Bundesministerium
der Finanzen

Addendum to the Update of the German Stability Programme

– January 2009 –

1. Changed situation and new policy measures adopted

Accompanied by a sharp drop in demand and production in many countries including Germany, the global economic conditions and outlook have seen further sharp decline since the Update of the Stability Programme was published in December 2008. This deterioration means additional measures to stabilise the economy are necessary. On 27 January 2009, the Federal Cabinet therefore adopted further steps with the *Pact for Employment and Stability in Germany: Safeguarding Jobs, Strengthening the Forces of Growth and Modernizing the Country* as well as the supplementary budget required to implement it. The Federal Government is determined to use this package of measures to combat the deep recession and to counter a looming downwards spiral, as well as to strengthen the long-term drivers of growth in order to bolster Germany's growth potential as a result.

The focus is on safeguarding jobs and businesses' capacity to invest. The measures will markedly increase investment in future-oriented sectors, with educational infrastructure at the forefront. They will ensure the supply of credit to healthy, competitive companies. They will further empower the workforce to gain qualifications and they will provide lasting relief to households and businesses alike. The total volume of the package of measures in the aggregate public-sector budgets in 2009 and 2010 will be almost €50 billion. Together with the steps adopted in the autumn, this represents total funding of approximately €80 billion to support the economy. This will be supplemented by the stimulus of €8 billion in conjunction with the retroactive reinstatement of the commuter tax allowance.

This means that, overall, Germany has now decided on measures to support and stimulate the economy for 2009 and 2010 to the tune of almost €90 billion (an annual average of approximately 1¾% of GDP in 2009 and 2010 respectively). Germany is thus making an above-average contribution to implementing the agreement reached by the European Council in December 2008 to allocate 1.5% of GDP for measures to stimulate the economy. In addition, Germany will continue to allow the automatic stabilisers to take their full effect.

The individual measures approved by the Federal Government for 2009 and 2010 within the framework of the Pact include the following:

Public-sector investments in the future

- Additional investment by the Federal Government of around €14 billion forms the largest part of this package. Of this sum, roughly €4 billion will be used for additional direct federal investments. The remaining €10 billion will be made available as financial assistance for future-oriented investment by the *Länder* and local authorities in educational infrastructure (especially nurseries, schools and universities; to make up two thirds of overall planned expenditure) and other infrastructure (particularly hospitals, urban development and information technology). The *Länder* and local authorities will additionally contribute around €3.3 billion themselves. Overall, 70% of the financial support should reach local authorities.
- Investment will be accelerated by temporarily simplifying of the rules for tendering.

Ensuring the supply of credit to businesses, fostering innovation and targeting specific sectors

- A €100-billion programme of loans and credit guarantees will be implemented by expanding existing measures and creating new instruments. This includes increasing the flexibility of the KfW's 2009 initiative directed at SMEs and introducing a comparable loan programme for larger companies.
- The funding available to support SMEs' R&D projects will be extended in 2009 and 2010 (€450 million in additional funding per annum).
- The spread of broadband networks will be accelerated, guided by a comprehensive broadband strategy aimed at providing fast broadband access by the end of 2010 to all areas not presently covered.
- The demand for cars will be stimulated by means of an environmental bonus for scrapping a car above a certain age and purchasing a new replacement in 2009 that has low emissions (approximately €1.5 billion in funding).
- The existing motor vehicle tax will be replaced by a tax on emissions, with implementation envisaged by 1 July 2009.

Securing jobs and raising levels of qualification

- Support will be provided to ensure short-time work takes precedence over redundancies by subsidising employers' social insurance contributions in 2009 and 2010 (approximately €2 billion of relief).
- Extra funds of approx €2.5 billion will be made available for activation, support and training measures for job seekers as well as short-time and agency workers.

– 5,000 additional posts will be created at Federal Employment Agency offices to improve the placement of and provision of support to jobseekers.

