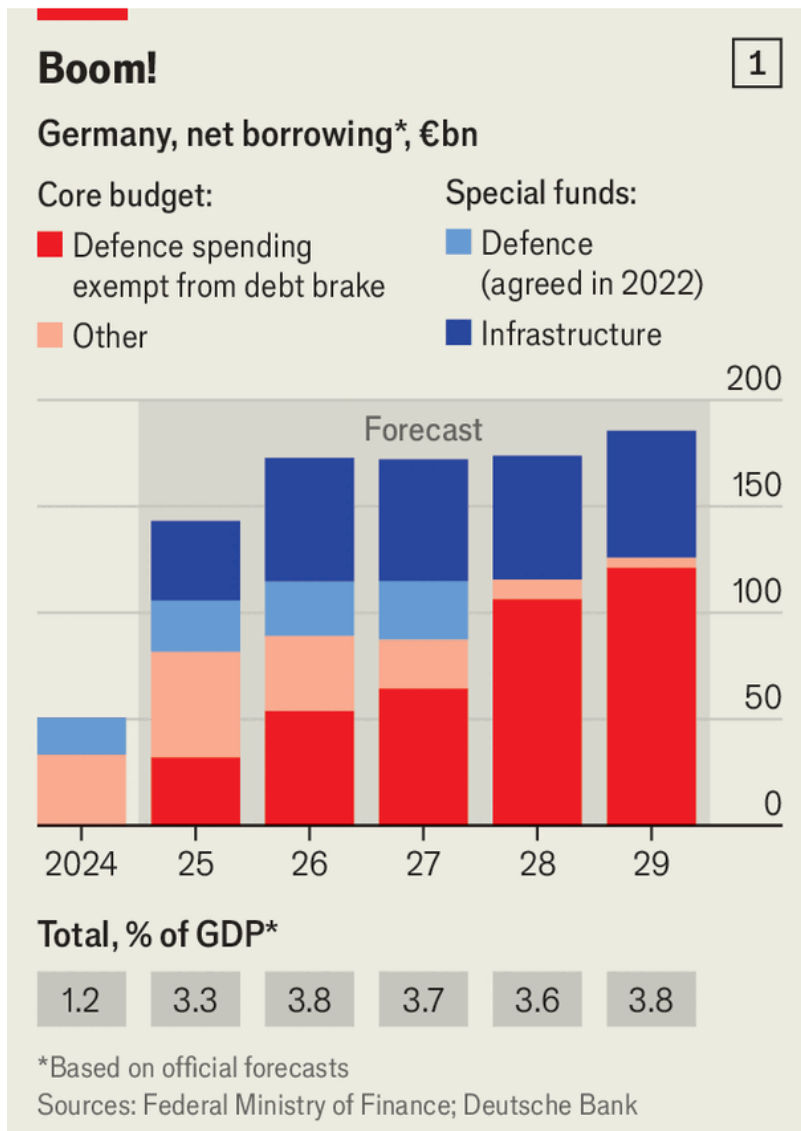


Germany is embarking on an almighty borrowing binge

THESE DAYS the streets of Berlin run red with the blood of sacred cows. On June 24th Lars Klingbeil, the finance minister, unveiled plans to borrow vast sums for a debt-funded €500bn (\$580bn) infrastructure programme and a giant rearmament scheme. The world’s third-largest economy is jettisoning its hard-earned reputation as Europe’s champion of flinty austerity. It is a bold move, and one welcomed by Germany’s allies and the financial markets. But it is not without risks.



Mr Klingbeil wants to open the taps as soon as the Bundestag passes his budget for 2025 (disputes over which felled the last government), and then to ramp up spending on defence and infrastructure—especially on Deutsche Bahn, the miserable state of which has come to symbolise Germany’s dilapidated public realm. Public investment will grow by two-thirds between 2024 and 2026. Perhaps most eye-catching, Germany says it will reach the new nato defence-spending target of 3.5% of gdp by 2029, a full six years before the deadline leaders agreed to this week. To pay for it all, Mr Klingbeil wants to borrow €850bn over this parliament (see chart 1). That could mean annual deficits of over 3% of gdp.

