Federal Ministry
of Finance

Fiscal and Economic Policy

German Stability Programme

2011 Update

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Contents

Tables

Introduction

In accordance with the provisions of the Stability and Growth Pact, the Member States which have adopted the euro are obliged to submit annually updated stability programmes to the Economic and Financial Affairs Council (ECOFIN).

This update of the German Stability Programme was approved by the Federal Cabinet on 13 April 2011. Its format and contents follow the Guidelines on the format and content of Stability and Convergence Programmes (Code of Conduct). The Federal Government submits each update of the German Stability Programme and the corresponding Council Opinion on the updated German Stability Programme to the competent committees of experts of the German Bundestag, the Finance Ministers' Conference (*Finanzministerkonferenz*) and the Stability Council (*Stabilitätsrat*).

The Federal Ministry of Finance (*Bundesministerium der Finanzen*) publishes the updated Stability Programme along with the programmes for preceding years online at:

http://www.bundesfinanzministerium.de

All of the EU Member States' programmes, the corresponding European Commission analyses and ECOFIN recommendations are published on the European Commission website at:

http://ec.europa.eu/economy_finance/sgp/convergence/index_en.htm

1 Summary

By pursuing the line of fiscal policy presented in this Stability Programme, Germany will comply with the fiscal policy requirements at national and European level. Alongside the institutional reforms that are being taken (such as the sharpening of the Stability and Growth Pact (SGP) and the adoption of the Euro Plus Pact), Germany is thus making a major contribution to the functioning of European economic and monetary union through its national fiscal policy as well.

Having posted budgetary surpluses in 2007 and 2008, the crisis meant Germany recorded a general-government deficit of 3.0% of gross domestic product (GDP) in 2009. With a deficit ratio of 3.3%, the reference value of 3% of GDP was thus exceeded last year. The debt level also shot up from 73.5% to 83.2% of GDP – in particular because the newly established winding-up institutions (*Abwicklungsanstalten*) for banks were classified as belonging to the general government sector. On 2 December 2009, in line with Article 126 of the Treaty on the Functioning of the EU (TFEU), ECOFIN determined that Germany was running an excessive deficit and called on the country to reduce its deficit by 2013.

Against this background, the core economic and fiscal policy tasks are currently to phase out expansive fiscal policy measures and to maintain a course of consolidation that is sustainable and good for growth. Germany's new budget rule for the Federation and the federal states (*Länder*) set a constitutional limit on borrowing which anchors the medium-term objective (of having a structural general government deficit of -½% of GDP) and, consequently, the preventive components of the SGP, in Germany's Basic Law (*Grundgesetz*). By putting together a budget consolidation package (called the *Zukunfspaket*), the Federal Government laid the foundation in 2010 for a growth-oriented consolidation strategy that puts the budget rule into practice. Tax relief – especially for the lower and middle-income brackets – is to be implemented as soon as possible. However, this depends on sufficient fiscal latitude being acquired – while also complying with the requirements at EU level and under the budget rule.

With the shift away from the previous years' expansive fiscal policy (through the introduction of consolidation measures) and as a result of the continuation of the economic recovery, the general government deficit will this year amount to 2½% of GDP. The deficit will consequently fall below the Maastricht reference value two years earlier than required under excessive deficit proceedings. With sustained consolidation, this positive trend will continue gradually over the coming years, which means that the budget will be close to balance and the medium-term objective achieved at the end of the period covered by the Stability Programme. This year also marks the reversal of the debt ratio trend. By the end of the projection horizon in 2015, the debt ratio is expected to fall to around 75½%.

2 German fiscal policy in the European context

The SGP provides the basis for the fiscal surveillance of the EU Member States. The SGP was concluded to facilitate the functioning of European economic and monetary union, while observing Member States' national responsibility for public finances. However, the European debt crisis clearly demonstrated that the current SGP was unable to secure this objective. Germany therefore actively supported work to strengthen the SGP (that will lead to enhanced fiscal surveillance) and create a new procedure for monitoring excessive macroeconomic imbalances (by monitoring competitiveness). A first step was achieved through the introduction of the European Semester, which is designed to improve the efficiency of economic and fiscal policy coordination within the EU from 2011 onwards (see box below).

European Semester

The processes of budgetary coordination in line with the SGP and structural reform in line with the EU's Europe 2020 growth strategy were previously separate. The European Semester aligns the timing of these processes and combines them. This should ensure that the European dimension is incorporated from an early stage into discussions about the structure of public budgets for the coming year.

The European Semester in each case extends over the first six months of a year. In January the European Commission issues an Annual Growth Survey containing the main economic challenges facing the EU for the current year as well as recommendations for forward-looking policy measures. On this basis, ECOFIN prepares conclusions on macroeconomic and fiscal guidance. The European Council thereupon adopts horizontal economic and fiscal policy recommendations in March. Taking these recommendations into account, the Member States submit their stability and convergence programmes as well as their national reform programmes in April. At the start of June, the European Commission develops an initial draft for country-specific policy recommendations. These are then discussed by the respective Council configuration (in the case of stability and convergence programmes, this is primarily ECOFIN), modified were necessary, and endorsed by the European Council at the end of June. The Member States are to take these recommendations into account when preparing and passing their budgets.

A key focus during further stages of reform will be to enhance the binding character of the requirements under the SGP's preventive arm, especially the medium-term budgetary objective, which is intended to guarantee that public finances are sustainable in the long term. In the SGP's corrective arm, greater emphasis is to be placed on the debt level criterion in particular. Undesirable developments must be identified and halted at an earlier stage; stricter and credible threats of sanctions are indispensable in his regard. Fiscal surveillance must also be optimised through further reforms that the Member States themselves need to undertake. This includes the establishment of suitable fiscal frameworks and the production of reliable data. Structural reforms improving competitiveness are also crucial in terms of having effective prevention; for emergency situations, a robust crisis resolution mechanism that sets appropriate incentives needs to be put in place.

At the meeting of the European Council on 24/25 March 2011, the heads of state and government of the euro area as well as Bulgaria, Denmark, Latvia, Lithuania, Poland and Romania adopted the Euro Plus Pact which will achieve a new quality of economic policy coordination, with the objective of improving competitiveness. As part of the Pact, the participating Member States committed to undertake concrete actions to be achieved within 12 months. Alongside its economic policy focus, the Pact contains fiscal elements to enhance the sustainability of public finances.

The fiscal requirements under the excessive deficit procedure, European Semester and Euro Plus Pact are set out below. By pursuing the line of fiscal policy presented in this Stability Programme, Germany will fully comply with these requirements. The economic policy components of the consolidation procedure are contained in the National Reform Programme, and the measures therein with financial impact are simultaneously covered by the fiscal strategy and projection for public finances that are contained in the Stability Programme.

2.1 Excessive deficit procedure in relation to Germany

On 2 December 2009, in line with Article 126 of the TFEU, ECOFIN determined that Germany was running an excessive deficit and issued recommendations regarding the reduction of this deficit. The recommendations set 2011 as the year in which Germany was to begin consolidation, called for an annual average reduction in the structural deficit of at least 0.5% of GDP, and required the deficit to be brought below the 3% of GDP reference value by 2013.

In the Opinion on Germany's 2010 Stability Programme, ECOFIN issued a call to Germany on 26 April 2010 to implement the budgetary strategy as outlined in the programme to correct the excessive deficit by 2013, to seize any opportunity beyond the fiscal efforts, including improved economic conditions, to accelerate the reduction of the gross debt ratio back towards the 60% of GDP reference value, to ensure full implementation of the new constitutional budget rule at all levels of government, and to reverse the deviation from the pension adjustment formula in 2008 as envisaged.

On 13 July 2010 ECOFIN found that Germany had, as planned, implemented measures in 2009 to support the economy. ECOFIN shared the European Commission's view that Germany was making adequate progress towards the correction of its excessive deficit within the deadline set.

2.2 European Semester

At its meeting on 24/25 March 2011 and building on the European Commission's Annual Growth Survey and subsequent ECOFIN Conclusions, the European Council made it clear that on the fiscal policy front, further efforts to consolidate public finances in the EU were a pressing matter. Restoring confidence was identified as the EU's most urgent task in order to break the vicious cycle of unsustainable debt, disruption of financial markets and low economic growth. To achieve this, the European Council said public expenditure should be put back on a sustainable track as a prerequisite for future growth.

