

Germany – Heading for Meltdown?

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Abstract: Germany looks prosperous, yet it suffers from low productivity growth and fiscal imbalances. These weaknesses could escalate in the future as the population continues to age. Measures to cut some entitlements and limit budget deficits have been taken, but it is doubtful that they will be implemented. German politicians are known to ignore such regulations and voters who should punish fiscal irresponsibility are in the throes of a *mentalité* that denigrates business activities, competitive markets, economic change and innovation. German politicians and voters extol the virtues of political action, social control, economic regulation, redistribution, and a life unsullied by commerce. Short of a radical change in such attitudes, voters will continue to call for productivity-reducing economic policies and an unsustainable level of welfarism. In the absence of a conjunction of contingent events favoring reforms, Germany could follow the well-trodden path of Southern Europe that ends inevitably in a fiscal meltdown.

Keywords: capitalism, Eurozone, German politics and economy, liberalism, *mentalité*, public finance, welfare state

- 1 Germany looks prosperous with a sound and dynamic economy, the strong man of Europe. This is an illusion. In reality, Germany is tottering on the brink like most of the rest of Europe. Voters demand more welfare payments; even freezing welfare expenditure is a recipe for electoral oblivion. The dance on the volcano goes on: additional welfare benefits are piled on existing ones although even the current system is unsustainable. For a while, this spending can be financed by tax increases and the outright expropriation of the middle-class, until, as in Greece, it will become clear that Germany is unable to service its debts. With structural reforms out of bounds, a meltdown seems inevitable.
- 2 The German economy has weathered the current economic crisis well. After a massive drop in national income it recovered quickly. Subsequently, economic growth continues at the anemic pace of before the crisis. Labor productivity has been barely budging for over a decade and incomes have been stagnating. At the same time, the government was unable to balance its budgets for decades even during booms, despite running down the country's infrastructure. Added to this, the prospect of rapidly mounting welfare expenditures looms. Demographic changes threaten to entirely destroy the government's financial position within foreseeable future. That is the story of this essay.[\[1\]](#)

Current Situation

- 3 The German economic success in recent years has come at a cost for its neighbors. Germany's competitiveness improved as its wage costs grew significantly less than those of its major competitors did.[\[2\]](#) Unable to compensate this disadvantage by devaluing their currencies, the members of the Euro Zone were particularly strongly affected.[\[3\]](#) As this improvement continued, Germany's current account surpluses that had temporarily vanished after reunification piled up again. [\[4\]](#) This increase in exports meant more employment in Germany and less in the rest of Europe.[\[5\]](#)
- 4 These surpluses in turn fed the borrowing boom in the countries whose economies

collapsed in the wake of the financial crisis. Germany's capital exports had helped to finance, at low interest rates, the housing bubble in Spain and the government deficits elsewhere. Germany now pays dearly for the credits granted in those years, some of which have to be written off completely. Having bought high levels of employment by subsidizing Euro member countries, Germany is now partially paying for the very goods and services that it had exported over the last decade.

