

## Public finance

### Central, regional and local authorities

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#### Trends in the third quarter

The central, regional and local authorities' budgets developed more favourably in the third quarter than in the same period last year. The deficit came to just under DM 22 billion, compared with DM 30 billion a year before. Nevertheless, in the first nine months taken together, it amounted to DM 71 billion and was thus about as large as in the corresponding period last year. The unfavourable trend in tax revenue continued to have an adverse effect. However, additional efforts were made to counteract this development by making short-term cuts on the expenditure side and by increasing receipts – especially through sales of assets.

*Overview*

The weakness in tax receipts, which has been observed for quite some time, continued in the third quarter, when revenue was once again lower than in the same period last year. Although revenue<sup>1</sup> fell by just ¼ % and therefore less than in the first six months, the decline in tax receipts continued to be at variance with the marked economic growth.

*Overall taxes*

Assessed tax revenue, in particular, was once again disappointing. In the case of assessed income tax, tax payments exceeded concurrent refunds by just under DM ½ billion; thus revenue deteriorated by DM 1 billion as against the corresponding period last year. Nevertheless, compared with the previous

*Assessed taxes*

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<sup>1</sup> Including the EU shares in German tax revenue, but excluding the receipts from local authority taxes, which are not yet known.

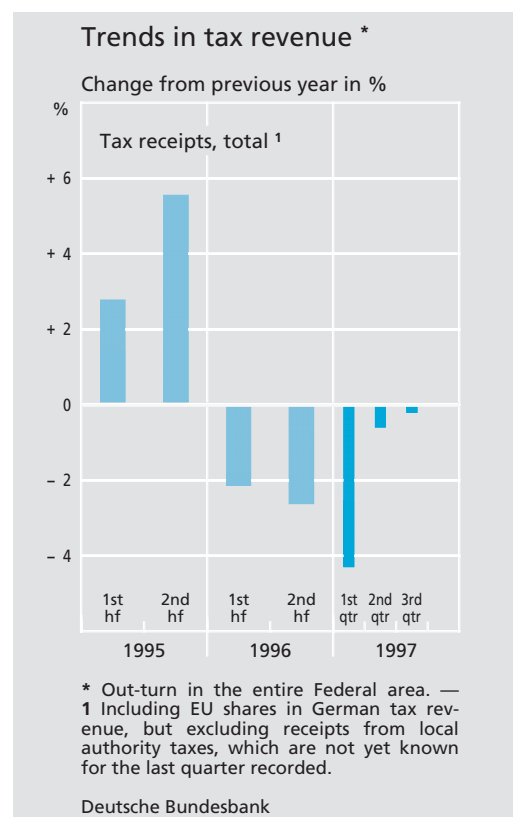
quarter when tax refunds had, in fact, distinctly outweighed tax payments, the picture looked somewhat brighter. However, recourse to various tax concessions and measures to minimise tax payments continued to affect trends in assessed income tax revenue adversely; in this context, additional shortfalls in receipts as against the previous year were probably due, above all, to the fact that the special 50 % depreciation allowance for investment in eastern Germany, which expired at the end of 1996, was applied for the last time. These factors also affected revenue from corporation tax, which yielded 1¾ % less in the third quarter than in the same period last year. However, special influences in the form of exceptionally large refunds in some cases of assessment had an even more marked impact. It would appear that, in contrast to what happened in the case of assessed income tax, corporation tax prepayments sharply increased as a result of the improved corporate earnings situation.

*Wage tax*

Receipts from wage tax were also slightly lower than in the corresponding period last year (-¼ %). The main reason for this development was child benefit, which was increased at the beginning of this year and which now impinges on wage tax. If calculated before deduction of child benefit payments, wage tax receipts grew by 1¼ %. Both the low increase in average earnings and the declining number of employed persons continued to have a retarding effect on the trends in wage tax revenue.

*Turnover tax*

In contrast to income taxes, turnover tax yielded 1 % more than in the same period last



year, but revenue did not keep pace with economic growth here either. The increase in revenue was restrained by the fact that the rise in economic activity is being fuelled to a large extent by exports, which are tax-free, whereas important components for measuring the macroeconomic VAT base – private consumption and, in particular, investment in the housing sector and investment by the public sector (which are subject to tax) – continued to be relatively weak.

