Public finance

Central, state and local government

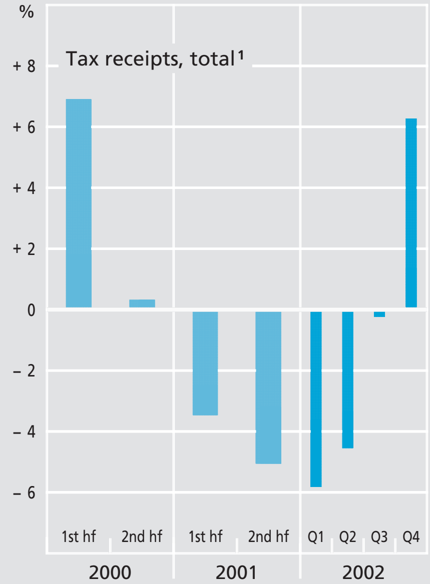
Overview

In the fourth quarter of 2002 the central, state and local government budgets – according to the results available so far – recorded a more favourable outturn than in the same period in 2001. However, at that time the development had been influenced by several negative exceptional factors, which means that the budgetary position has not necessarily changed for the better. In 2002 as a whole, each level of government (excluding the special funds) expanded its deficit considerably. The combined deficit of central, state and local government amounted to over €60 billion, after having already risen sharply to €47 billion in 2001. The main reason for this was the fall in tax receipts which also dragged down total revenue. Expenditure growth accelerated, not least owing to a sharp increase in labour market-related spending; the rise was probably under 2%, however.

Budgetary developments this year are being influenced by considerable uncertainties with regard to the overall economic outlook and the effects of fiscal measures which have been taken or which are still under discussion. The budgetary plans of the Federal Government and the *Land* Governments envisage markedly lower deficits vis-à-vis the results for 2002. A key requirement for achieving this, however, is the imposition of tight expenditure curbs in accordance with the targets set by the Financial Planning Council. Another major consideration will be whether the total amount of the envisaged consolidation measures is actually implemented.

Tax revenue

Change from previous year



1 Including EU shares in German tax revenue, but excluding receipts from local authority taxes, which are not yet known for the last quarter recorded.

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Tax revenue in the fourth quarter and in 2002 as a whole...

Tax receipts[1] in the fourth quarter of 2002 went up by just over 6% vis-à-vis the same period last year, after declining sharply in the first half of the year and stagnating in the third quarter. This end-of-year improvement was, however, partly attributable to the fact that corporation tax receipts had been dented by €1½ billion at the end of 2001 *inter alia* by an exceptionally high tax refund. But even after allowing for this special factor, corporation tax receipts recovered, whereas the other income tax receipts did not quite match the corresponding figures from the previous year and turnover tax receipts increased only marginally. According to the preliminary outturn – which includes only an estimate for local authority taxes – tax revenue in 2002 as a whole was 1.2% lower than in 2001. The overall tax ratio (as defined in the government's financial statistics) receded further by 0.7 percentage point to 20.9%, after already decreasing sharply in 2001 mainly as a result of the tax reform. Although tax receipts exceeded the most recent official estimate from November by €1½ billion, they still fell €25 billion (just over 1% of GDP) short of the comparable tax estimate from autumn 2001 – on which the budgets were largely based. The tax shortfalls vis-à-vis the budget plans were consequently twice as high as in 2001.

