GERMAN COUNCIL
of Economic Experts

PRESS RELEASE

Federal Budget: Fiscal Measures on Historic Scale Required

- Federal spending is projected to rise in the coming years, driven primarily by defence expenditure and interest obligations. This will widen the federal funding gap and drive up the debt-to-GDP ratio.

- Funding defence expenditures through continuous borrowing is unsustainable. The share of debt-financed defence expenditures should therefore be gradually reduced.

- Consolidating the federal budget demands a comprehensive package of fiscal measures: targeted subsidy cuts, reforms of the social insurance system, and a more efficient tax framework. Even combined, these measures will not fully close the funding gap.

Berlin, 11.11.2026 – Fiscal pressures on the German federal budget continue to worsen in the coming years, with the long-term funding gap hinging largely on the extent to which defence spending continues to be debt-financed. According to projections by the German Council of Economic Experts (GCEE), the funding gap could reach between 2.7 and 4.8 per cent of gross domestic product (GDP) by 2040, depending on the pace at which debt financing is reduced. “Closing these funding gaps will require a comprehensive policy package: targeted subsidy cuts, reforms of the social insurance system, and a more efficient design of the tax system. Yet, this will not be sufficient,” said Monika Schnitzer, chair of the GCEE.

Phasing out debt-financed defence spending

Federal spending has surged since the early 2020s, driven by crisis-related expenditures, expansions in the social security funds, and higher subsidies. Over the coming years, rising defence expenditures and interest obligations will place an additional strain on the federal budget. If defence spending continues to be debt-financed, Germany's debt-to-GDP ratio could reach as much as 98 per cent by 2040. The actual trajectory will depend primarily on whether – and how quickly – this debt financing is scaled back. “Germany must enhance its defence capabilities. However, financing defence expenditure permanently through additional debt is not sustainable. The gradual phasing out of borrowing should therefore be enshrined in the Basic Law,” explains Monika Schnitzer.

To reduce net borrowing, the threshold exempting defence expenditure from the debt brake should be raised. The GCEE proposes raising this threshold – currently set at 1 per cent of GDP – by 0.25 percentage points annually starting in 2031. This path would leave a federal consolidation requirement of 4.6 per cent of GDP in 2040. A gradual phaseout would spread the impact of necessary consolidation on the overall economy over a longer period. The decision on the reduction path should be taken before the end of this legislative term.

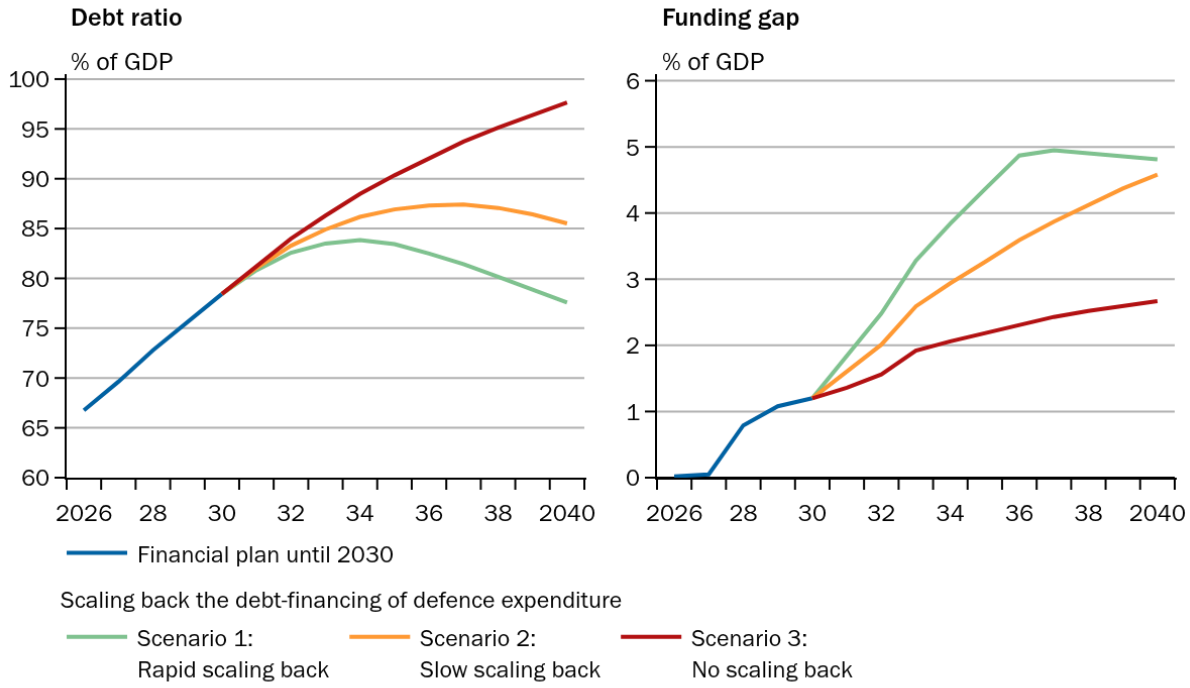
Consolidation requires a comprehensive package of measures

