Germany Urgently Needs A New Fiscal Policy

by Rainer Apel

If panic and despair were commodities traded on the market, Germany would be a flourishing economy under Minister of Finance Hans Eichel. For weeks, hardly any day has gone by without another attempt to promote deeper cuts in yet another budget item. But things have now taken an absurd course. Eichel's problem is that he cannot think of a reasonable alternative to the European Union's Maastricht system of strict budget rules, and because he sees no alternative, he keeps trying to do the impossible: staying loyal to the Maastricht rules while at the same time violating them, continuously.

Eichel is violating the rules now for the fourth time with his budget proposal for FY 2005, as tax revenues shrink because of the deepening economic depression, state expenses increase for unemployment support payments, and the burden of payments on old debt continues. Eichel is massively borrowing new money—an increase of 14.4 billion euros over FY 2004, to 43.7 billion in 2005.

In November 2003, Eichel escaped his third violation of European Commission sanctions because the finance ministers of France, Italy, and some other EU member governments were in a comparable precarious situation and voted with him to freeze the sanctions mechanism. But now, the fourth violation, which will be very difficult to avoid, would penalize Germany approximately 10 billion euros in 2005.

Issue 'Too Important' for the Finance Minister

That is why Chancellor Gerhard Schröder, who enlisted the support of the French President at their meeting in Berlin on Oct. 26, decided to make the Maastricht question an issue for himself. "The matter is too important to be left in the hands of the finance minister," Schröder said.

Chancellor Schröder wants a "reform" of the Maastricht rules—not one that would change the fundamentals of the system, but certain modifications that would give Germany more fiscal breathing room and get the sanctions threat off its back. Whereas France is thinking of exempting military expenditures from the Maastricht rules, Germany wants to exempt expenditures in science and education, and its annual payment of 9 billion euros to the common EU budget.

But this push for change, which does not seriously challenge the Maastricht structure, has no parallel in Germany's national fiscal approach. Quite the contrary, more austerity is being pursued to balance the budget. Finance Minister Eichel on Nov. 5 announced that he plans a budget freeze for all public sector workers for FY 2005, and he wants to avoid paying 5.5 billion euros in state support for the pension funds of the postal and telecom services, through an obnoxious scheme.

Eichel's scheme is a market sale of part of the annual income or of shares of the postal service and the telecom agency into the pension fund. The pension fund has legal claims on annual support from these two services in the range of 6 billion euros, and these claims are going to be sold to whatever institutional or private investor is interested. With a "price cut" incentive to the investor of about 500 million euros, Eichel expects to be paid by that investor 5.5 billion euros in advance, with which he can then cut the FY 2005 budget deficit. If the investor does not get his claim on 6 billion euros reimbursed, Eichel will have to compensate them in FY 2006.

Banking experts warn that the scheme will be more expensive in the long run than normal borrowing. But Eichel does not want to borrow, in order to avoid another violation of the Maastricht rules.

Indicative of Despair

Another scheme, to abandon German Unity Day (October 3) to create an additional working day, was dropped only two days after the German cabinet announced it on Nov. 3, because of stiff opposition among the governing Social Democrats of Chancellor Schröder. The affair is indicative of the despair that dominates the fiscal planning of the government these days.

Other Eichel atrocities include the announcement, on Oct. 1, of yet another freeze on pensions, for 2005. A freeze on pension increases for 2004 was sold to the 20 million retired citizens of Germany as a one-time cut that would "most likely" not be repeated in 2005 because the economic situation would improve. The situation has not improved, and the freeze for 2005 (which gives Eichel several billion euros) will likely not be the last either.

Fiscal mathematics is not something Eichel and his staff have mastered. This was revealed, once again, on Nov. 8, when his ministry said that it urgently needs an "unexpected" extra 1.4 billion euros, for payments to the long-term unemployed. This extra money is required, because Eichel's staff a year ago had forecast 1.87 million long-term unemployed, but in reality, it is already 2.3 million. This also implies that the 300,000 long-term unemployed will not receive any payment from 2005 on, and will be forced to cash in whatever property they have (cars, insurance, shares) to meet living expenses. And another 200,000 Germans, according to estimates, will have to be added, who were not accounted for in Eichel's statistics.

What Germany urgently needs is a new finance minister. But it also needs a totally new fiscal policy. The present policy is a disaster.