Providing relief for citizens and bolstering demand

– Income tax will be reduced through relief of approximately €3 billion in 2009 and around €6 billion from 2010 onwards by raising the basic tax-free allowance step-by-step, cutting the basic rate of tax by 1 percentage point to 14% and raising the tax schedule incrementally.

– The statutory health-insurance contributions paid in equal parts by employers and employees will be lowered by increasing the federal subsidy by around €3 billion in 2009 and approximately €6 billion in 2010.

– A one-off bonus of €100 per child will be paid to recipients of child benefit in 2009.

Sustainable fiscal policy and a budget rule to put consolidation back on track

– New legislation on the lines of the EU's Stability and Growth Pact will be adopted to impose a constitutional limit on net borrowing. The core elements of this will involve limiting structural net borrowing by general government to 0.5% of GDP in normal economic circumstances, avoiding procyclical fiscal policy and coupling budget planning to budget execution via a surveillance and correction procedure.

– This reform is to be adopted (by amending the constitution) in the course of 2009 as part of the Federalism Commission's work, with entry into force by 2015 at the latest, possibly including transitional arrangements that are yet to be defined.

The temporary measures will be subsumed into a special investment and redemption fund, equipped with its own borrowing authorisation of up to €21 billion and an effective rule on repayment. It is envisaged that from 2010 onwards the portion of the Bundesbank profit exceeding the amount appropriated in the federal budget will be used to repay the special fund's liabilities. The share of Bundesbank profit potentially available for the redemption rises because the amount of up to €3.5 billion currently earmarked for the federal budget will be lowered by €500 million in 2011 and by €1 billion in 2012. This holds out the realistic prospect of redeeming this special fund's liabilities in full and in a manageable timeframe.

2. Development of net borrowing/net lending

General government financial balance

In light of the new macroeconomic outlook and the measures approved in January, the situation facing public finances has changed substantially since as recently as December.

Arising from these measures and the recessive trend that is to be expected, the result is a substantial decline in the general government financial balance. In 2009 and 2010 the deficit according to Maastricht criteria is set to rise by around 2½ percentage points against December 2008's Stability Programme, and is 2 percentage points higher in the years thereafter (Table 1). The trend from 2010 onwards had already been set out in the December Programme and is to be predominantly defined by the impact of the *Bürgerentlastungsgesetz* (Citizens Relief Act – allowing tax-deductibility of health-insurance contributions) entering into force in that year. In 2011 and 2012 the general government deficit is set to fall below the 3% threshold as a result of the macroeconomic environment that is assumed to have improved by then.

Table 1: Development of the general government budget balance

	2008	2009	2010	2011	2012
	- as % of GDP -				
January 2009 forecast	**-0.1**	**-3**	**-4**	**-3**	**-2½**
p.m.:					
Change in real GDP in %	1.3	-2¼	1¼	1¼	1¼
December 2008 forecast	**0**	**-½**	**-1½**	**-1**	**-½**
p.m.:					
Change in real GDP in %	1.7	0.2	1½	1½	1½

In light of the uncertainty inherent in every forecast, the financial balance is rounded to one half of a percentage point of GDP.

The deficit trend indicated from 2011 onwards is to be understood as an extrapolation on the basis of the status quo. While this reflects the development incorporating the recently approved stimulus, it does not yet contain the consolidation measures that will be required at a later stage. These consolidation measures are nevertheless an integral part of the Coalition Committee's approval of the stimulus package, because the Committee made the package conditional upon the introduction of a new budget rule. Substantial consolidation will therefore be necessary in the years to come, which cannot, however, be reflected yet in the deficit trend indicated.

Financial balances by level of government

A breakdown of the Maastricht financial balances according to the individual tiers of government shows that the worst decline is at federal level. This is because the Federation bears the main impact of January's package of measures and the establishment of the investment and redemption fund places a burden on the Federation's special accounts as well (Table 2). However, deterioration in financial balances is also to be seen at the other levels, and in some cases this is considerable. At the end of the period covered by the forecast, it is likely that the social insurance funds are alone in posting a roughly balanced budget.

