

Public finances*

General government budget

Last year the general government budget recorded a surplus (+0.1% of GDP) for the first time since German reunification.¹ However, the public finance situation is likely to worsen somewhat in 2008, and a slight deficit is expected. Although the cyclical momentum is currently slowing, economic activity could continue to have a positive impact on the development of public finances on an annual average. Structural factors are to blame for the expected deterioration of the budgetary position. In particular, the sizeable tax and social security rate cuts have not been matched by the evolution of expenditure which, while still fairly moderate, is rising faster than in previous years. Germany's fiscal performance is admittedly particularly uncertain at present owing to the ambiguous macroeconomic outlook and risks associated with the financial market turbulence. While the government debt ratio, which amounted to 65% in 2007, should decrease markedly, the 60% ceiling stipulated by the EC Treaty will continue to be overshot.

Public finance situation will worsen somewhat in 2008

Government revenue is expected to decline significantly in relation to GDP during the course of 2008. This is mainly due to changes in legislation. The business tax reform and a further cut in the contribution rate of the Fed-

Tax and social security rate cuts leading to sharp fall in revenue ratio

* The "General government budget" section starts with an analysis of general government budget developments which is predominantly based on figures from the national accounts. The subsequent reporting on budgets of the various levels of government and the social security schemes is based on the budgetary figures as defined in the government's budgetary financial statistics.

¹ The surplus in 2000 was solely attributable to the one-off UMTS receipts.

eral Employment Agency from 4.2 % to 3.3 % will result in substantial revenue shortfalls, only a fraction of which will be offset by the rising contribution rates to the statutory health and public long-term care insurance schemes. In addition, the exceptionally robust growth trend in revenue from profit-related taxes (adjusted for legislative changes), which has been evident for several years now, could reverse during the remainder of the year. This is all the more likely given the turbulence on the financial markets. However, the general government revenue ratio is likely to be bolstered by the fact that the high revenue-yielding source of gross wages and salaries is increasing at a more rapid pace than nominal GDP. Wage tax receipts will be boosted in addition by tax progression effects following the recent markedly higher wage settlements.

Smaller fall in expenditure ratio

The government expenditure ratio will continue to fall this year. However, the decline will be distinctly more moderate than in the previous years and will probably be smaller than the fall in the revenue ratio. On the one hand, decreasing unemployment means lower expenditure, and the moderate wage growth of the past few years is continuing to have a dampening effect on spending. This is due to the fact that there is a time-lag before many government expenses, such as pensions and unemployment benefits, are adjusted to the wage trend. On the other hand, personnel expenditure, which made a major contribution to the decrease in the expenditure ratio in previous years, is unlikely to have a dampening effect in 2008 owing to the fairly sizeable pay rises in the public sector. Strong expenditure growth is expected for

government investment and in the healthcare sector. The effects of support measures for public sector banks cannot yet be gauged.² Overall, expenditure is expected to accelerate much faster than in 2007.

As things currently stand, the general government budget in 2009 could more or less balance as long as no further measures are taken. However, the general government outlook conceals the fact that central government in particular, but also other government areas, are likely to continue to record considerable structural deficits in the coming year. On the revenue side, a certain amount of additional income owing to the effects of tax progression might help to counter possibly subdued growth in receipts from profit-related taxes. The revenue ratio may stay roughly at this year's level since *inter alia* the announced increases and decreases in tax and social contribution rates largely cancel out. Expenditure growth is likely to accelerate again. Healthcare spending, in particular, is set to rise more rapidly, not least owing to new arrangements for the remuneration of outpatient treatment, while labour market-related spending is not likely to decrease further. While the government debt ratio is likely to drop further, it will probably still exceed the reference value of 60 % defined in the EC Treaty.

Similar situation expected in 2009

² If the guarantees and risk shields provided by public authorities are statistically classified as government assistance to prevent bank failures, government expenditure (as defined in the national accounts) would have to be increased by the difference between the original book value and the market value of the shielded assets when the risk shield was put into place. The Maastricht debt level would then increase by the book value of the assets (before depreciation).