- 5 The thriving German economy is more a reflection of the weakness of its neighbors than of its own strength. This is not to deny the stellar performance of German industry, particularly of its *Mittelstand*; in a recent article *The Economist* even talks about Germany's economic model that other countries would love to import. [6] However, this "model" is one of the industrial sector only, and even there, the Economist warns, the "platform for Germany's success looks precariously narrow." More to the point, manufacturing amounts to only 20 per cent of GDP and, still according to the Economist, the service sector "is in a much sorrier state." That the overall performance of the German economy has been far from outstanding shows most clearly in the feeble growth of labor productivity that indicates how much increase in real income people can expect.[7] Accordingly, since the turn of the century, German wages have hardly increased at all and the tiny growth in purchasing power was swallowed by tax increases.[8] Household incomes tell the same story; they have remained roughly constant for the low- and middle-income earners.[9] The German standard of living is in a phase of secular stagnation. Economic growth was driven mainly by adding inputs, particularly labor, to the production process; it was not the effect of productivity gains from innovation.
- 6 Beside the weak growth performance, the German economy has suffered from imbalances of the government budgets for decades. The government sector has continuously accumulated more and more debt. Indebtedness, measured in percentage of national income, began to increase during the 1970s; a trend that only slightly accelerated after unification and received another boost from the current economic crisis.[10]
- 7 The most recent public sector deficits cannot be attributed to this crisis. The artificially low interest rates benefited the public sector balance substantially.[11] Moreover, after the slump in the year 2009 the economy recovered quickly and returned to what amounts to full employment.[12] Yet only after a number of boom years was the government able in 2012 to balance its books for the first time in decades.[13]
- 8 The reason is simple: welfare spending is out of control. The trend towards an increasing proportion of national income spent on welfare goes back to the 1970s and hovers around 30 per cent today.[14] The endeavor to reign in welfare spending has been a continuous struggle in German politics, usually against strong popular opposition. The reforms of the labor market with its cuts in entitlements by the Schröder government, widely believed to have laid the foundation of the current low level of unemployment, have resulted in electoral suicide. [15] Merkel only failed to win her election against Schröder outright because she ran under a program that was even less redistributive. Thereafter she changed track and embraced a policy of welfare expansion. Recent elections confirm this voting pattern. Big spenders who promise more redistribution have won most recent State elections.[16] These experiences left deep traces in the thinking of the political class; hardly a week goes by without a discussion or the implementation of new measures to alleviate some social ill.[17]
- 9 The ensuing financial strains were partly compensated by cutting expenditures in electorally less sensitive areas, particularly public infrastructure.[18] Government net investment dropped to zero in the 1990s and turned negative at the turn of the millennium. German governments of all stripes have allowed public infrastructure to decay; the country literally consumed its future.[19]
- 10 To finance its expenditure, the German government showed few inhibitions. It systematically increases taxes by stealth. Bracket creep, the increase in taxes when inflation pushes income into higher tax brackets, is quite openly employed as a convenient way to increase taxation and government revenue. Indeed, recent discussions to eliminate some of the accumulated tax rises led to a barrage of polemics against the proposal on the ground that it amounted to a tax cut. Expropriation of income from assets has been a tool of German tax policy for decades.[20] The political class is now shifting gear. With the European central bank keeping interest rates at practically zero, the German state is able to finance much of its government debt at minimal cost as inflation reduces its real value, quite apart from pocketing the inflation tax derived from the cash issued by the central bank. At the losing end is a middle class that has made provisions for the future; it is now fleeced as taxes increase, the value of their pension funds contract, and revenues from life insurances rapidly fall.
- 11 Germany is a giant with feet of clay, with minimal growth of labor productivity, stagnating incomes, underinvestment in infrastructure, and highly precarious

government finances. However, such a situation is still far removed from a meltdown, a scenario that presupposes rapidly mounting financial pressures and the inability of the political system to reform its finances.

