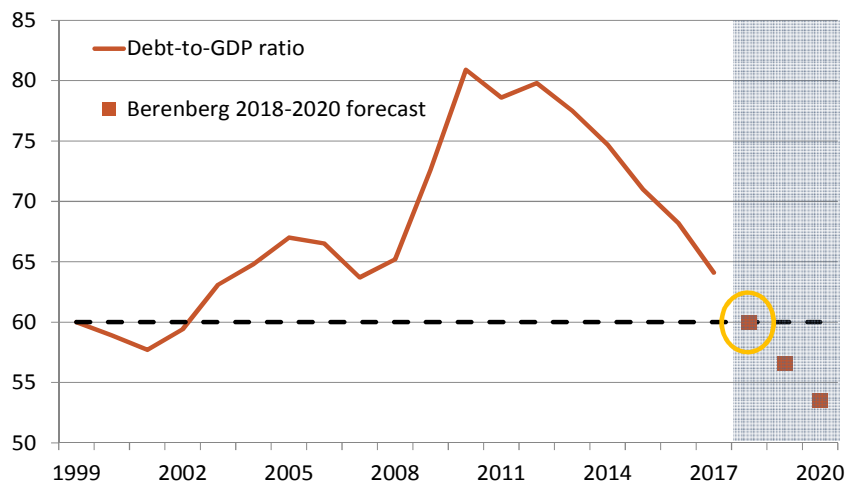


24 August 2018

German fiscal bliss: debt ratio can hit 60% this year

German debt-to-GDP ratio falling fast



Ratio of public debt to GDP, Maastricht definition. Source: Destatis, Berenberg projections

- Finally fit for the euro:** Germans have a half-deserved reputation for interpreting rules more rigidly than they were meant to be. On this basis, Germany would finally qualify to join the euro by the end of 2018 again. Excellent fiscal data for H1 2018 suggests that the German ratio of public debt to GDP will fall to 60% at the end of this year from 64.1% last year. Germany would thus hit exactly the Maastricht debt threshold.
- Record surplus:** Helped by a 5% surge in revenues, Germany achieved a fiscal surplus of €48.1bn in the first half of 2018, equivalent to 2.9% of its GDP, well above the €22.1bn surplus in H1 2017. Of course, such partial data are no reliable guide to the full-year outcome. Germany had no more than a caretaker government until mid-March 2018 and no regular federal budget until July. This constrained the rise in federal expenditure artificially in H1 2018.
- Bigger surplus, less debt:** Driven by a 7.2% surge in income and wealth taxes, as well as the 4.2% yoy gain in payroll taxes, Germany's overall tax revenues rose by 5% yoy in H1 2018. Strong increases in employment and a gradual advance in wage inflation underpin the encouraging revenue trend. Although expenditure growth will likely pick up substantially in H2 2018 from the paltry 1.2% yoy increase in H1 2018, the fiscal result for 2018 looks set to come in even better than we had projected so far. We revise our call for Germany's 2018 surplus from 1.5% to 1.7% of GDP after 1.2% in 2017. With a 3.6% rise in nominal GDP, that brings Germany's debt-to-GDP ratio down to 60%.
- The rewards of reform:** Germany's fiscal strength has one big reason. No, it is not austerity. Germany's fiscal policy has been mildly expansionary since 2015. Instead, Germany is reaping the rewards of its 2003-2005 labour market reforms. Core employment (subject to payroll taxes) has surged by 25% since early 2006, breaking a downtrend that had begun in 1993. Upon the 1999 start of the euro, Germany had been the sick man of Europe. As deficits surpassed 3% from 2001 through 2005, Germany's debt ratio had exceeded 60% even before the post-Lehman recession.
- The lesson is clear:** Countries with structural rigidities and a chronic fiscal problem such as Italy and France need to reform their labour market and make their countries better places to invest and create jobs. Whereas France is going the right way, Italy has started to backtrack on earlier reforms. See [here](#) for an assessment of UK trends. Low interest rates can help, as they do in the case of Germany, but they are not the key factor for fiscal trends.
- Not investing enough?** That Germany should spend more is a common refrain in global policy discussions. While often overdone, the point is valid. In one key respect, Germany is on track. The somewhat erratic data for public investment show a 12.3% yoy surge in H1 2018. Germany has the money to spend more. The constraints are lengthy planning procedures and a dearth of construction workers, which can be addressed only gradually.

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