Lower tax and social security rates and extra spending need counter-financing

The public finance situation in Germany has improved noticeably in the past few years. The European requirements for the medium-term budgetary objective arising from the Stability and Growth Pact and the reference value for government indebtedness stipulated in the EC Treaty could well be met in the not-too-distant future. However, this prospect is subject to considerable uncertainty. This concerns firstly the possibility of further budget-burdening measures. Thus the impending recalculation of the official socio-cultural minimum subsistence level can be expected to lead to an increase in the relevant tax allowances (and, in all likelihood, child benefit, too). Secondly, further cuts in tax and social security rates and extra spending are currently under discussion; these have not been included in the projections outlined above, which are based on legislative changes that have already been adopted. Thirdly, a substantial drop in revenue levels is likely to result from 2010 onwards owing to a ruling by the Federal Constitutional Court referring to the offsetting of health and long-term care insurance contributions against tax. If the balanced general government budgetary position that has been painstakingly achieved is not to be frittered away, any additional budget-burdening measures will require solid counterfinancing. Fourthly, the current macroeconomic outlook is fraught with considerable uncertainty. Past experience, but also the latest developments in some other countries, have shown just how quickly the public finance situation can deteriorate given an unfavourable economic setting. Not least the extremely sharp growth trend in profit-related taxes over the past few years harbours

the risk of a considerable setback potential, so that the structural position might appear much better than it actually is.

There have been calls to launch an economic stimulus package to be financed by additional borrowing. However, this would cause government budgets to promptly run into difficulties again – even without the risks described above materialising. In contrast to allowing the automatic stabilisers to take effect, attempts by general government to actively fine-tune economic policy inevitably give rise to substantial problems. In Germany's current situation it is especially difficult to predict the further pattern of economic development with any degree of reliability. For example, the somewhat dulled economic growth at the moment can be seen, at least in part, as a return to the steady state following an extremely sharp uplift in the first quarter (see the comments on the general course of economic development on pages 42-56). An economic stimulus package does not appear to be appropriate at present.

Stimulus package not appropriate

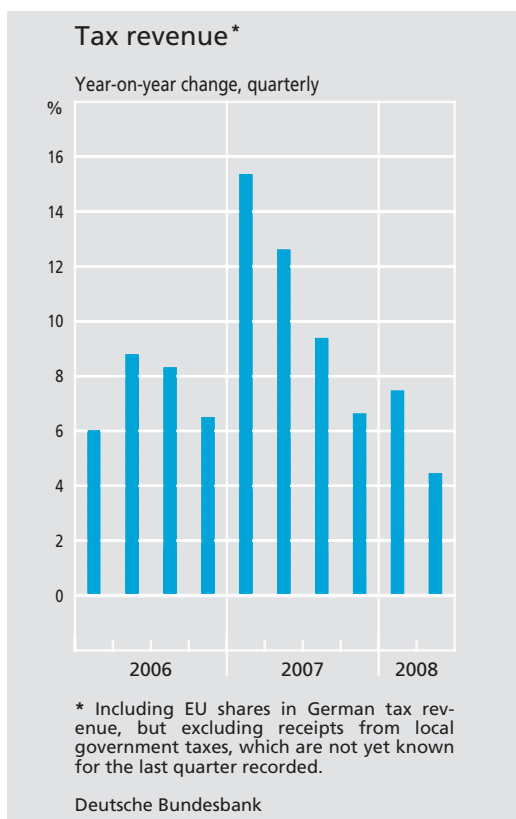
Budgetary development of central, state and local government

Tax revenue

Tax revenue³ rose markedly by 4½% in the second quarter compared with the same period last year (see the chart on page 60 and the table on page 61). Although this fell well short of the previous quarter's growth rate, it

Clear rise in tax revenue in Q2

³ Including EU shares in German tax revenue but excluding receipts from local government taxes, which are not yet known for the last quarter recorded.



