



Germany's elections and the future of Europe: How will the new German government influence EU reform?

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Germany has completed the cycle of major European elections this year, with four of Western Europe's seven largest economies having gone to the polls. The populist anti-establishment sentiment that last year led the United Kingdom to vote for Brexit and the United States for Donald Trump has receded — if not gone away. But the existential angst that gripped the EU immediately after the United Kingdom's Brexit referendum has dissipated. Support for the EU has, if anything, strengthened among the populations of continental Europe. The Union is now looking at how to move forward 'the European project' under the leadership of France and Germany, two countries whose leaders will now have a clear four-to-five year run in which to re-shape a reinvigorated EU untrammelled by London.

'Jamaica' coalition prospects

The formation of the 'Jamaica' coalition — made up of the Christian Democratic Union/Christian Social Union (CDU/CSU), Free Democratic Party (FDP), and the Green Party — is still in its early stages, influenced by a forthcoming state election in Lower Saxony. Complicating coalition formation is the number of parties involved — four if the Bavarian CSU is counted as a separate party — and the coalition's wide ideological spread, which is uncharacteristic in German politics. Moreover, the CDU and the CSU, which renewed their commitment to form a parliamentary bloc despite internal tensions over the past two years, are both in a weak position. Chancellor Angela Merkel experienced her worst showing in the four campaigns that she has fought; similarly, the CSU struggled and faces a tough election campaign in next year's state election in Bavaria. In particular, it will come under pressure from the populist far-right Alternative for Germany (AfD). Additionally, the two junior coalition parties, the liberal, business-oriented FDP and the left-wing liberal Green Party are in fierce competition for the same electorate. To secure an agreement, bridges will need to be built between the CSU and Green Party, as well as the Green Party and the FDP.

There are several reasons to expect these talks to result in a coalition agreement by Christmas or early next year. First, there are strong voter signals that a return to the polls in the next few months is undesirable. Second, there is no realistic alternative to a 'Jamaica' coalition. The Social Democratic Party — Merkel's current junior coalition partner — has said it would go into opposition.

Macron's future vision of Europe

Macron's speech on September 26 broke ten years of relative French silence on Europe and of German distrust. The Franco-German dialogue over the past ten years was dominated by France's desire for economic integration in the euro-area, which Germany opposed. Brexit and Merkel's weakened post-election position meant that the timing for Macron's speech was good. Another strength is Macron's credibility for having initiated reforms that several previous French presidents only spoke of. While these will be contested in the French streets, Macron can now credibly speak about reforms for Europe. This was a key problem for several French presidents who wanted to reform Europe but were unable to reform France first.

The tone of the speech was also an advantage; Macron presented real concerns about the state of Europe that were distinct from the picture that European Commission President Jean-Claude Juncker has painted. There also was an enthusiasm on Macron's part not demonstrated by a French president in a long time. Perhaps the greatest strength

of the speech was the way in which Macron glossed over economic and euro-area reform in the latter half of his speech as to not irritate the German government, and instead started with the question of defence.

The speech still showed several weaknesses, including the surplus of ideas included in his 77 proposals. He also recycled many old ideas, such as introducing a European corporate tax and building pan-EU candidate lists for European Parliament elections. Ideas such as a European carbon tax and a European carbon price will be very difficult to implement. Focusing on defence could become more difficult in the absence of the United Kingdom. Germany may be reluctant to increase defence spending substantially. Finally, most of the proposals have a vague and distant horizon of 2024.

The likely impact of Macron's speech will depend on two coalitions: the German coalition and the European coalition. The German response has been positive overall, and the idea of a 'multi-speed' Europe Macron is advocating has much resonance. However, there are other elements of Macron's plans that parts of the likely new coalition oppose. For example, the fiscally conservative FDP is sceptical of further political integration of the euro-area.

Elsewhere in Europe, many member states such as Spain and Italy are preoccupied with domestic crises and forthcoming elections. Judging from the reaction in Poland, Ireland, Luxembourg, Malta, Cyprus and much of Eastern Europe, these countries may not be very interested in what France is proposing. It is likely that Germany will continue heavily to influence European economic reform, while France will attempt to take a leading role in European defence and security. Nonetheless, it is hard to see how this will come to life in the immediate future.

Brussel's European project post-Brexit

In the immediate aftermath of the German elections, there will be a notable personnel issue in Brussels. The long reign of Wolfgang Schaeuble as Germany's finance minister has come to an end; Schaeuble was the only finance minister to be in office during the euro-area crisis and became one of the most dominant voices in its daily management. Schaeuble was passionately pro-European, yet simultaneously an unwavering advocate of fiscal rectitude. Germany's election will be marked elsewhere in Europe as the end of the Schaeuble era as he contributed significantly to European and Brussels-based economic policymaking.

