Federal Ministry
of Finance

German
Stability Programme

2013 Update

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Preface
to the German Stability Programme for 2013

In accordance with the provisions of the preventive arm of the Stability and Growth Pact, every year euro area Member States draw up Stability Programmes while the remaining Member States prepare Convergence Programmes. These reports are submitted in April to the European Commission and the Council of Economics and Finance Ministers (Ecofin Council).

This update of the German Stability Programme was approved by the Federal Cabinet on 17 April 2013. The programme follows 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 expert committees of the German Bundestag as well as to the Finance Minister Conference (Finanzministerkonferenz) and the Stability Council (Stabilitätsrat). The Bundestag and Bundesrat had the opportunity to deliberate on both the Council Recommendation of 10 July 2012 regarding Germany's 2012 National Reform Programme as well as the Council opinion on Germany's Stability Programme for 2012-2016.

The Federal Ministry of Finance publishes the updated Stability Programme along with the programmes for preceding years online at:
http://www.bundesfinanzministerium.de

The programmes of all EU Member States as well as the corresponding European Commission analyses and Ecofin recommendations are published on the European Commission's website at:

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

1. Summary

Sound public finances are a crucial factor in safeguarding a state's ability to take effective action and establishing lasting conditions that favour economic growth. In addition, they add flexibility to a state's fiscal strategy while boosting confidence in the future. Positive expectations regarding the future shape of public budgets help to foster investment and consumption by businesses and private households. Sound government finances go hand-in-hand with competitive economic structures.

Germany is determined to comply with all national and European fiscal policy requirements. This is the guiding principle behind the fiscal policy strategy presented in this Stability Programme. The fiscal policy targets that Germany laid down in last year's Stability Programme were achieved in full.

In 2012, Germany's general government balance posted a structural surplus for the first time since reunification. The general government's structural balance – i.e., adjusted for cyclical and one-off effects – stood at +0.4% of GDP. A slight structural surplus will be achieved in 2013 as well. This surplus is expected to grow to roughly 1/2% of GDP in the coming years thanks to continuing fiscal consolidation efforts, particularly on the part of the Federation. This means that Germany will achieve sustained compliance with its medium-term budgetary objective of a structural deficit no higher than 0.5% of GDP, which it fulfilled already last year; in fact, Germany expects to remain safely below this ceiling throughout the entire projection period to 2017. The debt-to-GDP ratio – which rose markedly due to the stabilisation measures taken in response to the financial and European sovereign debt crisis – is forecast to decline markedly to below 70% by the end of the Stability Programme's time frame in 2017.

The federal budget has improved in structural terms substantially as well. Since 2011, structural net borrowing is the basis for measuring compliance with the "debt brake" enshrined in Article 115 of the Basic Law, Germany's constitution. Under the debt brake, the Federation's structural deficit from 2016 onwards is not permitted to exceed 0.35% of GDP. Already in 2012, however, structural net borrowing stood at just 0.31% of GDP. This means that the Federal Government already succeeded in complying with the permanent upper limit in just the second year that the debt brake was in effect, and four years earlier than prescribed by law. According to the plans laid down in the 2013 Budget Act, this year's outcome will also remain below the upper limit. In fact, the benchmark figures for the 2014 federal budget and financial plan to 2017, which were approved by the Federal Cabinet on 13 March 2013, envisage no structural net borrowing at all. This means that structural net borrowing for these years will be well below the debt brake's upper limit that applies from 2016 onwards. Contingent upon the stable performance of the overall economy, the Federation aims to bring net borrowing down to zero already from 2015 onwards. The Federal Government is setting a fiscal policy milestone with these benchmarks.

Germany's 2013 National Reform Programme, which is prepared in tandem with the Stability Programme, depicts the progress that Germany has made in meeting the Europe 2020 growth strategy targets, implementing the country-specific recommendations for 2012, and pursuing the Action Programme 2012 for the Euro Plus Pact. Those measures in the National Reform Programme that have a fiscal impact also form part of the Stability Programme's fiscal strategy and public budget projection.

2. German fiscal policy in the European context

2.1 Fiscal policy guidelines and recommendations in the context of the European Semester

The European Semester aligns various processes of economic and fiscal policy coordination in the EU. The term "semester" refers to the fact that Member State budgetary and economic policies are coordinated and reviewed at European level during the first half of each year. During the second half of the year, Member States then implement corresponding requirements and agreements targeting budget planning and structural reforms. Each year's European Semester is launched by the Commission's Annual Growth Survey, which is published at the end of the preceding year. The Semester concludes in summer with the Council's country-specific recommendations to the Member States. These recommendations are proposed by the Commission and are based on an assessment of the National Reform Programmes and Stability/Convergence Programmes of the Member States.

In the area of fiscal policy, the Council recommended in July 2012 that Germany take action within the 2012-2013 period to "continue with sound fiscal policies to achieve the MTO by 2012. To this end, implement the budgetary strategy as envisaged, ensuring compliance with the expenditure benchmark as well as sufficient progress towards compliance with the debt reduction benchmark. Continue the growth-friendly consolidation course through additional efforts to enhance the efficiency of public spending on healthcare and long-term care, and by using untapped potential to improve the efficiency of the tax system; use available scope for increased and more efficient growth-enhancing spending on education and research at all levels of government. Complete the implementation of the debt brake in a consistent manner across all *Länder*, ensuring timely and relevant monitoring procedures and correction mechanisms."

Just prior to this, in May 2012, the Ecofin Council closed the deficit procedure for Germany after Germany had succeeded in bringing its deficit below the reference value of 3% of GDP two years earlier than required under the Council's recommendations.

Drawing on the most recent Annual Growth Survey, the Ecofin Council emphasised in February 2013 that sound and sustainable public finances are an essential prerequisite for confidence in a country's macroeconomic stability and therefore also for growth. It further stressed that Member States should adhere to their commitments in accordance with the rules of the Stability and Growth Pact. At the same time, the Council underscored the importance of well-designed fiscal frameworks, stating that credible fiscal adjustment strategies play a key role in enhancing confidence. This includes measures to increase the efficiency and effectiveness of spending. In particular, a priority should be placed on investments in education, research, innovation and energy, with policy-makers taking steps to ensure – and where necessary improve – the efficiency of these investments. In the area of tax policy, the Ecofin Council called on Member States to consider reducing the tax burden on labour, broadening tax bases, and eliminating unwarranted or harmful subsidies.

In the 14 March 2013 conclusions of the European Council, the EU heads of state and government provided the Member States with guidelines on this year's European Semester and emphasise the necessity of pursuing differentiated, growth-friendly fiscal consolidation. The European Council also called for continued progress towards structurally balanced budgets, stating that fiscal consolidation needs to go hand-in-hand with structural reforms to foster growth and jobs.

2.2 European and national fiscal policy framework

Germany's fiscal policy framework integrates European requirements and national rules. The debt brake, which was enshrined into the Basic Law in 2009, upholds the spirit of the Stability and Growth Pact and reinforces the binding effect of European rules by placing these rules within the framework of the national constitution. This is also in line with one of the basic ideas behind the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (Fiscal Compact): namely, to adopt binding and permanent national rules – preferably at constitutional level – for jointly agreed commitments. Given the close linkage between European and national institutional frameworks, this section discusses both aspects jointly.

As part of the Stability and Growth Pact, which applies to all government levels (in Germany, this means the Federation, *Länder*, municipalities and social security funds), Member States set their own medium-term budgetary objectives (MTOs) within the framework of prescribed limits. Germany set itself the MTO of a structural deficit no higher than 0.5% of GDP. This is in line with the Fiscal Compact.

When the Stability and Growth Pact was reinforced in 2011, a new expenditure benchmark was introduced to assess whether a Member State's adjustment path was sufficient to achieve its MTO or, if the MTO had already been achieved, whether a Member State's spending levels allowed it to remain in compliance with the MTO. According to this expenditure benchmark, expenditure growth (adjusted for interest payments, in particular) should in principle not exceed the medium-term potential growth rate.

The reinforced Stability and Growth Pact also introduced a benchmark for reducing excessive debt-to-GDP ratios, which was also enshrined in the Fiscal Compact. Under this "1/20 rule", Member States whose debt-to-GDP ratios exceed the reference value of 60% must reduce the gap between their debt levels and the 60% reference by an average of one-twentieth per year. Failure to comply with this benchmark can lead to the launching of an excessive deficit procedure. Germany's debt-to-GDP ratio currently exceeds the reference value by roughly 20 percentage points. This means that, under the 1/20 rule, Germany is required to reduce its debt-to-GDP ratio by approximately 1 percentage point per year on average. This benchmarking measurement is based either on the reductions achieved during the previous three years or on Commission forecasts for the previous year and the upcoming two years. For those Member States – including Germany – that were subject to an excessive deficit procedure at the time when the reinforced Stability and Growth Pact was adopted (November 2011), the 1/20 rule applies as of the third year following abrogation of the deficit procedure. This means that the rule will apply to Germany starting in 2015. During the transition period, sufficient progress must be achieved to ensure compliance with the 1/20 rule once the three-year period has passed. This condition is deemed to be satisfied if a Member State plans to reduce its structural deficit accordingly, at a minimum in accordance with a linear reduction path determined by the Commission. Significant deviations from this reduction path can result in the opening of an excessive deficit procedure. By more than meeting its MTO, Germany has fulfilled the condition of sufficient progress towards compliance with the 1/20 rule by 2015.

By enshrining the debt brake into its constitution, Germany has set stringent, stability-oriented limits on new borrowing by the Federation and the *Länder*, in line with the requirements of the Stability and Growth Pact. Accordingly, the Federation and the *Länder* must achieve generally balanced budgets. For the Federation, this condition is fulfilled when its structural net borrowing does not exceed 0.35% of GDP. When the debt brake took effect in 2011, public finances were still considerably burdened by the costs of the financial and economic crisis. For this reason, the 0.35% ceiling does not apply until 1 January 2016. Until that date, the structural deficit from fiscal year 2010 must be reduced in regular increments. Compliance with this rule is also monitored in the budget execution process on the basis of a control account. If a negative threshold is exceeded on the control account, this excess amount must be reduced in a cyclically appropriate manner by setting lower ceilings on net borrowing in subsequent years.

Länder budgets are to be balanced with zero net borrowing. The *Länder* have the option of adjusting revenues and expenditures for cyclical factors if a corresponding legal basis is established at Land level. They are also entitled to a transitional period: *Länder* budgets must be planned in such a way that the balanced budget requirement is satisfied by 2020.

While the design of *Länder* budget rules lies at the discretion of the *Länder* themselves, these rules must remain within the parameters laid down in the Basic Law regarding permissible exceptions and possibilities for taking cyclical factors into account. Moreover, the ban on new borrowing enshrined in the Basic Law is directly binding on the *Länder*. This means that the ban applies without exception to all *Länder* from 2020 onward, whether or not they have adopted more detailed legal provisions at Land level.

For the period up to 2019, five of the 16 German *Länder* (Berlin, Bremen, Saarland, Saxony-Anhalt and Schleswig-Holstein) are receiving consolidation assistance totalling €800 million per year. This assistance is being provided to help those *Länder* facing especially difficult fiscal circumstances and is financed in equal shares by the Federation and the *Länder*. To obtain assistance, the recipient *Länder* must reduce their 2010 structural deficits in regular increments to zero by the year 2020.

Municipalities are prohibited from borrowing to finance current expenditures; the only exception here allows for borrowing to cover short-term liquidity problems. However, loans may be taken out to finance investments, as long as the debts can be successfully serviced in subsequent years.

Likewise, social insurance funds are also prohibited from borrowing. Deficits in the social insurance funds can be paid for by reserves built up through revenues (contributions and federal grants) or by adjustments to contribution rates; for statutory pension insurance, such rate adjustments must be carried out in accordance with fixed criteria. Differences between revenues and expenditures in the miners' pension insurance system are offset by the Federation. Deficits run by the Federal Employment Agency may be covered by loans from the Federation, which must then be paid back in subsequent years.

