Public finances*

General government budget

In 2010, small rise in deficit but considerable structural deterioration

This year, the deterioration in German public finances will not be as sharp as initially predicted owing, in particular, to the unexpectedly strong economic upturn. Nonetheless, both the structural deficit and the debt ratio are rising significantly. The deficit ratio is likely to increase to around 3½%, after reaching 3% last year. While the fiscal policy stance is expansionary, not least because of additional stabilisation measures, this development is being bolstered by the positive cyclical influence[1] and one-off effects, most notably the proceeds from the auction of mobile phone frequencies. The debt ratio, which soared to 73.4% in 2009, will continue its steep rise, mainly as a result of the risk assets that were assumed when bad banks were set up for WestLB and HRE.

Falling revenue ratio…

The government revenue ratio will decline significantly in 2010. The sizeable tax cuts are the main factor behind revenue shortfalls. By contrast, in the case of social security contributions, the financial effects of the various measures are largely balancing each other out. In addition, the growth structure is depressing the revenue ratio, as – unlike in 2009 – key macroeconomic reference vari-

* The analysis in the "General government budget" section is based on data contained in the national accounts and on the Maastricht ratios. The subsequent reporting on the budgets of the various levels of government and social security schemes is based on the budgetary figures as defined in the government's (budgetary) financial statistics.
1 The cyclical component of the improvement in the fiscal balance is significantly smaller than GDP growth would suggest, as key macroeconomic reference variables for revenue are showing a weaker development than GDP. See also Deutsche Bundesbank, Germany in the financial and economic crisis, Fiscal policy, Monthly Report, October 2010, pp 71-85.

ables for general government revenue are likely to see a weaker development than gross domestic product (GDP).

... and expenditure ratio

The expenditure ratio, too, is likely to fall markedly after soaring in 2009. These fluctuations in the ratio largely reflect economic developments. The GDP in the denominator of the expenditure ratio is a particularly significant factor in this respect. After cyclical adjustment, there is actually a further slight increase in the expenditure ratio. Above all, the rise in healthcare costs is disproportionately large, as in the preceding years. Two additional factors are the rising outlays resulting from the economic stimulus packages and the further increase in child benefit. By contrast, the expiry of the car scrappage scheme and the child bonus, and the proceeds received in May from the auction of mobile phone frequencies all had an alleviating effect.[2]

Improvement in 2011 due to economic developments and consolidation strategy

As things stand, the general government deficit is likely to fall below the 3% threshold in 2011. Although certain one-off effects will expire (auction of mobile phone frequencies, higher insolvency benefit contributions), the economic trend is likely to further reduce the deficit. Furthermore, the previously expansionary fiscal policy stance will be reversed. A number of economic stimulus measures are gradually being phased out, and government investment is also likely to fall. In addition, the general contribution rates to the statutory health insurance scheme[3] and the Federal Employment Agency will be raised. Moreover, austerity measures will have an impact on the central government budget. All in all, the revenue ratio could remain almost constant, while, given the emerging expenditure trend, which is muted in comparison with the aggregate growth outlook, the expenditure ratio will probably fall significantly.

Very favourable conditions for fiscal policy exit

In retrospect, it is clear that the financial and economic crisis has had a key impact on the development of public finances both in 2009 and in 2010.[4] In 2009, the deficit ratio rose sharply owing mainly to the automatic stabilisers and the additional fiscal policy support measures. This year, it is increasing again, as the fiscal policy stance is still expansionary – alongside a favourable economic trend. Furthermore, the debt ratio has soared from its pre-crisis level, which was already overly high, and additional budgetary risks in the form of extensive guarantees have been taken on in the wake of the financial and sovereign debt crisis. Better-than-expected economic and budgetary developments mean that there is now a chance of bringing the deficit back below the 3% threshold more rapidly and achieving the aim of a balanced budget more quickly. This would also limit the increase in government indebtedness, which remains substantial despite the more favourable trend. To this end, a strict austerity course should be pursued at all levels in line with the underlying intent of the national and EU budgetary rules. No conces-

