

How Germany and Europe can regain competitiveness, growth, and prosperity

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A balance sheet lens shows divergent economic prospects



Can Europe unleash EUR 700bn annual investments?



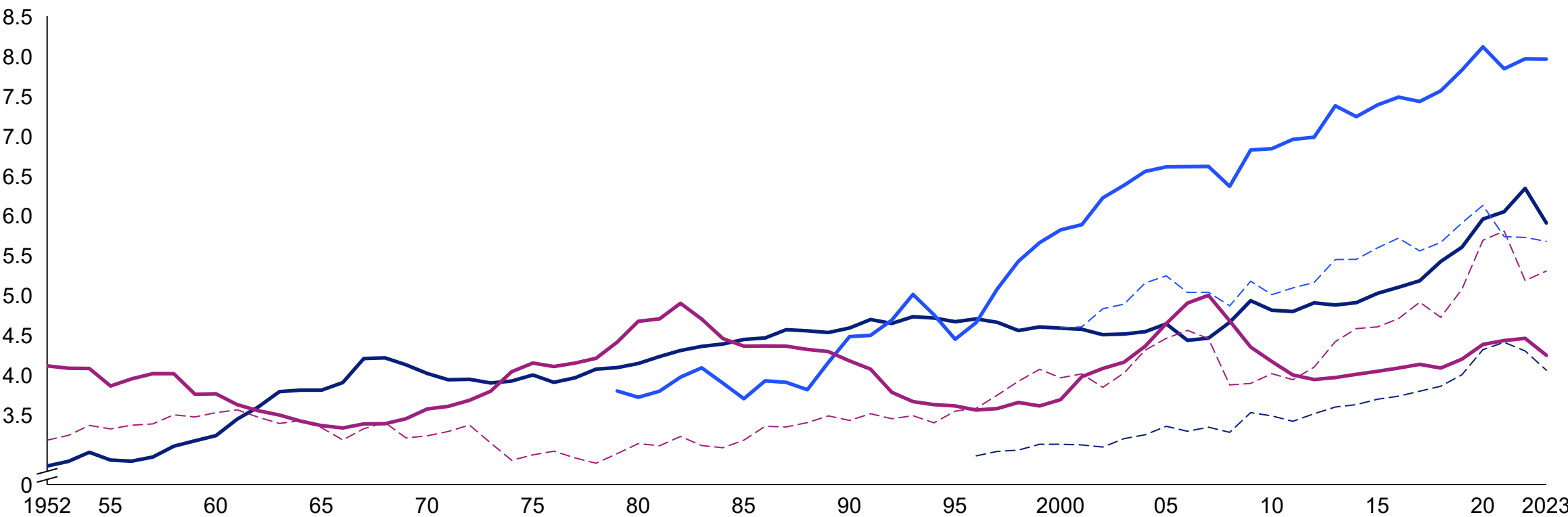
Can Germany double the value of its economy?

Have we reached peak balance sheet?

Net worth over time, selected economies

Germany Germany - Households China China - Households US US- Households

GDP multiple



Note: Data pre-2000 in China, and pre-1996 in Germany, is based off country net worth figures from the World Inequality Database. Full time series for the US is based off Federal Reserve data.

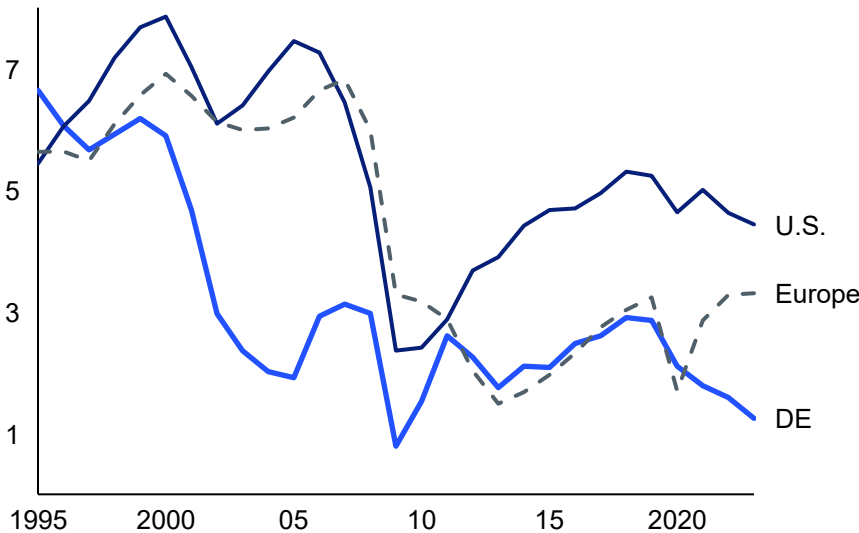
Source: MGI Analysis based on CEIC, Federal Reserve, OECD, Eurostat, Destatis, Deutsche Bundesbank, and World Inequality Database data

Are the forces that drove interest rates down and balance sheets up shifting for the long run?

Will demand for capital grow again?

Infrastructure; energy transition; intangible assets; geopolitics (defense, supply chains, industrial policy)

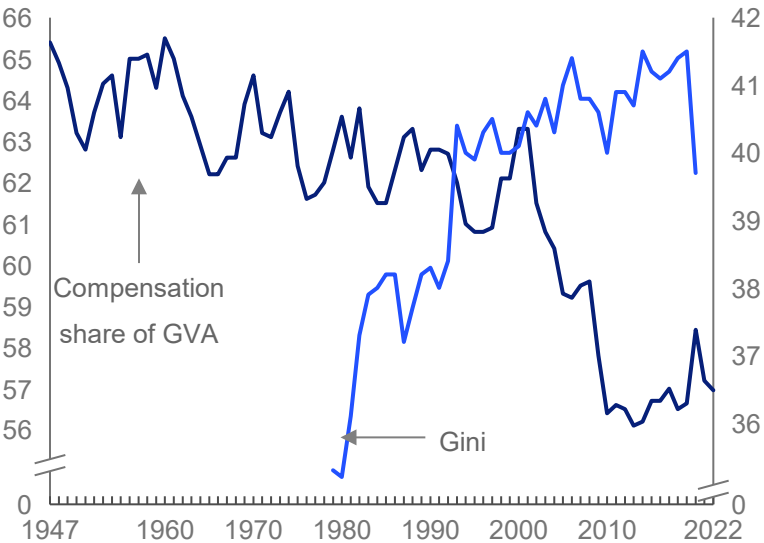
Net fixed investment as a share of GDP, %, 1990–2021



Are the forces behind the savings glut on the wane?