These shortfalls affected almost all major taxes. Turnover tax receipts declined for the second consecutive year with a drop of ½% and thus fell €7½ billion below the expectations of autumn 2001. This was mainly due to the fact that nominal domestic demand decreased last year for the first time in a long while. Moreover, the measures aimed at combating tax fraud, which were adopted at the end of 2001, did not apparently yield any significant additional revenue. The shortfalls in corporation tax receipts were even higher (€8½ billion), although positive receipts of just under €3 billion were recorded, after corporation tax receipts had been marginally exceeded by refunds in 2001. Corporation tax yielded considerably less than the amount that might have been arithmetically expected from the tailing-off effect of the large distributions of retained profits in 2001. Besides the further decline in advance tax payments as a result of the unfavourable earnings trend, a notable factor was the considerable

1 Including EU tax shares in German tax revenue, but excluding receipts from local government taxes, which are not yet known.

refunds in respect of fiscal 2001 with its poor profitability for which the corporate tax returns for 2001 appear to have been submitted earlier than usual by many firms. It was also the last chance for corporations to claim tax write-downs on their participating interests before the tax exemption of capital gains from the sale of domestic participating interests came into force at the beginning of 2002.[2] Wage tax receipts declined marginally vis-à-vis the previous year and were consequently almost €5 billion lower than expected in the autumn 2001 forecast. Before deducting child benefit, which was increased last year, they rose by 1¾%. This weak trend was mainly due to the fact that gross wages and salaries grew last year by just under 1%, which was 2 percentage points less than initially expected.

Trends in the revenue from major taxes

Type of tax	Revenue in € billion, Full year 2001	2002	Change from previous year in %
Wage tax	132.6	132.2	– 0.3
Assessed income tax	8.8	7.5	– 14.0
Corporation tax	– 0.4	2.9	.
Turnover tax	138.9	138.2	– 0.5
	of which Q4		
Wage tax	38.9	38.9	– 0.0
Assessed income tax	4.7	4.5	– 3.2
Corporation tax	– 1.9	3.2	.
Turnover tax	35.6	36.0	+ 0.9

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... and this year

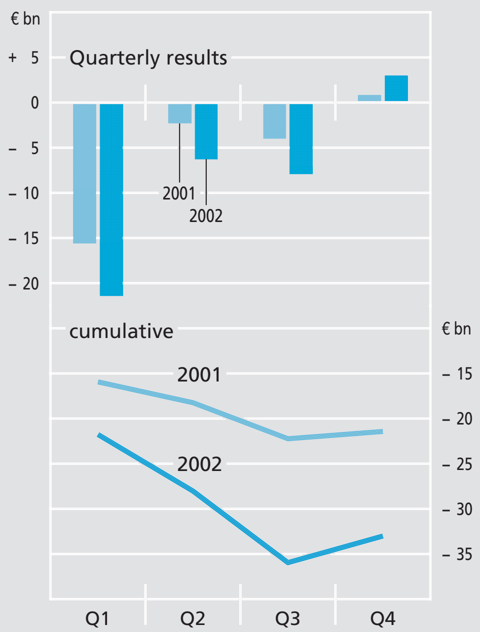
A marked rise in tax revenue – which is likely to exceed that of nominal GDP – is expected this year. This is due *inter alia* to the planned and partly adopted tax measures. A tax revenue increase of just over 4% was anticipated in the official estimate from November. If the additional revenue arising from curbing the exemptions from the "ecology tax" and the draft Act to Reduce Tax Subsidies is included, this gives a revenue increase of 5½%, based on the nominal economic growth expected at that time of just over 3%. As things stand now, however, it appears likely that overall economic growth will be down on the expectations made in autumn. Furthermore, it is still uncertain to what extent the Bundesrat will approve those parts of the tax package that require its assent.[3]

Federal Government budget in 2002 ...

In the fourth quarter the Federal Government budget recorded a surplus of €3 billion, which was somewhat higher than in the fourth quarter of 2001. In 2002 as a whole, however, the deficit rose steeply by €11½ billion to €32½ billion. This also significantly overshot the original budgetary expectations (€23½ billion).[4] On the one hand, this was at-

2 Losses arising from the sale of participating interests were likewise tax-deductible only until 2001.
3 For an assessment of the draft Act to Reduce Tax Subsidies now being considered by the Bundestag and the Act Continuing the Ecological Tax Reform, which has already been passed, see details in Deutsche Bundesbank, Recent tax revenue trends, *Monthly Report,* December 2002, in particular pp 27 ff.
4 However, the budget outturn was more favourable (by €4½ billion) than the supplementary budget adopted by the Federal Cabinet in November last year which, with a deficit of just under €37½ billion, took account of the tax shortfalls expected at the time and higher labour market-related expenditure. Tax revenue exceeded the corresponding estimate by almost €1½ billion, while expenditure was just over €3 billion below expectations.