In addition to these rules, federal and *Länder* budgets are monitored by the Stability Council, which commenced operation in 2010. The Stability Council coordinates budgetary and financial planning by the Federation and the *Länder*; key aims here are to uphold compliance with European commitments, to catch potentially adverse developments at an early stage, and to ensure that corrective measures are taken. The Council's independence is assured, among other things, by its voting rules: to be adopted, decisions require the Federation's vote plus the votes of two-thirds of the *Länder*, and the Land affected by the decision is not entitled to vote. Decisions affecting the Federation require a two-thirds majority of all voting members to be adopted. The Stability Council also monitors whether the *Länder* receiving consolidation assistance are complying with their agreed deficit ceilings and, based on the findings of this monitoring process, decides whether individual *Länder* should be granted continued assistance. Last year's review found that all of the affected *Länder* complied with their consolidation requirements. Regional governments facing a budget crisis coordinate fiscal consolidation measures with the Stability Council in order to prevent adverse developments and restore long-term fiscal health. The Stability Council has set up fiscal consolidation programmes with Berlin, Bremen, Saarland and Schleswig-Holstein and monitors compliance with these programmes on an ongoing basis. As part of the consolidation process, these *Länder* – which are also recipients of consolidation assistance – must not only provide proof that they have cut their deficits as agreed but must also present in advance the deficit-reducing measures they plan to adopt in order to achieve their consolidation targets.

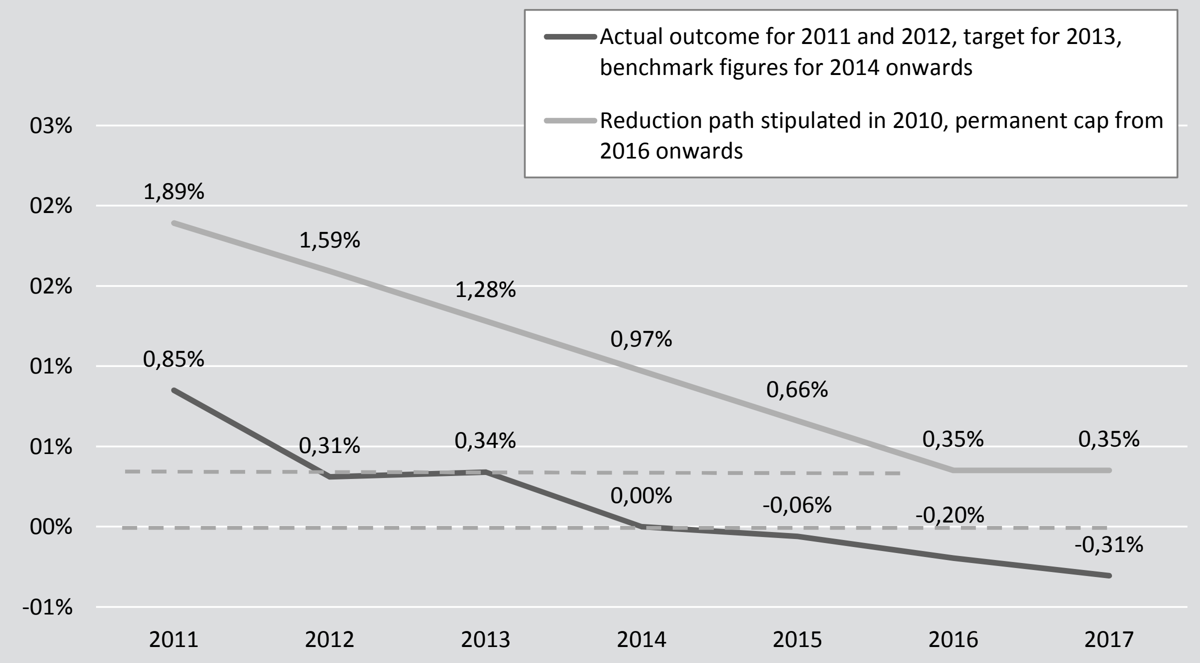
With the debt brake now enshrined in the constitution and additional provisions laid down in ordinary legislation, Germany has established rules that are geared toward compliance with the requirements of the Stability and Growth Pact as well as the Fiscal Compact. Moreover, the Federal Government has introduced legislation on the domestic implementation of the Fiscal Compact that supplements existing fiscal policy rules with an additional mechanism to prevent and correct adverse fiscal developments at all government levels. The plan here is to codify Germany's medium-term budgetary objective – i.e., capping general government structural new borrowing at 0.5% of GDP in line with the Fiscal Compact and the Stability and Growth Pact – into domestic law as part of the Budgetary Principles Act (*Haushaltsgrundsätzegesetz*). The Stability Council will be explicitly authorised to monitor compliance with this upper limit and to recommend suitable measures for eliminating excessive deficits. In so doing, it will take into account the recommendations put forward by the Ecofin Council as part of the preventive arm of the Stability and Growth Pact. The Stability Council's recommendations will be forwarded by the Federal and *Länder* governments to their respective parliaments. A new, independent council is to be established that will assist the Stability Council in monitoring compliance with the borrowing cap. These supplementary rules are also suitable for ensuring compliance with the debt brake – as required in the country-specific recommendations – through the adoption of additional control and correction mechanisms.

2.3 Germany's voluntary fiscal policy commitments within the Euro Plus Pact

Within the framework of the Euro Plus Pact, Germany committed itself last year to achieving its medium-term budgetary objective under the Stability and Growth Pact already in 2012, and to beating the debt reduction target for the federal budget in 2013 as well.

In 2012, the general government structural balance showed a surplus of 0.4% of GDP, thereby easily achieving the medium-term budgetary objective of a structural deficit no higher than 0.5% of GDP. Furthermore, in 2012 the Federation clearly beat its reduction target under the debt brake; even more, it succeeded in holding structural net borrowing below 0.35% of GDP – i.e., below the constitutionally stipulated permanent upper limit that does not apply until 2016. The target figure for structural net borrowing in 2013 is also slightly below 0.35% of GDP, which means that Germany plans to comply with the permanent borrowing cap and to beat its debt reduction target this year as well (see Figure 1).

Figure 1: Structural net borrowing by the Federation under the debt brake (% of GDP)



Furthermore, last year the Federal Government committed itself to reducing the tax burden caused by fiscal drag; it will do so by adjusting income tax rates in two steps – on 1 January 2013 and 1 January 2014. To this end, in late February 2013 legislation went into effect that raises the basic personal allowance for income tax in two steps, the first in 2013 and the second in 2014. (see also chapter 4.2). Legislative plans to reduce fiscal drag even further were unable to win over a majority of the Bundesrat. However, in the future the Federal Government will issue a bi-annual report analysing the effects of fiscal drag.

Other voluntary commitments made by the Federal Government included (i) improving macroprudential supervision in early 2013 by enacting legislation to improve German financial supervision, and (ii) temporarily reactivating the Financial Market Stabilisation Fund (SoFFin) until the end of 2012 in order to safeguard the stability of financial markets even in the event of a systemic crisis. Both of these commitments have been fully implemented. Furthermore, the Bundestag decided in November 2012 to extend SoFFin until the end of 2014.

On 20 March 2013, Germany adopted its Action Programme 2013 for the Euro Plus Pact. The Federal Government remains steadfastly committed to policies of growth-friendly consolidation. For 2014, it plans to draft a federal budget with no structural deficit.

In order to reinforce both the debt brake and general fiscal discipline, the Federal Government will take steps to ensure that any positive balance on the control account that has accumulated by the time the transitional period expires at end 2015 cannot be offset by negative account entries in the future. The Federal Government aims to enact legislation to this effect in 2013. A positive balance has accumulated on the control account during the past two years, because the deficit has come in below the debt brake cap that applies during the transitional period.

In addition, the Federal Government intends to further enhance the stability of financial markets. It aims to do this in particular by (i) simplifying procedures to wind up and restructure credit institutions and financial groups, (ii) requiring higher-risk activities to be separated from deposit-taking activities, and (iii) introducing clear criminal liability rules for bank and insurance company executives who violate their duties.

These and other commitments contained in the German Action Programme for the Euro Plus Pact are described in the 2013 National Reform Programme.

3. Economic situation and outlook

3.1 Macroeconomic situation in Germany in 2012

Germany's economy proved relatively robust in 2012 despite the euro area's weak economic performance. The German economy expanded for the third year in a row, although real GDP growth – at 0.7%– was noticeably weaker than in the preceding two years. This was mainly due to the slowdown in economic momentum over the course of the year. While first-quarter GDP expanded by 0.5% over the previous quarter (price, calendar and seasonally-adjusted), overall economic activity contracted considerably over the course of the fourth quarter.

The tangible slowdown in global economic growth was a key factor in dampening the German economy's performance. In addition, the uncertainty of market participants resulting from high levels of sovereign debt in advanced economies – especially in the euro area – apparently had a highly adverse impact on the German business sector's propensity to invest. For example, investment in machinery and equipment fell sharply on average in 2012 for the first time since 2009 (by 4.8% on the year, in real terms). In contrast, net exports boosted growth in 2012, led in particular by demand from countries outside the euro area. However, due to noticeably weaker growth especially in Europe, real exports increased at a slower pace than in 2011. Weaker exports and declining investment also weighed on imports. Imports expanded at a much more sluggish rate than exports on average in 2012, thereby boosting – in purely mathematical terms – the contribution of net exports to overall growth. An increase in private consumption (by 0.6% on the year in real terms) also helped drive growth. Private consumption was lifted by solid employment growth and higher wages, which gave a perceptible boost to household disposable income. Overall, the labour market performed well in 2012. As the year progressed, however, the loss of economic momentum began to have an impact. Registered unemployment averaged 2.9 million in 2012, about 80,000 lower than the average for 2011. Employment growth also slowed down considerably over the course of last year. Nevertheless, total employment still hit a new record high in 2012, averaging 41.6 million (up by 449,000 on the year). The number of people in jobs requiring social insurance contributions was up by more than half a million and thus grew much more markedly than employment as a whole. The consumer price index rose on average by 2.0% in 2012, a somewhat slower rate than in 2011. As in 2011, inflation in 2012 was driven primarily by the marked increase in prices for energy products.

3.2 Short- and medium-term outlook for the overall economy, 2013-2017

The positive turnaround in a number of sentiment indicators supports the Federal Government's assessment that the marked decline in German GDP in the final quarter of 2012 is likely to be a temporary cyclical slowdown. The global economy is expected to regain momentum over the course of 2013, and this is likely to give a new boost to German companies' sales prospects on export markets. Furthermore, monetary policy remains clearly expansionary for Germany. Financing conditions for investment are highly favourable, not least due to the fact that companies currently enjoy excellent conditions for self-financing. Thus in qualitative terms, the Federal Government's view of the economic outlook is consistent with that of the European Commission. For 2013, the Federal Government's annual projection expects overall economic activity to expand by 0.4% in real terms. This year's average rate of real GDP growth is markedly lower than last year's, particularly due to a carry-over effect that will have in statistical terms a negative influence on the annual growth rate in 2013. As the year progresses, seasonally adjusted current annual growth rates are expected to surpass the potential growth rate.

