NEW GERMANY FUND INC
Form N-CSR
March 10, 2006
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM N-CSR

Investment Company Act file number 811-05983

THE NEW GERMANY FUND, INC.

(Exact Name of Registrant as Specified in Charter)

343 Park Avenue, New York, NY 10154

(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, including Area Code: (212) 454-7190

Paul Schubert

345 Park Avenue

New York, NY 10154

(Name and Address of Agent for Service)

Date of fiscal year end: 12/31

Date of reporting period: 12/31/05

ITEM 1. REPORT TO STOCKHOLDERS

SUMMARY OF GENERAL INFORMATION

THE FUND

The New Germany Fund, Inc. is a non-diversified, actively-managed Closed-End Fund listed on the New York Stock Exchange with the symbol GF . The Fund seeks long-term capital appreciation primarily through investment in middle-market German equities. It is managed and advised by wholly-owned subsidiaries of the Deutsche Bank Group.

SHAREHOLDER INFORMATION

Prices for the Fund s shares are published daily in the New York Stock Exchange Composite Transactions section of newspapers. Net asset value and market price information are published each Monday in *The Wall Street Journal* and *The New York Times*, and each Saturday in *Barron s* and other newspapers in a table called Closed End Funds . Daily information on the Fund s net asset value is available from NASDAQ (symbol XGFNX). It is also available by calling: 1-800-GERMANY (in the U.S.) or 617-443-6918 (outside of the U.S.). In addition, a schedule of the Fund s largest holdings, dividend data and general shareholder information may be obtained by calling these numbers.

The foregoing information is also available on our Web site: www.newgermanyfund.com.

There are three Closed-End Funds investing in European equities managed by wholly-owned subsidiaries of the Deutsche Bank Group:

The European Equity Fund, Inc. investing primarily in equity or equity-linked securities of companies domiciled in European countries that utilize the Euro currency.
The New Germany Fund, Inc. investing primarily in the middle market German companies and up to 20% else- where in Western Europe (with no more than 10% in any single country).
The Central Europe and Russia Fund, Inc. investing pri- marily in Central European and Russian companies.

Please consult your broker for advice on any of the above or call 1-800-GERMANY (in the U.S.) or 617-443-6918 (outside of the U.S.) for shareholder reports.

These funds are not diversified and focus their investments in certain geographical regions, thereby increasing their vulnerability to developments in that region. Investing in foreign securities presents certain unique risks not associated with domestic investments, such as currency fluctuation, political and economic changes, and market risks. This may result in greater share price volatility.

[Graphic Appears Here]

The New Germany Fund, Inc.

Annual Report

December 31, 2005

20958

The New Germany

Fund, Inc.

[Graphic Appears Here]

LETTER TO THE SHAREHOLDERS

German equities posted double-digit gains in 2005, boosted by revitalized confidence in economic growth, subsiding inflation fears and increased risk appetite. Equity markets in Germany and much of the rest of the world dipped lower at the beginning of the fourth quarter on concerns of slowing growth and rising inflation, but the markets bounced in November and December to register strong gains for the year. The MidCap Market Performance Index reached its highest level since 2000, as 2005 marked the sixth consecutive year that small and mid caps outperformed large caps. In the fourth quarter of 2005, the strongest performance for small and mid cap stocks in Germany was related to takeovers and takeover speculation. In addition, some commodity-related stocks outperformed on the back of increased earnings estimates in the fourth quarter, while domestic-oriented consumer stocks underper-formed, as did stocks in the solar sector.

On the economic front, the German ZEW index, which measures economic expectations, had its largest one-month uptick in more than a decade while the Ifo Index, which measures the business climate, reached its highest level in five years. The European Central Bank raised rates for the first time in two and a half years, to 2.25%, while the US Federal Reserve raised rates twice during the fourth quarter, ending at 4.25%. The US dollar strengthened significantly against the euro in 2005. Oil prices ended the year 40% higher, while the top-performing commodity of the year, natural gas, gained 83% for the year.

For the fiscal year 2005, The New Germany Fund s total net asset value rose by 13.68% and its share price rose by 18.94%. During the same period, the fund s benchmark, the Midcap Market Performance Index, gained 14.17%.