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2 In the government's national accounts, the purchase and sale of non-financial assets are netted out and recorded on the expenditure side. The auction proceeds thus reduce expenditure (as was the case with the proceeds from the sales of UMTS mobile telephone licences in 2000), whereas in the government's (budgetary) financial statistics they increase revenue.
3 Owing to reforms, the additional revenue generated by further increasing the general contribution rate from 14.9% to 15.5% will probably only be partly offset by higher expenditure in 2011.
4 See Deutsche Bundesbank (2010), op cit, pp 71-85.

sions should be made in terms of the planned consolidation path. Unlike so often in the past, the necessary budgetary consolidation could thus be implemented under favourable conditions. It remains to be seen whether policymakers will comply with the objectives of the new budgetary rules and resist the temptation to postpone the necessary consolidation when times are good.

Improve EU rules for crisis prevention and management by…

The public finance situation is particularly dramatic in certain euro-area member states. In order to restore confidence in the sustainability of public debt, it is crucial that the euro-area countries strictly comply with the minimum requirements for budgetary consolidation at EU level and, in addition, take every opportunity to reduce their deficits more rapidly. Furthermore, the European institutional arrangements for crisis prevention and crisis management must likewise be improved. In the run-up to the crisis, the European fiscal framework and its implementation ultimately did not suffice to ensure sound public finances in all member states.

… tightening the Stability and Growth Pact…

The changes to the Stability and Growth Pact set in motion by the European Council at the end of October may result in progress vis-à-vis the *status quo*. However, these changes are yet to be fleshed out. The key factor here is to strengthen fiscal discipline as extensively as possible. However, it is already becoming evident that the adjustments will fall short of the more ambitious ideas proposed by the European Commission, among others. There appears to have been no majority for a larger degree of automatism and no details have yet been specified for a greater obligation to comply with the debt criterion. The way in which the Ecofin Council implements the rules will thus remain crucial in future. In addition to the changes to the fiscal policy framework, it is planned that more intensive macroeconomic oversight will ensure that serious problems are identified and combated at an early stage. However, it is advisable to guard against attempts at macroeconomic fine-tuning. Such requirements should, above all, help to avoid serious problems and imbalances, such as those relating to unsustainable current account deficits.

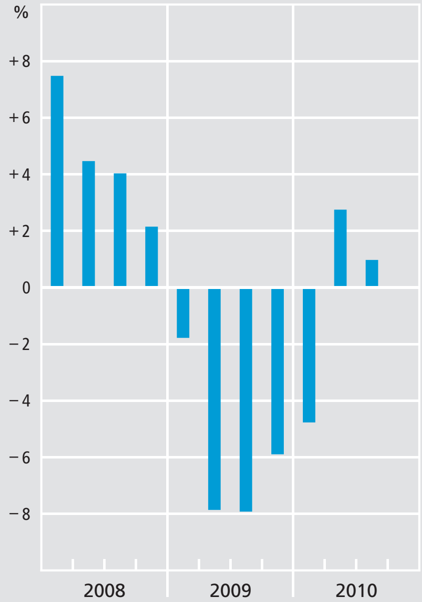
… more intensive macroeconomic oversight…

… and a crisis resolution mechanism with the participation of private creditors

The European Council has also laid the foundations for setting up a crisis resolution mechanism. In particular, the reaffirmation of the principle that neither the union nor the member states are liable for the debt of other member states is to be welcomed. This, along with the principle of autonomous responsibility for national fiscal policy, is a cornerstone of the existing union. Private creditors should not be absolved of their responsibility and there should be no one-way transfer of risks to the union. A crisis resolution mechanism that can, in very exceptional cases where the stability of the currency union is at risk, provide government aid based on strict conditionality and a very limited timeframe must not distort incentives for fiscal policymakers and investors. A transparent and predictable procedure which also notably guarantees a comprehensive and credible consolidation and reform programme could, in conjunction with improved financial market regulation, narrowly limit the risk of a systemic crisis. Relatively extensive sanctions in cases where the stability of the currency union is jeopard-

Tax revenue*

Year-on-year change, quarterly



* Including EU shares in German tax revenue, excluding receipts from local government taxes.