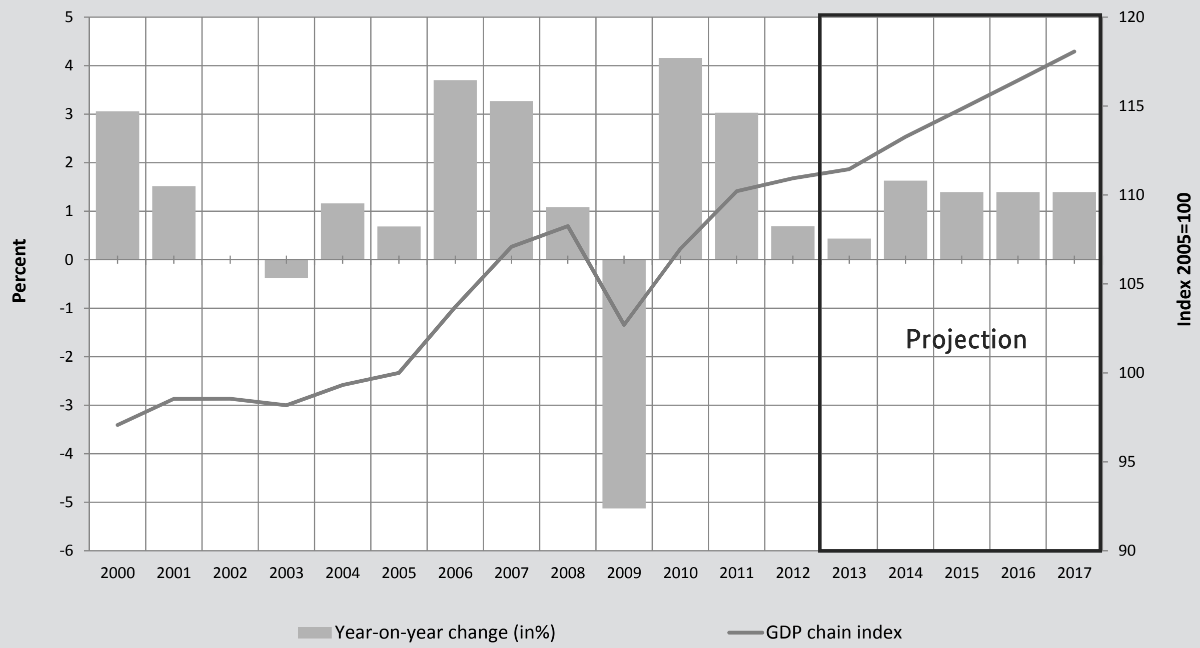
The stimulus from foreign trade and investment is likely to be considerably weaker in 2013 than it was last year. This trend has been taking shape since the final quarter of 2012. As a result, overall economic growth is expected to be driven mainly by domestic demand. In particular, the ongoing sluggishness of economic activity in the euro area – the destination of just under 40% of German exports – will cloud the foreign trading activities of German firms. However, export business is likely to bounce back over the course of the year as the global economy gains momentum. Accordingly, exports are expected to grow at a moderate tempo in 2013 (by 2.8% in real terms). Real imports are also projected to increase this year – by 3.5% on average – as domestic demand rises. This means that net exports are likely to make a slightly negative contribution to growth (−0.1 percentage points). At the same time, domestic demand is expected to boost growth by 0.6 percentage points. In particular, investment activity is likely to pick up substantially over the course of this year. As a result, the Federal Government anticipates that real gross fixed capital formation will increase by 0.5% on average in 2013. At the same time, construction investment is projected to climb by 1.3%. Given the negative impact of 2012 figures on statistical calculations for 2013, investment in machinery and equipment is expected to post a decline of 1.3% on average this year, but this apparent decrease disguises what is expected to be a swift recovery in investment activity following a slow patch at the start of the year.

Private consumption will again play a substantial role in supporting growth this year. Consumer expenditure is projected to post a 0.6% year-on-year increase in 2013. Given the marked increase in household disposable income (+2.3%) – lifted by sustained high levels of employment and rising incomes – favourable conditions are in place for the further expansion of private consumption. The labour market remains in solid shape in 2013 and total employment is expected to expand slightly by 15,000. At the same time, the number of unemployed persons will probably rise marginally as well (on average by 60,000 to a total of 2.96 million). This translates into an unemployment rate of 7.0%. Moderate price trends are also expected to bolster the purchasing power of private households and thereby lift consumer spending this year. The consumer price index is projected to rise by 1.8% on average in 2013, slightly down from the increase posted in 2012.

Thanks to the sustained economic upswing of the past three years, the output gap was nearly closed in 2012, even though GDP still remained slightly below the level of output that would signify normal economic conditions (potential output). Against the backdrop of the short-term growth projections, the under-utilisation of capacity in the economy as a whole will be more marked in 2013. However, it is assumed that the resulting negative output gap will close gradually over the medium-term projection period to 2017, when overall capacity utilisation is expected to return to normal.

The Federal Government expects the upswing to continue in 2014, with real GDP expanding by 1.6%. Furthermore, the Federal Government's medium-term projection for the 2015-2017 period assumes average annual GDP growth of approximately 1 1/2% (see Figure 2). The potential growth rate for the same period is estimated at just under 1 1/4% per year on average, although the growth rate is expected to slow down over the course of the projection period due to demographic factors. Positive trends on the labour market are projected to continue over the medium term, even though employment levels are expected to grow at a noticeably slower rate than during the past three years. The number of unemployed persons is forecast to fall to approximately 2.8 million by 2017. Structural unemployment is also expected to keep declining during the projection period.

Figure 2: Gross domestic product, in real terms



The medium-term projection expects the main stimuli for growth to come from domestic demand. In particular, private consumer demand is expected to make positive contributions to growth given the strong state of the job market, tangible increases in household disposable income and ongoing moderate price trends. In contrast, net exports will probably have a largely neutral impact on GDP growth in purely statistical terms, as the growth in imports resulting from robust overall demand is likely to slightly outweigh the increase in exports.

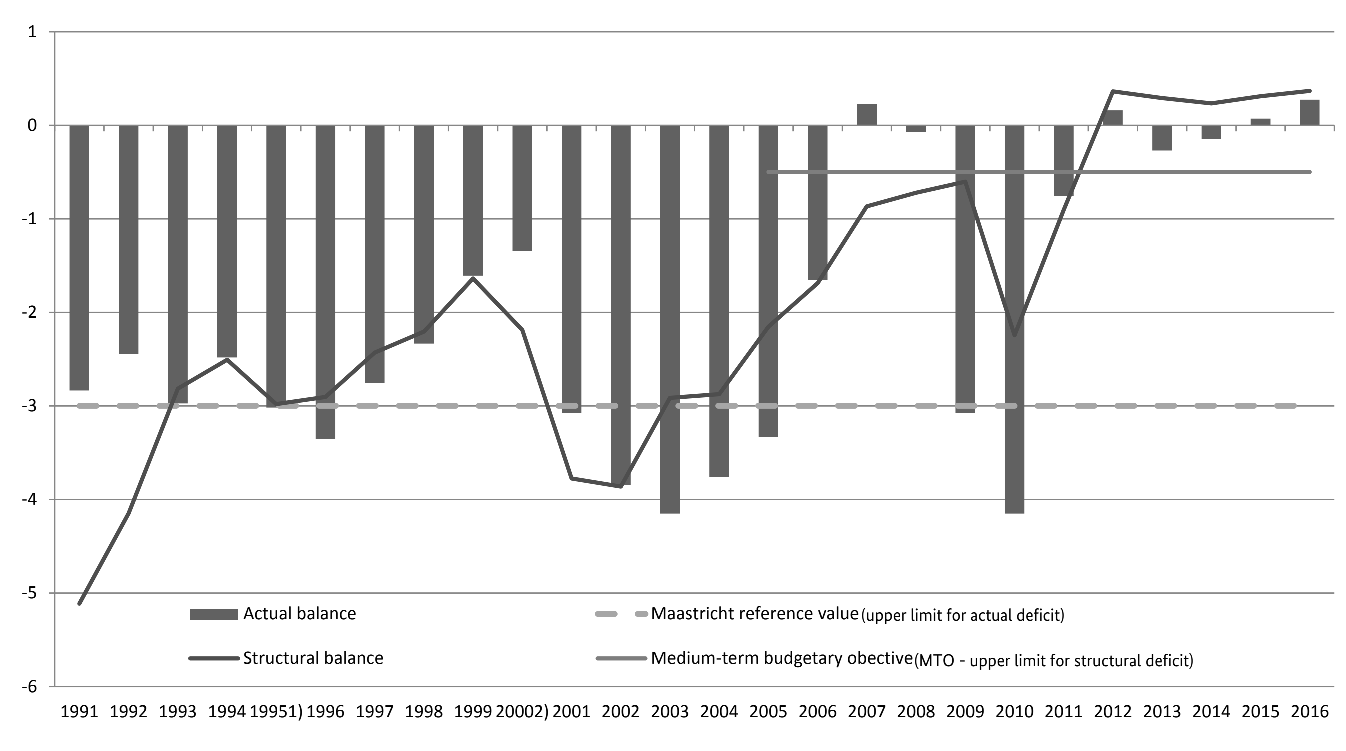
4. Fiscal policy in Germany

Germany is committed to a policy of growth-friendly consolidation. Sound public finances engender confidence. Together with a competitive economy, they lay the foundation for sustained growth and high levels of employment, which in turn boost the consolidation of government finances. This positive dynamic is demonstrated by developments in Germany in recent years. Employment and incomes are rising, while new borrowing – and interest payments in particular, thanks to the Federal Government's credible consolidation policies – are trending downward. Germany will continue to pursue growth-friendly consolidation both persistently and decisively, and it will consistently uphold the commitments it makes at national, European and international level. At the same time, the Federal Government is setting clear priorities in forward-looking policy areas and is continuously boosting its investments in the areas of education, research and infrastructure.

4.1 Fiscal situation and strategic direction

In recent years, Germany has made substantial progress in consolidating public finances. Cyclical increases in revenue have been used consistently to drive down deficits. While government budgets in 2009 and 2010 reflected the effects of the financial and economic crisis and concomitant stimulus measures, the return to a course of consolidation in 2011 produced immediate and tangible successes as both the actual and structural deficit declined markedly (see Figure 3). As a result, Germany brought its deficit below the reference value of 3% of GDP two years earlier than required, and the excessive deficit procedure against Germany was abrogated already in 2012.

Figure 3: Actual and structural general government balance (in % of GDP)

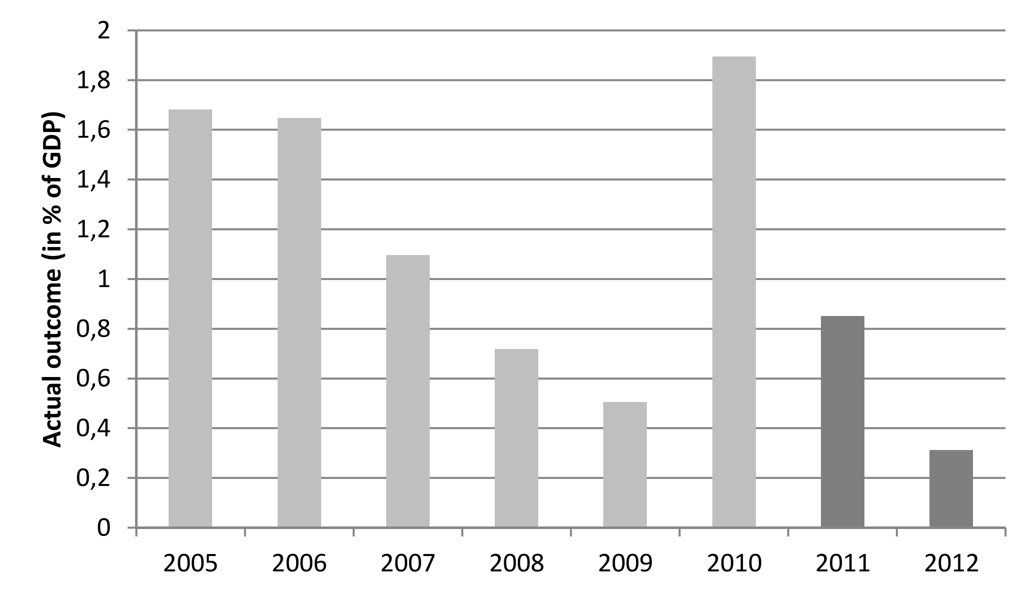


1. Excluding asset transfers resulting from the assumption of debts of the Treuhand privatisation agency and German Democratic Republic housing companies. When this effect is included, the general government deficit amounted to 9.5% of GDP.
2. Excluding UMTS proceeds. When this effect is included, the general government budget ran a surplus of 1.1% of GDP.

In that same year, Germany's general government finances posted a structural surplus for the first time since reunification. The general government's structural balance – i.e., adjusted for cyclical and one-off effects – stood at +0.4% of GDP. This means that Germany has easily achieved its medium-term budgetary objective of a structural deficit no higher than 0.5% of GDP. In fact, the structural balance improved even more than the actual balance, which was also in positive territory at +0.2% of GDP. As a result, Germany fulfilled both its voluntary commitment under the Euro Plus Pact as well as last year's country-specific recommendation on the medium-term budgetary objective. Germany will clearly meet its medium-term budgetary objective in the coming years as well.