should be noted, first, that the effect on cash receipts of the increase in VAT at the start of 2007 was still being felt in the first quarter and, second, that payments of the grant to homeowners (that is being phased out), which are deducted from revenue mainly in March, decreased significantly. Revenue from income-related taxes⁴ climbed on the year by a sizeable 8 ½ %. At 7 ½ %, growth in wage tax receipts was again strong due to the rise in gross wages and salaries, the decline in child benefit payments, which are deducted from cash receipts, and to the tax progression effect. Receipts from assessed income tax expanded particularly strongly. In addition to robust underlying dynamics, lower refunds to employees contributed to this development. Investment income tax receipts (non-assessed taxes on earnings and interest withholding

Sharp growth in income-related taxes despite business tax reform

tax) were again up by a substantial amount. By contrast, corporation tax revenue fell sharply, but the revenue shortfalls were more or less at the levels that were expected as a result of the relief arising from the business tax reform which entered into force at the start of 2008. No clear conclusions can be drawn, at any rate, about the possible effects of the financial market turbulence. Given the subdued growth in consumption, revenue from consumption-related taxes⁵ – which fluctuate sharply in the course of the year – grew by a total of only 1%. The increase in turnover tax receipts amounted to 2 % while the revenue from energy and electricity taxes decreased slightly on balance. Even revenue from tobacco tax declined, which is probably due in part to the extensive ban on smoking in public places.

Subdued development of consumption-related taxes

According to the last official tax estimate in May, revenue growth of just under 4 % (likewise excluding local government taxes) is expected for the year as a whole. The expected slowdown vis-à-vis the first half of the year (+6 %) is attributable in part to the fact that the cited positive one-off developments occurred only in the first six months. Furthermore, the shortfalls associated with the business tax reform appear not to have been fully reflected in the cash receipts for corporation tax. Independently of this, a high setback potential exists in relation to revenue from profit-related taxes, which have grown extraordinarily strongly for some years now. In

Tax revenue trend for 2008 as a whole likely to weaken somewhat amid continuing high uncertainty

⁴ Wage tax, assessed income tax, corporation tax and investment income tax plus the solidarity surcharge.

⁵ VAT as well as consumption-related taxes for central and state government (especially energy tax, tobacco tax, insurance tax, motor vehicle tax and electricity tax).

Tax revenue

Type of tax	H1		Year-on-year change		Q2		Year-on-year change		Estimate for 2008 1, 2
	2007	2008	€ billion	as %	2007	2008	€ billion	as %	Year-on-year change as %
	€ billion				€ billion				
Tax revenue, total ²	235.8	249.7	+ 13.9	+ 5.9	125.2	130.8	+ 5.6	+ 4.5	+ 3.8
<i>of which</i>									
Wage tax	62.7	67.5	+ 4.8	+ 7.6	32.2	34.7	+ 2.5	+ 7.6	+ 7.5
Profit-related taxes ³	36.3	42.2	+ 5.8	+ 16.0	23.1	25.3	+ 2.2	+ 9.5	+ 4.4
Assessed income tax	9.0	14.1	+ 5.0	+ 55.9	8.2	10.4	+ 2.2	+ 26.9	+ 20.1
Investment income taxes ⁴	15.7	18.5	+ 2.9	+ 18.4	8.7	10.1	+ 1.4	+ 16.0	+ 9.2
Corporation tax	11.7	9.5	- 2.1	- 18.1	6.2	4.8	- 1.4	- 22.5	- 17.8
Turnover taxes ⁵	83.0	86.2	+ 3.1	+ 3.8	41.0	41.9	+ 0.9	+ 2.2	+ 3.9
Energy and electricity tax	17.4	17.4	- 0.0	- 0.2	11.2	11.2	- 0.1	- 0.6	+ 2.1
Tobacco tax	6.4	5.8	- 0.6	- 8.8	3.5	3.3	- 0.2	- 5.6	- 5.9

¹ According to official tax estimate of May 2008. — ² Including EU shares in German tax revenue, but excluding receipts from local government taxes, which are not yet known for the last quarter recorded. — ³ Employee

refunds, grants paid to home owners and investors deducted from revenue. — ⁴ Non-assessed taxes on earnings and withholding tax on interest income. — ⁵ Turnover tax and import turnover tax.