Table 2: Financial balances by level of government

	2008	2009	2010	2011	2012
	in relation to GDP (%)				
Federation and special funds	-½	-2	-2½	-2	-1½
Regional and local government	0	-½	-1	-1	-1
Social insurance funds	½	-½	-½	0	0
Total government	-0.1	-3	-4	-3	-2½

In light of the uncertainty inherent in every forecast, the financial balance is rounded to one half of a percentage point of GDP.

3. Development of government revenue and expenditure

The recession and the adopted measures translate into falling revenue and mounting expenditure. The overall tax ratio to 2010 is set to fall by around 1½ percentage points to 22½% as a result. A slight increase by ½ a percentage point is to be expected until the end of the projection period. In contrast, the ratio of social contributions to GDP remains virtually unchanged at 16½% throughout the period covered by the forecast. The still comparatively favourable development in gross wages and salaries, and the higher contribution rate to statutory health insurance, raised in the first half of 2009, are counteracting the dampening effect arising from the reduced rate of contributions to unemployment insurance and the drop in employment.

The government spending ratio increases significantly by 2½ percentage points up until next year to 46½%. The government spending ratio is expected to fall to 45½% when the measures on the expenditure side terminate at the end of 2010, and because of a return to a more favourable macroeconomic dynamic as well.

4. Development of structural net lending/net borrowing

On account of the measures adopted in October, November and January, the structural deficit is set to increase substantially in the coming year to 3% in relation to GDP (Table 3).

However, the extrapolation on the basis of the status quo means it is not possible to draw information from the subsequent years' nominal or structural financial balances because the necessary consolidation measures are not included.

Table 3: Development of the structural general government budget balance

	2008	2009	2010	2011	2012
Real GDP (% change yoy)	1.3	-2¼	1¼	1¼	1¼
General government net borrowing/net lending (as % of GDP)	-0.1	-3	-4	-3	-2½
Structural net borrowing/net lending (as % of GDP)	-1	-2	-3	-2	-2

In light of the uncertainty inherent in every forecast, the financial balance is rounded to one half of a percentage point of GDP.

5. Development of the level of debt

Gross government debt is set to rise to around 68½% this year and will continue to grow in the subsequent years reaching approximately 72½% in 2012 (Table 4) largely as a result of the measures adopted and the consequently higher deficit trend, but also because of the significant slowdown in GDP.

Table 4: Development of gross government debt

	2008	2009	2010	2011	2012
	- Government debt as % of GDP -				
January 2009 forecast	**65½**	**68½**	**70½**	**71½**	**72½**
p.m.: December 2008	65	65	64	63	61½

6. Risks contained in the underlying forecast

All in all, the forecast is beset with substantial risks. In the absence of greater insight, the macroeconomic projection assumes that the cyclical setback is by and large limited to 2009. This means that the impact on the labour market in particular, and the effect at the level of the social insurance funds as a consequence, is also relatively constrained. Considerable risks are also posed by the possible adoption of further measures to stabilise the financial markets as well as defaults on guarantees awarded to non-financial enterprises within the framework of the package of measures approved in January.