The federal budget is in much better structural condition as well (see Figure 4). Since 2011, structural net borrowing is the basis for measuring compliance with the "debt brake" enshrined in Article 115 of the Basic Law, Germany's constitution. From 2016 onwards, the Federation's structural deficit is not permitted to exceed 0.35% of GDP. Already in 2012, however, structural net borrowing stood at just 0.31% of GDP. This means that the Federal Government already succeeded in complying with the permanent upper limit in just the second year that the debt brake was in effect, and four years earlier than prescribed by law.

Figure 4: Structural net borrowing by the Federation



Federal structural net borrowing outcomes if the debt brake had applied prior to 2011.

The Federal Government intends to continue surpassing the requirements stipulated under the debt brake. Its 2013 target for structural net borrowing is also below the ceiling of 0.35% of GDP. On 13 March 2013, the Federal Cabinet adopted benchmark figures for the 2014 federal budget and the financial plan to 2017. According to these benchmarks, Germany will achieve a structurally balanced federal budget in 2014. Contingent upon the stable performance of the overall economy, the Federation aims to bring net borrowing down to zero from 2015 onwards and even to achieve structural surpluses. The Federal Government is setting a fiscal policy milestone with these benchmarks.

The benchmark figures serve as the basis for the government's internal budget drafting process, which will conclude in June 2013 with the Federal Cabinet's decision on the government draft of the 2014 federal budget and the financial plan to 2017. This process will take into account the most current forecasts, particularly (i) the Federal Government's spring projection on the medium-term development of the overall economy (to be published on 25 April 2013) and (ii) the findings of the Working Party on Tax Revenue Estimates, which will be based on the spring projection. The Working Party will convene on 6-8 May 2013. After the Federal Cabinet takes its decision, the draft budget will be brought before the German Bundestag and forwarded to the Bundesrat.

Germany will also comply with the consolidation targets set out in the G20 Toronto Summit Commitments, which were agreed in 2010 and reaffirmed in 2012. These commitments include cutting deficits in half by 2013 and stabilising or reducing government debt-to-GDP ratios by 2016.

4.2 Key fiscal policy measures on the expenditure and revenue side

Successful consolidation is always based on economic and fiscal policies that are geared toward growth. Successful consolidation is not achieved through mechanical deficit cuts; instead, it is necessary to establish clear priorities and to leverage efficiency reserves that then lead to savings while simultaneously enhancing the conditions for economic growth. On the expenditure side, the Federal Government has set targeted priorities in the areas of education, research and infrastructure in order to boost long-term growth drivers. Nevertheless, according to the benchmark figures decision taken on 13 March 2013, government spending up to 2017 will increase at a lower rate than real GDP growth. Higher revenues will continue to be resolutely deployed for the purpose of reducing net borrowing.

In its country-specific recommendations, the Council called on Germany to "use available scope for increased and more efficient growth-enhancing spending on education and research at all levels of government." In this connection, the Federal Government has exceeded its target of investing an additional €12 billion in education and research during the current legislative period – the actual figure stands at over €13 billion to date. Overall, public and private expenditure on research and development in relation to GDP has continued to expand in recent years: in 2011, R&D spending amounted to just under 2.9% of GDP. This puts Germany well above the EU average of 2% and close to the Europe 2020 target of 3%. Additional measures that Germany is taking to make public spending more effective and growth-friendly are outlined in chapter 7.

A high-quality infrastructure is one of the essential keys to Germany's economic competitiveness. For this reason, the Federal Government has earmarked an additional €750 million for investments in federal transport infrastructure, primarily for new construction projects and upgrades. The funds will be disbursed starting in 2013 as part of the government's second infrastructure acceleration programme.

Ensuring sound public finances over the long term requires competitive and sustainable economic structures, together with well-financed social insurance systems that are capable of withstanding demographic change. Measures taken by the Federal Government in this area are described in chapter 6, which focuses on the sustainability of public finances.

The growth-friendly fiscal consolidation of recent years, together with positive trends in wages and employment, have made it possible this year not only to cut the deficit but also to implement a considerable reduction in taxes, social insurance contributions and fees. In 2013, the Federal Government will provide companies and private citizens with cost cuts totalling nearly €8 billion.

In February, new legislation to reduce fiscal drag took effect that will reduce income tax burdens. Under this legislation, the basic personal allowance will be increased in two steps – to €8,130 in 2013 and €8,354 in 2014 – in order to bring it into line with the rise in minimum subsistence income. This will reduce the cost burden on taxpayers by €0.9 billion in 2013 and by an annual €2.6 billion from 2014 onwards. At the same time, the basic tax rate will be held constant at 14%. The resulting reduction in tax revenue has been accounted for in the government's budgetary and financial plans.

With effect from 1 January 2013, the contribution rate to the general pension insurance scheme was further reduced from 19.6% to 18.9%, and the contribution rate to the miners' pension insurance scheme was further reduced from 26.0% to 25.1%. This measure relieves the contribution burden on employees and businesses by €3.2 billion each in 2013; furthermore, it reduces the financial burden on federal, *Länder* and municipal governments. The elimination of the mandatory quarterly medical consultation fee as of 1 January 2013 provides additional relief amounting to roughly €2 billion per year to individuals and lightens the bureaucratic burden on medical practitioners and health insurance funds.

Newly enacted legislation to amend and simplify business taxation and travel expenses law will make business taxation more conducive to growth and competition. For example, revenue-neutral rules simplifying consolidated tax-filing arrangements will ease the burdens on revenue authorities and taxpayers. In addition, an increase in the loss carryback will provide companies with extra liquidity in periods of crisis. Furthermore, simplified tax rules on travel, meals and accommodation expenses will contribute to bureaucracy reduction.

5. Projection of general government balance and debt until 2017

In the coming years, trends in Germany's general government budget balance and debt level[1)] will be shaped by the positive structural conditions that have been put in place thanks to the government's fiscal consolidation policies and the favourable performance of the economy. Up to 2017, Germany will meet its medium-term budgetary objective, remaining safely below its target of a structural deficit no higher than 0.5% of GDP. Likewise, the debt-to-GDP ratio – which rose sharply from 2008 onwards due to the stabilisation measures taken in response to the financial crisis and the European sovereign debt crisis – is expected to decline markedly to below 70% by the end of the Stability Programme's time frame in 2017[2)].

5.1 Trends in general government revenue and expenditure

Revenue ratio will remain stable

Apart from the distortions resulting from the steep recession in 2009, the government revenue ratio – i.e., the ratio of government revenue to GDP – has risen steadily in recent years, reaching 45.2% in 2012, its highest level since the year 2000. This is due primarily to the rising tax-to-GDP ratio which, after falling sharply at the start of the new millennium, now stands at 23.4%, nearly the same level as in 2000. While the current tax-to-GDP ratio has returned to basically the same level as in 2000, it is now drawn from a broader tax base. This reflects the more growth-friendly policy environment as well as the German economy's high level of competitiveness. Furthermore, the tax-to-GDP ratio has been boosted by (i) the addition of new taxes such as the nuclear fuel duty and the aviation tax as well as (ii) proceeds from the auctioning of CO2 emissions allowances and the bank levy, which count as tax revenue under the system of national accounts. In 2012, tax revenue increased at a dynamic pace for the second year in a row, up 4.9%. This momentum will slow down over the course of the projection period. Nevertheless, tax receipts will continue to increase at a faster pace (roughly 3% per year on average) than nominal GDP because domestic demand – which is more tax-intensive – will make a larger contribution to overall economic activity in the medium term. The tax-to-GDP ratio will post a negligible increase, remaining stable at approximately 23 1/2% (Table 1).

1. Where not otherwise specified, all data are based on the National Accounts definition (Maastricht definition) and encompass core budgets and extra-budgetary entities.
2. The projection of general government accounts was completed on 9 April 2013.

In contrast, social insurance contributions, which constitute the second major component of public revenue, have declined markedly in relation to GDP over the past 12 years, falling from 18.6% to 17.0%. This is due in part to the fact that contribution rates have been reduced by net 1.6 percentage points since 2000. Thanks to the positive development of the sustainability reserve, the government was able to reduce the contribution rate to statutory pension insurance again in 2012. This more than compensated for the minor increase in the contribution rate to long-term care insurance, which rose one-tenth of a percentage point to 2.05%.

Table 1: Trends in the government revenue ratio

	2012	2013	2014	2015	2016	2017
			- % of GDP -			
Tax ratio	23.4	23 1/2	23 1/2	23 1/2	23 1/2	23 1/2
Social contribution ratio	17.0	17	16 1/2	16 1/2	16 1/2	16 1/2
Tax & social contribution ratio	40.4	40 1/2	40	40 1/2	40 1/2	40 1/2
Total revenue						
April 2013 Update	45.2	45	45	45	44 1/2	44 1/2
April 2012 Update	45	44 1/2	44 1/2	44 1/2	44 1/2	-

Any differences between (i) the “tax and social contribution ratio” and (ii) the sum of the “tax ratio” and the “social contribution ratio” are due to rounding; projection figures are rounded to half.

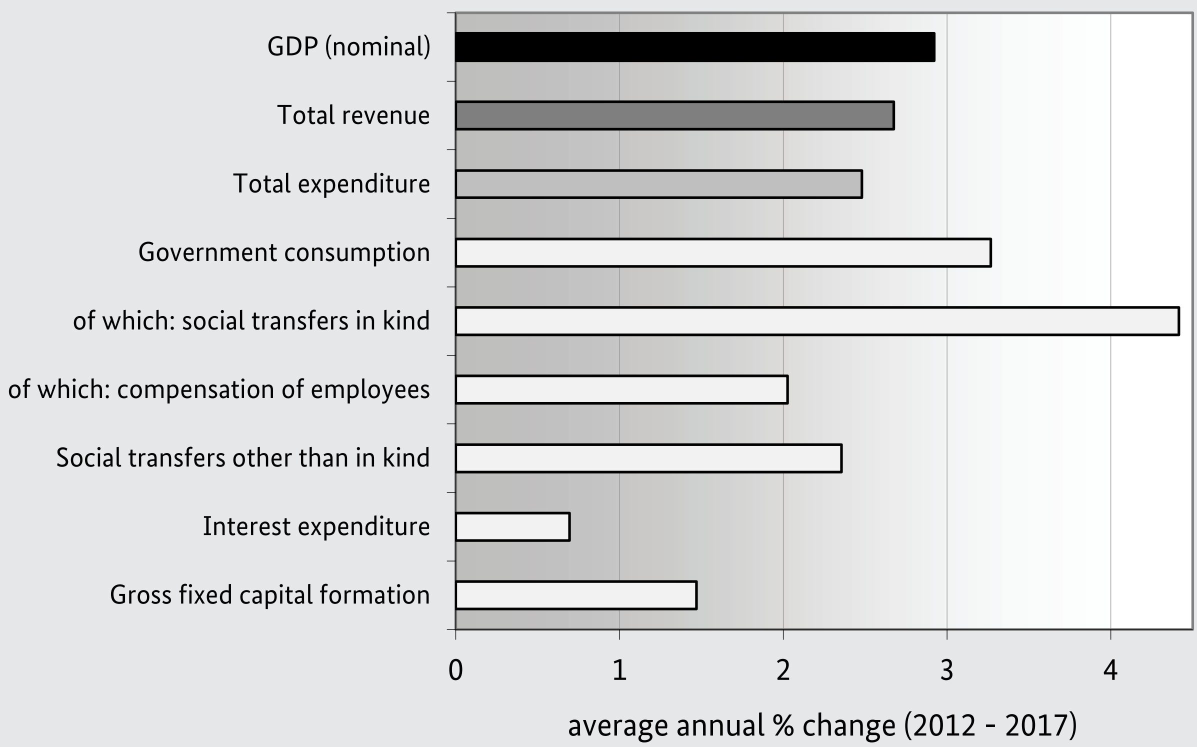
Given these trends in the tax ratio and the social contribution ratio, the total tax ratio – i.e., the sum of taxes and social insurance contributions as a percentage of GDP – is expected to register 40% to 40 1/2% during the projection period. The revenue ratio – which also includes miscellaneous government revenue such as fees and revenue from business activities (e.g., profit transfers from the Deutsche Bundesbank) – will decline slightly to approximately 44 1/2% by 2017, as miscellaneous revenue is expected to expand somewhat more slowly in relation to GDP.

