

Public finances*

General government budget

Outlook for 2022

Fiscal policy also focused on fallout from Russian war of aggression

Fiscal policy is currently largely focused on responding to the fallout, in terms of energy, social and defence policy, from the Russian war of aggression on Ukraine. The Federal Government is planning to become independent of Russian energy supplies and accelerate the shift to renewable energy. In addition, more funds are to be channelled into defence. Other measures aim to shield households and enterprises to a degree from the steeply rising energy costs. Assistance for refugees and for Ukraine is another factor. The Federal Government intends to finance these measures with new borrowing. To this end, further emergency loans are envisaged in the core central government budget, and a special fund for the German armed forces is planned. The coronavirus crisis, too, is continuing to weigh on public finances. However, the budgetary burdens associated with the crisis are likely to decline considerably this year.

Deficit ratio could nonetheless fall markedly in 2022, as coronavirus-related burdens taper off

From today's perspective, the general government deficit is likely to decline markedly this year (2021: deficit ratio 3.7%),¹ driven predominantly by fiscal coronavirus response measures expiring. The attendant relief will outweigh the budgetary burdens resulting from newly planned support measures. Moreover, current projections continue to foresee an economic recovery, assuming that the war and its fallout do not escalate further. This will also reduce the deficit. Under these conditions, the debt ratio will drop considerably (2021: 69.3%).

Outlook for 2022 significantly less favourable than expected at start of year

The outlook for 2022 is now significantly less favourable than expected at the start of the year. This is chiefly down to additional burdens on the expenditure side, among them the new fiscal measures. In addition, the unexpectedly sharp rise in prices will drive up costs for gov-

ernment consumption, in particular. The interest burden will increase, especially for inflation-linked Federal securities. The strain from new measures will be only moderate on the revenue side,² and the stronger price increases will even have an easing effect: in April, the Federal Government projected a weaker increase in real gross domestic product (GDP) for 2022 than in January but raised its projection somewhat for nominal private consumption and gross wages and salaries. Viewed in isolation, this increases the expected revenue from taxes and social contributions. However, the fact that revenue developments were surprisingly favourable up to the end of the period under review irrespective of this has had an even more positive effect: the latest official tax revenue forecast is around €40 billion higher than the forecast from autumn 2021 (see pp. 74 ff.).

Outlook for the medium-term planning period

Next year, the deficit is likely to decline further, assuming the coronavirus crisis does not flare up again and the fallout from the war in Ukraine does not worsen. While structural surpluses were recorded before the coronavirus crisis, the coming years are likely to see signifi-

Significant structural deficits likely in the medium term; central government with broad leeway for deficits

* The section entitled "General government budget" relates to data from the national accounts and the Maastricht debt ratio. This is followed by more detailed reporting on budgetary developments (government finance statistics). No data are yet available for local government or the statutory health and public long-term care insurance schemes for the reporting quarter. These will be analysed in the short commentaries in upcoming issues of the Monthly Report.

¹ Meanwhile, the Federal Government's stability programme from April reports a deficit ratio of 3.4% for 2022, which is almost unchanged from 2021. Compared with this, developments appear likely to be more favourable. For a more detailed assessment of the national accounts projection from the stability programme, see Independent Advisory Board to the Stability Council (2022).

² The national accounts record the one-off energy price allowance as a monetary social benefit. In the government finance statistics, it reduces tax revenue. In each case, it is recorded in net terms, i.e. less the income tax to be paid on it.

cant structural deficits, mainly at the central government level. While the Federal Government announced that compliance with the debt brake would resume from 2023 onwards, it is planning to make use of the extensive general reserves, which will result in a correspondingly higher deficit. Even more extensive deficits are expected in central government's special funds, particularly the planned Armed Forces Special Fund and the Energy and Climate Fund (ECF). The additional leeway for deficits in the special funds as well as from the core budget reserves amounts to around €230 billion in total (currently 6% of GDP, see p. 77). That is likely to be all but fully utilised by 2026, meaning that the deficits could be almost 1½% of GDP higher on average between 2023 and 2026 than without that scope.

High uncertainty

Outlook uncertain: economy as a whole, measures, use of special funds

However, the outlook for this year and beyond is highly uncertain. For example, the fallout from the war could intensify further and additionally impair macroeconomic developments.³ This may lead to the adoption of additional fiscal support measures. Moreover, it is difficult to predict how outflows from central government's special funds will develop from year to year. This is likely to have a significant impact on the path of general government deficits. It is also unclear whether the ECF is even allowed to make any use of credit authorisations: the vast majority were justified under the escape clause by the need to address the coronavirus pandemic. The Federal Constitutional Court is currently reviewing some of the transfers.

Fiscal policy in a difficult economic environment

No compelling case for broad-based credit-financed fiscal stimulus at present

Government budgets are a key anchor of stability in times of crisis. That said, there is no compelling case for a broad-based credit-financed fiscal stimulus at present. The baseline scenarios of current projections generally indi-

cate that the economy is recovering. The pace of recovery may now be more subdued than previously expected, but it has not ground to a halt. Supply-side disruptions, for one, have emerged, and broad-based price pressures have started to take hold. In an economic situation such as this, additional credit-financed demand impulses have smaller real effects and tend to increase price pressures.

If developments prove to be less favourable, with the economic recovery stalling or even suffering a setback, the automatic stabilisers will initially take effect. These include, in particular, expenditure-side benefits for unemployment or short-time work. In addition to the automatic stabilisers, further fiscal stabilisation measures may also be warranted.

If crisis intensified, automatic stabilisers would initially take effect; ...

If supply bottlenecks and high price pressures persisted in this case, a broad-based credit-financed fiscal demand stimulus would still not be advisable. Additional government assistance should then ideally target households and enterprises in need. Assuming overall demand is not suffering, it would be appropriate to counterfinance such targeted measures immediately. This is because, in a scenario of supply bottlenecks and high price pressures, it would be counterproductive to further strengthen general demand. In this context, counterfinancing ultimately means that any burdens on the private sector, such as those caused by high energy costs, are directly redistributed via the government budget without further exacerbating macroeconomic disruptions.

... if supply bottlenecks and price pressures persist, counterfinancing of further targeted measures appropriate; ...