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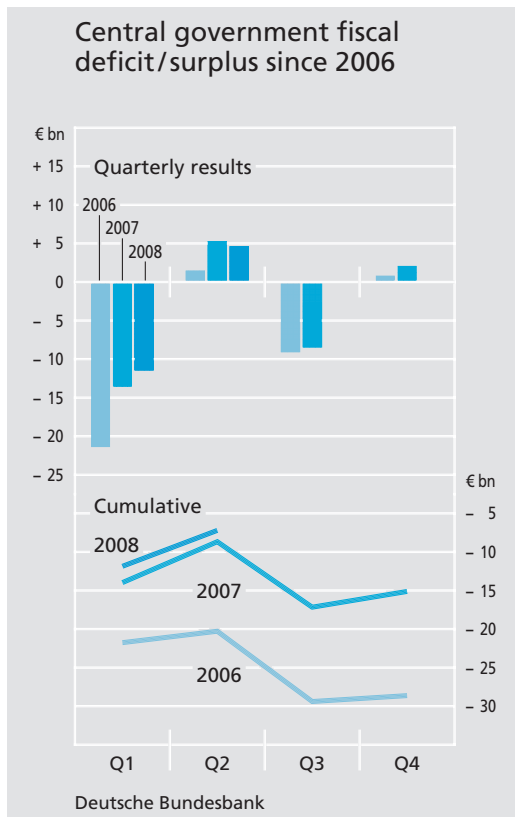
addition, considerable uncertainty exists with regard to the possible effects of the financial market turbulence.

Central government budget

Central government recorded a surplus of over €4½ billion in the second quarter of 2008 compared with just under €5½ billion in the same period of 2007. Total revenue continued to increase significantly by 4½ % (almost €3½ billion). However, tax revenue grew at a much slower pace (+2½ %) owing in part to larger payments to the EU, which fluctuate greatly over the course of the year. Non-tax revenue, by contrast, rose sharply by over €1½ billion, in particular as a result of bigger asset realisations. Furthermore, the re-integration payment from the Federal Em-

ployment Agency, which is intended to cover half of the labour market integration and administrative expenses in connection with the long-term unemployed, yielded over €½ billion more than the previous compensatory amount levied in the second quarter of last year. Expenditure was up 6 % (almost €4 billion) on the year. Current transfers again recorded sharp growth of 5½ %, predominantly due to transfers to the post office pension fund. Interest expenditure exceeded the corresponding prior-year level by 30 % (over €1 billion). In addition to higher interest rates, especially for Federal Treasury notes (Schätze), this was also attributable to the fact that debt servicing for the five-year Federal notes (Bobls) issued in the second quarter of 2007 began one quarter later than the series that expired at that time. Extra costs of 4 % were

Surplus declined somewhat in Q2



recorded for personnel expenditure, too, in the wake of increases in pay rates.

2008 deficit target expected to be met

For 2008 as a whole, the central government budget envisages only a moderate decrease in the deficit of €2 ½ billion to just over €12 billion. As things now stand, this appears to be an achievable target. In comparison with the draft budget, there are now a number of additional budgetary burdens, such as the extraordinary payment to support IKB Bank, the cancellation pursuant to a ruling by the European Court of Justice of a subsidy repayment by the post office previously ordered by the EU, and the higher-than-forecast increase in personnel remuneration. These burdens amounting to approximately €3 billion should be offset, however, by lower-than-budgeted expenditure in a similar amount, notably for

interest charges, transfers to the Federal Railways Fund, overall spending on the long-term unemployed and also for underwriting commitments drawn. Moreover, the latest tax estimate forecasts additional revenue of €½ billion.