In the third quarter, the Federal Government incurred a deficit of DM 16½ billion, which was DM 3 billion lower than in the same period last year. Tax revenue declined by 3½ % compared with last year, whereas the other – and usually sharply fluctuating –

*Federal budget*

### Trend in the revenue from major taxes

Type of tax	Revenue in DM billion		Change from previous year in %
	1996	1997	
1st-3rd quarters			
Wage tax	175.2	173.6	- 0.9
Assessed income tax	7.1	0.7	- 90.6
Corporation tax	22.0	22.7	+ 3.2
Turnover tax	174.5	178.0	+ 2.0
of which: third quarter			
Wage tax	60.1	59.9	- 0.3
Assessed income tax	1.4	0.4	- 73.6
Corporation tax	6.7	6.6	- 1.7
Turnover tax	58.8	59.4	+ 1.0

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receipts increased by 15 %. Receipts declined by 2 % overall.

The Federal Government's expenditure was reduced even further, falling by more than 4 %. The key factor here was that the transfers to the special funds were altogether DM 4 billion lower than in 1996. Another factor was that operating expenditure (notably on defence procurements) declined considerably; however, this expenditure had been extremely high at the beginning of the year. By contrast, a burden was imposed on the Federal Government by the fact that it had to spend 10 % more than last year on transfers to the wage and salary earners' pension insurance scheme, since the Federal grant to this scheme is linked to the contribution rate, which was raised at the beginning of the

year. The trends in labour-market-related expenditure varied. Whereas spending on unemployment assistance increased by one-fifth, hardly any transfers to the Federal Labour Office were necessary in the third quarter; this is in contrast to the DM 2 ½ billion transferred in the same quarter last year. Moreover, the expiry of the early retirement regulations in eastern Germany led to a marked easing of the pressure on the Federal budget.

In the third quarter the Federal special funds ran a surplus of just under DM 1 billion, which was just over DM 1 billion less than a year before. In this context, the Redemption Fund for Inherited Liabilities ended up in balance, after running a surplus of DM 1 billion a year earlier. On the one hand, Federal grants were DM 3 billion lower; on the other hand, the other receipts increased by DM 2 ½ billion. These receipts were due, above all, to payments made by east German banks which had been granted equalisation claims in return for loans that had been written off and which later received further payments on these claims. The ERP Special Fund recorded a surplus of DM ½ billion compared with one of DM 1 ½ billion a year earlier; in the first six months of the year, by contrast, its financial situation had been improving. Whereas in the third quarter the volume of the loans granted increased sharply, loan repayments remained on the high level already reached last year.

In the third quarter the deficit of the Länder Governments decreased considerably, viz. by DM 8 billion to DM 5 billion. This decline applied exclusively to the old Länder (includ-

*Special funds*

*Länder Governments*

ing Berlin), which incurred a deficit of DM 3 billion, whereas that of the new Länder rose slightly to DM 2 billion. The key factor for the more favourable result in the old Länder was that large receipts from privatisation led to an overall increase of 8½ % in receipts, despite a decline in tax revenue. Although on the expenditure side the Länder spent 1% more on staff, total expenditure decreased by just over 1½ %, with the east recording a fall of just over ½ %, and the west one of as much as 2 %.

*Local  
authorities*

In the third quarter the deficits incurred by the local authorities went up by DM 1 billion to DM 1½ billion, compared with the same period last year; western Germany recorded an increase and eastern Germany a reduction. Local authority spending in the west was reduced by just under 2 %, and in the east by as much as 8 %; altogether there was a decrease of 3 %. This was due, in particular, to reduced expenditure on social assistance – a development which is still attributable to the fact that since the middle of 1996 benefits paid by the statutory nursing insurance scheme also cover in-patient nursing care – and to a continuing decline in investment spending. There was also a decline in receipts, viz. of 4½ %, particularly as a result of the fact that transfers from the central and regional authorities had decreased, whereas tax revenue had remained at the same level as last year.<sup>2</sup>

*Total borrowing*

The central, regional and local authorities have again resorted to the credit markets to a large extent during the past few months. In the third quarter net borrowing amounted to

### Net borrowing in the market by the central, regional and local authorities

Period	Total	of which		Memo item Purchases of public debt instruments by non-residents
		Securities	Loans against borrowers' notes <sup>1</sup>	
1986	+ 38.0	+ 49.7	- 11.3	+ 37.2
1987	+ 50.0	+ 46.8	+ 3.6	+ 18.8
1988	+ 54.0	+ 42.1	+ 12.2	+ 6.6
1989	+ 25.8	+ 32.9	- 6.8	+ 18.8
1990 <sup>2</sup>	+ 112.2	+ 90.9	+ 21.7	+ 15.1
1991 <sup>3</sup>	+ 106.8	+ 71.3	+ 35.8	+ 50.9
1992	+ 102.4	+ 95.0	+ 7.9	+ 59.4
1993	+ 159.1	+ 120.3	+ 39.3	+ 109.1
1994 <sup>4</sup>	+ 85.8	+ 45.6	+ 40.6	- 20.9
1995 <sup>5</sup>	+ 97.6	+ 32.6	+ 81.4	+ 58.3
1996	+ 123.3	+ 65.2	+ 73.7	+ 54.1
of which				
1st hf	+ 31.1	+ 25.9	+ 14.3	+ 10.9
July–Oct. pe	+ 56.5	+ 29.3	+ 33.9	.
1997				
1st hf	+ 51.8	+ 57.1	+ 3.4	+ 36.6
July–Oct. pe	+ 32.0	- 6.1	+ 39.7	.

