Municipal investment backlog has reached a new high

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Authors: Dr Malte Borghorst, phone +49 69 7431-96268, malte.borghorst@kfw.de,
Dr Stefanie Brilon, phone +49 69 7431-99767, stefanie.brilon@kfw.de

The KfW Municipal Panel 2025 reveals a significant deterioration in the municipalities' fiscal position. They hold predominantly negative views of their current and future fiscal situation. The rise in municipal debt levels, too, indicates a tense fiscal situation.

Municipal construction spending fell in 2024 for the first time since the financial crisis. Although municipalities continue to plan high levels of investment amounting to EUR 48 billion for 2025, municipalities' perceived investment backlog has reached a record high of EUR 215.7 billion. It is particularly in the area of school infrastructure that the backlog has risen sharply.

This year's special section of the KfW Municipal Panel explores the topic of public funding programmes. Municipalities have broad experience in their use but consider the extensive and time-consuming application procedures and documentation requirements as challenging and advocate for bureaucratic simplifications. This finding is relevant not least for the effective implementation of the 'Special Fund for Infrastructure'.

Municipalities face fiscal challenges

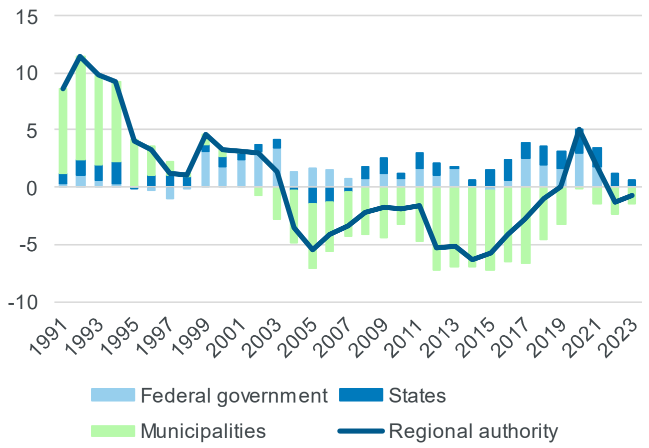
Municipal budgets face enormous fiscal challenges. In 2024, municipalities across Germany ran a deficit totalling EUR 24.3 billion in their core budgets alone. This also led to negative situation assessments by their treasuries, which were surveyed by the German Institute for Urban Affairs (Difu) under the KfW Municipal Panel 2025 between January and March 2025. Thirty-six per cent of municipal treasuries viewed their fiscal situation in 2024 as 'poor', while only around 40% described it as 'satisfactory' or better. At the same time, the share of municipalities that regarded their fiscal position as 'very good' or 'good' decreased significantly. The outlook on their future finances is also marked by uncertainty. For the fiscal year 2025, 84% of treasuries expect an 'unfavourable' or 'very unfavourable' development. With respect to the next five years, 91% of municipalities even expect their fiscal position to develop rather negatively.

Rising debt levels have not yet impacted on investment expenditure

According to the Federal Statistical Office, the debt level of municipalities and municipal associations increased to a total of EUR 169.4 billion in 2024, 9.5% more than the year before. The bulk of the debt consists of investment loans, which increased by 8.8% nationwide. But short-term loans, too, have grown again for the first time in 10 years (+13%), which indicates increasing fiscal uncertainty in many municipalities. The average per capita debt burden is EUR 2,192 but this varies greatly from region to region.

Although investment loans have increased, gross construction investment by municipalities fell by 2.6% in 2024. If we also take into account the depreciation of infrastructure assets as a result of ageing, a sobering picture emerges. Net construction investment by municipalities – gross construction investment minus depreciation – has been consistently negative since 2002, indicating a steady depletion of public capital stock at municipal level (Figure 1).