The 2009 central government budget, approved by the Cabinet at the beginning of July, envisages some consolidation progress overall. While the deficit is to be reduced by only €1½ billion – as announced in 2007 – to just over €10 ½ billion, privatisation proceeds are to be concurrently decreased by €6 ½ billion, so that the fiscal balance should improve by €8 billion after adjustment for proceeds from asset realisations. However, a number of items need to be factored out of the calculation: this year's non-recurring charges totalling over €2 billion from supporting IKB bank and from the cancelled subsidy repayment ruling by the European Court of Justice plus one-off budgetary relief estimated at approximately €2 billion owing to a retroactive methodological adjustment to EU financing and a change in the way that grants to the post office pension fund are appropriated, which will yield one-off budgetary relief amounting to €½ billion.

Consolidation progress in 2009 central government budget

Expenditure is expected to grow by almost 2% (€5 billion) in 2009 vis-à-vis the targeted figure for 2008. The ceiling of 1% set by the Financial Planning Council in November 2006 will therefore be perceptibly overshoot once again even though savings of €3 billion will result, in particular, from lower benefits for the long-term unemployed, the end of the all-day school programme and the termin-

Much higher spending compared to last financial plan

ation of parental benefits. The budget for 2009 indicates additional expenditure of €3 billion compared to the medium-term financial plan from last year. However, the aggregated increase recorded for the areas of defence, transportation, development aid, the environment, internal security and family assistance is significantly higher. This additional expenditure classified as having political priority was partly offset in accounting terms mainly by lowering the budget appropriation for interest payments by €1 ½ billion. This means that the margin of safety factored into this item was liquidated to help fund additional spending programmes. Forecast expenditure has been further lowered by shifting costs of €½ billion onto the Federal Employment Agency following a restructuring of contributions for child-rearing periods, which was planned in 2007, and by changing the payment date of VAT-financed central government grants.

Additional revenue curtailed by provisions for increasing child benefit

Revenue has been raised in the 2009 draft budget compared with the last financial plan as tax receipts, income from the planned increase in motorway tolls for heavy goods vehicles and proceeds from the sale of CO₂ certificates are expected to yield €1 billion each. Further extra revenue has been offset by a global revenue cut of €1 billion as a provision for the envisaged rise in tax allowances for children and in child benefit following a recalculation of the socio-cultural minimum subsistence level in the fourth quarter.

The medium-term fiscal plan maintains the target set last year of zero central government net borrowing as of 2011. However,

Central government's medium-term financial planning

Zero net borrowing from 2011 but no provision for foreseeable lower revenue

€ billion

	Actual 2007	Target 2008	Draft 2009	Financial plan		
				2010	2011	2012
Expenditure 1	270.4	283.2	288.4	292.4	295.2	300.6
of which						
Investment	26.2	24.7	25.9	25.9	25.5	25.3
Revenue 1, 2	256.0	271.3	277.9	286.4	295.2	300.6
of which						
Taxes 1	230.0	238.0	248.7	255.4	266.3	276.0
Privatisation proceeds	4.5	10.7	4.3	6.5	4.6	1.7
Net borrowing	14.3	11.9	10.5	6.0	-	-
<i>Memo item</i>						
Percentage increase in expenditure	+ 3.6	+ 4.7	+ 1.8	+ 1.4	+ 1.0	+ 1.8

1 After deduction of supplementary central government grants to state government and of shares in revenue from energy tax. — 2 Including proceeds from coin seigniorage.

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privatisation proceeds of €4 ½ billion are envisaged for 2011. In 2012, the final year of the medium-term financial projection, the budget will be almost balanced after factoring out one-off proceeds of €1 ½ billion. In 2010 and 2011 growth in expenditure should be limited to 1 ½% and 1% respectively. However, increasing rule-based transfers to the statutory health insurance and pension insurance schemes are likely to restrict this scope significantly. This means that other expenditure has to be kept to a minimum. The rise in special tax allowances for contributions to the health and long-term care insurance schemes stipulated by the Federal Constitutional Court as of 2010 is also likely to make it extremely difficult to achieve the envisaged deficit reduction. No provision has been made for this in the medium-term financial

plan. Policymakers should ensure that these budgetary strains, as well as other tax relief measures that are occasionally discussed, are fully counterfinanced so that the budget really can be balanced as envisaged.