A decision on the consolidation strategy should likewise be taken during this legislative term. The GCEE discusses a range of measures that would ease fiscal pressure on the federal budget by up to 2.2 per cent of GDP. Key measures include phasing out inefficient and environmentally harmful subsidies, fully implementing the Pension Commission’s recommend-

dations – notably abolishing early retirement with full benefits for long-term contributors ("pension at 63") – and the withdrawal of the "Mothers' Pension III." Yet even if all these measures were implemented, a residual funding gap of at least 2.4 per cent of GDP would remain, if debt-financing of defence expenditure is reduced along the path favoured by the GCEE.

Over the medium term, tax increases may become necessary, as higher economic growth alone cannot realistically close the funding gap. Such measures, however, should serve only as a last resort once other options have been exhausted. To ensure fiscal consolidation does not undermine vital capital investment in roads, rail, and waterways, the GCEE proposes to establish a dedicated transport infrastructure fund.

GCEE projections[1]



1 – Projections up to 2030 based on the Federal Government's financial plan. From 2031 onwards, own assumptions (see Box 10). The funding gap refers only to the Federal Government's core budget, while the debt ratio refers to general government as defined by Maastricht. Because the revision of the national accounts by the Federal Statistical Office in July 2026 is not taken into account in the 2030 financial plan and the projection, the ratio shown deviates from the GCEE's economic forecast.

Sources: BMF, BMWE, BRH, Deutsche Bundesbank, Federal Government, Federal Statistical Office, German Finance Agency, Independent Advisory Board of the Stability Council, Ochsner et al. (2026), OECD (2023), Poghosyan (2014), Werding et al. (2026)
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Funding gap and consolidation potential in the Federal Government's core budget