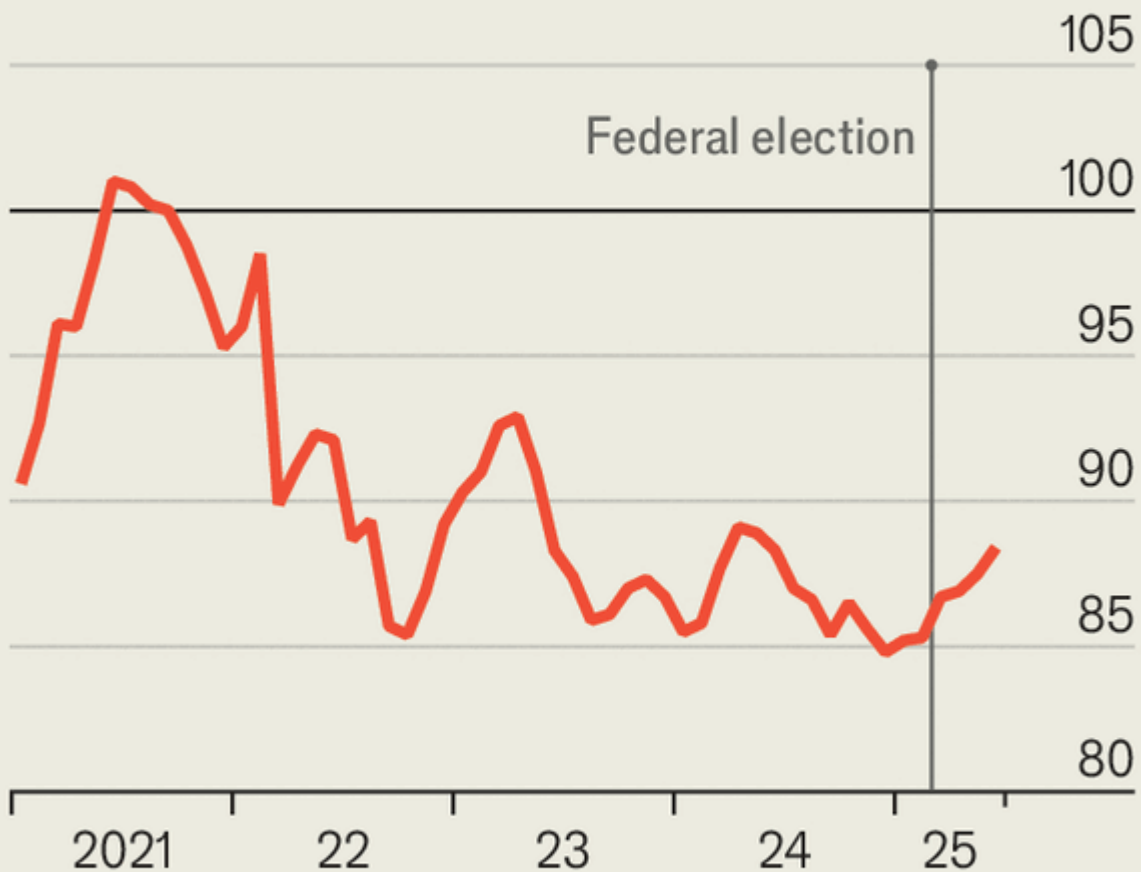
Three things have enabled this splash of cash. The first is a changed threat perception: Friedrich Merz, the conservative chancellor, wants to strengthen the Bundeswehr to deter Vladimir Putin, who German spooks say will be ready to attack nato by 2029. The second is a recent tweak to the constitution to exempt most defence spending from its rigid “debt brake”, and the creation of an off-budget vehicle for the infrastructure splurge, a demand of Mr Klingbeil’s Social Democrats.

The third is Germany’s lowish debt stock, just over 60% of gdp. Its more indebted NATO peers may have to make painful cuts to enable higher defence spending. But Germany’s borrowing looks affordable, though interest payments will grow. Balanced budgets are useless if “bridges and schools rot and the Bundeswehr is neglected”, said Mr Klingbeil.

Chilly

2

Germany, business climate index*, 2015=100



*Average of 9,000 companies' assessment of current business situation and expectations for next six months
Source: Ifo Institute

Thanks to this avalanche of cash, there are signs that the pall over Germany's economy is lifting. Economic institutes are modestly raising their growth forecasts—though the official projection is still of stagnation this year—and businesses and consumers are perking up. (With a July 9th deadline looming, Mr Trump's threatened tariffs could yet spoil the party.)

What are the risks? One is that bureaucracy, planning snarl-ups and labour shortages, especially in construction and engineering, make it harder to spend the money well, as previous governments have learned. A second is that most of the budget is still subject

to the debt brake, and here money remains tight: the government has already had to temper a pledge to reduce electricity taxes. There is a €144bn hole between estimated revenues and spending in 2027-29. Mr Klingbeil is betting that growth will plug it.

Most important, warns Robin Winkler, chief Germany economist at Deutsche Bank, stimulus-induced growth could ease pressure on the government to make necessary but politically tricky reforms. Subsidies to the pension system are the largest single item in the federal budget, and Germany is ageing fast. It desperately needs to expand working hours to alleviate its demographic woes, for example by expanding child care for women who want to work more. “To fix the labour market is to fix the budget,” says Florian Schuster-Johnson of Dezernat Zukunft, a think-tank in Berlin.

Jens Südekum, an economics professor and adviser to Mr Klingbeil, agrees that the injection of funds makes structural reform more, not less urgent—but strikes an optimistic note. Germany’s nugatory growth has left slack in the construction sector, and beyond that a pledge to spend the €500bn over 12 years gives firms the assurances they need to build up capacity. These are the reforms that most economists have long urged on Germany. Its voters—and Mr Klingbeil, who has designs on the top job—must hope Germany can pull them off.