Germany: Change would be good

The German economy continues its almost everlasting boom. The next new government should add some minor fiscal stimulus in the coming years, without going for the big economic strike.

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An impressive growth performance

Germans don’t like change. In this respect, 2017 was an excellent year and 2018 has all the ingredients to be another good one. Growth was and should remain strong; all economic sectors were and should continue to be booming and Angela Merkel was and should remain Chancellor. However, at least a little bit of change is urgently needed.

The economy grew by 2.2% (2.5% when adjusted for working days) in 2017. That’s a much stronger performance than expected one year ago.

Germans don’t like change. Therefore, 2017 was a good year and 2018 should also be good

Back then, the German recovery already looked rather stretched. Sentiment indicators stagnated and political risks were rising from Brexit and the upcoming Dutch and French
2018 should bring more of the same
The first steps to a new government have been taken

Exactly 110 days after the election, the three parties which have actually governed the country for the past four years agreed to start formal coalition talks. Just to be clear: there is no new German government, yet. But there is a clear determination of the current administration to govern for another four years. The so-called exploratory talks ended with a 28-page-long paper, forming the basis for the coalition talks. According to this compromise paper, which will be the basis for a possible coalition agreement, the next German government will put Europe at the forefront, even though the pro-European stance falls short of clear and concrete measures.

At the same time, the paper remains very vague as to the future of the Eurozone. Phrases such as ‘a close partnership with France to reform the Eurozone in order to make it resilient against future global crises’ will make Paris happy but keep lots of room for interpretation. The only concrete plan is to transform the European Stability Mechanism into a European Monetary Fund and enshrine it into European law. Some minor changes to the health care system, an increase in child benefits, some minor tax relief and investments in digitalisation and education are in the offing as far as economic policies are concerned.

All of this would currently add up to a total fiscal stimulus of around 45bn euro over the next four years (some 1.2% of GDP).

Is it a breakthrough? Well, it is a breakthrough in the way that it opens the door for Germany to finally get a new government.

No big breakthroughs for the economy

However, it is clearly not a breakthrough for the economy. Judging from the paper, the measures are positive for the economy and there are no real economic blunders or obvious electorate gifts such as, for example, the reduction of the retirement age. As far as economic policies are concerned, the agreement is a continuation of the well-known policies of the last few years: cautious steps forward, rather than any visionary experiments. Pro-growth structural
reforms, however, are still hard to find.

The political future depends on the SPD grassroots

The destiny of another grand coalition still dangles on a string, a string in the hands of SPD party members. Dissatisfaction at the party's grassroots level and fears that the SPD could lose further electorate support in yet another grand coalition make the outcome of the upcoming party votes anything but certain.

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Source: Thomson Reuters, all forecasts ING estimates

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