The Federal Government's financial balance in 2001 and 2002



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tributable to sizeable tax shortfalls, which – after netting with lower transfers to the EU budget – amounted to a little more than €7 billion. On the other hand, payments relating to unemployment assistance and grants to the Federal Labour Office together exceeded the expectations by €5½ billion. Other expenditure was, however, €3½ billion lower than anticipated. This applies particularly to interest payments, which profited from high premiums on the new issues of Federal securities, and guarantees. In the case of non-tax revenue, privatisation proceeds were down by around €3 billion, but this was offset by additional receipts in other areas (such as increased loan repayments). On balance, the marked overshooting of the targeted budget deficit was not due to a lax budgetary policy but was primarily a consequence of the macroeconomic trend, which was far more unfavourable than expected.

... and in 2003

The Federal draft budget for 2003, which was revised after the German parliamentary elections of September 2002, envisages that the deficit will decline noticeably to just under €19½ billion, whereas the original plans had anticipated a deficit of €16 billion. The upward revision of the estimated deficit is due to tax revenue shortfalls. Although the 2002 outturn was somewhat more favourable than had been expected in November, the budget for 2003 is subject to considerable risks. The Federal Government meanwhile expects real economic growth of merely around 1%; this is ½ percentage point lower than estimated in autumn 2002. This new forecast, too, is subject to significant risks. Moreover, the plans also include numerous relief measures, the realisation of which seems uncertain at the moment. For example, the projected extent of the savings from implementing the planned labour market reform (Hartz plan) is not yet assured.

If the 2003 Federal draft budget can be successfully implemented in a difficult macroeconomic climate, this would represent a considerable consolidation advance. Expenditure is to be cut by almost 2% vis-à-vis the supplementary budget estimate for 2002 and by ½% compared with the lower outturn for last year; even including additional expenditure on account of flood damage, this would be in line with the provisions of the Financial Planning Council's guidelines. This will require actual enforcement of the announced measures in the course of the budget implementation and ensuring that the envisaged volume of relief measures is actually achieved. Such structural consolidation is imperative in view of the large deficit recorded last year and also with regard to the credibility of national and international fiscal policy agreements.

Special funds

The special funds recorded a surplus of €8 billion in 2002, exceeding the figure for 2001 by €3 billion. The main reason for this was the marked increase in the share of the Bundesbank profit accruing to the Redemption Fund for Inherited Liabilities. However, the surplus is expected to decrease noticeably in 2003.

Land Governments

Although the deficit of the *Land* Governments fell by €4 billion in the fourth quarter of 2002 compared with the previous year to €11 billion, the deficit in the last quarter of 2001 had been particularly high owing to several significant exceptional factors, such as sizeable tax refunds, the repayment of natural gas extraction royalties and a substantial acquisition of participating interests. Contrary to the plans – which originally predicted a deficit reduction to about €20 billion – the deficit in 2002 as a whole came to €31 billion, thereby further exceeding the already high amount of €26 billion registered in 2001. The principal cause of this was the drop in tax receipts. At first glance, expenditure growth appears to have been stopped. However, after being adjusted to account for the aforementioned exceptional burdens, spending increased by 1½%; expenditure on personnel had a particular impact here, rising more markedly by 2½%. The budget plans of state government for 2003 envisage significantly lower deficits (of around €23 billion according to the current state of planning), not least by resorting to one-off measures, such as asset disposals. However, as is the case with the Federal Government, the plans contain a large degree of uncertainty.

