

EXECUTIVE SUMMARY: OVERCOMING THE CORONAVIRUS CRISIS TOGETHER; STRENGTHENING RESILIENCE AND GROWTH

Overcoming the pandemic-induced recession

Not losing sight of the long-term challenges

Utilising international cooperation

Strengthening resilience and growth

This is a translation of the original report published in German, which is the sole authoritative text.

1. The **coronavirus pandemic** has caused one of the most severe recessions in the post-war era. The economy recovered quickly when the acute measures put in place by governments against the pandemic in spring 2020 were lifted. However, the recent increase in the number of infections shows how fragile the situation remains. In various areas of the economy, a normalization of the economic situation is still not foreseeable. The corona crisis has not yet been overcome. In view of the renewed pandemic-related restrictions the recovery in Germany and in many other European countries is likely to be on hold. Furthermore, wider changes that are driven by the pandemic – such as new patterns of individual behaviour, changing consumer preferences and new framework conditions – could have a long-term economic impact.

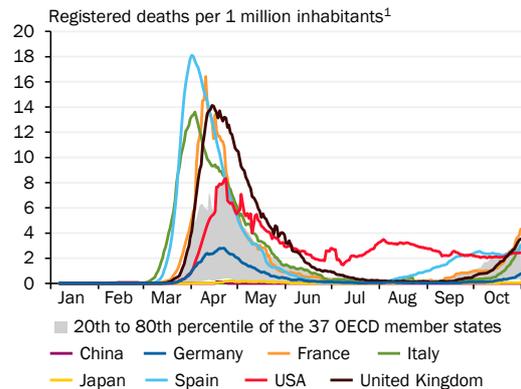
At the same time, the German economy was already confronted with **a number of long-term changes** even before the pandemic. The structural changes triggered by technological progress, demographic change and the transition to a carbon-neutral economy are major challenges, but at the same time offer opportunities. Economic policy is now called upon to overcome the crisis caused by the coronavirus pandemic, strengthen economic resilience in Germany and Europe, and increase growth potential.

Overcoming the pandemic-induced recession

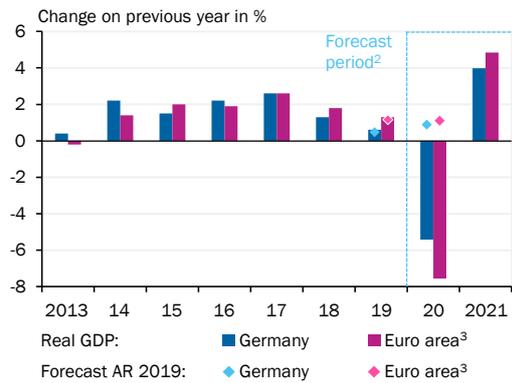
2. In **Germany**, the coronavirus pandemic led to the sharpest fall in economic output in a single quarter since the quarterly national accounts began in 1970. The strong recovery over the summer means that real **gross domestic product (GDP)** for 2020 as a whole is forecast to decline by 5.1 %, which is similar to the contraction seen in 2009 during the global financial crisis. The recovery is expected to continue next year, but at a slower rate of 3.7 %. ↘ [ITEM 45](#) It is unlikely that the pre-crisis level of the fourth quarter of 2019 will be reached before early 2022. The incidence of infection and any resulting restrictions will continue to determine the pace of recovery. In its forecast, the German Council of Economic Experts (GCEE) assumes the infection rate can be kept largely under control with limited interventions so that no further major lockdown on the scale seen in spring 2020 will be necessary and that international supply chains will not be massively disrupted. ↘ [ITEMS 45 FF](#). Clear communication on the part of policymakers – e.g., with regard to the criteria that determine when new restrictions are imposed or lifted – is crucial to the fight against the pandemic. ↘ [ITEMS 184 FF](#).
3. Developments in other countries also play an important role. China's economy is growing rapidly again and the strong recovery in the third quarter meant that the United States and the euro area were able to report a significant increase in GDP. ↘ [ITEMS 19 AND 21](#) However, the rate of recovery is now expected to slow down noticeably. For 2020, the GCEE expects GDP in the **euro area** as a whole to fall by a total of 7.0 %. ↘ [ITEM 42](#) Spain, Italy and France, three of the largest EU member states, have been among the most affected economies in the euro area. ↘ [ITEMS 42 FF](#). In 2021, the GDP growth rate in the euro area is expected to be positive again at 4.9 %. Given the ever-changing nature of the pandemic, however, there are considerable downside risks for global economic growth.