The European Council also called for structural deficits to be reduced by an amount above the annual adjustments of 0.5% of GDP. It was also recommended that expenditure growth in Member States that have not yet achieved their medium-term objectives should be kept below medium-term potential growth. It was said that the expenditure structure should be made more growth friendly, unjustified subsidies eliminated and the efficiency of spending increased in the process. All Member States were called on to produce their stability and convergence programmes on the basis of cautious growth and revenue forecasts.

2.3 Euro Plus Pact

By adopting the Euro Plus Pact, the euro-area Member States and the additional Member States mentioned above committed themselves to transpose the SGP's fiscal rules into their national legislation. Germany already fulfils this requirement thanks to the measures described under 4.2 below, concerning the institutional fiscal framework, especially the constitutional budget rule modelled along the lines of the preventive arm of the SGP. In addition, the long-term sustainability of public finances is to be strengthened – which includes the alignment of the pension system to the national demographic situation and the limiting of early retirement schemes. Germany fulfils the Euro Plus Pact's requirements in this area too – thanks, among other things, to the introduction of retirement at 67 and additional measures described in chapter 6.

Through the action programme of 23 March 2011 adopted as part of the Euro Plus Pact, Germany also commits itself to two fiscal policy objectives to be achieved within the next 12 months. Germany will come under the SGP's 3% reference value this year – which is two years earlier than required under the excessive deficit procedure. Net borrowing in the 2011 and 2012 federal budget will also be well below the level of deficit reduction plotted by the budget rule. The measures of the 2011 action programme are presented in detail in the National Reform Programme of 6 April 2011.

3 Macroeconomic situation and outlook in Germany to 2015

3.1 Macroeconomic situation in 2010

Following the deepest slump in the history of the Federal Republic of Germany that arose because of the global economic crisis, the Germany economy picked up strongly last year. On average for 2010, German GDP grew by 3.6% in real terms on the year. The increase in GDP was especially pronounced in the first six months of 2010. In the second half of the year, the climb in macroeconomic activity continued at a slower pace.

In addition to the clear rise in export activity, domestic growth gained momentum perceptibly in 2010. In particular, the vigorous expansion in investment and revival in private consumption make it clear that impetus from foreign trade and the improved labour market situation have now led to stronger domestic demand.

The labour market demonstrated encouraging robustness during the economic crisis and, in the upswing, it is now benefiting from the marked increase in macroeconomic activity. The temporary reduction in regular working hours at companies through rules under collective agreements and the use of short-time work (*Kurzarbeit*) noticeably cushioned the drastic economic slump's impact on the labour market. Taking the average for 2010, there was a clear drop in the number of unemployed by 179,000 to 3.24 million, while the number in work increased to a record level of 40.48 million (on average for the past year). With inflation of 1.1%, the consumer price index developed very moderately on average for 2010.

3.2 Assumptions underlying the macroeconomic forecast for 2011 and the medium-term to 2015

The Federal Government's projection is based on the following assumptions:

- Using forecasts by international organisations, the global economy is projected to post real growth of around 4% in 2011. The economic upswing will thus continue somewhat less dynamically than it did last year. Following the strong recovery in 2010 (at around +12%), global trade is likely to rise at a slower pace of around 7% in 2011. Thanks to its high level of price and non-price competitiveness, the German economy will especially benefit from the upturn in the volume of world trade, such that it will be able to defend its market shares into the medium-term as well.
- The technical assumptions for the price of crude oil and the euro's exchange rate against the US dollar correspond to the respective averages recorded during the final weeks before the forecast was drawn up in January 2011: the macroeconomic forecast assumes a price of USD94 per barrel of Brent crude oil and an exchange rate of USD1.32 to the euro. A further technical assumption is that the ECB's main refinancing operations rate will remain at the current level of 1.0% for the entire forecast period.
- The projection takes into account all of the economic and fiscal policy measures adopted prior to the completion of the Federal Government's 2011 Annual Economic Report (*Jahreswirtschaftsbericht*). For the medium-term projection period to 2015, it is assumed that the continued pursuit of the growth and employment-oriented reform policy in Germany will lead to an increase in potential growth. The German economy will almost close its negative output gap over the course of forecast period.

- Total payroll is expected to remain in line with the development of total productivity growth.

3.3 Short and medium-term outlook for the overall economy

The leading economic indictors suggest that the upturn is set to continue in Germany. In its January 2011 projection, the Federal Government expects GDP to increase this year at a real rate of 2.3%. For 2012, it is assumed GDP will rise by 1.8%. Because of a statistical carry-over from the previous year of 1.2 percentage points, 2011's growth dynamics are likely to be lower than the above-average pace of growth in 2010 when the economy recovered lost ground.

For one thing, the post-crisis pick up will slow down because the level of capacity utilisation in individual sectors of the economy has increased appreciably once more. For another, the German sales markets' decelerated pace of expansion means that the stimulus from foreign trade will be weaker in 2011 than it was a year ago (with net exports contributing +0.4 percentage points to growth, in place of +1.1 percentage points in 2010). Nevertheless, German exporters (with their specialisation in capital goods) should continue to benefit from the ongoing global upturn. The contribution to growth from domestic uses is, however, likely to be considerably higher (+1.9 percentage points) than that from net exports.

This means the growth profile in 2011 will shift further in the direction of domestic demand. While investment activity is likely to be dampened temporarily as a result of some deceleration in the global economy, a noticeable climb in real gross fixed capital formation in machinery and equipment by 8.0% is still expected overall in 2011 because firm's growing capacity utilisation will push plans to expand higher up the agenda. The upward trend in construction investment will probably flatten out this year. Private consumption will play a major role in assisting growth in 2011. At +1.6% this year, real private consumption expenditure will rise at an above average rate compared with the level of growth over the past decade (of around +0.4% annually). The clear increase in household's disposable income (up +3.4%) and a slightly reduced savings ratio are contributing to this. The anticipated ongoing rise in employment is also having a favourable impact in the process.

On an annual average for 2011, the number of employed persons will increase by roughly 320,000 to 40.8 million. This will be accompanied by a decline in registered unemployment by around 300,000 to just under 3 million. At a rate of 1.8% on average for the year, the increase in the consumer price index is projected to be higher than in 2010. This is primarily due to the strong rise in the price of crude oil and other raw materials on the world market which is clearly visible at the early stages of the production process. Overall, however, price level trends will remain within the ECB's stability target for the euro area.

Thanks to the strong growth last year, the German economy managed to reverse a substantial part of the decline in macroeconomic activity caused by the crisis. Over the medium-term projection period, GDP is still nevertheless expected to stay below potential output. According to the Federal Government's most recent medium-term projection, GDP will, on average, grow by a good 1½% in real terms each year between 2013 and 2015. At the same time, potential growth is expected to be almost 1½% p.a., and will weaken somewhat at the end of the projection period on account, among other factors, of a declining labour force potential. Overall, this means the extensive under-utilisation of the macroeconomic production capacity resulting from the 2009 slump will gradually be reduced. The negative output gap will, it is assumed, almost have closed at the end of the medium-term forecast period.

As in 2011, growth will mainly be supported by domestic demand in the medium-term forecast period as well. Export activity is projected to post average expansion in real terms of just under 4% p.a. However, strong domestic demand means that imports will increase to a similar extent, so that overall, net exports are likely to make only a low contribution to growth. Domestic uses, by way of contrast, will account for the majority of growth because of a persistently positive investment trend and buoyant private consumer demand. The number of persons in employment may reach around 41.1 million in 2015, which on an annual average since 2012, would mean a climb in the number of employed by nearly 150,000. This means there is set to be a further significant rise in household's disposable income. The price pressure in the domestic economy will remain moderate.

4 Fiscal policy in Germany

Sound public finances are a prerequisite for building confidence in a state's capacity to act and are essential in terms of having long-term favourable growth and employment conditions. The lack of confidence in the sustainability of public finances in some Member States was a major trigger for the crisis in the euro area. But this is not a one-way street – economic growth and increased employment create the best conditions for sustainable public finances. Quantitative and qualitative consolidation complement each other because the existence of public budgets that are built on sound finances is a decisive precondition for being able to place increased emphasis on future-oriented policy areas.

