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# Structural challenges for the German economy

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## 1 Introduction

Dear Monetary Workshop participants, dear ladies and gentlemen, I am delighted to be with you today. Glancing at the programme, I see that you have already been having intense discussions about Germany's reorientation today – and from very different perspectives at that.

The title of the workshop – which I assume is a deliberate slight exaggeration – asks whether Germany's economic model is in trouble. I wouldn't go that far just yet.

But one thing is certainly clear: the German economy is facing major challenges. I would like to take the opportunity to discuss these challenges, and potential solutions, with you today.

## 2 German economic growth under pressure

Before we discuss solutions, let's get a better idea of where we currently stand. Economic growth in Germany has been weak in past years. The German growth engine was beginning to sputter as early as the end of the 2010s.

One significant reason for this was the loss of competitiveness of German enterprises in the international markets. In recent years, this has been reflected in a significant decline in export market shares.

According to Bundesbank estimates, around three-quarters of this decline is due to decreased competitiveness.<sup>[1]</sup> This applies across two dimensions: some products are becoming relatively more expensive, while by contrast, others are not performing as well.

In addition, many German enterprises specialise in products for which global demand has recently been weak. The automotive industry is a key example of this. Accordingly, the German export goods mix, which has been a recipe for success for decades now, has also recently contributed to the decline in market shares.

China is likely to have played a particular role in all these developments.<sup>[2]</sup> For example, a recent survey of firms conducted by the Bundesbank shows that German exporters, in particular, have come under competitive pressure as a result of their Chinese competition.<sup>[3]</sup>

This is consistent with the fact that China's export industry has continued to gain market shares in recent years, driven by increased competitiveness. The most significant progress in China's competitiveness can be seen in the electrical, automotive and mechanical engineering industries. In other words, economic sectors in which Germany has traditionally been particularly strong.

The deterioration in the competitiveness of German enterprises also plays a role in the significant decline in exports to China. However, sluggish growth in the Chinese economy over the past few years was probably equally relevant.

Between 2021 and 2025, German exports to China fell by one-fifth. German motor vehicle exports to China were particularly hard hit. They have virtually halved since 2021, accounting for more than 60 % of the decline in exports to China alone.

The development of exports to China differed substantially from that of exports to other sales markets. Exports to all other countries have been at least largely stable since 2022.

Ultimately, however, subdued exports are merely a symptom of more fundamental problems. In general, the German economy is no longer growing as it used to. This is reflected, not least, in a sharp decline in potential growth since the early 2020s.

Between 1999 and 2019, potential growth was still increasing significantly, by more than 1 % per year. But since the onset of the coronavirus pandemic, it had already fallen markedly below 1 %. And our experts anticipate an annual potential growth rate of around only 0.4 % over the next few years.<sup>[4]</sup>

This figure is a warning signal. What exactly is behind this decline, and what measures would be appropriate to reinvigorate potential growth? These are the questions I would now like to address in detail.

### **3 Strengthen potential growth**

Potential growth can be broken down into three factors: first, labour input growth, second, capital input growth, and third, labour and capital input productivity growth, otherwise known as total factor productivity. There is considerable room for improvement in all three areas.

#### **3.1 The factor of labour**

Let me begin with the factor of labour. After many years of – in some cases strong – growth, the number of persons of working age in Germany is likely to have reached its peak in 2025.<sup>[5]</sup>

Demographic change is the main driver of this development. You may have heard it recently on the news: 2025 was the year with the lowest number of births in the post-war period. There were 650,000 births and 1 million deaths.<sup>[6]</sup> At the same time, life expectancy has risen significantly.

As a result, the ratio of people aged 65 and over to people of working age has already been rising steadily for just under three decades. Although this is a global phenomenon, it is more pronounced than average in Germany.

The ageing of our society has therefore been contributing to the contraction of our labour force potential for quite some time now. At the start of the 2010s, it was reducing the number of people of working age by just over 200,000 per year. This demographic decline rose to just over half a million people per year by the early 2020s.