Economic growth during the coronavirus pandemic

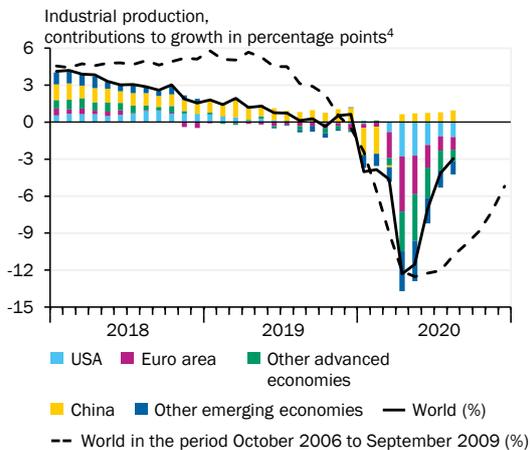
The coronavirus pandemic is affecting economic growth.



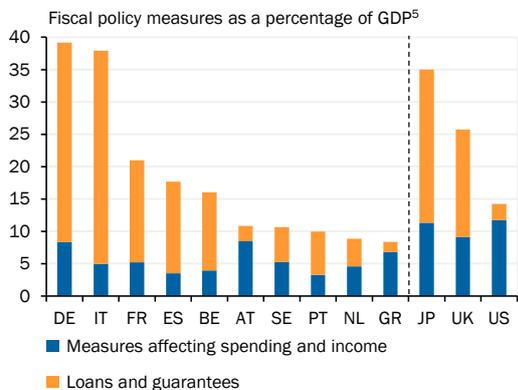
It has caused a severe recession in Germany and the euro area.



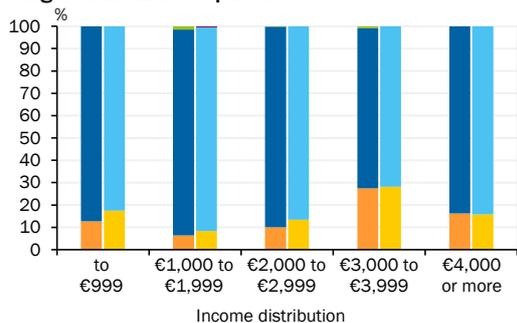
Industrial production is recovering faster than in the financial crisis.



Extensive monetary and fiscal policy measures are supporting the economy during the crisis.



The stimulus package is likely to boost economic output in 2020 and 2021; however, it is not targeted in all of its parts.



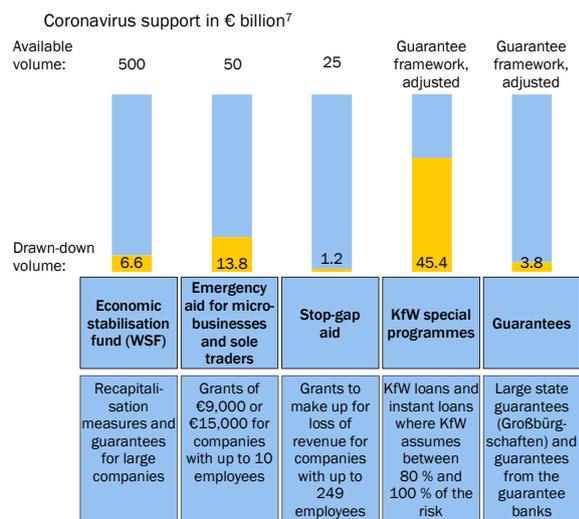
"Following the VAT cut, are you now buying more goods or more expensive goods than before?"⁶

Yes No Don't know / no input

"Are you planning to bring forward any major purchases that you would not otherwise have made until next year, or have you already done so?"⁶

Yes No Don't know / no input

Large parts of funds are still available.



