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REPORT FROM THE COMMISSION

Germany

Report prepared in accordance with Article 126(3) of the Treaty on the Functioning of the European Union

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1. INTRODUCTION

On 20 March 2020, the Commission adopted a Communication on the activation of the general escape clause of the Stability and Growth Pact. The clause, as set out in Articles 5(1), 6(3), 9(1) and 10(3) of Regulation (EC) 1466/97 and Articles 3(5) and 5(2) of Regulation (EC) 1467/97, facilitates the coordination of budgetary policies in times of severe economic downturn. In its Communication, the Commission shared with the Council its view that, given the expected severe economic downturn resulting from the COVID-19 outbreak, the current conditions permit the activation of the clause. On 23 March 2020, the Ministers of Finance of the Member States agreed with the assessment of the Commission. The activation of the general escape clause allows for a temporary departure from the adjustment path towards the medium-term budgetary objective, provided that this does not endanger fiscal sustainability in the medium term. For the corrective arm, the Council may also decide, on a recommendation from the Commission, to adopt a revised fiscal trajectory. The general escape clause does not suspend the procedures of the Stability and Growth Pact. It allows Member States to depart from the budgetary requirements that would normally apply while enabling the Commission and the Council to undertake the necessary policy coordination measures within the framework of the Pact.

Data notified by the German authorities on 31 March 2020 and subsequently validated by Eurostat[1] show that the general government balance in Germany reached a surplus of 1.4% of GDP in 2019, while general government gross debt stood at 59.8% of GDP. According to the 2020 Stability Programme, Germany plans a deficit of 7¼% of GDP in 2020, while debt is planned at 75¼ % of GDP.

The planned deficit for 2020 provides *prima facie* evidence of the existence of an excessive deficit as defined by the Stability and Growth Pact.

Against this background, the Commission has therefore prepared this report, which analyses Germany's compliance with the deficit criterion of the Treaty. The debt criterion can be considered to be met as the debt ratio in 2019 is below the Treaty reference value of 60% of GDP. It takes into account all relevant factors and gives due consideration to the major economic shock linked to the COVID-19 pandemic.

[1] https://ec.europa.eu/eurostat/documents/2995521/10294648/2-22042020-AP-EN.pdf/6c8f0ef4-6221-1094-fef7-a07764b0369f

Table 1. General government deficit and debt (% of GDP)

		2016	2017	2018	2019	2020 COM	2021 COM
Deficit criterion	General government balance	1.2	1.2	1.9	1.4	-7.0	-1.5
Debt criterion	General government gross debt	69.2	65.3	61.9	59.8	75.6	71.8

Source: Eurostat, Commission 2020 spring forecast

2. DEFICIT CRITERION

Based on the 2020 Stability Programme, Germany's general government deficit in 2020 is expected to reach 7¼% of GDP, above and not close to the Treaty reference value of 3% of GDP.

The planned excess over the Treaty reference value in 2020 is exceptional, as it results from a severe economic downturn. Taking into account the impact of the COVID-19 pandemic, the Commission 2020 spring forecast projects a contraction of real GDP in 2020 by 6.5%.

The planned excess over the Treaty reference value would be temporary based on the Commission 2020 spring forecast, which projects the general government deficit to fall under 3% of GDP in 2021. However, those projections are surrounded by an exceptionally high degree of uncertainty.

In sum, the planned deficit for 2020 is above and not close to the 3%-of-GDP Treaty reference value. The planned excess is considered to be exceptional as defined by the Treaty and the Stability and Growth Pact, while the nature of the excess is currently considered temporary. Hence, the analysis suggests that *prima facie* the deficit criterion as defined by the Treaty and Regulation (EC) No 1467/97 is not fulfilled.

3. RELEVANT FACTORS

Article 126(3) of the Treaty provides that, if a Member State does not fulfil the requirements under one or both of those criteria, the Commission has to prepare a report. That report must also "take into account whether the government deficit exceeds government investment expenditure and take into account all other relevant factors, including the medium-term economic and budgetary position of the Member State".