Inequality and declining labor share of income; aging; Asian savings glut

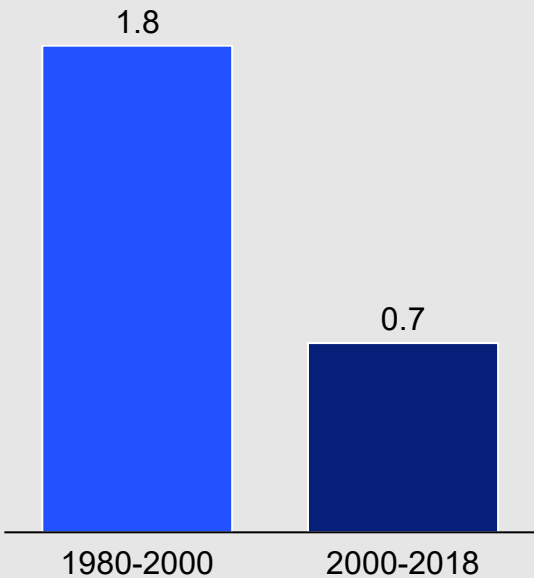
Total compensation share of gross value added, %



Can supply respond?

Headwinds from demographics and geopolitics
Upside from technology and productive investment

Average productivity growth, %, G7 countries¹



1. G7 includes Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States

A widening macro-disparity – and unusually high uncertainty



Secular stagnation with structurally low demand:
Back to low rates and large balance sheets



Higher demand and sustained inflation:
Inflating our way out



Balance sheet reset and lost decade:
Popping any bubbles



Accelerated productivity:
Supply responds to higher demand to grow out of oversize balance sheets



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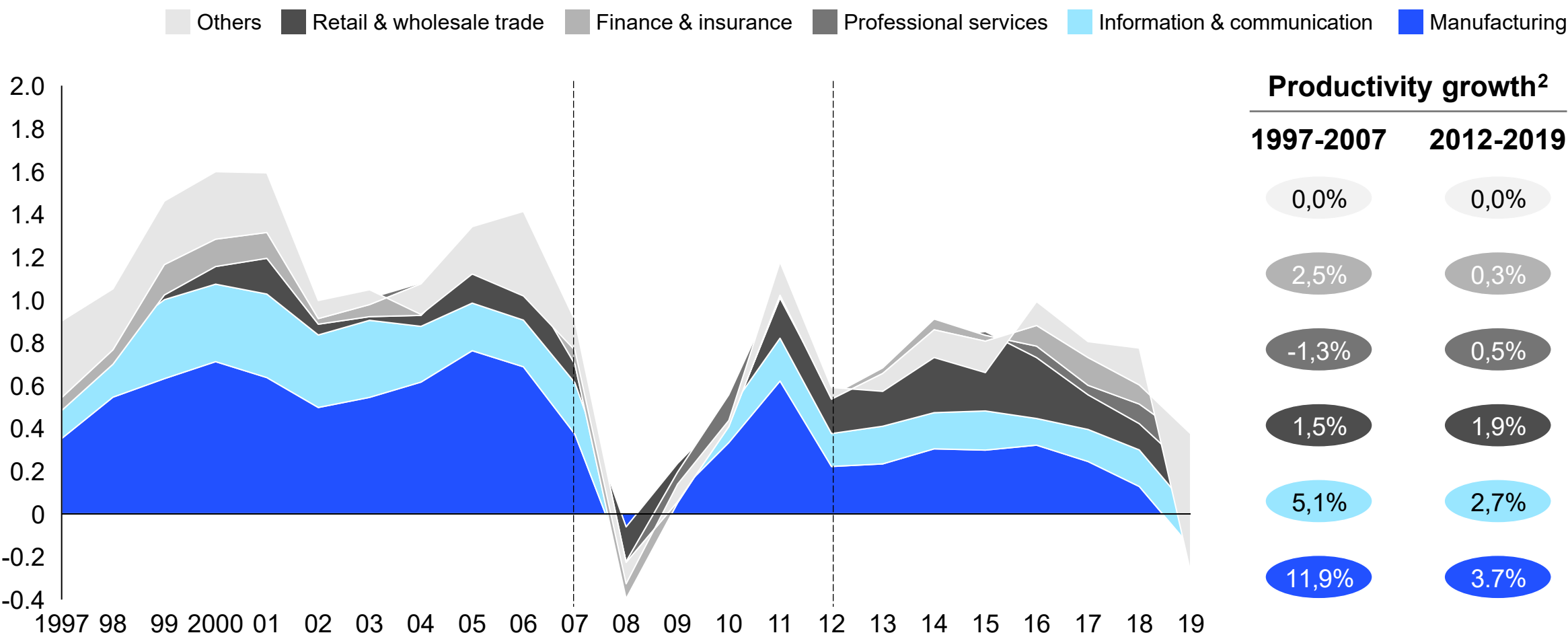
Can Europe unleash EUR 700bn annual investments?



Can Germany double the value of its economy?




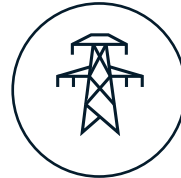
Industrial excellence has powered productivity growth in Europe

EU 5: Labour productivity growth contribution per sector, 3-year rolling average¹, all industries excl. RE, 1997-2019, %



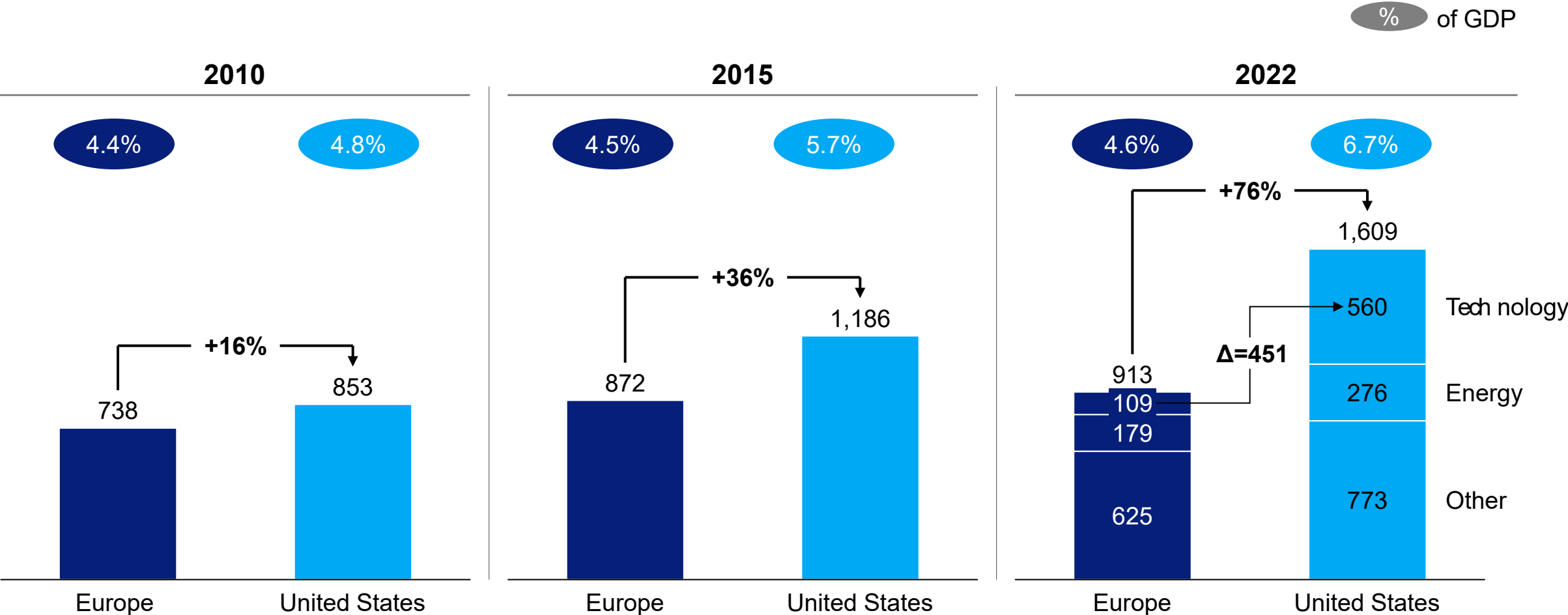
1. The value for each year is averaged with the previous and the following years;
2. CAGR
Note: Contributions are adjusted for the residual of their sum vs actual total productivity growth

