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Germany

Assessment of National Reform Programme

1. Real GDP growth in Germany averaged 2% over the period in 1996-2000. It fell to half that rate by 2005, before recovering to an expected rate of 2.4% in 2006. Over the last decade, labour productivity growth has been slightly above the EU average, and has been improving in recent years. GDP per capita is foreseen at 109% of the EU average in 2006. Employment is projected to increase to a rate of 65.8% of the working age population in 2006. Employment of older workers has continued to rise, reaching a rate of 45.4 % in 2005, which is above the EU average. Unemployment is forecast to fall to 8.9 % in 2006.
2. Germany's economic performance is held back by a high level of structural unemployment and sluggish productivity growth. To sustain growth and job-creation, economic policy is confronted with the task of tackling these structural bottlenecks, while consolidating public finances to ensure long-term sustainability.

PART I: GENERAL ASSESSMENT

3. The 2005-2008 National Reform Programme (NRP) identified six key challenges: the knowledge society; market functioning and competitiveness; business environment; the sustainability of public finances (including sustainable growth and social security); ecological innovation; and reform of the labour market. In its 2006 Annual Progress Report (APR) the Commission pointed out that a stronger response was needed regarding competition in services, integration of less qualified workers, and an increase in childcare facilities.
4. Germany is making some good progress in implementing its NRP, especially in the macro- and micro-economic fields. Progress is particularly strong in improving the business environment, where various better regulation measures have been implemented. On the key challenge of employment policies, implementation has moved ahead, but further work remains to be done on tackling high structural unemployment, including for priority categories. There remain, however, concerns over access to some telecommunications markets, over bringing less qualified workers into the labour market, and in the field of childcare.
5. Germany is responding reasonably well to the commitments made at the 2006 Spring European Council. An ambitious yet realistic target for investment in R&D has been set (3% of GDP by 2010). Steps have been taken towards creating a one-stop shop for business start-ups, though the process is not yet complete, and to widen entrepreneurship education. However, the Implementation Report does not refer to progress on creating a single contact point for hiring the first employee. Germany has set an objective of ensuring no young person remains unemployed for more than three months, which would go further than the Spring European Council commitment, but this has not yet been fully achieved.

6. Responsibility for the NRP and its implementation is now dealt with at ministerial level, and the consultation process has been improved by involving a large number of stakeholders. The 2006 Implementation Report provides most of the information needed to assess implementation of Germany's reform agenda, though budgets and timelines have not always been given, and aggregate budgets for the regional level would have been useful. The reduction of the number of laws requiring co-decision by the *Bundestag* and *Bundesrat* may facilitate and accelerate the reform if complemented by the announced revision of fiscal relations between the federal and state level. According to the draft National Strategic Reference Framework for 2007-2013, Germany's Structural Funds expenditure is consistent with the renewed Growth and Jobs Strategy.

PART II: ASSESSMENT BY POLICY AREA

Macro-economic policies

7. The NRP identified sustainability of public finances (including sustainable growth and social security) as the key challenge. The measures announced in the NRP have been implemented, and helped by a strong economic recovery, a government deficit below 3% of GDP will be reached in 2006, one year ahead of the 2007 deadline set by the Council. Without further measures, however, progress towards achieving the medium-term objective of a balanced budget is likely to be slow.
8. The NRP set out to improve the quality of public finances by shifting from consumption to investment on the expenditure side and from direct to indirect taxation on the revenue side. A reduction of the corporate income tax rate has been announced. On the expenditure side, the Federal Employment Agency is making progress in using its resources more efficiently.
9. In November 2006, the government adopted a draft law by which the statutory retirement age will be raised in steps to 67 years, from 2012 onwards. Although exemptions to the higher age limit are being granted to a considerable extent, the move will enhance the long-term sustainability of public finances. Some budget items and timelines in the Implementation Report are not sufficiently clear, in particular regarding the health care system, for which the NRP foresaw a financial reform and higher efficiency in service provision through more competition. The main points for reform in the health care system, as listed in the Implementation Report and in the draft law, contain elements aiming at improving efficiency and fostering competition, but further clarifications are needed to assess how the proposed "health care pool" (*Gesundheitsfonds*) would meet these objectives. Measures to adapt the statutory long-term care insurance to demographic changes by introducing elements of a funded scheme, announced in the NRP for summer 2006, have not yet been drafted but are announced for the course of 2007. The reduction of non-wage labour costs resulting from the reduction in the contribution rate to the unemployment insurance will partly be offset by an increase of contributions to the health and pension systems, so that the impact on employment will be lower than expected. The German government has recently taken measures to reduce contributions to unemployment insurance below the levels it had announced in the NRP.

10. The Implementation Report lists several measures designed to support the catching-up process of the eastern *Länder*. Further detail would be welcomed on measures to increase the effectiveness of the initiatives already in place.
11. Germany has in general made good progress with the implementation of measures responding to its macro-economic key challenge. It is too early to assess results, especially as regards the health care system, and to assess whether they will be sufficient both to ensure long-term fiscal sustainability and to reduce non-wage labour costs.