Local authorities

For local government only the results for the first three quarters are available. During this period, the deficit amounted to just under €6½ billion, which was double the figure for the first three quarters of 2001. The continued sharp decline in tax receipts (by 6½%) was the main reason for the decrease of almost 1½% in overall revenue. By contrast, expenditure growth accelerated to just under 2%; a further decline in construction investment was offset by a significant rise in social benefits, personnel expenditure and other operating expenditure. The development in the fourth quarter – which is not yet known – is unlikely to have had a decisive impact on the unfavourable underlying tendency for 2002 as a whole. The financial situation is not expected to improve this year, not least due to the fact that the forthcoming final settlement of the municipal tax-sharing arrangements is likely to result in lower grants to the local authorities. Furthermore, additional personnel expenditure will arise from the pay settlement for the public sector for the local authorities in eastern Germany, in particular, due to the further approximation of the wage scales for eastern Germany to the western level.

Indebtedness

Indebtedness of central, state and local government rose by just under €9 billion in the fourth quarter. Besides a relatively small in-

Net borrowing in the market by central, state and local government

€ billion

Period	Total	of which: Securities 1	of which: Loans against borrowers' notes 2	Memo item: Acquisition by non-residents
2001	+ 14.2	+ 56.3	– 6.6	+ 1.1
of which				
Q1	– 10.4	+ 13.9	+ 9.7	– 11.8
Q2	– 6.1	+ 7.5	– 13.7	– 0.5
Q3	+ 15.6	+ 18.5	– 1.8	+ 14.9
Q4	+ 15.2	+ 16.4	– 0.9	– 1.6
2002 pe	+ 54.5	+ 67.0	– 11.3	...
of which				
Q1	+ 25.6	+ 15.2	+ 10.5	+ 7.2
Q2	+ 1.5	+ 22.9	– 21.4	+ 11.7
Q3	+ 18.6	+ 25.1	– 5.4	+ 15.5
Q4 pe	+ 8.9	+ 3.8	+ 5.1	...

1 Excluding equalisation claims. — 2 Including cash advances and money market borrowing.

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crease in capital market indebtedness (€½ billion), short-term cash advances and money market loans went up sharply by just over €8 billion. In 2002 as a whole, net market borrowing amounted to €54½ billion. Whereas public authorities had much greater recourse to tradable capital market securities (€67 billion net), their outstanding amount of bank loans not serving to assure liquidity in the short term declined by over €15½ billion.

Social security funds

Statutory pension insurance scheme

Although the wages and salary earners' pension insurance scheme recorded its customary surplus in the fourth quarter of 2002 (of almost €1 billion), it was more than €1½ billion lower than in the same period of 2001. The main reason for this was the weak trend in contribution receipts. In 2002 as a whole the deficit reached €5 billion, thus exceeding the figure for 2001 by €4½ billion. With the decision to reduce the lower limit for the fluctuation reserve to 80% of one month's expenditure in order to be able to keep the contribution rate at 19.1%, the foundations for an increase in the deficit had been laid. But the actual level of the fluctuation reserve recorded at the end of 2002 – 63% of one month's expenditure – fell well short even of the reduced target since the growth of gross wages and salaries subject to compulsory insurance contributions was appreciably dampened by the unfavourable economic development.