A “perfect storm” is hitting Europe’s growth model

				
New era	A fragmenting world order	Technology disruption	Demographic forces	Energy shifts
Europe’s challenges	Globally interconnected value chains – and not used to projecting power	Competitive in only 4 of 16 technologies of the future	Aging rapidly	Seventy percent higher industrial electricity prices than the U.S.

Can Europe unlock 2x current corporate investment – particularly in technology and energy?

2010-2022 capital expenditure and R&D spend of European¹ and US corporates² with revenue > \$1 billion, €1 billion in 2022 prices³

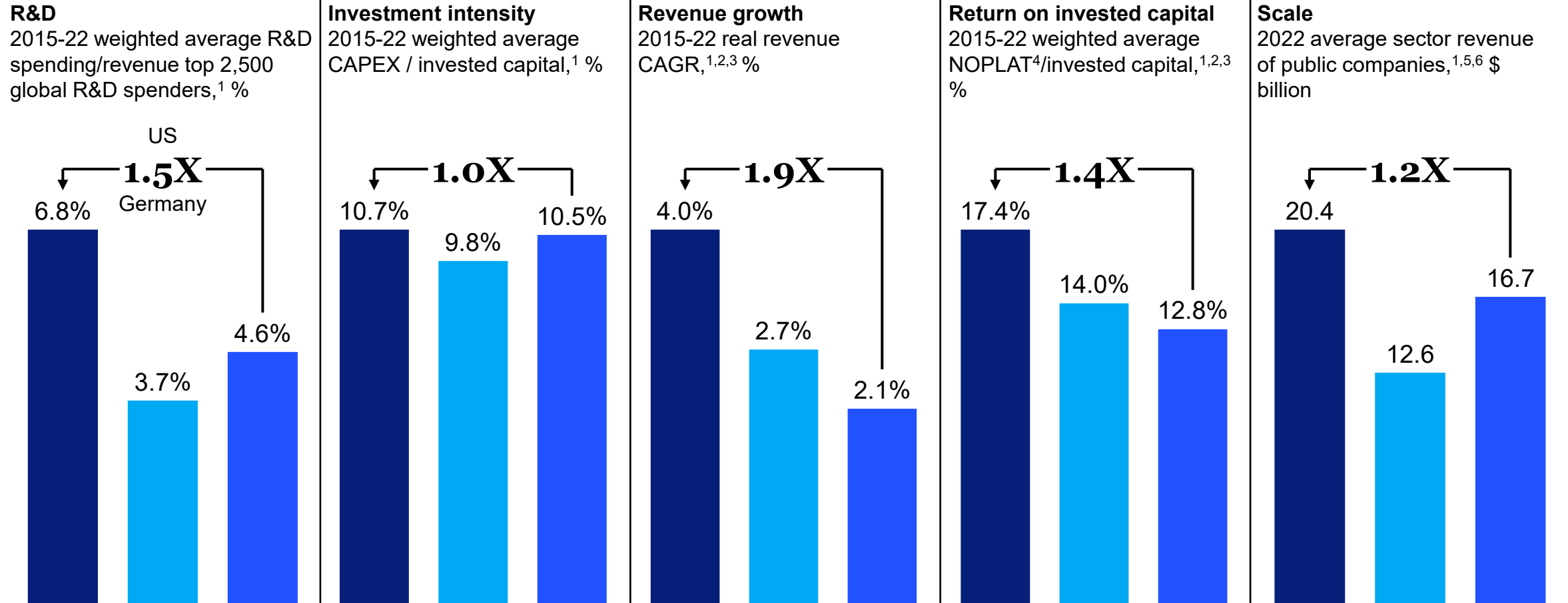


1. EU27 + United Kingdom, Switzerland and Norway (EU30); 2. Only considering public companies, excluding intangible assets; 3. Historical spending for both EU30 and US has been adjusted for inflation; for US, spending was converted from Euros (EUR) to US dollars (USD) using the FX rate for each individual year, then deflating for each year with USD inflation rates, and finally converting the deflated US spending figures back to EUR based on 2022 FX

European corporations lag US competitors on returns, growth, and innovation

Public companies with 2022 revenue of >\$1 billion

■ United States ■ Europe 30 ■ Germany



1. Excludes financial services and real estate companies

2. Inflation adjusted (2014 as base year) based on Eurozone inflation in EUR for Europe 30, German inflation in EUR for Germany, US inflation in USD

3. Excludes companies without complete revenues, net operating profit less adjusted taxes (NOPLAT), capital expenditure, or invested capital time series in 2014-22

4. Net operating profit less adjusted taxes

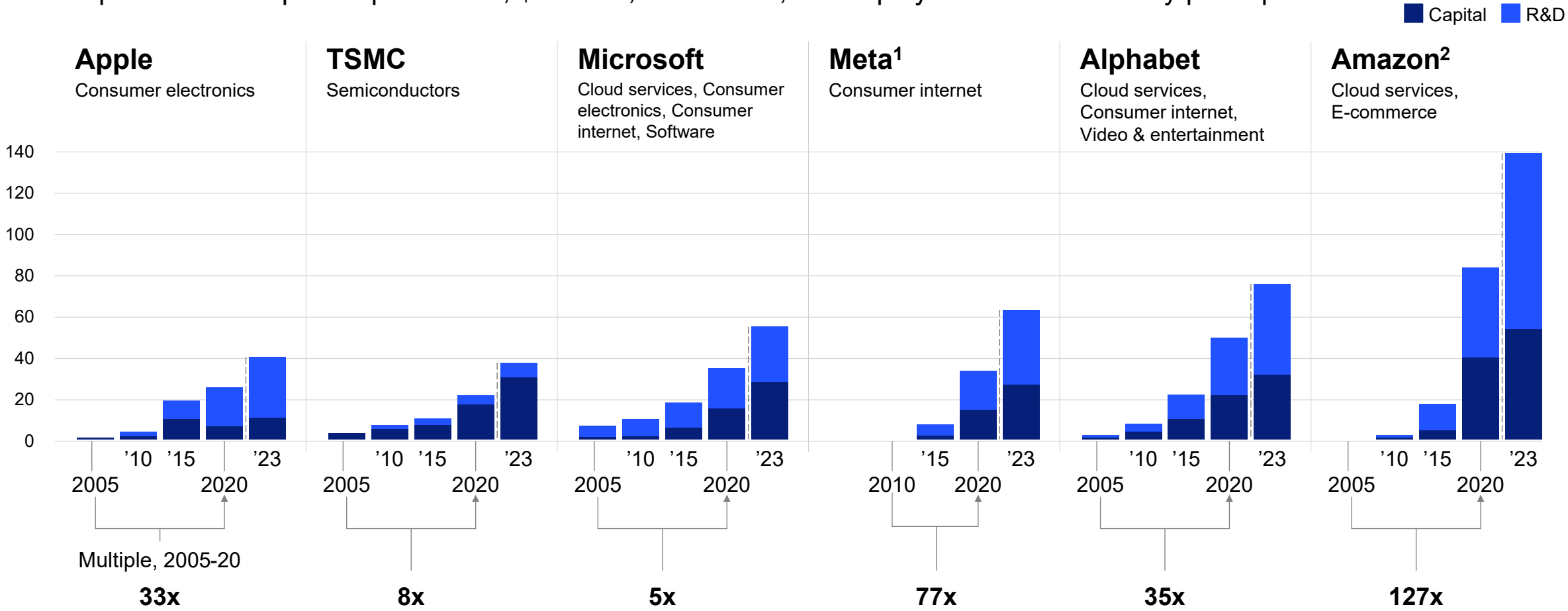
5. End of 2022 for public companies with >\$1 billion available market capitalization and revenue