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ised should also be a key element of this new fiscal framework.

Budgetary development of central, state and local government

Tax revenue

Slight rise in tax revenue in Q3

In the third quarter of 2010, tax revenue[5] was up by 1% on the year (see chart above and table on page 65). The shortfalls caused by extensive tax breaks[6] were thus more than offset by the positive underlying trend. Receipts from income-related taxes fell by a total of 1½%. This decline was mainly attributable to shortfalls in revenue from wage tax as a result of the relief measures and the increase in child benefit. By contrast, profit-related taxes posted a considerable overall rise (+9%). The positive underlying trend in assessed income tax was strengthened by a fall in deduction amounts (refunds to employees and grants to investors and homebuyers). Corporation tax revenue increased strongly from the level recorded one year previously, which was very low as a result, in particular, of high refunds. In contrast to the assessed taxes, investment income tax (primarily on dividends, interest income and capital gains) saw a steep net decline in revenue. Receipts from consumption-related taxes rose by 2%.

Small revenue rise expected for 2010 as a whole

According to the latest official tax estimate, tax receipts for 2010 as a whole are expected to rise by just under ½% (including local government taxes) on the year.[7] Although, on balance, changes in tax legislation are causing substantial shortfalls (amounting to around 4% of revenue, or €20 billion), these are roughly offset by growth resulting from the economic recovery. In addition, the burdening effect resulting from the tax refunds made in 2009 in connection with the earlier unconstitutional restrictions on the standard travel

5 Including EU shares in German tax revenue but excluding receipts from local government taxes, which are not yet known for the last quarter recorded.
6 These include, above all, the extended income tax allowances for insurance contributions, the second stage of the reduction in income tax rates, preferential turnover tax treatment for the hotel trade, corporate taxation relief measures and the increase in child benefit. Unlike in the national accounts, in the government's financial statistics child benefit payments are not recorded on the expenditure side, but are deducted from wage tax receipts.
7 The estimate is based on central government's current macroeconomic projection, which foresees real GDP growth of 3.4% and nominal GDP growth of 4.1% for 2010 (May 2010: 1.4% and +1.8% respectively). In 2011, real growth is expected to be +1.8% and nominal growth +3.0% (May 2010: +1.6% and +2.4% respectively). From 2012 onward, nominal annual growth is predicted to be +2.8% (May 2010: +2.9%).

Tax revenue

Type of tax	Q1 to Q3				Q3				Estimate for 2010 [1, 2]
	2009	2010			2009	2010			Year-on-year percentage change
			Year-on-year change				Year-on-year change		
	€ billion		€ billion	as %	€ billion		€ billion	as %	
Tax revenue, total [2]	352.8	351.7	– 1.1	– 0.3	115.6	116.7	+ 1.1	+ 1.0	– 0.0
of which									
Wage tax	96.6	91.1	– 5.5	– 5.7	32.2	30.4	– 1.7	– 5.3	– 5.4
Profit-related taxes [3]	45.4	48.5	+ 3.1	+ 6.8	11.3	12.4	+ 1.0	+ 9.1	+ 6.5
Assessed income tax	18.8	23.2	+ 4.3	+ 22.9	6.7	7.3	+ 0.6	+ 8.7	+ 17.7
Corporation tax	5.3	7.4	+ 2.0	+ 38.2	0.6	1.6	+ 1.0	.	+ 41.6
Investment income tax [4]	21.2	17.9	– 3.3	– 15.4	4.0	3.5	– 0.6	– 13.8	– 15.6
Turnover taxes [5]	130.9	132.2	+ 1.4	+ 1.0	44.4	45.0	+ 0.6	+ 1.4	+ 1.4
Energy tax	24.7	24.2	– 0.5	– 2.0	9.9	10.2	+ 0.3	+ 2.9	– 0.8
Tobacco tax	9.4	9.4	– 0.0	– 0.3	3.5	3.6	+ 0.1	+ 3.1	– 0.5

1 According to official tax estimate of November 2010. — **2** Including EU shares in German tax revenue, excluding receipts from local government taxes. — **3** Employee refunds, grants paid to homebuyers and investors deducted from revenue. — **4** Withholding tax on interest income and capital gains, non-assessed taxes on earnings. — **5** Turnover tax and import turnover tax.