Expenditures will increase at a lower rate than nominal GDP

Government expenditure grew by only 1.3% in 2012. This figure would be even lower – just 1.0% – if the €3.1 billion capital transfer in connection with the restructuring of WestLB were excluded. The small size of the expenditure increase is attributable mainly to the government’s fiscal consolidation policies and the ongoing positive performance of the labour market. For example, low interest rates caused interest payments to fall. In addition, gross capital formation declined due to the expiration of economic stimulus programmes. At the same time, social benefits other than social transfers in kind increased at a very moderate pace.

During the projection period, general government expenditure is expected to rise by an average of 2 1/2% per year. Government consumption expenditure is projected to rise at an above-average rate of just under 3 1/2% per year on average (Figure 5) and to comprise roughly 45% of total government expenditure in 2017. In general, this above-average rate of increase will be due to the sharp rise in social transfers in kind (particularly in the areas of long-term care insurance and statutory health insurance) which are expected to grow by nearly 4 1/2% per year on average. In contrast, compensation of employees is projected to rise at a below-average rate of about 2% per year. The other key categories of expenditure are expected to increase at a below-average rate as well. Of these, the largest increase will be posted by social benefits other than social transfers in kind, which are expected to grow by just under 2 1/2% per year. Likewise, gross capital formation will expand only moderately during the projection period, by about 1 1/2% per year. This will contrast with the years from 2009 to 2011, when gross capital formation grew sharply as a result of measures implemented in connection with the government's economic stimulus packages. After declining in 2012 due to the expiration of these measures last year, gross capital formation will increase again, returning to 2011 levels by the year 2017. The government's credible fiscal consolidation policies have paid off in the form of low interest rates. Furthermore, because the coming years will see a marked decline in net borrowing and even a return to surplus in the medium term, interest payments are expected to rise by only about 1/2% per year on average in the period from 2012 to 2017.

Figure 5: Average annual trends in general government revenue/expenditure and GDP trends from 2012 to 2017



In the medium term, moderate expenditure trends will cause the government expenditure ratio to decline: by the end of the projection period, government spending as a share of GDP is forecast to total approximately 44% (Table 2).

Table 2: Trends in the government expenditure ratio

	2012	2013	2014	2015	2016	2017
			- % of GDP -			
April 2013 Update	**45.0**	**45 1/2**	**44 1/2**	**44 1/2**	**44 1/2**	**44**
April 2012 Update	46	45 1/2	44 1/2	44 1/2	44 1/2	-

Projection figures are rounded to half.

5.2 Trends in the government budget balance

Government budget balance will return to surplus in the medium term

The sound shape of public finances in 2012 – which posted a slight surplus of 0.2% of GDP – will make it possible to implement the tax- and cost-cutting measures for businesses and private citizens outlined in section 4.2 above. In addition, because the deficit will come in well below the Maastricht reference value of 3%, automatic stabilisers will be able to function as intended in response to the cyclical slowdown this year. This means that cyclical spending increases and revenue shortfalls can occur without risking a deficit in excess of the Maastricht reference value. As a result, a slight deficit of just under 1/2% of GDP is projected for this year. However, the government budget balance is projected to improve steadily in the following years thanks to a stable revenue ratio, a declining government expenditure ratio, and a higher-performing general economy. The general government budget is expected to return to balance in 2014 and even to post a surplus of approximately 1/2% of GDP from 2016 onwards (Table 3).

Table 3: Trends in the general government balance

	2012	2013	2014	2015	2016	2017
			-in % of GDP-			
April 2013 Update	**0.2**	**-1/2**	**0**	**0**	**1/2**	**1/2**
April 2012 Update	-1	-1/2	0	0	0	-

Projection figures are rounded to half.

Balanced budgets at all government levels from 2014 onwards

All government levels improved their budget balances again in 2012. Of all the government levels, the Federation posted the highest deficit at 0.5% of GDP, but it also posted the largest year-on-year improvement, cutting its deficit ratio in half. In contrast, municipal governments and social security funds succeeded in further expanding the surpluses they achieved in 2011 (Table 4).

Over the entire projection period, the Federal and *Länder* governments will contribute to the gradual improvement of the general government balance by continuing to pursue fiscal consolidation and by even achieving moderately rising surpluses. Local governments taken as a whole will contribute to this improvement as well, although individual municipalities vary widely in their performance. Under the plans laid down in this year's benchmark figures decision, the core budget will achieve structural balance and even a structural surplus from 2014 onwards; these positive trends in the core budget will play a key role in improving the financial balance at federal level. Accordingly, the Federal Government's financial balance will remain well below the permanent ceiling that will apply under the debt brake from 2016 onwards (i.e., structural new borrowing no higher than 0.35% of GDP). As a result, the Federation will again make a substantial contribution to the improvement of the general government balance in 2014; in fact, by 2017, the Federation is projected to post a surplus of similar magnitude to that of the municipalities. Taken together, the *Länder* will also achieve a budget surplus from 2016 onwards.

Social security funds will achieve a close-to-balance budget throughout the entire projection period. The substantial surpluses of recent years were largely the result of the consistently positive performance of the labour market, which served to boost revenues and to ensure that expenditures grew at only a moderate pace. In 2013, a variety of unfavourable effects will converge: Revenues will decline, mainly due to (i) a reduction in the federal subsidy for statutory health insurance and (ii) the elimination of the federal contribution to funding job promotion measures carried out by the Federal Employment Agency. In return, the Federal Employment Agency will no longer have to pay an "integration contribution" to the Federation (i.e., a contribution to cover half the costs of reintegrating long-term unemployed persons into the labour market), but this will not offset the reduction in Agency revenues. Statutory health insurance will be adversely affected on the expenditure side by the elimination of the mandatory quarterly medical consultation fee paid by patients; in addition, the entry into force of the Act to Restructure Long-term Care (Pflege-Neuausrichtungs-Gesetz) will broaden social transfers. Furthermore, the slowdown in the economy's performance is expected to weaken revenue momentum and to exacerbate the rise in expenditures. The surpluses of recent years, especially in statutory pension and health insurance funds, allowed these systems to build up large financial reserves. As a result, any small deficits that may arise in these funds during the projection period can be easily financed without jeopardising the sustainability of the social insurance system. The Federal Employment Agency should be able to increase its reserves due to the sustained positive performance of the labour market.

Table 4: Budget balances according to government level

	2012	2013	2014	2015	2016	2017
			- in % of GDP -			
Central government	-0.5	-1/2	0	0	0	1/2
State government	-0.3	-0	-0	-0	0	0
Local government	0.2	1/2	1/2	1/2	1/2	1/2
Social security funds	0.6	-0	-0	-0	-0	-0
General government	0.2	-1/2	0	0	1/2	1/2

Discrepancies in totals are due to rounding. Projection figures are rounded to half..

5.3 Trends in the general government structural balance

Medium-term budgetary objective will be met on a sustained basis

In statistical terms, last year's improvement in the general government balance by 1 percentage point to 0.2% of GDP was composed of a structural improvement of 1 1/2 percentage points to of a structural surplus of 0.4% of GDP and – in view of the reduction in the output gap – a cyclical decline of half a percentage point. The one-off effects in 2012 resulting from (i) the restructuring of WestLB and (ii) impact of the EU Court of Justice's judgement regarding payment of child benefits to migrant workers from another EU Member State were basically of the same magnitude as one-off effects in 2011 and therefore had no effect on the development of the fiscal balance. The economy's output gap is expected to decrease again markedly this year due to the downshift in economic momentum and, following the output gap closure rule, will not close again completely until the final year of the projection period. The spending increases and revenue shortfalls arising from the adjustment programme for Greece adopted in November 2012 represent one-off effects for this year and subsequent years, and the general government structural balance has been adjusted for these effects. As a result, in the years from 2013 to 2017, Germany will continue to fulfil its medium-term budgetary objective of a structural deficit no higher than 0.5% of GDP, which it achieved for the first time already in 2012; moreover, it will fulfil this objective by clear and growing margins as the projection period progresses (Table 5). From 2014 onwards, the general government structural balance will show a surplus of approximately 1/2% of GDP.

Because Germany more than fulfilled its medium-term budgetary objective last year and will continue to do so, the expenditure benchmark under the Code of Conduct is not binding.

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

	2012	2013	2014	2015	2016	2017
Structural balance (% of GDP)	0.4	0	1/2	1/2	1/2	1/2
Actual balance (% of GDP)	0.2	-1/2	0	0	1/2	1/2
Real GDP (% change yoy)	0.7	0.4	1.6	1.4	1.4	1.4

Projection figures are rounded to half

5.4 Sensitivity of projection of government budget balance

The sensitivity analysis shows how the government budget balance would develop in the event of deviations from the macroeconomic assumptions. The sensitivity analysis looks at two alternative scenarios that would result from a half percentage point reduction and increase, respectively, in the real GDP growth rate in the years from 2013 to 2017. It is assumed that the GDP deflator and GDP composition remain constant vis-à-vis the baseline scenario.

Should nominal GDP growth amount to only 2 1/2% per year (which corresponds to real growth of 1%), the actual balance would worsen across the entire projection period, resulting in a deficit of 1% of GDP in 2017 (Table 6). In contrast, if GDP were to expand by half a percentage point more per year than assumed in the baseline scenario, this would improve the budget balance by roughly half a percentage point per year; this in turn would lead to clear surpluses and ultimately to a surplus of 2% of GDP by the end of the projection period (thus approximately 1 1/2 percentage points better than set out in the baseline scenario).

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

	2012	2013	2014	2015	2016	2017
GDP trends according to	**- general government budget balance in % of GDP -**					
- baseline scenario	0.2	-1/2	0	0	1/2	1/2
- alternative scenarios						
• -1/2 pp p.a. compared to baseline		-1/2	-1/2	-1/2	-1/2	-1
• +1/2 pp p.a. compared to baseline		-0	1/2	1	1 1/2	2

Projection figures are rounded to half.

5.5 Trends in debt levels

Following a marked decline in 2011, the debt-to-GDP ratio (Maastricht definition) increased by 1.5 percentage points to 81.9% in 2012. This decline was driven primarily by the measures to ward off the European sovereign debt crisis; the second rescue package for Greece alone accounted for 1.2% of GDP. Together with Germany's (i) share in the European Financial Stability Facility loans to Ireland and Portugal which is rerouted to the government sector, (ii) contibutions to the European Stability Mechanism and (iii) the capital increase for the European Investment Bank, the impact of the sovereign debt crisis on the debt-to-GDP ratio amounted to 2.5% of GDP in 2012, 1.8 percentage points more than in 2011. In contrast, the impact of the financial crisis diminished. The increase in debt caused by the transfer of additional assets to the Erste Abwicklungsanstalt (EAA) in connection with the restructuring of WestLB was nearly balanced out by the successful partial winding up of portfolios at two winding-up agencies, the EAA and FMS Wertmanagement. Altogether, the total impact of the financial crisis on the Maastricht-defined debt-to-GDP ratio fell by 0.3 percentage points in 2012 to 11.1% of GDP.

In 2013, the debt-to-GDP ratio is projected to decline to 80 1/2%. While the impact of the European sovereign debt crisis is likely to raise the debt-to-GDP ratio by about half a percentage point this year, the impact of the financial crisis is expected to decrease by roughly 1 1/2 percentage points. In the medium term, the positive development of the fical balances central, state and local governments, together with the continued winding up of portfolios at the resolution agencies, will lead to a steady decline in the debt-to-GDP ratio to approximately 69% in 2017 (Table 7). This means that, as called for in the country-specific recommendations, Germany will continue to make sufficient progress towards compliance with the debt reduction benchmark in line with the 1/20 rule. Under the projection presented here, in every year of the projection period Germany will easily beat the benchmark that will apply from 2015 onwards under the 1/20 rule.