1 – Moving average of the past 7 days. 2 – Forecast by the GCEE. 3 – Forecast based on seasonally and calendar-adjusted quarterly figures.

4 – Change on same month of the previous year, seasonally adjusted. Data and country definitions of the Dutch Centraal Planbureau (CPB).

5 – Measures announced as at 26 October 2020. DE-Germany, IT-Italy, FR-France, ES-Spain, BE-Belgium, AT-Austria, SE-Sweden, PT-Portugal,

NL-Netherlands, GR-Greece, JP-Japan, UK-United Kingdom, US-United States. 6 – Survey conducted for the GCEE by the infas Institute for Applied Social Sciences. For details see Chart 40. 7 – For details see Chart 29.

Sources: Association of German guarantee banks, BMF, BMWi, CPB, Eurostat, Federal Statistical Office, Feld et al. (2020), IMF, infas Institute for Applied Social Sciences, KfW, WHO, World Bank, own calculations

4. Policymakers have responded quickly and decisively to the crisis. **Extensive monetary and fiscal policy measures** were put in place, which supported the economy in the crisis. In addition, automatic stabilisers such as the progressive tax system, unemployment benefits and the short-time working scheme have provided a major source of support. In June 2020, the **German federal government** put together an economic stimulus package that is expected to boost economic output in 2020 and 2021. ↘ [ITEMS 163 FF](#). The funds have not yet been exhausted and are still available.

However, the stimulus package is not targeted in all of its parts. A survey carried out for the GCEE showed that the temporary cut in VAT has been of limited benefit to those households most affected by the crisis and that the tax cut has only partially led to increased consumption. ↘ [ITEMS 167 FF](#). In the further course of the crisis, **expanding the possibilities for tax loss carry-backward** and a more granular approach to stop-gap aid, depending on how affected recipients are by the crisis, would be beneficial. Moreover, an energy price reform could also provide additional stimulus. ↘ [ITEMS 195 AND 391 FF](#).

Other EU member states and **the EU** itself have also implemented a wide range of measures to counter the negative economic impact of the coronavirus pandemic. ↘ [ITEMS 258 FF](#). The **European Central Bank (ECB)** has provided a lot of liquidity into the banking system at highly favourable conditions in order to support lending and prevent a potential banking crisis. At the same time, the large expansion of the asset-purchase programme has helped to stabilise the financial and government bond markets. ↘ [ITEMS 105 FF](#).

5. **Digitalisation** helps cushion the effects of the coronavirus pandemic in many areas of the economy. ↘ [ITEMS 545 FF](#). Technology has enabled many companies to continue operating despite social distancing and hygiene regulations by switching to working from home. The pandemic has also highlighted deficits in the digitalisation of public administration, healthcare and education. In **healthcare**, a rapid expansion of the use of digital technologies in local public health authorities could create more efficient reporting paths and thus enable more rapid provision of information, which could be of major advantage in combating the pandemic. The carefully targeted use of such technologies could also help to contain further increases in the number of infections as the pandemic progresses. ↘ [ITEMS 186 AND 546 FF](#).

In the **education system** there should, as a minimum, be online solutions that can be implemented at short notice in case of further school closures. ↘ [ITEM 554](#) There is a risk that a prolonged reduction of access to education will diminish the development of skills and the **future employment opportunities of young people**, especially those from educationally disadvantaged backgrounds.