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allowance for commuters has now come to an end. A clear rise in receipts from profit-related taxes is expected for 2010 following last year's sharp decline from the high level recorded in 2008. The tax ratio as defined in the government's financial statistics will fall by just under 1 percentage point to 21.1%, essentially as a result of the changes in tax legislation.

Strong growth again in 2011 …

A steeper rise in revenue of just over 2% is expected for 2011. Although the economic trend will weaken perceptibly, and a negative special factor was included in these calculations,[8] the revenue shortfalls resulting from the legislative changes that were taken into account in the estimate will be much smaller on balance than in 2010. In 2012,[9] tax revenue is projected to climb by just under 5%.

… and further acceleration in 2012

Given a similar overall impact from the economic trend to that in 2011, the above-mentioned special factor will largely have come to an end, and legislative changes will have a positive net influence. Following a further marginal decline in 2011, the tax ratio would thus rise again to 21.3% in 2012.

8 The Federal Government is expecting a ruling this year in the Meilicke case regarding the treatment of corporation tax paid abroad in the taxation of dividends under the tax imputation procedure that was abolished in 2001. Temporary burdens arising from tax refunds are therefore included in the official tax estimate (a total of €5 billion, of which just over €3½ billion in 2011 and the remainder in 2012).
9 In a change from previous practice, the forecast for the year after next was also updated. From 2011, an estimate will be made in November for the medium-term planning period of the following year (eg forecast for 2011 to 2016 in November 2011), as the data will, in future, be needed at an earlier stage owing to a change in the procedure for drawing up the central government budget.

No account yet taken of planned legislative changes

As the official tax estimates are based on the legislative *status quo*, a number of measures that are to be adopted before the year is out (nuclear fuel tax, air traffic tax, reduction of energy and electricity tax concessions for the production sector, amendments to regulations on the tax allowance for an office at home) have not yet been included in the calculations. From 2011 onward, these measures are expected to lead to additional receipts totalling around ½% of revenue.

Revenue clearly above previous forecast

Compared with the previous official estimate in May, revenue expectations have been raised considerably. Adjusted for the legislative changes that have since been made, which are small in number, additional revenue is predicted to rise from €15½ billion this year to €23½ billion in 2012. This changed assessment is due crucially to the significantly more favourable macroeconomic fundamentals.

Central government

Only slight rise in deficit in Q3

Central government posted a deficit of €16½ billion in the third quarter of 2010. The year-on-year deterioration came to just over €½ billion and was thus much smaller than in the preceding quarters. Revenue fell by 3½% (-€2½ billion). Owing to higher transfers to the EU budget, there was a decline of 2% (-€1½ billion) in tax receipts. There were further burdens amounting to almost €1½ billion owing to the fact that – as in the previous quarters – the Federal Employment Agency had not yet made its reintegration payment. There was also a fall in expenditure (-2%, or -€1½ billion). This was mainly attributable to the sharp decrease of €4½ billion in interest expenditure, although this was largely due to the outpayment for the coupon date at the beginning of July being brought forward. However, central government also continued to benefit from the exceptionally favourable financing conditions. By contrast, payments to the social security funds rose significantly.[10]

Deficit for year as a whole considerably lower than projected

The 2010 central government budget envisages net borrowing of €80 billion. The Federal Ministry of Finance already presented a revised assessment in June with an improvement of €15 billion in the result. At the end of the third quarter, the deficit stood at €43 billion. Last year, a deficit of €10 billion was recorded in the final quarter, but this year's fourth-quarter figure should be much lower. The reintegration payment of almost €5½ billion from the Federal Employment Agency will not be made until around the end of the year. At the same time, central government's fourth-quarter payments to the Federal Employment Agency are likely to be lower than they were a year earlier. Furthermore, a significant fall in interest expenditure is expected. All in all, the latest tax estimate predicts a year-on-year improvement of €1½ billion, which should compensate for further additional burdens in connection with the health insurance fund. For 2010 as a whole, there is thus likely to be a deficit of around €50 billion, which is just over €15 billion lower than in the June estimate. After adjustment for the