Macron's speech has been touted for its similarities to Juncker's reform agenda set out in the State of the European Union address in Strasbourg. However, a crucial difference between the two exists. While Juncker's vision involves all 27 euro countries moving at the same speed, encouraging those in Eastern Europe to accelerate their plans to join the euro, Macron is in favour of a potential multi-speed Europe; this is a tension that will continue to develop within the next year.

Merkel's view of Macron's speech was enthusiastic, although she suggested that there was still more to be desired in the detail. Germany will find a strong ally in France, while Brussels will also be pleased with the idea of a dynamic French president. However, when it comes to the core details of euro-area reform and amending the architecture of how the EU operates, implementing change could become more difficult.

It was always a fallacy that the German elections would make a difference to the EU's approach to Brexit. If anything, the mood in the EU27 capitals towards the United Kingdom seems to be hardening in part due to the confusion seen in the United Kingdom's Conservative government and cabinet, where members of different factions are sending opposing signals.

Last week, the managing director of the Federation of German Industries proclaimed that German companies with a presence in the United Kingdom must make provisions now for the serious chance of a 'hard' Brexit, claiming it would be naïve to not do so. While there is a lot of discussion about the consequences of achieving no deal or a 'hard' Brexit for the United Kingdom, there is less appreciation in the United Kingdom that other countries are actively planning for this scenario as well.

Q & A Session

Reception of Macron's speech in France

Macron's speech was well received among French elites. He is unapologetically European, which elites see as a nice change from previous governments who were reluctant to emphasise that they were European, yet sought to play a role in Brussels. Macron's more open approach has been judged quite favourably by the French. With the other political parties in shambles, Macron has the perfect window of opportunity.

Reform of European institutions under a 'hard' Brexit

UK Prime Minister Theresa May made an opening financial bid to pay up to 20 billion euros into the EU budget in 2019 and 2020, which is a start that will be welcomed by the EU. Brussels and member state capitals fear that a critical hole will be left in the budget once the United Kingdom leaves. This will have political ramifications and make the next long-term budget round from 2020 much more difficult. To compensate for the loss of UK funds, either net contributors such as Germany and the Netherlands will need to pay more into the EU budget, or net recipients such as Poland receive less. This is a sensitive issue. The most serious quarrels in the EU tend to be over money and this gives the United Kingdom some leverage in the Brexit negotiations.

Position of the liberals in Germany

The overall reception of Macron's speech was quite positive in Germany even though there will be opposition to some of his specific proposals. However, the German political class has realized that Macron is Germany's last chance; it must be remembered that Macron's victory -- which looked improbable until a few months before the election -- came against the background of rising support for National Front leader Marine Le Pen, Brexit and Donald Trump's victory in the US presidential elections. In that sense, Macron can be seen from a German point of view as a saviour, despite the conflicts that will come up over the next years. Macron will be positively received overall, aided by his focus on promoting issues that are easier for the German government to accept.

Schaeuble has been close to Merkel for a long time, and they have a common vision of Europe which the next generation that will increasingly shape the German government does not necessarily share. FDP leader Christian Linder, who could become the new finance minister, is close in age to Macron and will look at the European project from a similar generational angle. This generation of Europeans is less likely to be emotionally attached to the European idea, but will also realise that Macron is Germany's last chance in reforming the EU.

Potential ministerial appointments

It is highly likely that Linder and the FDP will seek to secure the finance ministry. Speculation has Turkish-born Green Party leader Cem Oezdemir to become the next foreign minister. The CSU will want the interior ministry, which it sees as critical given its concerns over migration. Joachim Herrmann, interior minister of the state of Bavaria, could become the new federal interior minister. It is unclear whether Ursula von der Leyen, a co-deputy leader of the CDU and seen by some as a future Chancellor, will maintain her position as defence minister; she faces opposition from within the CDU and her ministry.

A two-speed Europe

Macron's speech points to two options. The first would be to rebuild the EU from the supposed core of the euro-area; this would be a natural platform as post-Brexit all the major economies will be within the euro-area. While Juncker outlined the prospect of a united Europe in which the EU budget for all 27 members states would be enlarged, Macron is interested in using an autonomous euro-area budget for the stabilization of any macroeconomic shocks. This idea would need the support of the Germany, which may be difficult to acquire given the FDP's scepticism of deeper euro-area integration.

