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July 14, 2022

**Statement by Mr. Andrianarivelo, Mr. Sylla, and Mrs. Boukpepsi on Germany
(Preliminary)
Executive Board Meeting
July 18, 2022**

We thank Staff for the comprehensive reports as well as Mr. Stephan and Mr. Krahnke for their informative Buff statement.

Despite weathering the Covid-19 pandemic well, the German authorities face significant near-term challenges. The economy was strengthening thanks to increased activity in auto production and services sector. Regrettably, spillovers from Russia’s war against Ukraine including surging energy prices, global inflation amid lingering pandemic, are now stalling growth. The outlook is riddled with considerable risks and uncertainties, including a complete shut-off of Russia’s gas exports to Germany and Europe as a whole, that would impact the largest economy on Europe and significantly worsen the macroeconomic situation with higher inflation and further growth slack. In this context, it is paramount that priorities continue to focus on firming energy security and build resilience by diversifying sources of gas supplies and accelerate the development of alternative energy sources, including through the REPowerEU, or solidarity agreements. The gas shutoff scenario presented in the report clearly stresses the importance of addressing this immediate challenge facing the country. *Staff’s update on the authorities’ ongoing assessments of the economic and financial implications of this scenario as well of contingency plans-if any-would be appreciated.* Looking ahead, scaling up targeted public investment to strengthen digitalization, decarbonization and climate infrastructure while tackling the country longstanding challenges remains also important.

Fiscal flexibility should be retained given heightened uncertainties surrounding the outlook. Under the baseline scenario, we note that the broadly neutral fiscal stance in 2022 and the plan to tightening the stance in 2023 and return to the debt brake rule are appropriate. However, we strongly encourage the authorities to stand ready to provide further targeted support. The activation of the escape clause of the debt brake rule for an additional year should also be considered. We welcome the income support and other measures to mitigate

the impact of high energy prices on vulnerable households and firms as highlighted in Annex IV and V of the report. Energy diversification away from one source of oil, coal, and gas, is paramount and we welcome the recent announcements made by the authorities on the timeline to do so.

We broadly concur with staff’s assessment and recommendations for the financial sector, which remains resilient to solvency and liquidity shocks, but continued close monitoring of vulnerabilities identified during the FSAP is warranted. In this regard, we see merit in monitoring of prudential ratios for the systemically important commercial banks, establishing when needed further specific buffers for less capitalized banks and improving data collection for less systemically important institutions. *We agree with staff that it would be suitable to conduct additional analysis of the impact of the war, sanctions, and energy prices spike on the German financial stability. Could staff indicated if this has been done since the finalization of the report and if yes what are the preliminary conclusions.* While the authorities estimate that the macroprudential policy package announced in January 2022 is appropriate, we agree with staff that close monitoring of risks from real estate is critical and further actions are needed notably, considering the overvaluation of the residential real estate in the largest cities.

Increasing green investment in line with the country’s climate and energy-security goals requires further improvement in public investment. We agree with staff that the authorities need to take the necessary steps to swiftly tackle the obstacles to scaling public investment such as heavy administrative procedures, legal complications, and difficult coordination across different levels of government. We take positive note of the establishment of a working group in the Chancellery to address these obstacles. As for the authorities’ climate-change mitigation policy, we welcome the recent “Easter package”, an accelerator for the expansion of renewable energy, the “Summer package” for decarbonization in transport, building, and agriculture. With the national carbon price been considerably lower than EU Emission Trading System (ETS), we take note of the authorities’ view on having a single carbon price in the EU *and would appreciate if staff could elaborate on where other EU countries stand on this.*

Boosting labor market participation and addressing deficiencies in the labor market such as gaps in human capital and skills are of essence. Along with the authorities’ investment program “childcare financing”, we support staff’s proposals to increase labor participation especially the inclusion of women, youth, and migrants. There is also further scope to increase productivity by encouraging innovation, enhancing competition in the ICT market, and improving digital connectivity and training in a post-pandemic era. We particularly welcome the “Hubs for Tomorrow” program that will support companies and employees to transition to a more digitalized economy and look forward to the “law for financing the future” aiming at reducing red tape, fostering digitalization and financial innovation, and facilitate access to private capital markets, notably for start-ups and SMEs as underscored in the Buff statement.

With these remarks, we wish the German authorities all the best in their endeavors.