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**Statement by Mr. Buissé, Mr. Rozan, and Ms. Gilliot on Germany
(Preliminary)
Executive Board Meeting
January 13, 2021**

We thank staff for their comprehensive report and Mr. von Kleist, Mr. Merk, and Mr. Buetzer for their very useful Buff statement. The Covid-19 pandemic has taken a significant toll on the German economy, with the recent rise in infections and the related lockdown impairing the outlook. The policy response of the Government to the crisis has been swift, strong and multi-pronged and the sizeable fiscal stimulus implemented together with substantial automatic stabilizers have been instrumental in cushioning the impact on the economy, highlighting the resilience of the German economy. The implementation of the EU supporting measures will amplify the positive impact of domestic actions on the recovery. As in other European countries, those measures will be key to foster the transformation of the economy toward a greener and more digital economy and, specifically for Germany, bolster the necessary rebalancing of the economy. We associate with Mr. Poso's statement and wish to offer the following comments for emphasis.

We fully share staff's macroeconomic diagnostic and risks analysis in a context of exceptionally high uncertainty around the baseline forecast. As for many other countries, caution should be exercised in growth's projections for 2021 given the new containment measures recently announced. The recovery will depend on a mix of domestic and exogenous variables including progress made on vaccine distribution, consumers and businesses' confidence, resources reallocation and credit supply. Nevertheless, shocks to trade and geopolitical tensions could exacerbate external demand disruptions impacting Germany's export-oriented economy.

We welcome the authorities' use of Germany's substantial fiscal space to support the economy. Further fiscal support should be provided if necessary. Germany's response to the crisis has been very substantial and was fully warranted. We are pleased to find that the 2021 budget maintains considerable demand support with the escape clause of the debt brake rule remaining activated to support this fiscal path. The fiscal policy should thus adequately continue to support the economic activity in 2021 including direct budget support and credit support for businesses, further extension of the successful *Kurzarbeitergeld* program and

households' incomes support already in place before the crisis. **Going forward, fiscal policy should remain accommodative and supported by the temporary suspension of the constitutional debt brake rule until the recovery is firmly under way.** It will help to keep fueling the recovery, boost public investment and domestic consumptions and allow the authorities to deploy additional support if growth falls short of expectations. Premature fiscal consolidation should therefore be avoided to protect the domestic recovery, but also to support the Euro Area and its rebalancing. In this context, we were surprised by staff's assertion in paragraph 10 that regional spillovers from a sizable fiscal expansion in Germany would be limited in scope. The economic literature mentioned does not seem to conclude to such limited impact. *Staff comments would be welcome.*

As described in Annex I on the External Sector Assessment, despite a temporary decrease initiated before the pandemic, the current account surplus remains higher than implied by medium- term fundamentals in 2020 and is expected to stabilize at a high level over the medium term. In this regard, we welcome staff's emphasis on the need for specific structural policies aiming at boosting public and private sector investment in key areas supporting the structural transformation of the German economy such as digitalization, infrastructure and climate mitigation. Moreover, and along with pension reforms, we fully agree that additional tax relief for lower-income households while boosting their purchasing power would contribute to reducing excess saving and diminish external imbalances.

Labor market policies should remain protective and could further facilitate the integration of workers and enhance the participation rate while protecting the most vulnerable groups including women, the youth and elderly workers. We welcome the expansion of the *Kurzarbeit* benefits through end-2021, as it continues to be a very effective crisis mitigation scheme. We share staff's view that support to crisis-hit workers excluded from this mechanism could be enhanced by reducing hiring costs for viable firms and boosting training and apprenticeship to ease the post-pandemic reallocation process of human capital across sectors, especially to sectors of the digital economy where opportunities exist. We would have seen merit in more detailed proposals to reform marginal employment, avoid the use of the so-called low paid and part-time "mini jobs" in the context of the crisis. The protection of the most vulnerable groups could be heightened with measures to strengthen social safety nets for marginal workers including women and the self-employed. Regarding taxation, we see merit in lowering the labor tax wedge on low- and middle-income households to increase disposable income and incentivize labor supply. **Going forward, given that this is a concern shared by a large number of Advanced economies, we see merit in staff further delineating their recommendations on how to facilitate the reallocation of labor across sector in the recovery phase.**

The well-capitalized and regulated German banking sector remains well positioned to weather the pandemic although its prolonged effects on capital should be monitored, in a context of low profitability. We note staff's long-standing recommendation in favor of banking-sector consolidation to address profitability and solvency concerns. In a context of low profitability (shared among advanced economies' banking system), *we would be interested in staff's further detailed recommendations on how to bring about this consolidation of the banking system.* We welcome the ongoing reform of Germany's auditing framework and accounting enforcement in the wake of the Wirecard fraud. While the recent

plan approved to combat accounting fraud is very positive, we would be interested in staff's analysis on whether this reform will comprehensively deal with the deficiencies analyzed.