Micro-economic policies

12. The NRP presented as key challenges; knowledge society; market functioning and competitiveness; business environment; and ecological innovation.
13. There has been good progress on R&D and innovation policies, notably the "Excellency Initiative", to bolster the position of top universities, the "Pact for Research and Innovation (2006-2010)", and the "High Tech Strategy", adopted in August 2006. Additional federal spending commitments have been made to reach the R&D investment target of 3% GDP by 2010. Reaching the target will mainly depend on the leverage effect of federal R&D spending on expenditure by businesses and the *Länder*. The Implementation Report also mentions new measures at regional level to promote innovation through closer cooperation between science, research and businesses, particularly in the area of ICT. An information society initiative iD2010 was decided upon in November 2006.
14. Considerable progress has been made in improving the business environment through better regulation. Legislation due to be adopted in 2006 will reduce administrative costs, particularly for SMEs. A standard cost model is being adopted, on the basis of which further targets for reduction of administrative costs will be set by mid-2007. Following a screening of federal legislation, an independent body for impact assessments (*Normenkontrollrat*) has become operational. Reporting requirements for SMEs are being reduced at federal level. A web-based information tool (*Startothek*) has been created as a first step towards establishing a one-stop-shop for company start-ups. The issues of "hiring the first employee" and reducing start-up times have been partly addressed. Some progress is visible regarding entrepreneurship education. The simplification of regulations on infrastructure planning is well under way, supporting the investment climate.
15. The federal regulatory office for network services has been given additional powers to improve incentives, review price setting and to address remaining problems such as the high market concentration, lack of transparency and vertical foreclosure in the energy markets. Since January 2006, the office has also been in charge of rail transport and ensuring non-discriminatory access to the rail infrastructure. Concerns remain regarding the intention not to introduce regulation which would open certain new markets, for example modern broadband networks, to competition, as well as the delay in effectively regulating wholesale bitstream access in other words the ability of competitors to offer their clients broadband products based on wholesale access to certain digital services provided by the incumbent). Regarding public procurement, the recent transposition into national law of the relevant EU Directives is a first step towards simplifying and modernising the German public procurement framework. In

the field of professional services, Germany has taken steps to relax the rules governing lawyers and architects, but significant restrictions remain in these and other heavily regulated professional services, as well as in the crafts sector.

16. The response to the key challenge "ecological innovation" was a strong point of the NRP, and good progress towards the well-defined objectives has been made. It is expected that the targets for greenhouse gas emissions will be reached, provided that remaining measures are implemented. However the market-oriented approaches to improving energy efficiency and diversity, mentioned in the NRP, are not described in the Implementation Report.
17. Overall, Germany has made good progress on the micro-economic key challenges, especially in the areas of knowledge society, business environment, and ecological innovation. However, the weak points referred to in the 2006 APR regarding the functioning of markets and competition have not been fully followed up.

Employment policies

18. The NRP focused on the education system and lifelong learning in the context of promoting the knowledge society. It called for: raising adaptability and employability; an increase in labour market participation; adapting the labour market to the demographic challenge through structural reforms of labour market institutions; and for improving the reconciliation of family life and work. The 2006 Implementation Report sticks to the challenges identified in the NRP.
19. Given the high level of unemployment among the low-skilled, the report announces more qualification measures for this target group and a review of the tax and benefit system. In the NRP an extension of the probationary period for new employees was proposed but this proposal was coupled with a proposal to abolish simple unconditional fixed-term contracts and subsequently both were dropped.
20. Major difficulties remain with respect to the effectiveness of the employment services in dealing with unemployed people who are hard to place, especially the long-term unemployed. The NRP objective that no young person should be unemployed for more than three months has not yet been met, and demand for apprenticeships by far outstrips vacancies for such positions. The design of measures aiming at a higher employment rate of older workers has been improved, but there should be more focus on prevention. The announced agreement with social partners to improve the qualifications of older workers has turned into an agreement to raise awareness and exchange good experiences about older workers' employment. Regarding participation of women in the labour market, and the reconciliation of work and family life, some progress has been made in the provision of childcare infrastructure, but the number of childcare places is still low. Important challenges such as the high gender pay gap are not addressed directly. Increased attention has been given to the integration of immigrants, including an announced "national integration plan" to improve the school education and vocational qualifications of young migrants.
21. The Implementation Report refers to various initiatives aiming at improving the educational system. The approach seems appropriate and should be closely monitored in close cooperation with the Länder, given their responsibility in the field

of education. A new expert forum is announced to develop recommendations for improving life-long learning, but no explicit reference is made to the plans of the NRP to develop vocational qualification for adults into a fourth pillar of the German educational system and to create a legal framework for improving the financing of adult vocational training.