During the fourth quarter, the fund reduced its holdings in the banks and financial services sector, in part due to a significant reduction in the fund s position in Hypo Real Estate, which graduated from the MidCap Market Performance Index to the large-cap DAX Index. The fund continues to hold a position in the company, due to our belief in its strong business model and a promising outlook. Meanwhile, the Fund initiated a position in Interhyp, which is the market leader in online real estate mortgage financing in Germany. The fund s position in Interhyp made the strongest contribution to performance in the fourth quarter. The Fund increased its overweight stance on the technology sector by initiating a position in Q-Cells, the largest non-integrated, pure cell manufacturer in the world, and increasing its position in Wincor Nixdorf.[3] As a pure-play solar cell manufacturer, Q-Cells is benefiting from the trend toward greater renewable energy adoption, while Wincor Nixdorf announced several major information technology contracts that should help the company continue its transition from a hardware to a software/services company. In the materials sector, the fund s long-term position in K+S and the underweight position in HeidelbergerCement burdened the fund s performance.

The fund purchased 689,500 of its shares in the open market during 2005. The fund s discount to net asset value averaged 13.13% for the year ending December 31, 2005, compared with 17.38% for the previous fiscal year.

The sources, opinions and forecasts expressed are as of January, 2006. There is no guarantee that the views, opinions and forecasts expressed herein will come to pass. This information is subject to change at any time based on market and other conditions and should not be construed as a recommendation for any specific security. Past performance does not guarantee future results.

1 DAX Index is a total rate of return index of 30 selected German blue chip stocks traded on the Frankfurt Stock Exchange.

2 The Midcap Market Performance Index is a total return index that is composed of various MDAX and TecDax issues, reflecting the performance of mid-caps across all sectors of the Prime Segment.

Index returns assume reinvested dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.

3 Overweight means the fund holds a higher weighting in a given sector or security than the benchmark. Underweight means the fund holds a lower weighting.

Sincerely,

/s/Christian Strenger	/s/Vincent J. Esposito
Christian Strenger	Vincent J. Esposito

Chairman President and Chief Executive Officer

For additional information about the Fund including performance, dividends, presentations, press releases, daily NAV and shareholder reports, please visit www.newgermanyfund.com

FUND HISTORY AS OF DECEMBER 31, 2005

Performance is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment returns and principal value fluctuate with changing market conditions so that, when sold, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit www.newgermanyfund.com for the Fund s most recent performance.

TOTAL RETURNS:

	For the years ended December 31,					
	2005	**2004**	**2003**	**2002**	**2001**	**2000**
Net Asset Value[(a)]	13.68 %	24.44 %	93.07 %	(39.60) %	(35.68) %	(11.46) %
Market Value[(a)]	18.94 %	30.50 %	102.42 %	(39.52) %	(33.86) %	(14.35) %
Benchmark	14.17 %[1]	23.46 %[1]	78.56 %[2]	(37.58) %[3]	(33.46) %[4]	(16.13) %[4]

(a) Total return based on net asset value reflects changes in the Fund s net asset value during each period. Total return based on market value reflects changes in market value. Each figure includes reinvestments of dividend and capital gain distributions, if any. These figures will differ depending upon the level of any discount from or premium to net asset value at which the Fund s shares trade during the period.

(1) Represents the Midcap Market Performance Index.***

(2) Represents an arithmetic composite consisting of 75% MDAX*/25% NEMAX 50** from 1/1/03 3/31/03 and 100% Midcap Market Performance Index from 4/1/03 12/31/03.

(3) Represents 60% MDAX/40% NEMAX 50 for 1/1/02 8/31/02 and 75% MDAX/25% NEMAX 50 for 9/1/02 12/31/02.

(4) Represents 60% MDAX/40% NEMAX 50.

* MDAX is a total rate of return index of 50 mid-cap issues that rank below the DAX. DAX is the total rate of return index of 30 selected German blue chips stocks traded on the Frankfurt stock exchange.

** NEMAX 50 is comprised of the 50 largest technology issues from the Prime Segment that are ranked below the DAX.

*** Midcap Market Performance Index is a total return index that is composed of various MDAX and TecDAX**** issues, reflecting the performance of the mid-caps across all sectors of the Prime Segment.

**** TecDax is a total return index that tracks the 30 largest and most liquid issues from the various technology sectors of the Prime Segment beneath the DAX.

Index returns assume reinvested dividends and, unlike Fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.

Investments in funds involve risk including the loss of principal.

This Fund is not diversified and primarily focuses its investments in Germany, thereby increasing its vulnerability to developments in that country. Investing in foreign securities presents certain unique risks not associated with domestic investments, such as currency fluctuation and political and economic changes and market risks. This may result in greater share price volatility. Shares of closed-end funds frequently trade at a discount to net asset value. The price of the Fund s shares is determined by a number of factors, several of which are beyond the control of the Fund. Therefore, the Fund cannot predict whether its shares will trade at, below or above net asset value. Closed-end funds, unlike open-end funds, are not continuously offered. There is a one-time public offering, and once issued, shares of closed-end funds are sold in the open market through a stock exchange. The Fund has elected to not be subject to the statutory calculation, notification and publication requirements of the German Investment Tax Act (Investmentsteuergesetz). As a result German investors in the Fund may be subject to less favorable lump-sum taxation under German law.