Outlook for 2003

Following the high deficit last year, both a rise in the contribution rate to 19.9% and a further increase in the Federal grant from the last stage of the ecological tax reform would have been necessary at the beginning of the year in the light of the expectations of autumn 2002 to bring the fluctuation reserve back up to the minimum level. In order to curb the negative macroeconomic impact of such an increase in non-wage labour costs, the required level of fluctuation reserves was reduced further to at least 50% of a month's expenditure. In addition, the ceiling for earnings subject to contributions was raised markedly. These measures made it possible to limit the rise in contribution rates to 19.5% (from 19.1%). However, in the meantime, several new burdens have appeared on the horizon. For example, the 2003 Annual Economic Report reduced the projected growth rate of gross wages and salaries by ½ percentage point to 2%. In addition, revenue shortfalls are anticipated to ensue from the new arrangements applying to low-paid part-time workers. Further strains may arise from the possibility as from December of shifting wage and salary payments to the end of the month contained in the latest public sector pay settlement as the related social security contributions will only be recorded in the following month, resulting in a one-off gap at the end of 2003. Therefore, the statutory pension insurance fund is likely to record a deficit in 2003, too.

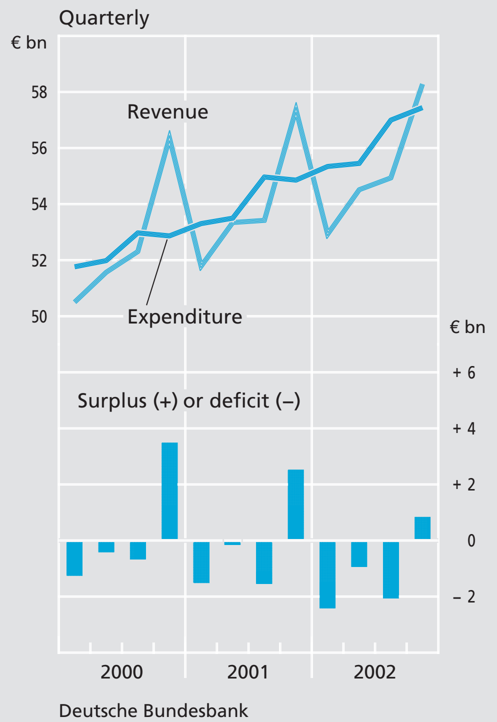
Federal Labour Office

The Federal Labour Office saw its deficit reach €1 billion in the fourth quarter of 2002, after recording a surplus of €½ billion in the same period of 2001. A marginal decrease in revenue from contributions contrasted with a steep increase in expenditure of just under 11%. In 2002 as a whole the financial gap amounted to €5½ billion, which was almost three times as high as the outturn in 2001 and as the budgeted deficit for 2002. While revenue grew by only ½%, expenditure rose by 7½%. The cost of unemployment benefit went up by almost 10%, chiefly as a result of a jump in the number of recipients.[5] Expenditure on active labour market measures rose by 1½%. Whereas spending on job creation measures fell by over one-sixth, spending on vocational training expanded by just under 6%.

Outlook for 2003

Despite the assumed anticipated further increase in the number of unemployed persons by 80,000 to 4.14 million, the Federal Labour Office's budget plans do not foresee a deficit in 2003. However, the macroeconomic trend is now being assessed more negatively and, according to the Annual Economic Report presented at the end of January, a steeper rise in the number of unemployed persons (to around 4.2 million) is now expected. This will lead to additional risks for both revenue and expenditure. Furthermore, it is uncertain whether the total budgetary relief expected from the adoption of the laws on modern labour market services (Hartz reforms) will actually be realised. Unless additional savings are made in the field of active labour market policy schemes which are significantly higher than those already envisaged in the budget, a Federal Government grant may be necessary in 2003, too, to offset a new deficit.