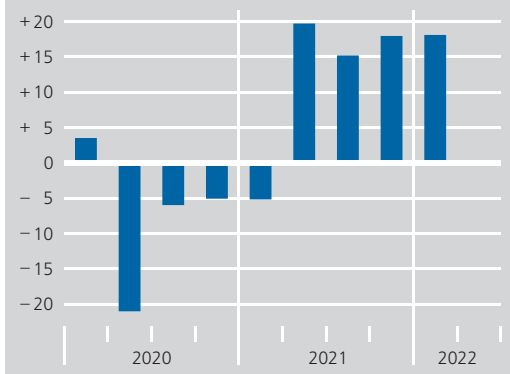
By contrast, a broad-based fiscal stimulus could be considered if demand looks set to weaken severely – for example, if export markets suffer a sizeable slump or substantial distortions on the financial markets spill over to the real economy. Given such conditions, the underlying price pressures would be expected to ease and expansionary fiscal policy to meet with underutilised capacity.

... credit-financed stimulus worth considering if demand weakens severely

³ See also Deutsche Bundesbank (2022a).

Tax revenue*

Year-on-year percentage change, quarterly figures



Source: Federal Ministry of Finance. * Comprises joint taxes as well as central government taxes and state government taxes. Including EU shares in German tax revenue, including customs duties, but excluding receipts from local government taxes.

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Energy policy: price signals set important incentives

Germany's energy policy is directed at making the country independent of Russian energy supplies as soon as possible and achieving net zero carbon emissions over the long term. These aims are well achievable, in particular, if the appropriate price signals are able to take effect. Prices reflect (relative) shortages and provide incentives to reduce energy consumption and switch to renewable energy. Government measures should not obstruct this process. Care should therefore be taken to ensure that government assistance to households and enterprises distorts price signals as little as possible.

Focus on low-income households, lump-sum transfers instead of price controls

One-off payments that top up means-tested social transfers such as the basic allowance are therefore particularly suitable for providing targeted support to households in the short term. Generally speaking, such transfers must be adjusted promptly if they would otherwise no longer cover basic needs. The one-off energy price allowance is designed differently: it will be paid out to all employees subject to income tax. As it is taxable, however, it will provide greater relief to low-income households. Irrespective of the distributional effects, the planned ad hoc energy tax cuts are detrimental for another reason: they weaken the – generally desirable – price signals.

New transfer, guarantee and loan programmes are in place for enterprises hit hard by soaring costs, disrupted supply chains or embargoes. Such programmes are relatively targeted as long as they are reserved for enterprises suffering substantial distress. They must meet the requirements of the European framework for state aid. It is important to limit such programmes to temporary crisis situations. Moreover, it is crucial that they do not hinder the necessary process of transformation. First, enterprises receiving support should have a business model that promises to be sustainable, also in view of the planned reduction of carbon emissions as part of the energy transition. Second, these programmes should maintain the incentive for enterprises to rapidly cut back on their energy consumption and turn to renewable sources.

Support hard-hit enterprises without hindering transformation

Budgetary development of central, state and local government

Tax revenue

First quarter of 2022

Over the first three months of 2022, tax revenue⁴ rose sharply on the year (+18%, or +€31 billion; see the chart above and the table on p. 73). However, this growth was also driven by sizeable base effects. First, VAT rates had been temporarily lowered in the second half of 2020, which was still dampening revenue in the first quarter of 2021. Second, revenue from import VAT was lower in the same quarter last year on a one-off basis, as the date on which payments were due had been pushed back. Third, revenue in the first quarter of 2022 is likely to have been bolstered by lower tax deferrals and the receipt of previously deferred payments.

Tax revenue grew sharply in Q1

⁴ Including EU shares in German tax revenue but excluding receipts from local government taxes, which are not yet known for the quarter under review.

Strong rise in VAT revenue

More than half of the unadjusted growth in tax revenue in the first quarter was thus attributable to VAT. Including the one-off effects mentioned above, VAT receipts shot up by 34%. Adjusted for these one-off effects, however, the increase in VAT revenue is still likely to have been considerable. It was boosted by dynamic growth in nominal private consumption and housing construction.

Wage and profit-related taxes likewise made significant contribution to growth

At 11%, growth in wage tax receipts was likewise strong. Gross wages and salaries rose dynamically, mainly because short-time work decreased considerably. Revenue growth includes the effects of fiscal drag. This was partly offset by relief in the tax scale. These measures compensate for the bracket creep expected in autumn 2020 for 2021: the basic income tax allowance was raised by 2½% and the other income tax brackets were also shifted just over 1% to the right (specified tax rates then only apply to higher nominal taxable income). Child benefit payments stagnated following the significant increase in benefits at the beginning of 2021. As child benefit is deducted from wage tax, this item rose as a result. Of the profit-related taxes, assessed income tax, in particular, saw a sharp increase. Corporation tax also grew dynamically. Advance payments for the current year, a major revenue item, recorded a considerable plus.

New tax estimate for 2022 to 2026 as well as additional tax cuts

Tax estimate for 2022 projects dynamic revenue growth of 6½%

According to the latest official tax estimate, general government tax revenue will rise by 6½% on the year in 2022 (see also the table on p. 74). This is mainly due to the dynamic economic growth in nominal terms, which is what the estimates are based on. Nominal private consumption, in particular, will rise sharply. Wages will likewise see a considerable increase – pushing up revenue, not least through progressive income taxation. Meanwhile, tax measures will have a marked dampening effect on revenue. Write-off provisions were im-

Tax revenue

Type of tax	Q1		Year-on-year change %	Estimate for 2022 ¹ Year-on-year change %
	2021	2022		
	€ billion			
Tax revenue, total ²	172.0	203.1	+ 18.1	+ 7.4
of which:				
Wage tax ³	50.9	56.2	+ 10.5	+ 8.1
Profit-related taxes	35.5	40.0	+ 12.7	+ 0.5
Assessed income tax ⁴	17.8	20.9	+ 17.3	- 3.1
Corporation tax ⁵	10.2	11.2	+ 9.6	- 0.9
Non-assessed taxes on earnings	4.3	5.1	+ 20.9	+ 17.7
Withholding tax on interest income and capital gains	3.2	2.8	- 13.6	- 14.3
VAT ⁶	54.8	73.6	+ 34.3	+ 12.9
Other consumption-related taxes ⁷	19.5	20.5	+ 5.3	+ 3.0

Sources: Federal Ministry of Finance, Working Party on Tax Revenue Estimates and Bundesbank calculations. **1** According to official tax estimate of May 2022. **2** Comprises joint taxes as well as central government taxes and state government taxes. Including EU shares in German tax revenue, including customs duties, but excluding receipts from local government taxes. **3** Child benefits and subsidies for supplementary private pension plans deducted from revenue. **4** Employee refunds and research grants deducted from revenue. **5** Research grants deducted from revenue. **6** VAT and import VAT. **7** Taxes on energy, tobacco, insurance, motor vehicles, electricity, alcohol, air traffic, coffee, sparkling wine, intermediate products, alcopops, betting and lotteries, beer and fire protection.

