Germany's economy is in a vicious downward spiral

by Lothar Komp

By continuing to pursue a policy of harsh austerity, dictated by the European Union under the Maastricht Treaty, the German government is repeating the disastrous economic policies of the 1930s. With every 1 billion deutschemarks cut from the federal budget, unemployment is rising, and the tax revenue base is being further strangled. This creates a new gap in the budget, giving rise to yet another counterproductive austerity measure by the Finance Ministry. This is being done at a time when, because of global free trade policies and a disintegrating financial system, per-capita investment in new machinery, plant, and equipment is shrinking worldwide, with only a few exceptions in eastern Asia. As a consequence, recent years have seen the most severe crisis in global machine production in postwar history. The German economy, being an exporter of high-quality capital goods, is among the principal victims of this global contraction.

In an op-ed in the German economic daily *Handelsblatt* on Nov. 13, former Labor Minister Herbert Ehrenberg (1976-82) attacked the self-destructive economic policy of the Bonn government. "Is there no one in Bonn who realizes, that repeating the same errors doesn't make them work?" he asked. By cutting budgets, the state is only creating new budget shortfalls. As a result, the estimated federal tax revenue for 1996 has fallen from DM 387.6 billion (roughly $242 billion) in October 1994, to DM 361.3 billion in October 1995, and now to DM 343 billion. In the past four years, said Ehrenberg, Germany has lost 1.2 million taxpayers or contributors to the social security systems. There are now 1.3 million more recipients of public expenditures, that is, 630,000 more people unemployed and 700,000 people entering early retirement. No austerity budget in the world could compensate for that, Ehrenberg said, describing the government's policy as a "vicious cycle of a self-amplifying downward spiral."

After several rounds of budget cuts, the German government is now farther away than ever from meeting the Maastricht criteria for joining the planned European Monetary Union. (To qualify to join the new currency group, a state must have cut its public deficit, including national, local, and public pension funds, to no more than 3% of Gross Domestic Product annually. Second, it must reduce the total public debt to no more than 60% of GDP. Other requirements govern interest rates and inflation.) On Nov. 14, the German Institute for Economic Research (DIW) stated that for most of the European Union countries, the Maastricht requirements on public budget deficits and public debts pose an "insurmountable obstacle." Even in Austria and Germany, prospects for meeting the targets are "extremely unlikely."

Rising bankruptcies

No other sector of the federal budget has been more slashed in recent years than transport infrastructure: From DM 55 billion in 1995, it was cut to DM 50 billion in 1996, and to DM 45 billion in 1997. No other public expenditure is rising faster than interest payments.

The stupidity of the austerity policy is illustrated by looking at the immediate public costs of unemployment. According to the state-run Institute for Labor Market Research, these costs amounted to DM 142.5 billion during 1995, out of which DM 77.6 billion was additional public expenditures and DM 64.9 billion was missing tax revenues and social security contributions. These estimates are very conservative, because they include neither the bigger share of social aid expenditures, nor the costs of state-financed education and training programs to foster job creation. In 1996, unemployment is once again 10% higher than the year before, and is now approaching an official level of 4 million. As a fair guess, the public costs of unemployment in Germany can be estimated at about DM 200 billion a year.

What about the private sector? The latest figures on corporate bankruptcies, released in early November by the Hermes credit insurance agency and the Federal Statistical Office, show that the disintegration of the German *Mittelstand* (small and medium-sized firms) is speeding up. Expectations of six months ago have been corrected—for the worse. The latest Hermes figures forecast 26,500 corporate bankruptcies in 1996, that is, 18.5% more than the year before, and about 30,000 corporate bankruptcies in 1997. Since 1991, the rate of bankruptcies in Germany has tripled. The total economic cost of the 1991-96 corporate bankruptcies will amount to DM 170 billion, and in the next year, another DM 50 billion will be added to that.