<sup>1</sup> Including cash advances and money market loans. — <sup>2</sup> Including GDR state budget (July 1 to October 2, 1990). — <sup>3</sup> From 1991 including east German Länder Governments and local authorities. Excluding the debt of the Federal Railways assumed by the Federal Government. — <sup>4</sup> From 1994 including Federal Railways Fund. — <sup>5</sup> From 1995 including Redemption Fund for Inherited Liabilities.

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DM 21½ billion; a further DM 10½ billion was taken up in October. Of the various types of debt, loans against borrowers' notes and short-term liquidity credits in the money market predominated. In the first ten months, taken together, new borrowing came to DM 84 billion, compared with nearly DM 88 billion in the same period last year.

At slightly more than DM 17 billion, more than one-half of net borrowing from July to October was attributable to the Federal Government. In this context, money market loans predominated with an increase of DM 16 billion. The considerable increase in the amount

*Breakdown of  
borrowing*

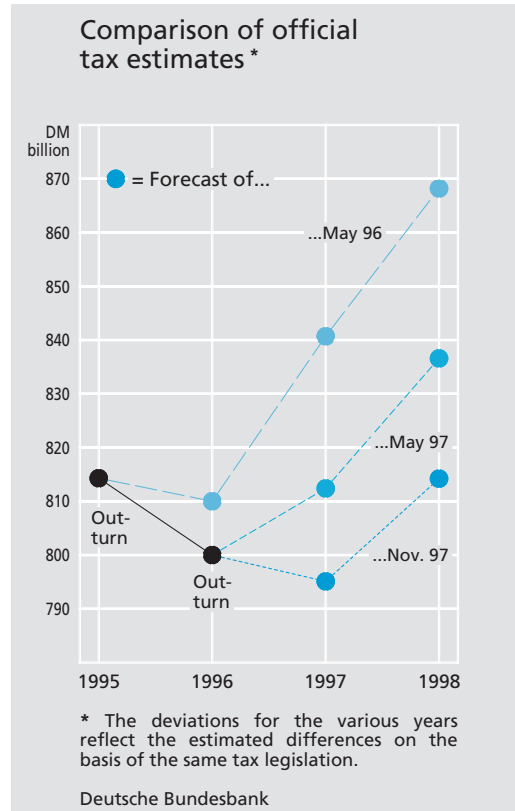
<sup>2</sup> Fee budgets are still excluded at the local authority level. This results in a reduction both in receipts (in particular, fees) and in expenditure (expenditure on staff, other operating expenses and investment).

of bonds outstanding was accompanied by sizeable redemptions of five-year special Federal bonds, which, altogether, resulted in a negligible level of new borrowing. This four-month period as a whole was characterised by the Federal Government's substantial refinancing requirements. Redemptions amounted to DM 78 billion while gross borrowing in the capital market came to DM 79 billion. The special funds redeemed about DM 1½ billion, on balance, with the "German Unity Fund" reducing its debt the most. From July to October, the Länder Governments borrowed just over DM 11½ billion net, mainly in the form of loans against borrowers' notes, the total amount of which rose by DM 10½ billion. At the local authority level, new borrowing came to an estimated DM 4½ billion, which was relatively high compared with the trend earlier in the year.

### Outlook for 1997 as a whole

#### Tax shortfalls

The budget results recorded by the central, regional and local authorities in the current year are once again overshadowed by the fact that tax revenue will fall far short of expectations at the time the budgets were drawn up. As early as May, the Working Group on Tax Estimates reduced the level of revenue expected for this year by DM 18 billion, compared with the forecast in the autumn of 1996, which had largely formed the basis of the budget plans; nevertheless, the revenue expected was revised downwards by a further DM 17.3 billion in November.