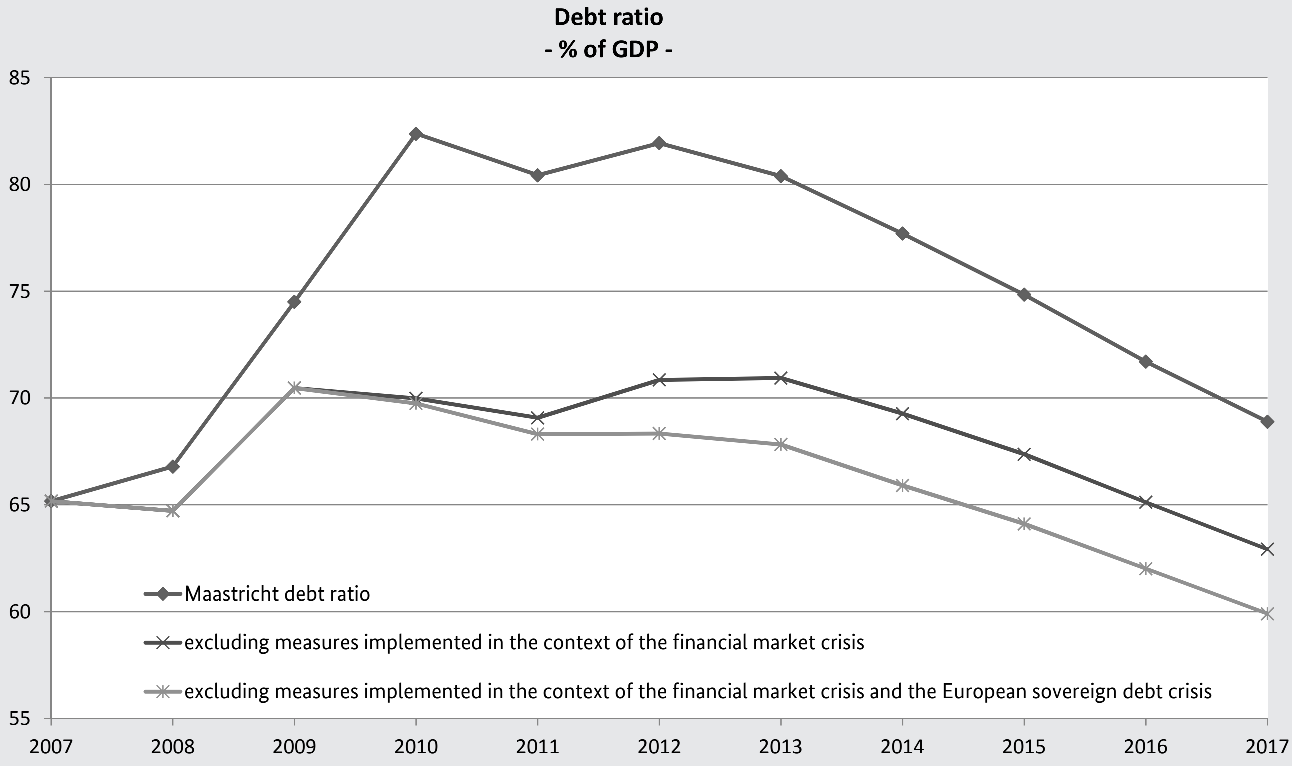
Table 7: Trends in the debt-to-GDP ratio

	2012	2013	2014	2015	2016	2017
	-Schuldenstand des Staates in % des BIP-					
April 2013 Update	**81.9**	**80 1/2**	**77 1/2**	**75**	**71 1/2**	**69**
April 2012 Update	82	80	78	76	73	-

Projection figures are rounded to half.

Figure 6 illustrates the impact that measures taken in connection with the financial crisis and the European sovereign debt crisis have had on the development of Germany's debt-to-GDP ratio (Maastricht definition). Since 2010 in particular, measures to cope with the financial crisis have had a major impact on the development of the debt ratio. The winding down of these measures will play a key role in reducing the debt-to-GDP ratio during the period to 2017. The debt impact of measures taken in connection with the European sovereign debt crisis has grown, especially since last year, but these effects will be outweighed by debt-reducing effects from this year onwards. Due to the consolidation strategy that has been pursued since 2009, public budgets taken by themselves are driving a clear downward trend in debt levels. This trend is expected to accelerate substantially from 2014 onwards, thereby causing the debt-to-GDP ratio (adjusted for crisis-related effects) to fall back under the Maastricht reference value of 60% already in 2017.

Figure 6: Debt impact of stabilisation measures taken in connection with the financial crisis and the European sovereign debt crisis

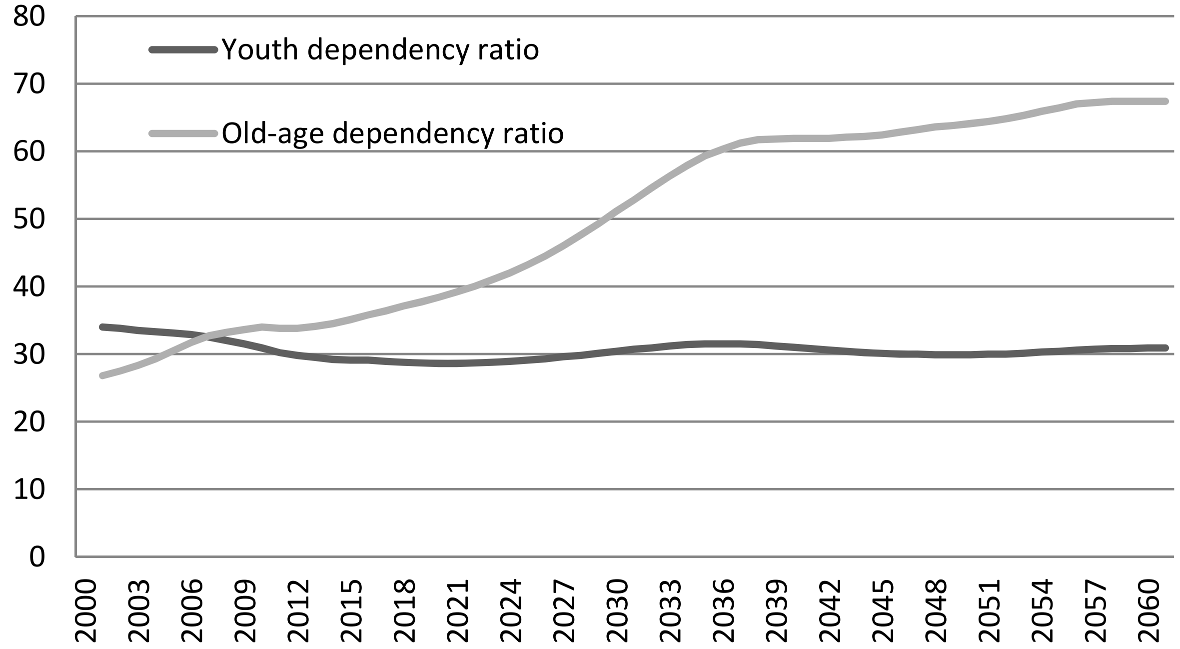


6. Long-term sustainability of public finances

6.1 Challenges to the sustainability of public finances

One of the primary challenges to the sustainability of public finances is demographic change, which is manifested in two main ways: a population that is (i) decreasing in size and (ii) becoming increasingly older. The demographic shift in Germany is likely to dampen growth prospects in the coming decades and to place considerable pressure on public finances. According to projections by the Federal Statistical Office, Germany's old-age dependency ratio is likely to increase nearly two-fold in the period from 2008 to 2060. In 2008, there were 34 persons aged 65 and over for each 100 persons of working age (20-64). This will nearly double to 67 by 2060 according to the 12th coordinated population projection, which based its calculations on an annual net migration of 100,000 persons and a fertility rate of 1.4 children per woman (see Figure 5).

Figure 7: Youth and old-age dependency ratio in Germany, 2000-2060



Source: Federal Statistical Office. For 2000-2008: results of intercensal population updates. For 2009 onwards: results of the 12th coordinated population projection, variant 1-W1. Youth dependency ratio: number of persons aged 20 and under per 100 persons aged 20-64. Old-age dependency ratio: number of persons aged 65 and over per 100 persons aged 20-64.

The Federal Government intends to tackle the social challenges of demographic change both comprehensively and at an early stage. To this end, it adopted a demographic strategy in April 2012, which is based on extensive preliminary studies, including a major demography report published by the Federal Government in autumn 2011. The strategy "Every Age Counts" sets out a framework to help safeguard long-term growth and prosperity in Germany while harnessing the opportunities presented by demographic change. Sound public finances form one of the strategy's central pillars, because sound finances are essential if the government wants to preserve its ability to take effective action. In October 2012, the Federal Government convened a demography summit to discuss key challenges with representatives from all sectors of society.

The summit launched nine working groups on:

- Strengthening the family
- Keeping the labour force motivated, skilled and healthy
- Living independently in old age
- Building an alliance for people with dementia
- Developing a national coordinating framework – strengthening regions

- Mobilising all potential to secure a sufficient supply of skilled workers
- Tapping the potential of foreign workers and creating a welcoming culture
- Promoting education throughout the life-cycle
- Enhancing the attractiveness of public service employment

The findings of the working groups will be presented at a second demography summit in May 2013.

Once per legislative period, the Federal Ministry of Finance publishes a Sustainability Report, which (i) provides regular information on how demographic change is affecting public finances while (ii) documenting the progress being made in priority policy areas relating to the issue of sustainable public finances. The methodology of the report's sustainability analyses is modelled closely after the sustainability analyses produced in a regular cycle by the European Commission. The third and most recent Sustainability Report was published in autumn 2011 and covers a projection period through the year 2060. The next report is planned for spring 2014.

The current sovereign debt crisis in the euro area demonstrates that fiscal sustainability analyses should not be limited solely to long-term projections covering the next 50 years, but should also focus on action that needs to be taken in the medium term. Therefore, in line with EU-level work, the Federal Finance Ministry's next Sustainability Report will supplement its usual long-term analyses with another projection period up to 2020/2030.

6.2 Government revenue and expenditure from a long-term perspective

The European Commission and the EU's Economic Policy Committee produce an Ageing Report every three years that contains long-term projections for government spending on age-related budget items. The latest reportfrom May 2012 is based on population projections by Eurostat and covers the time horizon up to 2060. According to the projections age-related costs in Germany will increase from 25.2% of GDP in 2010 to 30.4% of GDP in 2060. This 5.2 percentage point rise involves increases in the areas of pensions (+2.6 percentage points), health care (+1.4 percentage points) and long-term care (+1.7 percentage points) as well as decreases in the areas of education (−0.2 percentage points) and unemployment benefits (−0.3 percentage points). This overall increase is above the EU-27 average of 3.7 percentage points of GDP (and 4.1 percentage points for the euro area; see Annex, Table 6). However, taking into account the applicable regulations requiring long-term care benefits to be adjusted according to the general rate of inflation, the overall increase in age-related expenditures in Germany falls by 1.6 percentage points to 3.6 percentage points.

The European Commission's Fiscal Sustainability Report, which is also published every three years, builds upon the findings of the Ageing Report takes account of both spending and revenue while providing regular sustainability assessments for the individual Member States. The most recent Fiscal Sustainability Report 2012 classifies Germany as "low risk" in both the medium term (to 2020/2030) and the long term (to 2060). This is a clear improvement over the previous report from 2009 in the midst of the financial and economic crisis. The trajectory of Germany's fiscal health as outlined in the Commission's report is consistent with the findings of the Federal Finance Ministry's third Sustainability Report. Like the Commission's report, the Finance Ministry's report also found that the sustainability of Germany's finances in 2011 had already improved significantly compared to 2010, thanks in particular to the structural reforms of recent years and the policy of growth-friendly consolidation pursued by the Federal Government. According to the Commission's report, Germany has a long-term sustainability gap of 1.4% of GDP. This means that Germany would have to improve its general government structural balance (less interest costs) by 1.4% of GDP, both immediately and on a sustained basis, in order to meet all of its financial obligations over the long term.

6.3 Measures to ensure long-term sustainability

Germany is pursuing numerous reforms in order to ensure its social systems' capability to withstand the effects of demographic change and to enhance the sustainability of public finances.

In the area of health care, the Statutory Health Insurance Financing Act (GKV-Finanzierungsgesetz), which took effect in 2011, secured stable and sustainable financial resources for the statutory health insurance system by introducing non-income-based supplemental premiums while simultaneously fixing the contribution rates of employers. As a result, health insurance contributions have been decoupled from labour costs, thereby promoting jobs and growth, boosting resilience to demographic change, and reducing the German health care system's vulnerability to the effects of economic cycles. Moreover, the enhanced options allowing health insurance funds to charge non-income-based supplemental premiums and to pay rebates to insured persons add transparent and distortion-free elements of competition. Greater economic efficiency and improved quality have already become evident as a result, as demonstrated by the moderate trends in health care expenditure in recent years.