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proved and income tax rates lowered at the start of the year.

However, sizeable tax cuts not passed by the Bundestag until after the tax estimate was finalised have not yet been factored into it, as it only takes account of applicable law. For example, a one-off energy price allowance subject to income tax will be paid out of wage and income tax receipts to persons in employment. The fuel tax rates on petrol and diesel will be cut to the European minimum rate for three months. Furthermore, the basic income tax allowance is to be raised again retroactively from 1 January 2022. These are just some of the

However, additional tax cuts likely to considerably reduce growth

Official tax estimate figures and the Federal Government's macroeconomic projections

Item	2021	2022	2023	2024	2025	2026
Tax revenue ¹						
€ billion	833.2	889.3	928.4	964.7	997.8	1,031.7
% of GDP	23.3	23.4	23.2	23.5	23.7	23.9
Year-on-year change (%)	12.6	6.7	4.4	3.9	3.4	3.4
Revision compared with previous tax estimate (€ billion)	21.2	40.4	46.3	45.6	44.0	44.1
Memo item: Revenue shortfalls resulting from prospective tax relief (€ billion)						
Changes in tax law passed by the Bundestag ²	.	- 21.9	- 8.4	- 9.4	- 7.3	- 4.1
Revenue shortfalls if bracket creep is compensated for in same manner as previously ³	.	.	- 11.4	- 16.6	- 20.8	- 25.1
Real GDP growth (%)						
Spring projection (April 2022)	2.9	2.2	2.5	0.8	0.8	0.8
Autumn projection (October 2021)	2.6	4.1	1.6	0.8	0.8	0.8
Nominal GDP growth (%)						
Spring projection (April 2022)	6.0	6.3	5.2	2.6	2.6	2.6
Autumn projection (October 2021)	5.6	6.4	3.3	2.6	2.6	2.6

Sources: Working Party on Tax Revenue Estimates and Federal Ministry for Economic Affairs and Climate Action. **1** Including EU shares in German tax revenue, including customs duties, including receipts from local government taxes. **2** Fourth Coronavirus Tax Assistance Act (*Corona-Steuerhilfegesetz*), second Act Amending the Tax Code and the Introductory Act to the Tax Code (*Gesetz zur Änderung der Abgabenordnung und des Einführungsgesetzes zur Abgabenordnung*), Tax Relief Act 2022 (*Steuerentlastungsgesetz 2022*), Energy Tax Reduction Act (*Energiesteuersenkungsgesetz*), seventh Act Amending the Regionalisation Act (*Gesetz zur Änderung des Regionalisierungsgesetzes*), Act on Immediate Additional Children's Allowance and One-Off Payment (*Sofortzuschlags- und Einmalzahlungsgesetz*). **3** Since 2014, the income tax scale has shifted year after year, usually in line with the estimated inflation of the previous year. The figures shown here are the revenue shortfalls that will result if this practice is continued. For this purpose, the revenue effects are roughly estimated. The calculations are based on the Federal Government's current spring projection and wage tax receipts based on current tax estimates (according to the national accounts). The basic income tax allowance also shifts in line with the inflation rate of the previous year.

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measures that are planned. Overall, these steps are likely to reduce revenue in 2022 by 2½% of tax revenue.

Significant increase in revenue in tax estimate for 2023

In 2023, revenue growth is expected to amount to 4½%. Nominal macroeconomic growth will be significant and progressive taxation will continue to have a bolstering effect. On balance, legislative changes that have already been adopted and thus taken into account will not have any major effect.

Sizeable short-falls due to additional legislative changes likely in 2023, too

The tax cuts not passed by the Bundestag until after the tax estimate was finalised and therefore not factored into it will play a considerably smaller role in 2023 than in 2022, as the one-off energy price allowance and the fuel tax cut will only affect the current year. That said, the measures will still reduce next year's revenue by 1%. However, the Federal Finance Minister also announced that the Federal Government wishes to continue compensating for bracket creep in income tax. According to established

practice, the inflation forecast for 2022 released in the autumn of 2022 would be factored into the income tax scale from 1 January 2023. Owing to high inflation, this is likely to result in further revenue shortfalls amounting to just over 1% of tax revenue in 2022. In addition, the guidelines set out by the Federal Fiscal Court to prevent the foreseeable double taxation of future pensions still need to be implemented. One particular measure to this end under the coalition agreement is for the full deductibility of pension contributions to be brought forward from 2025 to 2023.

According to the tax estimate, revenue is projected to rise by an average of 3½% in the subsequent years up to 2026. On balance, legislative changes will play no major role. The forecast is therefore a fairly direct reflection of the assumptions regarding macroeconomic developments and progressive taxation. However, the basic income tax allowance is likely to be raised again in 2023 and the years that follow.

Solid growth in medium term partly reflects fiscal drag

In line with the approach taken since the middle of the last decade, further measures to compensate for bracket creep can also be expected. Given the Federal Government's macroeconomic assumptions, this would mean reductions of just under ½ percentage point in revenue growth each year. Risks also exist in connection with the solidarity surcharge, the constitutionality of which has been called into question for various reasons. All in all, tax revenue is therefore expected to be significantly lower in the medium term than indicated by the latest tax estimate.

Revision of the tax estimate compared with previous forecasts

Strong upward revisions for 2022 and subsequent years compared with autumn estimate

Compared with the autumn 2021 tax estimate, revenue is up and will reach a peak of €46 billion in 2023. One key reason for this is that the annual result for 2021 was far more favourable than anticipated – especially with respect to profit-related taxes. VAT revenue also saw stronger growth than forecast in the autumn. It was assumed that these positive developments would for the most part persist. The revised macroeconomic assumptions have also resulted in slight revenue increases. This is because the tax estimate looks at nominal developments, not the less favourable real (price-adjusted) developments. In this context, the especially high revenue-yielding macroeconomic reference variables (nominal private consumption and gross wages and salaries) were revised upwards. According to the new estimate, profit-related taxes will also develop significantly more favourably than forecast in the autumn – despite the growth rate of macroeconomic profits being revised downwards in the national accounts. The higher estimate is the product of the previous year's favourable outcome and the stable development of advance payments in the first quarter.