This disappointing trend in tax revenue primarily reflects the persistent structural weakness in taxes, which, for some years, has affected assessed taxes in particular; it was mainly the assessed income tax forecast that had to be revised downwards considerably again; this is partly due to the substantial use still made of tax allowances and opportunities to achieve the most favourable tax results – not least as a result of the regulations to promote economic growth in eastern Germany. Moreover, this year the Länder in particular will incur further considerable shortfalls in receipts because, contrary to initial expectations, shortfalls arising from the abolition of wealth tax were not completely offset in 1997 by the additional revenue resulting from the reform of inheritance tax and the increased tax on the acquisition of land and

buildings. According to the latest official estimate, total tax revenue in the current year will be a further 0.6% lower than in 1996; assuming a nominal economic growth of just over 3%, the tax ratio would decline by a further 0.8 percentage point to 21.8% of GDP (as defined in the financial statistics).

*Federal budget*

In the current year the Federal budget will show a distinctly higher deficit than originally planned (DM 53 ½ billion), but it will probably still be less than last year's deficit of DM 78 ½ billion. Despite the submission of the supplementary budget draft, which took account of the revenue shortfalls forecast in the tax estimate in May and provided for a deficit of just over DM 71 billion,<sup>3</sup> in the summer, additional adjustments had to be made after the recent tax estimate.

The supplementary budget for 1997 now adopted by the Bundestag (lower house of parliament) shows a financial deficit of just under DM 71 billion, which is almost the same amount as in the first draft. The tax shortfalls and the postponement of the sale of shares<sup>4</sup> resulted in an additional gap of just over DM 14 ½ billion, which was closed mainly by measures on the expenditure side. Transfers to the Redemption Fund for Inherited Liabilities were reduced by DM 6 billion, and labour-market-related spending, which had been revised upwards distinctly in the original draft of the supplementary budget, was cut back by DM 4 billion. Moreover, lower expenditure in various spheres – including those associated with the budget freeze imposed in the autumn – and increases in other receipts were provided for in the plans. The supple-

mentary budget envisages expenditure cuts of 2.4% compared with the previous year's out-turn; a decline of 1% is assumed on the receipts side.

The Federal special funds, taken together, will again run a surplus in the current year. As things now stand, however, it is unlikely to reach last year's surplus of DM 12 billion. The main reason for this is the Federal Government's reduced transfers to the Redemption Fund for Inherited Liabilities.

*Special funds*

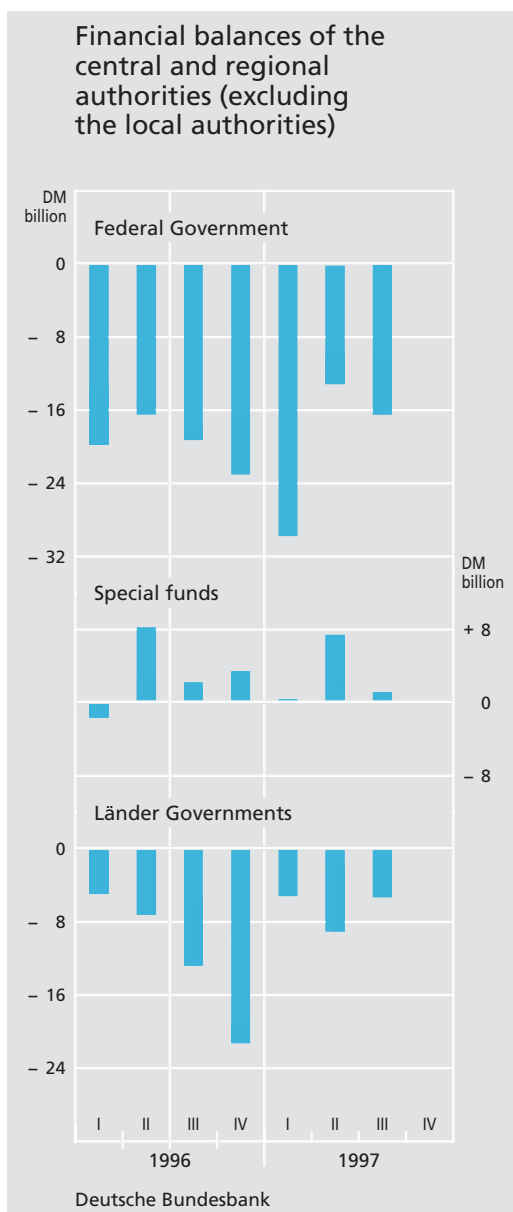
In the current year the budgetary developments of the subordinate levels of government, too, will be shaped, above all, by the expected shortfalls in taxes. The Länder Governments had originally provided for a deficit of DM 32 billion (compared with an out-turn of DM 46 billion in 1996). The tax shortfalls emerging in the course of the year were initially supposed to be offset mainly by additional economies and by increased sales of assets. However, the tax estimate in November revealed that the Länder Governments will considerably exceed their budget appropriations, although they will probably manage to achieve a lower deficit than last year. The course of retrenchment, which mainly affects investment expenditure, is continuing at the local authority level, too. Nevertheless, the local authorities will probably record less favourable results in the second half of this

*Länder  
Governments  
and local  
authorities*

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<sup>3</sup> For more details see: Deutsche Bundesbank, The economic scene in Germany in summer 1997, Monthly Report, September 1997, page 38.