Mentalité

- 12 In a well-functioning democracy, successful implementation of political reforms hinges on the dominant *mentalité*, a set of values, beliefs, conventions, and norms shared by members of a community that motivate political action and ultimately policy making. In what follows, an ideal-type of such a *mentalité* is constructed. This sketch includes those elements that are believed to be of major importance for economic policy making in the future. It includes a particular view of social justice, attitudes to capitalism, beliefs about the social and moral consequences of spontaneous social interaction, government control, as well as risk and economic change. These elements find support in a particular version of Romanticism that seeks the Good Life in activities of self-expression other than commerce. This is not to say that this *mentalité* is alien to other nations or cultures; its components can be found in all modern Western nations. What makes it culture-specific is the particular strength and combination of its parts.^[21]
- 13 The first element is a particular view of social justice, the dominant theme in political discourse.^[22] Yet this discourse is remarkably free from defining what social justice actually means. In practice, the slogan is used to justify redistribution from people who have more wealth or income to people with less, from employers to employees (except in case of top management), from producers to consumers, from men to women, from those who work to those who live from social security. The underlying principle of justice most closely associated with this type of reasoning is equality of outcome. However, this view of justice derives its force precisely from being left vague and insubstantial. It allows tainting those who question the wisdom of any redistributive proposal with moral dereliction. This kind of argumentation has taken on the power of dogma among mainstream journalists, TV moderators, and politicians.
- 14 A second element of its *mentalité* is a fierce hostility towards liberalism and capitalism. Belief in justice and hostility to capitalism are related. Social justice, however defined, has never been the forte of spontaneous human interaction as it manifests itself in markets or more generally in capitalism. The inequity generated has justified anti-poverty programs in any industrialized society. Nobody seriously expects a resolution of this debate about limits to the welfare state even among liberals or social democrats.
- 15 The unequal distribution of income ought not to detract from the achievements of capitalism. That even the poor in Germany live a life of affluence compared to their ancestors or other inhabitants of the globe is hardly in dispute. What characterizes the German *mentalité* is its refusal to attribute these achievements to capitalism. Even otherwise intelligent observers insist that the high standard of living of the average German is not due to the play of market forces, but to trade unions and social reformers.^[23] This failure to acknowledge the social benefits of capitalism leaves it largely without *raison d'être*.
- 16 The hostility to capitalism is not limited to denigrate its achievements but extends to its social and moral consequences. In this debate, the *mentalité* is dominated by the view that capitalism causes moral failures, is founded in greed, dissimulation, and distrust, in individualism and the disruption of communities. Spontaneous individual action is not, as liberals have it, individually enriching, advancing social trust, the foundation of civil society, but is rather promoting social and moral disintegration.
- 17 In mainstream political discourse, the penchant for equality of outcome and the dislike of spontaneous social action are complemented by the belief in the efficacy of government regulation and control. These standpoints do not necessarily go together. One might be skeptical about free markets but equally so about government intervention. That, however, is not the case in the German debate.
- 18 This leads to the third element of this *mentalité*; it combines misgivings about loosely regulated social interaction with trust in effective government control; generally, and more specifically, the assessment that governments are better able to relate income to merit than markets do. How far politicians are willing to go is illustrated by the proposal of a senior minister in the Merkel cabinet to attune pensions to a person's life performance.^[24] Such a position stands in stark contrast to liberal beliefs that, however tenuously income and wealth are related to merit in capitalist society, an allocation through the political process is unlikely to improve the relation.
- 19 The process of state control is not only believed to be effective, but also socially beneficial. Whereas competitive markets are assumed to cause moral deterioration and social anomie, political action is considered to be morally improving and conducive to social harmony: greed characterizes economic interaction and elevated motives guide political processes insofar as they are not perverted by capitalist interest

groups. As soon as this belief is formulated in a coherent fashion, the thesis reveals itself as patently absurd. No-one seriously maintains that the pursuit of self-interest is less prominent in politics than in business, but like the thesis of the desirability of equality of outcome, the notion of the different nature of motivations in economics and politics lives from its appeal to unconscious predispositions, from remaining diffuse and evading rational examination.

