1.5
Total employment	0.6	0.9	0.4
Unemployment rate in % (Federal Employment Agency definition) <sup>2</sup>	6.9	6.7	6.6
<b>GDP by expenditure (real)</b>			
Private consumption expenditure	0.8	1.1	1.6
Machinery and Equipment	-2.4	3.7	1.9
Construction	-0.1	3.4	2.2
Domestic demand	0.7	1.2	1.6
Exports	1.6	3.7	3.6
Imports	3.1	3.3	4.1
External balance of goods and services (contribution to GDP growth) <sup>3</sup>	-0.5	0.4	0.1
Total gross wages and salaries per employee	2.1	2.7	3.2

1 Up to 2014 results of the Federal Statistical Office; National Accounts Status: 15. January 2015.

2 In relation to the total labour force.

3 Absolute change (stocks/external balance) in per cent of pre-year GDP (= contribution to change in GDP).

weight of 7.5 tonnes and more. Also, there are plans to introduce an infrastructure levy in the form of a time-based electronic “vignette” for passenger cars. The introduction of this levy is not intended to impose a greater burden on a car registered in Germany than already exists.

12. In order to help Germany progress in the field of innovation, the Federal Government adopted the new High-Tech Strategy in September 2014. This strategy brings together a host of measures and flags up economic and social opportunities deriving from innovation. It identifies priority fields for the future in which forward-looking, applied research can foster the development of innovative products and services.

13. The digital transformation and the related rise in international networking is bringing about changes in almost all areas of society. Digitisation is also creating new scope for innovation and new business models in the commercial sector. In view of this, the Federal Government has adopted a comprehensive Digital Agenda 2014–2017, and it will continue to develop it and implement it on an ongoing basis together with commerce, science, unions and management, and civil society.

14. Germany needs a new “age of entrepreneurship”. The Federal Government is therefore promoting a spirit of enterprise, entrepreneurial initiative and better financing conditions in order to boost entrepreneurial dynamism and to better develop the potential for small and medium-sized enterprises to grow.

15. With its rapid technological developments, the digital age is also creating new challenges for competition policy. There is a need for effective merger control and protection against misuse of market power at national and European level on the dynamically developing online markets. Large parts of the regulatory framework for the digital economy should be anchored at European level. The Federal Government has submitted proposals for this to the European Commission.

16. A thoroughly revised set of European rules has been in place for the competitive award of public contracts and concessions since April 2014 in the form of three new EU public procurement directives. These EU directives need to be implemented in German law by April 2016. The Federal Government will take advantage of this implementation process to create modern, simple and user-friendly rules for public procurement in Germany which offer greater flexibility for the awarding of public contracts.

17. If companies are relieved of red tape, they have greater scope to add value, create jobs and generate innovation. On 11 December 2014, the Federal Government adopted key points for a further reduction in the level of bureaucracy affecting small and medium-sized enterprises. These key points contain 21 measures, e.g. on tax and accounting law, on relief for start-ups and young entrepreneurs, and on reducing obligations to provide statistics and information. In particular, the Federal Government will introduce the principle of “one in, one out” by 30 June 2015, so that in future any new regulations are balanced by a pruning of the same amount of bureaucracy.

18. The successful policy of fiscal consolidation puts important conditions in place for growth, employment, investment and innovation. The federal budget is playing a major role in the positive development of the overall public finances. A nominal balanced budget without net new borrowing was achieved in 2014 – a year ahead of schedule. The Federal Government’s sound, pro-growth fiscal policy is also reflected in its fiscal planning, which continues budget planning for the next few years without any new borrowing.

19. The overall public sector achieved a slight surplus in 2014, for the third year in succession. The overall financial surplus amounted to 0.4% of gross domestic product in 2014; there was also a structural surplus. This year, the public-sector budget will be close-to-balance. This means that Germany is continuing to comply with the deficit limits stipulated at European level. It has also been possible to keep reducing the debt ratio, from 79% in 2012 to an expected 74% in 2014.

20. As of 31 December 2019, the rules on fiscal equalisation in Germany – the Standards Act and the Financial Equalisation Act – will cease to apply. This also means that the rules on the distribution of the funding from Solidarity Pact II will expire. It will therefore be necessary to restructure federal-Länder fiscal relations in general. The Federation and the Länder will work together to design principles for agreements on questions of federal fiscal relations. The Federal Government aims to arrive at a result during this legislative term which meets the interests of the Federation and the Länder and which strengthens federalism in general.