The experts expect this decline to continue over the coming years, too. And unfortunately, their forecasts are quite reliable: in Germany, all of the young professionals of the next few years have already been born – or not, as the case may be.

In view of this trend, how can it be that the labour force nonetheless expanded substantially up until last year? Two factors more than offset this decline: namely immigration and higher labour force participation.

Up until 2019, they both contributed positively in equal part to the growth of labour force potential – as from the middle of the last decade, considerably more strongly than in the years before. The coronavirus pandemic caused a small dip, but this was offset again from 2022 onwards, in particular due to a strong influx of immigrants from Ukraine.

Our experts predict that in the years to come, immigration and higher labour force participation will continue to bolster the number of workers. However, going forward, these positive contributions are unlikely to be sufficient to offset the demographic decline.

The potential labour force is likely to contract in future, which will weaken potential output.

This forecast is based on the policy measures that can currently be anticipated. If policymakers turn the right levers, though, we will of course be able to change things.

So what exactly should be done? Speaking generally, Germany should do everything in its power to increase the labour supply.

One way to do this is to enable part-time employees, who often wish to increase their working hours, to do so. This applies in particular to women. The annual hours worked per worker in Germany are low compared with other advanced economies. One reason for this is financial disincentives in taxes, social security contributions and transfers, which often make additional work less attractive.

Another major obstacle is the insufficient provision of care for children and the elderly. A more reliable range of care facilities, longer opening hours and greater flexibility could increase the labour supply.

Germany also needs more labour market-oriented immigration. The reformed Skilled Immigration Act (*Fachkräfteeinwanderungsgesetz*) presents opportunities here. That being said, the current procedures are still too slow and too complex. A “work and stay” approach that includes faster digital processing, easier recognition of qualifications and better integration would be helpful here.

The Federal Government’s plans in this area, which form part of its modernisation agenda, are therefore expressly welcome. Language courses and the right to remain for family members could also ensure that skilled workers stay in Germany permanently. This is because, in the current environment, many immigrants from other EU countries leave Germany again within two years.<sup>[7]</sup>

Furthermore, Germany should make full use of the potential offered by older workers. It would seem logical to link the earliest possible retirement age – and then the statutory retirement age after 2031 – to life expectancy. If, in addition, there was no longer the option of taking early retirement without any benefit reductions after 45 years of contributions, significantly fewer people would have an incentive to retire early.

Together, these steps would reduce labour shortages and bolster potential growth. They would also strengthen the financing of the pension system.

But an increased labour supply alone is not enough.

### **3.2 The factor of capital**

The second factor behind greater potential growth is capital input, or in other words, how much is being invested. Here, too, urgent action is required.

Since 2019, there has been a perceptible decline in price-adjusted gross fixed capital formation in the economy as a whole. The corporate sector has seen a comparatively strong fall-off in investment, especially investment in machinery and equipment. In addition, construction investment has declined significantly since the end of the German real estate price boom. Only government investment has increased since 2019.

Less depreciation, amortisation and write-downs, fixed investment was actually negative in 2024 and 2025 for the first time since reunification. All that to say, Germany is eating into its capital stock. How can this development be explained?

In business surveys, bureaucracy is most frequently cited as a significant challenge and an obstacle to investment.<sup>[8]</sup> The costs of bureaucracy have increased. Various studies back this up.

According to the ifo Institute, for example, excessive bureaucracy is costing Germany almost €150 billion per year in lost economic output, or more than 3 % of GDP.<sup>[9]</sup> Calculations by the Institute for Employment Research show that firms have had to hire around 325,000 additional employees over the past three years simply to comply with new rules.<sup>[10]</sup> In a time when skilled workers are scarce, this is tying up staff who could be deployed productively elsewhere.