PART III: CONCLUSIONS

22. In the light of the analysis presented in the Commission's 2007 Annual Progress Report – Part II - and based on the Integrated Guidelines for Jobs and Growth, the following conclusions are appropriate:
23. Germany is making good progress overall in the implementation of its National Reform Programme, and especially on the macro- and micro-economic key challenges and priority actions. It is moving forward more slowly in the field of employment. Germany is also responding reasonably well to the commitments made at the 2006 Spring European Council.
24. Strengths of the reforms in 2006 include the progress in the area of consolidation and sustainability of public finances, as well as the implementation of various better regulation measures, such as the web-based information tool "*Startothek*" for business start-ups and the establishment of an independent council at federal level for impact assessment (*Normenkontrollrat*). Other strengths are evident in the field of knowledge society (R&D and innovation), as well as in the higher visibility given to measures for the integration of older unemployed people.
25. The policy areas in the German National Reform Programme where weaknesses need to be tackled with the highest priority are: improving the long-term sustainability of public finances; improving competition, notably in professional services and new broadband markets; and tackling structural unemployment. Against this background, it is recommended that Germany:
 - improve long-term sustainability of public finances by continuing fiscal consolidation, leading to debt reduction, and by implementing the health care reform with a view to keeping expenditure growth in check and strengthening efficiency in the health sector;
 - improve competition in product and services markets, notably by continuing to relax restrictive rules governing many liberal professions and effectively regulating wholesale bitstream access;
 - tackle structural unemployment including by integrating the low-skilled into the labour market through better access to qualifications, pursuing the proposed tax-benefit reform and by providing more effective employment services for the long-term and young unemployed.
26. In addition, it will be important for Germany over the period of the National Reform Programme to focus on: ensuring that health care reform makes the health system more efficient; improving public procurement procedures; removing barriers to competition in the rail sector and in gas and electricity networks, where unbundling has been ineffective; speeding up business start-ups and facilitating hiring the first

employee; building on existing measures to improve lifelong learning, including by developing adults' vocational training into a fourth pillar of the educational system; increasing the provision of childcare facilities.

PART IV: STATISTICAL GRAPHS AND DATA

GERMANY

	DE							EU25				
	2000	2001	2002	2003	2004	2005	2010 National target	2000	2004	2005	2010 EU target	
GDP per capita in PPS	111.9	110.0	108.5	108.1	108.0	109.3	3.0	100.0	100.0	100.0	70.0	
Labour productivity per person employed	101.2	100.1	99.6	100.2	99.7	101.4		100.0	100.0	100.0		
Employment rate												
Total	65.6	65.8	65.4	65.0	65.0	65.4b		62.4	63.3	63.8		
Women	58.1	58.7	58.9	58.9	59.2	59.6b		53.6	55.7	56.3		
Men	72.9	72.8	71.8	70.9	70.8	71.2b		71.2	70.9	71.3		
Employment rate of older workers												
Total	37.6	37.9	38.9	39.9	41.8	45.4b		36.6	41.0	42.5		
Women	29.0	29.4	30.6	31.6	33.0	37.5b		26.9	31.7	33.7		
Men	46.4	46.5	47.3	48.2	50.7	53.5b		46.9	50.7	51.8		
Gross domestic expenditure on R&D	2.45	2.46	2.49	2.52	2.50	2.51e		1.86e	1.86e	:		3.0
Youth education attainment level												
Total	74.7	73.6	73.3	72.5	72.8	71.5b		76.6	77.1	77.5		
Women	74.8	73.6	73.8	73.4	74.2	72.5b	79.5	80.1	80.3			
Men	74.6	73.6	72.6	71.6	71.5	70.4b	73.7	74.2	74.7			
Comparative price levels	105.6	107.1	107.5	108.7	106.6p	104.1p	100.0	100.0p	100.0p			
Business investment	19.7	18.3	16.7	16.2	16.0	15.9	18.3	17.1	17.4			
At-risk-of-poverty rate after social transfers												
Total	10.0	11.0	15.0b	15.0	16.0	:	16.0e	16.0e	:			
Women	11.0	:	18.0b	17.0	18.0	:	17.0e	17.0e	:			
Men	10.0	:	13.0b	13.0	13.0	:	15.0e	15.0e	:			
Dispersion of regional employment rates												
Total	5.7	6.1	5.9	6.0	6.2	5.6	13.4	12.2	11.9			
Women	6.5	6.5	5.9	5.7	5.9	4.8	20.5	17.3	16.9			
Men	6.2	6.8	7.0	7.1	7.6	7.2	9.9	10.2	9.7			
Long-term unemployment rate												
Total	3.7	3.7	3.9	4.5	5.4	5.0b	3.9	4.1	3.9			
Women	4.6	4.6	4.8	5.2	6.1	5.4b	4.8	4.7	4.5			
Men	3.0	3.0	3.3	3.9	4.8	4.7b	3.3	3.6	3.5			
Total greenhouse gas emissions	83.2	84.1	82.8	83.3	82.5	:	90.7	92.7	:			
Energy intensity of the economy	159.7	162.5	158.7	161.0	158.8	:	208.8	204.9	:			
Volume of freight transport relative to GDP	103.3	103.3	102.3	103.2	108.0	110.6	100.1e	104.6be	104.7e			

PERFORMANCE COMPARED TO EU-25