10 Of the €2½ billion increase, €1½ billion was accounted for by the health insurance fund alone owing to the one-off grant in 2010 and higher regular transfers. The Federal Employment Agency and the statutory pension insurance scheme each received additional funds of €½ billion.

cyclical component and financial transactions, this results in a structural deficit of under €45 billion from today's perspective, which is thus around €10 billion lower than was expected in June.

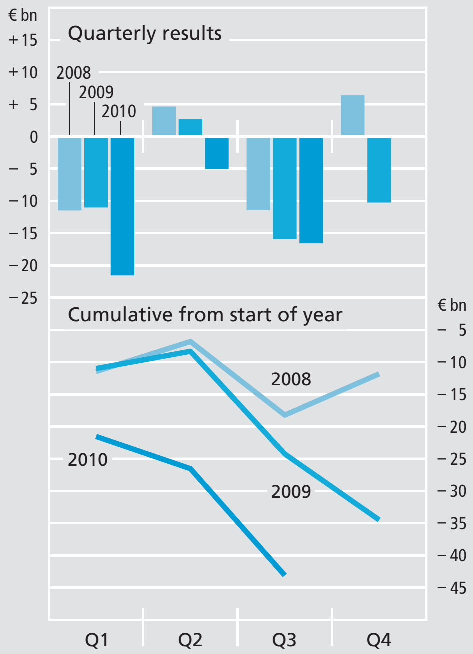
Further improvement expected for 2011

Following the Budget Committee's adjustment meeting, net borrowing of €48½ billion is envisaged for the 2011 central government budget. This is €9 billion lower than in the cabinet decision in July.[11] This is mainly attributable to tax revenue, which is now expected to be €7½ billion higher according to the November tax estimate. In addition, labour market costs, in particular, are estimated to be somewhat lower. Excluding the cyclical component and financial transactions, the structural deficit is projected to be just over €40 billion. Overall, the budget thus seems to be based on conservative calculations. If, at the same time, the measures from the austerity packages achieve the desired easing effect, a better outcome can be expected, in particular, for tax transfers to the EU budget, interest expenditure and labour market costs.

Implementation of debt brake warrants criticism

With regard to the new debt brake, the fact that it will apparently not be rigorously implemented even in the first year is a bad sign. When it was adopted in the spring of 2009, it was agreed, given considerable uncertainty about the likely course of macroeconomic developments, that there should be a transitional period up until 2016 during which the structural deficit recorded in the base-year 2010 would be reduced in equal steps. As the crisis-related strains are now obviously having a much smaller impact on the central government budget than was initially feared, the

Central government fiscal deficit/surplus



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base value – and thus the scope for new borrowing up until 2015 – should be reduced accordingly. In the summer, the German government rightly updated its adjustment path, but now evidently intends not to lower the base value further in line with the latest data. This gives policymakers greater discretion for new borrowing over the next few years which, if fully used, would – as so often in the past – put off the consolidation necessary when times are good until later years. The debt level might then be just over €25 billion higher by 2016 – with knock-on effects on the interest burden for future budgets. The clearly documented legislative intent of the new debt brake, which is currently regarded as a model for ensuring sustainable public

11 See Deutsche Bundesbank, Public finances, Monthly Report, August 2010, pp 61-72.

finances in other euro-area countries, too, would thus be violated on the very first occasion it was applied, thereby undermining confidence in the long-term effectiveness of the reform.

