Launch of the Economic Survey of Germany

Remarks by Angel Gurría,
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OECD

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Minister, Ladies and Gentlemen,

It is a great pleasure to present our 2014 Economic Survey of Germany. I would like to thank the Federal Press Conference for hosting this launch again. We are particularly honoured that Vice Chancellor Sigmar Gabriel is presenting and discussing the key policy messages.

In the face of recent crisis, the German economy has proved remarkably resilient

Germany has weathered the economic crisis remarkably well. Its GDP per capita is now 3½ percent above its pre-crisis level. And while many other European countries are fighting against double-digit unemployment rates, the German rate has come down from 8% in 2008 to 5.1% in the first quarter this year.

This performance is very impressive. Ambitious reforms, in particular in the labour market, have clearly helped to make this happen.

Backed by its robust labour market and a strong, innovative manufacturing sector, the country is now set for a broad-based recovery after having passed the pre-crisis peak already in 2011. We project growth to gradually rise to 1.9% this year and 2.3% next year.

Still, a number of important challenges remain. First, while income inequality and relative poverty in Germany are lower than in most OECD countries, the share of low-paying jobs is high and rising. Our figures show that around 22% of all workers earned less than two thirds of the median income.

A second challenge is the potential growth rate, which is estimated to fall to around 1 percent per year over the next 20 years due to demographic changes. The third challenge is to translate the success of the dynamic manufacturing export sector into more dynamic domestic demand and to reap the potential of the services sector as a driver of growth for the German economy.

And the fourth challenge relates to the banking sector. While German banks have navigated the euro area crisis fairly well, vulnerabilities remain. Risks arise in particular from the euro area debt crisis, the low interest-rate environment and large derivative exposures.

Last but not least, Germany is not an island. It is intensively connected not only to Europe but also on a global scale. Reforms to bring Europe' growth path back on track and to boost competiveness must continue also in other European countries which are Germany's main trading partners.

Let me now share with you the reforms which the OECD's 2014 Economic Survey of Germany proposes to tackle these challenges in order to make growth more inclusive, more sustainable and less resilient to adverse financial shocks.

Making economic growth more inclusive

One of our key messages is that Germany should promote a more inclusive model of growth, based on good wages, a fair tax system, equal opportunities in education and investment in people's skills.

Germany follows the philosophy of one of its greatest entrepreneurs and innovators, Robert Bosch. He said: “I don't pay good wages because I have a lot of money. I have a lot of money because I pay good wages.” Now it is time to apply this maxim also to those closer to the bottom of the labour market.

A minimum wage can raise revenues at the bottom of the pay distribution. We thus explicitly welcome the government’s plan to phase in a general minimum wage by the end of 2016. In German we say: “Die Pläne der Bundesregierung zur Einführung eines allgemeinen Mindestlohns sind zu begrüßen.” To avoid negative employment effects it is crucial that the minimum wage is not set too high initially. International experience shows that this can best be achieved if the minimum wage is set by an independent expert commission.

Moreover, cautious use should be made of legal extensions of collective agreements to set higher sectoral minimum wages. Such extensions may not sufficiently take into account the interests of outsiders, notably the unemployed and new firms entering a market.

We also recommend that the tax system should be made more supportive to inclusive growth by broadening the tax base, by updating taxable property valuations and by phasing out tax expenditures for activities that damage the environment. Part of the fiscal room gained in this way should be used to reduce the high tax wedge on labour, in particular for low-productivity workers as well as to raise spending to increase the wage mobility of low income earners.

Inclusive growth also means investing in people’s knowledge and skills. Breaking the link between students’ socio-economic background and their education performance is key to making economic growth more inclusive.

In Germany this link is stronger than in many other OECD countries, thus putting children from poor socio-economic backgrounds at a disadvantage.

Early childhood education should be improved and more resources should be channelled to schools with a comparatively high share of pupils from a poor socio-economic background. Moreover, all youth should be able to benefit from Germany’s enormously successful dual vocational education system.

Germany should also rethink the way it covers the self-employed in social security. Not all self-employed are covered by the public pension system and not all have access to publicly-provided health insurance. This can exacerbate precarious employment and poverty risks.

Making growth more sustainable

A key element of any strategy to boost potential growth should be to improve the competitiveness of the services sector and release its full growth potential. As in all high income countries, services contributed most to economy-wide value-added. However at 69% the services share in Germany did not increase over the past fifteen years and was the lowest among the 10 largest countries in the Euro area, given the large share of manufacturing activities. Our work on Global Value Chains shows that services and manufacturing are more and more interlinked and the services sector has an immense potential to contribute to economic growth – which is a debate you just started in Germany under the heading “Industry 4.0”.

According to our recently published Services Trade Restrictiveness Index, Germany exported services worth USD 270.5 billion and imported services worth USD 295.9 billion in 2012. Services account for 16% of Germany's gross exports, but almost 50% of value-added exports, indicating that Germany's exports of goods rely intensively on services inputs. Cost effective state of the art services are therefore of utmost importance for the competitiveness of the German industrial sector.

Against this background, regulation needs to be reassessed to remove unintended barriers to competition. For example, in telecommunications, broadening the rights to issue SIM cards beyond mobile spectrum holders for machine to machine applications could unleash innovation throughout the economy. Similarly, abandoning price regulation for some professional services, such as notary services, could significantly reduce the costs of setting up new businesses.

Reform is also needed to promote green growth and make the energy sector more sustainable. Support for renewable energy remains necessary to reach CO_2 emission targets, but the current scheme has considerably pushed up electricity prices. The new government's swift action, spearheaded by you, Minister Gabriel, to limit the costs of the scheme is welcome. While the burden of the costs of renewables' support could be spread more equally across users, this is only part of the more complex challenge to define and further develop Germany's energy mix in a sustainable but also cost-efficient way.

Finally, much scope remains to remove barriers to full-time employment of women. Even though the labor participation level may be on the high side compared with other advanced economies, women in Germany are overrepresented in part-time, low-paid jobs, and there are clear barriers for their career advancement.

Decisive action in this area would go a long way in offsetting the impact of ageing on the sustainability of labour supply. Most importantly, the government needs to further improve the availability of full-day childcare, and to reduce tax disincentives to the work of second-earners as well as reconsider incentives for women to stay home. Moreover, a cultural shift is necessary to help women and men take charge of the family and the elderly, and to have a fairer distribution of non-paid work.

Making growth more resilient to adverse financial shocks

The German authorities have taken significant steps to reform bank regulation. The new rules that aim at separating risky trading activities from deposit-taking are a welcome step to increase financial sector resilience. Banks' derivatives business, in particular, generates large risks for the financial system as a whole.

The separation requirements need to be strong enough to help ensure that the banks themselves are fully aware of the costs resulting from these risks. A leverage ratio requirement on large banks would also help to complement other capital-adequacy indicators.

Germany also needs to address remaining risks emanating from the Landesbanken through micro- and macroprudential regulation. While the local savings banks have proven to be efficient providers of financial services during the crisis, including to SMEs, several Landesbanken had to be rescued by the government. Progress in creating a banking union in the Euro Area, including a common fiscal backstop, would also have economic benefits for Germany.

Ladies and Gentlemen,

Germany is doing well, but it should increase its efforts to have “all on board”, with a more inclusive and dynamic growth path. Reform should never stop. It has to be a continuum, a “state of mind” as we say at the OECD, in order to lay the foundations for a strong, sustainable and inclusive Germany. Count on the OECD to support you in this endeavour!