6. Average based on in-sector revenue.

Source: McKinsey Corporate Performance Analytics; S&P Global; Eurostat; IMF; McKinsey Global Institute analysis

Big tech players alone spend almost as much on R&D as all of corporate Europe

R&D expenses and capital expenditures, \$ billions, 2005-2023; select players and arenas they participate in



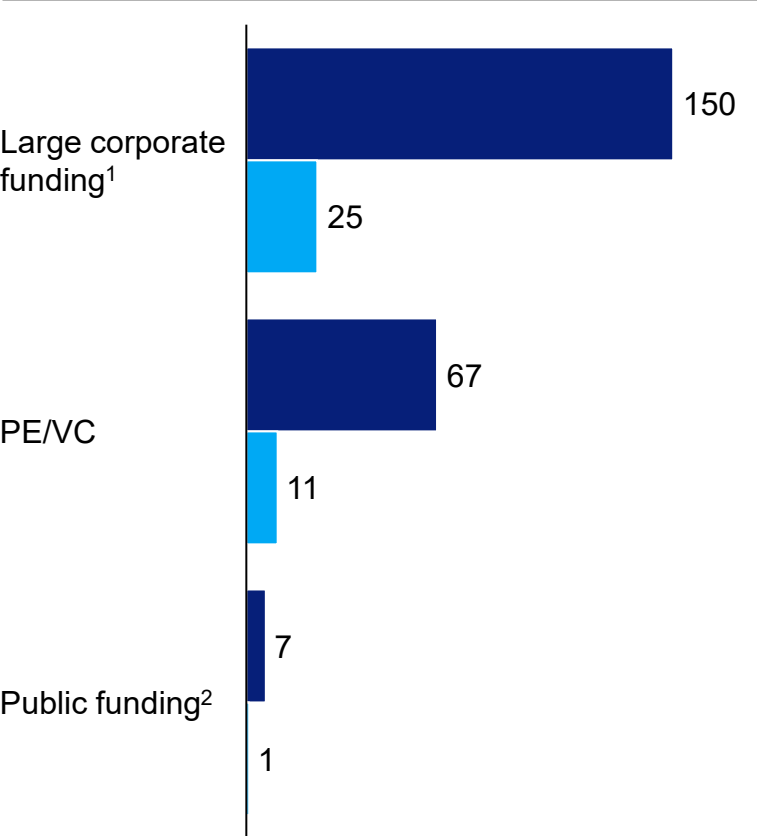
1. Numbers are indexed on 2010 instead of 2005 due to data availability

2. Amazon's R&D spend refers to an operating expense reported as 'technology and infrastructure' and may include expenses beyond what is typically reported as R&D

Example AI: How can Europe step up by an order of magnitude?