<sup>4</sup> Originally, proceeds of DM 10 billion in 1997 and DM 15 billion in 1998 from the sale of the Federal Government's shares in Deutsche Telekom to the Reconstruction Loan Corporation had been envisaged; however, DM 8 billion has now been postponed from 1997 to 1998.



year than they did in the same period last year, not least because the second stage of the nursing insurance scheme, which came into force in the middle of 1996, does not provide as much financial relief as it did last year. For that reason the deficits incurred by the local authorities will probably be higher than in 1996.

Generally speaking, the central, regional and local authorities will reduce their deficits from the level reached last year (DM 121½ billion), even if they do not do so to the extent expected at the beginning of the year. Moreover, the financial situation of the social security schemes, which last year incurred a deficit of DM 13 billion, will improve considerably although this will be due mainly to the higher rate of contributions to the statutory pension insurance scheme. The overall public sector deficit, which amounted to DM 135 billion in 1996, will therefore decline comparatively sharply in 1997. Even on the basis of the Maastricht Treaty definition, the deficit will fall below last year's figure (3.4 % of GDP). Owing to methodological differences, however, the improvement is smaller here than in the financial statistics.<sup>5</sup> According to the Federal Government forecast, which was submitted to the Financial Planning Council at its meeting in November, a deficit (as defined in the Maastricht Treaty) of 3.0 % of GDP will be incurred.

*Public budgets, total*

### Budget estimates for 1998

The central, regional and local authorities expect serious budgetary problems again in the year ahead, largely as a result of the persistent weakness in tax revenue. Compared with the forecast of May 1997, on which the draft budgets were largely based, the Working Group on Tax Estimates expects tax shortfalls of DM 22.4 billion. These expected shortfalls

*High tax shortfalls also in 1998...*

<sup>5</sup> It is important to note with regard to current developments that sales of participating interests and assets lower net borrowing and the deficit as defined in the financial statistics but not the public sector deficit as defined in the Maastricht Treaty.

even exceed the loss of revenue recently estimated for 1997, although forecasts on overall economic growth remained virtually unchanged with the growth rate of nominal GDP expected to be 4 ½ %.

*... especially in  
assessed taxes*

The main reason for the increase in tax shortfalls is that the working group has taken greater account of the risks associated with assessed taxes than before; assessed taxes are the main cause of the "detachment" of tax revenue from economic trends. Considerable use is likely to be made of tax concessions again in 1998. Furthermore, there is a risk that the shortfalls resulting from the abolition of trading capital tax will not yet be completely offset by the approved reduction in opportunities to achieve the most favourable tax result (particularly with regard to reserves) next year. Finally, it appears likely that enterprises will distribute profits to a larger extent than before.<sup>6</sup>

*Declining tax  
ratio and  
a distorted tax  
structure*

The working group forecasts no more than a 2.4 % rise in total tax revenue. Thus, the tax ratio (as defined in the financial statistics) would decline by a further 0.4 percentage point to 21.4 %; around one-half of this decline would be attributable to the reduction in the solidarity surcharge by 2 percentage points from the beginning of 1998. Although the tax ratio will therefore reach a very low level in a longer-term comparison, this does not at all indicate that the general tax conditions in Germany are favourable. Instead, the low figure is based on a tax structure that is distorted by an erosion of the tax base and the prevalence of high tax rates and that adversely affects economic trends owing to

problems arising from the distribution of incentives.

In their budgetary estimates, the central, regional and local authorities are trying to cushion the tax shortfalls as far as possible without resorting to additional borrowing. The main emphasis here, in addition to increased privatisation, is on spending cuts, not least short-term measures, deferrals of payment dates for financial obligations as well as cut-backs in investment expenditure which is not immediately necessary. As for the rest, the low level of interest rates is having an effect, as is the successful anti-inflation policy, which is containing the rise in government consumption and in many transfer payments that adjust automatically. The present budget plans and draft budgets suggest that there will be a 2 % expansion in spending, which would mean that expenditure would be distinctly lower than overall economic growth.