Those factors are further clarified in Article 2(3) of Regulation (EC) No 1467/97, which also provides that "any other factors which, in the opinion of the Member State concerned, are relevant in order to comprehensively assess compliance with the deficit and debt criteria and which the Member State has put forward to the Council and to the Commission" need to be given due consideration.

As specified in Article 2(4) of Regulation (EC) No 1467/97, as regards compliance with the deficit criterion in 2020, since the government debt-to-GDP ratio is planned to exceed the

60% reference value in 2020 and the double condition is not met – i.e. that the deficit remains close to the reference value and that its excess over the reference value is temporary – those relevant factors cannot be taken into account in the steps leading to the decision on the existence of an excessive deficit on the basis of the deficit criterion for Germany.

In the current situation, a key additional factor to take into consideration regarding 2020 is the economic impact of the COVID-19 pandemic, which has a very substantial impact on the budgetary situation and results in a highly uncertain outlook. The pandemic has also led to the activation of the general escape clause.

3.1. COVID-19 pandemic

The COVID-19 pandemic has led to a major economic shock that is having a significant negative impact throughout the European Union. The consequences for GDP growth will depend on the duration of both the pandemic and of the measures taken by national authorities and at European and global level to slow its spread, protect production capacities and support aggregate demand. Member States have already adopted or are adopting budgetary measures to increase the capacity of health systems and provide relief to those individuals and sectors that are particularly affected. Significant liquidity support measures and other guarantees have also been adopted. Subject to more detailed information, the competent statistical authorities are to examine whether those measures entail an immediate impact on the general government balance or not. Together with the fall in economic activity, those measures will contribute to substantially higher government deficit and debt positions.

3.2 Medium-term economic position

Economic growth reached 0.6% in 2019, mainly supported by the robust performance of domestic demand. However, due to the COVID-19 pandemic, the Commission 2020 spring forecast projects GDP to decline by 6.5% in 2020, reflecting the disruption in economic activity caused by the lockdown measures and an unprecedented fall in external demand in the first half of 2020. Private consumption is projected to be hard-hit due to increased uncertainty of consumers, an increase in unemployment and a sharp drop in wage growth. Business investment is also set to fall strongly in 2020 as uncertainty mounts and expectations of lower demand are likely to have an impact on firm's investment plans. Moreover, the macroeconomic outlook is subject to exceptional uncertainty related to the duration of the COVID-19 pandemic and its economic impact. This a mitigating factor in the assessment of Member State's compliance with the deficit criterion in 2020.

3.3 Medium-term budgetary position

Based on outturn data and the Commission 2020 spring forecast, Germany achieved its medium-term budgetary objective in 2019.

A supplementary budget for 2020 was adopted by the German Parliament on 25 March 2020, to finance the various and sizeable measures for protecting the economy against the effects of the COVID-19 pandemic as well as to compensate the shortfalls in tax revenues due to the downturn in economic activity. Those measures include support for the healthcare sector and developing a vaccine against the COVID-19 virus, but mainly focus on stabilising the economy by providing liquidity support for companies and grants to small companies and self-employed as well as keeping people employed by using short-time working schemes.

The Stability Programme lists the various measures adopted, which amount in total to more than EUR 450 billion (14% of GDP) in direct support measures and EUR 800 billion (25% of GDP) in additional guarantees for loans. The expected budgetary impact including shortfalls in tax revenues due to automatic stabilisers and granted tax deferrals amounts to -7.2% of GDP for 2020. The actual budgetary impact will also depend on the uptake of the support measures and on the calling of guarantees. The fiscal outlook is thus also surrounded by a high degree of uncertainty created by the COVID-19 pandemic.