Funding

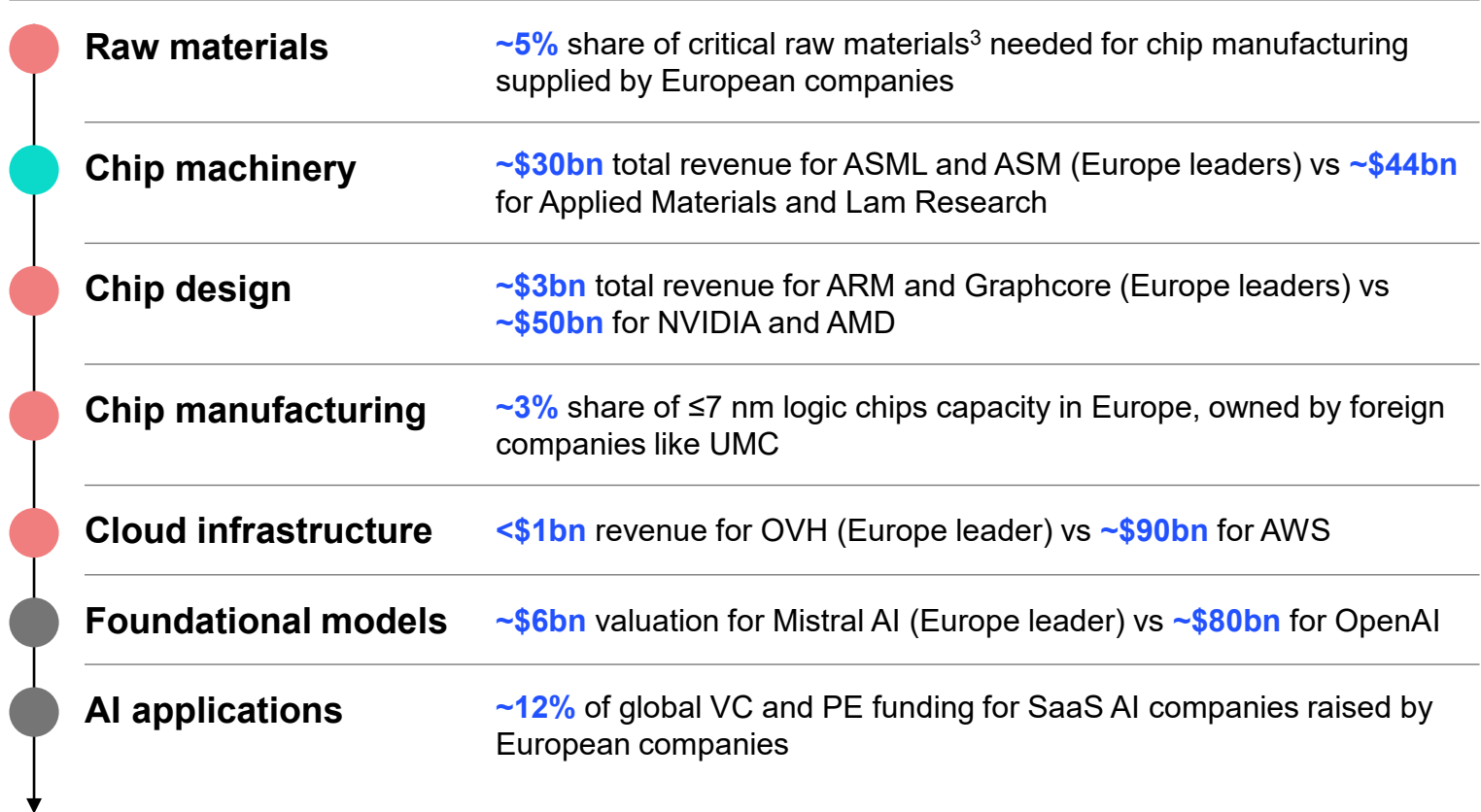
USD billion



1. Announced AI plans in 2024 by top 5 US and top 5 European tech firms
2. US federal NITRD, DoD, and contracting budgets for AI; EU rough estimates for annualized envelopes incl. NGEU 4.4bn, Digital Europe 2.1bn, Horizon Europe 0.1bn, not including member state funding programs
3. Critical and strategic according to EU definition. Critical based on Economic Importance (EI) and Supply Risk (SR) and Strategic based on importance for technologies that support the twin green and digital transition and defence and aerospace objectives

United States Europe Negligeable (<5%) Moderate (5-15%) Fair (>15%)

Market share



On technology, razor-sharp choices on where to play and how to win may be needed

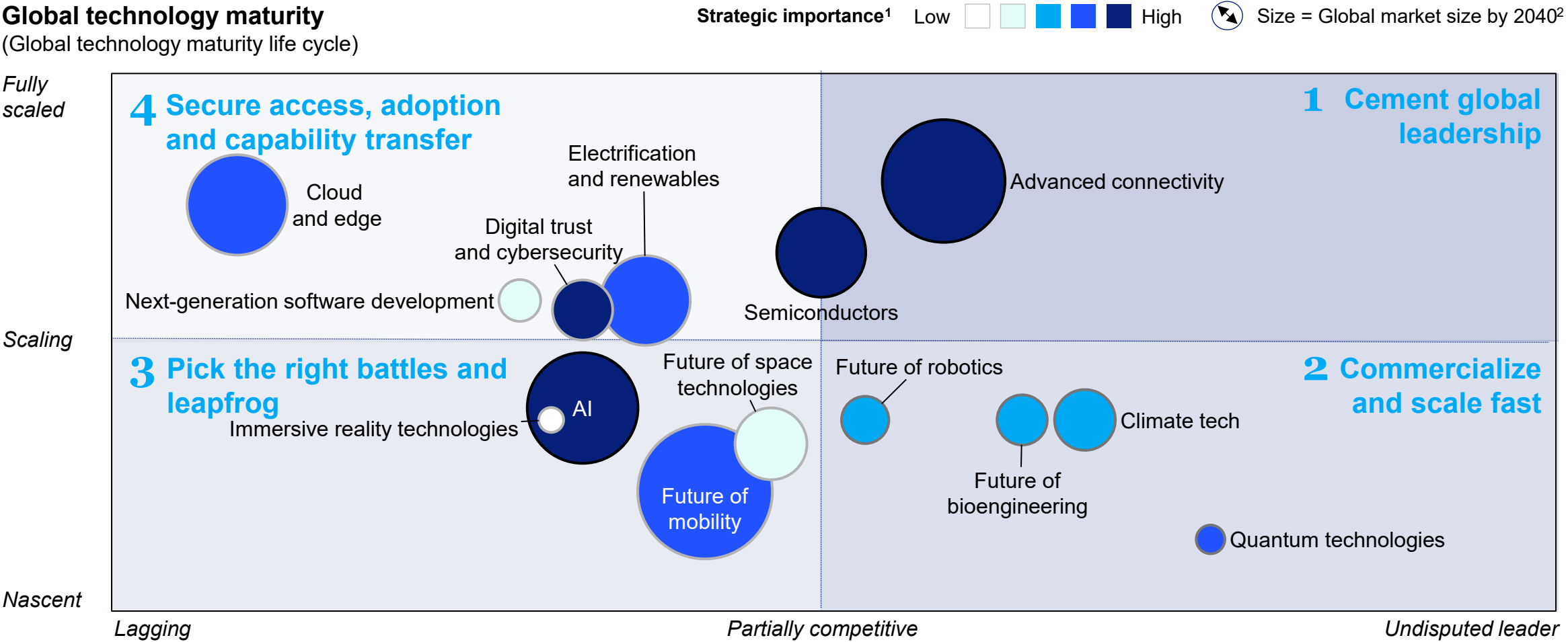
Assessment of European position in 14 significant technology domains

Global technology maturity
(Global technology maturity life cycle)

Fully scaled

Scaling

Nascent



Europe's starting position in 2024
(Based on investments, publications, patents and expert judgement)

1. Contribution to European sovereignty (based on analysis of import/export tariffs)

2. Market size by revenue based on estimates in MGI reports "The next big arenas of competition" (2024) and "Securing Europe's competitiveness" (2022)

Are business and policy leaders coalescing around ten “grands projets” that can change the investment environment?

1 Unleashing entrepreneurship: Creating a **28th regime** of uniform and radically simple business rules

2 Scaling up: A **pro-investment stance on European M&A** could drive scale and returns to accelerate investments

3 Speeding up: EU-wide, **digital, time-bound approvals** could reduce costly complexity

4 Simplifying: **Opportunity cost-based stance in regulation** could reduce the risk of falling behind

5 Funding risks: Instituting a **pension booster** could gear capital for investments towards venture capital and private equity

6 Creating markets: **Government as at-scale anchor customer** could create new markets and revenue streams

7 Building talent magnets: Developing **tech “CERNs”** could attract top tech talent in priority areas

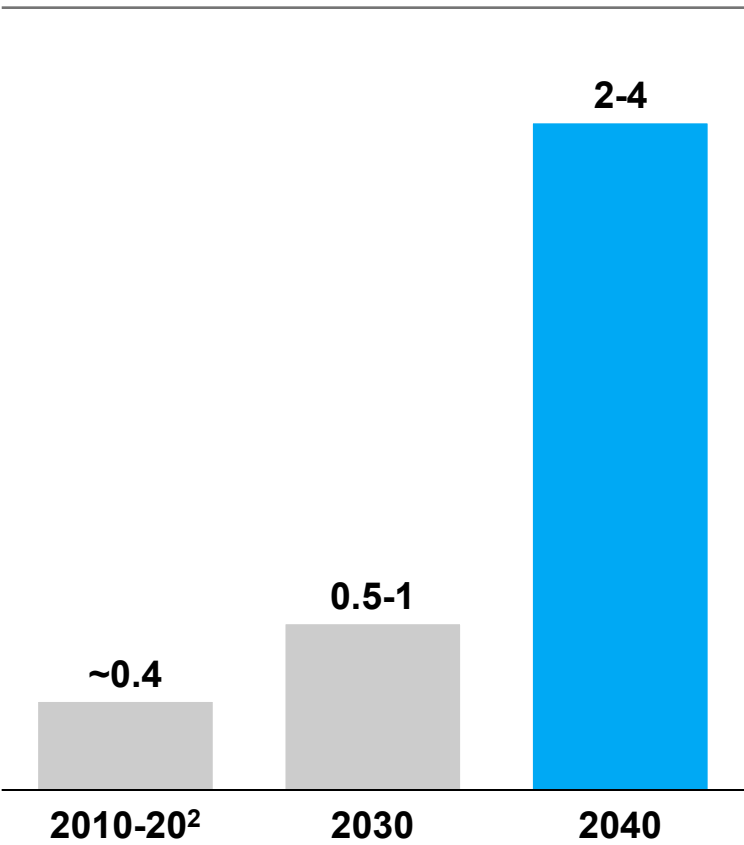
8 Securing skills: **Reskilling 1 million Europeans** could close the skills gap and solidify the tech talent baseline

