INTERNATIONAL MONETARY FUND

GERMANY

STAFF REPORT FOR THE 2022 ARTICLE IV CONSULTATION— SUPPLEMENTARY INFORMATION

July 12, 2022

Prepared By	European Department

This supplement provides information that has become available since the staff report was issued to the Executive Board on July 1, 2022.

1. **There are increasing signs of tightening gas supply in Germany.** Prices of natural gas futures for the second half of 2022 and early 2023 have continued to increase in recent days, standing, as of July 12th, 2022, 50 percent higher than their levels prior to the reduction in Nord Stream 1 flows. Staff continues to estimate that Germany can avoid, albeit narrowly, shortages of gas in the next two winters if gas flows from Russia do not decline further (and re-exports of gas decline proportionally with the recent reduction in gas flows through Nord Stream 1). However, gas reserves would drop to low levels even under normal winter temperatures, thus leaving Germany vulnerable in case of a stoppage of the remaining supplies of Russian gas.

2. **To avoid disorderly conditions in gas markets in case of a further drop in imports, the authorities have amended the Energy Security Act.** Key changes include a temporary legal amendment to facilitate rapid government intervention to stabilize critical companies in the energy sector, and a price adjustment mechanism that would allow the increased costs of gas procurement to be passed on to end users. Staff continues to encourage such pass through to incentivize energy savings and to ensure that gas inventories can be built further ahead of the winter.

3. **Escalating tensions in gas markets, a further downshift in consumer sentiment, together with growth slowdowns projected for many of Germany's trading partners, are expected to weigh on Germany's growth.** Staff has made the following revisions to the key macroeconomic projections, which will also be reflected in the July 2022 Update of the World Economic Outlook:

- Germany's GDP growth has been revised down to 1.2 percent for 2022 and 0.8 percent for 2023 (-0.3 and -1.1 percentage points relative to the staff report projections, respectively), reflecting expectations of more subdued activity

through 2023.[1] Growth is expected to pick up from the second half of 2023 onwards, as floating LNG terminals come online, temperatures increase, and tensions in the gas market thus begin to ease. The output gap is expected to close in 2026, one year later than previously envisaged.

- Average headline consumer price inflation has been revised up further to 7.7 and 4.8 percent for 2022 and 2023, respectively (about 0.3 percentage point higher than the staff report projections for both years), with consumer energy prices expected to increase relative to prior projections.

4. Staff's fiscal advice remains as set out in the staff report. The more precarious outlook—with weaker growth and higher inflation—underscores the need for fiscal policy to remain flexible and ready to respond with well-targeted measures. The draft budget, approved by the Cabinet on July 1 (as part of the regular budget process) with only minor changes relative to the draft unveiled in April, confirms the authorities' intention to return to the constitutional debt-brake rule. The tightening in the cyclically-adjusted deficit would be around 1½ percent of GDP, close to the projection in the staff report, reflecting the expected phase-out of the majority of temporary COVID-19 and energy-related relief measures. Staff assesses that even under the revised baseline, which incorporates some decline in energy prices in 2023 and an easing pandemic, the envisaged fiscal tightening would remain manageable, with reduced support for domestic demand helping to cool inflation pressures. Moreover, the budget rule is flexible enough to accommodate some extra spending if nominal GDP growth disappoints. But the economy—and in particular low-income households and energy companies—would likely need more support in case of a further sizeable increase in gas prices. The authorities should plan for such a contingency, which would require relief measures to be well-targeted and time-bound to avoid adding to inflation pressures. If there is a complete shut-off of remaining gas flows from Russia, the government should allow automatic stabilizers to operate fully and if needed consider activating the escape clause of the debt break rule for another year to be able to respond flexibly to the change in the outlook.

5. The thrust of the staff appraisal remains unchanged.

[1] The total downward revision to growth triggered by the partial shut-off of Nord Stream 1 flows is about 0.5 percentage point for 2022 and 0.6 percentage point for 2023, meaning that staff has shifted 30–40 percent of the output loss for 2022 and 2023 in a full shut-off scenario (as shown in the last row of Table 3 of the Selected Issues Paper) into the baseline.

Table 1. Germany: Selected Economic Indicators, 2020–25

	2020	2021	2022	2023	2024	2025
			Projections			
Output			(unadjusted)			
Real GDP growth (%)	-4.6	2.9	1.2	0.8	2.4	2.2
Total domestic demand growth (%)	-4.0	2.3	2.2	0.7	2.4	2.4
Output gap (% of potential GDP)	-3.6	-1.6	-1.2	-1.2	-1.0	-0.3
Employment						
Unemployment rate (%, ILO)	3.8	3.6	3.1	3.4	3.1	3.0
Employment growth (%)	-1.0	-0.7	1.6	-0.2	0.1	0.1
Prices						
Inflation (%, headline, period avg.)	0.4	3.2	7.7	4.8	3.2	2.2
Inflation (%, core, period avg.)	0.8	2.3	4.0	3.9	3.3	2.5
General Government Finances						
Fiscal balance (% of GDP)	-4.3	-3.7	-3.2	-1.8	-1.3	-0.9
Revenue (% of GDP)	46.5	47.9	47.1	46.9	47.0	47.1
Expenditure (% of GDP)	50.8	51.6	50.2	48.7	48.3	48.0
Public debt (% of GDP)	68.7	70.2	70.9	68.9	65.8	63.2
Money and Credit						
Broad money (M3) (end of year, % change) 1/	8.2	5.6				
Credit to private sector (% change)	4.9	5.4				
10-year government bond yield (%)	-0.5	-0.3				
Balance of Payments						
Current account balance (% of GDP)	7.1	7.4	5.7	6.2	6.9	6.9
Trade balance (% of GDP)	5.7	5.4	3.9	4.4	4.7	4.5
Exports of goods (% of GDP)	35.2	38.3	37.5	37.6	37.4	37.3
Volume (% change)	-9.0	10.0	1.9	4.2	4.3	4.3
Imports of goods (% of GDP)	29.6	32.9	33.7	33.0	32.5	32.5
Volume (% change)	-5.3	8.0	1.5	3.4	4.4	4.8
FDI balance (% of GDP)	-0.1	2.9	1.6	1.5	2.0	1.7
Reserves minus gold (billions of US$)	64.0	99.2				
External Debt (% of GDP)	165.1	171.8				
Exchange Rate						
REER (% change)	1.3	0.9				
NEER (% change)	2.4	0.8				
Real effective rate (2005=100) 2/	96.7	97.6				
Nominal effective rate (2005=100) 3/	103.8	104.7				

Sources: Deutsche Bundesbank, Eurostat, Federal Statistical Office, Haver Analytics, and IMF staff calculations.
1/ Reflects Germany's contribution to M3 of the euro area.
2/ Real effective exchange rate, CPI based, all countries.
3/ Nominal effective exchange rate, all countries.