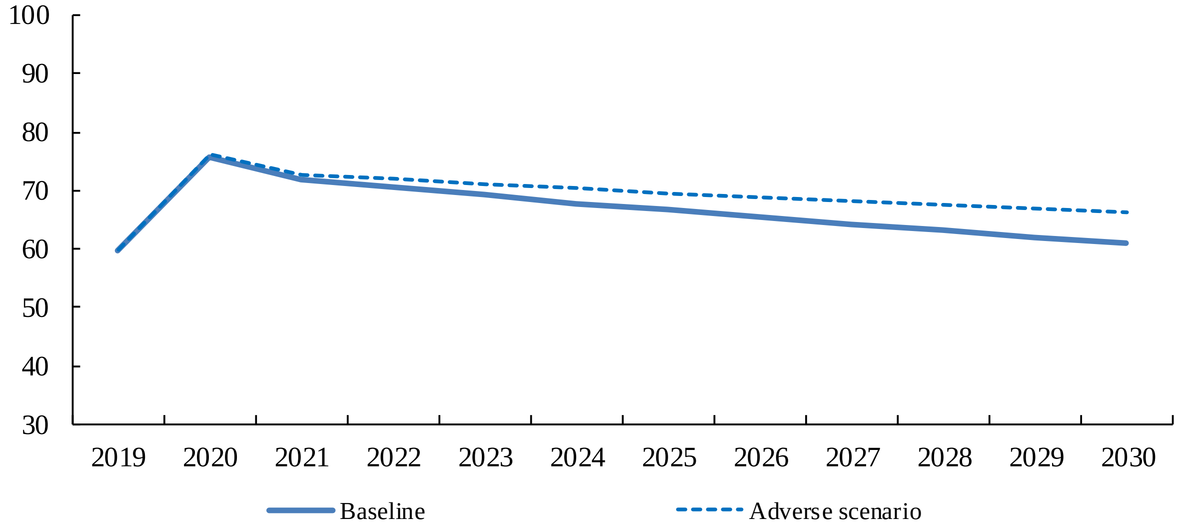
3.4. Medium-term government debt position

According to the Commission 2020 spring forecast, general government debt is expected to rise from 59.8% of GDP in 2019 to 75.6% in 2020.

The debt sustainability analysis has been updated with the Commission 2020 spring forecast. Overall, the debt sustainability assessment indicates that the debt position remains sustainable over the medium-term, which takes account of important mitigating factors (including the debt profile and status). In particular, while the government debt position has deteriorated as a result of the COVID-19 crisis, the debt-to-GDP ratio in the baseline is expected to be on a sustainable (declining) trajectory over the medium term.[2]

[2] The baseline is based on the Commission Spring 2020 forecast. Beyond 2021, a gradual adjustment of fiscal policy is assumed, consistent with the EU economic and fiscal coordination and surveillance frameworks. Real GDP growth is projected according to the so-called EPC/OGWG T+10 methodology. In particular, (real) actual GDP growth is driven by its potential growth and affected by any additional fiscal adjustment considered (through the fiscal multiplier). Inflation is assumed to converge gradually to 2%. Interest rates assumptions are set in line with financial market expectations. Under the adverse scenario, higher interest rates (by 500 bps.) and lower GDP growth (by -0.5 pp.), with respect to the baseline, are assumed (throughout the projection horizon).

Graph 1: Government debt-to-GDP ratio, Germany, % of GDP



Source: Commission services

3.5 Other factors put forward by the Member State

On 19 May 2020, the German authorities transmitted a letter with relevant factors in accordance with Article 2(3) of Regulation (EC) No 1467/97. The analysis presented in the previous sections already broadly covers the key factors put forward by the authorities.

4. CONCLUSIONS

According to the Stability Programme, Germany's general government deficit in 2020 is planned to reach 7¼% of GDP, thereby exceeding the 3% of GDP Treaty reference value. The planned excess over the reference value is considered to be exceptional and currently considered to be temporary.

In line with the Treaty and the Stability and Growth Pact, this report also examined relevant factors.

As specified in Article 2(4) of Regulation (EC) No 1467/97, as regards compliance with the deficit criterion in 2020, since the government debt-to-GDP ratio is planned to exceed the 60% reference value in 2020 and the double condition is not met – i.e. that the deficit remains close to the reference value and that its excess over the reference value is temporary – those relevant factors cannot be taken into account in the steps leading to the decision on the existence of an excessive deficit on the basis of the deficit criterion for Germany.

Overall, the analysis suggests that the deficit criterion as defined in the Treaty and in Regulation (EC) No 1467/1997 is not fulfilled.