9 Securing know-how: **Global capability transfer** could build out European ecosystems and capabilities

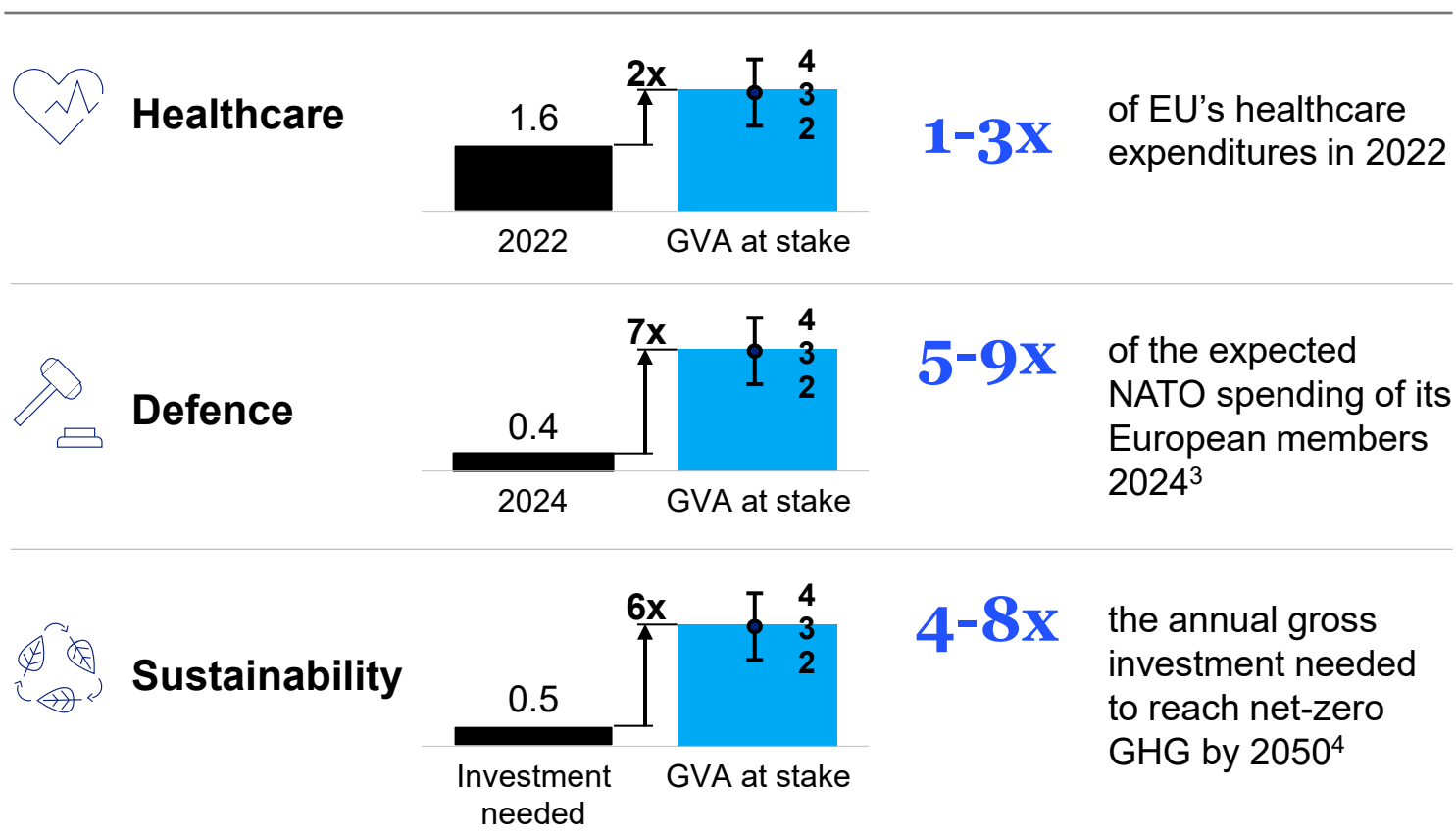
10 Driving action: Deploying a **nerve centre** and implementation governance could strengthen competitiveness

At EUR 2-4tn a year, the stakes are as high as adding the UK back to EU GDP

Annual value at stake from tech catch-up¹
Gross value-add (GVA), € trillion



GVA at stake represents a significant share of Europe's welfare spend
€ trillion



1. The corporate (gross) value-added (GVA) opportunity European firms could miss out on if Europe fails to improve on transversal technologies; 2. Annual European GDP/productivity loss due to technology lag vs the US during 2010-20 (corresponding to gap of 0.2-0.6% in productivity growth per year); 3. Based on estimations from North Atlantic Treaty Organization (NATO) from June 2024 using EUR/USD = 0.93; 4. Based on an estimate of annual gross investment needed for Europe to reach Net Zero by 2050 in the article *The net-zero transition: What it would cost, what it could bring*, by MGI (2022)

