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GERMAN POLITICAL UPDATE

Berenberg Macro Flash

STARTING SITUATION

- All major parties have expressed some preference for repeat elections, or at least indicated a readiness to go for a new vote
- Chancellor Merkel wants to lead her CDU into potential new elections
- Federal president Steinmeier is trying to avoid new elections

If the current Bundestag fails to agree on a coalition, Steinmeier would have to take the ultimate decision between a Merkel-led minority government or new elections. He seems to be playing for time, consulting in detail with party leaders and top representatives of parliament and the constitutional court first. As the situation is unprecedented for post-war Germany, it may well spring new surprises. For example, some discussion has started within the moderate wing of the SPD whether it may not be advisable to take advantage of Merkel's weakened position: If the SPD reconsiders its "no" and offers to stay in a grand coalition with Merkel, the SPD could probably extract major policy concessions. The SPD may shape policies more than before - and may not get a similar chance again. Some SPD officials have also wondered whether support for a CDU/CSU minority government may be an option. Expect a week or two of reflection first before the outlook becomes clearer, with some focus on the meeting between Steinmeier and SPD chairman Schulz (probably tomorrow according to tagesschau.de).

POTENTIAL OUTCOMES

In the order of likelihood

- 1) New elections, probably in April or March. Some observers have mentioned 22 April as a possible date
- 2) Merkel-led grand coalition with the SPD
- 3) Merkel-led minority government supported on a case-by-case basis by SPD, Greens and/or FDP
- 4) Renewed attempt to form a "Jamaica" coalition between CDU/CSU, FDP and Greens (least likely)

IS GERMANY PARALYSED?

No, it is not. Merkel's old government remains in office in a caretaker role without a time limit. As in the previous Bundestag, the government has a majority in the new Bundestag and needs the consent of some Greens to get major laws through the upper house of parliament, the Bundesrat. In this sense, the situation is the same as during Merkel's third term (2013-2017). CDU/CSU and SPD are fully able to react to events and take decisions that cannot wait. Bound together merely in a caretaker government, they may now find it difficult to take major initiatives jointly such as driving a European reform agenda. However, Berlin had only a limited readiness to go for a fundamental French-style overhaul of the EU27 and the eurozone anyway. To the extent that Merkel's CDU/CSU wants to explore Macron's reform ideas, the SPD and Greens would not stand in the way of letting the German caretaker government contribute constructively to such talks. On the EU schedule, namely to agree on the process and schedule for reform discussions on 14/15 December and take first key decisions by June 2018, such final decisions would not be due until after the Italian and the potential German new elections around March/April 2018 anyway. The schedule for EU/Eurozone reform decisions may slip by three months if Germany does not play a sufficiently active role in the negotiations before.



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How about **Brexit**? No change: This is no major issue or bone of contention in Berlin. By and large, Berlin will back EU chief negotiator Barnier's position. If Macron wants the EU27 to take a tougher line than Barnier, Berlin would probably side mostly with Macron.

WHAT COULD NEW ELECTIONS BRING?

For now, Merkel looks set to stay on. Facing potential new elections, the CDU seems likely to rally around their leader who has no obvious rival or successor. The biggest risks to Merkel would be if (i) her party does so badly in new elections that discontent in the CDU would boil over, and/or (ii) potential coalition partners demand the resignation of Merkel as a price for joining a coalition with the CDU/CSU after repeat elections. Not impossible but not highly likely at this stage. As long as Merkel wants to stay on, as she has said she wants to, she probably can.

The situation is too raw to put much faith in the few opinion polls taken since the failure of the "Jamaica" negotiations". The CDU/CSU may lose votes according to a "SPON" survey. In the last election, the major shifts happened in the last two weeks anyway. Early polls are no good guide to the potential outcome.

In the Bundestag elected on 24 September 2017, no coalition can be built against Merkel's CDU/CSU. The right-wing AfD is and will continue to be ostracised by all other parties. It would take a major shift in votes in repeat elections to change the situation that the CDU/CSU will be the senior partner in any new government.

- To make an **SPD-Green-Left Party** alliance possible, the three parties would have to increase their joint share of the popular vote from 38.6% to the roughly 47.5% needed for a majority of seats (roughly 5% of the vote may again go to small parties that don't make it into parliament). That is a very tall order, especially as many shifts in voting preferences are usually within the various political camps, that is between, say, SPD and Left Party or Greens, rather than between the combined centre-left/left and the centre-right.
- For a two-way coalition between **CDU/CSU and Greens** – whose leaders seemed to get on fairly well in the Jamaica talks despite serious policy differences – the two parties would need to raise their combined share of the vote from 41.8% to roughly 47.5%, again a fairly tall order.
- For a more conventional **CDU/CSU-FDP** alliance, the two parties would need to attain the mark of roughly 47.5% from their current 43.6%. While that looks a bit less challenging, it remains a stretch nonetheless. For example, the FDP may gain some votes from the AfD but lose some to the CDU. That the failed Jamaica talks have left some bitter feelings between the two sides may not make the task easier, to put it mildly.

All parties would likely fight new elections with renewed vigour, with a chance to mobilise their base better than before as the repeat elections would seem less boring than those on 24 September when most people assumed that Merkel would win anyway. If the result does not change very dramatically, new elections would probably lead to the same situation: either the SPD or FDP and Greens would have to join the CDU/CSU as junior partner(s) in a coalition in Berlin. Unless the CDU/CSU does very badly (or she were to resign on her own initiative), Merkel could lead such a new government. Net/net, the SPD may find it a little easier to re-join a coalition with Merkel after new elections than before. Of course, we need to add a big disclaimer: the situation is not settled enough yet to come to firm conclusions.

See also our Monday comments [German politics: Limbo in Berlin](#) and [Four German questions](#).



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