21. The regional disparities in the economic structure, the labour market situation and demographic development make it necessary to continue to provide support to structurally weak regions after 2019. As a consequence, the Federal Government will develop a nationwide support system for the period after 2020 which embraces all

the structurally weak regions in Germany and brings various funding elements together into a coherent system. Consideration will also be given to whether and how the funding programmes which so far have been focused on eastern Germany can be built into the new system.

22. The Federal Government is helping the Länder and the municipalities by providing a total of approx. €10 billion, e.g. for childcare, schools and higher education, immigration and urban development, during this legislative term, thus boosting the scope for municipalities and Länder to invest. Furthermore, the municipalities are to benefit from an annual €5 billion towards integration aid in the context of the adoption of the Federal Participation Act. The Federation and the Länder have expanded the scope for cooperation permitted to them by the Basic Law in the field of education and science. The Federal Government is providing an additional €3 billion for research.

23. The Federal Government will also aim to keep developing and adapting tax legislation in order to bring it into line with the needs of a modern society in a globalised world. Here, the aim is particularly to arrive at an inheritance tax and a gift tax which meet the needs of small and medium-sized businesses, to modernise the land tax, and to reduce the effects of fiscal drag. Furthermore, the fight against the shifting of profits across borders by companies which operate internationally is of great significance; the German government is working together with its G20 partners on this.

24. In order to ensure that as many workers as possible can benefit from the good labour market situation, the Federal Government has launched a number of policy measures. Since 1 January 2015, there has been a general statutory gross minimum wage of €8.50 per hour worked. The minimum wage will be adjusted every two years – the first time will be in June 2016 with effect from 1 January 2017 – as proposed by a commission of the social partners.

25. The Act on Uniform Collective Bargaining is to resolve conflicts between trade unions in collective bargaining. If the parties to collective bargaining are unable to resolve conflicts between trade unions about which one is responsible, the collective agreement which is negotiated by the trade union with the most members in the facility will be used. Forms of employment like the use of temporary workers or work on the basis of contracts for work and services enable many people to participate in working life and permit companies to respond flexibly. However, the Federal Government will take effective action against

illegal contract clauses. The use of temporary workers is to be oriented towards its core function.

26. Recently, the long-term unemployed have not benefited as much as others from the good development on the labour market. For this reason, the continued battle against long-term unemployment – not least via preventive action – is a priority aspect of labour market policy for the Federal Government.

27. Affordable rents and decent accommodation are important prerequisites for appropriate participation in society. The brake on rental prices is intended to restrict inappropriate rises in rents charged when properties are re-let, particularly in large cities and university towns. The Federal Government intends to raise the level of housing benefit from 1 January 2016 in order to relieve the burden of housing costs for low-income households.

28. The Federal Government has closed gaps affecting the fairness of social security. Thanks to the continuing favourable financial development in the pension insurance system, the contribution rate was cut to 18.7% on 1 January 2015, and current calculations suggest that it will stay at this level until 2018. Not least due to the increasing demand for skilled labour, the pension system is to make it more attractive for employees in good health to remain in work for as long as possible. In order to give greater support to working patterns that fit in with other aspects of life, the statutory framework for a more flexible transition from working life to retirement is to be improved. Also, a working group is looking both into continuing flexible work up to the statutory effective pension age, and into the possibilities of attractive continuing work after that age.

29. The Federal Government has placed the financing of statutory health insurance on a viable long-term basis. The general contribution rate to statutory health insurance was cut from 15.5% to 14.6% on 1 January 2015. The previous special contribution of 0.9% to be paid solely by the members no longer applies. Instead, the statutory health funds can levy income-based additional contributions. The Act to Strengthen Long-Term Care substantially expanded the services available to those in need of long-term care and their family members from 1 January 2015. In order to make it easier to combine long-term care with working life, the Federal Government has improved the possibilities for employees to have themselves fully or partially released from work in order to provide long-term care to family members.

30. Together with the social partners, the Federal Government is developing strategies to counteract the effects of demographic change on the business sector and to maintain the performance of the German economy. The Federal Government's aim is firstly to strengthen and activate the potential pool of skilled labour in the domestic economy, and secondly to make Germany more attractive for qualified professionals from other countries.