4.1 Fiscal situation and strategic direction

Public finances in Germany were gravely affected by the financial and economic crisis as well as government stabilisation measures. Having returned surpluses in 2007 and 2008, Germany's general government budget balance worsened in 2009 to post a deficit of 3.0% of GDP. The last update of the stability programme from January 2010 projected a general government deficit ratio for that year of 5½% of GDP. However, this forecast was undercut markedly on account, in particular, of the economy performing better than initially expected.

With a deficit ratio of 3.3% of GDP in 2010, the reference value of 3% of GDP was nevertheless exceeded and the requirements of the SGP breached as a consequence.

The GDP development shaped the development of general government revenue and expenditure (i.e. there was a denominator effect). The increase in both government revenue and expenditure was far less pronounced than GDP growth in 2010, which means the revenue ratio fell to 43.3% and the government expenditure ratio dropped to 46.6%. The debt level shot up from 73.5% in 2009 to 83.2% in 2010 – in particular because the newly established winding-up institutions for banks were classified in the government sector.

Against this background and on account of the requirements arising from the excessive deficit procedure and the European Semester, the core economic and fiscal policy tasks are currently to exit expansive fiscal policy measures and to maintain a course of consolidation that is sustainable and supports growth. By pursuing the line of fiscal policy presented in this Stability Programme, Germany will comply with the European requirements stated in chapter 2. The deficit will, as set out in the forecast in chapter 5, be brought under the 3% of GDP reference value within the year – two years earlier than required under the excessive deficit procedure. Germany is committed to pursuing a sustainable fiscal policy and stands by the medium-term objective of achieving a structural deficit of ½% of GDP.

4.2 Institutional framework conditions

Germany's budget rule for the Federation and the *Länder* set a constitutional limit on borrowing which anchors the medium-term objective and, consequently, the preventive components of the SGP, in Germany's Basic Law. Social security funds and local authorities are also subject to narrow borrowing limits, which means that the fiscal rules in Germany will ensure compliance with the medium-term objective in future too.

In light of the grave impact of the financial and economic crisis on the budgetary situation, transitional provisions lasting up to and including 2015 (in the case of the Federation) and 2019 (in the case of the *Länder*) were agreed when the budget rule was introduced. The Federation is required to reduce the 2010 structural deficit in equal steps to a maximum, applicable from 2016 onwards, of 0.35% of GDP. Under the transitional arrangement, the Federation is required to reduce its structural deficit annually by around 0.3% of GDP by 2016. The budget rule's symmetrical treatment of cyclical impacts ensures that a cyclically-induced easing of the pressure on the budget is not used for additional structural spending or revenue, but it does, however, mean that cyclical deterioration in the budget situation can be borne.

As of this year, the federal budget is being drawn up using a top-down approach in order to better accommodate the requirements of the budget rule. On 16 March 2011, the Federal Cabinet approved the key figures for the 2012 federal budget and financial plan up to 2015 which serve as the basis for further budgeting along departmental lines. This outline is then used in the government's internal budget drafting procedure; this in turn concludes with the

Federal Cabinet's decision to adopt the federal budget and financial plan. Insofar as the Federal Government's macroeconomic spring projection in April, the pension forecast at the start of May or the results from the Working Party on Tax Revenue Estimates (*Arbeitskreis "Steuerschätzungen"*) in mid-May entail changes relevant to the budget, the resulting fiscal burdens and relief will be taken into account in full when the final net borrowing for the 2012 government draft and for the financial plan to 2015 is established.

From 2020 onwards, it will no longer be permissible for the *Länder* to have a structural deficit. Until that time, the arrangements specific to the *Länder* and contained in their individual constitutions and budget codes will continue to apply on a transitional basis. The *Länder* of Berlin, Bremen, Saarland, Saxony-Anhalt and Schleswig-Holstein – which face particularly difficult budget situations – will receive budget consolidation assistance from the Federation and remaining *Länder* of €800 million annually, subject to the condition that they clear their 2010 structural deficits in 10 equal steps by 2020.

Closely linked to the reform concerning the budget rule is the introduction of a Federation-wide early warning system to prevent budgetary emergency situations. The Stability Council which commenced its work in 2010 was set up for this purpose. The Federal Minister of Finance, the *Länder* finance ministers and the Federal Minister of Economics are members of the Stability Council. The Stability Council monitors the development of the budgets of the Federation and *Länder* using four indicators (structural net lending/borrowing, the borrowing-to-expenditure ratio, the debt level and interest-tax ratio) as well as a projection of the medium-term budget trend on the basis of uniform assumptions. If the Stability Council finds that the Federation or a *Land* is threatened with a budgetary emergency, it is to agree a budget rehabilitation programme with them. The budget rehabilitation programme covers a period of five years and is monitored on an ongoing basis by the Stability Council. The aim is to avert the impending budget emergency at the relevant level of government. By conducting budget monitoring and through the instrument of budget rehabilitation programmes, the Stability Council has a central part to play in strengthening budgetary discipline at federal and *Länder* level.

4.3 Fiscal policy measures

The Federal Government is resolutely implementing the exit strategy for withdrawing government crisis management measures as planned. Because the supply of credit to businesses steadily improved during the upswing, it was possible to phase out the credit and guarantee programmes at the end of 2010 as envisaged. The bulk of additional investment spending by the Federal Government during the crisis was channelled into an Investment and Redemption Fund (*Investitions- und Tilgungsfonds*). The measures from this fund may only be financed until the end of December 2011, after which time only the fund's debts will be wound up. The exit strategy also entails the gradual withdrawal of government assistance for banks, which lawmakers made possible by enacting the Financial Market Stabilisation Act (*Finanz-*

marktstabilisierungsgesetz) in October 2008 for purposes of stabilising financial markets. The deadline for decisions on guarantees and recapitalisation measures from the Financial Market Stabilisation Fund (*Finanzmarktstabilisierungsfonds,* SoFFin) established under the Act expired at the close of 2010.

By putting together a budgetary consolidation package, the Federal Government laid the foundation in 2010 for a growth-oriented and socially balanced consolidation strategy while complying with the budget rule. The guiding principles are to limit government consumption, reduce subsidies, increase incentives and anchor the priority for education and research in budget planning. The package contains deficit-reduction measures totalling around €80 billion to 2014. The individual elements already presented in the August 2010 report on the implementation of measures to reduce the excessive deficit (*Bericht über die Umsetzung von Maßnahmen zum Abbau eines übermäßigen Defizits*) aim, *inter alia,* to make the economy greener by correcting e.g. energy tax relief in areas where it is misallocated. Incentives to take up employment will be improved by realigning social benefits and making job placement more efficient. And finally, the federal administration will contribute to consolidation by making far-reaching savings. September 2010's Budget Support Act (*Haushaltsbegleitgesetz 2010*) firmed up implementation of further elements of the consolidation package for the coming years.

The key figures for the 2012 budget and the financial plan to 2015 safeguard funding for measures concerning the national implementation of the five core objectives contained in the EU's 2020 Strategy, which are described in the National Reform Programme. Education and research are central in terms of ensuring Germany's future viability and are explicitly protected from budgetary savings. These fields of the future will therefore be strengthened with a total of €12 billion in the period from 2010 to 2013. The level reached in 2013 will be maintained in 2014 and 2015. The Federation is thus playing its part in raising the R&D quota to 3% and increasing spending on education and research combined to 10%. The Federation's transport investment will be held at a high level of around €10 billion annually.

At the Federal Cabinet meeting on 6/7 June 2010 the Federal Government initiated a reform of the armed forces. The suspension of conscription for basic military service that has since been approved and the gradual reduction in the number of military and civilian personnel will lead to substantial spending reductions that will grow over time. Over the financial planning period from 2011 to 2015, the defence budget will therefore make its contribution to consolidation, adopted last year, of €8.3 billion, and thus bear its part of the necessary savings in the federal budget.

A special Energy and Climate Fund (*Energie- und Klimafonds*) was set up with effect from 1 January 2011 as part of efforts to implement the Federal Government's Energy Concept (*Energiekonzept*). This special fund places the financial underpinning of national and international climate protection and energy efficiency on a reliable footing. The special fund draws on several sources of financing, namely the contractual payments from nuclear power plant operators and receipts from emissions trading that exceed the financial planning so far. In future, this means that alongside the federal budget, additional funds can increasingly be made available to promote an environmentally sound, reliable and affordable energy supply as well as further measures for international climate and environment protection.

