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IWH Mid-term Projections: The German Economy and Public Finances 2018 to 2025

In 2018 the general government overall balance is likely to be in surplus by almost 60 billion euros. In the medium term, however, demographic conditions will deteriorate, as will public finances. The financial position of the German state will nevertheless remain stable until 2025, unless major negative shocks occur. “But even if interest rates rose significantly or foreign demand declined markedly, only moderate deficits would arise”, says Oliver Holtemöller, head of the Department of Macroeconomics and vice president at Halle Institute for Economic Research (IWH). However, given the expected reduction of the surplus under existing legislation, there is no room for further increases in spending.

In Germany the number of economically active people will decline in the medium term due to the aging of the population. While economic growth will therefore be lower than it had been in recent years, the federal government has decided on a number of additional government expenditures. A projection based on the IWH macroeconomic model for Germany, however, shows that the budget will probably stay in surplus by 2025, even if all the fiscal measures contained in the coalition agreement are implemented. In case important macroeconomic conditions worsened, for example due to a significant increase in interest rates or a marked decline in foreign demand, the general government balance would turn negative, but expected deficits would still be less than 0.5% relative to gross domestic product. A decline in foreign demand would dampen production more than an interest rate shock, but the effects on the general government balance would be comparable. That is because interest rate shocks affect domestic demand which is a more important source for government revenues than foreign demand. All in all, the German public budget should be quite robust for the coming years. However, it should be noted that the additional expenditure resulting from the pension package of the coalition agreement will make a significant contribution only after 2025.

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Table

Revenues, expenditure, and general government overall balance up to 2025 – baseline case

	2017	2018	2019	2020	2021	2022	2023	2024	2025
including pension package, basic pension, and reduction of solidarity surcharge									
Bill. €									
Revenues	1 473,8	1 545,2	1 587,1	1 641,7	1 685,4	1 737,3	1 792,4	1 850,0	1 907,3
Expenditure	1 439,8	1 485,6	1 544,9	1 604,3	1 663,0	1 717,7	1 777,0	1 837,2	1 900,7
Balance	34,0	59,6	42,3	37,4	22,4	19,6	15,4	12,8	6,6
in relation to GDP in %									
Revenues	45,0	45,7	45,4	45,2	45,0	45,0	45,1	45,3	45,5
Taxes	23,4	23,7	23,5	23,5	23,2	23,2	23,3	23,3	23,4
Net Social Contributions	16,7	16,9	16,9	16,9	16,9	16,9	17,0	17,0	17,1
Expenditure	43,9	43,9	44,2	44,2	44,4	44,5	44,8	45,0	45,4
Monetary Social Expenditure	15,4	15,4	15,6	15,6	15,7	15,8	15,9	16,0	16,1
Property income paid (interest payments)	1,0	0,9	0,9	0,8	0,8	0,7	0,8	0,8	0,8
Balance	1,0	1,8	1,2	1,0	0,6	0,5	0,4	0,3	0,2
Structural Balance	1,1	1,7	1,2	0,9	0,5	0,4	0,4	0,3	0,2

Long Version:

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 Mittelfristprojektion des IWH: Wirtschaftsentwicklung und Öffentliche Finanzen
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