The second option is a multi-speed Europe. There would be a strengthening of coalitions and partnerships centered on various projects within areas such as defence and migration. This could be chaotic, and it is difficult to understand how this would work within the euro-area whether consolidated or not. In this case, there might be three 'Europes':

the full EU27; the euro-area; and the assorted coalitions of countries willing to move forward on certain projects. The success of any option will depend on Germany in respect of consolidating the euro-area. Macron intends to strengthen the euro-area and have it as the core area, as well as try to move on defence.

A euro-area tax regime

Macron's proposals for a common tax regime currently only embrace Germany, but would eventually encompass the whole euro-area. Macron wants to harmonise corporate-tax rates and converge France's social systems with Germany's to strengthen the bilateral relationship. This would provide an underpinning for the idea of rebuilding Europe on a Franco-German core.

Euro-area finance minister

A euro-area finance minister is not high on the German agenda, possibly because a euro-area finance minister is not high on the German agenda, possibly because of its symbolic power, given the history of the euro. Merkel will likely focus on the broader picture while seeking to address some of the issues Macron has raised as far as economic governance is concerned. Opposition to EU bond issuance is not specific to the FDP; some in the CSU/CDU have blocked this option from the beginning, and the results of the election will continue to harden attitudes.

In terms of the overarching position of Germany, there are three main layers which may not be easy to reconcile. First is the idea of the two-speed Europe concentrated on bilateral relations with France. Next is the notion of an 'a la carte' Europe based on various coalitions which is also in Germany's interests. The core idea for Germany as far as European development is concerned is to stabilise its environment. For Germany, its place in the EU is central to its security and sense of identity. The third layer is that Germany has a continued interest in keeping as many members within as many circles as possible, and will be concerned with the positioning of Europe post-Brexit.

Prospects for an EU defence force

Money has always been a sticking point in the EU defence debate. However, Brexit has changed the equation as the United Kingdom has traditionally been the anchor halting cooperation and progress on defence at the EU level. As it became clear in the aftermath of the Brexit vote that flagship projects would be needed to show the unity and strength of the other 27 member states, defence cooperation being an obvious choice.

There have been significant steps forward in the last few months. In June, the European Council decided to establish a military planning and conduct capability as part of a much more coordinated military planning structure. On a bilateral level, Merkel and Macron announced intentions to develop joint defence projects, including the development of a new generation of European fighter jets.

The UK position has always been to question the need for EU-level defence coordination given the existence of NATO. The rhetoric during Trump's election campaign made it clear that other countries would need to pay their way much more than they had done in the past. While several past US presidents have made similar statements, the concern of Trump's implicit threats led countries in Europe to believe that more cooperation amongst themselves was needed as an alternative to relying on the United States. The advent of Trump and the advent of Brexit have given a fairly significant impetus to EU defence.

EU governance reform

A large part of Macron's speech is devoted to the question of Democratic Europe. As a survivor of European populism in the form of Le Pen, he is keenly aware that elites have to address the growing distrust among citizens. He has proposed holding democratic conventions next year to begin to build a democratic vision for the European Parliament election of 2019 and establish the Parliament as the core of a new democratic Europe. Creating a transnational list would in his view make the European Parliament elections genuinely European and generate European political parties. However, it is an ambitious plan, and it is unclear if other countries will oblige.

Electoral success of the AfD

The rise of the AfD is a significant factor in German politics which reverberates throughout the rest of Europe. It has had major effects on the debates within the last 2-3 years on topics such as migration and the future of the euro-area. The AfD-allied National Front party in France is financially supported by Russian banks, and many of its key leaders are pro-Russian. Regarding foreign policy, there has been a broadening of the debate in Germany to encompass options that go beyond the traditional classical consensus. Germany's trust of the United States has disintegrated, fundamentally more so than that of the United Kingdom.

Upcoming risks

Possibly the EU's largest challenge in the next few years will be addressing the East-West divide. For example, the Merkel-Macron alliance is based on values which they view as fundamentally different to those of the Polish or Hungarian government.

Catalonia is a challenge within Spain, and other countries are nervous at the suggestion of secessions within a member state. However, this is unlikely to become a Europe-wide phenomenon.

Regarding Macron and Juncker's grand visions, it is quite possible, indeed seems likely, that the euro-area will continue to muddle through. The euro-area crisis has faded for the moment -- euro-area GDP growth is now above 2% and unemployment rates, while still high in Greece, have come down significantly.

It may also be that debates on migration and energy supply take precedence over these difficult architectural questions within the euro-area. This may lead to a dangerous temptation to put these concerns on the back-burner again.