Tax policy has to strike a balance between strengthening the forces of growth on a lasting basis and securing the financing of government tasks long term. The tax policy measures in the Federal Government's consolidation package – the majority of which were implemented in the 2011 Budget Support Act (*Haushaltsbegleitgesetz 2011*) – are an example of the fact that these objectives are mutually compatible. The savings and revenue enhancements adopted do not require any increase in direct taxation and do not, therefore, have a negative impact on growth potential or social equilibrium.

The tax policy measures aim to make the economy greener by, e.g., correcting energy tax relief where it is misallocated. The introduction of an aviation tax with effect from 1 January 2011 is intended to strengthen the incentives for more environmentally friendly behaviour in international air travel. The revenue from the aviation tax is expected to contribute €1 billion annually from 2011 onwards towards budget consolidation. A new tax on the use of nuclear fuel has also been levied since the beginning of the year There has furthermore been a moderate rise in tobacco duty. The Federal Government is also working to ensure that the financial sector makes an appropriate contribution to the costs arising from the financial crisis by means of a financial market tax.

The measures in the 2011 Tax Simplification Act (*Steuervereinfachungsgesetz 2011*) adopted by the Federal Government on 2 February 2011 serve to simplify and modernise the taxation process. This means taxpayers and the inland revenue service will benefit appreciably from a less burdensome system of tax returns, auditing and administration; eligibility conditions for tax benefits will be streamlined and paperwork will be reduced. Overall employees and families with children will be the main beneficiaries of relief worth around €590 million annually, without the consolidation course being jeopardised. This legislation is to enter into force on 1 January 2012; some measures will apply retroactively from 1 January 2011.

Through this consolidation strategy, the Federal Government intends to create latitude for providing tax relief that will further boost the dynamism of the domestic economy. Those in the lower and middle-income bracket especially are to receive the tax benefits as quickly as possible. However, this depends on acquiring the necessary budgetary leeway – while complying with the requirements at EU level and under the budget rule – by maintaining strict spending discipline.

In the field of business taxation, the Federal Government has initiated a review of additional options to improve the tax system. The intention is to modernise business tax legislation further and make it internationally competitive. A working group comprising representatives from the Federation, *Länder* and local authorities is to present proposals in autumn 2011 on reorganising loss-offsetting rules as well as alternatives to the current concept of treating groups as a single-entity for German tax purposes (*Organschaft*). When reviewing the reorganisation of loss offsetting, special attention will, however, be given to companies' substantial loss carry-forwards of over €500 billion in the case of corporation tax and trade tax, which jeopardise tax revenues and the financing of public budgets as a result. A realignment of local authority finances and, as a consequence, the future of local authorities' trade tax are also being discussed. There are plans for the Federation to relieve the burden on local authorities that is posed by the basic income support provided in old age and in the event of reduced earning capacity. A commitment has already been made to mutually approve this move within the context of the Local Authority Finance Commission (*Gemeindefinanzkommission*). A review of the reduced VAT rates is also on the agenda.

The Federal Government will integrate a decision about the introduction of a tax subsidy for research and development into an overall budget and tax policy concept, in line with the coalition agreement between the governing parties and taking into account the appropriate course of consolidation and the way the economy develops.

5 Projection of public budget trends

Given that the macroeconomic trend has outperformed expectations, the state of public finances is developing much more favourably than projected as recently as in January 2010's stability programme. Added to this, the Federal Government adopted a consolidation package in the summer of 2010 and many of the measures it contains will have an impact right from this year. Taken together, this will lead to a speedy improvement in the general government budget balance and, also as a result of that, to a marked decline in the debt ratio even within the period covered by the Stability Programme.

5.1 Development of general government revenue and expenditure

Stable development of general government revenue

The favourable economic outlook also applies to the development of general government revenue. Having climbed by 1.5% in 2010, the recovery in the revenue trend will continue in the coming years. Looked at on an average for the 2010 to 2015 period in question, general government revenue is expected to rise by 2½% annually. Nevertheless, the trend over the projection period will lag behind the development of nominal GDP, which means that the general government expenditure ratio will decline further by around ½ a percentage point to approximately 42½%. This is caused by the fall in other revenues of GDP (cf. Table 12 in the Appendix). Throughout the entire projection period, the general government expenditure ratio is expected to remain relatively constant at 39½%.

Given the favourable macroeconomic momentum, the tax revenue ratio will slowly recover over the years and reach a level of around 23½% at the end of the projection period (cf. Table

1). Here it is assumed that the measures contained in the consolidation package will be implemented in full. As defined in the System of National Accounts, tax revenue also encompasses the levy payable to the Restructuring Fund (*Restrukturierungsfonds*) for banks.

The social contribution ratio will decline further this year although there has been an increase in the rate of contributions to the statutory health insurance system, although the stimulus package's temporary reduction in the contribution rate to unemployment insurance has come to an end, and despite the fact that the labour market is still performing vigorously, with the associated increase in gross wages and salaries which that brings. This trend will also persist in the medium term. One of the main causes will be the falling contribution to statutory pension insurance from 19.9% at present to 19.1% by 2014 which will arise because of the development of the sustainability reserve (*Nachhaltigkeitsrücklage*) built up by the statutory pension insurance institutions. Under section 158 of Book VI of the Social Security Code (*Sozialgesetzbuch VI*), the contribution rate to statutory pension insurance must be reduced at the beginning of the year if keeping the contribution rate to the end of this year would mean that the sustainability reserve is expected to exceed 1.5 times the average spending to the detriment of the general pension insurance institutions for one calendar month.

Table 1: Development of tax, social contribution and fiscal charges ratios

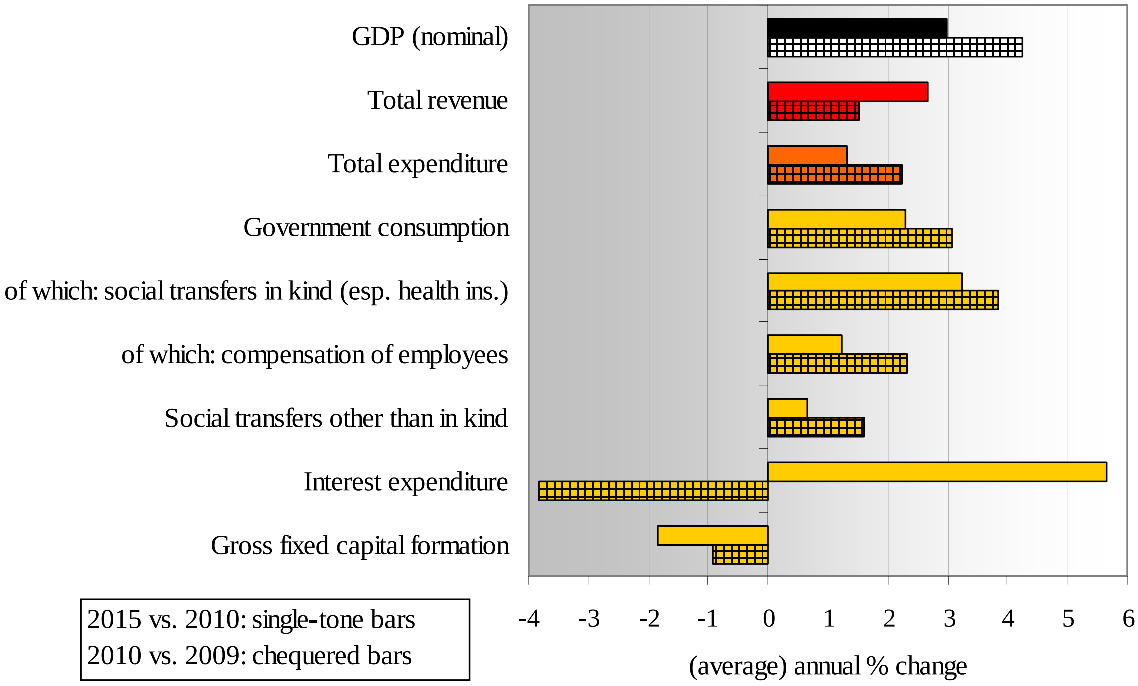
	2010	**2011**	**2012**	**2013**	**2014**	**2015**
	- % of GDP -					
Taxes	**22.7**	**23**	**23**	**23 1/2**	**23 1/2**	**23 1/2**
Social contributions	**16.8**	**16 1/2**	**16 1/2**	**16 1/2**	**16**	**16**
Taxes & social contributions						
April 2011 Update	**39.6**	**39 1/2**	**39 1/2**	**39 1/2**	**39 1/2**	**39 1/2**
January 2010 Update	39	38 1/2	39	39	-	-

Discrepancies between the fiscal charges ratio and the sum of the tax and social contribution ratios are the result of rounding. The figures for the projection years are rounded to a half a percentage point of GDP.