Off-budget entities record deficit again

As in the previous year, central government's off-budget entities recorded a total deficit of just over €1 billion in the third quarter of 2010. There were net outflows of just over €1½ billion from the Investment and Repayment Fund. Above all, there were large payments (€1 billion) for state and local government investment activities. Since the spring of 2009, however, there have been outflows of only €3½ billion, or just over one-third of the total volume of €10 billion. The legally binding aim of calling at least half of the funds by the end of 2009 was thus very clearly undershot. Again, this shows the difficulty of using government investment in a targeted manner to swiftly stabilise macroeconomic developments. The Financial Market Stabilisation Fund, from which assistance measures can only be requested until the end of the year, posted a surplus of €½ billion, above all as a result of proceeds from the provision of guarantees. The other off-budget entities once again recorded an almost balanced overall result. The deficit of all of the off-budget entities taken together is likely to have increased again by the end of the year and may be in the order of €10 billion for 2010, compared with €22 billion in 2009.

State government[12]

In the third quarter, too, the state government budget situation was somewhat better than it had been a year earlier.

Improvement continued in Q3

The deficit fell from just over €6 billion in the same quarter of 2009 to €5½ billion. Revenue rose by 3½% (€2 billion). Payments from the Investment and Repayment Fund alone, which initially go to the federal states, increased by €1 billion. In the wake of the economic recovery, tax revenue also climbed by 3%. At the same time, expenditure saw a rise of 2% (just under €1½ billion). Staff costs increased further, not least as a result of wage adjustments, and growth was likewise recorded in fixed asset formation and, to a lesser extent, other operating expenditure. By contrast, there was a further sharp decline in interest expenditure and in general grants to local government, which are generally linked – with a time lag – to the level of tax revenue.

High deficit expected for 2010 as a whole and no major decline in 2011

The deficit in the state government budgets is likely to be markedly below the previous year's figure (€25 billion). However, excluding the recapitalisation of BayernLB (€7 billion), which was reflected in the cash position in 2009, the deficit will be at roughly the same high level as in 2009 despite the additional revenue now forecast. There is no prospect of a major decline in 2011, either. The expected increase in revenue is likely to be eclipsed by significant growth in expenditure. Staff costs, other operating expenditure and general grants to local government are on the rise. Furthermore, particularly after a ruling by the Constitutional Court for the Federal State of

12 The development of local government finances in the second quarter was analysed in greater detail in the short articles in the Bundesbank's October Monthly Report. These are the most recent data available.

North Rhine-Westphalia,[13] it is to be expected that state government will have to bear a greater share of the costs of the expansion in child day care facilities.

Threat of budgetary hardship in Berlin, Bremen, Saarland and Schleswig-Holstein, ...

On the basis of the stability reports presented by central government and the federal states, the Stability Council stated at its second meeting in mid-October that there are signs of imminent budgetary hardship in four of the five states which are to receive consolidation assistance (Berlin, Bremen, Saarland, Schleswig-Holstein).[14] An evaluation committee is to examine the budgets of these federal states in more detail by May 2011; on this basis, the Stability Council will decide whether the states are considered to be in budgetary hardship and, where appropriate, agree on a programme of restructuring. In order to prevent the necessary consolidation from being postponed, the agreed consolidation assistance is essentially tied to a gradual reduction in the initial structural deficit, for which the calculation method and data timeframe have not yet been agreed. Great efforts will be needed from the federal states concerned. However, in view of the present favourable economic outlook, it is strongly advisable for other federal states with high deficits to swiftly consolidate their budgets, too, even though the transitional period will last until the end of 2019. A secure legal framework could be created to achieve this by promptly enshrining the debt brake in the constitutions of the federal states and by passing implementation acts that also stipulate binding rules for the transitional period. This has already been put into practice by Schleswig-Holstein, and the parliament of the state of Hesse, for example, is now working on a draft to amend its constitution. The amendment borrows heavily from the German constitution (Basic Law) but is not yet tied to implementation provisions. In addition, there are no clear regulations for the transitional period.[15]

... but rapid and stringent implementation of debt brake needed in other federal states, too

Social security funds[16]