- 20 Beliefs in the moral depravity of competitive markets and capitalism coupled to the idea of the beneficial working of the state are one of the constants in German politics, connecting the Bismarck era, the Weimar republic, National Socialism, Communist East Germany, and West German politics. Liberalism never had much support in Germany and only dominated policy making during the Erhard years immediately after WWII. Even then, it was deeply unpopular, not only among the left but also among many conservatives.
- 21 Inherent in this dominant worldview is a bias towards regulation and government provision. Manifest government failures are attributed to legislative shortcomings – leading to calls for further regulation. Deregulation is deemed a step backwards. And those privatizations that have occurred were mainly means to alleviate fiscal strains. Enterprises offering public services must remain “communal property” as a matter of principle, even when it comes to waste disposal or “recycling.”
- 22 A fourth main element in the German *mentalité* is the aversion to change generally and to all risks to social and personal life. This element is captured by the proverbial *Zukunftssangst* – anxiety about the future. Germany may well be the only country where university students are keenly interested in government pension schemes. General risk aversion implies dislike of technical innovations as they mostly come with uncertainties of some sort. Whatever one may think of the threats atomic power plants pose, deciding to shut down a major source of electric energy within a short period of time without having a clue how to replace the ensuing shortfall is a panic reaction of a deeply fretful society. Similarly, no rational argument is likely to convince the German public that genetically modified food is neither a threat to their health nor the environment. Nor is it likely that the extraction of natural gas by fracking will be allowed even where the risk of environmental damage is minimal and can be contained. On the other hand, technological change of the risk reducing kind receives extraordinary support, even if it is costly and the chance of successful risk-reduction are well-nigh zero – as in case of solar energy programs that are extremely expensive and have no discernible impact on what they aim at, the reduction of global warming.
- 23 However, even where no risks loom change is rejected by “concerned citizens” if it threatens to disrupt humdrum existence. This leads to remarkable political twists, such as the Green Party as an avowed proponent of public transport fighting against the introduction of a transport system involving a new technology, or even against the expansion of a railway station.^[25] The overriding motivating force ceases to be environmental and transmutes into hostility to any disruption of private life. Public life becomes diffused with an economic conservatism that in turn is closely connected to Romanticism, the last element of this sketch of a *mentalité*.
- 24 Romanticism is conventionally associated with opposition to rational thought, science, technology, and capitalism. It thus highly correlates with the *mentalité* described here. Yet on a different plane, it is the status of liberty that underpins the thinking of much what has been presented so far.
- 25 Why liberty? Attitudes to liberty in Germany are highly ambiguous. On the one hand, there is outright hostility. People who stress the value of liberty as an important element of the Good Life are strongly distrusted, often because more liberty is thought to lead to less equality. The current president of the republic is very unusual in this respect, but even he had to tune down his eulogies on liberty. Particularly commercial liberty is distrusted. Ideally, the state caters for work and income directly or indirectly through the regulation of working conditions, wages, unemployment insurance, free education, health services, and pensions through a vast apparatus of social security and employment agencies, state education and health facilities, as well as government enterprises.
- 26 On the other hand, liberty is highly valued, particularly the freedom to consume. Indeed, even those who condemn consumerism tend to engage in much leisure related activities, preferably in exotic places. Thus it is expected that the state guarantees a high income sufficient for an affluent existence, a large well-equipped flat or house with all the modern amenities, access to information technology, high quality education and health services, free individual or subsidized public transport and public entertainment. *Panem et circences* for those who often think of themselves as pursuing an “alternative,” “unconventional,” and “anti-bourgeois” lifestyle.
- 27 The ambiguous attitude to liberty is grounded in the Romantic cult of individuality and self-expression. In contrast to the view of the Good Life of traditional societies where people find a meaningful existence by being integrated into prevailing social

and occupational structures, the Romantic view presumes that each human being has a particular personality with different needs that require a unique lifestyle that allows the unfolding of this individuality or personality through self-expression. Self-expression, however, is not something greatly enhanced by commercial activities; “true” self-expression finds outlets in political, social, and cultural pursuits. Like much of the elements of current *Zeitgeist*, the underlying ideas are spurious – when challenged probably few people would cling to the view that all business activities are inherently less creative, rewarding and fulfilling than those of the “more elevated” type.

- 28 The Good Life, then, consists of a secure and comfortable material existence with a great amount of leisure where individual liberty is employed in the pursuit of self-expression.[26] Social control or social and political constraints not freely chosen are merely chains that hamper the pursuit of untrammelled individualism. Any outcome of political processes not matching one’s predilection is rejected to the point of violent resistance, even when it comes to rejuvenating a railway station. The legitimacy of political decisions does not hinge on whether they followed due process – the foundation of democratic life – but whether the outcome conforms to individual desires. This not only increases the difficulty of political decision-making, but also is associated with a ruthless pursuit of entitlements. In one of its more bizarre manifestations, student protests that found wide public support forced a number of state (*Länder*) governments to rescind a student fee of roughly € 500 per semester – university education ought to be “free.”
- 29 The ideal-type outlined is an abstract construct meant to provide an understanding of the motives and intentions of individual actors. As these are not observable, the closest measurable evidence available is its conformity to attitudes as expressed in surveys.[27] Thus the confidence in an ideal-type is greatly impaired if it dramatically contradicts findings of attitude-surveys. It turns out that the presented ideal-type corresponds well to the data available from the World Values Survey. German respondents are highly supportive of government intervention and income equalization. Their support exceeds not only the levels in Britain and the United States but those in France and Italy as well; only Spaniards, although not sharing the German penchant for redistribution, are equally keen on government intervention in business and social life.[28]
- 30 This *mentalité* stands in the way not only of innovation, creative destruction, and growth of labor productivity, but also of successful fiscal reforms, the main political challenge in the next decades.