*Efforts to  
reduce  
expenditure*

All in all, the central, regional and local authorities are planning to reduce the budget deficits, despite the high shortfalls in tax revenue. Another factor affecting the public sector as a whole is that once again the social security funds are likely to be in a more favourable position than in the current year, because a surplus must be achieved in the pension insurance scheme in order to replenish the fluctuation reserve up to the minimum level of one month's expenditure. As things

*Declining public  
sector deficit*

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<sup>6</sup> One reason for this is that a reduction of 20 percentage points in corporation tax on profit distributions stemming from reserves that were formed prior to 1994 and are subject to a 50 % tax rate may be claimed only up to the end of 1998. From 1999, there will be a reduction of only 15 percentage points in corporation tax.



now stand, the overall public sector deficit in budgetary terms could therefore be reduced distinctly, perhaps by ½ percentage point of GDP. If the definition used in the national accounts is applied, the reduction is likely to be smaller because then the substantial proceeds expected from privatisation do not count as deficit-reducing receipts.

*Federal budget benchmarks*

The Federal budget approved by the Bundestag in November envisages a deficit of DM 56.4 billion, which is DM 1.4 billion below the estimate in the original budget plan approved in July and is slightly less than total investment expenditure (DM 58.1 billion). The volume of overall expenditure is DM 456.8 billion, 2.7 % more than the amount envisaged in the supplementary budget for 1997.

*Additional gaps compared with the draft budget...*

Additional payments of slightly more than DM 20 billion had to be incorporated into the budget plan recently approved. Of these additional payments, DM 9.5 billion is attributable to shortfalls in tax revenue contained in the most recent tax estimate, and just over DM 6 billion to the lowering of the solidarity surcharge approved last October. On the expenditure side, additional labour-market-related expenditure of DM 3 billion will make itself felt; most of this sum is to meet the unemployment assistance paid to the long-term unemployed. Furthermore, the Federal grant to the pension insurance scheme will increase by an additional DM 1.5 billion because in the budget plan it has been assumed that there will be a higher increase in the contribution rate from the beginning of 1998 than originally envisaged (see also p. 43 f.).

The postponement until 1998 of sales of Deutsche Telekom shares amounting to DM 8 billion to the Reconstruction Loan Corporation is the main means of closing these additional budgetary gaps. If the sales that were already envisaged in the draft budget are included, the Federal Government will be selling, in 1998, a stake worth DM 23 billion in this enterprise. There was also a further cut – of DM 5 billion – in the grants to the Redemption Fund for Inherited Liabilities, a measure which will delay the elimination of the Fund's debt. The remaining relief measures concern a variety of items, with further sales of participating interests and assets having an impact on the receipts side.

*... and measures to be taken to close them*

The reduction of DM 14½ billion in net borrowing envisaged for 1998 in the budget plan is considerable when compared with the amount envisaged for 1997. As things now stand, the risks in making tax estimates and forecasting labour-market-related expenditure appear to be significantly lower than in previous years, when it was mainly these factors that caused an excessive overshooting of the planned deficits. However, it should be borne in mind that the relief is mainly of a non-recurrent nature and in some cases will lead to lower receipts at other levels of government, with the result that in the medium term the need for consolidation will continue to be very high.

*Strong impact of non-recurrent measures*

The Länder Governments' budget plans, parts of which have not been concluded yet, will also be adversely affected by large shortfalls in tax revenue; at slightly more than DM 10 billion, compared with the spring esti-

*Länder Governments' budget plans*

mates, they are, in fact, even higher than the shortfalls at Federal level. Although the Länder Governments intend to contain the rise in spending to approximately 1%, only a relatively small reduction in deficits is expected owing to the tax shortfalls. The size of this reduction depends not least on the extent to which the Länder Governments will eventually realise their plans for substantial privatisation. The Länder budgets will also be considerably affected by the public sector pay settlements, the level of which is still uncertain. As there is still considerable pressure to consolidate, the Länder Governments are likely to endeavour to offset any fairly large pay increases by stepping up their efforts to limit staff levels.

*Prospects for  
local authorities*

The budget deficits of local authorities appear more likely to increase somewhat in 1998. The relief in the field of social assistance afforded by the introduction of the nursing insurance scheme will no longer have a restraining influence on the rise in expenditure. The most significant factor on the receipts side is that the transfers from the Länder Governments will probably continue to be limited. In view of the persisting pressure of financing requirements, it is unlikely that the local authorities will be able to reverse the trend in their capital formation, which has been declining for a number of years now.

### **Social security funds**

The financial trends in the statutory pension insurance scheme for wage and salary earn-

ers have been characterised by various conflicting influences in 1997. The main relief, in addition to the extra revenue provided by the raising of the contribution rate from 19.2% to 20.3% at the beginning of 1997, has come from new legal provisions. Thus, the shift in the dates by which the social security contributions have to be paid resulted in non-recurrent additional receipts. On the expenditure side, reductions in benefits in the field of rehabilitation are leading to considerable savings. By contrast, the unfavourable trend in employment, which is slowing down the increase in contributions, is the main negative factor.