Consolidation reduces government expenditure ratio significantly in the medium term

General government expenditure increased by 2.2% in the past year (cf. Figure 1). On its own, this rise appears to be moderate. However, it has to be seen in light of the strong expansion of spending in 2009 arising from the operation of automatic stabilisers and the adoption of stimulus packages. Taking 2009 and 2010 together, general government expenditure increased on average by a substantial 3.6% each year.

Figure 1: Average annual development of general government revenue and expenditure and GDP from 2010 to 2015 and in 2010 in comparison with the preceding year



Following the crisis-induced climb in expenditure, Germany has this year started to phase out discretionary stabilisation measures. Across all spending categories – apart from interest expenditure – there will be a reduction, in some cases substantial, in the average annual growth rates during the projection period. On an annual average for 2010 to 2015, expenditure will rise by only 1½% p.a. and, in comparison with nominal GDP growth averaging around 3% annually, will consequently be very low in proportion. Alongside the development of the largest spending item (namely government consumption, the annual average increase of which will decline to just under 2½%), this largely has its roots in the fall in gross capital formation by an average of almost 2% p.a. There will first be a marked decline in gross capital formation, mainly because of the expiry of the Future Investments Act (*Zukunftsinvestitionsgesetz*) which had precipitated an immediate and therefore anticyclical expansion in general government investment. At the end of the projection period, gross capital formation will, nevertheless, start to rise again, but it will not reach the pre-crisis level. The strong, crisis-induced expansion in net borrowing at all levels, however, means that, taken over the whole period from 2010 to 2015, there will be a noticeable rise in interest expenditure of 5½% on average per year, which restricts scope for other spending or lowering revenues.

The government expenditure ratio (government spending in relation to GDP), which had already declined last year due to the strong macroeconomic momentum, will therefore continue this trend undiminished and is thus projected to stand at only about 43% at the end of the projection period (cf. Table 2).

Table 2: Development of the general government expenditure ratio

	2010	2011	2012	2013	2014	2015
	- % of GDP -					
April 2011 Update	**46.6**	**45 1/2**	**44 1/2**	**44**	**43 1/2**	**43**
January 2010 Update	48	47	46	45	-	-

Figures for the forecast years are rounded to half a percentage point of GDP.

5.2 Development of net lending/borrowing

Excessive deficit reduced as early as 2011

The relatively stable development of general government revenue over the past years in comparison to general government expenditure stood in marked contrast to the increase in the general government expenditure ratio in 2008, and led to substantially less deterioration in the general government budget balance than initially predicted. The deficit therefore exceeded the Maastricht reference value of 3% of GDP last year only. This is particularly remarkable given that without the measures to stabilise the financial markets, the general government deficit ratio would only have stood at 2.9% of GDP in both 2009 and 2010, and thus would have been below the Maastricht reference value. In both years the recapitalisation of Hypo Real Estate (HRE) increased the deficit. Last year the establishment of winding-up institutions for WestLB (Erste Abwicklungsanstalt, EAA) and HRE (FMS Wertmanagement, FMS-WM) that are classified as belonging to the general government sector also had one-off effects on the deficit.

This year the general government deficit will already be brought back to 2½% of GDP, thanks to the shift away from previous years’ expansive fiscal policy (through the introduction of consolidation measures) and as a result of the continuation of the economic recovery (cf. Table 3). Germany will thus reduce its excessive deficit two years ahead of the 2013 deadline required under the excessive deficit procedure. This positive trend will continue gradually over the coming years, which means that the budget will be close to balance at the end of the period covered by the Stability Programme.

Table 3: Development of the general government budget balance

	2010	2011	2012	2013	2014	2015
	- in % of GDP -					
April 2011 Update	**-3.3**	**-2 1/2**	**-1 1/2**	**-1**	**- 1/2**	**- 1/2**
January 2010 Update	-5 1/2	-4 1/2	-3 1/2	-3	-	-

The net lending/borrowing figures are rounded to half a percent of GDP.

Net lending/borrowing by level of government

The continued deterioration in the general government budget balance in 2010 only affected the public budgets and, here, the Federation and its off-budget entities in particular[1] (cf. Table 4).

Table 4: Net lending/borrowing by level of government

	2010	2011	2012	2013	2014	2015
	- in % of GDP -					
Central government	-2.3	-1 1/2	-1	-1	- 1/2	- 1/2
State government	-0.7	- 1/2	- 1/2	- 1/2	-0	-0
Local government	-0.4	- 1/2	-0	-0	-0	0
Social security funds	0.1	-0	0	0	0	0
General government	-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2

The net lending/borrowing figures are rounded to half a percent of GDP.

On the reverse side, the improvement in the general government budget balance this year is also mainly due to the development at federal level. In the case of the federal budget, this is largely the result of the introduction of the new budget rule and the course of consolidation it prescribes. For the federal budget and the off-budget entities of the Federation, the discontinuation of one-off measures is also making a contribution. Following the end of the Investment and Redemption Fund’s financing phase, the Federal Government’s decision on key figures for the 2012 budget and financial plan to 2015 will yield a further reduction of the federal deficit to around ½% of GDP in 2015, taking Germany perceptibly below the structural deficit figures required in the transition phase of the new budget rule. For the expenditure savings (of €4.8 billion in 2014 and 2015 respectively) not yet implemented in specific measures, the technical assumption has been made that the resultant level of consolidation required is spread proportionately across all forms of spending – with the exception of interest expenditure and transfers to other government levels and abroad.

The deficits of the *Länder* and local authorities (including their off-budget entities), which have also worsened on account of the economic and financial crisis, will remain almost unchanged this year – albeit at a much lower level than in the case of the Federation. The *Länder* and local authorities are, however, expected to consolidate their budgets over the projection period. *Länder* budgets are projected to be close to balance in 2014. The local authorities – with a great degree of variation – are likely to achieve balanced budgets overall as early as 2012 because of the considerable improvement in their financial position thanks to the recovery in tax revenue and, in particular, thanks to the Federation’s assumption of the costs for basic income support provided in old age and in the case of reduced earning capacity. In comparison with the previous estimate, a mix of additional investment expenditure, lower *Länder* transfers and a more favourable balance have consequently been assumed.

[1] This especially includes the Financial Market Stabilisation Fund and the Investment and Redemption Fund established to finance a large part of the economic stabilisation measures of an investment nature.

The social security funds' budget balance, which posted a surplus last year, deteriorates again briefly this year. This was on account of the Federation making a loan to finance the deficit of the Federal Employment Agency (*Bundesagentur für Arbeit*) which, unlike a grant, does not reduce the Maastricht deficit of the respective public or social budgets. However, the budget of the social security funds remains close to balance and will record surpluses in the following years. Here it is assumed that the reduction in the Federation's contribution to the costs of job promotion by the Federal Employment Agency will be compensated by lower spending on the part of the Agency, e.g. through gains in efficiency.

5.3 Development of structural net lending/borrowing

Medium-term budgetary objective will be achieved within the programme period

Given the cyclical improvement, the deterioration of the general government budget balance last year must have had structural origins. While the structural deficit, i.e. the financing deficit net of cyclical and temporary effects, rose by more than 1 percentage point to 2% of GDP (cf. Table 5), this was far less than anticipated. In the last stability programme, it had still been necessary to assume an increase of 3 percentage points. Despite the receipts from the auction of mobile frequencies, there were, on balance, negative one-off effects of just under ½% of GDP on account of the impacts on the deficit arising from the recapitalisation of HRE, the establishment of the winding-up institutions for banks as well as the ruling on the tax deductibility of home offices.