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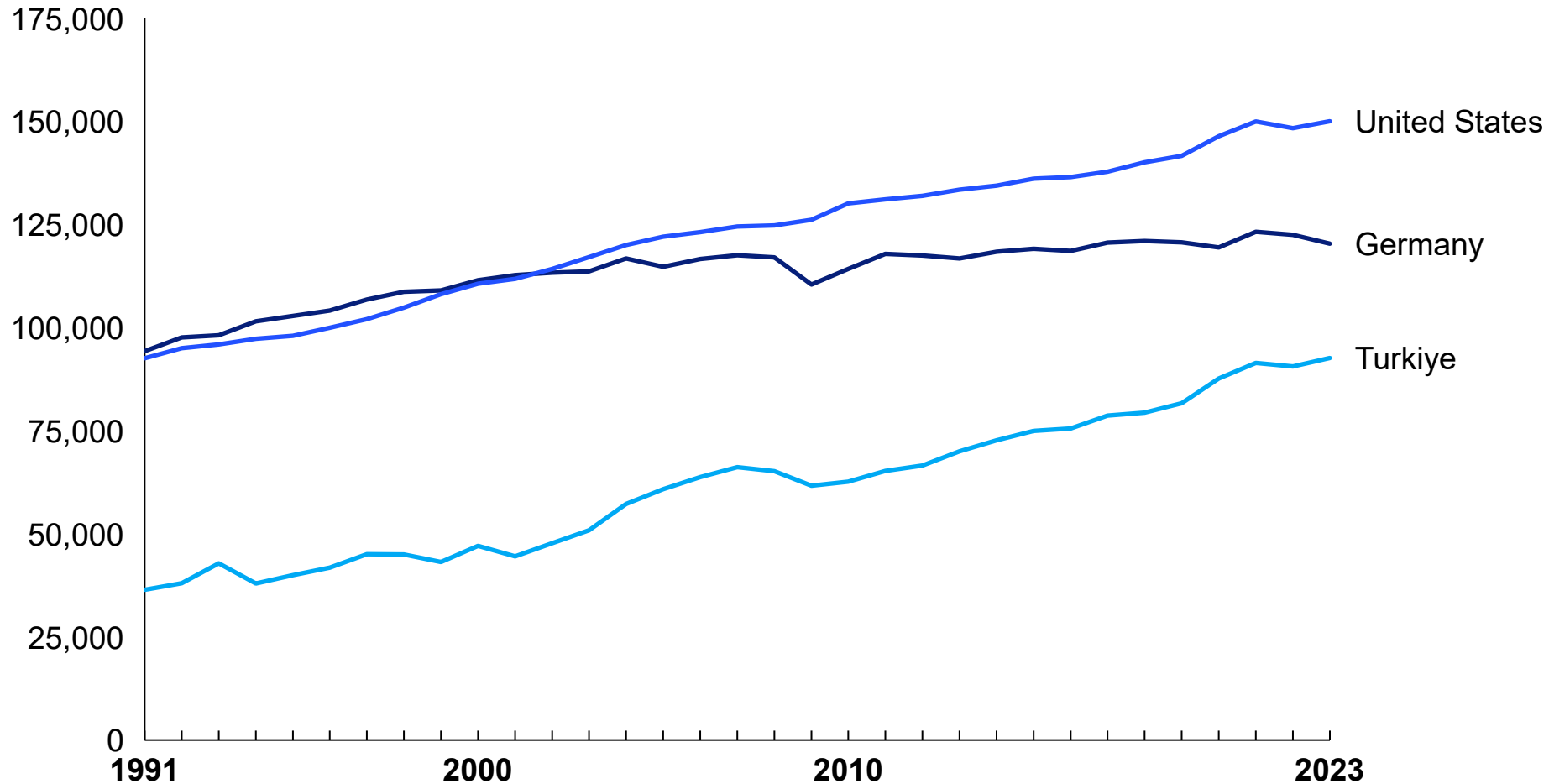
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Can Germany double the value of its economy?

How did Germany miss out on a free Ferrari for everyone?

Labor productivity – value added per worker in 2021 PPP USD



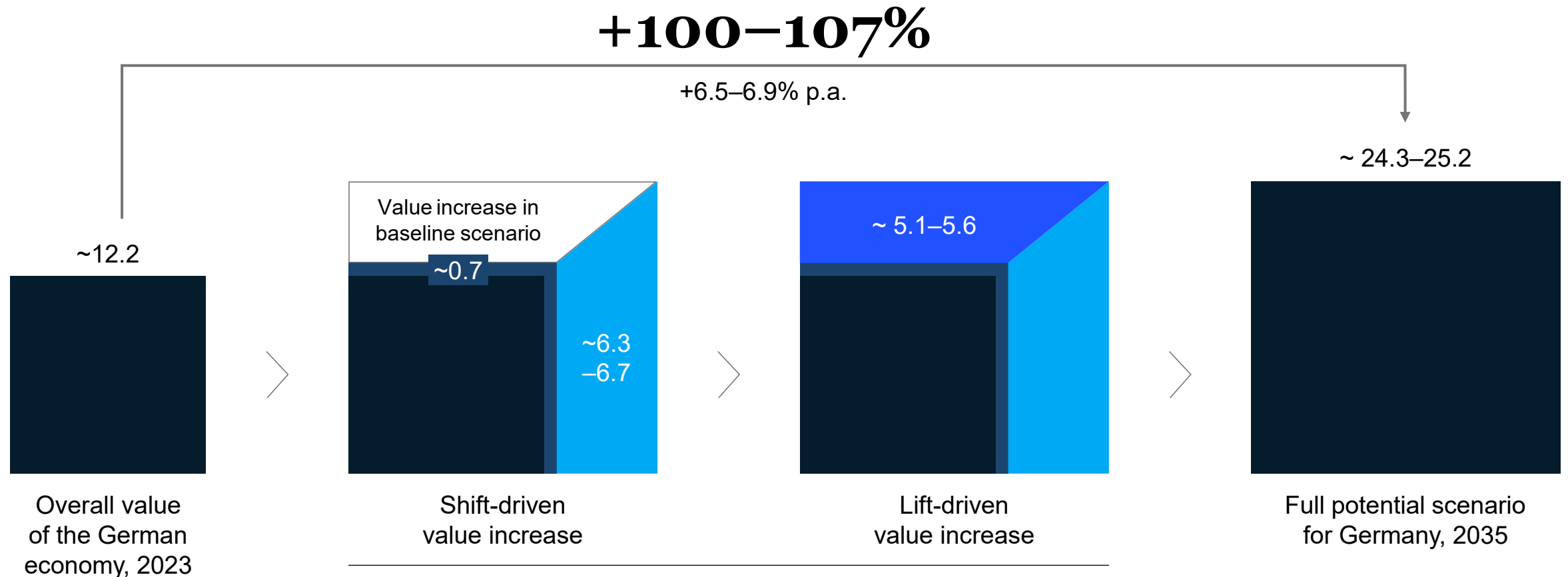
3x per capita
healthcare spend?



The cost to lease
a **Ferrari**?

Germany can double the value of its enterprises with a dual strategy of “shift” and “lift”