Future challenges

- 31 Little has changed since Adam Smith: “Great nations are never impoverished by private, though they sometimes are by public prodigality and misconduct.”[29] Such fiscal collapse is the stuff revolutions are made of, including its archetype, the French Revolution. To assess the likelihood of a German fiscal meltdown, future fiscal problems are presented that are already evident today[30] together with an appraisal of the ability of the political system to cope with these strains.[31]
- 32 Germany’s fiscal position will be strongly influenced by demographic factors; its population is estimated to contract from today’s 80 to somewhere between 65 and 70 million in 2060. Of these, 9 million will be over 80 years old.[32] The shrinkage of the working age population is particularly large; it will be dropping by 20 per cent by 2035[33] and one third by 2060.[34]
- 33 These demographic changes will have severe financial consequences for Germany’s social security system that is organized along the pay-as-you-go principle: those in employment pay for pensions and health care of the retirees. The principle implies a rapidly deteriorating financial position as the workforce shrinks and the number of retired people surges. This deterioration is captured by the old-age dependency ratio (those aged 65 and more as a share of 20- to 64-year-olds), which stood at 34 in 2008, is projected to increase by 80 per cent by the end of the 2030s and will roughly double by 2060.[35] In other words, by the latter date 10 people of working age have to maintain more than 6 pensioners. This most widely used figure used to illustrate the effect of an aging population on social security still underestimates the true level of dependency. The relevant ratio is the active labor force relative to those who have to be maintained by it. If, as projected, the labor force participation rate is not going to change greatly,[36] we arrive at the troubling conclusion that by the middle of the century one person in employment must provide nearly one pensioner with suitable income and health care facilities, including the millions of over 80 in intensive care. Since it is hardly conceivable that the employed are willing and able to carry this burden, the system is heading for collapse.
- 34 A popular minority view disagrees with this prediction and postulates that productivity growth will generate enough resources to salvage the welfare system. However, it remains true that one worker would have to maintain nearly one

pensioner, but because those in employment produce more and have higher incomes, the high rate of taxation might hurt less. Is this hope realistic?

- 35 Productivity improvements will have to come in the main from innovation and improvements in human capital. Unfortunately, the productivity of a rapidly aging workforce is likely to decline. Physical fitness and mental agility decrease. Work motivation suffers with approaching retirement and incentives to further training diminish. Business dynamics will be negatively affected too because younger age groups are participating disproportionately in entrepreneurial activities. At the same time, there are few indications that the quality of those entering the work force is improving. Most people in Germany possess a solid professional training already; only one in six is without such qualifications and often a recent immigrant. This proportion is predicted to remain stable.[37]
- 36 There are further developments that tend to depress labor productivity. The increasing level of regulation is one.[38] An obvious case is environmental regulation that is adversely affecting the productivity of the energy sector and jacks up electricity prices. The pace of new safety and labor regulations is unlikely to abate too. Deregulation faces high political hurdles; even where there is a political consensus that reforms are needed as in the case of the enormously complex and constantly changing tax system. Vested interests have proved too strong to overcome. At best, labor productivity will continue the sluggish path of the past decade that was barely sufficient to keep real wages constant.
- 37 That productivity growth is not an answer to the fiscal problems has long been recognized by the vast majority of the political class and has resulted in two approaches to reform, one aiming at the social security system directly, and the other at the overall fiscal deficits.
- 38 Reforms of the welfare system include an increase in the retirement age from 65 to 67 and the introduction of a demographic-sustainability factor that reduces retirement benefits as the old-age dependency ratio rises. The main reform addressing the fiscal deficit is the so-called *Schuldenbremse* or debt-break, a constitutional provision that limits budget deficits; [39] if adhered to public finances would be rapidly consolidated.
- 39 However, these steps amount to little more than statements of intent since they are supposed to be implemented only gradually.[40] This is true of the retirement age and reduction of pensions as well as the *Schuldenbremse*. Moreover, according to the best available estimate the reduction in deficits would still require large budget cuts or major tax increases beyond the various social security reforms already agreed upon. [41]
- 40 This leads to the question whether these reforms will actually be implemented. One indicator for such a prediction is the degree German politicians are willing to follow formal rules and that laws and regulations are a binding constraint on political action. The technical term for this is the degree of institutionalization. If the level of institutionalization is low, rules and regulations will only be implemented if it is in the interest of the political class to do so. Thus, two questions arise: what is the level of institutionalization, and if it is low, will it be in the interest of the political class to implement reforms?
- 41 Germany gives the impression of a country with a high level of institutionalization where rules and regulations are generally adhered to even in the absence of sanctions. Recently, this image suffered some damage when various German governments did not feel the need to insist that European fiscal policy rules are to be obeyed by other members of the community and finally disregarded these obligations themselves.[42] This did not come as a major surprise. The German constitution had already contained the sensible provision that limited the yearly debt increase to investment spending.[43] The rule has been honored mainly by its breach. *Prima facie* evidence suggests that German politicians disregard fiscal rules if these are onerous and are not supported by sanctions. However, the level of commitment of those who designed debt limits did not go so far as to envisage penalties for violating these. This leaves electoral punishment as the main incentive to practice fiscal rectitude.
- 42 The gradual introduction of retirement at age 67 is by no means generally accepted, and this at a time when experts already call for retirement at 68 or 69 after 2029.[44] Even more contested is the reduction of the level of government pensions.[45] Tampering with health benefits is taboo, too – anything less than access by everybody to a treatment of all physical and mental ills at the highest medical standards is unacceptable.[46] The only realistic reform proposal that would significantly improve the financial position of the health care system is to increase the contributions of high-income earners – in essence, a form of a tax increase for the better off.
- 43 If, as recent elections have shown, voters are not only refusing to accept a consolidation of the welfare state but want more of it, there are few incentives for the political class to practice fiscal prudence. However, voters' preferences might change if