Tightening of constitutional borrowing limits

In the second phase of the reform of Germany's federal structure, central government aims to tighten the borrowing limits enshrined in Germany's Basic Law. An outline paper put forward at the end of June by the chairmen of the reform commission extends this goal to include state government and further defines the contents of the reform. A number of the additional projects, such as an early warning system, transitory consolidation assistance for overindebted state governments, restricted fiscal autonomy and various administrative reforms, are very worthwhile, and a package solution aimed at tightening borrowing limits could increase the chances of reaching an agreement in these areas. Yet the introduction of an effective constitutional safeguard against what has hitherto been largely unabated growth in government debt is of particularly great importance. The idea contained in the outline paper of pegging this objective to the requirements of the Stability and Growth Pact would prevent any inconsistencies from arising between national and European fiscal rules. Moreover, given the looming demographic burdens it would seem sensible to greatly restrict the as yet undefined scope for structural borrowing. It may also be necessary to carefully monitor the deficits that have been classified as cyclically induced. If these deficits are not offset by surpluses during upturns, then consolidation measures would be necessary to prevent gov-

ernment debt from permanently growing.⁶ If it proves impossible to reach a satisfactory agreement with the state governments, borrowing limits could be tightened for central government alone as it has been responsible for the largest share in the growth of government debt over the past decades.

State government budgets⁷

The favourable development of state government finances continued in the second quarter, albeit a little less strongly. The surplus increased by almost €1 billion to €6 ½ billion on the year. Revenue continued to grow sharply (+5 %) owing to an ongoing positive trend in tax receipts. However, expenditure likewise rose significantly (+4 %). Besides an evidently continued large rise in transfers to local government under the tax revenue-sharing arrangements, this is attributable not least to the clear increase in personnel expenditure (+2 %), reflecting the adjustment of civil servants' pay and pensions in line with the collective pay agreements for salaried employees.

Favourable development of state government finances continued in 2008 Q2, ...

However, during the remainder of the year, notably slower tax growth and higher personnel expenditure are likely to have a rather negative effect and counteract any further in-

... however, burdens evident in later part of 2008

⁶ For more information on various aspects of budgetary rules, in particular the need to take account of estimation errors, see Deutsche Bundesbank, Reform of German budgetary rules, Monthly Report, October 2007, pp 47-68 and J Kremer und D Stegarescu (2008), Eine strenge und mittelfristig stabilisierende Haushaltsregel, in Wirtschaftsdienst, Vol 88 pp 181 ff.

⁷ The development of local government finances in the first quarter of 2008 was analysed in greater detail in the short articles in the Bundesbank Monthly Report of July 2008.

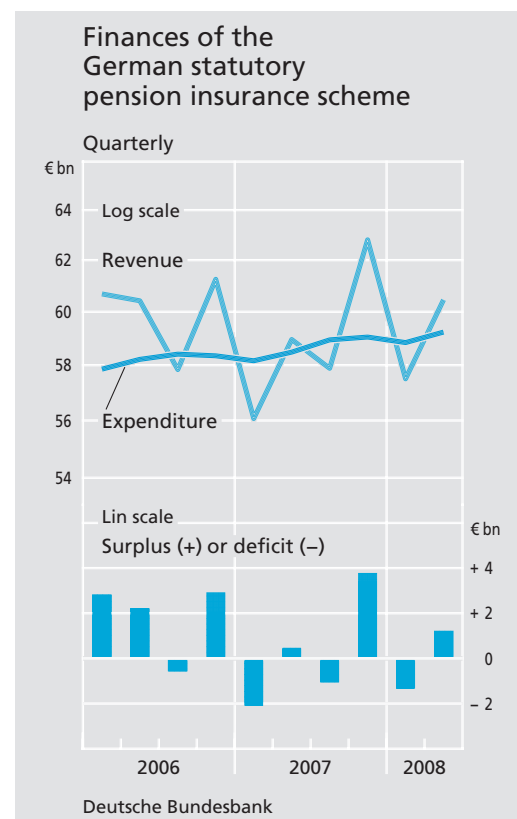
crease in the surpluses. In fact, the budgets foresee an aggregate deficit of €6 ½ billion although almost half of state governments do not intend to take up any new loans and even intend to repay some debt. Yet in spite of favourable growth in tax revenue, those states with extremely high *per capita* borrowing, especially Bremen, Saarland and Schleswig-Holstein, that have featured prominently in claims for budgetary assistance, are not expecting to make any significant progress towards consolidation this year and in part are even planning to borrow more than last year. Furthermore, the difficult financial situation of some Landesbanks continues to pose a threat for the states affected. However, the charges allotted in budgets for this purpose could remain rather limited over the next few years as the assets that are currently greatly impaired are mostly to be held until maturity under the protection of risk shields erected by the bank owners. It is not possible at present to estimate the losses that will then have to be made good by state governments.