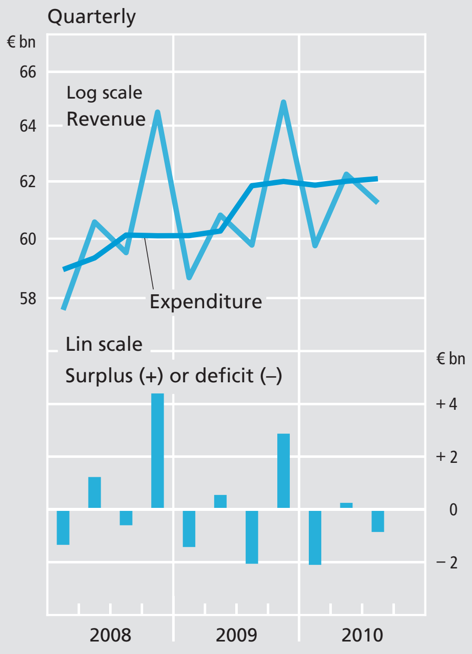
Statutory pension insurance scheme

Positive contribution trend, weaker expenditure growth

The deficit recorded by the statutory pension insurance scheme came to just under €1 billion in the third quarter, after being more than twice as high a year earlier. Whereas revenue increased by 2½%, expenditure grew by only ½%. Employees' compulsory contributions climbed by as much as just under 3% on the year.[17] On the expenditure side, following the waiver of the pension adjustment scheduled for mid-2010, the pension payments were only slightly above the level recorded in the same quarter of 2009 (+½%).

13 Although this ruling is only binding for North-Rhine Westphalia, it is likely to be relevant for numerous other federal states owing to the principle of connexity enshrined in most state government constitutions.
14 See the press release and the documents provided at http://www.stabilitaetsrat.de/DE/Home/home_node.html (in German only).
15 See also the Bundesbank's statement on the consultation in the state parliament of Hesse at http://www.hessischer-landtag.de (in German only).
16 The financial development of the statutory health and public long-term care insurance schemes in the second quarter of 2010 was discussed in the short articles of the Monthly Report of September 2010. These are the most recent data available.
17 As the figure for compulsory contributions also includes the contributions made for short-time workers, which are now down significantly on the year, the inflow of contributions related to actual pay developments actually rose even more steeply.

Finances of the German statutory pension insurance scheme



Safeguard clause causes substantial additional expenditure

Without the extension of the safeguard clause, the pension payment amounts in western Germany would have been cut by around ½%, as per capita earnings there declined in 2009. Over the past few years, the safeguard clause has prevented pension cuts amounting to 3.8% in western Germany and 1.8% in eastern Germany. For the statutory pension insurance scheme, this has resulted in additional expenditure of around €8 billion per year, which is equivalent to around 0.8 percentage point of the contribution rate. In the coming years, the calculated pension increases are to be halved until the pension cuts that were waived have been offset in order to comply with the long-term contribution rate targets.[18]

Financial deterioration due to central government's austerity package

The favourable revenue trend and moderate expenditure trend can be expected to continue throughout the rest of the year. It can therefore be assumed that a surplus will be recorded for the year as a whole despite the cumulated deficit of just over €2½ billion for the period up to the end of September. Nonetheless, the financial situation looks less favourable for the coming year, as pension contributions on behalf of recipients of unemployment benefit II and reimbursements from central government for burdens resulting from the reunification of Germany, jointly totalling just over €2 billion, will be cut as part of the consolidation of the central government budget. In the longer term, however, this will be offset by reduced outpayments from the statutory pension insurance scheme. This will, incidentally, prevent pension payments to those who are not in need of assistance from being increased in future.

Federal Employment Agency

Clear financial improvement even after adjustment for special factors

The Federal Employment Agency posted a deficit of €¾ billion in the third quarter of 2010, compared with a deficit of €5½ billion one year earlier. However, the result for the third quarter of 2010 was distorted by the fact that no transfers had yet been made to central government to meet the reintegration payment.[19] In addition, the grant from central government was up by almost €½ billion on the year in the third quarter. Excluding these

18 The contribution rate to the statutory pension insurance scheme must be no higher than 20% in the years up to 2020 and a maximum of 22% in the years up to 2030.
19 The reintegration payment is set at €5¼ billion for the fiscal year and, in 2010, will be paid in one instalment at the end of the year rather than on a quarterly basis.

