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The Economic Rebuilding of the East under Fire (June 28, 2004)

Against the backdrop of an intensive discussion about the economic future of the new *Länder*, the *Gesprächskreis Ost* [*Roundtable East*] recommended a change of course. According to its suggestions, money should no longer be used solely to build infrastructure, but rather to advance economic enterprises, research, and economic clusters. The *Gesprächskreis Ost* saw the rebuilding of the East as part of a reform policy for all of Germany. The group's thirteen members came from the spheres of politics, business, and science; the federal government had charged them with analyzing the policy of subsidies in the economic rebuilding of the East.

Course Correction in the Economic Buildup of the East

Summary in Theses

(1) Since unification, great progress has been made in the economic buildup of the New *Länder*. Hard work and large financial transfers by the West German federal states for the economic rebuilding of the East have made this possible. The considerably increased material living standard in the East, the extensively expanded or newly built infrastructure, and the external appearance of cities and villages show what has been accomplished.

(2) At the same time, an extreme deindustrialization took place in the years after the *Wende*, and this was accompanied by a collapse in industry-related research. And despite comprehensive support, it was not possible to achieve self-sustaining economic development in the new federal states. This is demonstrated most dramatically by the average unemployment rate, which is catastrophically high, by the stagnation – for several years now – of added value at only around 60% of the added value in the West, and by the continuous outmigration, especially of highly productive individuals. An adjustment of the added value in the East to an average of 90% of that in the West by 2020 would mean above-average real growth of 4-5% in the East: an unlikely “economic miracle” that reveals the gravity, but also the challenge, of the economic buildup of the East.

(3) A stagnating East with a high need for transfer payments is a great threat to the future development of all of Germany. Evidently, the goal of a self-sustaining economy in the East cannot be attained by following the present course. That is why the economic rebuilding of the

East must emphatically stand at the center of political action. A course correction in the economic buildup of the East is necessary.

(4) The federal government is putting the further buildup of infrastructure at the center of its strategy for the economic rebuilding of the East. But the manufacturing sector, especially industry, accompanied by a comprehensive research landscape and corresponding education and training, should stand at the heart of the strategy for the economic rebuilding of the East. For these are the indispensable foundations of self-sustaining economic development. By contrast, the infrastructure in the East is already largely competitive. There is very little that needs to be added to build up competitive enterprises.

The course correction must therefore take place through

- a shift in focus from infrastructure to the buildup of business enterprises and a supportive research landscape to accompany them;
- a transition from across-the-board [growth] promotion to an emphatic concentration on growth clusters;
- a transition from start-up subsidies to more long-term, revenue-supporting measures, both for newly arrived businesses, and for existing ones (which are generally too small, financially too weak, and not yet sufficiently rooted in the market).

(5) This course correction has consequences for financing the economic buildup of the East. The financing volume hitherto planned for in Solidarity Pact II¹ is apparently the upper limit; it must not be reduced, nor should too much be used for state consumption. And there must not be any reduction in the obligations of the Shared Task of Economic Promotion [*Gemeinschaftsaufgabe Wirtschaftsförderung (GA)*]. The funds for investment subsidies, whose elimination is being proposed, should be incorporated into GA funding.

(6) The reallocation of funds from any infrastructure project that is no longer absolutely essential to direct support for business and research can make possible the above-mentioned shift in focal points. To that end, beginning immediately, all infrastructure projects must be strictly reviewed as to their importance for business development. In the future, only absolutely essential projects should be carried out.

(7) A successful economic structure presupposes a regional concentration and aggregation of branches in the East as well. This must be done in close joint cooperation with the business sector, the scientific community, and the state. However, identifying growth clusters for purposes of support can only be successful across states if the federal government is given a

¹ In 2001, the federal government and the federal states agreed to continue special financial support for the federal states in the former GDR. The so-called Solidarity Pact II covers the period 2005-2019; the total volume of special transfer subsidies amounts to 156 billion Euro – eds.

decisive participatory voice in decision-making; this must be worked out with the *Länder* in a binding agreement.

(8) The concentration on growth regions demands a reasonable incorporation of the weaker growth regions into transportation planning.

(9) As a result of the enlargement of the EU, special provisions must be drawn up for the border regions.

(10) The future regional and substantive strategy for economic rebuilding must be brought together in a regional master plan (growth clusters: infrastructure; business; science; agriculture and food production; rural areas). The plan serves to coordinate economic measures for the growth clusters and should be agreed upon, continually revised, and eventually reworked by the federal government and the *Länder*.