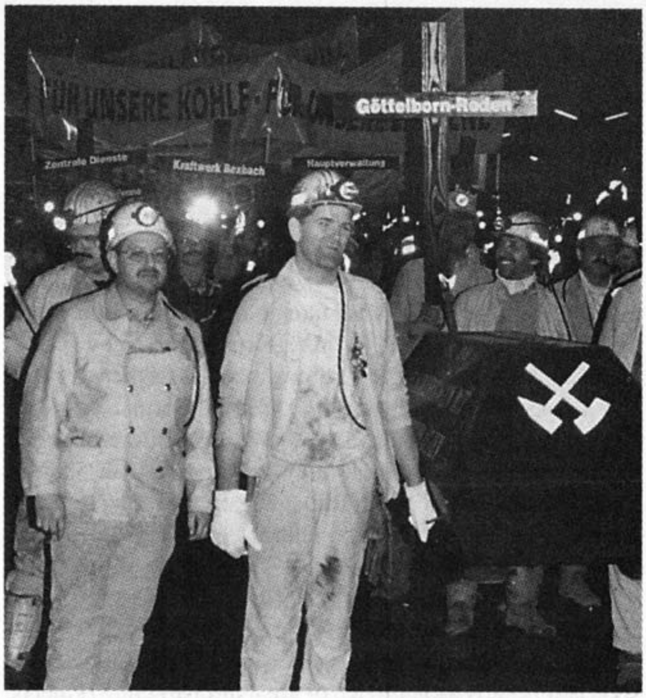
According to the Federal Statistical Office, the bankruptcies in eastern Germany had increased by more than 50% during 1995, rising toward 5,900. In 1997, this figure will have jumped toward 11,000. After five years of radical deindustrialization, eastern Germany today has 20% of the German population, but only 4% of Germany's industrial production, and only 1.7% of German exports.

The worst is yet to come. At a November conference of the Thuringia state government, Lothar Späth, the former Baden-Württemberg state governor who is now head of Jenoptik AG (Carl Zeiss Jena), warned that another "huge crisis" awaits eastern Germany. In the coming five years, he stated, half of the remaining industrial jobs will disappear, as medium-sized industrial companies are threatened by demolition.

Destruction of eastern German production

In 1991, one of the cornerstones of the German economy, the machine production sector, employed 1.5 million people. At the end of 1996, this figure had fallen to 950,000. In the first three quarters of 1996, machine orders fell 7% (in the case of domestic orders, 11%). The situation in eastern Germany is particularly bad. On Oct. 28, several hundred workers of the biggest eastern German machine tool producer, Heckert Chemnitzer Werkzeugmaschinenbau, marched through Chemnitz in protest, ending up in front of the Deutsche Bank office. The demonstration was sparked by the decision of a group of banks, headed by Deutsche Bank, to deny the company a DM 15 million credit that was urgently needed to overcome a short-term liquidity gap. Heckert had been seen as the most successful case of privatization in the eastern German machine sector. There was no lack of orders, just a liquidity gap, which was an immediate consequence of the collapse of the western German machine tool producer Traub, which had bought Heckert during the privatization drive. On Oct. 30, Heckert had to file for bankruptcy.

About 2,000 jobs in the Chemnitz region are dependent on Heckert. The company was formed in 1885, and later became Europe's biggest producer of metal-cutting machines. Under the communist regime, Heckert was the center of East Germany's biggest machine tool-producing conglomerate, with 27,000 employees. In 1990, the group was split, and Heckert



A demonstration of the German Mining and Energy Workers union. The Bonn government's austerity programs have sparked an upsurge of labor protests, as living standards and industrial production plummet.

emerged with 4,300 employees. Today, only 500 are left.

However, Heckert is not an exceptional case. The workforce of the Magdeburg-based machine producer Sket was slashed, over five years, from 30,000 jobs to 1,500, before the firm went bankrupt earlier this year. There are ongoing negotiations to save some 500 of these jobs.

In eastern German machine production, described in 1992 as "the backbone of industrial development" by the Treuhand agency (the federal agency in charge of dealing with the former communist companies), five years after reunification, only 78,000 out of 312,000 jobs remain.

Even more devastating, is machine tool production. Since 1990, the number of jobs in the eastern German machine tool sector collapsed from 100,000 to 10,000, while jobs in western German machine tool production dropped from 100,000 to 60,000.

Immediately after the fall of the Berlin Wall in 1989, in Chemnitz alone, there had been 12,000 jobs in machine production; only 10% of these jobs have survived. While employment at the machine tool producer Heckert had fallen from 4,300 to 500, jobs at the machine producer Union fell from 2,500 to 100; at Schleifmaschinenwerk, from 1,200 to 100; at Modul, from 1,600 to 100; and at the Chemnitz-based subsidiary of the machine tool producer Niles, from 2,000 to 150. Overall employment of the Berlin-centered Niles group, fell from 22,000, to 175. Several smaller machine producers in Chemnitz, which, during privatization, were bought up by the Frankfurt-based Rothenberger investment group, have completely disappeared. The destruction of the Chemnitz machine production has caused expenditures by the Chemnitz Unemployment Office of DM 10 billion so far.