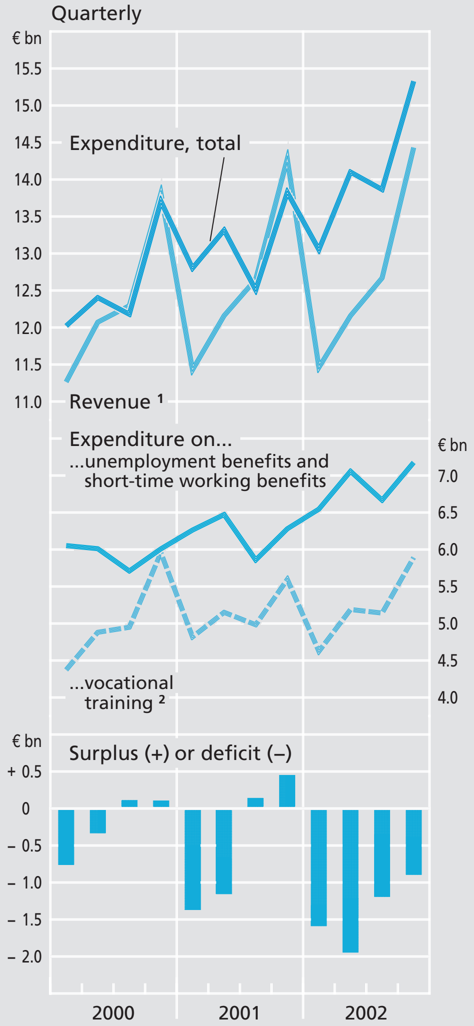
Wage and salary earners' pension insurance scheme



5 The number of unemployed persons averaged 4.06 million during the year (compared with 3.89 million forecast in the budget plans) and the number of people receiving unemployment benefit also exceeded the estimate by some 170,000.

Federal Labour Office

Quarterly



1 Excluding Federal Government liquidity assistance. — 2 Including job creation measures.

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Statutory health insurance scheme

Health insurance contributions were increased at the beginning of 2002, in part in order to replenish the reserves following the substantial deficit sustained in 2001. The average rate went up by over 0.3 percentage point to 14.0%. This was the main reason why the revenue of the statutory health insurance funds grew by just under 3½% in the first three quarters. However, expenditure grew nearly as fast, fuelled primarily by a surge in the outflow of funds spent on pharmaceuticals and hospital treatment. The outturns of the other social security sectors indicate an unfavourable contribution trend in the fourth quarter of 2002, which means it is unlikely that the deficit was lower last year than the almost €3 billion recorded in 2001. This year numerous measures are envisaged, which should yield total savings of €3 billion, such as compulsory discounts in the pharmaceutical sector, a freeze on budgets for hospital and doctors' fees and making it harder for patients to switch to private health insurance schemes by raising the earnings ceiling below which such a switch is not possible. Even so, many statutory health insurance institutions had to raise their contribution rate again perceptibly, so that the average rate is now probably around 14.4%.

General government budget trends

Deficit ratio over 3% in 2002

According to the preliminary outturn, the general government deficit ratio, as defined in the Maastricht Treaty, was 3.7% in 2002 compared with 2.8% in 2001.[6] On 21 January the Ecofin Council decided that Germany has an excessive deficit as defined in the Maastricht Treaty (see box on page 53). Whereas the sharp rise in the deficit in 2001 was largely attributable to the sizeable tax cuts and was therefore of a structural nature, the fiscal policy stance in 2002 had little bearing on the increase in the deficit. The main

6 At the beginning of each year, the Federal Statistical Office publishes the preliminary national accounts outturn for the previous year, in which the development in the fourth quarter, in particular, is largely estimated.

The excessive deficit procedure applied to Germany

In the Maastricht Treaty adopted in 1992 – which was later concretised and supplemented by the Stability and Growth Pact – the member states of the European Union committed themselves to avoiding excessive deficits. In particular, the provisions stipulate that the government debt ratio and the deficit ratio may exceed their respective reference values of 60% and 3% only in very exceptional circumstances. This is intended to ensure sound public finances and *inter alia* make it easier for the European Central Bank to carry out its task of safeguarding price stability. To ensure compliance with these provisions, an early warning system for undesirable fiscal developments and a system of sanctions ("excessive deficit procedure") were established. A year ago the European Commission recommended that an early warning be issued to Germany (and also to Portugal) because it had fallen well short of the targets set in the 2001 stability programme and its deficit ratio was very close to the 3% ceiling. However, the Ecofin Council did not put the Commission's recommendation to the vote since Germany had already promised to try to comply with the reference value for the deficit ratio in 2002 and to achieve a close-to-balance budget by 2004.