(11) A successful development must realistically begin with the current economic structure in the New *Länder*. In the industrial sphere, that structure is characterized by mostly small enterprises with weak market positions, inadequate research potential, but also low equity bases and nearly insurmountable problems in procuring loans.

It is therefore essential to redefine the cooperation between the KfW² and the principal banks – taking into account risk and cost – so as to facilitate the business sector's access to development loans and capital.

(12) In addition, the development funds that are freed up by the proposed reallocation should be used to establish an Equity Capital Fund for Venture Capital, which would serve to stabilize existing small and medium-size enterprises and to set up new, innovative enterprises.

(13) Financial problems inherited from the former GDR and undesirable developments caused by unification in the area of communal housing construction, as well as in wastewater treatment systems, should be cleared up by, among other things, the consolidation of enterprises and capital write-downs. To that end, the Redemption Fund for Inherited Burdens [*Erblastungstilgungsfond*] should be reopened.

(14) But corresponding savings measures at the state level are also required. This task for the *Länder* is essential in expanding the financial leeway of the *Länder* and the municipalities in promoting business.

² The KfW banking group is jointly owned by the federal government (80%) and the federal states (20%). It was founded in 1948 as the *Kreditanstalt für Wiederaufbau* (KfW) [Credit Institute for Reconstruction] – eds.

(15) The New *Länder* must be accorded the greatest possible leeway so that each *Land* can scale back its bureaucracy according to its own needs. The “Artikelgesetz”³ proposed by Helmut Schmidt would be a suitable instrument to this end.

(16) The special situation on the East German labor market also calls for regularized, additional flexibility, as well as the use of wage supplementation measures, in order to also provide labor-market access to groups of people who can no longer be retrained.

(17) For the implementation of the indicated measures, time-specific targets, control mechanisms, and timely, unvarnished reporting should be put in place.

(18) To that end, better organizational solutions are needed in the federal government. The coordination of the tasks of the various ministries and the implementation of decisions must be improved. To achieve this, it would be useful if the federal government charged a person with coordinating these tasks, this being his sole responsibility. This person should have the continuous support of a committee of experts with practical experience.

(19) Given the magnitude and importance of the tasks for all of Germany, the *Gesprächskreis* (roundtable) proposes that the measures be anchored in an “Economic Rebuilding Pact for the East,” in which the federal government, the *Länder*, parties to collective wage agreements, and representatives from the research community should participate jointly.

The *Gesprächskreis* assumes that the reorientation of goals and instruments proposed here, and a stronger political focus, can not only make the rebuilding work more effective, but can also serve to strengthen East German citizens’ confidence in the future of their region once again, ameliorate the outmigration, and enhance the attractiveness of investments there.

It should be emphasized once again: the proposed steps for the East do not relieve Germany as a whole from the need for a substantial general structural renewal (reform) of the nation. For there is no conflict between a reform policy for all of Germany and a targeted strategy for the economic rebuilding of the East. On the contrary: one is contingent upon the other. Only together, and only if the problems of East and West are put into a politically comprehensible context, can we in Germany finally create the positive climate we have longed for for so long. The Germans must be able to recognize that it is not their inefficiency, but rather the special challenge they face as a result of unification that is hampering growth in Germany today. And only if the economic rebuilding of the East is undertaken with resolute determination will all of Germany once again have the prospect of a promising future.

³ The term “Artikelgesetz,” or article law, refers to a law that changes several laws; that is, in addition to creating new legislation, it also amends existing legislation. In a 1997 article in the weekly newspaper *Die Zeit*, former chancellor Helmut Schmidt criticized the massive number of legal rules that hindered business and the creation of new jobs. Among others, he called upon politicians to only pass laws that eliminated or simplified existing rules and regulations – eds.

The *Gesprächskreis* sees itself as an all-German advisory council to the federal government, one tasked with focusing on the problem area of the New *Länder*. We hope that our proposals will also be received in this way and that they will be regarded with the same seriousness with which they were drawn up. With our proposals, we wish to advance the East and contribute to a new mindset that focuses on development in East and West.

It is our hope, therefore, that the federal government will succeed in creating what we regard as the necessary organizational preconditions, and that after the 2004 summer recess it will thus work together with the federal states, collective wage agreement parties, and scientific organizations to create the necessary foundation for a course correction through an Economic Rebuilding Pact for the East.

For what Germany needs is the spirit of a new beginning borne by all strata of society.

Source: *Kurskorrektur des Aufbau Ost. Bericht des Gesprächskreises Ost der Bundesregierung* [Course Correction in the Economic Buildup of the East. Report by the Federal Government's Roundtable East]. Edited by Klaus von Dohnanyi and Edgar Most. Hamburg and Berlin, 2004.

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