Figures from the European Investment Bank indicate that, by European standards, firms in Germany especially are suffering under rules that are too numerous and too complex.<sup>[11]</sup> The study identifies the share of firms that view corporate sector regulation and taxes as obstacles to investment. In Germany, this share increased from well below 30 % to just under 50 % between 2022 and 2025. By comparison, the share in the EU as a whole rose less sharply, from 25 % to 34 %.

Unnecessary red tape urgently needs to be cut in order for investment in Germany to bounce back. The Federal Government's reform initiatives to reduce bureaucracy and speed up government processes are a step in the right direction. Now it is crucial to commit to implementing these initiatives.

However, even large amounts of investment can only truly have an impact if labour and capital are used productively.

### 3.3 Total factor productivity

This brings me to the third factor: total factor productivity. Total factor productivity measures how efficiently factors of production are used. Its development is particularly influenced by technological progress.

In Germany, trend total factor productivity growth has recently been exceptionally weak, averaging just 0.2 % over the past five years. In the 2010s, it grew at an average of 0.5 % per year.

What is behind this decline in German productivity growth? One reason for the weak productivity growth is the large regulatory burdens I have already mentioned. Another reason could be that a major portion of spending on research and development is occurring in the German mid-tech sector.<sup>[12]</sup>

The mid-tech sector encompasses sectors with mid-level research intensity, which form a strong industrial base in Germany. It includes the automotive industry, for instance. When it comes to investment in the high-tech sector, on the other hand, Germany is clearly lagging behind.

Herein lies the problem: the high-tech sector is, for the most part, much more innovative and thus gives a greater boost to productivity. In addition to the aforementioned reduction in red tape, policymakers should look into how they can create better conditions for innovation in the high-tech sector.

The Federal Government's current plans for more research and development and better conditions for start-ups are generally to be welcomed and should be implemented swiftly. They include, for example, a one-stop shop for quick business start-ups.

At the same time, further measures are needed. Creating better financing opportunities for start-ups by deepening the European capital markets union would be one such measure.

For another, tax incentives for investing in start-ups and venture capital funds may make sense under certain circumstances. It would be important to ensure they are effective. This could be done, for example, by capping the tax benefits and granting them only if a minimum holding period is met.

To sum up, one thing can be said for sure: Germany is facing major challenges that relate to all three growth factors. Or, to put it another way, there can be no sustainable prosperity without more labour, more investment and more productivity.

That said, there are also positive developments that we should not lose sight of and which are encouraging. I would like to finish my speech by briefly touching on two of these glimmers of hope.

A first glimmer of hope is that business start-ups have trended up substantially since 2019 – albeit from a low level. In 2025, they were roughly at the level of the early to mid-2010s.

It's important to note here that many start-ups last year were in the sectors of information and communication technology (ICT) and business-related services. Firms in these sectors often have a great deal of potential for innovation.

Bundesbank analyses show that efficiency gains in the digital sectors have been a significant driver of aggregate productivity growth in Germany.<sup>[13]</sup> If these recent developments stabilise, this could support productivity growth in the medium term.

A second glimmer of hope is the use of artificial intelligence (AI). To realise the potential of AI, it is essential that firms use this technology broadly and intensively. How are things looking in Germany?

This very question is the subject of a recent study based on the Bundesbank Online Panel – Firms (BOP-F).<sup>[14]</sup> The survey shows that the use of generative AI in German enterprises has increased significantly in recent years. Both the number of users and the intensity of use have gone up.

Let me cite a few figures to support this. The share of firms that use or plan to use generative AI rose from 26 % in 2024 to an expected 56 % in 2026. At the same time, firms expect the share of working hours in which generative AI is used to increase from 7.5 % in 2024 to around 8.9 % in 2026.

Adoption is particularly widespread in the services sectors. This underscores the potential of broad application of the technology.

What gives us reason for hope is that the vast majority of firms that use generative AI expect to see noticeable productivity gains from this. Specifically, for 2025 and 2026, more than 50 % of firms using generative AI expect to see a related increase in labour productivity of at least 2 %. Around one-quarter even expect growth of 5 % or more.