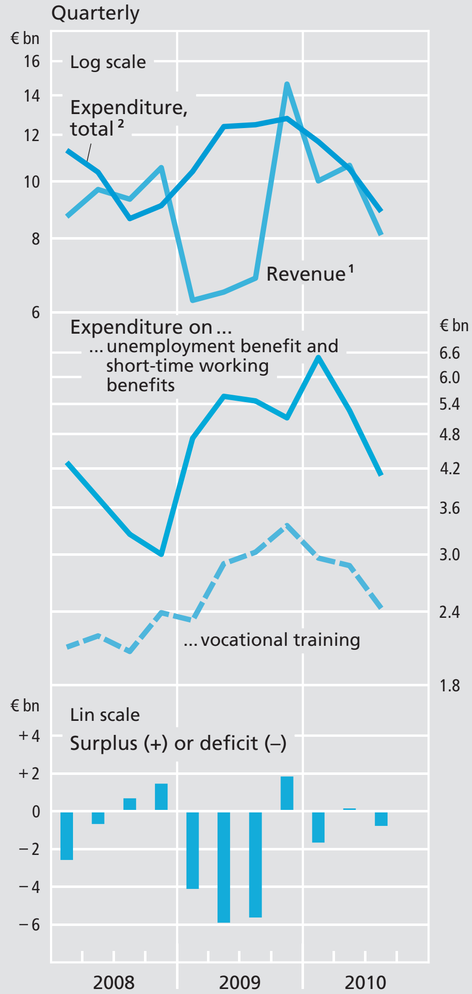
special factors, the deficit fell by €3 billion, and the increase in revenue, at 13%, was very sharp. The strong growth in the inflow of contributions (4%) was not the main factor in this development. The additional receipts from insolvency benefit contributions following the significant increase in the contribution rate for 2010 had a greater influence.[20] Excluding the reintegration payment, the Federal Employment Agency's outlays were down by 21% on the year. Spending on unemployment benefit I, short-time working benefits and active labour market policy measures (including refunds of social security contributions for short-time working made to employers, which fall into this category and have been declining sharply) was, in each case, just over €½ billion lower in the third quarter. Contrary to expectations, moreover, insolvency benefit payments remained far below the level recorded a year earlier.

Grant required for 2010 considerably lower than expected

The deficit of the Federal Employment Agency for the first nine months of 2010 came to just under €2½ billion. In operational business, only a slight deficit is to be expected at the end of the year. However, transfers amounting to almost €5½ billion to meet the reintegration payment are due before the year is out. All in all, a sizeable deficit can be expected for 2010 as a whole, although it could be smaller than the figure recently estimated by the Federal Employment Agency itself (€10 billion). €3 billion of this sum can be offset by releasing reserves. The remainder will be covered by a one-off central government grant. From 2011 onward, the Federal Employment Agency will only receive loans to

Finances of the Federal Employment Agency

Quarterly



1 Excluding central government liquidity assistance. — **2** Including transfers to the civil servants' pension fund set up in 2008.

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eliminate its deficit, which must be repaid in better times.

Contribution rate of 3% only sufficient if lasting savings are made

At the beginning of 2011, the contribution rate will be raised from 2.8% to 3.0%. How-

20 The rate for insolvency benefit contributions was raised from 0.1% to 0.41% for 2010, with the aim of compensating for the fact that expenditure on insolvency benefit payments substantially exceeded contribution receipts in 2009 and covering the outlays expected for 2010.

ever, the total revenue that can be achieved in this way and the regular central government grant will only be sufficient across the economic cycle if spending, such as on active labour market policy, is significantly and lastingly reduced. Otherwise, the Federal Employment Agency will not be able to use surpluses in better times to fully repay future central government loans.