*Statutory  
pension  
insurance  
scheme*

In the third quarter of the year, the pension insurance scheme recorded a deficit of just over DM 2½ billion, against almost DM 5 billion in the corresponding period of 1996. Receipts from contributions rose by slightly more than 5%, which is mainly attributable to the considerable increase in contribution rates. Owing to the marked increase in Federal grants associated with this increase, total receipts in the period from July to September were actually almost 6½% higher than at the same time last year.

*Financial  
results in the  
third quarter*

Total expenditure rose by 3½%, the main reason being the 4% rise in pension payments. On July 1, 1997 pensions were raised by 1.65% in western Germany and by 5.55% in eastern Germany. In eastern Germany, however, the continued reduction in replenishing amounts employed in the course of the pension insurance transference led to a slower increase in pension payment amounts. A further factor leading to an increase in ex-

*Expenditure  
on pensions*

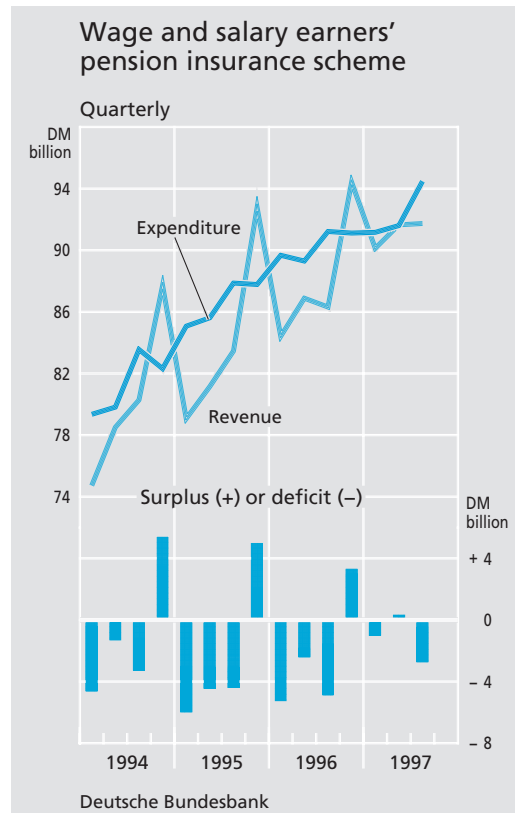
penditure was the increase in the number of pensions paid, the main reason for which may be the difficult situation in the labour market.

*Trends in 1997  
as a whole*

If the first three quarters are taken together, the deficit of the pension insurance scheme amounted to DM 3¾ billion, which was almost DM 9 billion below the figure in the same period last year. A surplus may be recorded in the last quarter of the year owing to the large amount of contributions usually received as a result of the "Christmas bonuses" in this period. However, this effect on receipts is expected to be weaker than usual this year because the negotiated annual special income was cut back in many sectors of the economy in the course of bargaining to retain the payment of wages and salaries during illness.

*Required  
fluctuation  
reserve again  
falls short*

The surplus needed at the end of 1997 to restore the fluctuation reserve to its legally required level of one month's expenditure will fall far short of its target. Efforts will therefore have to be made again next year to achieve a surplus of receipts. It was assumed in the 1997 Pension Insurance Report that in 1998 a contribution rate of 20.6% would be necessary. Especially in view of the less optimistic forecast on employment, a contribution rate of 21% would actually have been necessary now to comply with the statutory fluctuation reserve requirement by the end of 1998. In the light of this the Bundestag and the Bundesrat (the upper house of parliament) agreed at an inter-house mediation hearing to raise the standard value-added tax from 15% to 16% from April 1998 and to use the



extra revenue for an additional Federal grant to the pension insurance scheme. An increase in the contribution rate was thereby avoided.

Despite the persistently unfavourable conditions in the labour market, the financial situation of the Federal Labour Office improved distinctly in the third quarter, primarily as a result of special factors. While there had been a deficit of DM 2½ billion a year earlier, there was now a surplus of DM ¼ billion. In the first six months of 1997, by contrast, the deficit had increased by DM 1½ billion to DM 9½ billion compared with the same period last year.