31. The Federal Government has agreed on an alliance for training together with the business community, the trade unions, the Federal Employment Agency and the Länder. By reforming the Federal Training Assistance Act, the Federal Government is making an important contribution towards improving the situation of students at school and in higher education. Making family and working life more compatible contributes not only to equality of opportunity, but also to activating additional skills for companies. For this reason, the Federal Government will in future use "parental allowance plus" to help young parents to work part time and thus to get back into working life more quickly.

32. The Federal Government aims to improve the equality of women and men both in the private sector and in the federal public service. In the case of companies which have full codetermination and are listed on the stock exchange, supervisory boards gaining new members from 2016 must have at least 30% of their membership from each sex.

33. In past years, the Federal Government has already improved the possibilities for foreign professionals to immigrate, and has worked to foster a culture of welcome in Germany. The Federal Government has continued to develop the Qualified Professionals Initiative, an information and mobilisation campaign forming part of the Skilled Labour Concept, and has stipulated new priorities.

34. The energy transition is a project stretching across the generations and signifies nothing less than a comprehensive restructuring of Germany's energy supply up to 2050: much of the future energy system is to be based on renewable energy and to be highly efficient. If the ambitious targets are to be met, whilst Germany remains a competitive base for economic activity, the energy transition needs to be a success not only in environmental, but also in economic terms. This will happen if it becomes a driving force for investment and modernisation for an innovative economy and contributes to growth and jobs. The overarching principle for the future implementation of the energy reforms is the "energy policy triangle" of a secure, affordable and environmentally compatible energy supply.

35. The Federal Government's reform of the Renewable Energy Sources Act (EEG) has placed the future expansion of renewable energy sources on a viable basis. The other key projects for this legislative term have been brought together as a 10-point Energy Agenda, and coordinated in terms of timing and substance so that the energy transition can be rolled out in a methodical and efficient manner. In order to examine various options for the future design of the electricity market, the Green Paper entitled "An electricity market for the energy transition" was published at the end of October 2014 and made available for public discussion up to the beginning of March 2015.

36. The National Energy Efficiency Action Plan, which was adopted in December 2014, sets out the Federal Government's efficiency strategy for this legislative term. It aims to raise awareness of the economic viability of efficiency measures on a cross-sectoral basis and to put the conditions in place for full use to be made of the potential for efficiency improvements. The energy efficiency strategy for buildings, which the Federal Government is drafting this year, is intended to make a major contribution towards the achievement of a virtually climate-neutral building stock in Germany by 2050. In the 2020 Climate Action Plan, the Federal Government has adopted further measures to reduce greenhouse-gas emissions by at least 40% between 1990 and 2020 in Germany.

37. The Grid Expansion Acceleration Act and the Federal Requirements Plan Act provide the framework for a methodical and accelerated expansion of the transmission grids. The first formal procedures for federal planning of the expansion of the transmission grids have been set in motion. The distribution grids are also to be made fit for the energy transition, and the rules are to be made more investment-friendly. A package of ordinances is under preparation for the use of smart metering systems and meters.

38. The Federal Government is also working at European and international level, and particularly in the context of the G7 Presidency, towards an ambitious climate and energy policy. It is calling for the conclusion of an ambitious and binding climate agreement at the Climate Change Conference at the end of 2015.

39. The prosperity and quality of life of people in Germany and Europe depend not only on dynamic development in the gross domestic product, but also on social cohesion and sustainable development. As part of the government strategy entitled "Living well in Germany – what's important to us", the Federal Government will launch a comprehensive citizens' dialogue covering all issues.

40. A sustainable economic development in Europe is a crucial precondition for growth and employment in Germany. Sustainable, balanced economic growth which opens up opportunities for economic and social participation for all citizens can also improve and safeguard the social situation of people in the European Union. In order to improve the potential for growth in Europe on a lasting basis, the Federal Government is relying on a triad of accelerated investments, ambitious structural reforms and pro-growth fiscal consolidation. This requires national efforts by the member states, but also joint measures at European level. The strengthened Stability and Growth Pact offers an appropriate framework to place the budgets on a sustainably sound basis, to ensure that debts can be coped with in all the euro countries, and at the same time to set pro-growth priorities in such a manner that efforts to ensure fiscal discipline and to strengthen growth are mutually reinforcing.