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FUND HISTORY AS OF DECEMBER 31, 2005 (continued)

STATISTICS:				
Net Assets				$ 281,825,046
Shares Outstanding				24,960,198
NAV Per Share				$ 11.29
DIVIDEND AND CAPITAL GAIN DISTRIBUTIONS:				
Record Date	**Payable Date**	**Ordinary Income**	**LT Capital Gains**	**Total**
12/22/05	12/30/05	$ 0.410	$	$ 0.410
05/19/05	05/27/05	$ 0.140	$	$ 0.140
12/22/04	12/31/04	$ 0.230	$	$ 0.230
05/06/04	05/14/04	$ 0.050	$	$ 0.050
12/22/03	12/31/03	$ 0.022	$	$ 0.022
07/24/03	07/30/03	$ 0.003	$	$ 0.003
11/20/00	11/29/00	$ 0.010	$ 1.30	$ 1.310
09/01/00	09/15/00	$ 0.070	$ 0.35	$ 0.420
OTHER INFORMATION:				
NYSE Ticker Symbol				GF
NASDAQ Symbol				XGFNX
Dividend Reinvestment Plan				Yes
Voluntary Cash Purchase Program				Yes
Annual Expense Ratio (12/31/05)*				1.64 %

* Represents expense ratio before custody credits. Please see Financial Highlights section of this report.

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PORTFOLIO BY MARKET SECTOR AS OF DECEMBER 31, 2005 (As % of Portfolio s Market Value*)

ORIGINAL DOCUMENT CONTAINS BAR CHART HERE

BAR CHART DATA

Materials (7.7%)
Information Technology (12.6%)
Consumer Discretionary (8.6%)
Consumer Staples (1.5%)
Financials (15.2%)
Energy (0.5%)
Telecommunication Services (2.0%)
Industrials (31.5%)
Health Care (20.4%)

10 LARGEST EQUITY HOLDINGS AS OF DECEMBER 31, 2005 (As a % of Portfolio s Market Value*)

1 .	European Aeronautic Defense	8.6	%
2 .	Merck KGaA	4.8	%
3 .	Rheinmetall	4.3	%
4 .	K + S	4.3	%
5 .	Fresenius	3.6	%
6 .	United Internet	3.6	%
7 .	Depfa Bank Plc	3.5	%
8 .	Puma	3.4	%
9 .	Celesio	3.3	%
10 .	Stada Arzneimittel	2.9	%

* Percentage (%) of market value refers to all securities in the portfolio, except cash and equivalents. Portfolio by Market Sector and 10 Largest Equity Holdings are subject to change.

Following the Fund s fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC s Web site at www.sec.gov, and it also may be reviewed and copied at the SEC s Public Reference Room in Washington, D.C. Information on the operation of the SEC s Public Reference Room may be obtained by calling (800) SEC-0330.

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INTERVIEW WITH THE CHIEF INVESTMENT OFFICER

Question: **How has the outlook for the German economy and stock market changed now that Angela Merkel has been sworn in as the new chancellor of Germany? What are the priorities of the new government and what will Merkel be able to accomplish in the context of the grand coalition?**

Answer: Although the grand coalition between Ms. Merkel s Christian Democratic Union party and the Social Democratic party could be an uneasy alliance, the coalition government has developed a joint agenda, which places emphasis on measures to improve the country s fiscal health, such as the 3% VAT increase to take place on January 1, 2007 proposed to Parliament for approval. In addition, Merkel has highlighted lower unemployment as a top priority, though she has been hesitant to set a specific goal. She has taken a cautious approach in setting other targets as well, perhaps hoping that this will increase the chance of positive surprises. Despite conservative expectations as to how much the new government will be able to achieve, business and consumer confidence have picked up in Germany since Merkel took office, and economists expect gross domestic product growth to improve in 2006. As the financial performance of multinational companies becomes increasingly independent of local economies or politics, we remain optimistic that the business environment for German companies will continue to benefit from the strong export market and corporate restructuring efforts. We believe that any improvement in the domestic macroeconomic environment has not been priced in and will further enhance the performance of German equities.