*Federal Labour  
Office*

The Federal Labour Office's receipts grew by slightly more than 5% in the third quarter. The reason for this was an advance payment

*Increased  
receipts owing  
to special  
factors*

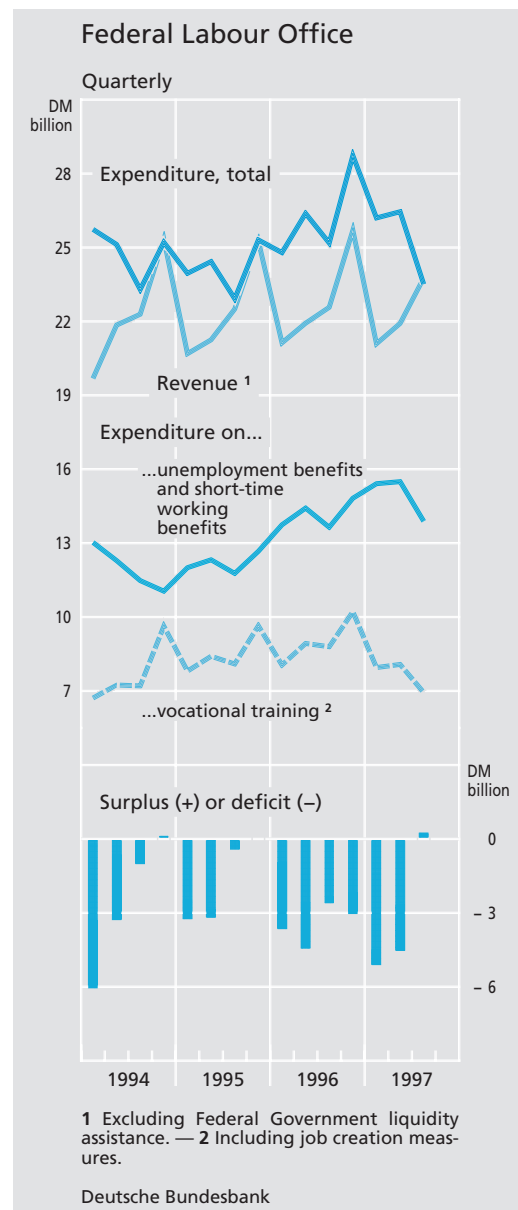
on the sale of Federal Labour Office assets, which had been laid down in the 1996 Growth and Employment Promotion Act. However, the amount of contributions received did not increase any further. Although a slight increase (+ ½ %) was recorded in western Germany, this increase was offset by a distinct decline in eastern Germany (-9 ½ %). The Federal Labour Office is particularly affected by the negative trend in employment because, unlike the other branches of social security, it does not receive any contributions for the unemployed.

*Decreased expenditure*

The Federal Labour Office's total expenditure in the third quarter was 6 ½ % below the level in the same period last year. The main reason for this decrease was the lower expenditure in connection with the "active labour market policy". The amount of funds spent on training programmes and on job creation schemes decreased by slightly more than one-fifth and approximately one-quarter, respectively, against the level a year before. Thus, the trend towards eliminating unregistered unemployment continued. By contrast, expenditure on unemployment benefit grew by a total of 2 ½ %. This increase, however, was lower than in the first six months of the year (+ 10 ½ %). The new regulations under the Work Promotion Act had some effect here; under these regulations, wage substitutes have been disbursed only once a month instead of every two weeks since July 1, 1997.

*Prospects*

Judging by the trends so far this year, which have been characterised not least by the



spending cuts approved by parliament, the grant provided for in the Federal supplementary budget appears likely to be sufficient for balancing the Federal Labour Office's deficit of DM 12 billion in 1997. In view of the fact that the situation in the labour market will be unfavourable next year as well, however, the Federal Labour Office's need for grants will continue to be very high. In its 1998 budget

plan, the Federal Government provided DM 14.1 billion for this.

The financial trends in the statutory health insurance institutions are currently being significantly affected by the various measures taken to contain the rise in costs in the health sector. After the 1996 Contribution Relief Act had led to a decrease in expenditure on benefits in the first half of 1997, the New Regulation Acts, which came into force in the middle of the year and which provide primarily for higher personal contributions on the part of insured persons to the cost of prescribed medicines, are now showing their effects.

In the third quarter, expenditure on benefits was slightly more than 3% below last year's level; the main reason for this was the sharp

drop in expenditure on prescribed medicines (- 15%) and in payments of sickness benefits (- 22 ½%). Thus, despite the continued weakness in contribution receipts, the health insurance institutions achieved a surplus of almost DM 0.8 billion, against last year's deficit of DM 1.4 billion. In the period from January to September 1997 as a whole, the deficit, at DM 3.2 billion, was DM 5.5 billion lower than in the same period last year. As a surplus may be expected in the fourth quarter, primarily as a result of seasonal factors, the cash position of the statutory health insurance institutions over the whole of 1997 is likely to be more or less in equilibrium. However, the health insurance institutions in eastern Germany are again expected to record a deficit due to the particularly unfavourable trends in receipts there.