Appendix

Table 5: General government budgetary prospects

	ESA Code	2007	2007	2008	2009	2010	2011	2012
		Level	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP	% of GDP
Net lending (EDP B.9) by sub-sector								
1. General government	S.13	-4.2	-0.2	-0	-3	-4	-3	-2 1/2
2. Central government	S.1311	-26.2	-1.1	- 1/2	-2	-2 1/2	-2	-1 1/2
3. State an local government		11.6	0.5	0	- 1/2	-1	-1	-1
5. Social security funds	S.1314	10.4	0.4	1/2	- 1/2	- 1/2	0	-0
General government (S13)								
6. Total revenue	TR	1065.9	44.0	44	43 1/2	42 1/2	42 1/2	43
7. Total expenditure	TE[1]	1070.1	44.2	44	46 1/2	46 1/2	45 1/2	45 1/2
8. Net lending/borrowing	EDP B.9	-4.2	-0.2	-0	-3	-4	-3	-2 1/2
9. Interest expenditure	EDP D.41	67.4	2.8	3	3	3	3	3
10. Primary balance		63.2	2.6	2 1/2	-0	-1	-0	1/2
11. One-off and other temporary measures[1]			-0.3	- 1/2	0	-0	-0	0
Selected components of revenue								
12. Total taxes (12=12a+12b+12c)		576.3	23.8	24	23 1/2	22 1/2	22 1/2	23
12a. Taxes on production and imports	D.2	304.7	12.6					
12b. Taxes on income, wealth, etc	D.5	270.8	11.2					
12c. Capital taxes	D.91	0.8	0.0					
13. Social contributions	D.61	399.9	16.5	16 1/2	16 1/2	16 1/2	16 1/2	16 1/2
15. Other [4]		89.8	3.7	3 1/2	3 1/2	3 1/2	3 1/2	3 1/2
16=6. Total revenue	TR	1065.9	44.0	44	43 1/2	42 1/2	42 1/2	43
p.m.: Tax burden (D.2+D.5+D.61)			40.3	40	40	39	39	39 1/2
Selected components of expenditure								
17. Intermediate Consumption **Social transfers in kind** **Compensation of employees** **Other taxes on production**	P.2 D.63 D.1 D.29	448.2	18.5	18 1/2	19 1/2	19 1/2	19 1/2	19 1/2
18b. Social transfers other than in kind	D.62	418.4	17.3	17	17 1/2	17 1/2	17	17
19=9. Interest expenditure	EDP D.41	67.4	2.8	3	3	3	3	3
20. Subsidies	D.3	27.1	1.1	1	1	1 1/2	1	1 1/2
21. Gross fixed capital formation	P.51	35.6	1.5	1 1/2	2	2 1/2	2 1/2	2 1/2
22. Other		73.4	3.0	3	3	2 1/2	2	2
23=7. Total expenditure	TE[1]	1070.1	44.2	44	46 1/2	46 1/2	45 1/2	45 1/2
p.m.: Government consumption (nominal)	P.3	435.6	18.0	18	19	19	19 1/2	19

(1) A plus sign means deficit-reducing one-off measures.

Table 6: General government debt developments ("Maastricht" debt)

% of GDP	ESA Code	2007	2008	2009	2010	2011	2012
1. Gross debt		65.1	65 1/2	68 1/2	70 1/2	71 1/2	72 1/2
2. Change in gross debt ratio		0.3	2	3	3 1/2	2 1/2	2 1/2
Contributions to changes in gross debt							
3. Primary balance		-2.6	-2 1/2	0	1	0	- 1/2
4. Interest expenditure	EDP D.41	2.8	3	3	3	3	3
5. Stock-flow adjustment		0.2	2	1/2	- 1/2	-0	-0

Table 7: Comparison of projections in the December 2008 Stability Programme and the Stability Programme updated in January 2009

	ESA Code	2007	2008	2009	2010	2011	2012
Real GDP growth (%)							
Previous update		2.5	1 1/2	0	1 1/2	1 1/2	1 1/2
Current update		2.5	1 1/2	-2 1/2	1	1	1
Difference		0.0	- 1/2	-2 1/2	-0	-0	-0
General government net lending (% of GDP)	EDP B.9						
Previous update		-0.2	0	- 1/2	-1 1/2	-1	- 1/2
Current update		-0.2	-0	-3	-4	-3	-2 1/2
Difference		0.0	-0	-2	-2 1/2	-2	-2
General government gross debt (% of GDP)							
Previous update		65.1	65	65	64	63	61 1/2
Current update		65.1	65 1/2	68 1/2	70 1/2	71 1/2	72 1/2
Difference		0.0	0	4	6 1/2	9	11