This year's improvement in the balance is due, in particular, to the continued macroeconomic recovery. As a result of budget consolidation, the structural deficit will decline substantially in the coming years. From 2014 onwards, Germany will have achieved the objective of having a budget close to balance. This means Germany will be able to comply on a lasting basis with the medium-term objective of having a structural deficit of -½% of GDP (and which also takes anticipated demographic trends into account).[2]

[2] In line with the provisions of the SGP, there are two methods for calculating the medium-term objective. Both possible methods produce a medium-term objective of -½% of GDP, i.e. whether 33% of the costs as a result of ageing are prefinanced or all costs as a result of ageing are covered until 2040.

Table 5: Structural balance compared with actual balance and GDP trend

	2010	2011	2012	2013	2014	2015
Structural balance (% of GDP)	-2	-2	-1	-1	- 1/2	-0
General government net borrowing/ net lending (% of GDP)	-3 1/2	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
Real GDP (% change yoy)	3.6	2.3	1.8	1 1/2	1 1/2	1 1/2

The balances and the medium-term GDP growth rates are rounded to half a percentage point (of GDP).

5.4 Sensitivity of net lending/borrowing forecast

The sensitivity analysis shows the net lending/borrowing trends that arise when there are deviations from the macroeconomic assumptions. The sensitivity analysis looks at two alternative scenarios which result from a reduction and an increase in the annual growth rate of real GDP of ½ a percentage point, respectively, from 2011 to 2015. It is assumed that the GDP deflator and GDP composition are constant compared with the baseline scenario.

The same picture emerges under the sensitivity analysis in qualitative terms. In both scenarios, the deficit will fall from this year onwards. In quantitative terms, however, marked differences result (cf. Table 6). Under the scenario with less dynamic macroeconomic performance, budget consolidation would take much longer. The general government budget balance would still be -1½ of GDP at the end of the programme period. If, by contrast, GDP were to develop at a yearly rate which is ½ a percentage point more favourable than assumed in the baseline scenario, the medium-term objective would be achieved by 2013 already. By the end of the projection horizon, there would, statistically, even be a general government surplus of 1% of GDP.

Table 6: Sensitivity of the projection for the general government budget balance

	2010	2011	2012	2013	2014	2015
GDP as in	**- general government budget balance in % of GDP -**					
- baseline scenario	-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
- alternative scenarios						
• - ½ pp p.a. compared to baseline		-3	-2	-2	-1 1/2	-1 1/2
• + ½ pp p.a. compared to baseline		-2 1/2	-1	- 1/2	1/2	1

The net lending/borrowing figures are rounded to half a percent of GDP.

5.5 Development of debt

The development of the debt ratio as defined by the Maastricht Treaty will, in the medium-term, be shaped by the budget trend and impact of the financial market crisis. The debt ratio using the Maastricht definition takes into account the impact of government support measures to fend off the financial crisis in the banking sector, as well as the debts arising from bilateral loans and loans given by the European Financial Stability Facility. From 2013 onwards, the forecast contains the paid-in capital instalments to the European Stability Mechanism.

After a clear increase by 9.7 percentage points in 2010, resulting in particular from the foundation of the EAA and FMS-WM winding-up institutions which are classified as belonging to the general government sector, the debt ratio will fall by around 1 ½ percentage points to just under 82% of GDP in the current year. The most important reason for this is the liquidation of the winding-up institutions' portfolios, which will also continue over the coming years. The government debt ratio will decline in line with the amount by which these institutions' liabilities are reduced. In 2011 there will be a slight decline in federal, *Länder* and local authority budgets as well, although financial assistance provided as part of the European debt crisis will dampen the reduction of the debt ratio.

From 2012 onwards, the consolidation efforts undertaken by the different levels of government will additionally make themselves felt, which means that the debt ratio is expected to fall to around 75½% by 2015 (cf. Table 7).

Table 7: Development of the debt ratio

	2010	2011	2012	2013	2014	2015
	- in % of GDP -					
April 2011 Update	**83.2**	**82**	**81**	**79 1/2**	**77 1/2**	**75 1/2**
January 2010 Update	76 1/2	79 1/2	81	82	-	-

The debt ratios are rounded to half a percent.

6 The long-term sustainability of public finances

6.1 Challenges to the sustainability of public finances

For a number of years, concern about the long-term development of public finances has been a common feature of reporting in the national stability and convergence programmes and the evaluation thereof by the European Council and the European Commission. Demographic change was the decisive trigger. The post-war baby-boom generations are now gradually reaching retirement age. As a consequence, the old-age dependency ratio, which describes the ratio between those of retirement age and those of working age in the population, will climb more quickly than it has done in the past. This is demonstrated by the population projections produced by the statistical office of the EU (Eurostat) and the Federal Statistical Office (*Statistisches Bundesamt*). In Germany the problems which may arise from this development were identified at an early stage and have led to the introduction of corresponding reforms, e.g. in the field of old-age pensions. But that aside, there is hardly any area of society that will not be affected by the expected demographic changes. Coordinated by the Federal Ministry of the Interior (*Bundesministerium des Innern*), the Federal Government is currently putting together a report on the demographic situation and future development of Germany (*Bericht zur demografischen Lage und künftigen Entwicklung des Landes*), which describes the demographic processes and their impact on the economy, labour market, social security systems and infrastructure. Building on the report scheduled for autumn 2011, the Federal Government will develop a strategy to address demographic change; the Federal Government will present the results next year.

The Federal Government provides comprehensive information about the possible long-term risks for public finances, and the measures taken to contain them, through the Sustainability Report (*Tragfähigkeitsbericht*) which is produced once each legislative period by the Federal Ministry of Finance. This report is not dedicated solely to the consequences of demographic change, but also examines other causes of potential fiscal problems – such as the relevant debt level reached and the most recent budget situation. The global economic and financial crisis – with its impact on public finances in many countries – has shown how quickly matters can deteriorate. It is not only possible to identify this from quantitative indicators such as the sustainability gaps calculated by the European Commission as part of the budgetary monitoring process – gaps which have in some cases grown dramatically. It can also be gathered from the risk classification undertaken thereafter: as far as the long-term sustainability of public finances is concerned, there are only a few countries left where there is a low risk in that regard. The vast majority of Member States now fall into the group of countries with a high risk. Germany's position has not changed. In light of the burdens on public finances that will be incurred in future, Germany will continue to belong in the group of medium-risk countries.

The Federal Government's current view of the situation will be set out in the new Sustainability Report, through which the Federal Ministry of Finance will this very year continue the national reporting on sustainability.

In the Euro Plus Pact the participating Member States furthermore agreed to undertake concrete policy actions to improve the long-term sustainability of public finances. As described in chapter 2.3, the German action programme has Germany complying with the requirements under the excessive deficit proceedings ahead of time (namely that the deficit will be brought under the 3% reference value by 2011 already) and, in the case of the 2011 and 2012 federal budgets, has the course of reduction set by the budget rule being undercut.

6.2 Government revenue and expenditure from a long-term perspective

At both the national and EU level, long-term budget forecasts are drawn up at regular intervals covering several years. The results of the model calculations most recently published by the EU's Economic Policy Committee and the European Commission were already mentioned in last year's update of the German Stability Programme. The model calculations have been incorporated into the risk evaluation which ECOFIN undertakes as part of its subsequent review of all stability and convergence programmes with respect to the long-term sustainability of public finances, and concentrate on those budget components most likely to be heavily influenced by changes in the composition of the population (cf. Table 16). The timescale for these projections currently extends until 2060. The demographic assumptions adhere to Eurostat's 2008 forecasts, the first to be presented for all 27 EU Member States.

To measure the anticipated increase or decrease in the fiscal burden, the expenditure incurred each year is stated of the GDP calculated for that same year. As far as the general government revenues are concerned, it is normally assumed that they will develop in a broadly similar manner to overall economic output. There would be no changes to the general government revenue ratio in this scenario. The pressure on public finances that arises from population ageing is then reflected in the climb in the respective general government expenditure ratio.

The model calculations produced at Community level show that – assuming otherwise constant conditions – demographic change will drive public spending on old-age provisions (statutory pensions and civil service pensions) and the expenditure on health care and long-term care upwards to a much higher level than was reached in the past. In the EU, the age-dependent budget components would increase by around 4¾ GDP percentage points up to 2060 overall. The increase in demography-related burdens calculated for Germany (in relation to overall economic output) is on a comparable scale. However, the range produced for the EU Member States overall is very broad. In many cases double-digit values are attained.