Upward revision also compared with pre-coronavirus outlook

Even compared with expectations from the period directly prior to the coronavirus crisis, the working group's forecast is now significantly higher than had been projected in au-

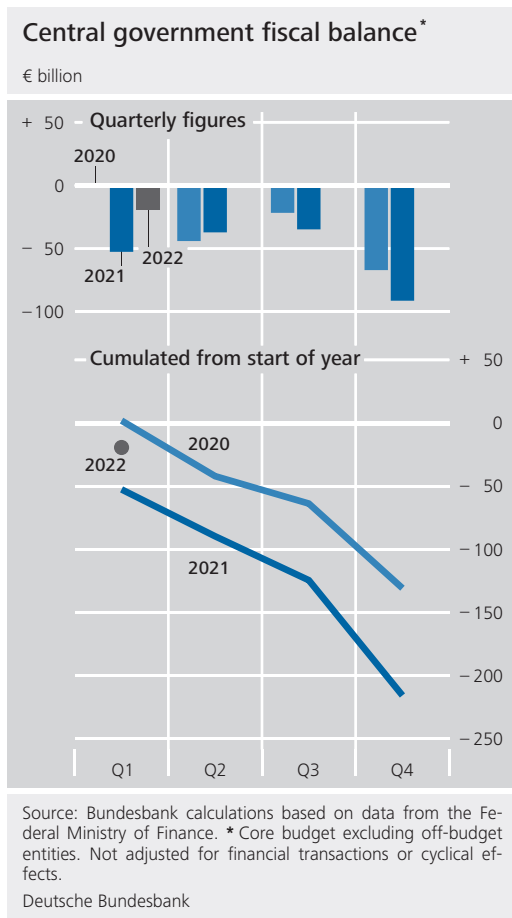
turn 2019 for these years. Revenue-reducing legislative changes enacted in the meantime will therefore be more than offset. The current estimate exceeds the autumn 2019 forecast by €14 billion for 2022. A large amount of additional revenue will be generated by unexpectedly high profit-related taxes up to the first quarter of 2022 and more favourable nominal macroeconomic assumptions. These positive influences will outweigh the revenue shortfalls stemming from legislative changes enacted in the meantime, even though such shortfalls will also be significant this year, at almost €40 billion. In 2023 and 2024, additional revenue will increase to €24 billion and €30 billion compared with the autumn 2019 estimate: the upward revision of nominal macroeconomic assumptions will become more relevant and the improved write-off provisions agreed in the meantime will cease to cause significant shortfalls.

Central government budget

First quarter of 2022

Central government posted a deficit of €19 billion in the first quarter of 2022. This constitutes a decrease of €33 billion on the previous year. Revenue rose sharply, going up by €20 billion (26%) almost exclusively on account of higher tax receipts (+28%). Only part of this could be explained by the lack of the previous burdens arising from VAT measures and savings from EU contributions (€4 billion reduction in advance deductions from tax revenue). Underlying dynamics were also strong. As in 2021, the Bundesbank did not distribute any profit because it increased its risk provisions in the wake of asset purchases. Overall, expenditure fell sharply, decreasing by €13 billion (-11%). This was mainly due to declining transfers to enterprises in response to the coronavirus pandemic (-€7 billion) and reduced loans to the Federal Employment Agency (-€6 billion).

Sharp decrease in deficit in Q1



2022 budget planning

March draft of central government budget contains pandemic-related emergency borrowing

In mid-March, the Federal Government presented a new draft of the 2022 central government budget. Like the previous government's original draft, this envisaged net borrowing of almost €100 billion. According to the new draft, the borrowing limit imposed under the debt brake was to be exceeded by €81 billion. The government justified this on the basis of an emergency resulting from the coronavirus pandemic.⁵ The draft also included the first energy price relief package. However, it did not yet account for the impact of the Russian war of aggression on Ukraine. An amendment to the draft budget was therefore announced.

The Federal Government adopted this amendment to the draft budget on 27 April, which increases the projection for net borrowing by €39 billion. A global revenue shortfall item of €13 billion covers tax revenue losses resulting from the second energy price relief package of

24 March. The amendment also includes larger allocations of VAT funds by central government to the state governments to compensate them for costs relating to refugees from Ukraine. The spending increase of €26 billion includes higher transfers for Ukraine and basic allowance benefits for refugees. It also covers new business aid, with transfers totalling €5 billion being budgeted for businesses hit hard by higher energy costs. However, the bulk of additional spending is bundled into a global precautionary item of €14 billion. Its intended purpose is to finance measures that have already been approved or for which approval is imminent.⁶

Amendment to draft budget contains additional borrowing authorisations of €39 billion for war-related budgetary burdens

The Bundestag's Budget Committee did not make any changes to the estimated net borrowing figure in its final deliberations. Owing to the now more favourable tax estimate, additional revenue will amount to €12 billion net. This is offset by higher expenditure appropriations in the same amount. On balance, the majority of these are attributable to coronavirus-related spending in the healthcare sector. In addition, estimated interest expenditure was revised upwards by €5 billion in view of interest rate developments in the capital markets. This is reflected in significantly reduced expected premia for new issues.⁷ Higher other expenditure appropriations, particularly for business aid, are offset by a decrease in budgeted global spending increases.⁸

Final deliberations: revenue increases from tax estimate offset by additional spending

Net borrowing therefore remains at €139 billion. A cyclical burden (€8 billion) and financial transactions (€3 billion) are factored out of the debt brake.⁹ On balance, this leaves a structural

Standard limit under debt brake exceeded by €116 billion

⁵ For details on the context provided back when the first draft budget for 2022 was passed in June 2021, see Deutsche Bundesbank (2021).

⁶ For the sake of budgetary clarity, it is important to attribute budgeted expenditure to specific budget items, wherever possible.

⁷ The volatility of interest expenditure could be prevented by recording premia and discounts on an accrual basis. See Deutsche Bundesbank (2022c), p. 61.

⁸ This means that, on balance, budgeted global spending cuts are the dominant factor here.