government finances deteriorate, as they undoubtedly will. A long list of democratic countries has pulled back from the brink including the United Kingdom, Australia, New Zealand, Ireland, and Sweden. Will Germany be able to follow this lead?

- 44 Here is what such a change in preferences would require: a reassessment of innovation and the economic disruption that innovation entails; an acceptance of entrepreneurship and competitive markets as the foundation of the welfare state; the recognition that individuals and society embodied in families and civic groups are primarily responsible for the conduct of their own life; and the awareness that a substantial degree of inequality is socially desirable and that there are limits to the scope of the welfare state. It would involve a veritable revolution of political culture that currently blames capitalism, competitive markets, globalization, and innovation for all social ills and virtually demonizes reformers like Margaret Thatcher instead of accepting that in the situation of Britain in 1970s some structural reforms were unavoidable. That such a change of a deeply rooted *mentalité* will occur before the state is on the verge of bankruptcy is unlikely. Much more probable is a scenario that voters continue to believe that the creaking welfare system and the stagnating wages are the fault of neo-liberalism, capitalist greed, and globalization, that they continue to opt for populist policies and seek a solution to their woes in more state control of the economy, higher taxation, expropriation through inflation and more redistribution.
- 45 In the absence of predictable causes for a policy change there is always the possibility of contingencies fashioning an environment in which strong leadership emerges and is able to assert itself in the manner of Margaret Thatcher winning the Tory nomination. Without such a conjunction of accidental events, such as the destructive behavior of a trade union movement that ensured Thatcher's election and the Falkland war her re-election, Germany is bound to follow the well-trodden path of Greece, Italy, or the Argentina of Peron and the Kirchners toward fiscal meltdown.

Conclusion

- 46 The German economy suffers from a number of weaknesses: Low productivity growth, a stagnating income for the vast majority of the population, and large fiscal imbalances with welfare expenditures out of control. These weaknesses will become more pronounced in the future as the population continues to age. The vast majority of the political class has accepted that reforms of the social security system are inevitable to avoid a fiscal breakdown and has taken steps to cut some entitlements and limit budget deficits in the future. Whether these far-reaching reforms will be implemented is doubtful, however. German politicians are known to ignore fiscal regulations if they do not correspond to their interests and sanctions can be avoided. Voters who might punish fiscal irresponsibility are in the throes of a *mentalité* that denigrates business activities, competitive markets, economic change and innovation, and extols the virtues of political action, social control, economic regulation, redistribution and a life unsullied by commerce. Short of a cultural revolution, voters will continue to call for productivity-reducing economic policies and an unsustainable level of welfarism. In the absence of a conjunction of contingent events that trigger reforms, Germany will experience a fiscal meltdown.