6. In the medium term, **scope for fiscal and monetary policy** should be created to enable an appropriate response to any future crisis. ↘ [ITEMS 196 FF](#). The sustainability of public finances should be ensured by appropriate consolidation steps that are designed according to the economic situation and promote growth. ↘ [ITEM 219](#) ↘ [DIFFERING OPINION ITEM 235](#) Monetary policy should communicate strategies for normalising the pandemic support measures, and avoid the risk of fiscal dominance

of monetary policy. ↘ [ITEM 203](#) The establishment of a debt-financed recovery fund at the European level, which was decided upon in July 2020, offers the opportunity to increase the resilience and competitiveness of the European economy through carefully targeted investment and reforms in the member states of the EU. ↘ [ITEMS 269 FF.](#)

Not losing sight of the long-term challenges

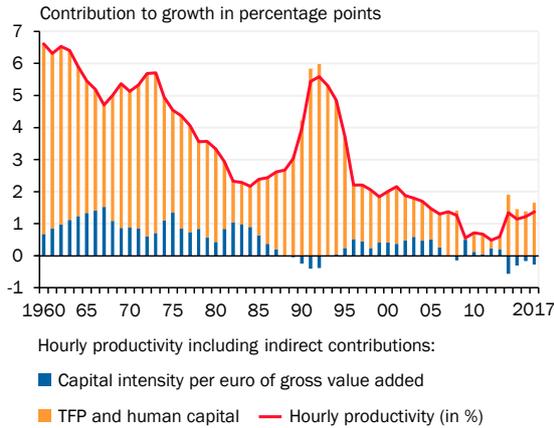
7. Despite of the coronavirus pandemic the **long-term challenges** for the German economy must not be forgotten. Productivity growth has been declining in Germany for several decades. Technological change and digitalisation in particular are giving rise to new business models and production processes that lead to profound changes in the economic structure and the labour market. A similarly comprehensive structural change is pending as a result of the planned reduction in greenhouse gas emissions, which makes a transition to a climate-neutral economy necessary. In addition, accelerating demographic change in Germany means that there will be more and more pensioners and fewer and fewer people in work in the years to come. These structural changes are interlinked in various ways. If policymakers succeed in addressing these challenges, **opportunities** for the German economy may arise.

Once the economy is clearly on course for recovery from the coronavirus pandemic, it will be important to focus on the economic framework conditions that ensure a sustained upturn and long-term growth. Support measures should not impede the **transition to long term competitive structures**. ↘ [ITEMS 205 FF.](#) The expansion of the short-time working scheme has prevented a sharp rise in unemployment. However, while this programme is still in place, even more extensive incentives should be offered and opportunities utilised to help employees develop their skills and equip themselves to prepare for future challenges. ↘ [ITEM 212](#)

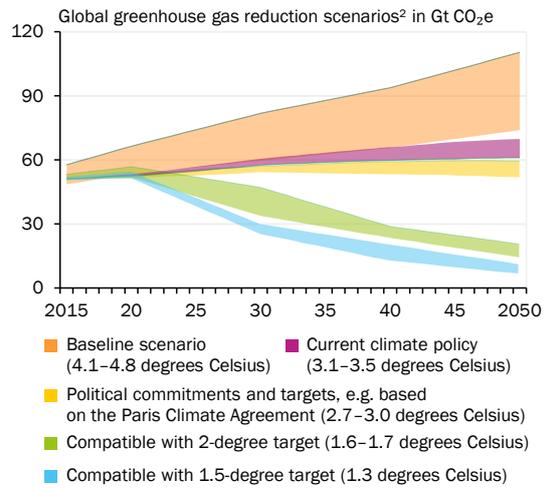
8. Structural change requires high levels of **private and public investment**. For **private investment**, the economic framework – and particularly the incentives for businesses and households – are crucial. ↘ [ITEMS 570 FF.](#) Climate policy that is designed to encourage a move towards climate-friendly technologies and products along complex value chains should focus on market-based incentives such as uniform pricing of emissions across sectors. Government-induced distortions caused by levies and transfers should be eliminated – along with indirect support of fossil-fuel technologies – as part of a comprehensive energy price reform. This could strengthen the coordination function of carbon pricing and provide better incentives for sector coupling. ↘ [ITEMS 371 FF.](#)
9. A significant portion of the economic stimulus package in Germany and funds from the EU recovery package are to go into **public investment**. If carefully targeted, this could boost long-term growth. During times of economic crisis, public sector investment can create a growth stimulus provided that projects can be implemented without lengthy delays. However, even without the pandemic there are bottlenecks that prevent timely implementation. These include a lack of spare capacity in the construction industry, a lack of planning and administrative capacity