While these assessments do not constitute a forecast for the aggregate economy, they are consistent with the prevailing optimism around the growth potential of generative AI in the macroeconomic literature.

## **4 Closing remarks**

Ladies and gentlemen, this brings me to the end of my speech. We can't sugarcoat it: Germany is facing considerable challenges.

To permanently safeguard our model of prosperity, reforms are needed in many areas: strengthening the potential labour force, better conditions for investment and greater support for innovation.

Nevertheless, we should continue to be optimistic about the future. Because alongside all these challenges, we also have reason to hope: for example, there are more business start-ups, more enterprises using AI, and more enterprises making more intensive use of AI.

To close, I would like to briefly address the question of what we as central banks can do. One thing is clear: Eurosystem monetary policy cannot solve Germany's structural challenges. But it can facilitate reform efforts through a stable macroeconomic environment.

The Governing Council of the ECB left key interest rates unchanged at its most recent meeting at the end of April 2026. The medium-term impact of the Iran war on the inflation rate remains hard to gauge.

The Governing Council's wait-and-see approach is a way of gaining a clearer view of developments. However, the Governing Council is aware of the increasing risks to price stability and remains very vigilant. We will do what is necessary to prevent energy-driven price rises from spreading and becoming entrenched.

And now I look forward to discussing this topic with you. Thank you very much for your attention.

## Footnotes:

1. See Deutsche Bundesbank (2025a), What's behind the sustained decline in German export market shares?, Monthly Report, July 2025.
2. See Deutsche Bundesbank (2026a), German balance of payments in 2025, supplementary information: Latest developments in German export market shares and their driving forces, Monthly Report, March.
3. See Deutsche Bundesbank (2026b), German balance of payments in 2025, supplementary information: The impact of US tariffs on German firms, Monthly Report, March.
4. Deutsche Bundesbank (2025a), Forecast for Germany: Economy gradually returns to recovery path, Monthly Report, December 2025.
5. See Gartner, H. et al. (2025), IAB-Prognose 2025/2026 – Fiskalpolitik stützt Konjunktur und Arbeitsmarkt, IAB-Kurzbericht 19.
6. See Destatis (2026), Zahl der Geburten sinkt im Jahr 2025 auf den niedrigsten Stand der Nachkriegszeit, Pressemitteilung Nr. 146.
7. See Hammer, L. and M. Hertweck (2022), EU enlargement and (temporary) migration: Effects on labour market outcomes in Germany, Deutsche Bundesbank Discussion Paper No 02/2022.
8. See Deutsche Bundesbank (2025b), Challenges Faced by Firms, Bundesbank Online Panel – Firms (BOP-F), 30 October 2025 and von Maltzan, A. and L. Zarges (2024), Der Investitionsstandort Deutschland aus Unternehmenssicht, ifo Schnelldienst 3/2024, Vol. 77.
9. See ifo Institute (2024), Bureaucracy in Germany Costs 146 Billion Euros a Year in Lost Economic Output, press release, 14 November 2024.
10. See Institute for Employment Research (2025), 325.000 Arbeitskräfte waren laut Betrieben in den letzten drei Jahren zusätzlich nötig, um die gewachsene Bürokratie zu bewältigen, Press information, 20 October 2025.
11. See EIB Investment Survey 2025.
12. See Dietrich, A. et al. (2024), Europe's Middle-Technology Trap, CESifo EconPol Forum 4, Vol. 25.
13. See Deutsche Bundesbank (2023), The impact of digitalisation on labour productivity growth, Monthly Report, March 2023.
14. See Deutsche Bundesbank (2026c), Sectoral structural change and its impact on productivity growth in the euro area, Supplementary information: Generative AI in German enterprises: adoption, costs and expected economic impact, Monthly Report, March 2023.