	Nominal consolidation potential for the year of calculation	% of GDP[1]
Funding gap in 2040 in scenario 3 / 2 / 1		**2.7 / 4.6 / 4.8**
Memo items:		
Funding gap with higher potential growth[2]		*2.4 / 4.3 / 4.5*
Funding gap in the alternative scenario with defence spending of 2 % of GDP		*2.1 / 3.1 / 3.0*
I. Consolidation potential through subsidy cuts		**1.3**
Cuts in financial assistance	up to €20.9 billion (2026)[a,b]	0.45
Reduction of inefficient and/or environmentally harmful tax expenditure according to the Subsidy Report	up to €17 billion (2026)[a,b]	0.37
Reduction of further tax expenditure[3]	up to €23 billion (2026)[a,b,c,d]	0.50
II. Consolidation potential on the expenditure side		**0.6**
Statutory pension insurance benefits		
Proposals of the Pension Commission[4]	up to €9.6 billion (2040)[b,e]	0.17
Reversal of mothers' pensions III (Mütterrente III)	€4 to 5 billion (2030/2040)[f]	0.07
Reversal of the extension of the 48 % pension level safeguard	€9 to 15 billion (2030/2040)[f]	0.27
Merging basic income support, housing and child benefits	up to €1.7 billion (2025)[g*]	0.04
Across-the-board reduction in personnel costs by 10 %	€3.3 billion (2025)[b]	0.07
III. More efficient design of the tax system		**0.2**
Limited real splitting	€2.9 billion (2023)[h,i*]	0.07
Reduction of tax privileges on real estate sales	€4.3 billion (2022)[j]	0.11
Curbing value-added tax fraud	at least €2.4 billion (2023)[k]	0.06
Total consolidation potential from I.–III.		**2.2**
IV. Adjustment of tax schedules		
Increase in the value-added tax rate by 1 / 2 / 3 percentage points (PP)[5]	€7.5 / 15 / 22.5 billion (2027)[b*]	0.15 / 0.31 / 0.46
Personal income tax		
Proportional increase in all marginal tax rates by 3 / 6 / 9 %[6]	€4.0 / 7.9 / 11.6 billion (2027)[b*]	0.08 / 0.16 / 0.24
Alternatively: further increase in the second rich tax rate by 1 PP	€0.5 billion (2027)[l]	0.01
Supplementary levy for defence of 2.5 / 5.0 / 7.5 PP[7]	€10.5 / 20.7 / 30.7 billion (2027)[b*]	0.21 / 0.42 / 0.63
Increase in flat-rate withholding tax rate by 3 / 5 / 7 PP[8]	€0.8 / 1.2 / 1.7 billion (2027)[b*]	0.02 / 0.02 / 0.03

* – The calculation takes behavioural responses into account. 1 – Differences in totals due to rounding. 2 – Additional annual potential growth of 0.5 percentage points from 2031 onwards. 3 – Energy tax concession for diesel fuel, value-added tax on animal products, commuting tax allowance, company car privilege, energy tax exemption for kerosene used on international flights. 4 – Strengthening the sustainability factor,linking the statutory retirement age to life expectancy, introduction of a capital-funded pension component (Kapitalrente), abolition of early retirement without deductions for the especially long-term insured, inclusion of self-employed persons not covered by a compulsory pension scheme. 5 – Pass-through rate of 100 %; elasticity of the tax base with respect to the net rate of 0.2. 6 – Elasticity of 0.34 (Dörrenberg et al., 2017). 7 – Elasticity of 0.34 for wage tax and personal income tax (Dörrenberg et al., 2017), 0.6 for the flat-rate withholding tax and 2.55 for corporate income tax (Dwenger and Steiner, 2012). 8 – Extrapolation of the simulation results of Bach and Buslei (2017). Elasticity of 0.6.

a – BRH (2026). b – Own calculations. c – Federal Government (2025c, 2025d). d – Burger and Bretschneider (2021), Gerhards et al. (2026). e – Werding et al. (2026). f – Federal Government (2025b). g – Blömer et al. (2025); study based on the legal framework in 2025, including citizen's benefit (Bürgergeld). h – Blömer and Peichl (2023). i – GCEE Annual Report 2023. j – Bach and Eichfelder (2021). k – European Commission (2024). l – Federal Government (2026c).

Sources: sources indicated, BMF, BMWE, Federal Statistical Office, own calculations

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The German Council of Economic Experts (GCEE) provides support to policymakers and the general public on questions and matters of economic policy. It was founded as an independent body in 1963 and currently consists of the council members: Professor Gabriel Felbermayr, Ph.D., Professor Dr. Veronika Grimm, Professor Dr. Dr. h.c. Monika Schnitzer (chair), Professor Dr. Achim Truger, Professor Dr. Martin Werding. By publishing regular reports, the GCEE aims to help the general public and decision-makers in politics, business and society to form a reasoned opinion on economic policy developments in Germany.

Further information on the German Council of Economic Experts and its publications are available at http://www.sachverstaendigenrat-wirtschaft.de/en.

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