Germany has also implemented key reforms in the field of statutory pension insurance in recent years. Two measures in particular that have considerably enhanced the financial sustainability of the pension system are the phased increase of the standard retirement age to 67 by 2029, which started on 1 January 2012, and the introduction of a sustainability factor in the pension adjustment formula. In order to ensure that the economic consequences of demographic change are spread fairly across the younger and older generations, German pension law provides for upper limits to contribution rates and for guaranteed minimum levels of security. In addition, the government provides financial support for private, supplementary funded pensions that can offset declining benefit levels under the statutory pension insurance system.

Recent reforms in the area of long-term care insurance have bolstered the role of home care services, which are less expensive on average and preferred by individuals in need of long-term care. The previous sustained trend towards ever more institution-based care has not held up in recent years. Improved benefits under the Act to Restructure Long-term Care (Pflege-Neuausrichtungs-Gesetz) aim to further enhance the role of home care services. Against the background of ongoing demographic trends, the government now provides support for private, supplementary long-term care insurance plans to top up benefits provided under statutory long-term care insurance, thereby completing a necessary step towards more sustainable financing of long-term care needs.

Education and vocational training are essential factors in enhancing an individual's earning capacity, boosting long-term growth prospects in Germany, and thus safeguarding the long-term sustainability of public finances. The measures that the Federal Government has taken to date in the area of educational policy have been successful. The share of school leavers without a lower secondary school leaving certificate (Hauptschulabschluss) fell from 8.0% in 2006 to 6.2% in 2011. The percentage of individuals in an annual cohort who are entitled to enter higher education went up from 37% in 2000 to over 50% in 2011; in other words, just over half of the students in a particular annual cohort are now qualified to enter higher education. The percentage of individuals aged 30-34 who have completed tertiary education or equivalent now stands at just over 42%, and the trend continues to point upward given the sharply growing number of university entrants. In the coming years, existing measures will be strengthened and, where appropriate, new priority areas established with the aim of improving educational curricula and enhancing the quality of the education system's various sectors.

The Federal Government's economic policies also aim to strengthen the foundations for long-term economic growth and thereby to boost the long-term sustainability of public finances. A key factor is certainly the need to secure a sufficient long-term labour supply in Germany. In 2011, the Federal Government adopted a Skilled Labour Strategy that encompasses systematic targets and measures covering five priority areas. A first progress report on the strategy was completed in January 2013. The strategy's priority areas encompass labour market activation and the securing of jobs; ensuring equal opportunities for education; training and integrating immigrants; and improving work-life balance. In order to ensure sufficient child care for children up to three years of age, municipal and *Länder* governments are pressing forward resolutely with the expansion of child day care services. The Federal Government is providing financial support for this purpose. In addition, the Federal Government provides support to foster family-friendly working environments and to support re-entry into the workforce. A better work-life balance not only boosts employment but also aids young couples in their decision to have children.

Along with harnessing the full potential of the domestic workforce, it is also necessary to pursue smart migration policies that will help Germany secure a sufficient long-term supply of skilled workers. For this reason, by enacting legislation implementing the EU Blue Card Directive, the Federal Government last year realigned its immigration policies with a view toward attracting skilled workers and adopted rules that will make it easier for skilled foreign workers to migrate to Germany. The EU Blue Card for Germany exhausts the full scope of the EU directive. Existing opportunities for migrating to Germany are now to be expanded to cover additional skilled labour sectors involving workers who lack university degrees but possess the necessary vocational qualifications. In addition, together with the *Länder* governments, the Federal Government has simplified procedures for evaluating and recognising vocational qualifications acquired outside of Germany.

Germany's National Reform Programme contains further details on these and other economic policy measures to enhance potential growth, including measures to achieve a sustainable energy supply and to reinforce the competitive framework of the economy.

7. Quality of Public Finances

The basic preconditions for sustainable economic growth are sound fiscal policies; growth- and job-friendly economic structures; and an efficient allocation of resources that preserves the financial leeway for forward-looking investments. This is why the Federal Government is committed to pursuing a strategy of growth-friendly consolidation. This strategy involves strict adherence to quantitative consolidation targets as well as targeted qualitative objectives that aim to boost the effectiveness and efficiency of public revenue and expenditure, to expand investment in education, research, and infrastructure, and to ensure that social security systems are financed in a way that can withstand the effects of demographic change. Furthermore, all of these objectives are backed by pro-competition reforms.

7.1 Measures to enhance effectiveness

The Act to Improve Opportunities for Integration into the Labour Market (Gesetz zur Verbesserung der Eingliederungschancen am Arbeitsmarkt), which entered into force in 2012, enhances the efficiency of resource allocation in the areas of job promotion and the basic allowance for jobseekers. The legislation boosts the effectiveness and efficiency of labour market instruments by placing a greater emphasis on decentralised decision-making; tailoring the use of specific instruments more towards individual case needs; and enhancing transparency for workers as well as individuals looking for training or employment. In this way, resources to foster integration into the workforce can be allocated in a more targeted manner than was previously the case. This has helped people find jobs – in particular, jobs requiring social insurance contributions – more quickly.

Investment in education and research is a key driver of economic growth and thereby makes a decisive contribution to the quality of public finances and to prosperity in Germany. From a global perspective, countries with high levels of educational attainment and above-average levels of R&D investment achieve higher rates of economic growth on balance. For this reason, the Federal Government places a high priority on tailored, efficient investments to ensure a strong education and research system. In the current legislative period, the amount of federal spending originally earmarked for education and research has been topped up by over €13 billion.

In the field of health care, the Pharmaceutical Market Restructuring Act (Arzneimittelmarktneuordnungsgesetz) of 2011 took steps to strengthen competition on the pharmaceutical market. The aim of the

Pharmaceutical Market Restructuring Act and of the introduction of benefit assessments for pharmaceuticals containing new active substances is to be able to negotiate fair prices on the basis of a new medication's proven additional benefits over comparable treatments. In addition, the Act to Improve Care Structures in Statutory Health Insurance (GKV-Versorgungsstrukturgesetz), which entered into force in 2012, establishes for the first time a uniform framework for competition at the interface between institution- and home-based care. This will significantly enhance the quality and economic efficiency of health care services over the medium and long term.

Likewise, effectively and efficiently designed subsidies heighten the quality of government spending. All subsidies require specific justification and regular evaluation. The Federal Government has adopted a set of subsidy policy guidelines for this purpose. These guidelines provide for the regular cost-benefit analysis of subsidies and stipulate that subsidies are to be both temporary and degressive by design. This is to ensure that subsidies are used in an efficient and targeted manner and that their continuation is subject to regular review. The Federal Government's bi-annual Subsidy Report documents the implementation of the subsidy policy guidelines. According to the latest Subsidy Report, which covers subsidies granted during the period from 2009 to 2012, external evaluations were conducted on 70% of the total volume of subsidies granted in the form of tax concessions and on 46% of the total volume of subsidies granted in the form of financial assistance. The subsidy policy guidelines played a crucial role while policy-makers were designing measures to stabilise the economy during the financial and economic crisis. The guidelines ensured that measures taken to overcome the crisis would be designed in a targeted manner and, because they were temporary, would then be wound down effectively after the crisis had passed.

Key measures to improve efficiency are described in detail in the 2013 National Reform Programme.

7.2 Institutional framework to enhance transparency and effectiveness

In its Conclusions from June 2007, 20 October 2009, and 5 March 2013, the Ecofin Council reaffirmed the key role of institutional frameworks in ensuring the quality and sustainability of public finances. In recent years many EU Member States have enacted comprehensive institutional reforms to make their budgetary procedures more results-oriented and efficient.

The Federal Government has taken important steps in this direction as well. For example, in 2012 it introduced the top-down approach for preparing the federal budget. The new budget preparation procedure implies that all stakeholders must establish policy priorities at an early stage. In this way, the new procedure facilitates the setting of targeted pro-growth spending priorities within the upper ceilings stipulated by the debt brake and the Fiscal Compact. Another reform initiative demands that, all federal ministries are successively realigning the structure of their budgets to place a greater emphasis on specific policies and programmes. As a result, budget structures will become more transparent. In addition, forewords to individual departmental budgets will be updated on an annual basis. These forewords will identify key policy areas and targets, and introductory remarks to each budget chapter will specify fiscal priorities and targets. This new procedure was tested by three ministries as part of the 2013 federal budget and is set to be adopted for all departmental budgets within the framework of the 2015 federal budget.

Annex

Table 8: Forecast of macroeconomic trends

	ESA Code	2012 Index 2005=100	2012	2013	2014	2015 to 2017 (3)
			% change p.a.			
1. Real GDP, chain index	B1g	110.94	0.7	0.4	1.6	1 1/2
2. Nominal GDP (€bn)	B1g	2643.9	2.0	2.3	3.3	3
Components of real GDP, chain index						
3. Private consumption expenditure (1)	P.3	105.60	0.6	0.6	1.0	1 1/4
4. Government consumption expenditure	P.3	113.25	1.4	1.0	0.9	1
5. Gross fixed capital formation	P.51	111.28	-2.5	0.5	4.1	2 3/4
6. Changes in inventories (GDP growth contribution) (2)	P.52 + P.53	-	-0.5	0.0	0.0	0
7. Exports	P.6	139.14	3.7	2.8	4.4	4 3/4
8. Imports	P.7	136.28	1.8	3.5	4.5	5 1/4
Contributions to real GDP growth (2)						
9. Domestic demand (excluding stocks)		-	-0.3	0.6	1.5	1 1/2
10. Changes in inventories	P.52 + P.53	-	-0.5	0.0	0.0	0
11. External balance of goods and services	B.11	-	1.0	-0.1	0.2	0

2012: Federal Statistical Office, February 2013
2013 and 2014: results of the short-term forecast for the 2013 Annual Projection, January 2013
2015 to 2017: results of the medium-term forecast for the 2013 Annual Projection, January 2013

(1) Including private non-profit organisations serving households
(2) Contribution to GDP growth rate
(3) Values rounded to 1/4

Table 9: Price developments – deflators

	ESA Code	2012 Index (2005=100)	2012	2013	2014	2015 to 2017 (2)
			% change p.a.			
1. GDP		107.14	1.3	1.8	1.7	1 1/2
2. Private consumption expenditure (1)		110.25	1.6	1.7	1.8	1 3/4
3. Government consumption expenditure		109.07	1.7	2.6	1.8	1 3/4
4. Gross capital formation		105.18	1.6	1.3	1.5	1 1/4
5. Exports		106.55	1.0	0.8	0.9	1
6. Imports		110.65	1.7	0.8	0.9	1

2011: Federal Statistical Office, February 2013
2013 and 2014: results of the short-term forecast for the 2013 Annual Projection, January 2013
2015 to 2017: results of the medium-term forecast for the 2013 Annual Projection, January 2013

(1) Including private non-profit organisations serving households
(2) Values rounded to 1/4

Table 10: Labour market trends

	ESA Code	2012	2012	2013	2014	2015 to 2017 (6)
		Level	% change p.a.			
1. Employment, persons (domestic) (1) (m)		41.6	1.1	0.0	0.2	1/4
2. Employment, hours worked (2) (bn hours)		58.1	0.4	-0.9	0.4	1/4
3. Unemployment rate (3) (%)		-	5.3	5.4	5.1	4 1/2
4. Labour productivity (4) (2005=100)		103.9	-0.4	0.4	1.4	1 1/4
5. Labour productivity (5) (2005=100)		106.5	0.3	1.3	1.2	1
6. Compensation of employees (€bn)	D.1	1375.5	3.7	2.4	2.9	2 3/4
7. Compensation per employee (thousand €)		37.1	2.5	2.3	2.7	2 1/2

2012: Federal Statistical Office, February 2013
2013 and 2014: results of the short-term forecast for the 2013 Annual Projection, January 2013
2015 to 2017: results of the medium-term forecast for the 2013 Annual Projection, January 2013