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Notes

[1] The story is limited to the prospect of the German economy. What ails Germany does ail other countries as well to a greater or lesser degree. Introducing comparisons is beyond the scope of this essay and irrelevant for the conclusions arrived at.

[2] After unification unit labor costs rose rapidly and then stabilized around 1995, years before the much vaunted reforms of the labor market by chancellor Schröder beginning in 2003. Indeed, in 2006 unit labor cost were slightly below those of 1995 (Sachverständigenrat 2013, Lohnstückkosten nach Wirtschaftsbereichen).

[3] Competitiveness improved also in comparison to non-Euro countries, again partly as an effect of the Euro: it appreciated less against other currencies than the German Mark would have done.

[4] The current account went into deficit in 1991 and remained there until 2001. In a phenomenal turnaround, it then reached a surplus of 8.2 per cent of GDP in 2007 (Sachverständigenrat 2013, Zahlungsbilanz, Bruttoinlandsprodukt).

[5] These developments correspond closely to those of the classic beggar-they-neighbour policy of currency depreciations. They were unintended, of course. According to economic theory, the relatively rapid increase of the demand for goods

and services ought to have boosted German wage costs relative to those of other countries, precisely the opposite of what actually happened. Real wages in Germany remained constant, whereas labour market rigidities ensured that Spanish ones, for example, increased despite high levels of unemployment.

[6] The Economist 2012.

[7] Labor productivity increased in the period from 2002 to 2012 by 0.61 per cent a year (Sachverständigenrat 2013. Arbeitsproduktivität je Erwerbstätigen). This compares West German to yearly growth rates in the 1970s and 1980s of roughly 2.3 per cent on average (Bundesministerium für Arbeit und Soziales 2012, Table 3.1, Industrieproduktion und Produktivität).

[8] They are now at the level of 1991 (Sachverständigenrat 2013, Löhne und Produktivität; Verbraucherpreise).

[9] Bundesregierung 2013, 323; 2008, 19.

[10] Government indebtedness as a proportion of GDP remained constant from the 1950s to the mid-1970s at 20 per cent of GDP. It reached 42 per cent at unification, rose to 68 per cent before the current crisis, and is now over 80 per cent (Sachverständigenrat 2013, Verschuldung der Öffentlichen Haushalte).

[11] Real interest rates are now negative thanks to the massive expansionary monetary policy of the European Central Bank and the capital flight from Euro-zone countries to the relative secure German sovereign debt.

[12] The unemployment rate reached its peak in 2005 with 10.7 per cent and then dropped continuously until it reached 5.3 per cent in 2012 (Sachverständigenrat 2013, Erwerbstätigkeit).

[13] Ministerium für Finanzen. 2013. The budget surplus amounted to 0.2 per cent of GDP.

[14] Social expenditures amounted 20.2 per cent in 1970 and hover currently around 30 per cent (Bundesministerium für Arbeit und Soziales. 2012). This quota has been stabilized mainly by a reduction in pension and unemployment entitlements and the reduction in unemployment caused by the current boom.

[15] The Hartz-Reforms introduced between 2003 and 2005.

[16] Most significantly Baden-Württemberg 2011; Rheinland-Pfalz 2011; Schleswig-Holstein 2012; Niedersachsen 2013.

[17] A typical recent example is the “family policy” to boost the birth rate.

[18] The current amount of investment spending by local communities, responsible for much of the infrastructure, barely exceeded the nominal outlay of before unification (Sachverständigenrat 2013). Net investments have fallen to zero in the 1990s and have been negative during much of the first decade of the new century (Deutsche Bundesbank 2009: 15-34).

[19] Infrastructure problems go well beyond the well-known case of the dilapidated infrastructure of Ruhr valley towns. The Kiel canal, the world’s most highly used artificial waterway connecting the North Sea and the Baltic, had to be closed for weeks because of the derelict locks (Frank 2013: 1).