Long-term challenges facing the German economy

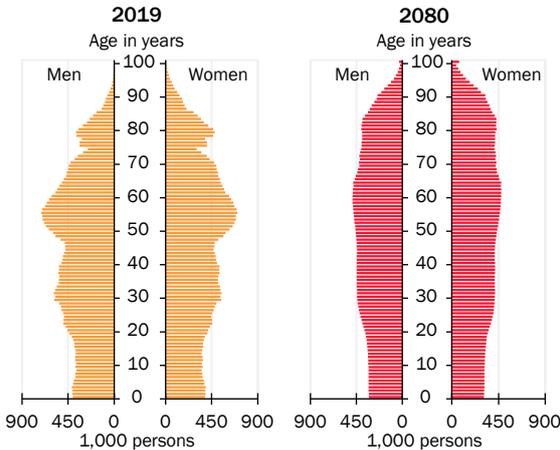
Productivity growth has been declining in Germany for several decades.¹



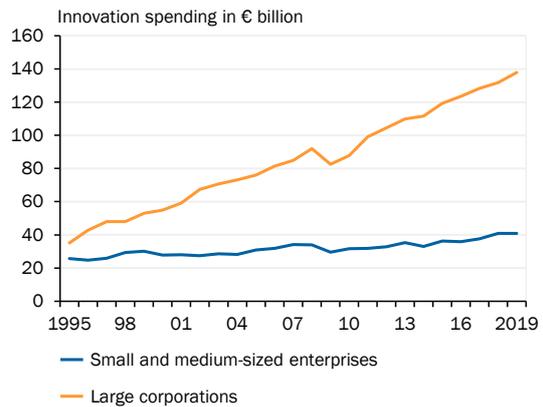
Stopping climate change requires a transition to a carbon-neutral energy system.



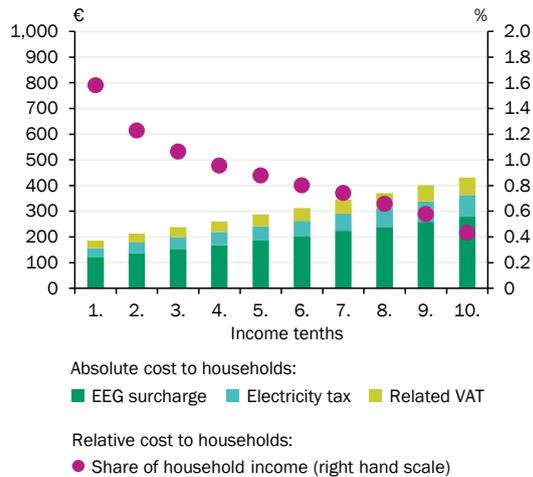
Demographic change in Germany means that there will be more and more pensioners and fewer and fewer economically active people in the years to come.³



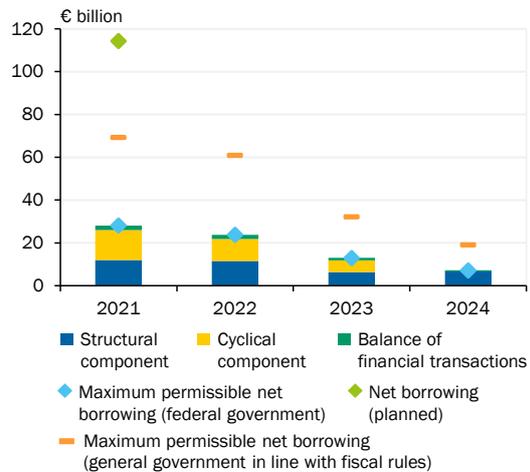
The innovation process is key to long-term growth. In Germany, innovation expenditure is concentrated on large companies.⁴