⁹ The debt brake ceased to apply to special funds without their own borrowing authorisation at the start of 2022; according to the government's March decision, it expects them to record deficits of €12 billion.

Key central government budget data in connection with the debt brake*

€ billion

Item	Actual 2020	Provisional actual 2021	Target 2022
1. Expenditure ¹	441.8	556.6	495.8
of which:			
1.a Investment	50.3	45.8	51.5
1.b Global spending increases/cuts	–	–	– 6.5
2. Revenue ^{1,2}	311.1	341.0	356.2
of which:			
2.a Tax revenue ¹	283.3	313.5	328.4
2.b Global revenue increases/shortfalls	–	–	– 1.0
3. Fiscal balance (2.-1.)	– 130.7	– 215.6	– 139.6
4. Coin seigniorage	0.2	0.2	0.2
5. Transfer to (–)/withdrawal from (+) reserves	–	–	0.5
6. Net borrowing (–)/repayment (+) (3.+4.+5.)	– 130.5	– 215.4	– 138.9
7. Cyclical component in the budget procedure	– 42.6	– 12.5	– 7.9
8. Balance of financial transactions	– 6.6	3.0	– 2.8
9. Structural net borrowing (–)/repayment (+) (6.-7.-8.)	– 81.3	– 205.9	– 128.2
10. Amount exceeding limit (12.-9.)	69.6	193.8	115.7
11. Memo item: Amount exceeding limit incl. special funds (10.-14.)	41.9	124.8	127.6
12. Standard upper limit: structural net borrowing (0.35% of GDP) ³	– 11.7	– 12.1	– 12.5
13. Structural balance (3.-7.-8.)	– 81.5	– 206.1	– 128.9
13.a As before, with estimate of potential output acc. to spring 2022 economic forecast	– 95.2	– 202.6	– 128.9
14. Memo item: Balance of off-budget entities relevant up to this point ⁴	27.7	69.0	– 11.9
14.a Energy and Climate Fund	25.3	53.9	– 6.4
14.b Relief Fund (2013 flood)	– 0.4	– 0.2	– 0.5
14.c Fund to Promote Municipal Investment	– 1.0	– 1.0	– 1.2
14.d Digitalisation Fund	1.3	0.2	– 0.2
14.e Fund for Primary School-Age Childcare Provision	2.5	0.5	– 0.4
14.f Flood Relief Fund (2021 flood)	–	15.6	– 3.2
15. Memo item: Balance of the planned Armed Forces Special Fund ⁵	–	–	– 20.0
15.a Borrowing authorisation remaining thereafter	–	–	80.0
16. Reserves of special funds for 14.	43.2	112.2	100.3
17. Level of general reserves	48.2	48.2	48.2
18. Balance on control account	47.7	47.7	47.7
19. Total outstanding repayment amount including Armed Forces Special Fund (from 10. and 15.)	69.6	263.4	399.1

* Sources: Federal Ministry of Finance and Bundesbank calculations. For methodological notes, see Deutsche Bundesbank (2016). ¹ After deduction of supplementary central government transfers, shares of energy tax revenue, compensation under the 2009 reform of motor vehicle tax and consolidation/budgetary recovery assistance to federal states, excluding transfers to/withdrawals from reserves. ² Excluding coin seigniorage. ³ Based on gross domestic product in the year before the (comprehensive) budget is prepared. ⁴ Budgeted figures for 2022 from borrowing plan contained in Bundestags-Drucksache 20/1000. ⁵ Assuming constant annual allocation of funds from 2022 to 2026.

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net borrowing figure of €128 billion, exceeding the standard limit by €116 billion. The consequence that this will have for the repayment schedule is that, from 2028 onwards, the available scope for borrowing will be just over €3½ billion lower annually.

In the amendment to the draft budget, the government cites two emergencies in its reasoning for exceeding its borrowing limit. First, it points out that the budgetary situation is particularly strained due to the fallout from the pandemic and the war. Second, it considers the planned measures necessary, but does not explain the reasons in more detail. The Constitutional Court of Hesse had previously called for detailed discussions on the Hessian debt brake in such a context.¹⁰ According to the court, justification would have to be given, in particular, as to why the additional measures and their

Little justification for exceeding standard limit

Plans cautious as things currently stand, but fraught with uncertainty

As things currently stand, it appears that a generous approach has been taken in drawing up the plans for the current year – as in the budgets for previous years. However, the plans are also fraught with considerable uncertainty in view of the Russian war of aggression and its impact.

¹⁰ See Constitutional Court of Hesse (2021).

credit financing are appropriate for addressing the particular emergency situation. With regard to the amendment to the draft central government budget, the economic environment would probably be particularly relevant, as this is already characterised by steep price rises and supply bottlenecks. Higher government deficits tend to amplify such frictions (see the remarks on p. 71). The government's lowering of energy taxes also appears to require further explanation. Whilst it is true that this can offset higher energy prices, it masks price signals that would be helpful in overcoming the emergency caused by the energy crisis in an economically efficient manner.

Sparing reserves increases amount of net borrowing requiring repayment and therefore also seems to warrant a more detailed explanation

Emergency borrowing could be more limited in scope if the government already made use of its reserves of €48 billion this year. On the one hand, budgets would initially come under pressure starting in 2023 due to the absence of available reserves. On the other hand, pressure on budgets would be eased from 2028 onwards because the emergency loans that would have to be repaid would then be smaller. The government has stated that it needs the reserves in order to comply with the standard limit under the debt brake from 2023. However, it should then explain why it is not possible to make use of other financing options. Another reason why this appears remarkable is that the government has already created additional scope for borrowing for the coming years via special funds: specifically, the revised accounting method for special funds means that it has an additional €112 billion at its disposal compared with the plans drawn up by the previous government.¹¹

Planned deferral of repayments in conflict with debt brake objectives

Under the Basic Law, emergency borrowing must be tied to a repayment schedule. As things currently stand, the emergency loans taken out in 2020 are to be repaid at €3½ billion per year starting in 2023. The annual repayments of €11 billion for the 2021 budget are to then commence three years later. When it adopts the 2022 budget, the Bundestag is now expected to defer these repayment sched-

ules. The government is aiming to defer repayments until 2028 and to make repayments until 2058 instead of until 2042, as had previously been decided. The reasoning given for this is the timetable for the repayment of European debt for assistance provided in response to the coronavirus pandemic (NextGenerationEU). This delay is not compatible with the debt brake's intention to protect future budgets from borrowing burdens. However, from an economic perspective, it is worth considering amending the constitutional rules on repayment obligations given low debt ratios.¹²