Social security funds⁸

Statutory pension insurance scheme

Favourable financial development in Q2

The statutory pension insurance scheme recorded a surplus of almost €1½ billion in the second quarter of 2008. This amounts to a financial improvement of more than €½ billion on the year. Thanks to the favourable employment and pay trends, the increase in revenue (+2 ½ %) outstripped that in expenditure (+1 ½ %). Contribution receipts recorded particularly large growth (+3 ½ %), especially



for employees' compulsory contributions. However, contributions for recipients of unemployment benefits sank significantly once again. Transfers from the central government budget showed a marginal increase on the year. On the expenditure side, pension payments went up by 1%, over half of which is attributable to the 0.54 % rise in pensions as from 1 July 2007 and the remainder to the – again moderate – increase in the number of pensioners. Considerably more was spent on rehabilitation benefits.

The deficit that is customarily recorded in the first quarter was largely offset by mid-2008.

Bigger surplus expected for full year

⁸ The financial development of the statutory health and public long-term care insurance schemes in the first quarter of 2008 was analysed in the short articles of the Monthly Report of June 2008. These are the most recent data available.

In the first six months of 2007, the accumulated deficit had amounted to over €1½ billion. In the second half of 2008, a further boost from contribution receipts is expected. However, this will be partly offset by sharper growth in pension expenditure owing to the higher increase of 1.1% as from 1 July 2008.⁹ Overall, the financial outturn is likely to be appreciably better than last year when a surplus of just over €1 billion was recorded.

Federal Employment Agency

Only marginal deficit in Q2

The Federal Employment Agency recorded a deficit of just over €½ billion in the second quarter. Revenue went down by 10½% whereas expenditure went up by 10½%. In a year-on-year comparison, this constitutes a financial deterioration of €2 billion. On balance, this is almost entirely due to lowering the contribution rate from 4.2% to 3.3%. The financial outturn also includes transfers of almost €1 billion to the Agency's dedicated civil servants' pension fund to cover future civil servant pensions. Furthermore, the new reintegration payment (by means of which the Agency is supposed to reimburse half of central government's labour market integration and administrative expenses in connection with recipients of unemployment benefit II) was over €½ billion higher than the corresponding compensatory amount which it had to pay up to last year. Without these factors, the financial position of the Federal Employment Agency would have improved markedly.

On the revenue side, income from contributions was almost 12½% lower in the second

quarter than one year ago. After adjustment for the reduction in the contribution rate, this would have meant an increase of almost 11½%, although such an increase would have presented a distorted picture of the underlying development owing to the shift of payments from the first to the second quarter. In a year-on-year comparison of the first two quarters, which provides a more realistic picture, revenue from contributions, adjusted for the change in the contribution rate, grew by almost 5%. This reflects the favourable employment trend and the comparatively substantial wage increases. In the second quarter, the grant from central government was 17½% up again on the year as, for the first time following its introduction last year, it was based on the assumed full effect on cash revenue of 1 percentage point of the increase in the standard rate of VAT.

Contribution trend distorted in Q1 and Q2

On the expenditure side, there was once again a sharp drop in unemployment benefit I (-19% or almost -€1 billion), which was predominantly attributable to the declining number of recipients. However, this was offset, in particular, by transfers to the dedicated civil servants' pension fund and the higher reintegration payment (in the second quarter, these amounted to +€1½ billion). Higher spending on active labour market policy measures was of minor significance in quantitative terms.