Table 8: Forecast of macroeconomic development from 2008 to 2012[1]

	ESA Code	2007	2007	2008	2009	2010 - 2012[4]
		Level	% change p.a.			
Real GDP (2000=100)	B1*g	108.69	2.5	1.3	-2 1/4	1 ¼
Nominal GDP	B1*g	2422.90	4.4	2.7	- 1/4	2 ¼
Demands components of real GDP						
Private consumption expenditure[2]	P.3	102.11	-0.4	0.0	0.8	1
Government final consumption	P.3	104.97	2.2	2.2	2.4	1
Gross fixed-capital formation	P.51	102.22	4.3	4.1	-5.0	2
Changes in inventories and net acquisition of valuables (contribution % of GDP)[3]	P.52 + P.53	-	0.1	0.3	0.0	0
Exports of goods and services	P.6	163.52	7.5	3.9	-8.9	4 ½
Imports of goods and services	P.7	141.13	5.0	5.1	-5.0	4 ½
Contributions to real GDP growth[3]						
Final domestic demand (w/o inventories)		-	1.0	1.2	-0.1	1
Changes in inventories and net acquisition of valuables	P.52 + P.53	-	0.1	0.3	0.0	0
External balance of goods and services	B.11	-	1.4	-0.3	-2.2	0

(1) 2007 and 2008: Provisional result of the Federal Statistical Office of January 2009;
2009: Macroeconomic Forecasts of 21st January 2009;
2010 to 2012: Medium-term forecast of October 2008 adjusted to the results of Macroeconomic Forecasts of 21st January 2009.

(2) Including private non-profit organisations.

(3) Contribution to GDP growth rate.

(4) GDP rounded to within a ¼ of a percentage point, all other figures rounded to ½ of a percentage point.

Table 9: Price development – deflators[1]

	ESA Code	2007	2007	2008	2009	2010 - 2012[3]
		Index	% change p.a.			
GDP		108.08	1.9	1.4	2.1	1
Private consumption expenditure[2]		110.80	1.7	2.2	0.9	1 ½
Government final consumption		105.90	0.2	1.8	2.2	1
Gross capital formation		103.10	2.9	1.0	1.2	1
Exports of goods and services		101.03	0.5	0.8	-1.1	1 ½
Imports of goods and services		100.51	-0.1	1.7	-3.5	1 ½

(1) 2007 and 2008: Provisional result of the Federal Statistical Office of January 2009;
2009: Macroeconomic Forecasts of 21st January 2009;
2010 to 2012: Medium-term forecast of October 2008 adjusted to the results of Macroeconomic Forecasts of 21st January 2009.

(2) Including private non-profit organisations.

(3) GDP rounded to within a ¼ of a percentage point, all other figures rounded to ½ of a percentage point.

Table 10: Labour market development[1]

	ESA Code	2007	2007	2008	2009	2010 - 2012[4]
		Level	% change p.a.			
Employment, persons (domestic) ('000)		39768	1.7	1.5	-0.7	0
Employment, hours worked (bn hrs)		57.00	1.8	1.8	-0.8	0
Unemploymentrate (%)		-	8.3	7.2	7.9	8
Labour productivity[2] (2000=100)		106.99	0.7	-0.2	-1.5	1
Labour productivity[3] (2000=100)		109.94	0.6	-0.5	-1.5	1
Compensation of employees (€ bn)	D.1	1183.55	3.0	3.6	1.2	2 ½
Compensation per employee (€)		33510	1.1	1.9	2.0	2 ½

(1) 2008 Provisional results of th Federal Statistical Office of January 2009.
2009 Macroeconomic Forecasts of 21st January 2009.
2010 to 2012 Medium-term forecasts of October 2008 adjusted to the results of Macroeconomic Forecasts of 21st January 2009.

(2) GDP per person employed.

(3) GDP per hour worked.

(4) GDP and working population rounded to within a ¼ of a percentage point, all other figures to ½ of a percentage point.