Question: **The soccer World Cup takes place in Germany this summer. What is the expected impact on the German economy and German business?**

Answer: During the last World Cup tournament, in Asia in 2002, an average of more than 300 million viewers tuned in for each game of the monthlong tournament, and 1.1 billion viewers watched the final match. Both the government and corporate sectors in Germany have ambitious plans to capitalize on the spotlight that the tournament will bring to the 12 German cities that are hosting games. In preparation for the event, scheduled for June 2006, 4 billion euros is reportedly being spent on infrastructure and transportation. In addition, the government is spending 30 million euros on a soccer-inspired cultural program leading up to the tournament, while the business community is staging a 20 million

euro public relations campaign to showcase its products. In addition, businesses are expected to open longer hours during the tournament to encourage shoppers. While it is difficult to predict what the exact economic impact will be, many analysts are factoring the World Cup into their earnings estimates for those German companies that are expected to have high visibility through advertising at the tournament.

Question: **The first steps of a pension reform program were implemented in 2005. Why is this reform so important, and what are the implications for the German market?**

Answer: Germany, like many other countries, is expected to undergo a significant demographic shift over the next several decades that will drastically alter what is known as its dependency ratio (defined as the percentage of the population that is over 60 years old compared with the population that is between 15 and 59 years old). It is expected that there will eventually be more people over the retirement age than of working age in Germany, which has significant implications for the German pension system. In short, Germans will need to supplement their public pensions with private savings. To help address this issue, the German government has created a new tax-deferred retirement savings vehicle to encourage its citizens to save for retirement. Beginning in 2005, Germans are eligible to deduct up to 12,000 euros in contributions. Over the next 20 years, the tax incentives will increase, creating increasing demand for private retirement savings products. As a result, the market for such products is expected to undergo sustained structural growth as Germans increasingly invest their personal savings in private retirement funds. The first signs of the impact of these reforms on the German financial sector should become visible in 2006 as companies begin to see increased demand for these products. In fact, in the year since the government introduced the new tax incentives, financial intermediaries have been adjusting their business models and hiring and training additional advisors in order to better service this growing market. Currently, companies that service wealthier clients are expected to be the primary beneficiaries, but as the impact of these reforms becomes more visible, the sector is expected to continue to evolve. Sandra M. Schaufler, Chief Investment Officer of the New Germany Fund, Inc.

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REPORT FROM THE INVESTMENT ADVISER AND MANAGER

The New Germany Fund - Economic Outlook

The remarkable resilience of macroeconomic data from the major world economies, particularly the United States, as well as companies reporting earnings above expectations helped sustain equity markets throughout 2005. We see this as confirmation of our view that the global economy is in good shape, with moderate economic growth overall and limited inflationary threats. We believe the global macroeconomic environment is favourable for German equities.

Consumer confidence indicators surprised on the upside at the end of 2005, in part due to a moderate decline in unemployment. Nonetheless, private consumption is expected to remain sluggish in 2006, given that real wage growth remains modest. The 3% VAT hike scheduled to go into effect in January 2007 may provide an artificial boost to consumption in 2006 as purchases are brought forward to avoid the increased tax rate. German exports have grown 25% over the past five years and should continue to drive German growth in 2006. Investment in machinery and equipment improved in 2005 and may pick up further as increased confidence convinces cash-rich companies to invest. This is further supported by data showing that German manufacturing orders have soared due to strong external demand.

As 2005 came to a close, inflation registered at 2.1%. In 2006, inflation is likely to stay above the European Central Bank s (ECB) 2% target due to the impact of higher energy prices, though the core rate should remain contained. At its first meeting of the year, the ECB kept interest rates unchanged at 2.25%. We believe that the ECB is likely to raise rates by another 0.50% in the first half of 2006, with the next move likely to be a 0.25% hike in March. However, any signs of weakness in the economic indicators could cause the ECB to refrain from further rate hikes. A stabilizing interest rate differential with the United States should be supportive of the euro.

Special Considerations

The observations in this letter reflect our own opinions as of January, 2006 and are based on our own analysis, and others may have different opinions. Events may not transpire as we or they currently expect. Also, while economic events can influence broad market trends, political, monetary and other factors are also relevant to stock performance. In any event, investment results will depend on our success in identifying individual stocks, which are influenced by many factors beyond general economic matters. We cannot predict investment results or whether they will be successful.

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DIRECTORS OF THE FUND

Name, Address and Age*	Principal Occupation(s) During Past Five Years	Other Directorships Held by Director
John Bult, 69(1)(2) Class II	Chairman, PaineWebber International (asset management)	Director, The European Equity Fund, Inc. (since 1986) and The Central Europe and Russia Fund, Inc. (since