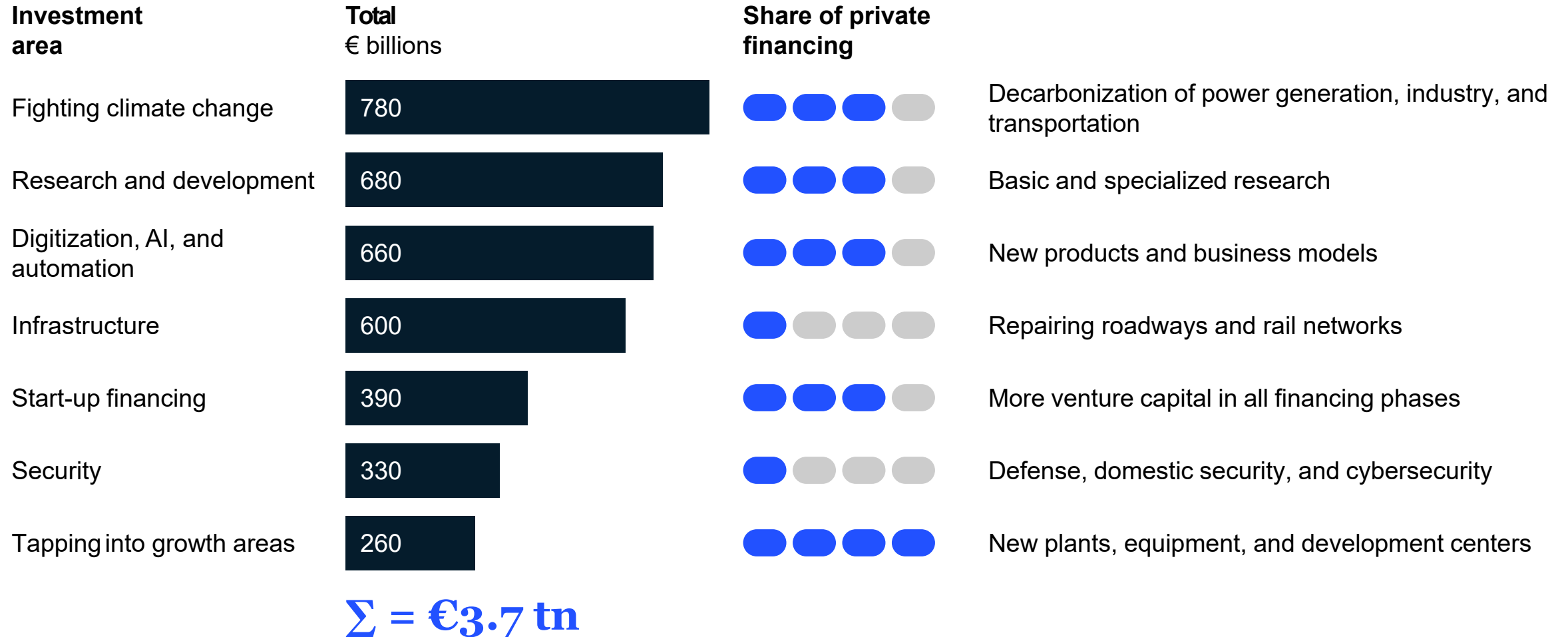
€ trillions



Shift and lift value creation potential

(Shift = new activities with greater growth potential,
Lift = efficiency gains in existing activities)

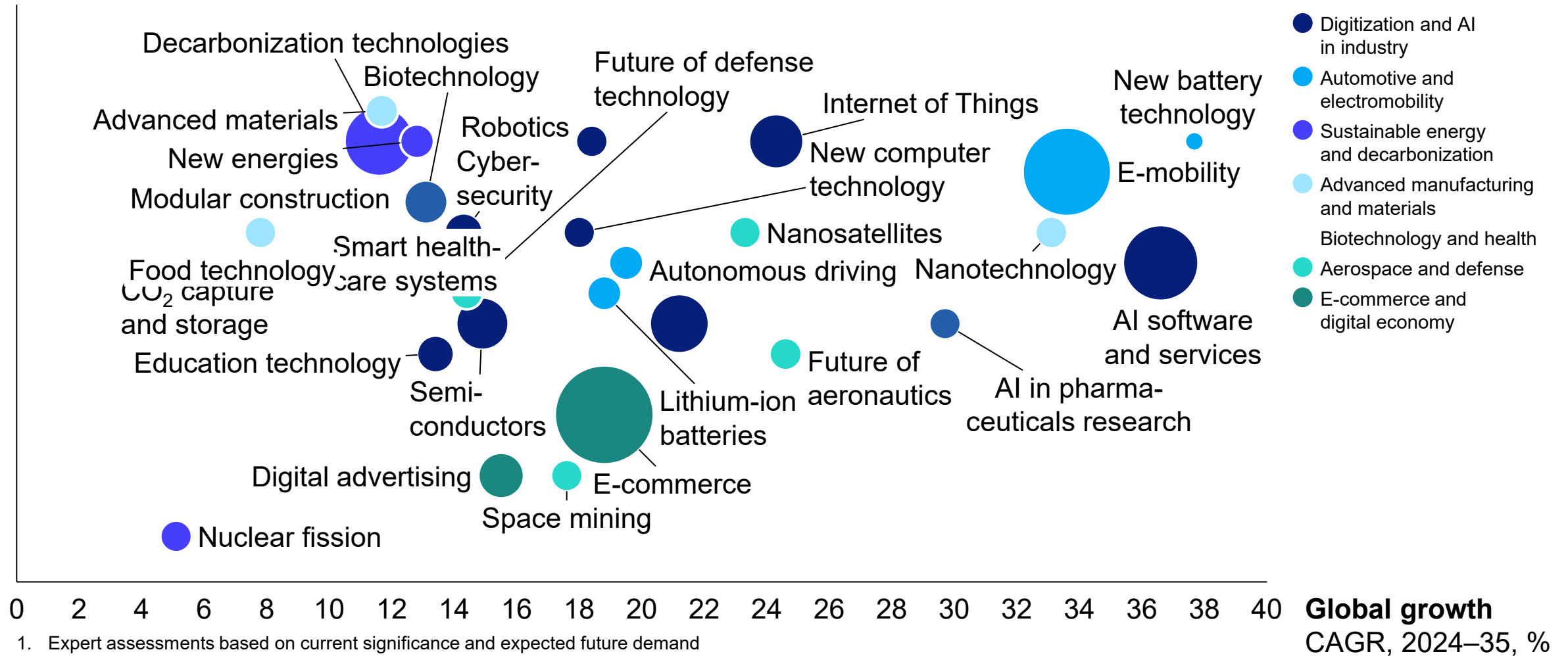
A shift in trajectory requires a step up in investment akin to the reunification



Possible future-oriented areas for Germany

Not exhaustive

Compatibility with circumstances in Germany¹



Source: Data Bridge Research; Fortune Business Insights; Grand View Research; expert assessments

Prerequisites for more investment in Germany

Which factors would increase your company's investments in Germany most and/or contribute to expanding your presence in Germany?

1	Talent and labor rules	Increased “flexicurity” and simplified labor market regulations
2	Macro-environment	Strong and stable demand outlook (e.g., based on fiscal incentives)
3	Energy	Natural gas and electricity prices in line with those in the US and China (around half of current prices)
4	Integrated EU single market	A 28th regime of the EU with uniform and corporate-friendly labor, tax, and product regulations
5	Innovation	A comprehensive EU budget of around €100 bn for “pre-commercial innovation procurement”
6	Industrial policy	Support comparable to the Inflation Reduction Act in the US
7	Trade and supply chains	Long-term access to key materials
8	Competition policy	Simplified consolidation processes
9	Capital	Capital markets union along with deepening of the private equity and venture capital markets

Main takeaways

- Elevated balance sheets are harbinger of economic uncertainty and divergence
- Europe's and Germany's growth models are hit by a perfect storm of geopolitics, energy shocks, and technology disruption
- A step-change in the environment for investment, innovation, and productivity will be required



Corporate leader implications

1

Prepare for uncertain and divergent economic scenarios

What geographic strategies can manage risks and capture opportunities as they unfold?

2

Prepare for and help shape potential shifts in the European policy environment

What would recommendations by Draghi and others mean if implemented?

3

Don't wait – drive competitiveness for Europe and for your company

What can you do yourself and in private sector alliances to change the European landscape and drive productivity and innovation in your company?

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