Benchmark figures up to 2026

In mid-March, the Federal Government also adopted the benchmark figures for the 2023 budget and for the medium-term fiscal plan up to 2026. From 2023, it plans to resume compliance with the debt brake's standard limit for structural net borrowing. To this end, it intends to use up the reserves by the end of 2025: it plans to withdraw €28 billion next year, and the remainder in the two years thereafter. To ensure compliance with the standard limit, nominal expenditure will also increase very little in the later planning years. To some extent, this means that expenditure cuts are needed in real terms. Defence spending is a different matter, though. This is set to rise permanently to over 2% of GDP. This is not reflected in the benchmark figures, as the government wishes to initially finance the additional expenditure via borrowing by a new Armed Forces Special Fund. It is not yet known how the spending increases will be financed in the core budget after that. Pressure on the central government budget will be eased with respect to payments to the social security funds: as of next year, the special grants for the statutory health insurance scheme are set to be discontinued. However, it is likely that the health insurance institutions will then have to sharply raise their supplementary contribution rates. The repayment obliga-

Benchmark figures up to 2026: return to standard debt brake limit with reserve funds and tight expenditure appropriations

¹¹ See Deutsche Bundesbank (2022b), pp. 70 ff.

¹² See Deutsche Bundesbank (2022c), p. 64.

tions for emergency loans no longer appear in the figures, as they have – as explained above – been deferred to a period outside the fiscal planning horizon. In the longer term, demographic developments are also likely to place a serious strain on the central government budget in the form of higher grants to the pension insurance scheme. The fact that the replacement rate for a standard pension is set to be frozen at 48% beyond 2025 will have an exacerbating effect. As previously planned, the retirement age is to remain fixed at 67 from 2032. Under these conditions, the contribution rate and the central government grants linked to it will rise considerably.

Central government’s off-budget entities: first quarter and outlook

Central government’s off-budget entities (excluding the Financial Market Stabilisation Fund (SoFFin), bad banks and other entities that use commercial double-entry bookkeeping) posted a surplus of €½ billion in the first quarter of 2022.¹³ This constituted a year-on-year improvement of €5 billion. The ECF saw its deficit shrink by €2 billion. This was due, on balance, to the higher price of electricity, which reduced the need for subsidies for electricity from renewable energy sources. At the start of 2021, the Economic Stabilisation Fund was still €1½ billion in deficit as a result of coronavirus aid for enterprises (in particular guaranteed assistance loans provided via the KfW). At the beginning of this year, repayments culminated in a surplus of €2 billion.

For 2022 as a whole, a surplus is expected for the existing off-budget entities, albeit on a significantly smaller scale than the previous year’s figure (€76 billion).

- The Federal Government is planning a deficit of €6 billion for the ECF. Last year, a special payment from central government produced a surplus of €54 billion.¹⁴

- The Flood Relief Fund will record a deficit this year. Last year, it posted a sizeable surplus as a result of pre-funding by central government amounting to €16 billion.
- The Economic Stabilisation Fund should see its surplus climb considerably (2021: €2 billion), provided this is not counteracted by new assistance measures.
- The off-budget entity “Provision for final payments for inflation-indexed Federal securities” will see significant growth in its surplus on the back of increased transfers to the fund by central government due to the high rate of inflation.

Overall, the off-budget entities could nevertheless end up in deficit this year. This is because, over the course of the year, a new special fund is to be introduced, financing additional defence spending via borrowing. The Federal Government is planning the increased expenditure in response to Russia’s war of aggression. The special fund is to sit outside the scope of the debt brake and receive borrowing authorisations of €100 billion. The plans provide for a repayment obligation but without a specific timeframe attached. Setting up the special fund in the form envisaged will only be possible with the approval of opposition parties – a high bar which ought to avoid setting a precedent undermining the binding effect of the debt brake. Given that a budget plan for the special fund has yet to be presented, for the current year it is almost impossible to gauge the volumes involved in procurement and thus to say what the fund’s deficit will be.

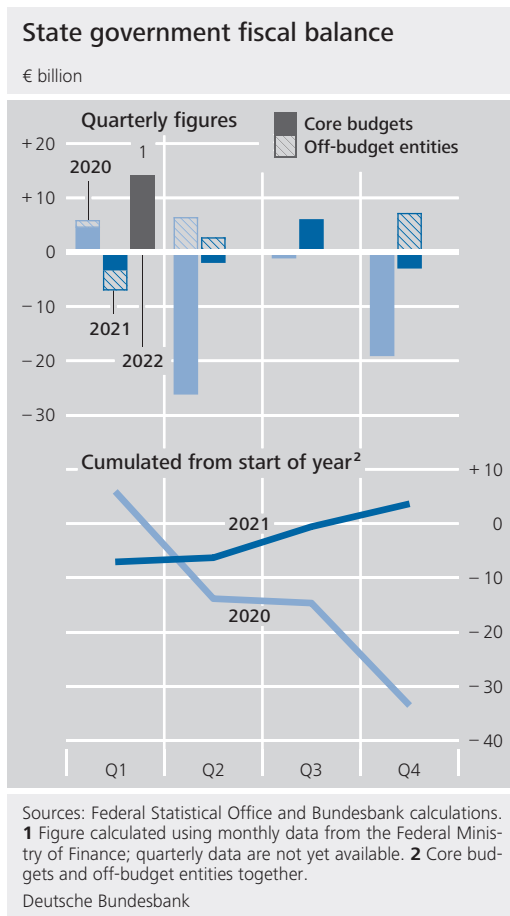
High borrowing authorisation for planned Armed Forces Special Fund ...

Improved result for central government’s off-budget entities in Q1 2022: alleviating factors for ECF and Economic Stabilisation Fund

Off-budget entities set to record surplus for 2022 as a whole

¹³ According to figures from the Federal Ministry of Finance. The Ministry does not publish quarterly data for off-budget entities that keep commercial accounts, such as the bad bank FMS Wertmanagement. The deficit generated by SoFFin, which uses a single-entry accounting system, has also been excluded, as it is largely a result of the loans passed on to FMS Wertmanagement.

¹⁴ Central government made this payment under recourse to the escape clause. This is currently the subject of review by the Constitutional Court in response to a constitutional complaint lodged by the opposition.