[20] With a taxation rate of 50 per cent, average revenue of 4 per cent and an inflation rate of 2 per cent, the whole real return of 2 per cent was taxed away. The expropriation of income led to massive capital flight abroad and to tax avoidance schemes that enriched mainly the providers of these schemes. Tax rates have come down meanwhile, although the opposition parties have announced they would increase them again in case they come back to power.

[21] Of interest here is not how Germany’s *mentalité* differs from other societies, but how it influences policy making.

[22] The main opposition party, the Social Democrats, decided to fight the federal election 2013 under motto “social justice financed by tax hikes” (ARD 2013).

[23] Piper 2013.

[24] Entwurf eines Gesetzes zur Anerkennung der Lebensleistung (Lebensleistungsanerkennungsgesetz).

[25] The Stuttgart central station.

[26] Self-expression is another of these shibboleths of Romanticism, presupposing the phantom of some given “self.”

[27] The mentalité does not describe attitudes, but goes a step further and gives an understanding of why particular attitudes are adopted.

[28] World Values Survey (2013). Respondents ranked questions on a scale of one to ten. The three relevant questions are: “Incomes should be made more equal” versus “we need larger income differences as incentives,” “private ownership of business should be increased” versus “government ownership of business should be increased,” and “the government should take more responsibility” versus “people should take more responsibility.” The comparison included Germany, the U.S., Britain, France, Italy, and Spain. Looking at the percentage of answers with the highest collectivist leanings (i.e. the three highest ranks), Germany always took the pole position with one exception, the question on the government ownership of business. There it was marginally overtaken by Spain. Comparing means leads to a similar result, only Spanish respondents are slightly more averse to private ownership and personal responsibility. The three questions were surveyed systematically only in the latest wave; no long-term comparison is available (World Values Survey 2005-8).

[29] Smith 1776: II.3.30.

[30] This implies a focus on welfare expenditures. Highly contingent fiscal problems are neglected, like potential liabilities from Euro rescue packages or common debt policies.

[31] This is a very different procedure from that of most mainstream economics that focuses not on the actual fiscal challenges ahead and on the political decisions required to solve them but estimate “sustainability” of fiscal policy on the basis of past patterns of income and expenditure. No conclusions for the future – that is located outside the frame of reference of these studies – can be drawn from such analyses.

[32] Federal Statistical Office 2009: 12; 17.

[33] From today’s just under 50 million to roughly 40 million in 2035 (Federal Statistical Office 2009: 6).

[34] Sachverständigenrat 2011: 8; 94.

[35] Federal Statistical Office 2009: 6; 20.

[36] According to the Sachverständigenrat (2011: 93). It stands currently at 72.6 per cent (OECD 2012).

[37] Sachverständigenrat 2011: 98.

[38] One of the most bizarre pieces of legislation regulates the recycling of cans whose expensive provisions achieved the opposite of its intentions but still remains on the books.

[39] It limits additional Federal Government debt to a 0.35 per cent of GDP a year. State budgets ought to be balanced. Structural deficits, highly susceptible to interpretation, are used as criteria and there are exceptions to the rules.

[40] The provisions are fully in force in case of the Federal Government in 2016 and the State Governments in 2020.

[41] Sustainable fiscal conditions would require an improvement of the fiscal balance by 3 per cent of GDP. Without such consolidation, the debt would accumulate to 270 per cent of GDP by 2060 (Sachverständigenrat 2011: 10). To illustrate: The increase in the retirement age would leave the old-age-dependency still significantly above the current one (Federal Statistical Office 2009: 21) at roughly 8 pensioners per person employed in 2060.

[42] When an excessive deficit procedure against Germany was abandoned in November 2003.

[43] Article 115 of the constitution (Grundgesetz).

[44] Sachverständigenrat 2011: III.

[45] Retirement benefits are expected to drop by roughly 20 per cent by 2030. For a reaction see DGB 2007.

[46] Typical for absurdly low level of the debate is the importance of the alleged “zwei Klassen Medizin” or a different type of treatment for the rich and powerful, as if those leading politicians deploring the practice had not benefited by it and as if this could be prevented except by a totalitarian system abolishing all private medical treatment.

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