The burdens on public budgets that arise from population ageing may make it substantially more difficult for all of the countries affected by the economic and financial crisis to reduce the increased government indebtedness stemming from the crisis. The resulting risks therefore need to be taken particularly seriously where this concerns the future development of countries to which Germany is tied in the monetary and economic union.

6.3 Need for action and structural reforms in the social security systems

Over the past years, Germany has already made considerable efforts to secure the long-term sustainability of public finances. Because demographic change is accompanied by a decline in the labour supply, it tends to have a dampening effect on economic growth. Sustainable policymaking takes this as its starting point and creates the framework conditions for the economic performance of the Federal Republic of Germany to improve even in an ageing society.

The course of the economic and financial crisis in Germany has in no small part shown that the structural reforms of recent years have made the German labour market considerably more flexible. Looking ahead, the Federal Government's policies are geared toward increasing the labour force participation of women and older people in particular as well as low-skilled workers and individuals with an immigrant background. At the same time, it is important to further reduce structural unemployment in Germany and to get more people into employment. To this end, the Federal Government will optimise incentive structures in order to further improve the functioning of the labour market.

Furthermore, reforms in the field of statutory pension insurance in particular have helped to strengthen the financial sustainability in this area considerably. The contribution rate is not permitted to exceed 20% in 2020 and 22% in 2030. Between 2012 and 2029, the general retirement age will be raised gradually to 67. In recent years, trends in the employment of older workers have improved much better than employment trends overall – which is, *inter alia*, due to the shift away from the practice of early retirement. The annual pension adjustment is based on the development of gross wages and salaries per employed person. The adjustment formula continues to take into account employees' expenditure on pensions. In addition to changes in the rate of contributions to statutory pension insurance, this includes the growing expenditures on fully-funded supplementary pensions introduced in 2002. Through its sustainability factor, the formula accounts for demographically induced changes in the ratio of pension beneficiaries to contributors. The downward adjustments not applied over previous years because of a safeguard in the rules will, as required by law (and called for in the Council recommendation regarding Germany's 2010 stability programme), be reclaimed from 2011 onwards by halving any positive pension adjustments until the postponed adjustment is made good.

To secure the long-term financial viability of the statutory health insurance system, the Federal Government launched a fundamental reform with its Statutory Health Insurance Financing Act (*GKV-Finanzierungsgesetz*) which entered into force on 1 January 2011. On the expenditure side, the Act contains effective consolidation measures; and on the revenue side, it largely decouples non-wage labour costs from trends in health care expenditures, so that the latter do not give rise to increasing labour costs which would jeopardise growth and jobs. Greater transparency and increased competition are the cornerstones of the new financing system. To curtail the particularly dynamic rise in expenditures connected to the provision of medicinal products, the Federal Government has introduced a range of measures aimed to cut costs and increase competition.

In light of demographic change, social long-term care insurance must be geared toward the increasing needs of a growing number of people requiring care. The financial basis must be secured within the context of a shrinking and ageing population, and no generation should be unduly burdened. For this reason, the Federal Government is developing a concept for a funded system to supplement the existing pay-as-you-go method in social long-term care insurance.

Appendix

Table 8: Forecast of the macroeconomic development from 2010 to 2015[1]

	ESA Code	2010	2010	2011	2012	2013 to 2015[4]
		€bn/index	% change p.a.			
Real GDP, chain index	B1g	109.00	3.6	2.3	1.8	1½
Nominal GDP	B1g	2,498.80	4.2	3.3	2.9	3
Components of real GDP, chain index						
Private consumption expenditure[2]	P.3	103.75	0.4	1.6	1.5	1
Government consumption expenditure	P.3	112.83	2.3	1.0	1.0	1
Gross fixed capital formation	P.51	100.21	6.0	4.3	3.7	2
Changes in inventories (GDP growth contribution)[3]	P.52 + P.53	-	0.6	0.0	-0.1	0
Exports	P.6	164.87	14.1	6.5	6.5	4
Imports	P.7	148.91	12.6	6.4	6.9	4
Contributions to real GDP growth[3]						
Domestic demand (excluding stocks)		-	1.8	1.9	1.8	1½
Changes in inventories	P.52 + P.53	-	0.6	0.0	-0.1	0
External balance of goods and services	B.11	-	1.3	0.4	0.1	0

[1] 2010: Provisional result from the Federal Statistical Office, February 2011
2011 and 2012: Results of the 2011 Annual Projection (*Jahresprojektion 2011*), January 2011
2013 to 2015: Medium-term projection on the basis of the 2011 Annual Projection
[2] Including private non-profit organisations serving households
[3] Contribution to GDP growth rate
[4] GDP rounded to ¼; all remaining quantities rounded to ½

Table 9: Price developments – deflators[1]

	ESA Code	2010	2010	2011	2012	2013 to 2015[3]
		Index	% change p.a.			
GDP		111.15	0.6	1.0	1.0	1¼
Private consumption expenditure[2]		114.69	2.0	1.7	1.5	1½
Government consumption expenditure		110.06	0.7	0.9	0.9	1
Gross capital formation		103.16	0.3	0.1	-0.1	½
Exports		101.01	2.7	1.6	1.1	1
Imports		100.19	4.9	2.3	1.1	1

[1] 2010: Provisional result from the Federal Statistical Office, February 2011
2011 and 2012: Results of the 2011 Annual Projection, January 2011
2013 to 2015: Medium-term projection on the basis of the 2011 Annual Projection
[2] Including private non-profit organisations serving households
[3] GDP rounded to ¼; all remaining quantities rounded to ½

Table 10: Labour market developments[1]

		2010	2010	2011	2012	2013 to 2015[4]
	ESA Code	Index	% change p.a.			
Employment, persons (domestic) (m)		40.483	0.5	0.8	0.4	0
Employment, hours worked (bn hours)		57.43	2.6	1.3	0.1	- 1/2
Unemployment rate (%)		-	6.8	6.0	5.5	5
Labour productivity[2] (2000=100)		105.40	3.1	1.5	1.4	1 1/2
Labour productivity[3] **(2000=100)**		109.43	1.0	0.9	1.7	1 3/4
Compensation of employees (€bn)	D.1	1,260.03	2.8	3.1	2.6	2 1/2
Compensation per employee (€)		34,936	2.2	2.3	2.1	2 1/2

[1] 2010: Provisional result from the Federal Statistical Office, February 2011
2011 and 2012: Results of the 2011 Annual Projection, January 2011
2013 to 2015: Medium-term projection on the basis of the 2011 Annual Projection
[2] Labour productivity per employee
[3] Labour productivity per hour worked
[4] Number of persons in employment and productivity rounded to ¼; all remaining quantities rounded to ½; unemployment ratio: value for 2015

Table 11: Sectoral balances[1]

% of GDP	ESA Code	2010	2011	2012	2013 to 2015
1. Net lending/borrowing vis-a-vis the rest of the world	B.9	5.1	4.7	4.8	6
of which:					
- Balance on goods and services		5.2	5.0	5.0	6
2. Net lending/borrowing of households[2]	B.9	6.0	5.8	5.8	6 1/2
3. Net lending/borrowing of general government	EDP B.9	-3.3	-2 1/2	-1 1/2	-1/2
4. Statistical discrepancy		0.0	0	0	0

[1] 2010: Provisional result from the Federal Statistical Office, February 2011
[2] 2011 and 2012: Results of the 2011 Annual Projection, January 2011; 2013 to 2015: Medium-term projection on the basis of the 2011 Annual Projection