Last November the European Commission forecast a deficit ratio for Germany of 3.8% in 2002. A similar figure was assumed in the German stability programme which was updated in December. On 21 January this year the Ecofin Council, acting on a recommendation from the European Commission, then decided that an excessive deficit existed in Germany. After Portugal, Germany thus became the second country since the beginning of monetary union for which an excessive deficit procedure has been set in train. At the same time, the Council issued a recommendation to Germany. It calls for the German government to correct its excessive deficit as rapidly as possible. In addition Germany is urged to seek resolutely to achieve the aim – based on predicted growth of 1½% – of reducing the deficit ratio in 2003 to 2¾% as envisaged in the updated stability programme. The Council's recommendation notably demands stringent budget management and the implementation of the measures announced for this year, amounting to 1% of GDP. In line with the provisions of the Stability and Growth Pact, Germany has been given a deadline of four months, ie until 21 May 2003, to carry this out. If any of these measures are not implemented, they should be replaced by others so as to maintain the overall volume of consolidation. Finally, the Council recommended Germany to prevent its debt ratio from increasing further in 2003, and to reduce it in subsequent years. If Germany fails to carry out these recommendations, further steps will be taken which may ultimately lead to the imposition of sanctions, which may include severe fines.

In its opinion on the updated German stability programme, the Council considers the real growth rate expected for 2003 of 1½% (which has since been revised to 1% in the Federal Government's Annual Economic Report) to be overly optimistic. In order to enhance the country's growth potential, the Council calls for reforms of the labour market and the social security systems. In the Council's view, the objective of reaching a structural budget position that is close to balance by 2006, as envisaged in the programme, is attainable only if the announced measures are implemented in full, the expenditure targets for 2003 and 2004 are met and strict spending limits are set for the subsequent years, too. Given these provisions, the structural budget position would improve by more than 0.5% of GDP each year except in 2005. The German authorities have been requested to ensure that the next stages of the tax reform in 2004 and 2005 are compatible with a steady adjustment path towards a balanced budget. Although the Council welcomed the agreements on the "national stability pact", it considered them insufficient to guarantee compliance with the general government budget objectives in the context of Germany's federalist system.

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reason for the rise was the much weaker revenue trend both of central, state and local government and of the social security funds. The overall taxes and social security ratio receded by almost ¾ percentage point, even though some excise taxes and health insurance contributions were raised substantially. Revenue from taxes and social security contributions developed far more unfavourably than would have been expected based on the development of nominal GDP. Not least, temporary factors, such as write-downs in the corporate sector, are also likely to have had an impact.

In 2002 expenditure grew by 2% and thus somewhat more sharply than in 2001 (1¾%), even though several extraordinary burdens had been recorded in 2001 – especially for the *Land* Governments. Expenditure in 2002, however, was fuelled particularly by the increase in child benefit and the marked rise in labour market-related spending. The outlays of the social security funds went up considerably more sharply (by 3½%) than those of central, state and local government (2%, or 1% excluding transfers to the social security funds). Among other factors, lower investment spending and – in view of the favourable interest rate – broadly stagnating interest expenditure had a dampening effect on the overall expenditure of central, state and local government.

2003 marked by great uncertainty

The development of public finance in the current year is marked by great uncertainty ensuing from geopolitical and macroeconomic risks. Furthermore, various fiscal projects are still being debated in parliament, and the impact of some measures which have already been adopted is difficult to gauge. Nevertheless, from the present vantage point it still seems feasible to reduce the general government deficit ratio to a maximum of 3%. If the planned consolidation package is implemented in full and, concurrently, a stringent budgetary course is maintained in line with the Financial Planning Council's guidelines, the deficit ratio is still likely to fall noticeably even if real GDP growth is weaker than the figure of 1½% assumed in the German stability programme. The revenue trend, in particular, will make itself felt because the taxes and social security ratio will rise considerably in the wake of the higher contribution rates to the statutory pension insurance scheme and the statutory health insurance fund and the tax measures (primarily concerning excise taxes). Lowering the high deficits of the social security funds will necessitate introducing and implementing reforms of the statutory health insurance system and the Federal Labour Office and, in addition, keeping expenditure under tight control.