Figure 1: Net construction investment in EUR billion



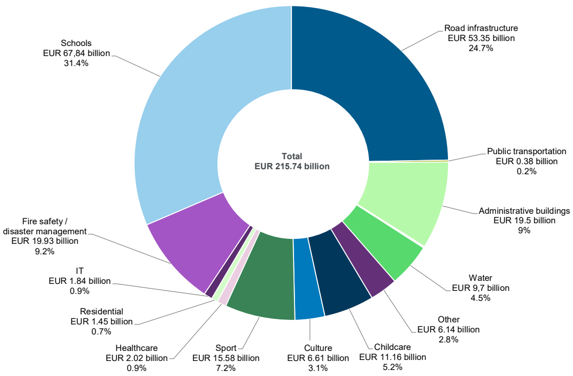
Source: Federal Statistical Office, national accounts, own rendition

Municipalities are less able to maintain their infrastructure and perceive an increased investment backlog

The limited fiscal scope of municipalities also affects their ability to maintain existing infrastructure. Thus, 19% of municipalities admitted that they were unable or only partly able to maintain their infrastructure, 5 percentage points more than in the previous year. In the areas of schools and roads, 17 and 32% have difficulties, an increase of 6 percentage points each.

Municipalities' perceived investment backlog has grown by 15.9% to a new high of EUR 215.7 billion (Figure 2). The investment backlog increased most sharply in schools, fire safety and disaster management and sporting facilities. Road infrastructure constitutes the second highest share of the backlog, at 24.7%. The trend of the past years has therefore continued. But while most of the increase in the backlog in the past years was due to higher prices, the investment backlog in 2024 also rose sharply after adjusting for price increases.

Figure 2: Perceived investment backlog



Source: KfW Municipal Panel 2025

The municipal treasuries were also asked to provide a qualitative assessment of the investment backlog. A particularly high share of 23% of municipalities reported a serious investment backlog in the area of roads and transport. In the area of schools, 56% of municipalities mentioned an at least significant backlog. In cities with 50,000 or more inhabitants, that share even rose to 90%. At the same time, close to 40% of municipalities expect the investment backlog in the education sector to decrease over the longer term.

Use of public funding programmes for investment

The mix of instruments used to fund investment has changed only little compared with the previous years. Besides own funds, municipal loans play a major role. More than half the municipalities also expect to borrow more, which is likely due in part to improvements in borrowing conditions compared with previous years. More than 80% of municipalities used public funding programmes or promotional funds to finance investment in 2024. They made up around one fifth of their total investment expenditure. This year's special section of the KfW Municipal Panel is therefore dedicated to the topic of public funding programmes, which are defined as purpose-tied grants or allocations from the public budget but do not comprise transfers under the municipal fiscal equalisation system or promotional loans. The survey revealed that promotional funds are very widely used. Thus, 96% of municipalities reported having already successfully received promotional funds once and 70% were in the process of applying at the time of the survey. Given the large number of promotional programmes at all levels of the state, the question is how municipalities keep abreast of the complex promotional landscape.

Bureaucratic hurdles and challenges

The KfW Municipal Panel shows that the process requires staff input across all administrative levels and often at executive level. This ties up significant human resources. Furthermore, using promotional funds to finance relevant investments also requires considerable bureaucratic effort on the part of municipalities. Barriers often mentioned are documentation requirements (91%), comprehensive application documents (88%) and inconsistent application procedures (88%). Other challenges include the prohibition to combine promotional programmes (82%) and the complexity of application documents (82%), which pose difficulties particularly for towns and communities with smaller administrations and limited financial capacities.

Calls for administrative simplification

Against this backdrop, many municipalities support proposals for administrative simplification. This finding is also of great relevance with respect to the specific ways in which funds from the Special Fund for Infrastructure are awarded. Municipalities would like the promotional conditions to be clearly and transparently communicated and the application processes to be simplified in order to make it easier to use promotional funds and increase investment activity.

Conclusion: Investment challenges remain

Even if the municipalities have expanded their investment plans, it is necessary not just to clear the sharply increased backlog but also to tackle newly emerging investment challenges. Given that tax revenues are forecast to rise more slowly and expenditure to remain high, the fiscal situation of municipalities can be expected to remain tense. Even if the Special Fund for Infrastructure can contribute to strengthening investment, it will not solve the financial woes of municipalities at structural level. Without fundamental reforms, a correction could prove to be difficult. But non-monetary barriers, too, act as a brake on investment, for example because of staff shortages in administrations and time-consuming contracting and planning procedures. In order to avoid further exacerbating these problems, it is therefore essential to streamline the allocation of funds as much as possible.

The KfW Municipal Panel

The KfW Municipal Panel is based on an annual survey of treasuries of cities and municipalities with more than 2,000 inhabitants and of all rural districts. The representative nationwide survey is conducted by the German Institute for Urban Affairs (Difu) and supported by the leading municipal associations.

Further information on the KfW Municipal Panel can be accessed here.