



**Interview with the
Portfolio Manager of**

**The Germany Fund, Inc. (GER)
and
The New Germany Fund, Inc. (GF)**

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Question: *German economic growth is expected to lag the rest of Europe this year. What is the rationale for investors to put their money in Germany?*

Answer: Although Germany is expected to grow at a slower rate than the rest of Europe in 2005, here are signs that the economic situation in Germany is stabilizing. For example, retail sales finally returned to positive territory at the end of 2004, indicating that domestic demand may pick up in 2005.

In addition, the ZEW index, which measures economic growth expectations, has recently reversed its downward trend, signaling increased optimism. Nonetheless, the overall economic picture for Germany remains mixed.

However, global growth is expected to continue at a strong pace this year and, as the world's leading exporter, Germany stands to continue benefiting from this growth. (1) With often

more than 50% of their revenues coming from overseas, German companies offer investors an effective means to reap the benefits of strong global growth.

This is evidenced by the fact that, despite modest domestic economic performance, the German markets performed well relative to other markets last year, finishing 2004 at the highs of the year.

Question: *You mentioned Germany's position as the world's leading exporter. Which sectors of the country's export-driven economy will be affected the most by continued weakness of the dollar?*

Answer: German companies lost almost no export market share in 2004 despite a 3.8% appreciation of the real effective exchange rate. While the continued appreciation of the euro in 2005 may finally begin to affect German companies, this impact will be limited due to the fact that more than 40% of German exports remain within the Eurozone.

While potential effects vary even within sectors, depending on an individual company's currency exposure, the automotive sector is likely to be the most negatively affected by continued dollar weakness. Chemicals, pharmaceuticals and industrials may also be adversely affected.

Consumer retail companies, on the other hand, are well-positioned to benefit from the weaker dollar. In particular, companies that produce goods in Asian countries with dollar-pegged currencies will benefit from reduced operating expenses.

Question: *The German government launched the latest phase of its labor-market reforms on January 1, 2005. How quickly are the reforms expected to have an impact on unemployment, which rose again in 2004?*

Answer: The goal of the German government's Hartz IV labor-market reform is to encourage unemployed citizens to re-enter the workforce. As part of the plan, unemployment and welfare benefits have been combined into a single benefit category, effectively reducing the

number of people eligible to receive benefits and thereby providing an incentive for those people to find jobs.

Changes in the criteria for who is counted as unemployed under the new program are expected to have a negative short-term effect on unemployment figures. For example, a significant number of welfare recipients who were not previously counted as unemployed will now be counted as such. Thus, unemployment figures for the early part of 2005 could increase to around 5 million, though this will not necessarily reflect a real deterioration in the labor market.

In addition, a new measure of German unemployment will be released by the Federal Statistical Office beginning in March 2005 that should conform to standards of measurement currently used in the United States.

The new statistic is expected to describe a lower level of unemployment than the current government figures reflect. In summary, 2005 will be a transition year for the German labor market in terms of both data measurement and real progress toward reducing unemployment.

While the reforms are not expected to produce a significant reduction in unemployment levels this year, they should gain traction as the year progresses.

Question: *Germany has continually exceeded the 3% of gross domestic product (GDP) budget deficit limit imposed on European Union member states as part of the Stability and Growth Pact. There are indications that member states may fail to*

rein in the budget deficit again in 2005. What are the ramifications if Germany does not rectify this situation?

Answer: In theory, a fine of not more than 0.5% of GDP per year could be levied for failure to meet this provision of the pact. However, a number of steps must occur before a fine can be imposed. First, the Commission must notify the member state that it has an excessive deficit (Germany was so notified in January 2003) and recommend corrective actions for the member state to undertake.

The Commission subsequently reviews the situation to determine whether the government has taken sufficient steps to address its deficit level. If the Commission decides that the member state has failed to take adequate corrective measures, the member state may be sanctioned in the form of a non-interest-bearing deposit. The member state has two years from that point to correct the excessive deficit.

On December 14, 2004, the Commission concluded that Germany has taken action to correct its excessive deficit by 2005, and therefore, no movement to impose sanctions has been taken at this time.

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