The only productive sector that was booming in the early 1990s in eastern Germany, was the construction sector. A large part of construction work was state-financed infrastructure projects. However, public construction orders are now falling. In the first half of 1996, construction orders in Germany decreased by 8%, while unemployment in the construction sector went up by 32%; in eastern Germany, by 47.5%. Here, the Maastricht budget-cutting mania is further accelerating a process that has been ongoing in the German economy for decades: The percentage of federal expenditures invested in construction has fallen to 2.2%, compared with 5.2% in 1970. In the states of North Rhine-Westphalia, Baden-Württemberg, and Hesse, this ratio plunged from 25% in 1970, to 12% today.

Great projects needed

Unless Germany's self-destructive economic policies are soon reversed by an approach of great infrastructure projects, such as building a Eurasian land-bridge of transportation corridors linking Europe to Asia, Germany will no longer exist as a leading supplier of capital goods to the world economy in the next century.

In this context, Jürgen Schrempp, the chairman of the Daimler-Benz Group, otherwise known as a strong proponent of "shareholder value," gave a speech on Oct. 30 at a Berlin banking seminar, in which he strongly criticized the giant transportation bottlenecks at the border of Germany and Poland. Today, the train ride from St. Petersburg to Paris takes longer than it did 90 years ago, he said. He called for rapidly developing big and efficient east-west transport routes, in the same way that the big north-south routes were built in Western Europe during the 1960s.

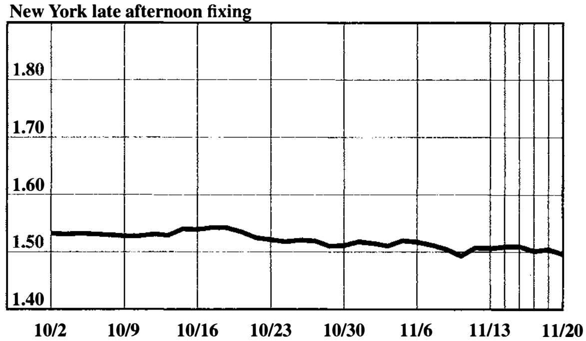
Said Schrempp: "We need the revival of the big European development axis Paris-Berlin-Warsaw-Moscow. It also serves the reunification of Germany, because it connects the economies in the West and the East. Transport grids develop regions, they activate hidden potentials. . . . Imagine an east-west infrastructure corridor, a highway running across the entire distance, a high-speed train route running along this axis. A project of such large dimensions, which would manifest the political and economic commitment, could work as a catalyst for investment, growth, and employment. This concept will blow away the signs of fatigue from which unified Europe is presently suffering. . . . This initiative should be the beginning of a European alliance for employment, which could fight the frustrating mass unemployment. Industry will not stand idly by, when the EU Commission pushes forward its already-designed [TEN/Delors Plan] infrastructure projects."

Strangely enough, Schrempp's speech was left almost unnoticed by the German media.

Currency Rates

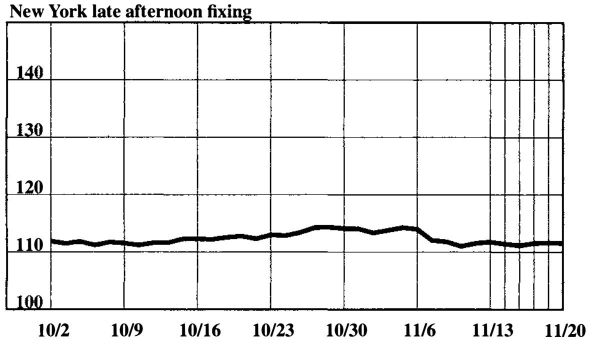
The dollar in deutschemarks

New York late afternoon fixing



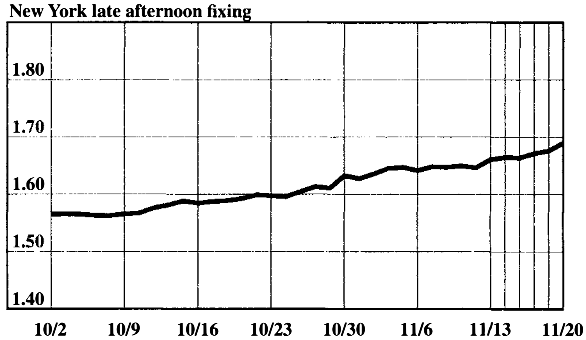
The dollar in yen

New York late afternoon fixing



The British pound in dollars

New York late afternoon fixing



The dollar in Swiss francs

New York late afternoon fixing