

Germany: 'Yes' or 'no? What's it gonna be, SPD?

While Italy votes, financial markets should also have a close eye on German politics on Sunday. In fact, the result of the SPD's member vote on whether or not to join a coalition with Angela Merkel's CDU could have a bigger impact on markets and Europe than the Italian elections



Source: istock

German politics have been extremely exciting; at least since the September elections. Long-lasting coalition talks, many twists and turns and above all a social-democratic party in a permanent identity crisis. This political rollercoaster ride will now either be over (at least for some time) on Sunday or will get another even more exciting chapter.

Germany's political destiny is in the hands of some 460,000 citizens

More than 460,000 SPD members had the chance to vote on whether or not the party should join

another grand coalition with Angela Merkel's CDU on the basis of the negotiated coalition agreement. The result of the vote will be announced on Sunday. The outcome of this vote is in our view highly uncertain. Remember that the SPD party assembly only voted with a majority of some 56% in favour of starting the coalition talks. The party's grassroots are expected to be more sceptical. Also, more than 20,000 people have joined the party since the beginning of the year, most of them with probable intention to vote against a grand coalition.

Why is the SPD such a 'hard-to-catch'?

The scepticism against another grand coalition stems from huge losses of the SPD at the last elections and the perception that Merkel's CDU has moved so much to the political left that the SPD has lost its political profile. On election eve in September, then-party leader Martin Schulz had immediately announced that the SPD would under no circumstance be available for the next government, going for a complete political renewal of the party in the opposition. The U-turn over the last months can be explained by the SPD's willingness to take up responsibility for the country but was not appreciated by all party members. The party vote now will in our view not be decided by topics from the coalition agreement but rather by the question of whether party members opt for renewal in the parliamentary opposition or for government responsibility.

In light of the above, the fact that in recent opinion polls the SPD has fallen into third place behind the far-right AfD, polling just some 15%, will have only increased the gap between the proponents and opponents of a grand coalition. For the SPD leadership, these results are proof that the party must enter a grand coalition, otherwise, it could be lost in the political wilderness. In our view, however, the fact that other European social-democratic parties have failed to combine political renewal and governing a country at the same time could support the 'no' votes. Also, as Merkel's CDU would get two ministries (health and economics) that are less prestigious but important for SPD voters in the coming years, the feeling amongst SPD party members that the CDU is again undermining the SPD's profile could also be strengthened. All of this means that in our view, it will be a very close decision and the option of a 'no' should clearly not be underestimated.

'Yes' or 'no' - what would be the implications?

For financial markets, the economy and the future of Europe and the Eurozone, the SPD will be a binary event. It is either 'yes' or 'no'. There will be no grey areas. It will not matter how big or small the winning margins will be.

With a 'yes' the last hurdle for Merkel's fourth term has been cleared and Germany will get a new government, probably before the forthcoming EU Summit in two weeks time. This scenario should bring some relief to the German public and the economy as Germans are simply not used to not having a government. It would be a government which delivers a small positive fiscal stimulus over the next few years, pushing the right topical buttons, only not hard enough. It would also be a government which would cautiously and slowly push forward with European and Eurozone integration; no bold steps. The most exciting project is, in our view, the intended economic and tax harmonisation between France and Germany.

In the longer term, however, chances are high that this grand coalition will not make it until the end of the four-year period, the SPD will further lose voters' support and the AfD could be strengthened (not so much as an anti-Euro but rather as an anti-establishment party). Note that with a grand coalition the AfD will be the biggest opposition party in parliament.

In case of an SPD 'no', uncertainty will increase, markets should react negatively, at least in the short run. Germany would then have to figure out what's next. There is no direct route towards new elections. According to the German constitution, the parliament has to vote on a chancellor. In the first two rounds with an absolute majority and in a possible third round with a simple majority. This leaves a small chance for reviving the idea of a minority government with the CDU and either the Greens or the FDP. However, given the cumbersome Jamaica coalition talks, this is a very unlikely scenario. Theoretically, Merkel and her party could govern alone in a minority government after the third round vote. In practice, however, the German president has to decide whether he accepts a chancellor elected by simple majority or whether he prefers new elections. Given president Frank-Walter Steinmeier's publicly announced concerns against a minority government, we would eventually expect new elections.

To keep it short and simple: an SPD 'no' will first lead to a couple of days/weeks of uncertainty before new elections are eventually announced. New elections would then be organised in mid-June or mid-September, leading to a European standstill and more policy uncertainty.

Because they can

The German economy is simply too strong to be substantially harmed by a possible SPD 'no' and subsequent political uncertainty. For Europe and the Eurozone, however, another six months of political standstill and uncertainty in Germany could be more harmful as it would further delay any new steps towards more integration. In the past it was often said that the destiny of Europe was eventually in the hands of the judges at the German Constitutional Court, at least this Sunday, it will be in the hands of some 460,000 SPD party members.

Author

Carsten Brzeski

Global Head of Macro

carsten.brzeski@ing.de

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security

discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.