The focus should be on market-based incentives. Energy price reform could reduce distortions caused by the state through levies and transfers.⁵



In the medium term, there needs to be more flexibility in fiscal and monetary policy to enable a full-scale response to any future crisis.⁶



1 – TFP-Total Factor Productivity. For details see Chart 73. 2 – Annual emissions reduction quantities based on the warming projections of the Climate Action Tracker (CAT). For details see Chart 58. 3 – For details see Chart 101. 4 – For details see Chart 76. 5 – For details see Chart 65. 6 – For details see Chart 45.

Sources: BMF, BMWi, CAT, European Commission, Federal Statistical Office, Feenstra et al. (2015), Mannheim Innovation Panel (MIP), Penn World Table Version 9.1, RDC of the Federal Statistical Office and Statistical Offices of the Länder, Einkommens- und Verbrauchsstichprobe 2018 Grundfile 5 (HB), Werdung (2020), ZEW, own calculations

and lengthy planning and approval procedures, particularly at municipal level.
 ↘ ITEM 179 In some areas, public investment could be a useful complementary measure to accompany emissions trading in encouraging the transition to a carbon-neutral economy. ↘ ITEMS 433 FF.

10. The **innovation process** plays a central role in long-term economic growth. ↘ ITEMS 485 FF. Innovation and the use of new technologies are also particularly important for the transition to a carbon-neutral economy. In order to strengthen productivity growth, government innovation policy can support private-sector investment, which is inefficiently low due to positive knowledge externalities. In Germany, the private sector accounts for around two thirds of research and development (R&D) spending. Innovation expenditure is increasingly concentrated on large companies. As small and medium sized enterprises are particularly affected by obstacles to innovation, their incentives to innovate should be strengthened in order to accelerate the diffusion of new technologies. ↘ ITEMS 507 FF.
11. Digital technologies are often cross-sectional technologies that can be used to increase productivity across large sections of the economy. In order to speed up the **diffusion of digital technologies** and enable the development of new business models, additional investment in digital infrastructure is required, along with elimination of the red tape that hinders its development. Germany's small and medium-sized companies, in particular, are still finding it difficult to reap the benefits of digitalisation, implement the necessary organisational adjustments and make the necessary complementary investment in knowledge and skills. ↘ ITEMS 541 AND 563 FF. To face the deficit in the **digitalisation** of the public sector exposed by the pandemic, policymakers can use financial support for healthcare and education to provide the stimulus needed to close these gaps and to ensure that the benefits from the rush to digitalisation brought about by the pandemic are enduring. The measures included in the economic stimulus package may help. ↘ ITEMS 160 FF. However, the success of these measures will not hinge solely on the amount of funding available. Even more important will be the administrative implementation.
12. Demographic change is restricting the supply of skilled workers. Especially in construction and crafting, but also in the care sector, in medical activities and in information and communication technologies, there is already a shortage of skilled workers. In addition, rapid technological change and the transition to a carbon-neutral economy are likely to lead to greater demand for specialists in the STEM (Science Technology Engineering Math) professions. ↘ ITEMS 443 F. **Education, further training and lifelong learning** will play an important role to meet this demand in the long term. Targeted measures in schools could be particularly effective in helping to promote women in STEM subjects and the promotion of equal opportunities in education in order to close the gap in the future. A flexible education and training system can help employees to prepare for technological change. Digital key competencies should therefore be taught in schools and lifelong learning should be promoted, for example through professional development, lifelong learning and training opportunities throughout working life. ↘ ITEMS 580 FF. Such a system also improves the chances for uninterrupted employment, reduces the risk of a reduction in earning capacity, and is therefore the most

effective preventive measure against poverty in general and old-age poverty in particular. ↘ ITEM 699

13. The impact of demographic change may also make it more difficult to consolidate public finances after the coronavirus pandemic. Increasing life expectancy combined with lower birth rates and moderate levels of immigration, as well as the fact that the baby-boomer generation approaches retirement age, will substantially increase the burden on the **social security systems**. In the short term, the reintroduction of the ‘catch-up factor’, which was suspended in 2018, could counteract the rise in costs of statutory pension insurance. ↘ ITEMS 609 FF. This would gradually reverse any pandemic-related increase in the ratio of pension and wage levels in the coming years.