Table 12: General government budgetary prospects

	ESA Code	2010 Level	2010 % of GDP	2011 % of GDP	2012 % of GDP	2013 % of GDP	2014 % of GDP	2015 % of GDP
Net lending (EDP B.9) by sub-sector								
1. General government	S.13	-82.0	-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
2. Central government	S.1311	-57.9	-2.3	-1 1/2	-1	-1	- 1/2	- 1/2
3. State government	S.1312	-17.2	-0.7	- 1/2	- 1/2	- 1/2	-0	-0
3. Local government	S.1313	-10.0	-0.4	- 1/2	-0	-0	-0	0
5. Social security funds	S.1314	3.0	0.1	-0	0	0	0	0
General government (S13)								
6. Total revenue	TR	1,082.1	43.3	43	43	43	42 1/2	42 1/2
7. Total expenditure	TE	1,164.1	46.6	45 1/2	44 1/2	44	43 1/2	43
8. Net lending/borrowing	EDP B.9	-82.0	-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
9. Interest expenditure	EDP D.41	59.8	2.4	2 1/2	2 1/2	2 1/2	2 1/2	2 1/2
10. Primary balance		-22.2	-0.9	-0	1	1 1/2	2	2 1/2
11. One-off and other temporary measures[1]		-7.0	-0.3	-0	0	0	0	0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		568.3	22.7	23	23	23 1/2	23 1/2	23 1/2
12a. Taxes on production and imports	D.2	310.5	12.4	12 1/2	12 1/2	12 1/2	12	12
12b. Taxes on income, wealth, etc	D.5	257.8	10.3	10 1/2	11	11	11	11
12c. Capital taxes	D.91	0.0	0.0	0	0	0	0	0
13. Social contributions	D.61	420.3	16.8	16 1/2	16 1/2	16 1/2	16	16
14. Property income	D.4	18.5	0.7	1/2	1	1	1	1
15. Other		75.1	3.0	3	2 1/2	2 1/2	2 1/2	2 1/2
16=6. Total revenue	TR	1,082.1	43.3	43	43	43	42 1/2	42 1/2
p.m.: Tax burden (D.2+D.5+D.61)		988.5	39.6	39 1/2	39 1/2	39 1/2	39 1/2	39 1/2
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1 + P.2	298.1	11.9	11 1/2	11 1/2	11 1/2	11	11
18. Social payments	D.62	654.8	26.2	25 1/2	25	25	24 1/2	24 1/2
19=9. Interest expenditure	EDP D.41	59.8	2.4	2 1/2	2 1/2	2 1/2	2 1/2	2 1/2
20. Subsidies	D.3	33.0	1.3	1 1/2	1	1	1	1
21. Gross fixed capital formation	P.51	39.0	1.6	1 1/2	1 1/2	1	1	1
22. Other		79.6	3.2	3	3	3	2 1/2	2 1/2
23=7. Total expenditure	TE	1,164.1	46.6	45 1/2	44 1/2	44	43 1/2	43
p.m.: Government consumption (nominal)	P.3	486.7	19.5	19 1/2	19 1/2	19	19	19

[1]A plus sign means deficit-reducing one-off measures.

Table 13: General government debt developments ('Maastricht debt')

% of GDP	ESA Code	2010	2011	2012	2013	2014	2015
1. Gross debt		83.2	82	81	79 1/2	77 1/2	75 1/2
2. Change in gross debt		12.8	1	1 1/2	1/2	1/2	0
Contributions to changes in gross debt							
3. Primary balance		0.9	0	-1	-1 1/2	-2	-2 1/2
4. Interest expenditure	EDP D.41	2.4	2 1/2	2 1/2	2 1/2	2 1/2	2 1/2
5. Stock-flow adjustment		9.5	-1 1/2	-0	- 1/2	- 1/2	-0
p.m.: Implicit interest rate on debt[1]		3.4	3	3	3 1/2	3 1/2	3 1/2

[1]Proxied by interest expenditure divided by the debt level of the previous year.

Table 14: Cyclical developments

% of GDP	ESA Code	2010	2011	2012	2013	2014	2015
1. Real GDP growth (%)		3.6	2.3	1.8	1 1/2	1 1/2	1 1/2
2. Net lending of general government	EDP B.9	-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
3. Interest expenditure	EDP D.41	2.4	2 1/2	2 1/2	2 1/2	2 1/2	2 1/2
4. One-off and other temporary measures[1]		- 1/2	-0	0	0	0	0
5. Potential GDP growth (%)		1	1 1/2	1 1/2	1 1/2	1 1/2	1 1/2
contributions:							
-labour		0	1/2	1/2	0	0	-0
-capital		1/2	1/2	1/2	1/2	1/2	1/2
-total factor productivity		1/2	1/2	1/2	1/2	1	1
6. Output gap		-2	-1	- 1/2	- 1/2	- 1/2	-0
7. Cyclically budgetary component		-1	- 1/2	- 1/2	- 1/2	-0	-0
8. Cyclically adjusted balance (2 - 7)		-2 1/2	-2	-1	-1	- 1/2	-0
9. Cyclically adjusted primary balance (8 + 3)		0	1/2	1 1/2	2	2 1/2	2 1/2
10. Structural balance (8 - 4)		-2	-2	-1	-1	- 1/2	-0

[1] A plus sign means deficit-reducing one-off-measures.

Table 15: Divergence between the April 2011 and January 2010 stability programmes

	ESA Code	2010	2011	2012	2013	2014	2015
Real GDP growth (%)							
Previous update		1.4	2	2	2		
Current update		3.6	2.3	1.8	1 1/2	1 1/2	1 1/2
Difference		2.2	1/2	-0	- 1/2		
General government net lending (% of GDP)	EDP B.9						
Previous update		-5 1/2	-4 1/2	-3 1/2	-3		
Current update		-3.3	-2 1/2	-1 1/2	-1	- 1/2	- 1/2
Difference		2	2	2	1 1/2		
General government gross debt (% of GDP)							
Previous update		76 1/2	79 1/2	81	82		
Current update		83.2	82	81	79 1/2	77 1/2	75 1/2
Difference		6 1/2	2 1/2	- 1/2	-2 1/2		

Table 16: Development of age-related general government expenditure from a long-term perspective

	2007	2020	2030	2040	2050	2060
	Expenditure as % of GDP					
Pension expenditure[1]	10.4	10.5	11.5	12.1	12.3	12.8
p.m.: Contribution revenue[2]	7.2	6.9	7.8	8.3	8.4	8.6
Health care expenditure[3]	7.4	8.1	8.5	9.0	9.2	9.2
Long-term care expenditure[4]	0.9	1.2	1.4	1.8	2.2	2.4
Education expenditure[5]	3.9	3.2	3.3	3.4	3.4	3.5
Unemployment insurance[6]	0.9	0.6	0.6	0.6	0.6	0.6
	Assumptions					
Productivity gains (%)	1.5	1.7	1.7	1.7	1.7	1.7
Potential growth (%)	1.4	1.5	1.3	1.1	1.0	1.0
Labour force participation (%)						
- Men (15 to 64)	82.1	83.9	83.2	83.3	82.9	83.0
- Women (15 to 64)	70.2	74.1	75.3	77.0	76.5	76.5
Unemployment rate	8.4	6.2	6.2	6.2	6.2	6.2
Old-age dependency ratio	29.9	35.3	46.2	54.7	56.4	59.1
Total population (m)	82.3	81.5	80.2	77.8	74.5	70.8
Population aged 65+ (m)	16.3	18.6	22.1	24.2	23.6	23.0

[1] Statutory pension insurance and civil servants' pensions
[2] Statutory pension insurance
[3] Statutory health insurance
[4] Social long-term care insurance
[5] Excluding education expenditure by the Federal Employment Agency
[6] Wage replacement benefits

Source: Results of model calculations by the Economic Policy Committee of the EU (EPC) the European Commission (DG ECFIN) presented in *The 2009 Ageing Report.*

Comments:

The dynamisation of expenditure on long-term care in line with the amount of the change in GDP per person in employment that is assumed in the reference scenarios does not correspond to current legislation. An alternative calculation based on applicable law and using a medium-term development in payments corresponding to the general rate of inflation produces a rise of a maximum 1.1% of GDP in 2050.

Statements about productivity gains (measured using labour productivity) and potential growth (measured using aggregate potential output) relate to changes against the previous year. In the case of the old-age dependency ratio, the limits for the population of working age (15-64) are the same as those for labour force participation.

Work is currently underway at Community level to update Eurostat's population projections and the long-term calculations for the macroeconomic and fiscal development for all 27 Member States of the EU. Work on this is not expected to be concluded until next year.

Table 17: Technical assumptions for the projection of macroeconomic developments

	2010	2011	2012	2013 to 2015
Short-term interest rate (annual average)	1.0	1.0	1.0	
USD/€ exchange rate (annual average)	1.3	1.3	1.3	1.3
Growth of German sales markets	10	6 1/2	6 1/2	5
Oil price (Brent, USD/barrel)	80	94	94	94