... weighing on outlook for off-budget entities

Together with the pre-funded ECF, it is foreseeable that the off-budget entities will post relatively large deficits over the next few years.

State government budgets¹⁵

Core budgets in the first quarter of 2022

Very high surplus in Q1 against backdrop of strong tax growth

State government core budgets finished the first quarter with a very high surplus of €14 billion. In the same quarter last year, where the effects of the pandemic were more strongly felt, they had posted a deficit of €3 billion. Revenue went up by 15%, driven primarily by strong growth in tax revenue (+25%, or +€18 billion). Receipts from public administrations went down. A contributing factor here appears to have been the lower central government payments for business aid, which are channelled through the state budgets.

There was barely any increase in expenditure overall. On the one hand, other operating expenditure, in particular, climbed significantly (+9%), not least as a result of the regular coronavirus testing in schools. In addition, personnel expenditure – a major expenditure item – rose rather strongly, by 6%. This was partly because the federal states were still paying out coronavirus bonuses with preferential tax treatment to salaried employees and civil servants in the first quarter of 2022. There was also a distinct increase in transfers to public administrations, especially to local government. Meanwhile, other expenditure fell sharply. Lower volumes of business aid, which – as mentioned previously – is financed by central government, probably played an especially significant role here.

Barely any expenditure growth in net terms

Core budgets and off-budget entities in 2022 as a whole

Taken together, the federal states' core budgets and off-budget entities recorded a surplus of €3½ billion last year. This year, the outturn could be similar. On the expenditure side, a continued marked increase is likely not least in personnel expenditure – a sizeable budget item; transfers to local government will also probably show another perceptible rise. When it comes to other operating expenditure, however, declining spending on vaccination centres and school testing in particular will likely take some of the pressure off over the remainder of the year. On the other hand, rising prices will probably exert a counter effect. The Russian war of aggression is affecting federal states' expenditure levels primarily in the form of additional costs associated with refugees. Central government appears to be shouldering the bulk of that burden, however. According to the most recent tax estimate, tax revenue will continue to rise markedly this year, even after the surprisingly high result of the previous year. While that increase will be much less strong

Core budgets and off-budget entities: result could change to only a limited extent this year

¹⁵ The quarterly data on state government budgets are based on the monthly cash statistics for the core budgets.

than at the beginning of the year, it will nevertheless ease the strain on state government budgets. Even so, the tax cuts passed by the Bundestag could weigh on state government revenue.

State government debt brakes

Only limited burdens left over from coronavirus pandemic; emergency borrowing needs careful justification

Many federal states have activated the debt brake escape clause again this year in order to cope with the coronavirus crisis. Pandemic-related encumbrances ought now to be modest, however. The year 2021 already saw tax revenue exceed the level expected in the last pre-crisis tax estimate of 2019. The same is true of the tax revenue now projected for the current year. On the expenditure side, coronavirus measures appear to have weighed on the federal states as a whole to the tune of almost €10 billion in 2021. As things stand today, those encumbrances are likely to at least halve this year. Overall, it must be ensured that emergency borrowing is utilised in a targeted manner for overcoming emergency situations. This was also stressed in the ruling delivered at the start of April by the Federal Constitutional Court for Rhineland-Palatinate. Consequently, the federal states must give sound justification in the event of recourse to emergency borrowing.

■ Social security funds

Pension insurance scheme

First quarter

Balanced result for the quarter; steep growth in contribution receipts

In the first quarter of 2022, the statutory pension insurance scheme had a largely balanced budget, an improvement of €3 billion on the year. Total revenue increased by 4½%. There was a strong 5½% rise in contribution receipts, bolstered by the sharp decline in short-time work. Central government funds increased by 1%: their growth was subdued on account of the rules coupling them to the weak wage developments of 2020 this year.

At 1%, expenditure growth was much weaker than growth in revenue. The reason for that minimal growth was the fact that pensions were not raised in western Germany in mid-2021 (eastern Germany: +0.7%). The number of pensions hardly changed. Moreover, it appears that the volume of supplementary payments being made and retroactively paid out in connection with the basic pension introduced last year remained very limited.

Low pension adjustment from previous year dampened expenditure dynamics

2022 as a whole

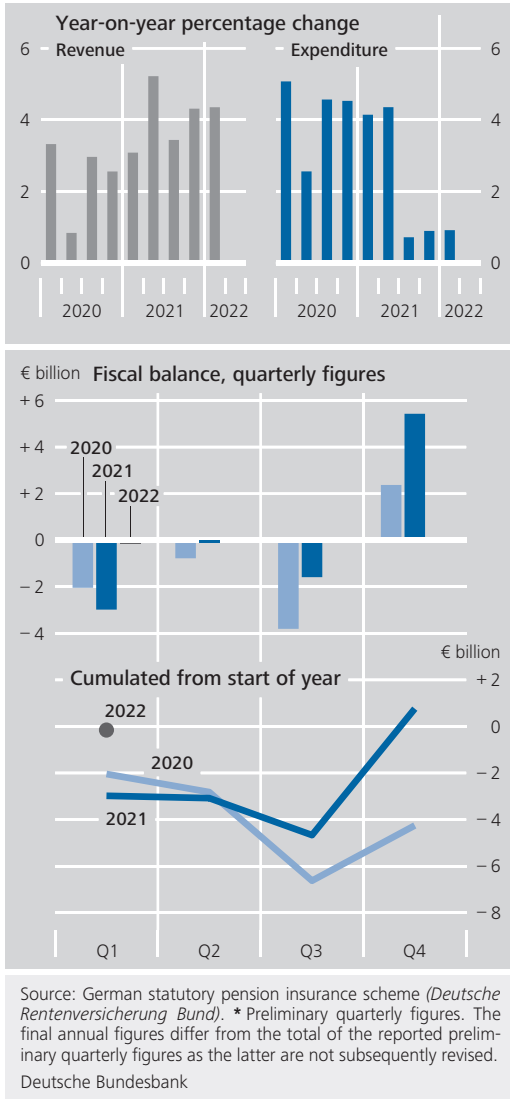
Expenditure in the year as a whole is rising significantly more strongly than in the first quarter of 2022. Most notably, individual pensions on an average for this year are growing far more strongly, increasing by 3% in total. Mid-year will see them rise by a sharp 5½%, averaged across Germany (5.35% in western Germany and 6.12% in eastern Germany). The key reason behind this development is the high wage growth recorded in 2021, which was driven by declining short-time work. The catch-up factor will dampen the pension adjustment by just over 1 percentage point: after being temporarily suspended it has now been reactivated by the Federal Government. This factor compensates for the application of the safeguard clause in 2021 that meant that pensions were not cut. The Federal Government expects the number of pensions to grow somewhat more strongly again than in the previous year (2021: +0.2%). On top of this, expenditure on the basic pension is climbing: the pension insurance scheme is paying it out on an increased scale and still has basic pensions for 2021 to pay out retroactively. By contrast, revenue growth is likely to be significantly weaker for the year as a whole.