In the long term, an increase in the legal retirement age – for example by linking it to rising further life expectancy – could alleviate the sustainability problem. Two thirds of the **increase in life expectancy would be allocated to a longer working phase and one third to a longer retirement phase**. ↘ ITEM 639 ↘ DIFFERING OPINION ITEMS 705 FF. An actual extension of the working phase will be achieved only if the workforce is enabled to work longer. Systematic further training and education, opportunities to retrain, avoidance of incentives for early retirement, incentives for working longer and better protection against incapacity for work will play a key role. ↘ ITEMS 667 F.

Utilising international cooperation

14. **International cooperation and division of labour** are essential in overcoming the coronavirus pandemic and coping with the long-term challenges. The coronavirus pandemic is affecting both supply and demand and interfering with national and international supplier and end customer relationships. In an open economy such as Germany, economic recovery relies on the virus being contained also abroad so that the global economy can return to normality. ↘ ITEMS 22 FF.

Germany and the EU enjoy substantial welfare and productivity gains thanks to international trade and the international division of labour. However, during the coronavirus crisis, there has been a tendency to limit cross-border **trade**, as has often been the case during periods of major economic uncertainty in the past. New protectionism in the wake of the coronavirus crisis should be vehemently opposed. The EU has a key role to play in keeping trade open – primarily that of coordinator. ↘ ITEMS 325 FF. It should operate a **joint crisis management** system with regard to supply chains.

15. Climate change is another problem that can only be tackled at a global level, which is why national and European efforts must always be seen in a global context. Germany and the EU can already initiate or push ahead partnerships in areas such as the hydrogen strategy that increase the chances of meeting global **climate targets**. ↘ ITEMS 461 FF. In addition to the commitment to an internationally coordinated approach to reducing greenhouse gas emissions, a shift from national and

sectoral targets to a cross-sectoral European emissions trading scheme would be necessary to achieve the European targets efficiently. ↘ [ITEMS 372 FF](#).

16. For its member states, the EU is an opportunity to act together internationally and use the opportunities offered by the single market. The primary goal should be for all member states **to emerge from the crisis stronger than before** by encouraging productivity and growth and increasing **resilience to future crises**. The sustainability of public finances, an effective fiscal framework and the stability of the financial system are essential prerequisites for a resilient Europe in the future. It is also important to identify the tasks that would be better located at the EU level or that should remain at the national level due to the principle of subsidiarity. For example, the EU should play a stronger role in foreign policy, defence policy, migration and asylum policy, the fight against international crime, climate protection and research funding. ↘ [ITEM 254](#)

The EU responded to the coronavirus pandemic with the recovery fund, which will largely benefit the national budgets of the member states and provides new funds for various EU programmes. The **temporary recovery fund** offers EU member states the opportunity to **overcome the crisis together and improve the resilience** of their economies. However, like the other temporary crisis measures, it cannot continue in the longer term without a transparent transfer of responsibilities to the EU and agreement by the member states to relinquish sovereignty accordingly. ↘ [ITEM 256](#)

Strengthening resilience and growth

17. The German economy will continue to live with the coronavirus pandemic and its consequences for a long time. In such an exceptional situation, it is important to take strong economic countermeasures at all levels and with the necessary strength. Moreover, there are long-term challenges that have to be overcome. New opportunities lie, for example in the pandemic-related boost to digitalisation and innovation triggered by the pandemic, the transformation to a climate-neutral economy and increased European cooperation. Economic policymakers should seize these opportunities and create the framework conditions necessary for a **resilient and future-oriented economy**.