German government presents third relief package

The German government is increasing fiscal stimulus to offset the impact of higher energy prices, but we doubt that these measures will be sufficient to prevent a recession

German Chancellor Olaf Scholz

The German government on Sunday announced a third relief package to cushion citizens and companies from soaring energy costs while also vowing to reform the energy market to collect windfall profits and cap prices. The measures are aimed at, at least, partly offsetting the impact of higher energy prices on low-income households but the more groundbreaking elements of the package are so far only plans and not actual measures.

The announced measures in more detail:

- One-off financial support of 300 euro for pensioners and 200 euro for students.
- Extension of housing allowance from currently 700,000 recipients to around 2 million recipients and a slight increase
- Cuts in social security contributions for people with a monthly income below €2,000
- Increase in the child allowances by 18 euro per month
- The reduction of the VAT to 7% for restaurants and bars, which was part of the pandemic

stimulus package, will be extended
- Extension of furlough schemes
- Credit support for companies

And here is what the government did not announce or plans that still need additional work:

- The government announced a price cap on electricity prices but this price cap is linked to a mechanism to tax windfall profits, which the government wants to be agreed at the European level.
- The government did not announce a price cap on gas consumption but only the start of a task force to look into this issue.
- There is no new incentive to use public transportation but the government offered to spend 1.5bn euro per year if the regional states find an agreement on the details of such an incentive and are willing to spend at least the same amount as the federal government.
- Interestingly, the government also talks about a concerted action between social partners for the next wage rounds, offering to exempt one-off payments by companies to their employees from taxes and social contributions.

Hardly enough

The new relief package, which comes on top of two previous packages that together amounted to 30bn euro, is obviously aimed at bringing financial relief for low-income households and the ones who will be hit the hardest by higher energy prices. How much relief this package will actually provide remains unclear. At the press conference, German Chancellor Olaf Scholz talked about a 65bn euro package. However, as so often with these kind of packages, it is unclear how the number is really calculated.

In any case, while the announced package will indeed bring some relief for the financially weaker ones, it is doubtful that the package will be enough to offset the impact from higher energy bills entirely. Don't forget that 65bn euro are less than 2% of German GDP. German fiscal stimulus during the pandemic, excluding guarantees, amounted to roughly 15% of GDP. Also, the fact that two crucial elements, price caps and a windfall profit tax, are still works in progress suggests that the full package is hardly operational this year. The fact that there is basically no support for households, which currently do not receive social transfers and that there is also little support for companies, implies that the package will probably fall short in preventing the broader economy from falling into recession.

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