41. At the end of last year, the European Commission presented proposals to boost investment activity. The Federal Government welcomes the European Commission's investment initiative. In addition to investment in key areas like energy and digital infrastructure, the Federal Government believes that it is particularly necessary to bring about lasting improvements in the environment for private-sector investment – which accounts for the bulk of investment activity – in all EU member states. To this end, impediments to growth and investments in the member states are to be identified, and corresponding measures taken. Further to this, the best possible use must be made of funding from the new European Fund for Strategic Investments (EFSI), the EU budget and the European Investment Bank in order to counteract critical bottlenecks affecting growth and investment.

42. If growth prospects are to be improved on a lasting basis, many member states will need to undertake more structural reforms. Following the outbreak of the financial and economic crisis, the EU reformed or introduced a number of procedures in order to improve fiscal, economic and employment-policy coordination and to largely avoid future crises. The Federal Government is continuing to call for closer and binding economic policy coordination in Europe. At the same time, the existing procedures for better fiscal, economic and employment-policy coordination and for the avoidance of future crises must be thoroughly applied and strengthened. To this end, the member states must take greater ownership of the country-specific recommendations in particular.

43. Stable and functioning financial markets offer efficient financing to companies and a risk-appropriate yield to investors. The Federal Government, the EU and the G20 countries have therefore rolled out a large number of regulatory measures since the onset of the financial crisis in order to make the financial system more stable

44. The Federal Government has also ensured, and will continue to ensure, that as far as possible the thorough banking regulation and banking supervision does not result in evasive shifts into the “shadow banking” system.

45. The continuing development of the single market for banks and the banking union are making major contributions towards improving the stability of the banking system and thus the entire monetary union. For the EU as a whole, harmonised rules have been adopted for the resolution of banks – with liability primarily being borne by the owners and creditors – and for a banking levy. The rules of the national deposit insurance systems have also been improved. Further to this, a single supervisory mechanism and a joint mechanism for the resolution of banks have been adopted for the eurozone.

46. The Federal Government continues to press for the implementation of a financial transaction tax via enhanced co-operation, with a broad assessment basis and a low tax rate.

47. Stability is also to be increased in the field of insurance companies. The new Solvency II supervisory regime, which is to be launched throughout Europe in 2016, will thoroughly modernise and further harmonise insurance supervisory law in Europe. The ongoing low-interest environment is creating major challenges for life insurance providers in particular. In order to ensure that insured parties will continue to receive the payments promised to them in future, the Federal Government has implemented a number of measures in the Life Insurance Reform Act, which entered into force on 7 August 2014, so that all the stakeholders in the insurance business can make an appropriate contribution.

48. Successful integration into the global division of labour is essential for the open German economy so that prosperity, growth and employment can develop successfully and sustainably. The Federal Government is therefore advocating a further improvement in international economic relations.

49. The G7 bears particular responsibility for reliable and sustainable conditions in the global economy. Germany assumed the G7 Presidency in June 2014; the G7 summit

will be held at Schloss Elmau on 7–8 June 2015. The Federal Government will focus particularly on those aspects which are of global urgency and are of central significance for quality of life.

50. The Federal Government supports the thorough implementation of the Bali Agreement of the World Trade Organization. It is also advocating free-trade agreements in order to improve market access for German and European companies in major – in terms of market size and market potential – third countries. The negotiations on a Transatlantic Trade and Investment Partnership (TTIP) between the EU and the USA commenced in 2013. The Federal Government is calling for their conclusion by the end of 2015. The aim is to open the markets further on both sides of the Atlantic and thus to foster growth and higher employment. The draft Comprehensive Economic and Trade Agreement between the EU and Canada (CETA) is currently being checked for legal consistency and translated. The Federal Government would like to bring the procedure to a good conclusion. However, there is still a need for improvements on certain aspects of investment protection.

51. The Federal Government is in favour of greater transparency on exports of military equipment. The Federal Government is sticking to its strict rules governing the export of military equipment. Licences are only issued following in-depth consideration of all the circumstances of each case, particularly checking whether German military equipment is being misused to violate human rights or to exacerbate crises.