Large pension adjustment in 2022 accelerating growth in expenditure

Compared with the previous year, 2022 as a whole is thus likely to see a deterioration in the finances of the pension insurance scheme. Following a surplus of almost €1 billion last year (according to provisional figures), a significant deficit is now on the cards for 2022, which could amount to around €2½ billion. There are

Considerable deficit anticipated for 2022 as a whole

Finances of the German statutory pension insurance scheme*



year as to maintain a minimum replacement rate of 48%. Without this measure, they would be just over 2% higher on an annual average for a time. While there are other new measures which will increase expenditure, they will have less of an impact. One such measure is a blanket rise in pensions from 2024 onwards for those who entered retirement due to a reduction in earning capacity between 2001 and 2018.

Once reserves have run down to their minimum level, balance will need to be restored to the budget. To achieve this, as things stand today, the contribution rate will need to rise by roughly 1 percentage point around 2025 (without factoring in any risks related to the Russian war of aggression). The contribution rate currently sits at 18.6%.

Contribution rate will nevertheless rise sharply around 2025

Looking at the longer term, further measures will bring increased financial pressures for the pension insurance scheme. The Federal Government is planning to continue the 48% threshold for the replacement rate beyond 2025. In order to fund this, contribution rates will need to rise more sharply. This will also place a greater strain on the central government budget because central government funds will increase along with the contribution rate, among other things.

Contributions set for strong increases in the long term against backdrop of permanent 48% threshold

risks on the revenue side with regard to the economic impact of the Russian war of aggression.

Medium and long-term outlook

It is to be expected that the deficits recorded by the pension insurance scheme will increase over the coming years. The reserves will then gradually be depleted. On balance, new measures will serve to curb the rise in pension expenditure up to the end of 2025, though. The suspension of the pension adjustment formula until 2025 means that pensions will grow at a slower pace, increasing by only so much every

New pension policy plans will alleviate pressure over medium term

Federal Employment Agency

First quarter

The Federal Employment Agency posted a deficit of €2 billion in the first quarter of 2022.¹⁶ This was €8 billion lower than in the same quarter of 2021 because the Federal Employment Agency was no longer as severely affected by the coronavirus crisis.

Sharp fall in deficit in year-on-year terms

¹⁶ In the core budget, i.e. excluding the civil servants' pension fund. Transfers to the fund are recorded as expenditure, lowering the core budget balance. These transfers were suspended in 2022 because of the coronavirus crisis (as they have been since 2020).

Strong increase in revenue from higher contribution receipts

Revenue rose substantially, by 7½% overall. Growth in contribution receipts was somewhat stronger still, at 9½%. This was due, not least, to the recovery in employment after the coronavirus crisis. Revenue from insolvency benefit contributions fell by 13%, pushed down by the reduction in the contribution rate from 0.12% to 0.09% at the start of 2022.

Sharp decline in expenditure due to improved labour market situation

Expenditure was 42% down on the same quarter of the previous year, though it was still 24% higher than in the last pre-crisis year of 2019. In the first quarter of 2022, expenditure on unemployment benefits fell by 26% on the year (-€1½ billion) and expenditure on short-time work by as much as 74% on the year (-€6 billion).

2022 as a whole

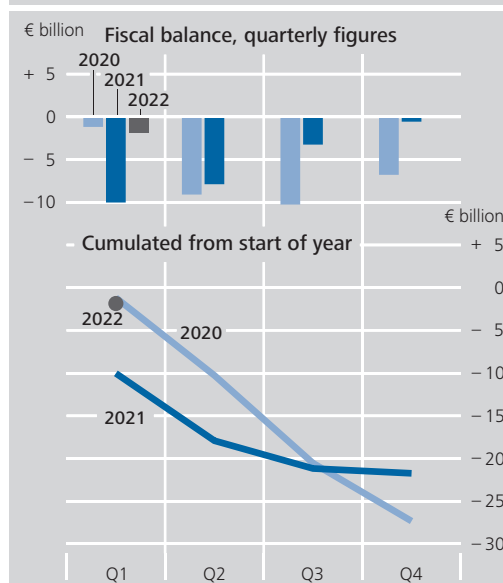
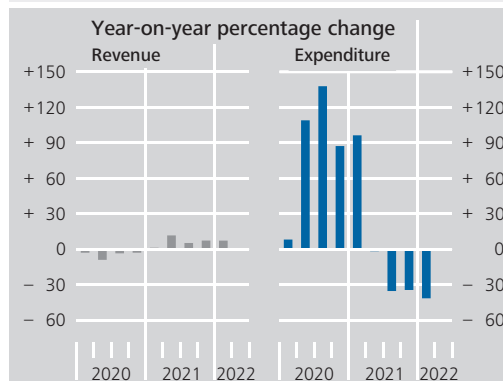
Favourable labour market developments, but risks in connection with war

The Federal Employment Agency's finances will improve considerably in 2022 provided that the labour market and wages develop in line with the Federal Government's spring projection. However, if the Russian war of aggression exerts stronger impacts these could quickly place a significant strain on the Federal Employment Agency, for example through short-time working benefits.

Current baseline scenario more favourable than the Federal Employment Agency's budget plan

The Federal Employment Agency's budget plan from last autumn still envisaged a deficit of €1½ billion in the core budget. However, as in the past, the estimates for spending on active labour market policy measures are likely to be on the generous side. The Federal Government's spring forecast also shows revenue growing at a markedly higher rate than had

Finances of the Federal Employment Agency*



Source: Federal Employment Agency. * Including transfers to the civil servants' pension fund and before payment of central government grants.
 Deutsche Bundesbank

been projected. Overall, this scenario foresees a close-to-balance budget, following a deficit of €22 billion last year (before central government grants of €17 billion).

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