(1) Employed persons, domestic concept
(2) National accounts definition
(3) Unemployed (ILO) / labour force
(4) Real GDP per person employed
(5) Real GDP (adjusted for inflation) per hour worked
(6) Values rounded to 1/4; unemployment rate: value displayed is value for last year of forecast (2017)

Table 11: Sectoral balances

	ESA Code	2012	2013	2014	2015 to 2017 (1)
			% of GDP		
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	6.3	6.2	6.2	5 3/4
of which:					
- Balance on goods and services		5.7	5.5	5.6	5 1/4
2. Net lending/borrowing of households	B.9	5.3	5.4	5.2	5
3. Net lending/borrowing of general government	EDP B.9	0.2	- 1/2	0	1/2
4. Statistical discrepancy		-	-	-	-

2012: Federal Statistical Office, February 2013
2013 to 2014: results of the short-term forecast for the 2013 Annual Projection, January 2013
2015 to 2017: results of the medium-term forecast for the 2013 Annual Projection, January 2013

Data in 1. and 2 rounded to 1/4, in 3. Rounded to 1/2 in all years; value in last year of forecast (2017)

Table 12: General government budgetary prospects

	ESA Code	2012	2012	2013	2014	2015	2016	2017
		bn. €	% of GDP					
Net lending (EDP B.9) by sub-sector								
1. General government	S. 13	4.1	0.2	- 1/2	0	0	1/2	1/2
2. Central government	S. 1311	-12.2	-0.5	- 1/2	0	0	0	1/2
3. State government	S. 1312	-6.8	-0.3	-0	-0	-0	0	0
4. Local government	S. 1313	6.1	0.2	1/2	1/2	1/2	1/2	1/2
5. Social security funds	S. 1314	17.0	0.6	-0	-0	-0	-0	-0
General government (S.13)								
6. Total revenue	TR	1,194.1	45.2	45	45	45	44 1/2	44 1/2
7. Total expenditure	TE (1)	1,190.0	45.0	45 1/2	44 1/2	44 1/2	44 1/2	44
8. Net lending/borrowing	EDP B.9	4.1	0.2	- 1/2	0	0	1/2	1/2
9. Interest expenditure	EDP D. 41	65.1	2.5	2 1/2	2 1/2	2 1/2	2 1/2	2
10. Primary balance (2)		69.2	2.6	2	2 1/2	2 1/2	2 1/2	3
11. One-off and other temporary measures (3)		-3.5	-0.1	-0	-0	-0	-0	-0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		618.7	23.4	23 1/2	23 1/2	23 1/2	23 1/2	23 1/2
12a. Taxes on production and imports	D. 2	298.3	11.3	11 1/2	11	11	11	11
12b. Current taxes on income, wealth, etc	D.5	320.3	12.1	12 1/2	12 1/2	12 1/2	13	13
12c. Capital taxes	D.91	0.0	0.0	0	0	0	0	0
13. Social contributions	D.61	448.7	17.0	17	16 1/2	16 1/2	16 1/2	16 1/2
14. Property income	D.4	24.2	0.9	1	1	1	1	1
15. Other (4)		102.6	3.9	4	3 1/2	3 1/2	3 1/2	3 1/2
16. = 6. Total revenue	TR	1,194.1	45.2	45	45	45	44 1/2	44 1/2
p.m.: Tax burden (D.2+D.5+D.61+D.91-D.995) (5)		1,067.3	40.4	40 1/2	40	40 1/2	40 1/2	40 1/2

	ESA Code	2012	2012	2013	2014	2015	2016	2017
		bn. €			% of GDP			
Selected components of expenditure								
17. Compensation of employees + intermediate consumption	D.1+P.2	333.8	12.6	12 1/2	12 1/2	12 1/2	12	12
17a. Compensation of employees	D.1	203.2	7.7	7 1/2	7 1/2	7 1/2	7 1/2	7 1/2
17b. Intermediate consumption	P.2	130.6	4.9	5	5	5	5	4 1/2
18. Social payments (18=18a+18b)	D.3	644.9	24.4	24 1/2	24 1/2	24 1/2	24 1/2	24 1/2
of which: unemployment benefits (6)		46.1	1.7	1 1/2	1 1/2	1 1/2	1 1/2	1 1/2
18a. Social transfers in kind supplied via market producers	D.6311, D.63121, D.63131	214.4	8.1	8 1/2	8 1/2	8 1/2	8 1/2	8 1/2
18b. Social transfers other than in kind	D.62	430.5	16.3	16 1/2	16	16	16	16
19. = 9. Interest expenditure	EDP D.41	65.1	2.5	2 1/2	2 1/2	2 1/2	2 1/2	2
20. Subsidies	D.3	23.7	0.9	1	1	1	1	1
21. Gross fixed capital formation	P.51	39.5	1.5	1 1/2	1 1/2	1 1/2	1 1/2	1 1/2
23. Other (7)		83.1	3.1	3	3	3	3	3
24. = 7. Total expenditure	TE (1)	1,190.0	45.0	45 1/2	44 1/2	44 1/2	44 1/2	44
p.m.: Government consumption (nominal)	P.3	515.4	19.5	20	20	20	20	20

1. Adjusted for the net flow of swap-related flows, so that TR-TE=EDP B.9.
2. The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).
3. A plus sign means deficit-reducing one-off measures.
4 . P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).
5. Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D.995), if appropriate.
6. Includes cash benefits (D.621 and D.624) and in kind benefits (D.631) related to unemployment benefits.
7. D.29+D4 (other than D.41)+ D.5+D.7+P.52+P.53+K.2+D.8.

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

Table 13: No-policy change projections

	2012	2012	2013	2014	2015	2016	2017
	bn €	% of GDP					
1. Total revenue at unchanged policies	1,194.1	45.2	45	45	45	44 1/2	44 1/2
2. Total expenditure at unchanged policies	1,190.0	45.0	45 1/2	44 1/2	44 1/2	44 1/2	44

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

Table 14: Amounts to be excluded from the expenditure benchmark

	2012	2012	2013	2014	2015	2016	2017
	bn. €	% of GDP					
1. Expenditure on EU programmes fully matched by EU funds revenue	3.5	0.1	0	0	0	0	0
2. Cyclical unemployment benefit expenditure (1)	10.6	0.4	1/2	1/2	1/2	1/2	1/2
3. Effect of discretionary revenue measures	-1.6	-0.1	- 1/2	-0	0	-0	0
4. Revenue increases mandated by law	0.0	0.0	0	0	0	0	0

Figures for the forecast years are rounded to half a percentage point of GDP.
1. Derived from unemployment benefit expenditure (COFOG, Code 10.5) and semielasticity of unemployment-related expenditure.

Table 15: General government debt developments (Maastricht-definition)

% of GDP	ESA Code	2012	2013	2014	2015	2016	2017
1. Gross debt		81.9	80 1/2	77 1/2	75	71 1/2	69
2. Change in gross debt ratio		3.1	1/2	-0	- 1/2	-1	- 1/2
Contributions to changes in gross debt							
3. Primary balance		2.6	2	2 1/2	2 1/2	2 1/2	3
4. Interest expenditure	EDP D.41	2.5	2 1/2	2 1/2	2 1/2	2 1/2	2
5. Stock-flow adjustment		3.2	-0	0	- 1/2	- 1/2	-0
p.m.: Implicit interest rate on debt (1)		3.1	3	3	3	3	3

1. Proxied by interest expenditure divided by the debt level of the previous year.
Figures for the forecast years are rounded to half a percentage point of GDP.

Table 16: Cyclical developments

% of GDP	ESA Code	2012	2013	2014	2015	2016	2017
1. Real GDP growth (%)		0.7	0.4	1.6	1.4	1.4	1.4
2. Net lending of general government	EDP B.9	0.2	- 1/2	0	0	1/2	1/2
3. Interest expenditure	EDP D.41	2.5	2 1/2	2 1/2	2 1/2	2 1/2	2
4. One-off and other temporary measures (1)		-0.1	-0	-0	-0	-0	-0
5. Potential GDP growth (%)		1.3	1.3	1.3	1.1	1.1	1.2
contributions:							
- labour		0.4	0.4	0.3	0.1	0.0	0.1
- capital		0.4	0.4	0.3	0.4	0.4	0.4
- total factor productivity		0.5	0.6	0.6	0.7	0.7	0.8
6. Output gap		-0.1	-1.0	-0.7	-0.4	-0.2	0.0
7. Cyclical budgetary component		-0.1	- 1/2	- 1/2	-0	-0	0
8. Cyclically-adjusted balance (2 - 7)		0.2	0	1/2	1/2	1/2	1/2
9. Cyclically-adjusted primary balance (8 + 3)		2.7	2 1/2	3	3	2 1/2	3
10. Structural balance (8 - 4)		0.4	0	1/2	1/2	1/2	1/2

1. A plus sign means deficit-reducing one-off measures.
Figures for the forecast years are rounded to half a percentage point of GDP.

Table 17: Divergence between the forecasts in the April 2013 and the April 2012 stability programmes

	ESA Code	2012	2013	2014	2015	2016	2017
Real GDP growth (%)							
Previous update		0.7	1.6	1.6	1.6	1.6	-
Current update		0.7	0.4	1.6	1.4	1.4	1.4
Difference		0.0	-1.2	0.0	-0.2	-0.2	-
General government net lending (% of GDP)	EDP B.9						
Previous update		-1	- 1/2	-0	0	0	-
Current update		0.2	- 1/2	0	0	1/2	1/2
Difference		1	1/2	1/2	0	0	-
General government gross debt (% of GDP)							
Previous update		82	80	78	76	73	-
Current update		81.9	80 1/2	77 1/2	75	71 1/2	69
Difference		-0	0	- 1/2	-1	-1 1/2	-

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

Table 18: Long-term trends in age-related general government expenditure

	2010	2020	2030	2040	2050	2060
			as % of GDP			
Pension expenditure (1)	10.8	10.9	12.0	12.7	13.0	13.4
p.m.: Contribution revenue (2)	7.4	7.1	7.9	8.5	8.6	8.7
Healthcare expenditure (3)	8.0	8.6	9.0	9.3	9.5	9.4
Long-term care expenditure (4)	1.4	1.7	2.0	2.4	3.0	3.1
Education expenditure (5)	3.9	3.4	3.5	3.7	3.7	3.8
Employment insurance expenditure (6)	1.0	0.8	0.8	0.8	0.8	0.8
			Assumptions			
Productivity gains (%)	0.9	1.4	1.5	1.5	1.5	1.5
Potential growth (%)	1.2	1.0	0.5	0.8	0.8	0.8
Employment rate (%)						
- Men (15 to 64)	82.4	83.2	82.5	82.8	82.3	82.4
- Women (15 to 64)	70.8	73.5	74.6	75.5	75.3	75.3
Unemployment rate	7.2	6.1	6.1	6.1	6.1	6.1
Old-age dependency ratio	34	39	52	61	63	65
Total population (m)	81.7	80.0	77.7	74.6	70.6	66.2
Population aged 65+ (m)	16.8	18.6	22.1	23.6	22.8	21.7

Source: Results of model calculations by the Economic Policy Committee of the EU (EPC) and the European Commission (DG ECFIN) published in the 2012 Ageing Report.

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

Comments: The adjustment of long-term care expenditures in line with GDP per person employed, as assumed in the reference scenarios, does not correspond to current legislation. An alternative calculation based on applicable law and using a medium-term adjustment in benefits in line with the general rate of inflation produces a maximum increase of 1.7% of GDP in 2050, which then falls to 1.5% in 2060. Data on productivity gains (based on labour productivity) and potential growth (based on aggregate potential output) represent year-on-year changes. The old-age dependency ratio is based on a working-age population aged 20-64.

Table 19: Technical assumptions

	2012	2013	2014	2015 to 2017
Short-term interest rate (annual average in %)	0.9	0.75	0.75	0.75
USD/€ exchange rate (annual average)	1.29	1.31	1.31	1.31
Growth of German sales markets (in %) (1)	1 3/4	3	4 1/4	5
Oil price (Brent, USD/barrel)	112	110	110	110

1. Values rounded to 1/4

Table 20: Contingent liabilities

% of GDP	2012
Public guarantees	23.5*
Of which: linked to the financial sector	2.2

* Year 2011

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