Only slight rise in operating costs

⁹ If the adjustment formula had been applied, this would have resulted in a pension increase of 0.46%. However, the 2008 Pension Adjustment Act suspended for two years the dampening effect of deducting employees' (putative) costs of supplementary private pension provision. The resulting larger pension adjustments will lead to additional expenditure of over €½ billion in the second half of this year, €2 billion next year and €3 billion in the following years.

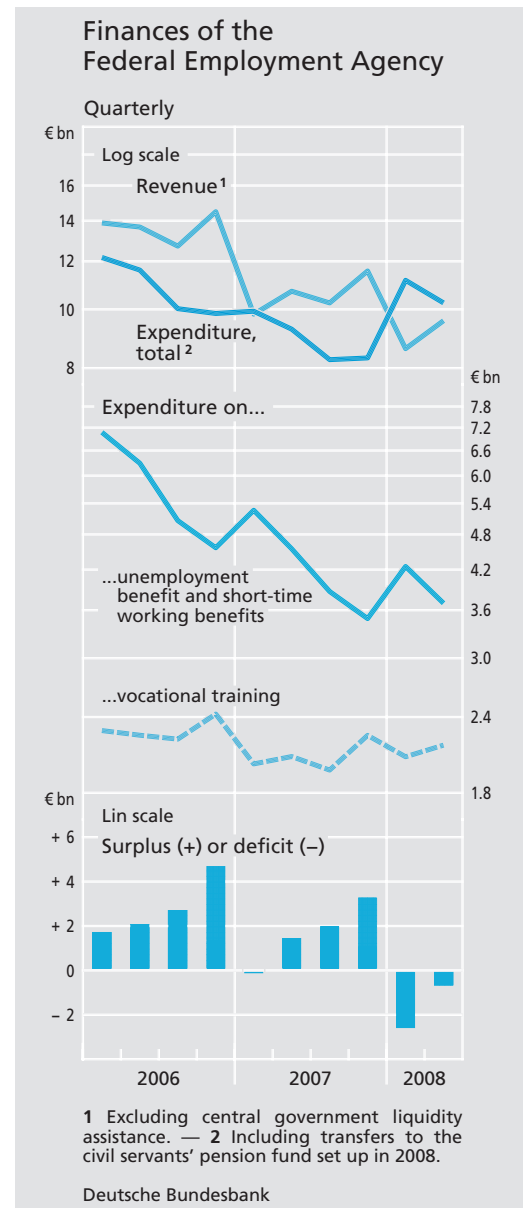
Measured by actual operating costs, ie excluding the one-off transfer to the civil servants' pension fund, expenditure rose by not quite 1% in the second quarter.

Financial situation better than estimated in budget

In the first six months of 2008, the Federal Employment Agency recorded a deficit of almost €3 ½ billion. However, including the civil servants' pension fund, the total deficit amounted to less than €1 billion. The financial situation for the year as a whole looks much better than estimated in the Federal Employment Agency's budget. The budgeted deficit of €5 billion (including expenditure of €2.5 billion on the one-off transfer to the civil servants' pension fund) will turn out to be considerably smaller. A surplus is likely to be posted in the second half of the year, mainly owing to higher receipts from contributions at the end of the year, although the longer period of entitlement to unemployment benefit I and extra vocational training costs will result in additional expenditure. In consolidated terms, ie including the civil servants' pension fund, it is also possible that the year as a whole will conclude with a surplus.

Federal Employment Agency's finances very volatile over the economic cycle

Ultimately, labour market developments are the key factor for the Agency's outlook. The Federal Employment Agency's finances are especially sensitive to fluctuations in employment as these have a knock-on effect both on contribution receipts and on expenditure on wage substitutes. Any further lowering of the contribution rate would increase the risk that, if the labour market dynamics were to



slacken, large deficits could again be incurred and the available reserves (€14 ½ billion as at mid-2008) would be quickly depleted. As a consequence, it may be necessary to raise contribution rates again in an ensuing downturn, thus magnifying its consequences.