Stability programme envisages balanced budget by 2006

The updated German stability programme presented in December emphasises the importance of the European Stability and Growth Pact as the anchor of a stability-oriented fiscal policy in Europe. According to the medium-term forecast, the general government deficit ratio is to be lowered to 2¾% this year and completely eliminated by 2006 (see table on page 55). This is to be attained by reducing the government expenditure ratio by 4 percentage points while leaving the taxes and social security ratio unaltered. The forecast is based on the assump-

Key data of the Federal Government's updated stability programme

in %

Item	2001	2002	2003	2004	2005	2006
Basis scenario:						
Real GDP growth						
Stability programme 2002	0.6	½	1½	2¼	2¼	2¼
Stability programme 2001	¾	1¼	2½	2½	2½	–
Deficit ratio (–)						
Stability programme 2002	– 2.8	– 3¾	– 2¾	– 1½	– 1	0
Stability programme 2001	– 2½	– 2	– 1	– 0	– 0	–
Debt ratio						
Stability programme 2002	59.5	61	61½	60½	59½	57½
Stability programme 2001	60	60	59	57	55½	–
Structural deficit ratio (–)	– 2¾	– 3	– 2	– 1	– 1	– ½
Risk scenario (stability programme 2002):						
Real GDP growth	0.6	½	1½	2	2	2
Deficit ratio (–)	– 2.8	– 3¾	– 2¾	– 1½	– 1	– ½

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tion that the agreements reached by the Financial Planning Council to limit spending are observed and that an economical expenditure policy is pursued up to 2006. Further assumptions are that the planned consolidation measures will be implemented largely in line with the government's decisions from last autumn, that the budgets of the social security funds will close more or less in balance and that the overall economic climate will improve steadily over the next few years. In the meantime, however, the Federal Government – in its Annual Economic Report – has assessed the macroeconomic outlook for 2003 less favourably. The expectation for real GDP growth was lowered by ½ percentage point to around 1%. Nonetheless, the deficit ratio is still not expected to exceed 3%.

Uncertainty also concerning fiscal policy orientation

The past two years in Germany were marked by a dramatic increase in the general government deficit. Starting from a non-balanced budget in 2000 when the economic climate was favourable, this resulted last year in an overshooting of the 3% ceiling set by the Maastricht Treaty. The deficit increase and the general fiscal policy discussion have contributed to widespread uncertainty, particularly since doubts have arisen regarding the manageability and the future orientation of fiscal policy, and the fiscal policy framework in Europe has been called into question in some quarters.

Sustainable consolidation through implementing the announced course

German fiscal policy is now faced with the task of reinforcing public confidence in the ability of government to govern and in the national and international fiscal rules by implementing a sustainable consolidation process. In the shorter term – even based on the less favourable outlook for macroeconomic growth assumed in the Annual Economic Report – every effort should be made this year, as also demanded by the Ecofin Council, to implement the announced extent of the fiscal measures and to comply with the national agreements at all budgetary levels to ensure that the 3% deficit ceiling is not breached. In the medium term the strategy outlined in the stability programme of reducing government activity with a view to reaching a balanced budget position and subsequently facilitating further tax cuts should be vigorously supported as this would improve the conditions for achieving growth. All levels of government should therefore critically reappraise their current service level and not baulk at making unpopular decisions. Each of the tiers of government should be obligated to achieve a balanced budgetary position in the medium term.